CORAL GABLES RETIREMENT SYSTEM
Minutes of March 13, 2014
Youth Center Theater/Auditorium
405 University Drive
8:00 a.m.

MEMBERS:	F 13	M 13	A 13	J 13	A 13	S 13	O 13	N 13	J 14	F 14	M 14	APPOINTED BY:
Andy Gomez	-	-	-	-	P	P	P	P	P	P	E	Mayor Jim Cason
Manuel A. Garcia-Linares	P	P	P	P	P	P	P	P	P	P	P	Vice Mayor William H. Kerry, Jr.
Bob Campbell	-	-	-	E	E	P	P	E	P	E	P	Commissioner Patricia Keon
Jon G. Ridley	-	-	-	-	-	P	P	E	P	P	P	Commissioner Vince Lago
James Gueits	P	P	P	P	P	P	P	P	P	P	P	Commissioner Frank C. Quesada
Joshua Nunez	-	-	-	-	-	P	P	E	P	E	P	Police Representative
Randy Hoff	P	P	P	P	P	P	P	P	P	P	P	Member at Large
Donald R. Hill	P	P	P	P	P	P	P	P	P	P	P	General Employees
Troy Easley	P	P	P	P	P	P	P	P	P	P	P	Fire Representative
Diana Gomez	-	-	-	-	-	-	-	P	P	P	P	Finance Director
Elsa Jaramillo-Velez	-	-	-	-	-	-	-	P	P	P	P	Human Resources Director

STAFF:
Kimberly Groome, Retirement System Administrator
Alan E. Greenfield, Board Attorney
Dave West, The Bogdahn Group

P = Present
E = Excused
A = Absent

GUESTS:
Craig Leen, City Attorney
Ron Cohen, Rice Pugatch Robinson & Schiller
Colleen Brennan, Northern Trust
Jivko Chiderov, Northern Trust Securities Lending
James Dominguez, Northern Global Investments

Vice-Chairperson Randy Hoff calls the meeting to order at 8:08 a.m. There was a quorum present. Mr. Campbell and Mr. Nunez were excused.

1. Roll call.

2. Presentation of the 2013 State Annual Report and final 2012-2013 audit report by Goldstein Schechter Koch. *(Agenda Item 5).*

   Clement Johns informs that he is presenting the State Annual Report for approval so they can have the report signed and can send it onto the State. The annual report reports supplemental schedules. The entire report is over 200 pages. The annual report is just a copy of the financial statements and supplemental information required by the State for compliance purposes.

A motion was made by Mr. Hoff and seconded by Mr. Hill to approve the State Annual Report. Motion unanimously approved (11-0).

3. Consent Agenda. *(Agenda Item 2)*

All items listed within this section entitled "Consent Agenda" are considered to be self-explanatory and are not expected to require additional review or discussion, unless a member of the Retirement Board or a citizen so requests, in which case, the item will be removed from the Consent Agenda and considered along with the regular order of business. Hearing no objections to the items listed under the "Consent Agenda", a vote on the adoption of the Consent Agenda will be taken.

2A. The Administrative Manager recommends approval of the Report of the Administrative Manager.

2B. The Administrative Manager recommends approval for the following invoices:

1. The Bogdahn Group invoice no. 9688 dated February 18, 2014 for Performance Evaluation and Consulting Services from October 1, 2013 to December 31, 2013 in the amount of $36,250.00. This invoice is in accordance with the contract between The Bogdahn Group and Coral Gables Retirement System signed on June 1, 2008 and in accordance with the fee increase approved by the Board and signed by the Chairperson on April 28, 2011.
2. GRS invoice #405559 dated February 12, 2014 for actuarial consulting services rendered during the months of December 2013 and January 2014 in the amount of $8,602.00.
3. Nyhart invoice #0100643 dated January 31, 2014 for actuarial consulting services from January 3, 2014 through January 31, 2014 in response to questions from new actuary regarding pensionable pay and components of liabilities in the amount of $540.00.

A motion was made by Mr. Garcia-Linares and seconded by Mr. Hoff to approve the Consent Agenda. Motion unanimously approved (11-0).

4. Items from the Board attorney. *(Agenda Item 3).*

Alan Greenfield reports that they have had a quiet monthly legally. He has worked on a number of matters with Ms. Groome but it is nothing that needs to be brought to the Board’s attention. He sent letters out as requested by the Board to the Mayor and Commissioners and to the State and County Ethics Commissions regarding the Finance Director/Trustee seat on the Board. He received a response from the State saying that it was not an ethics matter to be considered by the State and that it is a legal matter where you either change the ordinance or you went to court. Those were some of the comments in the letter received by the Ethics Commission. He hasn't been in contact with the Ethics Commission in Dade county. He understands that the head of the Commission is on vacation and will not be back until this week. He has not received any response from the City or any of the Commissioners relative to the other letter that was sent. It didn't require a response but he would have thought they would have had a response.

Mr. Leen states that Robert Meyers who was the former director for the County Ethics Committee is currently an attorney for Weiss Serota. He asked Mr. Meyers to send something regarding this issue and he did. Mr. Greenfield informs that he did not receive a copy of that letter.

