

**MINUTES OF MARCH 13, 2014 RETIREMENT BOARD
CITY OF ALEXANDRIA
FIREFIGHTERS AND POLICE OFFICERS PENSION PLAN
DUE DILIGENCE MEETING**

PRESENT

| <u>Members</u> | <u>Others</u> |
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| Elizabeth Davies (Management, Alternate) | Steven Bland, Retirement Administrator |
| Patrick Evans ¹ (Fire) | Bryan Capelli, Retirement Specialist |
| Tom Gates, ³ Chairman, (Management) | Kadira Coley, Retirement Specialist |
| Jean Kelleher ² (Management) | Stephen McElhaney, FSA, Cheiron |
| Shirl Mammarella ³ (Police, Alternate) | Kathy, McGugan, ASA, Cheiron |
| Ed Milner ¹ (Police) | Elizabeth Wiley, FSA, Cheiron |
| Rick Muse ³ (Fire, Alternate) | |
| Al Tierney ² (Police) | |
| Laura Triggs ³ (Management) | |

Absent:

Michael Cross,² Secretary, (Fire)

Nelsie Smith (Management)

Terms: 1/1/2014 – 12/31/2015

¹Purchase of Service Credit Committee

²Technical Corrections and Plan Document Review Committee

³Vendor & Service Provider

CALL TO ORDER

Mr. Gates called the meeting to order at 8:43 AM on March 13, 2014. There was no quorum.

Mr. Evans arrived at 8:48 AM. The meeting attained a quorum.

MEETING RECORD

Mr. Tierney made a motion to

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| Approve the January 9, 2014 minutes. |
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Ms. Triggs seconded the motion. The motion was unanimously approved (8 – 0).

Ms. Davies was introduced. Mr. Routt is leaving the board. Ms. Kelleher will move from Alternate Trustee to Trustee, and Ms. Davies will become an Alternate Trustee.

FINANCIAL REVIEW

Financial & Economic Review

Mr. Bryant provided a brief economic and market summary to set the stage for performance review.

Investment Review

The portfolio has more equity weighting than the average in the peer universe. Equities did well for the quarter and the year, so the portfolio outperformed. Domestic equities outperformed international equities. That too led to portfolio outperformance. Developed international market equities outperformed emerging market equities. The portfolio overweights emerging market equities, so this led to portfolio outperformance. Large cap outperformed mid and small cap in the quarter. The portfolio overweights mid and small cap, and this held the portfolio back slightly.

Real estate and timber outperformed fixed income. The portfolio holds more of these than its peer universe average, helping the portfolio performance.

Inflation hedges such as TIPS underperformed, and the portfolio has little exposure to these.

Handout 2 (b) (iii) Exhibits 1 & 2 are returns for the savings plans: deferred compensation (457) and the Fire & Police defined contribution plan (401 (a)) as well as the Roth. Best practice for quarterly reports is to only include information on accounts that are invested for the full quarter. The transitions at ICMARC took place in mid – October, so the first full quarter will be January through March. This will be brought to the board at the May meeting.

Mr. Bryant discussed risk measures. These will have meaning after data is accumulated over a period of time. The current history is too short to be credible.

MANAGER REVIEW ATTRIBUTION ANALYSIS

Staff discussed some approaches to manager review and attribution analysis. Most of the discussion followed the handouts. Some questions are rather universal. Others are manager specific. The manager specific issues are deferred until May when Herndon is present. Handout 3 exhibits 3 and 4 address the impact of style (value vs. growth) and capitalization (size). Exhibit 5 is an example of attribution analysis.

GLOBAL TACTICAL ASSET ALLOCATION

Staff provided a context for the presentation. Global Tactical Asset Allocation (GTAA) could provide some risk management assistance. However, not much had ever been said of how tactical asset allocation managers do their work. Staff dignified the GTAA effort by saying that the portfolio management process can be quite quantitative and need not be driven by “hunches.” A chart (handout 4 (a) exhibit 1) was displayed with a remarkable correlation between the price of the S&P500 and the

level of stock buybacks. Stock buybacks was but an example. Another handout (handout 4 (a) exhibit 2) listed a large number of data points a firm might use to quantify asset allocation weighting decisions.

Mr. Muse arrived at 9:00 AM.

Mr. Bryant would like to speak at a future meeting on:

- How well the plan has performed compared to AMRSVA peers
- Risk Management, and
- Dahab associates new asset allocation model

Handout 4 (b) is to support an asset allocation study. When an asset allocation study is performed, providing a range will narrow down the possibilities to a manageable size, making work easier and more focused for both the board and Dahab Associates.

