

# VERMONT MUNICIPAL EMPLOYEES' RETIREMENT SYSTEM

Meeting of the Board of Trustees

February 20, 2004

## **Board members present:**

STEVEN JEFFREY, Chairperson, Employee Representative (term expiring July 1, 2004)

DAVID LEWIS, Employer Representative (term expiring July 1, 2006)

W. JOHN MITCHELL, II, Vice-Chairperson, Employee Representative (term expiring July 1, 2005)

MARIE DUQUETTE, Governor's delegate – **arrived later in the meeting**

JEB SPAULDING, Vermont State Treasurer

## **Also attending:**

Cynthia Webster, Director of Retirement Operations

David Minot, Director of Investment Services

Elizabeth Pearce, Deputy State Treasurer

Dick Charlton, Ellen Griggs, Kevin Kondry, NEPC

Doug Hoffer, Economic Consultant

Rob Kellogg, Institutional Shareholder Services – **via conference all**

Jana Bagwell, City of Montpelier

Michael McShane, Assistant Attorney General

Investment Manager personnel

The Chairperson, Steve Jeffrey, called the meeting to order at 9:35 a.m. on Friday, February 20, 2004, in the Treasurer's Conference Room #1 at 133 State Street, Montpelier, Vermont.

## **ITEM 1: Approval of the minutes of December 30, 2003**

**On a motion by Mr. Mitchell seconded by Mr. Spaulding, the Board voted to approve the minutes of December 30, 2003, as submitted.**

Ms. Duquette arrived during the next item.

## **ITEM 2: Investment Consultant Q4/03 Report**

Mr. Charlton, Mr. Kondry and Ms. Griggs reviewed the fourth quarter 2003 performance. They reported the market value of the fund balance at approximately \$210.2 million and a quarterly return of 8.1%, an under performance of the 8.4% median public fund. The one-year return was 20.8%, three-year return 3.4% and a five-year return of 4.7%.

Mr. Spaulding advised the Board that the Senate passed the Unitization Proposal with no substantive changes and is now in the House. He will notify the Board via e-mail if there are any major changes as it progresses.

A. Adopt Investment Policy Guideline

On a motion by Ms. Duquette seconded by Mr. Lewis, the Board unanimously voted to adopt or ratify the Investment Policy Guideline document titled H:\DonnaH\VMERS objs & guidelines\EWG VMERS Approved 9-24-02 Adopted 11-22-02.doc.

B. Adopt Asset Allocation Structure

On a motion by Mr. Spaulding seconded by Ms. Duquette, the Board unanimously voted to reaffirm and adopt the currently approved target as presented effective 2/20/04 which will be amended in the Investment Policy Guideline on page A8 to read:

<b>Equities</b>		
Large Value	Delaware	17.0%
Large Growth	Alliance	16.0%
<b>Total Large Cap</b>		<b>33.0%</b>
Small Cap Core	Lazard	10.0%
<b>Total Small Cap</b>		<b>10.0%</b>
International Equity***	UBS	14.0%
Alternative Investments	Alternatives	4.0%
<b>Total Equities</b>		<b>61.0%</b>
<b>Fixed Income</b>		
Core Fixed Inc	Seix	27.0%
Global Fixed Income		0.0%
High Yield	Seix	5.0%
<b>Total Fixed Income</b>		<b>32.0%</b>
<b>Real Estate</b>	Met Life / SSR	<b>7.0%</b>
<b>Hedged Strategies</b>	-	<b>0.0%</b>
<b>Cash</b>	-	<b>0.0%</b>
<b>Totals</b>		<b>100.0%</b>

On a motion by Mr. Spaulding seconded by Ms. Duquette, the Board unanimously voted to adopt the NEPC Proposed Target asset allocation as presented effective 2/20/04 which will increase the International Equity allocation from 14% to 16%, and decrease the Alternative Investments allocation from 4.0% to 2.0% and will be amended in the Investment Policy Guidelines on page A8 to read:

<b>Equities</b>		
Large Value	Delaware	17.0%
Large Growth	Alliance	16.0%
<b>Total Large Cap</b>		<b>33.0%</b>
Small Cap Core	Lazard	10.0%
<b>Total Small Cap</b>		<b>10.0%</b>
International Equity***	UBS	16.0%
Alternative Investments	Alternatives	2.0%
<b>Total Equities</b>		<b>61.0%</b>
<b>Fixed Income</b>		
Core Fixed Inc	Seix	27.0%
Global Fixed Income		0.0%
High Yield	Seix	5.0%
<b>Total Fixed Income</b>		<b>32.0%</b>
<b>Real Estate</b>	Met Life / SSR	<b>7.0%</b>
<b>Hedged Strategies</b>		<b>0.0%</b>
<b>Cash</b>		<b>0.0%</b>
<b>Totals</b>		<b>100.0%</b>

C. Appropriate Timing of Rebalancing

Mr. Minot reported that the current schedule for rebalancing, pursuant to the Investment Policy Guidelines, is February and August. His recommendation, in concert with NEPC, is to change the schedule to March and September.

