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# GENERAL EMPLOYEES RETIREMENT BOARD MEETING
## August 8, 2003, 9:00 A.M.



## I. CALL TO ORDER

The meeting of the General Employees Retirement Board of Trustees was called to order by Chairman James McC. Wearn at 9:00 a.m., August 8, 2003, in the Town Council Chambers. Attending were Chairman Wearn, Vice Chairman Robert Garvy, Secretary Patricia McLean, and Trustees Tom Bradford (in lieu of Peter Elwell, who was absent), and Brett Madison. Also attending were Town Attorney John McCracken, Finance Director Jane Skittone, and Human Resources Director and Plan Administrator William Crouse.

## II. APPROVAL OF AGENDA

Mrs. McLean requested that item XI, discussion of employee request for benefit adjustment be postponed to a later date.

**Mr. Madison moved approval of the agenda, as amended, Mr. Bradford seconded, and the motion carried unanimously.**



## III. APPROVAL OF MINUTES OF REGULAR MEETING OF MAY 9, 2003

**Mrs. Garvy moved approval of the minutes, Mrs. McLean seconded, and the motion carried unanimously.**

## IV. ADMINISTRATOR'S REPORT

Mr. Crouse stated that the status of the self-directed DROP agreement was resolved. The Vice-President of ICMA agreed that the contract should be amended, and thus he overruled the company's attorneys. Mr. Crouse then stated that the agreements had been received and they were ready for signature. Mr. Wearn commended staff administrator and Town attorney for their good work in carrying out the Board's policy decision in securing a contract which was beneficial to the Town.

Mr. Crouse distributed an assessment, produced by Brad Armstrong, as previously requested by the Board, of what the retirement system would have to budget for various assumptions. It was noted that the current assumption was 8%.

Mr. Crouse then distributed copies of an e-mail from Mr. Martino, a Town resident, along with a response by Jane Skittone. The e-mail involved issues regarding the pension plan. Ms. Skittone stated that the resident had requested information regarding the funds and specific investments, and the reasons for the pension fund losses. Ms. Skittone further discussed that Mr. Martino was informed that there were reports available for his review or purchase and that he was welcome to attend future retirement Board meetings. At the request of Mr. Wearn, a moment was taken for the Board members to review both the request and the response. Mr. Garvy then expressed that the citizen was reflecting the concerns of many people about the pension fund. Mr. Garvy then stated that the concerns were valid and ones that needed to be addressed and would be addressed during the Board meeting, during which Ms. Valcik would introduce other alternatives, such as hedge funds and absolute return strategies. Mrs. McLean commended Ms. Skittone for responding to Mr. Martino's e-mail in a very timely manner with a very comprehensive response. Mr. Wearn requested clarification on the second paragraph. Ms. Skittone responded that at recent Town Council meetings, there were discussions of budget, particularly regarding the Town's contribution which had increased dramatically, and therefore, one of the reasons stated was because of the losses. Mr. Wearn was satisfied with the response.

Mr. Crouse proceeded to discuss Mr. Randolph's letter dated July 29, 2003, which responded to a request from Mrs. McLean. Mr. Crouse stated that the response had a cost involved, and he then requested that the Board approve the payment of the cost. Mr. Crouse stated for purposes of confirmation and/or clarification that it had been procedurally the rule of the Board to direct any inquiries, reports, opinions or informational requests made to the Board attorneys, actuaries or consultants, and before any such actions were taken, they were to be handled through the administrator via requests directly from the majority of the board members. Mr. Crouse stated that the board should discuss whether this procedure would be changed for the future. Mr. Wearn questioned what the cost or expense was anticipated to be. Mr. McCracken mentioned that by the appearance of the letter, there did not seem to be much research time involved. Mr. Wearn requested whether there was a possibility to identify a "not to exceed" figure, as there was considerable concern over the request of the administrator for the board to give a blanket approval retroactive to work that had been done without knowing exactly what the expense was, without setting an upper parameter. Mr. McCracken stated that he was comfortable with stating that the cost would not be more than $1,000. Mr. Wearn then brought up discussion regarding the request not having gone through the administrator prior. Mr. McCracken responded that upon receipt of the letter, it was passed on to Mr. Randolph as the letter was Sunshine Law related, and Mr. Randolph had attended the last meeting to present discussion on the

Sunshine Law. Mrs. McLean apologized for her lack of knowledge in the area, specifically regarding the fact that she had to go through Mr. Crouse first. Mrs. McLean then stated that she had another request in place for information on HIPAA regulations. Mr. McCracken responded that this was a separate



issue and that the work had already been done by Rhoda Yen, an attorney who worked with Mr. Randolph on the Sunshine Law. Mr. Crouse stated that he was not aware of the request. Mr. Crouse then stated that HIPAA would not affect the Town of Palm Beach until April 14, 2004. Mr. Crouse proceeded to mention that Human Resources had already researched, implemented, and was in the process of implementing the forms and procedures for compliance with the Federal Law and had this been discussed prior, the board would have saved Rhoda and others the duplication of the effort, since it had already been done internally. Mr. McCracken stated that the HIPAA law did not apply to this board at all, so there was no concern in that area. Mr. Wearn stated that the Board had a practice in the past of all matters going to a Board professional or consultant that may lead to a bill, first be presented to the Board for consideration so as to determine whether the request would be submitted for opinion or information from the professional or consultant in order to avoid situations where, after the fact, it was ascertained that there was going to be a charge and what the charge was going to be. He explained that approving it after the fact could cause difficulties with the auditor if the Board were to continue. Mr. Wearn continued that the members have to function as a Board and cannot individually go out and function on their own. He continued that it was similar or parallel to the Town Council under the Charter, and that the Town Council cannot give directions to any of the Town staff or to the Town Manager or to any consultants of the Town. Mr. Wearn then stated that the actual Town Council would take action and direct the Town Manager who then in turn would direct his or her staff as the Town Manager would see fit. He then stated that it was a parallel basis and it was a practice which was essentially based on the Town Charter and that mirrored the Town Council type policy. Mr. Wearn did not feel it was necessary to formalize that policy, but that it was important that the Board subscribe to it and if there was a wish to change that policy, the Board should recommend that change to the Town Council for its consideration.