ACTUARIAL PRESENTATION

Experience Study

Mr. McElhaney introduced his coworkers and then went through the experience study.

Pages 3 - 4: Investment experience was dominated by the 2008-2009 financial crisis and the smoothing of those losses. 2013 showed the first gain in years. The basic plan largely had liability experience gains. The disability component had liability component losses.

Pages 6 – 15: Economic experience is rather consistent across the country. The inflation assumption is 3.0% and no change is recommended. Real wage growth has assumed to increase .75% annually. Cheiron recommends it is set to .50%. This would have two offsetting actions: 1) Salaries are assumed to grow more slowly, *decreasing* contribution rates, and 2) amortizing the unfunded liability over a smaller salary base, *increasing* contribution rates. The net impact will be very small.

Pages 15 – 17: The salary increases net of wage growth (merit, promotion, etc.) should be held steady for 1-5, 6 – 10, and over 16 years of service. For the 11 – 15 years of service employees the assumed rates should be modestly decreased.

Pages 18 – 22: The investment return assumption of 7 ½% was discussed. It is in line with our public plan peers in Virginia as well as statewide systems. The actuary feels it is in compliance with Actuarial standard of practice #27.

Pages 25 – 26: Termination rates are recommended to change from age based to service based.

Pages 27 – 29: The actuary recommends three changes: 1) assumptions should increase the total number of expected disabilities, 2) the pitch of the rates have a hump at 35 years old as opposed to a steadily increasing curve currently used, and 3) the assumed mix of Partial Service Connected disability increase.

The recommended changes would have different impacts on the disability & pension components. However, in aggregate, increasing disability utilization rates will increase contribution rates.

Pages 30 -31: The actuary recommends an increase in the retirement rate through age 55. This will increase contribution rates.

Page 32 – 35: Changes to the mortality assumptions for the pension component were made in the 2011 valuation. There is no recommendation to revise them at this time.

In this plan disability typically impairs the ability to work or the quality of life, but not length of life (effecting morbidity, not mortality). The actuary recommends revision to the disability tables.

Pages 37 – 41: The cost method is the most common method used, encouraged by GASB and GFOA, and should be retained. The asset smoothing meets standards of practice.

The actuary points out that the amortization period (a closed sixteen years to the year 2029) merits review. First, as the period shortens, future changes in the UAAL will lead to significant swings in funding – which is undesirable. Second, a layered approach to future gains and losses is suggested as best practice.

Staff said the amortization period is described with precision by the plan document. Under the current structure there is no option to adopt the actuary’s recommendation. This could be referred to the Technical Corrections and Plan Document Review Committee.

Staff said that Appendix A in the plan document held several assumptions that should be updated to reflect the actuary’s experience study.

Ms. Mammarella made a motion to

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| Adopt the revisions to Appendix A in the board packet that reflect the Actuary’s recommendations. |
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Mr. Tierney seconded the motion.

Discussion:

The Actuaries said they had reviewed the handout in advance and it was consistent with their recommendations.

The motion was unanimously approved (8 – 0).

Annual Valuation

Ms. McGugan presented the 2013 actuarial valuation.

Pages 1 – 2: Introductory remarks and context were presented.

Page 3: Changes were disclosed: plan provisions, assumptions & methods, and experience.

Page 4: Investment experience was favorable.

Pages 5 - 6: The funding ratio is 71% and 40% in the pension and disability components respectively.

Pages 7 – 8: Employer contributions in the pension component will hover above 30% for the next several years. Employer contributions in the disability component will climb from below 6% to above 12% in the next several years.

Pages 9 - 10: The level of active participants has remained relatively stable since 2006. Retiree counts have increases continuously since 2004.

Pages 11 – 12: Results compare: a) 2012 historical valuation results, b) 2012 valuation results with the experience study changes, c) 2013 baseline results, and d) 2013 valuation results with the new assumptions. Recommended total contribution rates are increasing, with pension and disability costs going in opposite directions.

Pages 13 - 14: For the pension component investment and liability gains lower contribution rates while changes to the amortization result in an increase. In the disability component the assumed increase in utilization result in significant contribution increases. The changes in contribution rates are expected to change the pattern of cash flows. The cash flow positive pension component will become cash flow negative soon, but the disability component will be cash flow positive through FY 2019.

Pages 15 – 16: Cheiron’s P-Scan offers several projections.