5. Discussion regarding the 2013 Cost of Living increase for retirees.

Mr. Greenfield informs that he was going to speak on the matter dealing with COLA which is an important issue as an attorney item but it is a separate item on the agenda. He has read Mr. Cohen's letter and has read the letter from the actuary. He spoke to Mr. Cohen this morning and asked him about the status of the lawsuit that was pending against the City relative to the COLA. If the Board recalls they granted the COLA last year. It went to the Commission and the Commission reversed the Board. A lawsuit was filed by one of the employee groups and that lawsuit is pending in the Court system. The ultimate result of that lawsuit would be that either the City wins and no COLA should have been granted or that the City loses and the COLA should have been granted and the COLA then would be granted. His opinion is that the Board should table the question of COLA for this year. He doesn't think they should take any action. He thinks it would be a useless action for the Board to say that under the ordinance they have met that threshold and grant the COLA. Then it would then go to the Commission, the Commission would take the same position they took last year and that would be added to the present lawsuit. He thinks that would be a waste of time, effort and energy on everyone's part. He thinks if they table the issue until the outcome of the lawsuit they would know whether there was or was not the ability to grant the COLA.

Mr. Cohen raises some very interesting issues in his letter. He thinks it would be very helpful if they had a workshop session, open to the public, where they can discuss these things and not take any action. Mr. Cohen can present these issues and the City can respond to them. It would be in a workshop atmosphere and then the Board can see if they feel they want to take any further action. In the meantime they will see the progress of the lawsuit. He understands there are motions to dismiss that have been filed that are coming up for hearing on one count. That is his recommendation relative to the COLA issue.

Mr. Garcia-Linares asks Mr. Greenfield if nothing is changing from last year to this year. Mr. Greenfield responds that it is not. Mr. Garcia-Linares clarifies that it is the same issue before the Board. Mr. Greenfield answers affirmatively.

A motion was made by Mr. Garcia-Linares and seconded by Mr. Hoff to table the issue until the final decision of the Court.

Discussion:
Mr. Hill asks how long the lawsuit will take to go through the court. Mr. Greenfield does not know. It depends on the judge and the judge's calendar. It depends on how aggressive the attorneys are in pushing the case forward.

Chairperson Gueits asks Mr. Leen if there is anything procedural he can tell the Board with respect to the status of the case. Mr. Leen responds affirmatively. He explains that the City filed a motion to dismiss. It is pending. They filed an earlier motion to dismiss and he believes the plaintiffs amended their complaint. Then they brought another motion to dismiss. The motion to dismiss is targeted at the breach of contract count. There is also an ordinance count which the City plans to address the summary judgment. Chairperson Gueits asks if that is a breach of the ordinance. Mr. Leen states that basically that the plaintiffs are saying that the City violated the ordinance. Their positions are pretty clear in this lawsuit. The City is saying that State Law requires the City to take a certain act which he wrote an interpretation on and would like to put in the record. The plaintiffs are saying that the City is violating the ordinance and State Law doesn't preempt or prevent them from paying the COLA. So that issue is going to be decided likely at summary judgment in his view which they would file after the motion to dismiss this is addressed.

He would like to address one point in the letter which is the view that the City has the duty to pay the COLA even if the money doesn't come out of the pension fund and that the City has a duty and a contract to pay it. He thinks that what is being implied is that the Commission would take it out of general revenues. There are a couple of provisions in the pension code and the City Code that say that the benefits under the pension plan are not to be paid out of anything but the pension. There are expressed provisions that say that. Their view is that if State Law indicates that it can't be paid out of the pension plan it can't be paid out of City funds based on the ordinance that has existed for many years. That is their position. They do have specific provisions they have cited in the opinion in paragraph 3 so he did want to make clear that they don't agree on that issue although he does understand what he is saying.

Chairperson Gueits asks Mr. Greenfield if the decision in the pending case be dispositive on the issue of the granting of future COLAs. Mr. Greenfield answers affirmatively.

Ronald Cohen of Rice Pugatch Robinson & Schiller, P.A. states that he didn't mean to say that the COLA should be paid out of City coffers. They believe it gets paid out of this plan and he thinks the Board should consider pre-funding it. He thinks that is something they can consider at a workshop. He understands they got the letter from GRS this last week and they got his letter late last night. Ms. Groome was kind enough to send him the actuary's letter and they put together their letter as quickly as they were able to. He has no problem with the motion of tabling it. It may be okay to table it until after the lawsuit. He just asks that the motion considered is that the issue be tabled for today. Then they can schedule the workshop but they shouldn't preclude themselves or anyone from coming back before the Board sometime before the lawsuit is over if someone thinks the Board needs to take action one way or the other.

Mr. Garcia-Linares asks if they think the City will come forward and have a workshop where they have informal discussions during the lawsuit. He doesn't see that happening during the pending of the lawsuit. Chairperson Gueits asks if there has been any settlement discussion that they can couch as a workshop. Mr. Cohen responds negatively. He thinks they all can hold a workshop. He thinks they should consider that because they have a new actuary now. He thinks there are considerable funding issues about the COLA. Mr. Garcia-Linares states that there is a defining legal issue. Mr. Cohen has one interpretation and the City has another interpretation. Until a court authority says who is right on the interpretation what is the point of a workshop?
Mr. Cohen thinks he should let Mr. Greenfield answer that but he would just ask if they want to table it to today that is certainly understandable. He just asks that they don't preclude any interested party or any of the stakeholders from coming before the Board at some point before the lawsuit is over and saying that they have a reason why they think the Board should consider the issue again. He doesn't think they should foreclose on that today. Chairperson Gueits thinks that is reasonable.

Mr. Greenfield informs that when he had suggested a workshop he suggested it based on the fact that perhaps it would be a vehicle of getting the parties together and maybe there could be a settlement made. It was just a vehicle because at some point in time the court might say to them they are going to go to a mediator. You don't go to trial before you go to a mediator and so if they are going to go to a mediator and sit there and talk about their perspective positions they might as well do it early and save money for everyone. That was one of the thoughts he had. It doesn't mean they have to sit down and it doesn't mean they have to mediate. It doesn't mean they have to settle. He was just thinking when you get people together who have different issues things might happen.

