

**EMPLOYEES' RETIREMENT SYSTEM OF THE CITY OF MILWAUKEE
ANNUITY AND PENSION BOARD**

Minutes of the Regular Meeting held October 23, 2017

The meeting was called to order at 9:04 a.m.

Board Members Present: John Barmore, Chair
 Thomas Bell
 Tom Klusman
 Rudolph Konrad
 Martin Matson
 Mark Nicolini
 Himanshu Parikh
 Gust Petropoulos

Board Members Not Present: Deborah Ford (arrived 9:12 a.m.)
 Nik Kovac (excused)
 Larry Holland (excused)

Retirement System Staff Present: Bernard J. Allen, Executive Director
 Melody Johnson, Deputy Director/Chief Financial Officer
 David Silber, Chief Investment Officer
 Erich Sauer, Pension Investment Analyst
 Thomas Courtright, Pension Investment Analyst
 Mary Turk, Business Operations Analyst
 Liisa Gary, Administrative Assistant II
 Jan Wills, Board Stenographer

Others Present: Troy Jaros, Conduent HR Consulting Services, LLC; Debbie Sweeney, Dan Kwiecinski, Hays Companies, Inc.; Mike Joecken, Callan Associates; Jason Ellement (via teleconference), Callan Associates; Miriam Horwitz, Ellen Tangen, Andrea Fowler, City Attorney's Office; Molly King, Budget Office; Amanda Cervantes, Ald. Kovac's office; Terry Siddiqui, Partner, DS Consulting Group, LLC; Jean Burnside, Larry Woytek, Milwaukee Retirees' Association.

Approval of Minutes. Mr. Barmore presented the minutes of the Regular Meeting held September 25, 2017. It was moved by Mr. Petropoulos, seconded by Mr. Klusman, and unanimously carried, to approve the Minutes of the Regular Meeting held September 25, 2017.

(Ms. Ford arrived at 9:12 a.m.)

Chief Investment Officer Report. As a matter of information, Board members received the performance report. Mr. Sauer presented the performance report and said the Fund value as of September 30, 2017 was \$5.25 billion dollars. The Fund return of 1.6%, net of fees, outperformed the blended benchmark by approximately 0.2% in September. The Fund outperformed the benchmark in all time periods, net of fees, except for the 10-year period. The

main driver of September returns, Mr. Sauer stated, was the Fund's Style Bias. Exposure to US Small Cap Equity added 26 basis points to returns. He said the U.S. Value Equity style bias detracted 16 basis points. As of October 20, 2017, the Fund return is up 1.1%, month-to-date and 13.5% year-to-date, net of fees. The Fund's approximate value is \$5.31 billion as of that date. Mr. Sauer commented that 10 out of 16 active managers are outperforming year-to-date, net of fees. He commented that the Public Equity, Fixed Income and Absolute Return asset classes, along with the Total Fund, are outperforming their respective benchmarks year-to-date, net of fees. Mr. Sauer said year-to-date, the Fund has generated a capital market gain of \$652.6 million, has paid benefits and expenses of \$302 million and has received contributions of \$84.1 million. Mr. Sauer stated this month's withdrawals are \$10 million each from BlackRock Global Alpha Tilts and DFA US, \$8 million from William Blair, \$7 million from Polen, \$6 million from DFA International, \$5 million each from Brandes and MFS, and \$4 million each from CastleArk and Earnest. Mr. Sauer noted the amounts are higher than normal as steps are taken to implement the new allocation that was approved as part of the asset liability study.

Mr. Silber noted all the asset classes were outperforming, net of fees. He stated Allianz, an Absolute Return manager who has been a Fund manager for three years and has realized a 10% net annualized return, will present at the November 9 Investment Committee Meeting. Mr. Silber said Allianz will discuss their current strategy as well as Portable Alpha on top of a Fixed Income Strategy which Callan modeled in the AUM study which was approved last month. He said Callan would also provide a real estate performance and re-structuring update.

Approval of Loomis Sayles Guideline Extension. Mr. Sauer referred the Trustees to the memos from Mr. Sauer and Loomis Sayles requesting an extension of the waiver for the guideline in the portfolio that allows up to 3% of the portfolio to be made up of securities that have been downgraded below B- or B3. Mr. Sauer noted this went into effect when a large withdrawal was made from their portfolio with the new fixed income structure. Mr. Sauer said Loomis thought the securities were undervalued and selling them would have been detrimental to the portfolio. He said the guideline was then extended and the securities have held up well and are now closer to the guideline amount. The securities were at 3.52% and are now at 3.22%. Mr. Sauer said some of the securities were sold and because progress is being made, another six-month extension is recommended. Discussion ensued. It was moved by Mr. Petropoulos, seconded by Mr. Matson, and unanimously carried to approve the Loomis Sayles Guideline Extension.

