

**CITY OF KALAMAZOO EMPLOYEES' RETIREMENT SYSTEM
INVESTMENT COMMITTEE MINUTES
THURSDAY, August 28, 2014**

A meeting of the City of Kalamazoo Retirement Investment Committee was held on Thursday, August 28, 2014 in Room 207-A of the Kalamazoo County Administration Building. Chairman Salisbury called the meeting to order at 4:00 p.m.

Members Present: Chair Robert Salisbury, Vice-Chair Randy Eberts, Dean Bergy and Dan DeMent.

Guests: Sandi Doctor, prospective candidate for the RIC Committee. Another prospective member is Joel Wittenberg from the Kellogg Foundation, unable to be present today.

Others present: Chris Ruppel, Consultant; Barb Miller, City Commissioner; Clyde Robinson, City Attorney; Tom Skrobola, Chief Financial Officer; and Patricia Vargas, recording secretary.

Absent: Jan Van Der Kley.

Randy Eberts motioned and Dean Bergy supported excusing Member Jan Van Der Kley. The motion passed by voice vote.

2014 2nd Quarter Meeting Minutes

Dan DeMent motioned and Randy Eberts supported approval of the May 28, 2014 meeting minutes. The motion passed by voice vote.

Trip Reports

Comment: Chris Ruppel noted the defined contribution plan conferences. The Vanguard due diligence will be rescheduled for later in the year.

Tom confirmed that the City offers a 457, deferred compensation plan, consisting of two carriers: Nationwide and ICMA.

Investment Portfolio

Assets

Tom Skrobola noted for Sandi Doctor's benefit, that the Pension assets are accounted separately from OPEB assets under the Group Trust at our custodian, State Street.

Bob Salisbury commented that the joint trust was set up at State Street within the past year.

Investment Performance Review

Mr. Ruppel presented. The market value of portfolio assets increased from \$624.4 million to \$641.8 million during the second quarter of 2014, an increase of \$17.4 million or 2.8%.

The weighted average return for the quarter net of manager fees was 3.9%. The 1-year return was 19.6%. The return since October 1982, net of manager fees, through the end of the quarter has been 11.6%.

Equities comprised 70.5% of the City portfolio at the end of the quarter. The equity portion of the City portfolio returned 4.5% for the quarter and 25.5% year-on-year.

Fixed income comprised 24.5% of the City portfolio at the end of the quarter. Total fixed income returned 2.1% for the quarter and 4.3% year-on-year.

At the end of the quarter real estate investments were 5.0% of the portfolio. Real estate returned 4.7% for the quarter and 13.9% for the year.

The portfolio assets finished the quarter with 70.5% in equities, 24.5% in fixed income, 5.0% in real estate, and 0.1% in cash. The portfolio target allocation is 70% equities, 25% fixed income, and 5% real estate.

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The inflation-adjusted or real return, for the quarter was 3.0% as the inflation rate for the quarter was 0.9%. With a year-on-year inflation rate of 1.8% the one year real return was 17.5%. Since October 1982 the return on the portfolio, net of manager fees, has been 11.6% nominal and 8.7% real.

Comment: Bob Salisbury commented on the committee's success however noted that the committee has had its share of rough times, will have rough times in the future and will keep moving forward.

Account Update

2014 2nd Quarter Cash Flow Report

Tom Skrobola presented, summarizing second quarter movement, including benefit payments, management fees and receipt information. Overall fees and expenses are what we have anticipated.

2014 2nd Quarter Expense Report

Tom Skrobola did not see anything unusual or questionable in the expense report.

Dean Bergy questioned receipts and disbursements/unrealized gains and losses, suggesting that those be pulled out to a beginning balance. Tom will update the data, which will result in a report that makes more sense.

Bob Salisbury requested that the committee provide approval for the total miscellaneous expenses only.

Randy Eberts motioned and Dan Dement supported to accept the 2014 2nd Quarter total miscellaneous expenses by roll vote.

Bob Salisbury, Randy Eberts, Dean Bergy, Dan DeMent, in favor. MOTION PASSED.

