

# VERMONT STATE TEACHERS' RETIREMENT SYSTEM

Meeting of the Board of Trustees

February 18, 2004

## **Board Members present:**

JOSEPH MACKEY, Chairperson (Active No. 29334), term expiring July 1, 2005  
JON HARRIS, Vice-Chairperson (Active No. 25669), term expiring July 1, 2007  
JAY KAPLAN, Association of Retired Teachers of Vermont, term expiring July 1, 2004  
THOMAS CANDON, representing Commissioner of BISHCA  
VAUGHN ALTEMUS, representing Commissioner of Education  
JEB SPAULDING, VT State Treasurer

## **Also attending:**

Cynthia Webster, Director of Retirement Operations  
David Minot, Director of Investment Services  
Michael McShane, Assistant Attorney General  
Bridget Asay, Assistant Attorney General  
Dick Charlton, Ellen Griggs, Kevin Kondry, NEPC  
Rita Rinehart, Association of Retired Teachers of Vermont  
Angelo Dorta, VT-NEA  
Doug Hoffer, Attorney and Economic Consultant  
Rob Kellogg, Institutional Shareholder Services  
Investment Manager personnel

The Chairperson, Joe Mackey, called the meeting to order at 8:10 a.m. on Wednesday, February 18, 2004, in the Treasurer's Conference Room #1 at 133 State Street, Montpelier, Vermont.

## **ITEM 1: Approval of minutes of December 16, 2003**

**On a motion by Mr. Candon seconded by Mr. Kaplan, the Board unanimously voted to approve the minutes of December 16, 2003, with the following amendments:**

**Page 1, Item 2, paragraph 2: strike the last sentence**

**Page 5, Item 13, final paragraph: strike the last sentence**

**Page 5, Item 14, paragraph 3 motion: ...VSERS and State Treasurer. ~~to attend.~~**

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

Mr. Charlton, Ms. Griggs and Mr. Kondry reviewed the fourth quarter 2003 performance. They reported a market value fund balance of \$1.217 billion and a quarterly return of 9.1%, an out performance of the 8.4% median public fund. The one-year return was 23.8%, three-year return 3.2% and five-year return 5.1%.

## **ITEM 3: Investment manager Presentations**

**J & W Seligman:** Dorothy Buckley, Senior VP, and Rick Ruvkun, Managing Director and Portfolio Manager, appeared before the Board. The small cap growth portfolio was reported to have a market value of approximately \$73.8 million with a Q4/03 return of 15.3% compared to the Russell 2000 Growth index of 14.5%; one-year return was 40.2%, three-year return (2.0%), and five-year return 1.6%.

**Delaware Investmen:** Patty Karoli, Senior VP, John Kirk, Director Global FI & Currency, Ryan Brist, Senior VP and Senior Portfolio Manager, and Christopher Welker, VP and Senior Investment Grade Trader, appeared before the Board. The global fixed income portfolio was reported to have a market value of approximately \$210.9 million with a Q4/03 return of 4.0% compared to the CITI WGB index of 5.2%; one-year performance was 13.3%, three-year return 11.6%, and five-year return 7.9%.

Mr. Kaplan asked if the Board added more money and included a high yield mandate if the fees would remain the same. The answer was in the affirmative.

Pursuant to the VSTRS Investment Guidelines, Mr. Brist advised the Board that Delaware Investments is exercising their option to opportunistically use "interest rate futures" to manage the duration of the US portfolio.

**MetLife (SSR):** 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 \$23.2 million of the market value is from the VSTRS. 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%.

Mr. Loehr discussed the fund's underperformance and what actions are being taken to make corrections.

**ITEM 4: Director of Finance & Investments Report**

A. 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 the third week of March and September.

**On a motion by Mr. Kaplan seconded by Mr. Altemus, the Board unanimously voted to amend the Investment Policy Guideline to schedule the semi-annual fund rebalancing to March and September.**

B. Securities Litigation Follow-Up

Mr. Minot reported that the AG's Office and BISHCA are working to recover potential losses to pension funds as a result of possible fraudulent and/or bias research by some managers during the 2000-2002 timeframe.

Mr. McShane reported the State of Vermont has been registered as a participant in class action law suits against Enron and WorldCom.

C. Commission Recapture Update

Mr. Minot reported that negotiations have resulted in a contract which is being reviewed by the AG' Office and will be sent to the Chair for signature in the near future.