**On a motion by Ms. Duquette seconded by Mr. Mitchell, the Board unanimously voted to amend page A9, *Rebalancing*, of the Investment Policy Guideline to schedule the semi-annual fund rebalancing to March and September and for the 4<sup>th</sup> sentence in the section to read ... on or about the later half of March and September, each year.**

Ms. Griggs advised that she would provide new copies of the Investment Policy Guideline to the Board, which will have a new cover page, amended page A8, page A9, and will also include the asset allocation handout in entirety in the Investment Policy Guideline as section D.

The Board thanked the Deputy Treasurer, Ms. Pearce, and NEPC for their research and the asset allocation presentation.

**ITEM 3: Investment Manager Presentations**

**MetLife:** John Loehr, Managing Director appeared before the Board. The actively managed open ended, commingled, core portfolio of equity real estate was reported to have gross assets of \$1.5 billion of which approximately \$13.66 million of the market value is from the VMERS. The portfolio consists of 51 properties in 22 markets. The Q4/03 return was 0.6% compared to the NCREIF Index of 2.0%, one-year return was 7.0%, three-year return 4.8% and five-year return 7.7%.

*Because of a conflict for Mr. Jeffrey and Mr. Lewis, **the next quarterly investment meeting of the Municipal Retirement Board will be moved to Tuesday, May 18, 2004**, from the originally scheduled date of May 21, 2004. The Investment Consultant's schedule was confirmed to accommodate this change. Managers will be notified.*

**Alliance Capital Management:** Karen Sestin, Senior VP and Portfolio Manager, and Carter Reynolds, Senior VP Institutional Marketing and Client Services, appeared before the Board. The domestic large cap growth portfolio was reported to have a market value of approximately \$34.1 million with a Q4/03 return of 8.8% compared to the Russell 1000 Growth index of 10.4%; 1-year performance was 26.1%, three-year return (8.9)%, and five-year return (3.7)%.

**On a motion by Mr. Spaulding seconded by Ms. Duquette, the Board unanimously voted to authorize Mr. Minot and NEPC to pursue and execute a separately managed account with Alliance Capital if the change is cost neutral or economically favorable.**

**Lazard Asset Management:** Patrick Mullin, Director and Portfolio Manager, and Brad Rudner, VP Institutional Marketing, appeared before the Board. The small cap core portfolio was reported to have a market value of approximately \$22.7 million with a Q4/03 return of 14.7% compared to the Russell 2000 Index of 14.5%, 1-year performance was 40.0%; three-year return 11.2%. The manager has not established five-year performance results.

**ITEM 4: Discuss/Act on Proxy Voting Policy**

The Board discussed the Proxy Voting Policy. Mr. Rob Kellogg joined the meeting via conference call.

**On a motion by Mr. Spaulding seconded by Mr. Mitchell, the Board voted to accept the Proxy Voting Policy (draft #4), to be effective March 1, as presented. Mr. Spaulding, Ms. Duquette, and Mr. Mitchell voted yes. Mr. Lewis voted no. Mr. Jeffrey abstained.**

**ITEM 5: Treasurer's Report**

A. VT Targeted Investment Report

Mr. Spaulding presented a report prepared by Mr. Douglas Hoffer, written at the Treasurer's request in response to a Legislative directive to study and report on how states can appropriately use pension funds for in-state targeted investing.

The Board requested a future agenda item with NEPC to discuss the 2% investment allocation to alternative investments.

B. Money Manager Behavior Policy

The Board reviewed the 2/6/04 proposed *Business Conduct* policy, which has received review and comments by Bill Griffin, Chief Assistant Attorney General.

**On a motion by Mr. Spaulding seconded by Mr. Mitchell, the Board voted not to adopt the 2/6/04 Business Conduct policy, as written. Mr. Spaulding and Mr. Mitchell voted yes. Mr. Jeffrey, Ms. Duquette and Mr. Lewis voted no.**

The Board members who voted no on the motion stated they supported the concept embodied in the draft policy, but felt the current Investment Policy Guidelines already allowed the Board to address inappropriate behavior and that the proposed policy would confuse the issue.

**ITEM 6: Director of Finance & Investments Report**

A. Breakout of State Street Alternative Investments

Mr. Minot distributed and discussed a list of alternative investment holdings.

Mr. Minot will include the funds of \$313,655.44 in the 2% alternative investment asset allocation in a category entitled "VT Investments".

B. DC Contract Recommendations

Mr. Minot advised the Board of the currently advertised RFP, with a March 4, 2004 submission deadline, sponsored by the Vermont State Employees' Retirement System and Vermont State Treasurer for an Investment Consultant to examine the 457 Deferred Comp and State's Defined Contribution plans. Mr. Minot suggested the Board consider participation in the contract when awarded. He explained that the Board would benefit from the consultant's research of the plan fund options, etc.