2014 2nd Quarter Liquidations

Tom Skrobola provided a summary of the 2nd Quarter Liquidations. Chris Ruppel specified that the June report shows that REEF is overweight and he will be taking out of that.

Chris also noted that funds were taken from Vanguard REIT.

Audit

A&G summarizes the report in the cover letter as well as offers an audit opinion (Page I of the document). Tom Skrobola provided the initial review with RIC review by Jan Van Der Kley.

Bob Salisbury: Let the minutes reflect thanks to Jan Van Der Kley's continuing work in helping us with this.

Due Diligence

Chris Ruppel provided information on upcoming due diligence meetings.

Communications

Derivatives Report

Mr. Ruppel indicated that Jennison is using the derivatives as it is supposed to and BlackRock uses them for cash and cash only.

Articles of Interest

The 2nd Quarter articles of interest were acknowledged.

PCIC Report

Chris Ruppel highlighted the City of Kalamazoo Perpetual Care Fund report items.

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Chris Ruppel proposed the elimination of PIMCO, due to specific concerns with PIMCO Total Return Funds (fund specific and the amount of derivatives used) and replacing it with two Vanguard fund accounts. RIC members committed to studying the proposal and all its implications prior to taking action.

New Business

Bob mentioned for Tom and Clyde, Jennison has asked each of the sponsors to sign what they refer to a forward transaction, a very complicated government regulation of derivatives. Dan DeMent has been working with them to help understand where they are. Once at the appropriate point, RIC members will ask the City to sign off on.

Bob wanted to discuss the OPEB funding situation, that there is a potential bonding of up to \$100 million to pre-fund the OPEB.

Tom Skrobola provided an update. The OPEB/Legacy Task Force was commissioned by the City Manager and included representatives from the CMO, City Commissioners, residents and City staff. The Task Force recommended:

1. The City must explore ways to reduce OPEB costs
2. The City should issue OPEB bonds for up to \$100 million by the end of 2014

The City Commission took action to authorize the City to move forward with an application to the State Treasury Department on August 18th, 2014. If bonds are issued, the funds are invested alongside the Pension Funds under the existing Group Trust. The use of operating funds would be capped to provide fixed bond payments and fixed contributions to the OPEB Trust Fund. The OPEB Trust Fund would be sustained for the term of the OPEB Bonds (2044) by the bond proceeds, interest income and fixed contributions, and if necessary, reductions to retiree health care benefits.

It is understood that the City Commission will require that written agreements be reached with the bargaining units to institute the operating fund caps and also the requirement to lower retiree health care benefits if necessary to sustain the OPEB Trust Fund. If investment income doesn't materialize as expected, then we will work with our bargaining units to make gradual adjustments to benefits and costs for non-legacy retirees (who retired since 1/1/2007) and future retirees. This will result in a risk sharing scenario with our bargaining units. This way, OPEB Bonds will help to preserve jobs and services for the City and build a frame work to make it sustainable and affordable.

Bob Salisbury: If City decides to go ahead and do the bond issue, should all bond monies be invested right away? Mr. Skrobola indicated that dollar cost averaging is being considered as a way to mitigate potential investment loss.

Bob Salisbury noted a good summary, providing context to what has been read in the paper/media and encouraged Tom to continue work and keep the committee apprised of project status.

Bob Salisbury, Dean Bergy and Clyde Robinson confirmed the State law's 20% limit on the Pension System's investments in foreign holdings. Dean noted the legal status is pending conclusion of work and Bob requested the discussion be put on next quarter's meeting agenda.

Future Meetings (all room 207-A Kalamazoo County Administration Building)

Monday, November 24, 2014 @ 4:00 p.m.
Wednesday, February 25, 2015 @ 8:45 a.m.
Wednesday, May 27, 2015 @ 9:30 a.m.
Wednesday, August 26, 2015 @ 8:45 a.m.
Monday, November 23, 2015 @ 4:00 p.m.

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Around the Table

Adjourn

There being no further business, Chair Salsbury adjourned the meeting at 5:05 p.m.

A handwritten signature in black ink, appearing to read "Thomas Skrobola". The signature is written in a cursive style with a large, prominent initial "T".

Thomas C. Skrobola,
Secretary