Approval of New Disclosure Related to September Approval of U.S. Large-Cap Value Manager Contract for the purpose of Investing in U.S. Equities. Mr. Barmore advised that the Annuity and Pension Board may vote to convene in closed session on item (II. B.) as provided in Section 19.85(1)(e), Wisconsin State Statutes, to deliberate or negotiate the purchasing of public properties, the investing of public funds, or conducting other specified public business, whenever competitive or bargaining reasons require a closed session. The Annuity and Pension Board may then vote to reconvene in open session following the closed session.

It was moved by Mr. Petropoulos and seconded by Mr. Bell to convene in closed session. Mr. Barmore noted a unanimous vote was made to go into closed session at 9:12 a.m.

The Board reconvened in open session at 9:26 a.m.

It was moved by Mr. Konrad, seconded by Mr. Nicolini, and unanimously carried to approve the New Disclosure Related to September Approval of U.S. Large-Cap Value Manager Contract for the Purpose of Investing in U.S. Equities.

Administration & Operations Committee Report. Mr. Barmore reported that he chaired the meeting on October 19, 2017. He said the contract amendment for Baker Tilly for additional audit services was approved and forwarded to the Board for approval today. The proposal for contract renewal with DS Consulting was discussed and referred back to staff for negotiations. He said it was posted for closed session but did not convene in closed session. Mr. Barmore stated the IT Projects Portfolio was received and the IT Reorganization is in process with DER with a year-end deadline. He said a successful Business Continuity Test was held in September. He said the Organizational and Personnel Updates were received and interviews are near completion for the Chief Financial Officer and the Pension Accounting Manager position has been posted externally. Mr. Barmore said the reclasses are in process with DER. Discussion ensued.

Approval of Baker Tilly Contract Amendment. It was moved by Mr. Barmore, seconded by Mr. Petropoulos, and unanimously carried, to approve the Baker Tilly Contract Amendment.

Approval of the DS Consulting Contract Renewal. Mr. Barmore stated the DS Consulting Contract Renewal is a placeholder and is referred back to staff.

New Business.

Mr. Barmore took the agenda out of order to item IV. E.

Approval of Renewal of Fiduciary Liability Insurance. Mr. Kwiecinski and Ms. Sweeney of the Hays Companies discussed the proposed renewal including additional coverage of a new policy for a non-indemnifiable insurance policy at a \$10M limit with a \$500,000 retention at a premium price of \$30,000. Mr. Kwiecinski said Hays was hired in 2008 to review the insurance program and engaged as a broker in 2009. He said the insurance is in place to protect the Plan as well as the Trustees personally. He said currently there is \$40 million in limits with insurance provided by four carriers and RLI being the primary carrier. He stated coverage is also provided by Chubb, Axis, and additional coverage by RLI. Mr. Kwiecinski discussed pricing and changes from a coverage standpoint. Mr. Kwiecinski recommended making a change from RLI to Hudson with RLI as a second layer. He said the premium would be reduced by \$5,000. Mr. Kwiecinski said in summary Hays looks at the benchmark, limits relative to peers, retention and price per million. He said the limits are reasonable based upon the benchmark, the retention is lower than peers, and the CMERS premium is well below the median. Discussion ensued.

It was moved by Mr. Petropoulos, seconded by Ms. Ford, and unanimously carried to approve the Renewal of Fiduciary Liability Insurance with the additional coverage.

Mr. Barmore called for a break at 9:56 a.m. and resumed the meeting at 10:08 a.m.

Mr. Barmore returned to the agenda at IV. A.

Presentation by Conduent, Inc. of Analysis of the Financial Impact of Alternate Levels for Economic and Demographic Assumptions and Proposed Amendments to the Funding Policy Pursuant to MCC-36. Mr. Jaros discussed assumptions (including demographic and economic), the impact from assumption changes (including actuarial accrued liability, normal cost and employer contribution) and presented a summary of recommended tables and assumptions. Mr. Ellement attended the presentation via teleconference. Mr. Jaros said the demographic assumptions are related to retirement, withdrawal, disability and mortality while economic assumptions pertain to the rate of return, inflation, and salary. Mr. Jaros also stated demographic assumptions are based on the 5-Year Experience Review from January 1, 2012 through December 31, 2016. Mr. Jaros then discussed various retirement patterns for general city, police, fire, duty disability, and terminating employees between actual and expected retirement assumptions. Mr. Jaros also discussed mortality experience for healthy pensioners and disability retirements. Mr. Jaros also discussed economic assumptions, including investment rate of return, inflation rate, and salary increases. Mr. Jaros said Conduent is recommending an inflation rate of 2.5%. Discussion ensued. Mr. Jaros confirmed his firm recommends changing the actuarial cost method from projected unit credit to entry-age normal, as well as, certain other changes to the amortization schedule and removal of the asset corridor as outlined in his presentation dated October 23, 2017 on file with the ERS. Mr. Allen stated the board has full authority in Chapter 36.15.15 to change the demographic and economic assumptions. He said changes to the funding policy in the City Charter require an amendment by the Common Council and approval by six trustees of the Board. Mr. Jaros presented five discount rate scenarios requested by the Board. Discussion ensued.