Chairperson Gueits asks Mr. Greenfield if there is any scenario where he can see the two sides reconciling their interpretations of the ordinance because that is what this is about at the end of the day. Mr. Greenfield answers affirmatively. That is why he thought a workshop would be good because Mr. Cohen brings up an issue that is not in the lawsuit per se. His letter brings up an issue of funding and where the money could come from. If you take his issue as a separate item it circumvents the problems that are presented in the lawsuit. If the Board would agree with his position that the Board has a way of funding this then there would be a COLA granted. The Commission would or would not approve it and it may or may not go forward but he thought at least to be fair to everyone and to let everyone speak to the Board and it wouldn't be in a formal Board meeting. Workshops do have a benefit in letting everyone speak officially but there is no action taken by the Board at all. That is why it was his suggestion.

Mr. Leen states that the interpretation he made regarding actuarial experience is not subject to settlement. He has given that opinion and that is his view of the law. Under the Code he is the one who gives it. He doesn't compromise those sorts of things. They sent it to the Division of Retirement and the Division of Retirement agreed with his interpretation. Now the issue is in Court and the Court can certainly overturn it. If it is overturned he will follow whatever the Court says. They might appeal if they lose though. It is a big case for the City because they are in substantial deficit regarding the actuarial experience. It is not something they have done lightly. He has always given the opinion that the pension board could give a discretionary COLA but that would have to be approved by the City Commission and funded. Whether you can prefund it now and how you would do that is something he would want to study.

Chairperson Gueits calls the question.

The motion was restated.

A motion was made by Mr. Garcia-Linares and seconded by Mr. Hoff to table the issue until the final decision of the Court.

<u>Discussion:</u>

Mr. Hoff asks if Mr. Garcia-Linares is okay with amending the motion to remove the "until the final decision of the Court". He doesn't want a definitive time frame because he thinks that is what Mr. Cohen was asking was to not table the issue until the court decision. Mr. Garcia-Linares thinks they need to give Ms. Groome some direction. If they just table it then he thinks it comes back on the next agenda. He thinks that anybody can always come back on old business and raise the issue.

Mr. Hoff asks if the motion can be brought up again before the court renders a decision. Mr. Greenfield doesn't believe it could. He thinks that if there were something different involved in the matter coming before the Board subsequent to the table, the Board could consider it but if you tabled it until the decision someone can come in and ask you to reconsider the tabling of it because there is a change in circumstance. Mr. Garcia-Linares thinks it requires somebody who voted in favor of it to make a motion to reconsider. He would leave the motion as is.

Motion unananimously approved (10-0).

6. Attendance of Colleen Brennan (Northern Trust Relationship Manager), Jivko Chiderov (Northern Trust Securities Lending) and James Dominguez (Northern Trust Global Investments) reviewing the 2013 fees.

Colleen Brennan, the relationship manager at Northern Trust for the Coral Gables Retirement System, introduces Jivko Chiderov from Securities Lending and James Dominguez from their asset management side. Coral Gables has had the same fee agreement since 1997. There have been no changes to it. What is different from them as a custodian is the investment fees are included in the custody fee invoice. That might be where there are questions in regards to the increase of the fees. Also, the market value charges are only charged on the separately managed accounts and the cash accounts. The way the fee agreement is broken out is market based fees, asset based fees and transaction based fees. Chairperson Gueits asks if those are the three fees they pay. Ms. Brennan answers affirmatively. The custody fees include market value based and asset based. The custody charges and transaction fees remain pretty consistent. The market based fee has gone up due to the investment into the ACWI ex USA fund. Market value charges are only on their separately managed accounts and the cash accounts. Mr. Garcia-Linares informs that what raised the flag is when they went through their audited statements last month with the auditors is the fees more than doubled from last year to this year in the way they were presented to the Board.

Mr. Campbell asks how their fees compare to other fees of other public pension funds in Florida. Ms. Brennan answers that they have a very nice fee structure. They have four south Florida clients and they are all around 2 basis points which for custody alone are right around where this fund is. Mr. West informs that he and Troy Brown reviewed the fees of some of the custody searches and they came up with a fee schedule of 3.5 basis points for custody fees which does not include the index fund. Based on what they have been seeing, in their opinion, the fees are competitive. They aren't the cheapest on the market and if they add into that they are able to negotiate lower fees on the investment product with the index funds and view the relationship as a whole. It appears to be reasonable. Mr. Campbell asks for a staff recommendation. Ms. Groome responds that they have been using the same fee schedule since 1997 and if there is a problem in the reporting then they have to fix the reporting. Mr. Campbell asks again what is the staff's recommendation on fees and should Northern Trust remain the custodian. Ms. Groome responds that her recommendation would be to keep Northern Trust as the custodian. She thinks that if they change the fee structure it will be higher comparing 1997 to 2014.

