

**CITY OF PONTIAC, MICHIGAN  
POLICE AND FIRE RETIREMENT SYSTEM  
MARCH 30, 2006**

A regular meeting of the Board of Trustees was held on Thursday, March 30, 2006 in the Shrine Room on the Main Level of City Hall, 47450 Woodward Avenue, Pontiac, MI 48342. The meeting was called to order at 9:08 a.m.

**TRUSTEE PRESENT**

Craig Storum, Chairman  
Ed Hannan, Secretary  
Brian Lee  
Thomas Miller, Vice Chairman

**TRUSTEES ABSENT**

Mayor, Clarence Phillips (*absent*)

**OTHERS PRESENT**

Cynthia Billings, Sullivan, Ward, Asher & Patton, P.C.  
Laurence Gray, Gray & Company  
Ellen Zimmermann, Retirement Systems Administrator  
Jane Arndt, M-Administrator Assistant

**CONSENT AGENDA**

- A. Minutes of Regular Meeting: February 23, 2006
- B. Communications:
  - 1. Correspondence from Lerach Coughlin Stoa Geller Rudman & Robbins Re: Updated Settlement Reports
  - 2. Correspondence from Atlantic Asset Management Re: January Report
  - 3. Correspondence from Munder Capital Re: New CIO
  - 4. Correspondence from Morgan Stanley Re: February Portfolio Update
  - 5. Conferences:
    - a. Washington Legislative Update – IFEBP - May 22-24, 2006
    - b. Investments Institute –IFEBP - April 24-26, 2006
    - c. 11<sup>th</sup> Annual Public Funds Summit – IMN – April 2-5, 2006
    - d. Technology Solutions for Public Fund Management and Operations – IMN – April 3-5, 2006
    - e. 52<sup>nd</sup> Annual Employee Benefits Conference – IFEBP – Oct. 8-10, 2006
- C. Financial Reports:
  - 1. Financial Reports – February 2006
  - 2. Securities Lending Report – January 2006
  - 3. Commission Recapture Report – January & February 2006
  - 4. Accounts Payable – March 2006

D.	Final Pension Calculations:		
	1. Norman Lee (revised)	#2305	\$3,139.42
	2. Gail Wojciechowski (revised)	#2312	4,525.06
	3. Roy Johnson	#2239	3,897.99

**RESOLUTION 06-016** By Hannan, Supported by Lee  
 Resolved, That the items of the consent agenda for March 30, 2006, be approved as amended.

Yeas: 4 - Nays: 0

**CONSULTANTS**

**Re: Gray & Company – Real Estate**

Guggenheim Contract

Ms. Billings advised the Board that Guggenheim refused to acknowledge their fiduciary responsibility under PA 314. She stated that Guggenheim asked for a letter saying that they're not an investment fiduciary.

Mr. Gray told the Board that there should not be a problem selecting a manager. He described American Realty Advisors and Guggenheim Real Estate, LLC which are open-ended funds. Harbert Management is a closed-end fund that requires a seven to ten year investment with no liquidity. He stated that expected returns are 13-15% for American Stable Value Fund, 16-18% for Guggenheim Real Estate *PLUS* and 22-24% for Harbert Real Estate Fund III. He also commented that he understands that the Board does not feel comfortable locking up funds.

Chairman Storum asked if there had been any further contact with Guggenheim Management. Ms. Billings commented that she had spoken with their attorney and a management representative on the phone. They both told her that they were not willing to go to the expense of hiring a Michigan attorney. Mr. Gray told the Board that they are fiduciary and that Bay City currently has funds invested in Guggenheim. Ms. Billings stated that Bay City may not have required that Guggenheim acknowledge their fiduciary responsibility in the adoption agreement.

Chairman Storum suggested moving on and making a decision. Mr. Gray asked if the Board was looking for more or less liquidity. Trustee Lee replied that he liked American Realty Advisors because of their liquidity. Chairman Storum felt that both open-ended firms were good and that he had liked Guggenheim because they were more diverse. He also stated that Harbert Management offered higher returns but were a closed-end fund.

Trustee Hannan commented that he had not been present for the interviews. Mr. Gray mentioned that Guggenheim had American Stable Fund as part of their portfolio. Trustee Miller remarked that he was happy with either American or Guggenheim.