Regarding the first issue, Mr. Wearn requested whether there was any discussion on the retroactive approval of the expenditure for the attorney's opinion letter not to exceed $1,000.

**Mr. Bradford moved approval of the expenditure not to exceed $1,000 for the Town attorney's opinion letter. Mrs. McLean seconded, and the motion carried unanimously.**

Mr. Wearn then questioned whether or not the Board should reiterate, confirm or recognize and acknowledge the policy that had been a practice based upon the Town Council Charter and Town Council action or whether the wish was to make a change. Mrs. McLean commented that she wished to reiterate the policy and acknowledge on the record her knowledge of that policy. Mrs. McLean continued that she apologized to the Board and to Mr. Crouse. Mr. Garvy recommended that since the Board did have a policy in this regard, it was just a concurrent practice, that it was probably a good idea to make it a policy of the Board as well. Mr. McCracken commented that it was a good idea.

Mr. Garvy requested to make a motion that the Board adopt a policy that all matters that might require an opinion of outside counsel, be brought first to the administrator for approval and/or input. Mr. Wearn stated that the policy that was stated was consistent with the Town Charter and the Town Council's policy. Mr. Crouse requested clarification on the motion. Mr. Wearn commented that he understood the motion to state that any matter should first go to the administrator. The administrator would then have a proper practice of bringing it back to the Board. Mr. Garvy requested to strike the words "approval by the administrator". Mr. Garvy stated that the motion instead would state "have the administrator refer to the Board". Mr. Garvy then stated that perhaps in an urgent situation, have the administrator refer to the chairman. Mr. Wearn indicated that emergencies were handled differently. However, up until that point, there had not been an emergency.

Mr. Madison stated that upon beginning his term with the Board, he had requested the ordinance, and Mr. Crouse had provided the information. Mr. Madison then stated that if there were policies which were listed as separate from those previously provided, perhaps those would be distributed, as the information was very beneficial. Mr. McCracken recommended that, if possible, Mr. Crouse could put together for new board members a package which would contain policies such as the statement of investment policy, manager retention policy, and other formal policies. Mr. Wearn stated that this should not be a time consuming effort. Mr. Bradford made a brief comment that although the policy would be adopted, there was nothing wrong with Board members bringing issues to the attention of the administrator or to ask questions from time to time. Mr. Bradford continued that it did not mean that communication had been halted, instead, it was going to be more structured.

**Mr. Garvy moved that the Board adopt a policy that all matters that might require an opinion of outside counsel, be brought first to the administrator who will refer to the Board for approval, Mr. Madison seconded, and the motion carried unanimously.**

Mr. Wearn thanked Mr. Crouse for the administrator's report.

## V. QUARTERLY REPORTS

A. Roanoke Asset Management

Ed Vroom of Roanoke Asset Management appeared before the Board and presented the quarterly report, a copy of which is on file with the Plan Administrator.

Mr. Garvy questioned the PE in the book of price ratio on the portfolio. Mr. Vroom responded that the price of forecasted earnings was 22 times of forward earnings. Mr. Garvy then questioned whether actual earnings were ever looked at instead of forecasted earnings. Mr. Vroom responded that the difficulty lay in that 25% of the portfolio was in companies that were in trough earnings. Mr. Vroom continued that the number looked at trailing 12 months would be quite distorted and lead to the wrong conclusion about the overall portfolio. Mr. Vroom stated that Roanoke had tried alternatives such as normalizing earnings, and it resulted in a significant amount of work for an incorrect conclusion. As a result, Mr. Vroom stated that it had been the reason why it was looked at going forward 12 months out.

Mr. Garvy then stated presumably that the stock prices were at trough as well, if the earnings were. Mr. Vroom responded that it depended on where one stood. Mr. Vroom stated that if one were to look at what had recently happened in the market, there had been a good recovery, as there had been a lift in earnings. Ms. Valcik of Callan Associates stated that in defense of the change in the industry, stock market prices impounded what was going on in the future earnings. Ms. Valcik further explained that a company's earnings were not looked at on one particular day. They should look to the future earning stream discounting it back to present value, and then come up with the price of the stock. Mr. Wearn questioned whether this would inject greater risk. Mr. Garvy responded that with forecasted earnings there was no correlation between forecasted earnings and actuaries. Mr. Garvy stated that real earnings and real PE's were fundamental. Mr. Vroom responded that 2003 forecasted earnings were based on six months of actuals in the bank. Mr. Vroom continued that it was more substantive because a trend line was done to the fourth quarter. Mr. Vroom offered to run a report trailing what the 12 months PE was, as he believed it would be lower than the 2002 PE, because there was six months of earning growth. Mr. Garvy made a statement that the current price range ratio on the S&P500 was approximately 30, which was down from 52. Mr. Garvy continued that it was forecasted to be 19 over the next year, which suggested that the earnings were going to grow on the S&P by 72% during the following 12 months. Mr. Vroom responded that he remembered when he was growing up that the time to buy General Motors was when it was selling at the highest price earnings ratio. Mr. Vroom continued that when GE was selling at 40 or 50 times earnings, that was the time to buy, because it was at the low point of its cycle. Mr. Garvy stated that plenty was being counted on the second half on the rebound. If that rebound did not occur, there would be another reaction of the market. Mr. Vroom responded that he did not believe it would be a severe reaction, because there was growth going on, and companies had restructured themselves, cut costs and had fixed their balance sheets. Mr. Vroom continued that there had been a snap back. The earnings were good, but people were expecting that during the second half, there was going to be some directional confirmation of the move in the market.

Mr. Wearn thanked Mr. Vroom for the quarterly report.



B. Loomis Sayles

David Sowerby of Loomis, Sayles & Company appeared before the Board and presented the equity results of the quarterly report, a copy of which is on file with the Plan Administrator.

Mr. Garvy stated that the yield on the portfolio was in the two percent area. He then stated that historically, yields that were low, were also associated with market highs. Mr. Garvy then questioned what was so different where everyone was expecting the market to continue up and yet there were measures that went back 200 years that were at historic lows. Mr. Sowerby responded that in the late 1990's, many investors wondered whether yields were going to go the way of dinosaurs and hula hoops, because if companies took the cash and redeployed it in the company, they would get a positive rate of return. Mr. Sowerby then stated, after brief discussion, that it was starting to be seen that yield was resurrecting itself.