Chairperson Gueits states that the question is if Northern Trust is cheaper than another custody manager. Ms. Gomez doesn't know if they want the cheapest. She is comfortable at this point with Northern Trust's quality of service. Ms. Brennan points out that this is the first time this issue has come up with this plan and she can look into the issue. She doesn't think the financial statements are accurate and she feels the numbers are wrong. On average the fees are $23,000 to $25,000 a quarter so she feels more comfortable with the $90,000 than the $55,000 number. Ms. Groome informs that they will have to go back and compare the reports given to the auditor last year and this year. Ms. Gomez states that she can't say with any certainty that an RFI is the best for this Board but it is always good to look at and see what others can do and then decide if they want to move forward. Chairperson Gueits seems to recall a conversation where this question has come up before regarding the fees with the custodian. He seems to recall they were also investing in some of their proprietary product and that was also one of the reasons they wanted to stay with them because they felt it was a solid product. Mr. West states that there are qualitative issues beyond just fee consideration and what is being discussed here is strictly fees. From their perspective, based on informal awareness of activity, the fee for services appears to be competitive. Then you add on the other qualitative factors to that in making any decision. He thinks the audit numbers may also be reflecting a material increase in market value as to what exactly the auditor put into those numbers. They don't know but if the proprietary investment product fees were included in that, there has been very material increase in market value which by default would make the fees go up. That is another factor.

Mr. Campbell comments that it isn't about the fees of Northern Trust. His consistent request is that he feels like they come to the meetings and he is used to having someone do the work, someone make the recommendation and someone go on the record. His request in literally every subject is that he would like to hear from staff of the recommendation and how did they arrive at it. His consistent request is if they can show up and for every agenda item have a staff recommendation. Chairperson Gueits thinks that is a fair comment. Perhaps what they can do is put together some sort of preliminary observation and recommend something and flag those items. Ms. Groome explains that this item was an informational item for what was being requested at the last meeting. There is no recommendation to give for the information Ms. Brennan has brought to the Board. Chairperson Gueits states that is a good point. Ms. Groome explains that they are not suggesting changing the custodian. It was a question that came up at the last meeting so she contacted Ms. Brennan to come to the Board and explain it. Chairperson Gueits asks if there is any follow-up that would need to be done at this point and go back to the auditor to find out what their number was based on. Maybe the index performance is the reason for the increase in fees. Maybe that follow-up is warranted at this point. Ms. Groome responds that she will do that.

Mr. Hill expands on Mr. Campbell's statement. He states that Mr. West is one of their consultants and he is considered staff as well as the actuary, GRS. So when these people are making the recommendations they can be considered as staff. Mr. Campbell understands that Mr. West is a consultant to the Board but he keeps coming back to the day to day management of all their consultants. He thinks it should be from the everyday staff. He thinks the work should be done before the Board members show up and after staff has done their due diligence of what their recommendation is so that is a starting point for their discussion instead of finding their own way through the jungle. They may come up to exactly the same conclusion. It seems to him they are taking a lot of time to get to the point. Ms. Groome informs that a recommendation is made when a decision needs to be made but in this circumstance it is really for informational purposes. If you want her to expand on the agenda for items that are for information only and no recommendation is needed then she can do that. Chairperson Gueits thinks they need a mechanism that requires some legwork ahead of time and not every item will need that. Mr. Campbell states that in the course of the year there are some major decisions they make to engage or re-engage their investment managers, their actuary, their accounting firm, their approval or review of major actuarial assumptions. He doesn't know how they can do it showing up two hours a month if the staff doesn't already do the work and doesn't come prepared with their actuarial recommendation or their advisor recommendation. He doesn't think the Board should do the day to day work running the City's pension. Ms. Groome responds that she does do the day to day work in running the pension. Mr. Campbell states that when major decisions need to be made he would like to hear from staff. Ms. Brennan informs that she and Ms. Groome can work together to find out what happened regarding the fees.

Jivko Chiderov of Northern Trust Securities Lending presents the securities lending program the plan is in with Northern Trust. The plan has been with securities lending since 2004. The total net earnings of the plan since that period were at $985,000. The fee split at the moment is at 65/35 which means that 65% of the revenue goes to Coral Gables and Northern Trust keeps the 35% acting as the lending agent in this relationship. There have been no losses due to securities lending for that period through the financial crisis. For 2013 the average loan balance was at $53 million and the average lendable base was $147 million. Any time they make a loan for one of their securities they over collateralize those loans and the collateral they take is in the form of cash. When they take that cash it is reinvested into one of their collateral pools to earn additional yield. In this case the cash is getting reinvested in the basic collateral pool.

Mr. Garcia-Linares asks how these earnings compare to other clients that have done this. Mr. West responds that he is not prepared to give an opinion. This arrangement pre-dates the Bogdahn Group and their involvement. It is strictly between the Board and Northern Trust. They don’t have any direct involvement and typically would not with this type of investment. He is not in a position to offer an opinion. Mr. Garcia-Linares asks if this is an investment they would recommend to other clients. Mr. West responds that it is an area they don’t enter into. If they do a custodial search they act as a facilitator and if there is an interest in this product line from a particular custodian they make sure it is included. A custodian that is brought forward is being hired for their demonstrated expertise list of product delivery services and then from that point on they are engaged to deal directly with the client. They would not have any involvement on this. If the Board would like to task them on it and try to do some research to come up with some sort of proxy comparison they would be happy to do that.

Mr. Garcia-Linares would like to know if they should continue this program. It seems to him that there is a lot of risk involved for the returns they are getting. Chairperson Gueits asks for an explanation as to how this works. Mr. West suggests that there are several new trustees on the Board and it has been several years that they have had a securities lending review with the Board so it would be good for an update and address the risk issues and address any changes or enhancements that have been made since the 2008/2009 crisis.