ADMINISTRATOR’S REPORTS

Regular Investment Reports

No rebalancing was required. January’s and February’s strong markets were nearly offsetting.

Returns for three NCREIF benchmarks were distributed: timber, farmland, and real estate.

Other Items

Education: conferences, seminars and training

Two websites with valuable information are listed. One site has best practices for boards on alternative investments, such as how to do an RFP or performance manager review. The other website hosts a significant number of two to five minute videos on definitions and explanations of alternative investment terms.

CAFR

Ms. Triggs provided an overview of the pension footnote to the City's annual report (CAFR).

Determination letter from IRS

The application and documentation for a determination letter had been submitted prior to the deadline. The wait for results was unpredictable, but typically rather long.

CAPPP Class

Staff requested prices from the IFEBP for bringing a CAPPP class to Northern Virginia.

Farmland

The Plan has no farmland. The board previously made a commitment to a farmland limited partnership. That partnership collapsed prior to the final close. Staff mentioned that Macquarie was a finalist. The board generally liked Macquarie but there was some concern over the exposure to Brazilian properties. Since Macquarie's first presentation more properties have been purchased and the weighting to Australia will be larger and to Brazil smaller than originally anticipated. This might make the Macquarie partnership more attractive than before. Mr. Bryant will work with staff and put this on the May agenda.

Federal Reserve Board

At a prior meeting Mr. Eger requested information on the Federal Reserve Board ("the Fed") in general and quantitative easing (QE3) in particular. A Nobel Prize winner in economics from George Mason University produced a video on the Federal Reserve Board's duties. It provides background. Future meetings will pursue other aspects of the Fed and QE3. In the interest of time the video was not shown during the board meeting. A link is provided and trustees are encouraged to watch the video.

Mr. Milner arrived at 10:43 AM.

Real Estate – cash vs. reinvest

Mr. Bryant suggested staff make the decision to take PRISA distributions in cash or reinvest in the fund. The monthly reinvestment report reports weighting so a means is available for trustees to monitor the actual vs. target real estate allocations.

P/E Ratio

At a prior meeting a question was raised as to the average price to earnings ratio. Handout 6(b)(iv)(4) showed the P/E ratio for 120 years. Currently the P/E ratio is on the high side, but not at historic extremes.

Portfolio Construction & Volatility

At a prior meeting a trustee asked how adding a volatile asset to a portfolio could lower volatility. Staff indicated it could if the correlations of the volatile asset to other parts of the portfolio were low enough. This counter-intuitive thought was demonstrated by graphs and tables.

Vendor Start Dates

Previously a handout of vendor start dates was distributed. Additional information was requested and the information redistributed.

Financial & Investment Planning: Individual vs. Institutional

At a prior meeting a trustee asked about ways to analyze the plan's investments. Staff distributed a high level compare & contrast sheet of factors and considerations in managing individual versus institutional assets.

Rebalancing History

A history of recent rebalancing was distributed.

PIMCO Management Changes

Mohamed El-Erian recently left PIMCO. He was the Co-CEO and generally considered one of the greatest investment minds of the last several decades. There are two reasons to bring up this topic: 1) it is best practice to inform investors (the board) of significant changes with an investment manager, and 2) for the board to consider whether or not it is appropriate to reconsider commitments to PIMCO.

It remains to be seen if the departure merits the board's consideration of reassigning plan assets. Mr. Bryant and staff will bring this topic back to the board at the May meeting.

Cash Payouts - PLOP

A police officer recently retired and elected the PLOP provision.

Cash Payouts - COLA

The CPI rose 1.58% from month end January 2013 through month end January 2014. Eligible members will receive a COLA of 1.58% in their May benefit payment.

OLD BUSINESS

ICMA-RC Update

When the ICMARC platform was being updated there was a request for a follow up report. Handout 7 (a) was presented as a table of contents or outline of such a report. Board members were asked to send comments on the proposed outline to the Pension Administration Division.

Strategic Discussion – Equity Exposure

Mr. Bryant would like to take a strategic view of Asset Allocation over two meetings. He proposes to discuss:

- 1) The asset allocation and performance public pension plans in Virginia,
- 2) Risk with an emphasis on historical records,
- 3) Dahab's new asset allocation model, and
- 4) New strategies.

Mr. Bryant mentioned three books:

1. Pioneering Portfolio Management, by David Swenson
2. Unconventional Success, David Swenson
3. Against the Gods, Peter Bernstein.