**RESOLUTION 06-017** By Lee, Supported by Hannan

Resolved, That the Board of Trustees approve pending legal contract approval that \$7 million be invested in American Stable Value Fund.

Yeas: 4 – Nays; 0

High-Yield Bond Manager Search

Mr. Gray said that both plans have high-yield fixed income managers that consider themselves high-quality junk bond managers which is an oxymoron. He stated that Seix Advisors and Atlantic have the same long-term performance issues and are unable to keep up with the benchmark. Neither is a true high-yield manager which prevents them from buying below investment grade bonds like their peers. He told the Board that Atlantic has lost 400 basis points during the last three years with performance of 10% versus 13.9% for the index .

Mr. Gray discussed the list of managers with the Board. He stated that they are all considered best of breed high-yield managers in the country and the list contains a mixture of conservative to more aggressive managers.

He reviewed the managers with the Board stating that Babson is a mid-size manager with \$4.3 billion in their high-yield fixed income product. He described DDJ and Peritus as true high-yield managers with CCC bond weighted portfolios. He described Delaware, JP Morgan and NY Life as good large fixed income core managers. He also mentioned that JP Morgan has a huge campus just outside of Columbus, Ohio. He said that PENN and Reams are fully immersed in high-yield.

Mr. Gray explained the different bond ratings to the Board showing the difference between investment grade and junk bonds. He showed how various grades of bonds performed during different time periods versus the Merrill Lynch High Yield Index. To offset any concerns the Board might have in regards to investing in low-rated bonds, he stated that 60% of the S&P 500 invest in CCC or junk rated bonds.

Mr. Gray reviewed the list of manager's trailing year and calendar year returns and detailed the risk adjusted returns with the up and down market capture ratios for each manager. He specifically pointed out the exceptional down market capture performance of Peritus and DDJ whose numbers went up when the market went down.

Mr. Gray discussed bond maturity stating that the current yield index is three to five years, but the bulk is in the five to ten year range. Mr. Gray displayed the portfolio characteristics of the manager. He showed how the average coupon relates to yield and maturity. He stated that the average coupon returns 11% with DDJ's split B-rated bond yield at 12.2%. He told the Board that all of these firms are true high-yield managers that offer great returns because a large segment of their portfolios are lower quality bonds.

Mr. Gray discussed the diversity in the credit quality of bonds between the managers. Peritus has 61.41% of their portfolio invested in CCC-rated bonds with Delaware at 16.4%.

Mr. Gray reviewed the three-year and five-year risk return charts. He described manager performance on the charts pointing out Peritus as being high on the return chart. He discussed the mixed group of managers and how they differed on the risk scale. He told the Board that these charts display what a true high yield manager looks like.

Chairman Storum asked how Atlantic differs from Penn. Mr. Gray replied that Penn is able to buy down at opportune times. Chairman Storum asked about DDJ and the 16% listed in the Other column. Mr. Gray said that they occasionally fish deep but would not buy D-rated bonds.

Trustee Miller asked if it was necessary to replace the fund's high-yield manager. Mr. Gray replied that it is totally at the discretion of the Board. He stated that the high-yield index is invested 15-20% in CCC-rated bonds. He told the Board that Atlantic doesn't buy any and if you extract the performance of the C-rated bonds Atlantic looks good. However, the issue is that the fund does not have a true high-yield manager but a 10% return is not bad.

Mr. Gray said that he visited Oppenheimer and that they are a solid core manager as is Goode at 4.6%. He remarked that a large chunk of the fund is in protected principal and that they have hedged well to protect the fund from the rising interest rate environment.

Trustee Miller commented that he felt they were doing well with the funding status of the plan. He questioned the risk and that 10% was a good return. Mr. Gray responded by saying that there is no push but he will continue to report that the manager could not keep up with the high-yield index. He also said that he would take a 10% return on a three-year rolling number. He told the Board that they currently have more of a core plus manager.

Mr. Gray reviewed the high-yield allocation stating that Atlantic was about 400 basis points below the index and that they represented 2% of the portfolio. Chairman Storum commented that Atlantic is not a true high-yield manager. Trustee Miller noted that \$5 million of a \$253 million portfolio is a small risk. Trustee Hannan asked how it would impact the mix of the plan as a whole. He also questioned how it compares to being consistently below the benchmark. Mr. Gray responded by saying that it affects the plan but not a great deal.