Mr. Chiderov explains the securities lending program. The client has securities and is considered the lender of the securities. Northern Trust acts in the middle as the lending agent. They take the securities and negotiate loans with the borrowers. The borrowers are institutions like Goldman Sachs, Merrill Lynch, and Barclays. They are large institutions. When they lend out a security on loan to the borrowers they collateralize that loan so they always over-collateralize at the value of 102% for U.S. loans or 105% for non-U.S. loans. When they pay that cash as collateral, Northern Trust reinvests that cash for the purposes of earning additional yield in the portfolio on the client’s behalf. When the revenue is getting generated from securities lending is when a borrower borrows a security from the portfolio. If that security happens to be a very hot security in the market, or very illiquid or in high demand the borrower pays premium basis points to be able to borrow the security from the portfolio. That is the intrinsic value of the revenue. The reinvestment value of the revenue is when the cash is being reinvested into the collateral pool and then they earn additional yield on top of the intrinsic value. This is how the transaction works. It is an investment product so there are risks involved. As they saw through the financial crisis those risks became more evident. Fortunately for this plan, there were no losses suffered due to securities lending from the financial crisis.

The first risk they face in securities lending is a borrower risk. That is the risk when they lend out securities to a borrower that the borrower may default so they may not be able to get the security back. That is why they over-collateralize every loan so if the borrower defaults they cease the collateral and they use that collateral to go into the open market and purchase the security in place and put it into the lender's account. If there is a case where that collateral is insufficient to purchase the security in the open market then Northern Trust steps in and provides the difference. This is the borrower indemnification that they offer at no interest to their clients. It mitigates borrower risk. In the case with Lehman Brothers in 2008 when they went into default, Northern Trust was able to unwind every single loan to Lehman Brothers and ceased their collateral. At the end of the day they actually returned collateral back to Lehman Brothers because they had excess amount of collateral.

Mr. Campbell asks if Northern Trust indemnifies this plan for investment loss. Mr. Chiderov responds that Northern Trust indemnifies this plan from a default of a borrower. Mr. Campbell states that if they loan out a security to Lehman Brothers and they go under and they lose their assets then Northern Trust protects the plan. Mr. Chiderov agrees. When they lend out their securities to Lehman Brothers, they have their collateral. If they lent out $100 of a security they will have $102 in the account. Chairperson Gueits states that they would execute the collateral and if there is a difference between that collateral and the purchase price in the open market for the security that difference would be covered. Mr. Chiderov agrees. Chairperson Gueits asks what the circumstances are that would give rise to a Lehman Brothers or Goldman Sachs to have to borrow securities. Mr. Chiderov explains there are a couple of different reasons why borrowers would borrow a security. They would borrow a security in order to turn around to lend it to a hedge fund, for example. Northern Trust does not directly deal with hedge funds. They may also borrow a security for settlement purposes or for a type of shorting strategy. There are several different reasons a borrower might borrow a security. Chairperson Gueits states that apart from the collateral there is a premium. Do they pay any type of a coupon? Mr. Chiderov responds that they pay a rebate rate and that rate is negotiated based upon the demand for that security. If that security demand is really high from the borrower to borrow the security then there would be a bigger premium for that specific stock.

Mr. West explains that it is basically operationally cheaper for these financial institutions to borrow to buy the bread to stock the shelves as it is to go long and the cost to carry to physically stock that bread on the shelf. Mr. Chiderov adds that sometimes it is operationally cheaper and it makes more sense. No one wants to fail on a certain transaction that creates financial wealth and also reputational risks for the borrower counter party. When you talk about emerging market transactions the cost of failing on specific trades is significant.

Chairperson Gueits asks if he can put the risks into context for them. It sounds like the business is pretty solid. He doesn't know whether the risks outweigh the potential rewards. Is the risk level contained? Mr. Chiderov responds that they would like to think so. The borrower risk is one of the risks of securities lending and the most visible one. They would like to think they are managing that risk and the risk isn't really to the borrower it is to Northern Trust because they back up that transaction.

Mr. Campbell asks how many pension funds participate in securities lending. Is this common among pension funds? Mr. West replies that it would be a function of asset size. It is a common procedure to see this in other pension systems. Because the incremental return is small it becomes a function of scale and they will not see it except in the larger pension asset pool. Chairperson Gueits asks what percentage of their assets are available at any one time to be lent out. Mr. Chiderov explains that as of 2013 they had about $147 million available for lending in the portfolio. This is only for separately managed accounts. They cannot lend from mutual funds. Out of the $147 million about $53 million was lent out on average which is an average of 36%. Some asset classes are utilized more than others. On the U.S. equity side they only lent out about 30% of the portfolio. They only utilize what is in demand.

Chairperson Gueits asks if there is a limit in the amount they allow Northern Trust to lend out. Mr. Chiderov replies that there are no caps. One of the things they addressed during the financial crisis is that they allow clients to customize their programs more so than before so clients can customize a program they are more comfortable with. If they are not comfortable with a specific borrower for any reason they can restrict that borrower from lending or they can place a cap or percentage on the loan. It is very customizable so they are comfortable with the program. Ms. Gomez asks if there is a specific time limit for the transactions. Can they get the securities back right away? Mr. Chiderov explains that is another one of the things that has changed since the financial crisis. Before they used to do term loans where they would set a term for dates in the future of that loan and now all the loans are open loans. They are renegotiated on a daily basis. At any given time they can make a decision to get out of the loan and get the security back and the same thing for a borrower. At any given time a borrower can give back the security. Ms. Groome informs that every month the summary of securities lending of the previous month is in the Administrative Manager's report. She can include a detailed report also. Chairperson Gueits asks what amount they lend out on a monthly basis. Mr. Chiderov replies that he prefers to give the average annual fee and last year they lent about 36% on average.