Mr. Garvy referenced Mr. Martino's letter regarding the losses that the pension fund had suffered, and his concern about the soundness of the fund going forward. Mr. Garvy requested Mr. Sowerby's view on how to deal with an issue similar to this. Mr. Sowerby responded that it came back to realistic expectations and to put it in context of how dividend yield will help out more versus the 1980's and 1990's when stocks were compounding at 18% in both decades and people were not enchanted by getting excited about a three percent dividend yield and a cereal maker like Kellogg. Mr. Sowerby continued that the challenging job going forward as a Board, was going to be answering the question, whether diversification would be implemented in the portfolios. Mr. Sowerby continued that diversification in the different asset classes that were available and within the asset classes was going to be the real key going forward.

Steve Dougherty of Loomis, Sayles & Company then presented the fixed income portion of the quarterly report.

Mr. Garvy stated that the recent government auction had not been very successful. Mr. Dougherty responded that it was a situation which had not been seen in recent time. Mr. Dougherty continued that the real question was going to be the ten years, which was the real benchmark.
Mr. Garvy stated that Mr. Dougherty had mentioned that there was over $200 billion of additional financing coming, however the country was into the largest budget deficit ever seen in history. He continued that the demand for credit was driving these rates up close to unprecedented, and that there was a deterioration of the junk bond market, because of the default risk concerns. Mr. Garvy questioned what the people in the bond market were saying about this in terms of its effect on the economy. Mr. Dougherty responded that it went back to the $64 trillion question of whether the higher interest rates had a detrimental impact on the economic growth. Mr. Dougherty continued that the credit situation as a whole, high yield bonds over the last nine months had averaged about 25% return, so with the historically low interest rates, there had been an insatiable demand for yield. A year ago, when we spoke, we talked about the accounting scandals and the issues with WORLDCOM, investors were flocking out of any corporate bonds that they had and it was unbelievable because there was so much uncertainty. As that uncertainty diminished, you starting seeing a lot of money moving back into the corporate credit market, and where it first went to was the high yield market. The fourth quarter last year and the first couple quarter this year, strong returns in the high yield market and really it was in the weaker credits, triple C's returned over 40% year to date. Single B's were about 30%, and the double B's were about 20%. So, investors are comfortable with credit risk now in my view, and default rates of decline, companies that were on the brink of defaulting are now able to come into the credit markets and access capital and borrow debt at reasonably strong or good levels of interest rates of yield. Mr. Garvy then questioned where those yields are in the junk market now. Mr. Dougherty responded that a year ago, the premium for a junk bond company, if treasuries were at the time, say five percent, a single B average junk bond company would probably have to borrow at about a twelve to thirteen percent interest rate. Now, treasuries have declined, that's ten years, treasuries now, ten years about four percent. Now, its probably ten percent. That premiums come in, maybe even less than that. It depends on the industry. The bonds that have performed the strongest in the corporate market, a lot of

those TELECOM bonds, that is where the money is coming back in. Quest, Sprint, things of that nature. Those kinds of bonds have done extremely well. As far as the credit issue is concerned, I think we are okay there. The real issue is what level of interest rates would the treasury have to take interest up to to dampen the economic growth. I don't think even a 450 ten year, I don't think it is going to be enough. It is still historically low, and it has taken a long time, because I know I have said it before, when you look at four percent treasury yields, investors are going to have to extend out to lower quality, to longer maturities to get higher yields to hit that benchmark that you have, especially when the stock wasn't giving good returns. It has taken a while, we've had that bump in the road with the accounting scandals. I don't think it is going to be an issue right now, I think it is a tremendous amount of borrowing, and the deficits next year. Right now, we are forecasting anywhere from four to $450 billion again. Next year is a little bit greater uncertainty than this year, I think we are going to be okay this year as far as economic growth continues to be strong. But next year is going to give us worry because it is going to have borrow an equal amount of treasury financing.

Mr. Wearn thanked Mr. Sowerby and Mr. Dougherty for the quarterly reports.

A short break was taken.

The Board reconvened at 10:53 a.m.



C. Callan & Associates

Jeanne Valcik of Callan Associates appeared before the Board and presented the performance report through June 30, 2003, a copy of which is on file with the Plan Administrator.

Mr. Garvy referred the Board to page 18, and expressed that he was pleased to see the good performance that had occurred from Loomis Sayles. He then stated that the information ratio, sharp ratio and excess return ratio remain low, all in the fourth quartile. Mr. Garvy requested whether Ms. Valcik had any observations. Ms. Valcik responded that her observation was that it was against the S&P500. She further mentioned that it had been previously discussed to run the pages against the Russell value benchmarks, and that she would produce that for the Board. Mr. Garvy agreed. Mr. Garvy then expressed that he felt it would be more appropriate, since it was a value manager versus a value universe for information ratio purposes. Ms. Valcik stated that with the permission of the Board, next quarter she would run both reports. The Board would have one quarter to compare and then go from there. Mr. Garvy agreed without objection from the Board. Mr. Garvy then stated that there was a similar situation on page 19. Ms. Valcik responded that everything, once the official benchmark is set for the portfolio, everything would run against the S&P. Mr. Garvy then recommended that Mr. Sowerby see that against a value benchmark as it would be beneficial. Mr. Sowerby agreed. Mr. Garvy questioned whether those changes would be made as well. Ms. Valcik agreed. Ms. Valcik stated that she would run all the pages and run them by Mr. Sowerby as well.

Mr. Garvy then referred the Board to page 25 and there was brief discussion held on the performance of Roanoke. Mr. Garvy stated how he was surprised to see that Mr. Vroom was disappointed with the last quarter, being in the first percentile ranking. Mr. Vroom stated that the comparison of the Russell 2000 and 2500 had been his reference to the disappointment in the quarter. Mr. Vroom continued that Roanoke is very happy with the one percent. Mr. Garvy made note that Mr. Vroom had been serving the retirement Board for over 20 and that his rank was most likely in the top five. Ms. Valcik agreed.

