

**CITY OF OWOSSO
EMPLOYEES RETIREMENT SYSTEM BOARD**

AUGUST 20, 2009

7:10AM

CALL MEETING TO ORDER:

Chairperson Farrell called the meeting to order at 7:10 a.m.

ROLL CALL:

PRESENT: Trustees Michael Bruff, Michael McCloskey, Mark Mitchell, James Treadway, Vice Chairperson Frances Kukulis, and Chairperson Wilfred Farrell.

ABSENT: Trustee Mark Owen.

ALSO

PRESENT: City Attorney William C. Brown; Merrill Lynch Advisor Maral Thomas; and Merrill Lynch Investment Consultant Marie Vanerian;

APPROVE AGENDA:

Motion by Trustee McCloskey to approve the Agenda as presented with the move of Payment Authorization items d, g, and h to New Business.

Motion supported by Trustee Bruff and concurred in by unanimous vote.

APPROVE MINUTES OF JUNE 18, 2009 REGULAR MEETING:

Vice Chairperson Kukulis noted a typo in the sentence noting the motion to set the interest rate at 5% and asked it be corrected. She also asked that an item examining the method for determining the contribution required for each group within the system be placed on the October agenda.

Motion by Vice Chairperson Kukulis to accept the minutes, amending the date from April 19, 2009 to April 16, 2009.

Motion supported by Owen and concurred in by unanimous vote.

CITIZEN COMMENTS:

There were no citizens comments.

CONSENT AGENDA:

Motion by Trustee Bruff to approve the consent agenda as follows:

Approve Pension Check Reports:

- | | |
|--------------|---------------|
| a. June 2009 | \$ 124,122.68 |
| b. July 2009 | \$ 123,660.31 |

2. **Approve Statements:**

- a. **Alliance Bernstein**
As of June 30, 2009

- b. MD Sass
As of June 30, 2009
- c. Franklin Templeton Investments
As of June 30, 2009
- d. Merrill Lynch Consulting Services
May 31, 2009 Year to Date Summary
- e. Merrill Lynch Consulting Services
June 30, 2009 Year to Date Summary
- f. City of Owosso Employees Retirement Fund
June 30, 2009

3. Payment Authorizations:

| | |
|---|--------------|
| a. <u>Rigel Capital, LLC</u> For period 07/01/09 through 09/30/09 | \$ 7,764.79 |
| b. <u>M.D. Sass</u> For period 04/01/09 through 06/30/09 | \$ 7,552.87 |
| c. <u>Franklin Templeton Investments</u> For period 04/01/09 through 06/30/09 | \$ 10,113.66 |
| d. <u>Merrill Lynch - AllianceBernstein</u> For period 04/01/09 through 06/30/09 | \$ 3,038.02 |
| e. <u>Wentworth, Hauser, and Violich</u> For period 04/01/09 through 06/30/09 | \$ 2,870.00 |
| f. <u>Ronald J. Tobey, City Treasurer</u> Report of Checks Written – June 2009 | \$146,016.70 |
| g. <u>Ronald J. Tobey, City Treasurer</u> Report of Checks Written – July 2009 | \$125,947.80 |

Motion supported by Trustee McCloskey and concurred in by unanimous vote.

COMMUNICATIONS:

- o James Koss, Gabriel Roeder & Smith – 2010 projected actuarial fees
- o Amy K. Kohagen, City Clerk – Rigel purchase of SPDR Sector Index Funds
- o The Vanerian Group – Invitation to dinner at MAPERS Conference

The following communications, publications and conference announcements are on file with the City Clerk – if you would like to read them, please contact her:

- Merrill Lynch: *Comprehensive AIM Report, Q1 DVD*
- MD Sass – Investment Outlook & Strategy Commentary
- CMA Money Fund: *Annual Report March 31, 2009*
- Coughlin Stoia Geller Rudman & Robbins: *Corporate Governance Bulletin, 3Q 2009*
- Institutional Investor: *June and July/August 2009*

MONEY MANAGER REPORT:

RIGEL CAPITAL, LLC – Christopher Reynolds, Senior Vice President

Mr. Reynolds thanked the City for its business. He indicated the portfolio is up 9% year to date, the benchmark is up 22%. He gave a brief overview of the financial conditions for the year and noted this has been a very different year. Rigel started the year with a very defensive posture. The immediate, and unexpected, turn in the market caught them unprepared as low quality equities outperformed high quality equities. Though they will not entertain the idea of purchasing poor quality stocks they have made adjustments in their sector weighting to take advantage of the upturn. Looking to the future they will continue to hold high quality stocks as all indicators point toward the purchase of such equities. Mr. Reynolds again went on to say what an unusual year we have had and said he felt the portfolio should do fine once the market becomes more rational.