Mr. Greenfield doesn't understand under additional risks with taking cash as collateral. It says "cash collateral investment becomes impaired or decreases in value." How does cash decrease in value? Mr. Chiderov explains that the other risk involved to securities lending is when you take cash that is collateral for your loans and that cash is getting reinvested into the basic collateral pool. They take that cash and reinvest it. They purchase securities on the fund's behalf and create an investment vehicle that is managed a lot like a 287 type money market fund so it is very conservative and short term in nature. Chairperson Gueits states that it isn't the fact that the cash loses value it is just you are going back into the market and you may be paying more for a security than you would have. Mr. Chiderov explains that they place the cash in the vehicle in order to earn additional yield and when you place your cash in an investment vehicle there are risks associated with it depending on how much potential revenue you are going to get. Lending out a general collateral security is a majority of the loans. They have to pay the borrower the rate to be able to come into the transaction. When the actual security is in high demand the borrower is actually paying a negative rebate to Northern Trust. They are paying an additional premium note to borrow the security and Northern Trust has to pay the borrower a rate in order for them to give collateral to reinvest.

Mr. Campbell wonders if this program is worth putting $50 million of their assets in. The backstop is the Northern Trust balance sheet. If something happens to Northern Trust they could be out $50 million. He would like staff to study this more. Chairperson Gueits states that the securities that are available to be lent out are not committed. The securities they are using have a certain level of liquidity. They aren't tied up. Mr. Chiderov informs that securities lending is independent of the investment management activities. So the investment managers can buy and sell securities independent whether or not they participate in securities lending or not. It is separate from the asset management activities. When you have your portfolio active or are participating in securities lending, they place the securities into a large pool of assets at Northern Trust which have securities of 300 clients. When a borrower calls up their trading desk and says they want to borrow 100 shares of Tesla, they have an algorithm that rates clients based upon their activity, their size that tells them if client x, y and z have certain positions in Tesla. When a borrower demands that certain security, client x is the next one in line to get that loan approved. They lend out securities that are basically demanded from borrowers. If a client is not comfortable with certain limits then they can place a restriction in their portfolio saying they are only comfortable with lending out 30% of the securities or whatever percentage they are comfortable with. Half of their revenue comes from 15 securities so what they do for other clients as well is they specific their program on a time sensitive basis. They only lend out securities that are in high demand, 50 basis points or higher. They are sacrificing a little bit of their revenue so instead of only having $50 million on loan they have $10 million on loan. You limit your exposure and sacrifice a little of revenue but are participating in those trades that you get a higher premium from the borrowers.

Mr. Garcia-Linares feels more comfortable now. He still would like a recommendation as to whether or not it is worth whatever risk is out there. The percentage they return is very low versus the amount being lent. He thinks it needs to be analyzed. Mr. Chiderov informs that this is an ancillary service that is provided to the fund and a lot of plans use securities lending. They feel the risks are mitigated very well toward Northern Trust and the cash they are reinvesting in the collateral pool is managed very conservatively as a money market. They feel it is managed very well and they are willing to work with them to customize the program to address any concerns.

Mr. West comments that it is very common practice. If they look at the prospectus of the money market mutual funds, they do securities lending. Securities lending for mutual funds is common practice and for money market funds operating in a zero interest rate environment, securities lending has almost been the only source of revenue in money market funds that are achieving here. It is very common. You have to look hard and in some rare cases, like Northern Trust, you have the opportunity to select an index fund that does or does not do securities lending. If you go into the Vanguard index fund, they are already doing securities lending. It is a very common practice. Northern Trust was able to bring it to the fund and offer this service.

A motion was made by Mr. Campbell and seconded by Mr. Garcia-Linares for staff to look at securities lending and come back with a recommendation whether the fund should continue to secure the lendings and if so under what circumstances.

<u>Discussion:</u>
Ms. Gomez asks if they can limit the investment they put the cash back into. Mr. Chiderov informs that they can choose what they want to do with that cash. The basic is the most conservative collateral pools. Mr. Garcia-Linares comments that if the security you want to buy back is more than 2% then you have a loss. That is when Northern Trust backs them up. Mr. Chiderov states that scenario is highly unlikely when you have a borrower default in the market and at the same time the price equities going extremely high but in the case it happens Northern Trust backs it up. Ms. Gomez asks if that means they back up the value of what would have been of the security that is now lost. Mr. Chiderov replies that they back it up in the sense they go out to the market and purchase the security they had and whatever the price happens to be they back that up. Ms. Groome asks how many times that have happened. Mr. Chiderov responds that it hasn’t.

Motion unanimously approved (10-0).

James Dominguez of Northern Trust Global Investments informs that they are a multi-class asset manager. They primarily focus on their indexing business, their fixed income business and their multi-manager solutions business. One of the strategies they are in is ACWI ex USA. That particular strategy alone in the past three years has grown by over 110%. They are seeing more people put their money in the passive management. He goes through the organizational chart of the global investment team. They have clients in 46 countries and offices in 19 countries. As of January 31st, the fund’s assets under management with Northern Trust were at \$38.6 million. They recently added the S&P 400. The market value of the S&P 500 as of January 31st was \$7.3 million. The S&P 400 was funded in December and that fund is right in line with the index. The ACWI Ex USA fund is down a couple of basis points but the since inception return is up 31 basis points. Since inception return of outperformance of 31 basis points this is attributed to the dividend tax differential. This particular international index fund, the index calculation assumes the highest possible dividend tax withholding rate which is Luxemburg. Since you are a U.S. based investor you benefit from the most favorable U.S. tax rate so the different tax rates from the index return calculation to the performance return calculation is what causes that positive excess return. You will see that across international funds. That is outperformance you will get right off the bat.