Mr. Wearn thanked Ms. Valcik for the quarterly report.

## VI. PRESENTATION ON HEDGE FUNDS

Mr. Garvy stated that he did not feel it was appropriate for a Board member to present an overview of hedge funds, but rather to participate with the other Board members in the discussion. Jeanne Valcik of Callan Associates then appeared before the Board and presented a very detailed presentation on hedge funds as previously requested by the Board at the May 9, 2003 meeting.

Mr. Garvy directed the Board to page nine of the presentation where there was discussion in regards to how public funds implement the hedge fund solution, and the dramatic movement towards investing in hedge funds. Mr. McCracken stated that the Public Safety Board began investing in hedge funds earlier in the year. Ms. Valcik stated that Public Safety invested in hedge funds through mutual funds. Mr. McCracken stated that one of the funds may be, but two of them are not. Mr. McCracken then commented that there had been much controversy because of the requirements of the funds.

Mr. Garvy stated that the volatility was being reduced by a factor of three. Ms. Valcik responded affirmatively. Mr. Garvy then questioned the solidity of the database. Ms. Valcik responded that with hedge funds, Callan had collected the data, created the database and had managers that had been stable and around for years. Ms. Valcik assured the Board that the database was as clean and high quality as Callan believed that the Town could get.

Mr. Garvy then stated that the mean return of the S&P500 would be slightly higher than the mean return of that hedge fund, fund to fund circle. Ms. Valcik responded affirmatively. Mr. Garvy continued that the reduction in the standard deviation was a factor of three, as a result, the euphoria despair factor was reduced substantially. Ms. Valcik confirmed and stated that there was considerable downside protection, a return somewhere between bonds and stocks. Ms. Valcik continued that the volatility was much lower, although the volatility was just slightly above what the bond market was. Mrs. McLean questioned whether the number of people who participate would affect the outcome. Ms. Valcik responded affirmatively. Ms. Valcik stated that if hedge fund managers did not figure out continued new areas to invest in, the alpha would be competed away in certain segments. The more people that invest in a particular strategy means that the returns do decline. Mrs. McLean then stated that her understanding was that part of the success of a hedge fund manager was involved in the secrecy of the transactions, so if a secret was no longer a secret, then it would affect the productivity. Ms. Valcik responded that the assumption that needed to be made was that these very bright people figured out how to make money in a particular strategy and they would move on and figure out how to make money in another strategy that other people had not know about.

Mr. Garvy made a reference back to page 12 where brief discussion was held regarding various strategies in fund to funds and others. Mr. Garvy stated that the result would be a big reduction in standard deviation, because of the correlations among the things which were varying and bringing the total volatility of the fund to funds quite low relative to stocks. Ms. Valcik responded affirmatively.

Mr. Garvy referred to page 16, and questioned the issue of custodian and protection of public funds. Ms. Valcik stated that her knowledge was superficial in this area. Mr. McCracken stated that in the funds of funds that were owned by the Public Safety Board, the investment of the Public Safety Board was in the fund to funds. The evidence of that security was held by State Street and accounted for by State Street. The agreements were clear that the underlying securities were owned by the managers who were selected by the manager of the fund of funds, which as a result even the manager of the fund of funds did not know what securities the underlying managers were investing in, although he did know what their custody arrangements were. Mr. McCracken continued that it was typically through brokerage houses, so that not only did the board know, but even the manager who was being hired, essentially was the manager of the fund to funds.

Mr. Garvy then questioned if the brokerage firm were to fail, would the funds be segregated in such a way that the beneficial owner of the assets would have access to them via the custodian, or would the funds simply disappear. Mr. McCracken responded that if the brokerage firm were to fail, the manager of the fund of funds would have whatever access to relieve the underlying manager. Mr. McCracken continued that he would step in the shoes of the underlying manager, if the underlying manager failed, but the underlying manager would have the claim against the brokerage house. Mr. Garvy questioned whether it was a part of the general claimant or was it segregated. Mr. Garvy requested that Ms. Valcik look into this area for clarification. Ms. Valcik agreed.

Mrs. McLean questioned the actual securities of the funds. She then stated that it would take a gigantic leap of faith to take retirement money and make investments, yet have no access to the status of the funds. Mrs. McLean continued that she would have a real problem with going to the members and saying that the board was not sure what was being done with their money, but that it was doing real well. Mr. McCracken stated that the situation was handled differently. Mr. McCracken stated that the board would hire a manager of a fund of funds, who would pick underlying managers who would exercise the discretion in a particular discipline. Mr. McCracken stated that Public Safety did not have this, however they did pick a specific strategy and then the fund manager picked the people who did that. Mr. McCracken continued that the board would rely upon the fund manager who was selected, or in the case of the Public Safety Board, they would rely on the fund managers who were selected by the consultant. Mr. Garvy then stated that when the manager buys stock in a company, he expects that the company would pursue the strategies they have asserted that they were going to pursue. They would run their business in a professional manner, they won't be fraud, however, as learned with ENRON, Global Crossing and others, there would be no guarantee. As a result, the fund to fund managers would need to carefully assess the background, the history and the character of the people.

Mr. Garvy stated it would not bother him as much as the question of whether if it is in a brokerage firm, and it is not custodied separately, are the assets segregated in such a way, that if the brokerage firm were to go bankrupt, that the board would not be tied up in a year's worth of litigation trying to get assets as everybody comes to the table or not. Ms. Valcik agreed to research this area further with her hedge fund expert.

Mr. Madison questioned where the monies would come from for the investments. Mr. Wearn stated that it would be the Board's policy decision. Mr. Madison then questioned whether the board cold do hedge funds based on bonds and hedge funds based on equities. Mr. Garvy confirmed Mr. Madison's question and stated that there would be stock and bond hedge funds for sure as well as possibly commodity funds. Ms. Valcik then directed the Board to review "Building A Hedge Fund Program", where further discussion was held.