Chairperson Farrell inquired if the transition from George Kauffman as CEO to Richard Stice had any effect on the performance of the portfolio. Mr. Reynolds indicated Kauffman and Stice had worked together closely for over 3 years and Mr. Kauffman was still accessible if needed. The firm has also brought in a retired CEO to provide experience and a calming influence in day to day operations.

Merrill Lynch Consultant Vanerian indicated many investment firms she works with have seen low results similar to Rigel's. She went on to say the steep decline then subsequent steep up-tick in the economy has been an issue for many firms focused on quality. Mr. Reynolds echoed her remarks saying the portfolio underperformed not because of what was in it but because of what was not in it. Rigel focuses on quality and requires a substantial amount of confirmation of that quality before they make a move.

The Board briefly asked Mr. Reynolds about the request from Rigel to allow the purchase of equities for firms worth \$3 - \$5 billion. Mr. Reynolds explained the huge decline the market experienced last year is reflected in over all lower net worth of the companies listed in the Russell 1000 Growth Index, thus the universe of available equities \$5 billion and over has decreased significantly. In order to maintain the same number of stocks in their universe Rigel has requested the City's permission to purchase companies with a net worth less than the previous floor of \$5 billion. The portfolio will continue to be a large cap portfolio with most holdings worth \$5 billion or more, this change will just allow them to purchase companies in the range of \$3 - \$5 billion if their process indicates they are quality investments.

Lastly, the Board inquired why Rigel was purchasing sector index funds in the last two quarters. Mr. Reynolds indicated the sector index funds allowed the firm to take immediate advantage of rallies in certain sectors while they search for specific stocks within that sector. Ms. Vanerian indicated this is a prudent tactic that has been used many times in the past.

OLD BUSINESS:

MERRILL LYNCH STATUS REPORT

Merrill Lynch Consultant Vanerian indicated Bank of America had hired Sallie Krawcheck to head the Global Wealth and Investment Management Group. She is a veteran investment banker from Citigroup and Sanford Bernstein. Ms. Vanerian indicated she felt this change was a good one as Ms. Krawcheck replaced a former consumer banking executive as the head of investments.

City Attorney William C. Brown indicated he had reviewed the Atlanta Capital hiring agreement and passed it on to Merrill Lynch who then submitted it to outside counsel. It is hoped this counsel will be advising Ms. Vanerian shortly. She will report back to City Attorney Brown at that time.

NEW BUSINESS:

AMENDMENT TO MARKET CAPITALIZATION RANGE

Rigel requested permission to lower the floor on large cap equity purchases from \$5 billion to \$3 billion. Their reasoning for doing so was detailed in a letter of agreement as follows:

“As you may be aware, every year in June, Russell reconstitutes its indexes to provide a more accurate reflection of the market's current composition. Since this process occurs only once a year the changes can be quite dramatic depending on the preceding market environment. This year, given the considerable market volatility, resulted in some of the more significant modifications on record. As a result of these recent changes, our benchmark, the Russell 1000 Growth, has seen large shifts in sector weightings and a downward movement in market capitalization. After the most recent reconstitution, the median market cap went down from \$5.42B on 6/30/2008 to \$3.53B on 6/30/2009, suggesting that a greater number of stocks below \$5B were added to the index.

Today, 60.5% or 380 stocks of the 628 stocks in the Russell 1000 Growth have a market cap below \$5B. This is significant because Rigel adheres to the strict covenant mandating a minimum market cap threshold of \$5B for securities in our large cap portfolio. Maintaining the covenant would effectively eliminate over half the universe of stocks in the benchmark from our consideration.

After careful analysis, we have determined it is in our clients' best interest to amend our strategy to define the market cap range by the market capitalizations of companies in the Russell 1000 Growth. It is not our intention to alter the characteristics of the portfolio away from our mandated Large Cap Growth style but to utilize, when thorough analysis dictates, the full universe to which we are compared so we may best add value for our clients.”

Vice Chairperson Kukulis inquired whether the City Attorney had any concerns about the adjustment. He indicated he did not.

Motion by Vice Chairperson Kukulis to approve the letter of agreement authorizing Rigel Capital to lower the floor on large cap equity purchases to \$3 billion.

Motion supported by Trustee Bruff and concurred in by unanimous vote.

2008 SUMMARY ANNUAL REPORT AND LIST OF EXPENSES PAID BY SOFT DOLLARS REPORT

Motion by Trustee Mitchell to accept the 2008 Summary Annual Report and List of Expenses Paid by Soft Dollars Report as follows:

CITY OF OWOSSO EMPLOYEES RETIREMENT SYSTEM

2008 Summary Annual Report and List of Expenses Paid by Soft Dollars

The Public Employees Retirement System Investment Act requires the City of Owosso Employees Retirement System to prepare and issue a summary annual report and to publish and make available annually a list of all expenses paid by soft dollars. The following information is provided for the year 2008.