Mr. Barmore requested a motion to recommend amendment of MCC-36-15-15 to the Common Council in conformance with Conduent, Inc.'s funding proposal dated October 23, 2017 as follows: 1. Replace the projected unit credit with entry-age normal actuarial cost method; 2. Replace the current 10-13 year rolling amortization method with a 15-year layered amortization schedule and payments increasing 2% annually; 3. Also, a separate 25-year amortization period for unfunded actuarial liability due to changes in assumptions; 4. Continue to use current asset smoothing but remove the asset corridor. It was moved by Mr. Nicolini, seconded by Mr. Matson, and unanimously carried, to approve Conduent Inc.'s proposal to amend the Funding Policy outlined in the 5 Year Experience Study presented by Mr. Jaros dated October 23, 2017.

Approval of Economic and Demographic Assumptions in Connection with the 5 Year Experience Study. It was moved by Mr. Matson, seconded by Mr. Bell, and unanimously carried, to approve the demographic assumptions as proposed in the 5 Year Experience Study dated October 23, 2017, on file with the ERS.

It was moved by Mr. Petropoulos, seconded by Mr. Matson, and unanimously carried, to approve the economic assumptions of a 2.5% inflation rate as outlined in the Conduent Inc. presentation dated October 23, 2017 on file with the ERS.

It was moved by Mr. Klusman to approve a discount rate of 7.75% for the next five years. Mr. Barmore asked if there was a second to that motion. The motion failed for lack of a second.

It was moved by Mr. Nicolini, and seconded by Mr. Bell, to approve a select and ultimate discount rate of 8.00% for five years and 8.25% thereafter, as outlined in Conduent Inc.'s presentation dated October 23, 2017 on file with the ERS. Discussion ensued. The motion prevailed by the following roll call vote: AYES: Ms. Ford, Messrs. Konrad, Matson, Nicolini, Parikh, Bell, Petropoulos. NOES: Messrs. Klusman and Barmore. Mr. Barmore stated the motion passed 7 – 2.

It was moved by Mr. Matson, seconded by Mr. Nicolini, and unanimously carried, to approve the salary assumption as outlined in Conduent Inc.'s presentation dated October 23, 2017 on file with the ERS.

(Mr. Barmore left the meeting at 11:40 a.m. and Mr. Petropoulos conducted the remainder of the meeting.)

Retirements, Death Claims, and Refunds. Mr. Allen presented the following activity for the month of September 2017.

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| Active Death Benefits reported | \$0.00 |
| Ordinary Death Benefits reported | \$120,615.82 |
| Retired Death Benefits reported | \$50,727.09 |
| Survivor Death – Termination Benefits reported | \$9,582.18 |
| Refund of Member Contributions paid | \$472,371.10 |

Mr. Petropoulos accepted and placed on file the Retirements, Death Claims, and Refunds.

Conference Requests. Mr. Barmore reported that requests to attend the following conferences had been submitted.

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| Ellen Tangen | Employee Benefit Plans of Tax-Exempt and Governmental Employers |
| Sponsor: | ALI-ABA |
| Location: | Washington, D.C. |
| Date: | October 5-6, 2017 |
| Estimated Cost: | \$839.30 |

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|-----------------|---|
| Mark Nicolini | Pensions & Investments Multi-Asset Investment Conference |
| Sponsor: | Pensions & Investments |
| Location: | Chicago, IL |
| Date: | November 7, 2017 |
| Estimated Cost: | \$408.00 |
| | |
| Himanshu Parikh | 2018 National Conference |
| Sponsor: | Callan Associates |
| Location: | San Francisco, CA |
| Date: | January 29-31, 2018 |
| Estimated Cost: | \$2,500.00 |
| | |
| David Silber | Public Funds Roundtable |
| Sponsor: | Institutional Investor |
| Location: | Los Angeles, CA |
| Date: | April 23-27, 2018 |
| Estimated Cost: | \$1,900.00 |

Mr. Allen also requested to attend the Pensions & Investments Multi-Asset Investment Conference in Chicago, IL on November 7, 2017 at an estimated cost of \$75.00. It was moved by Mr. Konrad, seconded by Ms. Ford, and unanimously carried, to approve the Conference Requests.