Chairperson Gueits asks if the S&P funds and the ACWI ex USA are the proprietary products that they invest in with Northern Trust. Mr. West answers affirmatively. Mr. Dominguez states that when they price funds for relationships like this fund they are looking at total assets under management, they are looking at multiple mandates and are looking at the overall relationship. That is what allows them to give the fees that that they give. Mr. Campbell asks if all of these are in the asset listings from the consultant. Mr. West answers affirmatively.

Mr. Easley remembers that Mr. Dominguez said something about passive investing and the shift towards it. Was he talking about institutional investing or individual investing? Mr. Dominguez responds that he was talking about institutional investing. What they are seeing is more and more investors moving over to the passive management side regardless of their views on whether an asset class is more efficient than another. For example the emerging markets are commonly looked at as one of the least efficient markets. Over the past three years they have seen an increase of over 85% in that asset class alone. It is a substantial increase which speaks to increased efficiency in that particular asset class but also the difficulty institutional investors are having in finding active managers that can consistently outperform the benchmark in that particular asset class. They are seeing across the board a 27% increase from a year ago in their passive management side. Passive management is a growing business. Mr. West informs that the two recent additions to this fund are the S&P 400 index fund and the ACWI ex USA fund. Chairperson Gueits asks if they are comfortable with these funds. Mr. West responds affirmatively.

7. Investment Issues.

Mr. West reviews the performance in February. The total fund of the month net of manager fees was up 3.32%. On a fiscal year to date they are at 7.09%. For the period ended February for the year they are at 15.75%. All the managers outperformed. The total equity was up 5.37% versus the benchmark at 4.85%. The combined fixed income with global bonds adding materially this month was up 1.19%. The real estate products continue to return steady returns at .42% for the month. The remaining alternative asset was up .67%. As an administrative update those assets should be transitioning out at the end of this month and the other transition item was moving Barings to WCM. A little more legwork than usual happened in getting out of that commingled fund but it is done and they are fully transitioned. MD Sass had a huge market and fiscal year to date they are at 19.85%. They have had very cyclical exposure. Eagle Capital has been able to hang about even of the benchmark. The Templeton Global Bond and the PIMCO diversified income fund both up under 2% and on a fiscal year to date basis they were 3.93% and 1.89% respectfully. With the recent allocation changes, they have increased the equity allocation target by 5% and decreased the alternatives by 5%. That will get implemented at the end of the month to get them at that higher allocation. The total bond investment grade exposure is at 15%. One negative with Thornburg is that they continue to struggle this month and fiscal year to date is at 1.28% versus the benchmark at 5.12%.

They will be in a position to give a better update on that manager at the end of the quarter. They will continue to keep a watch on them and if they have to make a change they will let the Board know as soon as any decision can be made on that by their research group. They opened the month at $336,819,342 and closed the month with $345,090,141 with an appreciation of $10,629,169.

8. Old Business.

Mr. Hill comments that Mr. Campbell keeps bringing up that he feels like he is uncomfortable making decisions without staff recommendation. He is on the Investment Committee whereas he feels that on the Investment Committee he is the staff and he is going to be making recommendations. Every year they are going out for RFP which is one of the things they voted on previously. He thinks this year it will be an RFP for the attorney. If Mr. Campbell is that uncomfortable then maybe he would like to be replaced. He was voted on the Committee when he wasn't at the meeting. Mr. Campbell responds that he is comfortable being on the Investment Committee as he is on the Board. Everyone is entitled to their own opinion. He came to one meeting and his take is that it is okay for the Retirement Board to set philosophy and strategy and review and set policy but he doesn't think it is a substantive for a 40 hour work week every week on behalf of the pension. He appreciates everything Ms. Groome does but Ms. Gomez is more senior from a finance standpoint. His observation is that they are doing all the work and he is afraid of doing poor quality work. He hasn't been on a Board that tried to do so much of the work. He didn't think they were the workers of the pension activity. He would just like a staff analysis. Often it is going to take a lot more work than it does with just two hours a month. It seems like there is one person who is swamped with a lot of work. He has a lot of appreciation for what she has to do but that's the only person working on this that he can tell. He thinks there is a difference in coming to these meetings versus thinking he is in charge of pension activity. That is just his observation.

Chairperson Gueits suggests that they can start moving into a direction whereby they can identify items that perhaps require staff research, input and a recommendation going forward. Mr. Garcia-Linares thinks the issue is that he doesn't think they ever put closure on whether or not they can bring in someone that can assist Ms. Gomez and Ms. Groome so that the routine items can be off their plate and they can focus on some of these other issues that Mr. Campbell has raised. He thinks they need to bring closure to that. Ms. Jaramillo-Velez states that the Board Attorney was going to do an analysis of what the City Code said in relation to all the responsibilities of staff. Mr. Greenfield informs that he and Ms. Groome have a meeting scheduled for next Wednesday.