Mr. Garvy stated that Ms. Valcik had previously mentioned that there was a weak benchmark for assessing hedge funds, however, that there were peer groups also. Ms. Valcik responded affirmatively that there are peer groups for hedge funds and that there was also benchmarks available. Ms. Valcik stated that the peer groups are segregated into two different types. Ms. Valcik then stated that at Callan Associates they offer one called "Core Diversified Fund to Funds", which are what the name says was the institutional quality, and the second called "Hedged Equity Fund to Funds", which was for those that have directional strategies. Mr. Wearn then questioned what the criteria was to establish the peer group. Ms. Valcik responded that for large cap value, Callan used style analysis, where the characteristics of the portfolio are looked at. By looking at characteristics, Callan can see whether its really core value or something else. Ms. Valcik continued that returns style analysis was where the return of the fund was looked at, and to see what they correlate to in terms of the particular market place. This style would allow you to get an idea of the sort of style of the manager. Mr. Garvy questioned whether there was any discussion in Callan about extending the peer groups. Ms. Valcik responded that not at the time, however, as more of the clients adopt fund to fund approaches, she would suspect that would occur. Ms. Valcik stated that Callan would create as the demand grew.

Mr. Garvy questioned whether the Board received Callan insights. Ms. Valcik responded that in order to receive the insights, you would need to sign up on the internet and then it would be sent to the subscriber via e-mail. Ms. Valcik stated that it was very helpful and informative and she highly recommended signing on. Mr. Garvy expressed his interest to be a recipient.

Mr. Wearn commented that the mortality seemed to be a significant factor in the "Hedging Your Bets with Absolute Return Strategies". Ms. Valcik stated that many hedge funds are launched, however many of them go completely bust. Ms. Valcik continued that one of the reasons why the hedge funds that were launched would go out of business was because they were based upon the profitability of the fund. If a fund manager launched a hedge fund to funds, and they had a dramatic down turn, they would see that they were going to run that fund for free for ten years and they would just close it down. That was one of the reasons why there was such a high default rate. Ms. Valcik then stated that the fund of fund managers were now picking fund managers that had previous experience with funds, fund managers that had been together for a long time.

Mr. McCracken stated that if the Board were to decide to go into hedge funds, they would have to have Town Council approval to get the investment policy changed, as was done by the Public Safety Board, and it was approved by the Town Council. Mr. Garvy questioned the difficulty of the effort. Mr. McCracken responded that it was not a difficult effort. Mr. McCracken continued that there had been anticipation that there would be a lot of questions and concern on the part of the Town Council, however there was not. The request was approved. Mr. Wearn questioned what the supporting documentation was to the Town Council. McCracken responded that the board amended their statement of investment policy to contemplate adding the particular type of investments, and that it was documentation which could definitely be provided for review. Mr. Wearn questioned whether there had been a supporting argument that was made in writing. Mr. McCracken responded that there was not, simply a few members of the Public Safety Board were in attendance at the Town Council meeting in anticipation of issues and the consultant as well. Mr. McCracken continued that the Town Council did not question anything, so there was no need for a presentation.

Mr. Garvy questioned how many manager searches and fund to fund searches Callan had done. Ms. Valcik responded that she was not certain, however she was sure that there was many. Mr. Garvy requested that Ms. Valcik look into it how many Callan had done historically and how many were currently going on and provide those numbers.

Mrs. McLean questioned whether there was a restriction on international investments. Mr. McCracken responded that they were limited by state law and prohibited by the ordinance. Mrs. McLean questioned whether it would have an impact on the hedge funds. Ms. Valcik stated that it could very much have an impact if Global Macro strategies were to be looked at. Mrs. McLean stated that they were one of the more successful ones. Ms. Valcik stated that it depended on the manager.

Mr. Garvy requested Ms. Valcik's opinion regarding the three points on page 22. Ms. Valcik responded that she believed that hedge funds, if understood by those who were involved, was certainly an appropriate investment. Mr. Wearn stated that the question of an appropriate investment was also related to the question of the policy statement. Ms. Valcik stated that the safest approach would be simply to mirror the changes that were made by the Public Safety Board. Mr. Wearn stated that what was being contemplating was the significant change or relatively small percent of the total funds or value under the direction management. Ms. Valcik agreed. Mr. Garvy stated that there also needed to be consideration that once the involvement is done, what would be the next steps taken.

Mr. Garvy commended Ms. Valcik for an excellent presentation on the funds, stating that it was very comprehensive and informative. Mr. Wearn stated that having the two papers as a predicate of the presentation was a very good foundation on which to learn.

Mr. Garvy made a recommendation that if suited by the Chairman and the Board, to have another session within four to six weeks that was devoted to a discussion of hedge funds to explore and determine whether to move forward or not. Mr. Wearn agreed and stated that it was a good idea, if the majority of the board felt similarly. Mr. Wearn questioned whether there were any questions from the board for Ms. Valcik and primarily toward whether or not the board should go forward with more in-depth consideration and perhaps a vote or hear any concerns regarding going forward or not. Mr. Wearn continued that if the board were to go forward, there would be a need to have a workshop devoted to expressly considering all of the issues, as there seemed to be substantial questions that needed to be addressed. Mr. McCracken stated through experience with the Public Safety Board, there was substantial documentation, agreements, disclosure papers and commitments involved Mr. McCracken then stated that it was a very arduous process.

Mr. McCracken questioned the difference between registered and unregistered hedge funds. Ms. Valcik responded that registered hedge funds meant that they were registered with the SEC, as a registered investment advisor. Mr. Garvy then stated that they were not regulated by the regulators, but that they met the requirements of the SEC. Mr. Garvy continued that they were not regulated by the SEC, unless voluntarily by the fact that they were registered with the SEC. Ms. Valcik stated that the SEC regulates mutual funds and then regulates the registered investment advisor. Mr. Garvy stated that it was very intense, a highly regulated industry, where audits were done every four years. Mr. Garvy continued that the SEC did want to be tainted with the image of fly by night risk taking entities. Ms. Valcik stated that Callan was pretty conservative, when looking at hedge fund to funds managers, they have to be registered. Mr. Garvy requested that Ms. Valcik research that if they do register, are they then subject to the four year cycle of an audit by the SEC or not, and what did the registration imply terms of what they have to do from a regulatory standpoint. Ms. Valcik agreed.