The Board requested Mr. Minot pursue the option of a waiver to Bulletin 3.5 from the Attorney General and Secretary of Administration similar to the State's request when they renewed their DC contract with Fidelity Investment.

**ITEM 7: Director of Retirement Operations Report**

A. Website Survey Results

The Board reviewed the survey result data distributed.

B. Montpelier Firefighters Update

Jana Bagwell appeared before the Board. She reported that in the City of Montpelier's prior retirement plan included only the base pay of employees, no overtime. The City of Montpelier believes it conveyed information to its employees that the practice would continue and that only base pay would be reported once the transfer to the VMERS plan happened. The costs established to convert prior service was calculated on that premise. The issue is that the municipality was told, and has in writing, that the practice of reporting base pay only could continue once the entity was enrolled in VMERS. Members of the fire fighter employee's union want their total compensation included in the transfer and reported. They are now trying to enlist other unions, custodians, etc. to aid in legal costs to require their overtime be included in prior service transferred to VMERS.

Mr. Mitchell disclosed that he is the President of Local #1369, Barre Town's municipal employee union chapter, and has received a call from Montpelier's custodian union requesting the opportunity to present the issue, and potentially solicit, support to their union.

C. Retirement Legislative Update

Mrs. Webster distributed a copy of her 2/18/04 memo to the House Government Operations Committee regarding housekeeping language.

Mr. Jeffrey advised that the Vermont Police Association is trying to change statutory language in Title 24 §5069 from "may" to "shall provide" health insurance.

He also reported that the Vermont Police Association is initiating discussions to require the state to pay for prior police service for police in the VMERS plan.

D. Disability Hearing Officer RFP

Mrs. Webster advised the Board that five responses were received and would be distributed to the Board Chairs and Mr. McShane with a matrix for final selection consideration.

E. Regional Planning Commissions

Ms. Webster distributed a memo regarding the history and status of Regional Planning Commissions currently enrolled in VMERS.

Mr. Mitchell left the meeting.

**At 3:47 p.m. on a motion by Mr. Lewis seconded by Ms. Duquette, the Board unanimously voted to enter into executive session pursuant to Title 1 § 313 to receive legal advise in connection with potential litigation.**

**At 4:10 p.m. the Board moved out of executive session.**

**On a motion by Mr. Spaulding seconded by Ms. Duquette, the Board unanimously voted to support an amendment to Title 24 § 5064(f) as presented by Assistant Attorney General, Mike McShane in draft #1.**

**ITEM 8: Any other business to be brought before the Board**

None

**Next Meeting Dates:**

The next scheduled quarterly investment meeting is Tuesday, May 18, 2004.

**On a motion by Mr. Jeffrey seconded by Ms. Duquette, the Board unanimously voted to adjourn at 4:14 p.m.**

Respectfully submitted,

Cynthia Webster  
Secretary to the Board

**GOALS**

The Board established the following list of goals to be addressed in the future:

**TO DO's**

<b>Who</b>	<b>What</b>	<b>When</b>	<b>Done</b>
<b>** = for possible 2004 legislative changes</b>			
CLW/All	Adopt final policy re: joining entities w/prior service liabilities (7/11#3)	ASAP	
CLW	Send letter to Fidelity re: info provided to potential DC members (7/11 #6)	ASAP	
D Minot	Question letter from NEPC (7/11 #8)	ASAP	
D Minot	List (annually) of all alternative investments (8/22 #3)	11/21/03	
NEPC	Global bonds, high yield, hedge funds education (8/22 #4)	11/21/03	
All	Examine new funding methods w/actuary (10/29 #2)	ASAP	
<del>NEPC</del>	<del>Asset Allocation &amp; Policy Guideline ratification (11/21 #3)</del>	<del>ASAP</del>	2/20/04
<del>Dave M</del>	<del>Breakout the alternative investments held in the State Street account (12/30 #5)</del>	<del>2/20/04</del>	2/20/04
Dave M	Provide the Board with a copy of the latest Green Mountain Capital annual report (12/30 #5)	ASAP	
<del>Dave M</del>	<del>Prepare DC contract recommendations for Board (12/30 #6)</del>	<del>2/20/04</del>	2/20/04
<del>Beth</del>	<del>History and adoption of the Investment Policy &amp; Guidelines (12/30#6)</del>	<del>2/20/03</del>	2/20/04
<del>Bill G/AG</del>	<del>proposed language changes to 24 VSA § 5062 Mr. Griffin will review and work language (12/30 #7)</del>	<del>ASAP</del>	Done
CLW	Research RPC's memberships (12/30 #10)	2/20/04	
All	Discuss the 2% investment allocation to alternative investments		