Staff had read these books and also endorsed them.

A handout from a prior meeting indicated four high level ideas for an overriding investment strategy. Staff was asked to expand the list. The list was extended and included in the packet.

Schedule of topics for 2014

Following the canceled February board meeting the schedule of visits from portfolio managers was modified. The calendar was updated and redistributed.

Adjustment Mechanism Update

Ms. Triggs provided a brief update on the Adjustment Mechanism Committee.

COMMITTEE REPORTS

Technical Corrections and Plan Document Review Committee

There was a motion by Ms. Triggs to:

The Board accepts the recommendation from the Committee documented on handout 8(a)(i).

Mr. Evans seconded the motion. The motion was unanimously approved (8 – 0).

Purchase of Service Credit Committee

There was a motion by Mr. Milner to:

The Board accepts the recommendation from the Committee documented on handout 8(b)(i).

Mr. Evans seconded the motion. The motion was unanimously approved (8 – 0).

Vendor & Service Provider Review Committee

No report was given.

NEW BUSINESS

Elections

The discussion on elections was pushed to the April meeting.

Floor Motion

There was a motion by Mr. Tierney to:

Approve and have Mr. Gates sign the letters of accommodation as presented to

the Board.

Ms. Mammarella seconded the motion. The motion was unanimously approved (8 – 0).

NEXT MEETINGS

1. Thur. April 10th 8:30AM, Sister Cities Room 1101, Interim Meeting
2. Fri. May 9th 8:30AM, Sister Cities Room 1101, Joint Due Diligence Meeting
3. Thur. June 12th 8:30AM, Sister Cities Room 1101, Joint Board Retreat

ADJOURNMENT

The meeting adjourned at 12:43 PM.

HANDOUTS

Distributed to Board members in the Board Packet:

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| Agenda |
| Minutes of Prior Meeting [1(a)] |
| Investment Performance Review [2(b)(i)] |
| Defined Contribution & Deferred Compensation Fund Returns [2(b)(iii)] |
| Manager Attributes [3 – Exhibit 1] |
| Manager Review - Factor Models [3 – Exhibit 2] |
| Manager Review – Market Performance & Market Cap [3 – Exhibit 3] |
| Manager Review – Market Performance & Style [3 – Exhibit 4] |
| Manager Review – Attrition Analysis [3 – Exhibit 5] |
| Tactical Asset Allocation [4(a) – Exhibit 1] |
| Tactical Asset Allocation – Methods & Indicators [4(a) – Exhibit 2] |
| Asset Allocation [4(b)] |
| Experience Studies Illustration [5(a) – Exhibit 1] |
| Experience Study Comments [5(a) – Exhibit 2] |
| Experience Study – Recommended Changes/Appendix A [5(a) – Exhibit 3] |
| Monthly Investment & Rebalancing Report [6(a)(i)] |
| Private Equity Cash Flow Report [6(a)(iii)] |
| NCREIF Returns - Timberland [6(a)(vi) – Exhibit 1] |
| NCREIF Returns - Farmland [6(a)(vi) – Exhibit 2] |
| NCREIF Returns - ODCE [6(a)(vi) – Exhibit 3] |
| CAFR Excerpts [6(b)(ii)] |

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| Administrator's Follow-Up Items List [6(b)(iv)] |
| Follow-up Item – Price to Earnings Ratio [6(b)(iv)(5)] |
| Follow-up Item – Portfolio Construction & Volatility [6(b)(iv)(6)] |
| Follow-up Item – Vendor Start Dates [6(b)(iv)(7)] |
| Follow-up Item – Financial & Investment Planning: Individual vs. Institutional [6(v)(iv)(8)] |
| Follow-up Item – Rebalancing History [6(b)(iv)(9)] |
| 2014 COLA [6(b)(vi)(2)] |
| Action Items & Recommended Motions [6(c)] |
| ICMA-RC Potential Transition Report [7(a)] |
| Strategic Discussion - Equity Exposure [7(b)] |
| Planning Meeting for 2014 [7(c)] |
| Technical Corrections and Plan Document Review Committee Report [8(a)] |
| Purchase of Service Credit Committee Report [8(b)(i)] |
| Elections Procedures Checklist [9(a)] |

Distributed at the meeting:

1. Actuarial Valuation Results Presentation as of July 1, 2013 (Cheiron)
2. Study of Plan Experience July 1, 2009 through June 30, 2013(Cheiron)
3. Dahab's Performance Review December 2013