Mr. Wearn questioned whether the Board wished to explore further into hedge funds. Mr. Madison made an observation regarding Mr. Martino's letter and the concern he felt that hedge funds appeared to be risky. Mrs. McLean stated that she was inclined to not go forward with hedge funds, however she was open to ideas as well. Mr. Bradford then commented that hedge funds were a potentially important tool for the future. Mr. Bradford continued that the idea to have a workshop meeting to review additional aspects of the concept would be worth while and it would answer more questions and concerns that the board members had. Mr. Garvy acknowledged that the board members' comments were valid concerns that are necessary when investigating or evaluating any potential alteration of a policy.

Mr. Garvy referenced page 12,and then stated that if the board chose to proceed with hedge funds that they look only to the fund to fund type of investment, as it was an area of much diversification and multiple strategies that were different from equity and bond strategies. Mr. Garvy continued that by limiting to the fund to funds, proceeding on the basis of the conservative approach that Callan took to everything and particularly to these funds, limited to registered funds, it would be worth while to explore further. Mr. Wearn agreed and stated that the concept was called a hedge fund which was intended to hedge against risk. Mr. Wearn stated that it was worth while to explore and find out exactly how it can benefit the Town by hedging against risk, especially the volatility. Mr. Wearn continued that even if the board decided not to go forward after the workshop, at least with the knowledge acquired, there would be a good foundation for future fiduciary action. Mr. Garvy then commented that in terms of Mr. Martino's letter, where the citizen had questioned what steps were being taken to attempt to deal with the severe losses that were suffered over the past few years. Mr. Garvy continued that in response to the letter, it was the responsibility of the board as fiduciaries to explore and be proactive in dealing with the issue. Mr. Garvy then stated that it would support the concerns of the taxpayers and citizens in wanting to see the board act responsibly. Mr. Wearn questioned whether there would be an objection to holding a further workshop expressly for the purpose of considering fund to fund hedge funds and the questions and issues that had been raised. With no objections from the Board, Mr. Wearn stated that the appropriate step to take was to ask the staff to get prepared to address the issues and questions that had come up and to ask what time frame would be needed for that. The board agreed that four to six weeks would be appropriate. Ms. Valcik commented on some ideas in regards to bringing in hedge managers and marketing personnel. Mr. Wearn expressed his concern that they would make some kind of a presumption that there was a direction of the Board which was presumed and did not exist. Mr. Garvy then stated that the area was so new, that it would explicitly be explained that it was completely educational in nature and had no implications of a sales pitch on their fund. Mr. Garvy continued that locally, there were registered fund of fund firms. Ms. Valcik stated that there was also one out of Chicago, which was good. Mr. McCracken stated that Jonathon Prime, the principal consultant which represents the Public Safety Board had extensive background in the area and did make a presentation to the Public Safety Board, which was very similar to what the general board was requesting, and there was a possibility that he could meet with the board also. Mr. Wearn stated that learning from all sources who are knowledgeable about it is a good idea. Mr. Wearn then stated that Mr. Crouse could contact him and ask if he would consider giving us what input and insight he would like to and answer questions the board may have. Mr. Garvy suggested that Callan Associates had experts in the area as well, and since Callan is the board's consultant, perhaps Ms. Valcik could look into whether or not their specialist in the West coast would be able to attend also. Ms. Valcik stated that there would be a possibility. Mr. Wearn then stated that the administrator would need to coordinate the dates and times of availability of the members of the Board and consultants who would be able to give input and come up with a date as soon as possible. Mrs. McLean then suggested that there was new legislation that was provided at FPPTA regarding instructional requirement for the Board. Ms. Valcik stated her recollection was that there was no specific hour requirement on the bill. Simply, it was stated that all Boards of Trustees for Florida plans should have educational opportunities and sessions. In fact, this board incorporated that in the IPS some time ago. Mr. McCracken and Mr. Wearn agreed. Mr. Wearn stated that this portion of the agenda should be documented in the record as educational. Mr. Crouse stated that without objection it would be. Mr. Wearn then requested that we bring together the people for a meeting, finding out availability of the chamber, and respond to the members as early as practical.

With no questions or comments from the Board, Mr. Wearn thanked Ms. Valcik for her presentation.

## VII. REQUEST AUTHORIZATION FOR AUDITOR AND ACTUARY TO COMPLETE IRS APPLICATION FOR DETERMINATION OF EMPLOYEE BENEFIT PLAN (IRS FORM 5300) AND FUNDING FOR SAME

Ms. Skittone stated that general employees had a determination letter from the IRS, however it was quite old and had been received when the boards were combined. Ms. Skittone then stated there was a need to file for another determination letter as the revised board. Ms. Skittone continued that the auditor had given a price of not exceed to $750, which would be less, depending on how much work the finance department would do up-front. Ms. Skittone requested authorization to spend $750 for a determination letter.

**Mrs. McLean moved to accept the funding request, not to exceed $750, for the auditor to complete the IRS application, Mr. Madison seconded, and the motion carried unanimously.**



## VIII. REPORT ON QUARTERLY EXPENDITURES

Ms. Skittone presented the report on quarterly expenditures and recommended a transfer of $200,000 from the State Street index fund.

**Mrs. McLean moved to accept the report and approve the money transfer, Mr. Bradford seconded, and the motion carried unanimously.**

**Mrs. McLean moved to accept the report on quarterly expenditures, Mr. Bradford seconded, and the motion carried unanimously.**

## IX. DISCUSSION OF PROPOSAL FOR ADOPTION OF SUNSHINE LAW POLICY

Patricia McLean appeared before the Board and presented a discussion of the adoption of the sunshine law policy, specifically regarding how the minutes and the agenda should be handled, a copy of which is on file with the Plan Administrator.

Mr. Wearn stated for purposes of clarification that the board was in full compliance with the State Law and that the Town Hall was in compliance with the Town Policy on the handling of the minutes and the agendas. Mrs. McLean responded that she agreed. Mrs. McLean stated that she was formalizing the procedures that were currently being done, and modifying a few of them.