The name of the retirement system is the City of Owosso Employees Retirement System. The Retirement System's investment fiduciaries are:

BOARD OF TRUSTEES: Michael Bruff, Wilfred Farrell,
Frances Kukulis, Michael McCloskey,
Mark Mitchell, Mark Owen,
James Treadway.

INVESTMENT MANAGERS: Alliance Bernstein
Franklin Templeton Rigel Capital
MDSass
Wentworth Hauser & Violich City of Owosso Employees
Ret. Board (for Small-Cap)

As reported in the actuarial valuation for the annual period ending December 31, 2008 the Retirement System's valuation assets were \$32,567,350 and its actuarial accrued liabilities were \$31,041,763, which produced a funded ratio of 104.9.

For the annual period ending December 31, 2008 the Retirement System's investment performance on a mark to market basis (net of manager fees and transaction costs) was -24.9%. On December 31, 2008 the market value of the assets was \$24,660,946.

For the annual period ending December 31, 2008 the Retirement System's non-soft dollar expenses were \$200,332 and benefit payments and member refunds were \$1,497,099. Expenses paid by soft dollars totaled \$36,225. Employer contributions required for the year covered by the report total \$328,824.

Motion supported by Trustee McCloskey and concurred in by unanimous vote.

EARLY RETIREMENT PROPOSAL

City Manager Joseph Fivas detailed the proposal as follows: all employees reaching 58 years of age by December 31, 2009 and having at least 10 years service to the City are eligible to retire with full pension benefits. Each of these employees will also be eligible for a \$10,000 incentive payment that will be used in calculating the final average compensation for the employee. The last day of service for those eligible for early retirement will be December 31, 2009. The intent of the program is to reduce/eliminate some positions to save money. Replacements could also be hired at a lower wage, further saving the City money. He went on to detail the increasing costs of health care, energy, retirement system costs, and DEQ expenses along with lower revenues due to declines in property values and the anticipated loss of a portion of State shared revenue. At least 5 people will need to take advantage of the proposal in order to see a true cost savings, any number lower than this could result in a retraction of the offer. The proposal would have an increased impact on the Retirement System of approximately \$415,000. It is intended the City pick up the cost for this proposal over the course of the next few decades.

There was inquiry whether the Board's approval of the proposal was required. City Manager Fivas indicated that while the Board's approval was not required he would give a high level of deference to the feelings of the Board and wouldn't feel comfortable taking a proposal to Council that did not have their support. City Attorney William C. Brown indicated he agreed with Mr. Fivas's analysis. He went on to say an ordinance amendment would be required to institute the proposal.

There was significant concern whether Board members would be protected from litigation given they do not have the ultimate power in deciding if the proposal should be instituted. City Attorney Brown indicated that while Board members could not insulate themselves from litigation completely, if the system should come under action it would be difficult to prove any underfunding was a direct result of this proposal, also the City carries insurance for just such occasions. He also indicated that Board members could not be held responsible for the actions of City Council.

It was asked whether the potential retirees would have to contribute 6% of their \$10,000 incentive payment to the fund. It was noted they would have to do so to have the money included in their final average compensation.

There was concern how the money would be reimbursed to the System and whether the City would be paying back the System in the 5-year time frame suggested by our actuary Gabriel Roeder Smith. There was also concern whether the City would pledge not to raise employee contribution rates to make up for

the extra cost of the proposal, as the participants in the system were not those initiating the proposal nor could they pull their funds from the system should it be enacted against their better judgment. It was responded the City intends to pay the System back over the course of time using the cost aggregate method. City Manager Fivas noted that while he agrees philosophically with the idea of paying the system back quickly, the City would lose any potential costs savings in doing so. The City was not willing to pledge employee contributions would not go up should this proposal be enacted as there was no guarantee of future economic conditions, nor could the actions of future Councils be predicted.

There were questions regarding whether an early retiree's final average compensation would be lower or higher than normal should they take advantage of this proposal. It was noted they would receive approximately the same pension payment they would have should they have retired at the normal age of 60 due to the inclusion of the \$10,000 incentive payment in the final average compensation computation.

It was asked whether the union groups involved in the pension system would potentially be responsible for funding any part of this proposal. It was noted that while Gabriel Roeder Smith has suggested a change in the method in which funds are distributed among the different groups in the system, use of the current method would prevent the union groups from shouldering any of the costs of the proposal.

There was discussion on how the amount of the \$10,000 incentive payment was reached, concern whether the City would be able to afford the payments required in the future, and the total cost savings of the program (approximately \$250,000 annually if 50% of the departing employees are replaced). There was also question whether the Board would be consulted again should 4 people elect to take advantage of the proposal. It was indicated the City Manager would make the final determination whether the proposal would be retracted in such an instance.