Approval to Suspend Disability Benefits for Non-Compliance with Outside Earnings Request. Mr. Allen said four of six people on the non-compliance list have complied with their outside earnings request with the exception of Mr. Krahn and Mr. Oettinger. Mr. Allen stated when Mr. Krahn and Mr. Oettinger submit their 1040 tax returns, they would receive their back pay.

It was moved by Mr. Bell, seconded by Mr. Nicolini, and unanimously carried, to approve the Suspension of Disability Benefits for Non-Compliance with Outside Earnings Request.

Medical Reports.

All Duty & Ordinary Disability Applications & Re-examinations. Mr. Allen presented certifications of the Fire and Police Medical Panel Physicians and the Medical Council relative to Duty & Ordinary Disability Retirement benefits as follows:

| <u>Police – Re-examinations - Duty</u> | <u>Recommendation</u> |
|--|-----------------------|
| Angela July | Approval |
| Deana Martinez | Approval |
| Cindy Warren | Approval |

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| <u>Fire – Re-examinations - Duty</u> | <u>Recommendation</u> |
| Michael Ambroch | Approval |
| Charles Smalley | Approval |
| Scott Van Roo | Approval |
| Jeffrey Wenzel | Approval |
| <u>GC New Applications – Duty</u> | <u>Recommendation</u> |
| Valerie Chapman | Denial |
| <u>GC New Applications – Ordinary</u> | <u>Recommendation</u> |
| Valerie Chapman Effective 11/09/2015 | Approval |
| Aron Gilbert Effective 10/24/2017 | Approval |
| <u>GC Re-examinations – Duty</u> | <u>Recommendation</u> |
| Cheryl Jeanpierre | Approval |
| Gregory Sarozek | Approval |
| <u>GC Re-examinations – Ordinary</u> | <u>Recommendation</u> |
| Kathleen Becker | Approval |
| Roxann Fisher | Approval |
| Sasha Gulley | Approval |
| Linda Rivera | Approval |
| Edward Sturino | Approval |
| Leann Wolfe | Approval |
| Karen Wozniak | Approval |

It was moved by Mr. Matson, seconded by Mr. Bell, and unanimously carried, to accept the aforementioned recommendations of the Fire and Police Medical Panel Physicians and the Medical Council.

Unfinished Business.

Legal Opinions and Service Requests Pending and Legal Opinions. Ms. Horwitz stated there were no outstanding legal opinions for the City Attorney. She said several service requests are in process and they are working with the negotiating partners.

Legislation Requests Pending and Proposed Legislation. Mr. Allen noted a new item with the Employer's Pension Reserve Fund as part of the budget submittal by the administration to drawdown \$5,000,000 in the Employees' Retirement Fund to offset employer paid contributions by the city to the Employees' Retirement System. He said the budget process is

ongoing. Mr. Petropoulos asked the value of the reserve fund and Mr. Silber stated it is \$15.5 million. He also noted the proposed amendment to Board Rule VII. G. regarding the contracting authority of the Investment Committee. He said it is pending as it has been referred to the Legislative Committee.

Executive Director's Report – Inventory of ERS Projects. As a matter of information, Mr. Allen presented a report on the ERS projects and updated the Board on ERS activities, a copy of which is on file with ERS. Discussion ensued.

Informational.

The following is a list of informational items:

- 1) Report on Claims and Litigation.
- 2) Conferences.
- 3) Class Action Lawsuit Report.
- 4) Minutes of the Administration & Operations Committee Meeting Held September 21, 2017.

The following is a list of activities since the last Board meeting, copies sent with meeting notice and attached to minutes:

- 5) Report on Bills.
- 6) Deployment of Assets.
- 7) Securities Lending Revenue and Budget Reports.
- 8) Preliminary Performance Report/Asset and Manager Allocation Pie Charts.

Mr. Petropoulos accepted and placed on file the aforementioned informational items.

There being no further business, Mr. Petropoulos adjourned the meeting at 11:54 a.m.

Bernard J. Allen
Secretary and Executive Director

(NOTE: All proceedings of the Annuity and Pension Board Meetings and related Committee Meetings are recorded. All recordings and material mentioned herein are on file in the office of the Employees' Retirement System, 789 N. Water Street, Suite 300.)