Mrs. McLean stated that the minutes should be recorded on a continuos basis, and they should be transcribed as soon as possible after the meeting. Brief discussion was held and it was agreed that the minutes were recorded on a continuous basis and the minutes would be transcribed within four to six weeks and disseminated to the board members, stamped "UNAPPROVED". Mr. Wearn stated that if there was a perception that the board was doing things behind closed doors, all members have full access to the minutes, they are available for anyone, once they are approved at the meeting. The members can come and get those minutes. If there is a critical matter, they can come and listen to the tape or buy a copy of the tape, which is readily available probably within 24 to 48 hours and listen to the tape themselves and hear verbatim exactly what had transpired at the meeting from the beginning to the end. Mr. Wearn continued that if there was a problem of perception, education would take care of the problem or the person should come and buy from the administrator's office a copy of the tape and sit down and listen to it. Mr. Crouse stated for purposes of confirmation that the tapes are readily available within 24 hours and the cost was $10. Mr. Wearn questioned whether any board member had comments in regards to having the minutes transcribed as soon as possible after the meeting. Mrs. McLean stated that the retirement meetings were several months apart and to have minutes approved three months later and then make them available did not always meet the needs of the membership. Mrs. McLean continued that there were times when employees would immediately question her about what happened in the meeting. She would like to be able to refer them to the minutes. She continued that it would be to their benefit to have them readily available on a timely basis. Mr. Wearn stated that unapproved minutes are public record and that they were available for copying once it prepared, which would happen four to six weeks after the meeting. Mr. Garvy questioned whether it would be possible to have the minutes ready within a month. Mr. Crouse stated that until about the last four years, the minutes were done elsewhere because we did not have the staff nor the time to put these out, and they were done more on a verbatim, and then they were summarized when they were brought into our office. Mr. Crouse continued that if it was the pleasure of the board, the efforts would be made to complete the unapproved minutes in a draft form in four weeks, and have them disseminated to the board members for their review. There would be a few exceptions to the four weeks, such as leave. Mr. Garvy questioned whether it was possible to have members come and listen to the tape instead of making the purchase. Mr. Crouse responded that to have someone come in and listen, the member would have to listen the tapes in the Town Clerk's office.

Mr. Wearn stated that the next item to discuss was that the minutes be transcribed in synopsis form, and the board agreed that they were currently being done in that form. Mr. Wearn stated that there was a combined utilization of synopsis and verbatim to ensure that the minutes were accurately reflected for the members, the Town and the tax payers.

Mr. Wearn stated that the next item to discuss was that any votes that were not unanimous should be roll called and recorded in the minutes. Mr. Wearn stated to his recollection the Board was currently in this practice. Mrs. McLean responded that during her first meeting with the board, she dissented on two separate votes and it was recorded as unanimous and that it had to be corrected in the minutes. Mr. Crouse stated that it might be good for Mr. Wearn to ask for a roll call since the board typically did not in the past, and that it was the Chair's prerogative to ask for a roll call. Mr. Wearn stated that when there was a dissenting vote, or that it be announced who is dissenting, so that it would be included in the minutes.

Mr. Wearn stated that the next item was that the unapproved minutes should be posted on the Town website. Mr. Wearn expressed his concern regarding posting the minutes on the website prior to approval. Mr. Wearn acknowledged the difficulty of getting to Town Hall due to construction, however the minutes can be faxed to whomever wishes to have them. Mr. Garvy questioned the possibility of the board members having the minutes in this one month time frame if they are available and having board members put forth their corrections or adjustments to the minutes, so that they could then be posted or available. The concern was that there was so much time that goes by that the issues that are being discussed become aged or lose interest in the part of the participants in the plan. Mr. McCracken stated if some member wanted the unapproved minutes, they were public record and anyone could request them. Mr. Crouse stated that if it was the pleasure of the board, the minutes could be mailed out to each member of the board as soon as they were done and every effort would be made to assure that they were done within the four week period of time following the meeting.

Mr. Wearn stated that the next item to discuss was that the recorded minutes should be available as public record and retained and destroyed in accordance with Town policy and Florida state statutes. Mr. Wearn stated that it was being done already. Mr. McCracken suggested that the minutes have a caption on each page that said "DRAFT". Mr. McCracken shared his concern that until the minutes were finalized, there was a risk that pages could get misplaced, and having the word "DRAFT" appended to the top of every page would avoid confusion. Mr. Garvy was in complete agreement and stated that "UNAPPROVED DRAFT" would be good to have on each page. Mr. Wearn also agreed.

Mr. Wearn stated that concerning the agendas, it was previously discussed at the last meeting that the agendas were being posted two days prior to the meeting being held. Mr. Wearn stated the agenda did not need to get legally posted earlier than that time. Mr. Wearn continued that all board members receive the agenda earlier than that and there was nothing to prohibit from taking the tentative agenda and posting it at the workplace area on a bulletin board. Mrs. McLean recommended distribution of the tentative agenda via e-mail. Mr. Bradford stated that Mrs. McLean's request was possible was a normal practice in the Town Manager's office. Mrs. McLean also stated that the agenda was not as detailed as she felt it could be, and she was looking for improvement in that area. Mr. Crouse expressed the difficulty in knowing what the speakers would present until the moment would come. Mr. Bradford questioned how Mr. Crouse felt regarding the distribution of the agenda at some point prior to the meeting electronically. Mr. Crouse responded that he did not have a concern with the electronic distribution, as long as it went to the employees that it really affected. Mr. Bradford stated that perhaps in an upcoming newsletter, it could be said that all general employees who were interested could submit their e-mail addresses to Human Resources and that they would receive all future general employee pension board agendas via e-mail. Mr. Crouse stated that it would create a large volume of work than just sending it to everyone. Mr. Bradford suggested than to make it easier, to simply post the tentative agenda on the website. Mr. Garvy suggested posting the tentative agenda one week prior to the meeting. Mr. Crouse stated that it was acceptable and that this agenda was in fact posted last Friday. Mrs. McLean agreed that it would meet the expectation. Mrs. McLean clarified that she was just requesting little steps to bring the board into what she felt was compliant with the Sunshine Law. Mr. McCracken stated those were not Sunshine issues, they were issues which were the tip of the iceberg. Mr. Wearn stated that all of the issues addressed were brought up at the meeting to ensure that the items were being covered at the meetings. Mr. Wearn stated that he would not want to see the Board tied to a black and white policy. Mrs. McLean stated that she would cancel her request for an official written policy and she would be willing to adhere by the directives that were discussed and that they were more than acceptable.