**ITEM 5: Act on Disability Retirement for Patricia O'Shea**

**On a motion by Mr. Kaplan seconded by Mr. Altemus, the Board unanimously voted to approve the disability retirement for Patricia O'Shea as recommended by the Medical Review Board.**

**ITEM 6: Comments from Putnam Investments**

Mr. Joseph Carrabes appeared before the Board to apologize for past behavior of Putnam Investment's Mutual Fund personnel.

**ITEM 7: Other Business Brought Before the Board**

Bridget Asay, Assistant Attorney General, appeared before the Board.

**At 2:10 p.m. on a motion by Mr. Altemus seconded by Mr. Candon, the Board unanimously voted to enter into executive session pursuant to Title 1 §313, to receive legal advice regarding pending litigation.**

**At 2:15 p.m. the Board moved out of executive session.**

**ITEM 8: Treasurer's Report**

A. 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. Kaplan seconded by Mr. Mackey, the Board unanimously voted to adopt the 2/6/04 Business Conduct policy and for it to be included in the body of their Investment Policy Guidelines.**

B. VT Targeted Investment Report

Mr. Hoffer appeared before the Board to discuss the report he prepared 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 agreed to add a discussion regarding the Economically Targeted Investment (ETI) policy to the TO-DO List.

**ITEM 9: New England Pension Consultants**

A. International Equity Manager Search Consideration

The Board reviewed and discussed the *Passive vs. Active – International Equity* report prepared by NEPC.

B. Discuss Asset Allocation Structure

The Board reviewed and discussed the current asset allocation.

**On a motion by Mr. Harris seconded by Mr. Mackey, the Board unanimously voted to reaffirm the currently approved asset allocation as presented effective 2/18/04, and add the following Asset Allocation Structure as section “D” to the Investment Policy Guidelines:**

<b><u>Equities</u></b>		
Large Value	Delaware	12.0%
Large Core	SSGA	8.0%
Large Growth	Fidelity	12.0%
<b>Total Large Cap</b>		<b>32.0%</b>
Small Value	Wellington	6.0%
Small Growth	Seligman	6.0%
<b>Total Small Cap</b>		<b>12.0%</b>
International Equity	SSGA Daily EAFE	8.0%
	Delaware	8.0%
<b>Total IE</b>		<b>16.0%</b>
Private Investments	Pru Timber/VVC	2.0%
<b>Total Equities</b>		<b>62.0%</b>
<b><u>Fixed Income</u></b>		
Core Fixed Inc	Loomis / Delaware	23.0%
Global Fixed Income	Delaware	7.0%
High Yield		0.0%
<b>Total Fixed Income</b>		<b>30.0%</b>
<b><u>Real Estate</u></b>	Lendlease/SSR/UBS	<b>8.0%</b>
<b><u>Hedged Strategies</u></b>		<b>0.0%</b>
<b><u>Cash</u></b>		<b>0.0%</b>
<b>Totals</b>		<b>100.0%</b>

C. Discuss Investment Policy Guideline

Ms. Griggs advised the Board that she would update the Investment Policy Guidelines and distribute it to the Board. The Alternative Investments section will also be amended by removing the final bullet point:

- The alternative asset program will be diversified to limit the exposure of any one investment to 2% of the assets of the State Teachers' Retirement System of Vermont's total assets.

**On a motion by Mr. Mackey, seconded by Mr. Candon, the Board unanimously voted to accept NEPC's recommendation to convert the Lend Lease holdings to the REIT Morgan Stanley PPF (Prime Property Fund).**

**ITEM 10: Director of Retirement Operations Report**

A. Retirement Legislative Update

Mrs. Webster distributed a copy of H.643 regarding proposed legislation that supports restoration of previously withdrawn service credit by re-depositing the contributions plus interest received at the time of withdrawal.

**On a motion by Mr. Spaulding seconded by Mr. Altemus, the Board voted not to support H.643 as written but to support language that mirrors VSERS Title 3 §477 language that required cost neutral payment, which includes the state's contributions. Mr. Spaulding, Mr. Mackey, Mr. Altemus, Mr. Candon and Mr. Harris voted yes. Mr. Kaplan voted no.**

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

Mrs. Webster advised the Board of a potential amendment and minimal cost involved in expanding the timeframe for active employees to apply for a military grant of service credit and payments of retiree stipends based on the federally expanded timeframe to include the 1,500 nationwide military servicemen that served during the pre-Viet Nam period of 2/28/1961 through 8/5/1964.