Ms. Gomez wants to be clear that when they look at the Trustee in the Code it is very specific as to what the Trustee does. She is the Finance Director for the City. That is separate. In terms of being the Trustee the duties of the Trustee are very specific in the ordinance. The Code basically said that the duty of the Trustee is to pay the bills. She knows that over the years the former Finance Director/Trustee was very involved in certain respects with the Board. She thinks there is a misconception of what the Trustee's role is. The Finance Director is for the City and the Trustee doesn't make recommendations according to the ordinance. Mr. Garcia-Linares understands but the decisions the Board makes effect the City so now Ms. Gomez is the Finance Director sitting in for the City as a Board member providing what the recommendation of the City is. Ms. Gomez thinks that is different from a recommendation of how the Board should proceed on something. She wants to make it clear because they want staff to make recommendations but she doesn't know if that is her role as Trustee.

Chairperson Gueits states that when a recommendation is made, he thinks they understand that the mouth piece is Ms. Groome. She is the Administrator. To the extent she requires input to formulate the recommendation she would go to the attorney, the consultant, the Trustee and generate a report. He has seen this at the County. He has gone in front of Boards and they always have staff with a report and the staff reads the report into the record, they make the recommendation and the Board votes. From a purely mechanical perspective he thinks to do this, Ms. Groome would be the point person and decide what the items that are coming that may require homework and a recommendation and then go to the respective consultants and take their input and create a recommendation. He thinks that, in taking Mr. Garcia-Linares's point, in order for Ms. Groome to do that well she needs to take off some of the administrative things off her plate so she can focus on the substantive issues in deciding what issues require a recommendation from the administrator. Mr. Garcia-Linares points out that Mr. Greenfield will come back to the Board with his report and make a recommendation as to whether or not Ms. Groome needs additional staff. Chairperson Gueits asks who would pay the salary. Ms. Groome responds that the Board pays the salary. Chairperson Gueits asks if they generate their own moneys to pay their own people. Ms. Groome answers affirmatively. Mr. Garcia-Linares states that they have the authority to hire their own people. Ms. Jaramillo-Velez informs that they can hire a company that would provide the same thing and they may want to look at that. Mr. Garcia-Linares doesn't want to hire a company that has different people that have no accountability to the Board if something goes wrong. Ms. Jaramillo-Velez explains that the City does hire employees all throughout the City from a company. Chairperson Gueits asks if they can make them accountable. Ms. Jaramillo-Velez answers affirmatively. Mr. Hoff states that they failed at that and he has police case numbers where that has occurred. Employees from outside of the City stole identities of city employees.

Mr. Campbell comments that the reason he keeps trying to suck Ms. Gomez into a bigger and more accountable role is because she is the senior finance person for the City and on the City's payroll. She is the most senior finance person in the City. He goes back to every so often they evaluate their investment managers, they evaluate their actuary, and they make decisions about actuarial assumptions they are going to be comfortable with. His view is Ms. Gomez has the skill set that may not work with other duties or may not work with independence and if it doesn't work then he thinks for a half a billion dollars in liability they need some kind of director of finance even if it is part time. He thinks they are under staffed.

Chairperson Gueits states that Mr. Greenfield will come back with a report and let them know how much they can pay someone. Their ability to pay someone is probably going to delegate the level of person they are going to get. Mr. Garcia-Linares thinks it works the other way. They need to find out if they can hire someone and then Ms. Groome needs to tell them what kind of person she needs and then they figure out what it costs. Mr. Hill agrees. Ms. Groome adds that 60% of the administration of the retirement system is not all finance.

Mr. Easley knows they were heavily concerned about the 415 and dealing with the actuaries and the hiring and firing but they did say that once they got through that they would start looking at doing RFPs for the other providers. He doesn't think it would do any harm to do their due diligence of periodically looking at their consultants, the attorney or whoever else. He is not saying do it right now but in the near future. Mr. Hill thought there was a vote at a previous meeting that every year they would do an RFP for their providers and that this year would be for the attorney. Mr. Garcia-Linares doesn't think they need to do an RFP. He thinks what they need a recommendation as to whether or not their attorney's fees are reasonable to his services compared to other funds and whether or not the consultant's fees are reasonable compared to other funds. He doesn't think they have to do a formal RFP that costs a lot of time and money if they don't need to make a change. Ms. Gomez believes that Mr. Hill is correct. At a previous meeting the Board had said that they should have a three year rotation of RFPs and pick a service every year to do an RFP. Mr. Hoff remembers because he brought it up. The 175 and 185 require every three years a review of their providers so it was suggested that based upon the issues at hand they picked the actuary as the first RFP and he thinks this year they were going to do an RFP for the attorney and then next year would be the RFP for the financial consultant. The reason he suggested three years is because Mr. Greenfield said they didn't have to do what 175 and 185 do but he thinks it is a due diligence issue.

Mr. Campbell is comfortable with that. He thinks that like when the Investment Committee did their due diligence on the actuary everyone once within about $2000 of each other and all the actuarial issues they had to do with it wasn't about price but who could do it the best. He thinks it all comes down to quality and performance. He would hate to get the cheapest provider without looking at contribution and performance.

Chairperson Gueits thinks this issue came up before specifically with the attorney and they voted to keep him. Now if some ordinance requires them to go through the process that is a different story. Mr. Garcia-Linares comments that if they decide to change a provider they have to go through an RFP but there is no requirement to make a change if they are comfortable with their attorney, their financial advisor, Northern Trust, etc.

9. New Business.
There was no new business.

10. Public Comment.
There was no public comment.

11. Adjournment.

The next scheduled Retirement Board meeting is set for Thursday, April 10, 2014 at 8:00 a.m. in the Youth Center Auditorium.

Meeting adjourned at 10:17 a.m.

APPROVED

JAMES GUEITS
CHAIRPERSON

ATTEST:

KIMBERLY V. GROOME
RETIREMENT SYSTEM ADMINISTRATOR