Mr. Madison stated that the November 2002 retirement meeting was on the intranet, however the February 2003 and May 2003 meeting minutes were not. Mr. Crouse stated that these files had been sent to IS for posting. Mr. Madison stated that it was understood that IS had an extremely busy department, however it would be nice to have the minutes posted in a more timely manner. Mr. Bradford stated that Peter Elwell and himself were working on an administrative procedure that would require approved minutes to be posted on the intranet within 48 hours after a board has approved the minutes. As a result, Mr. Bradford stated that any minutes that had not been posted, should be brought to Mr. Crouse's attention. Mr. Crouse agreed to make sure that IS posted the minutes in a more appropriate time frame.

With no further questions, Mr. Wearn thanked Mrs. McLean for her presentation.

X. **DISCUSSION OF 2% DROP REDUCTION**

Mrs. McLean presented a discussion of the two percent reduction, a copy of which is on file with the Plan Administrator.

Mrs. McLean stated that the 2% permanent reduction in the pension for the people who DROP, was written administratively. Mrs. McLean continued that it was currently being used as an adjustment in order to keep the fund cost neutral. Mrs. McLean stated that in talking with other people and funds about this issue, it had been realized that the DROP program was cost neutral in almost its very existence. Mrs. McLean stated that to use the 2% that was in the ordinance written administratively, as a way of reducing a problem that the board created, was not the right way to go. As a result, Mrs. McLean requested that the 2% reduction be dropped. Mrs. McLean continued that she did contact via e-mail to members of other boards and asked them if they had a 2% DROP or if they have any kind of reduction for their participants to DROP. Mrs. McLean stated that she asked these other members two questions, one, is their plan cost neutral, and number two, did their employees have any kind of reduction in their DROP. She then stated that she was only able to get a few responses to both questions, however, she was not able to find anyone who had any kind of DROP or penalty to their pension plan for their employees. Mr. Garvy questioned whether any of these plans had a guaranteed 7.5%. Mrs. McLean responded that she did not know the answer to that question. Mr. Wearn commented on the survey, that he was aware that Mrs. McLean was disappointed in the results that were obtained, however there were probably many more funds in the state of Florida and the survey results were too narrow and too few to statistically consider. Mr. Wearn then stated that in 1997 it was recommended that the DROP be modified to include the 2% reduction, as it would eliminate an employer and employee contribution rate increase, which was directly discussing cost neutral. Further discussion was held regarding the summary of valuation benefits considered by Gabriel, Roeder, Smith in 1997. Mr. Wearn stated that if it was the pleasure fo the board to do something about the matter, he suggested that the board consider going back and asking if the five year report of Gabriel, Roeder, Smith was still active, or if there was a change and be prepared to pay whatever the charge would be for that change. Mr. McCracken stated that even though he was not on the Board, he was there at the time, and did remember that it was quite a problem because the actuary took the position to make the program cost neutral this charge was necessary, otherwise it would not be cost neutral. Mrs. McLean questioned whether Public Safety was cost neutral and they do not have a reduction. Mr. Wearn stated that they do not incur any charge that would have to be funded and the Gabriel, Roeder, Smith report shows that they are cost neutral because of that reason. Mr. Wearn proceeded to show Mrs. McLean the report which provided a better explanation and brief discussion was held. Mrs. McLean requested to see a new report, since the board now had historical data available of the people who had previously dropped, and could get a flavor for what the preference was whether to DROP or not. Mr. Wearn stated that the Board would need to be prepared for an adverse result. Mr. Wearn then stated that it could be more than two percent. Mr. Garvy stated that it could take that particular turn if it took into account the seven and a half percent guaranteed that was embedded. Mr. Crouse stated that the seven and a half percent had created a loss to the entire plan. Mrs. McLean stated that she was not sure the board could assign that loss to the employees. Mr. Wearn stated that already having a policy in place, the state actuary could not make changes, however, if he were to find out that it went to five percent, for example, the board would have to be prepared to accept what remedies or actions the actuary would have. Mr. Wearn requested the pleasure of the Board. Mrs. McLean stated that she would withdraw her request for a review of the reduction. Mrs. McLean stated that she would bring the topic up a future meeting for discussion.

## XI. DISCUSSION OF EMPLOYEE REQUEST FOR BENEFIT ADJUSTMENT

Postponed to a later date.



## XII. ANY OTHER MATTERS

Mr. Garvy stated that he would like to recommend limiting the presentations by the money managers to ten minutes. Mr. Wearn stated that he was not in disagreement, however he did recognize the fact that some managers were on "watch", and they felt compelled to be as specific as they can. Mr. Wearn suggested that if the board perceives that there are many items to discuss, then the speakers could be informed to limit the presentations. Mr. Garvy stated that they need to have a rough idea of what their time frame is, possibly ten to twelve minutes, however that could vary depending upon the circumstances and our questions. Mr. Wearn requested that Mr. Crouse circulate a memo to the money managers expressing ten to twelve minute presentations and if they needed more time at the outset, then they can request more time to discuss certain issues. The Board was in agreement. It was clarified that the limitation did not include Callan Associates.

Mr. Madison commented that both he and Mrs. McLean appreciated the opportunity to attend the convention in Orlando in July. Mr. Madison continued that in October, there was another class, which would be the start of the FPPTA Trustee training. Mrs. McLean stated that the attendance and participation was outstanding. Mr. Madison expressed his appreciation to the Board and Town for the retirement system and the opportunity to participate.

Mrs. McLean stated that regarding Mr. Martino's letter, she felt there were two or three years where the employee contribution was actually in excess of the Town contribution, at least two years or three years in a row, and she felt Mr. Martino should be aware of the fact. Mr. Wearn stated that the information that Mrs. McLean was stating was in fact in the response that Ms. Skittone had sent to Mr. Martino.

XIII. **ADJOURNMENT**

**There being no further business, Mr. Garvy moved to adjourn. Mr. Madison seconded, and the motion carried unanimously.**

The meeting adjourned at 2:16 p.m.

Approved: ______________________
Patricia McLean, Secretary