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.

B. Disability Hearing Officer RFP

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

**ITEM 11: Update on Under Funding Issue**

Mr. Mackey thanked the Treasurer and his staff for the work involved in the presentation materials used to educate members of Legislature on the under funding issues.

Mr. Altemus reiterated the Chair's comments and also thanked Mr. Mackey for his participation.

The Board reviewed sections of the PowerPoint presentation and Mr. Spaulding advised the Board that the Governor has recommended a minimum \$3 million appropriation from the "waterfall" fund to the VSTRS for FY'05.

Mr. Spaulding distributed a copy of the *Annual Report* which also contains a section on the under funding issue.

**ITEM 12: Discuss/Act on Proxy Voting Policy**

Rob Kellogg of Institutional Shareholder Services appeared before the Board. Mr. Kellogg reviewed and discussed the Proxy Voting Policy.

**On a motion by Mr. Kaplan seconded by Mr. Mackey, the Board voted to accept the Proxy Voting Policy as presented. Mr. Spaulding, Mr. Mackey, Mr. Altemus, Mr. Kaplan and Mr. Harris voted yes. Mr. Candon abstained.**

Mr. Charlton suggested an amendment to the wording in paragraph 2 on page 4.

**On a motion by Mr. Candon seconded by Mr. Altemus, the Board unanimously voted to reconsider the previous motion.**

**On a motion by Mr. Harris seconded by Mr. Kaplan the Board unanimously voted not to adopt the Proxy Voting Policy, as written.**

**On a motion by Mr. Spaulding seconded by Mr. Altemus, the Board voted to accept the Proxy Voting Policy (draft #4) with an amendment to paragraph 2 on page 4. Mr. Spaulding, Mr. Mackey, Mr. Altemus, Mr. Kaplan and Mr. Harris voted yes. Mr. Candon abstained.**

**The first line of paragraph two (2) will be amended to read:**

**We expect our investment managers to vote our proxies solely in the best interest of plan participants and beneficiaries, and, for funds invested by the State Treasurer, Vermont citizens.**

**ITEM 13: Any Other Business to be Brought Before the Board**

None

**Next Meeting Dates:**

The next scheduled business meeting is March 15, 2004.  
The next scheduled quarterly investment meeting is May 19, 2004.

**On a motion by Mr. Harris seconded by Mr. Altemus, the Board unanimously voted to adjourn at 5:20 p.m.**

Respectfully submitted,

Cynthia L. Webster  
Secretary to the Board

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

Support full appropriation  
 Increased staff for counseling & continued training

**TO DO's**

<b>Who</b>	<b>What</b>	<b>When</b>	<b>Done</b>
<b>** = for possible 2004 legislative changes</b>			
CLW	Conclude RFP for evidentiary hearing officer	ASAP	1/27/04
CLW	Reportable wages (7/21 item 9)	ASAP	
NEPC	Comsn Recapture negotiations w/State Street Bank (8/20 item 3)	ASAP	2/18/04
David	Appropriate timing of semi-annual rebalancing (8/20 item 4)	11/19/03	2/18/04
NEPC	Enhanced Index manager options (9/23 item 2)	11/19/03	
CLW	Follow up on developing policy for independent/private school membership (9/23 item 4)	ASAP	
CLW	Evaluate magnitude/impact to system of potential 700 wavered teachers (9/23 item 11)	ASAP	
All	Consider formal Int'l Equity manager search (11/19 item 2)	TBD	2/18/04
CLW	Prepare draft policy for Board & AG re: Independent Schools (12/16 # 4)	ASAP	
Beth/CLW	Develop funding status presentation materials (12/16 #5)	ASAP	2/18/04
David	Follow up on securities litigation (12/16 item 8)	2/18/04	2/18/04
CLW	Actuary cost: increasing Group C bens above 50% (12/16 # 9)	ASAP	2/18/04
Jeb	Modify Manager Behavior Policy and re-distribute for Board comments (12/16 #11)	ASAP	
CLW	Modify legislative recommendations get actuary estimate and re-distribute for Board comments (12/16 #13)	ASAP	
All	discussion of Economically Targeted Investment (ETI) policy (2/18 item 8)	TBD	