A portion of the Board requested to see the entire actuarial report submitted by Gabriel Roeder regarding the early retirement proposal. It was noted there was personal information included in the report and it would not be released. The Board asked all sensitive information be redacted and the report released for their examination. The City agreed to do so.

City Attorney Brown asked when the City would be looking for a decision on the matter. City Manager Fivas noted he was hoping for a response this morning. Mr. Brown went on to address the Board regarding its fiduciary duty, suggesting a phone call to our insurance company may allay some fears of litigation. He also indicated that when drafting an ordinance to enact this proposal a provision could be added requiring the City pick up the cost for the proposal to further mitigate fears that system participants would shoulder the cost of the program. He suggested a possible special meeting to allow time to gather more information. One member indicated he was not in favor of another meeting and was prepared to render a decision today.

A second meeting was considered but turned down as an option due to scheduling conflicts.

City Attorney Brown reminded the Board that they had a recommendation and accompanying actuarial report in front of them and they had conducted robust discussion thus fulfilling their fiduciary duty in examining the proposal.

Motion by Vice Chairperson Kukulis to support the early retirement proposal as presented with the stipulation Council be informed the goal of the Board was to make sure the costs of the program not be shouldered by system members and that Council be asked to review the City's insurance to ensure Board members are properly covered for liability.

Motion supported by Trustee Bruff.

Roll Call Vote.

AYES: Vice Chairperson Kukulis, Trustee Bruff, and Chairperson Farrell.

NAYS: Trustees McCloskey, Mitchell, and Treadway.

ABSENT: Trustee Owen.

INVESTMENT CONSULTANT REPORT – 2nd QUARTER 2009

Merrill Lynch Consultant Marie Vanerian noted that the government has pumped an amount equal to 30% of GDP into the economy in an effort to prop it up. There was question whether the economy would be able to sustain its current level if the government pulls back. She noted the savings rate for the country had increased overall, though an increase in the savings rate indicates less spending and therefore a lower GDP. She went on to say that things are not necessarily getting better but the rate of decline has significantly decreased. There was hope the economy would see growth in the 3rd quarter, but Ms. Vanerian cautioned saying she expects unemployment not to peak in mid 2010.

All the current money managers are up so far for the third quarter, except Rigel and Atlanta Capital (our contract with them has yet to be finalized). Ms. Vanerian has been monitoring Rigel due to their lack of performance, though she pointed out that all firms with a buy/sell strategy similar to Rigel's have suffered from the same lack of performance. Rigel will be put on formal watch if they do not show progress by December 2009.

In summary, Ms. Vanerian noted she is pleased with the third quarter so far but would not be surprised if we see another market correction in the near future, though not as low as last year's correction.

Ms. Vanerian presented an overview of the following:

Total Portfolio Performance Summary for Period Ending 06/30/2009

| | Source of Funds Thousands of Dollars | | |
|----------------------------|---|--|---------------------------|
| | Quarter | | Cumulative 12/91-06/09 |
| Beginning Market Value | 23,632 | | 16,702 |
| Net Contributions | -360 | | -13,525 |
| Investment Earnings | -1,918 | | 22,014 |
| | ----- | | ----- |
| Ending Market Value | 24,815 | | 25,191 |

Trustee Treadway inquired about the performance of the firms included in our money manager searches. Ms. Vanerian indicated she would have a report for the Board in October.

PAYMENTS

Chairperson Farrell inquired whether Franklin Templeton usually bills separately for its investment services and its custodial services (for our former 5/3 equities). It was noted they do bill separately. He also asked whether the invoice from Gabriel Roeder Smith was higher than anticipated. It was indicated it was slightly higher, though when the budget was set for the system the previous year we were not in receipt of an estimate of charges for the year. It was further noted that while this cost exceeded budget the system would come in under budget overall. Lastly, Chairperson Farrell inquired about the invoice from Gabriel Roeder Smith for \$624, asking what it was for. It was noted a Gabriel Roeder Smith representative consulted with the City Manager regarding the early retirement proposal. It was also noted the system would be reimbursed for this amount.

Motion by Vice Chairperson Kukulis to approve the following payments:

1. Franklin Templeton Investments – former Fifth Third equities
For period 04/01/09 through 06/30/09 \$ 300.00

2. Gabriel Roeder Smith & Company
For period 07/01/2008 through 06/30/2009 \$ 17,500.00
3. Gabriel Roeder Smith & Company
Consultation 06/18/2009 \$ 624.00

Motions supported by Trustee Treadway and concurred in by unanimous vote.

CITIZENS COMMENT:

There were no citizen comments.

NEXT BOARD MEETING:

The next board meeting is scheduled for October 15, 2009 at 7:00am

ADJOURNMENT:

Motion by Trustee Bruff for adjournment at 10:06 a.m.

Motion supported by Vice Chairperson Kukulis and concurred in by unanimous vote.

Amy K. Kohagen, City Clerk