Mr. Gray then asked if the Board would like to interview any of the managers. Trustee Miller asked why they should take more risk. Trustee Lee commented that maybe it isn't the right time. Trustee Hannan suggested that the Police and Fire Board attend the manager presentations with the General Board. Chairman Storum commented that he sees this as an opportunity to gain ground and they're not taking advantage of this position.

Mr. Gray told them that they have seen the names and that when interest rates level out the Board can revisit the allocation and dial up high-yield. He also acknowledged that they had recently made two protective yet aggressive moves in the intermediate fund and the American Stable Value Fund.

Chairman Storum had questions regarding the prior asset allocation and how the addition of American Stable Value Fund affects the allocation. He asked if the current allocation meets the fund's liability. He also mentioned that the system is not capitalizing on the small cap

international investment. He said that he agrees that the Board needs to preserve the principal. However, he's not sure the fund is hitting those targets. He asked if the system is currently 107% funded if the plan meets its target.

Mr. Gray said that he would check with the actuary to look twenty-five to thirty years out. However, he did say that he feels the long-term numbers are good with the total plan five-year number at 10.3% being in the first percentile for similar funds. He said that the three-year and one-year numbers at 10.1% and 6.1% also include prior gains and losses.

Chairman Storum asked about the current mix in the portfolio noting that it had changed over the past ten years. Mr. Gray replied that the projected outlook was:

Fixed income was projected at 5% to 5.2% for the Lehman Aggregate  
Domestic large cap was projected at 8.6% mentioning that the American Stable Value Fund will track upward with interest rates  
Domestic small cap was projected at 9.1% to 9.2%  
International equity was projected at 9.4% to 9.5%

Chairman Storum asked if we bring back the current blend where would Atlantic fall on the risk return chart. Mr. Gray said at 5% it would be at the bottom of the left quadrant.

Mr. Gray spoke about his visit to Oppenheimer Capital. He said that his visit was to check out their research strategy. He said that during his visit he was introduced to a young woman who works with international small cap and dips down into emerging markets. He was very impressed and considered her borderline brilliant. He told the Board that it might be a good idea to start looking at some of these companies.

He discussed the Morgan Stanley product and how it had most always been closed to new investors. He told the Board that Dominic Caldecott opposed management wanting to open the product which may have influenced his decision to retire. Things are not improving at Morgan Stanley; international equity is currently more of a concern than high-yield.

Morgan Stanley's international equity product is really hurting. Ms. Zimmermann asked if Morgan Stanley has lost a lot of clients. Mr. Gray replied that they had and that the Board may want to change its international large cap manager.

Chairman Storum commented that he is concerned with the target and risk. He asked Mr. Gray how much risk is associated with small cap emerging markets. Mr. Gray told the Board that he would bring back a list of international equity managers who can dip down to small cap. Trustee Miller expressed his concern over the risk.

Mr. Gray stated that he likes to visit with managers and explore their investment strategies and philosophies, so it will take a few months before he brings back a list for the Board's review. He also told the Board that he would bring a forecast to the meeting with the current allocation along with a few variations for their review.

Mr. Gray again asked if the Board was interested in hearing the high-yield manager presentations. There was discussion with Trustees Storum and Lee stating that they would like to hear Penn Capital, DDJ and Delaware.

**RESOLUTION 06-018** By Hannan, Supported by Lee

**Resolved**, That the Board of Trustees will hear presentations on April 27, 2006 at 10:30 a.m. after the regular business meeting from the following high yield fixed income managers: Penn, DDJ and Delaware.

Yeas: 4 – Nays: 0

## **REPORTS**

**Re: Chairman** – None

**Re: Secretary** – None

**Re: Trustees** - None

- 1. Real Estate Committee** – None
- 2. Personnel Committee** – None

**Re: Staff**

### Disability Re-Exam

Ms. Zimmermann distributed the Medical Director's report of the disability exam for Gary Hutchinson.

**RESOLUTION 06-019** By Miller, Supported by Storum

**Resolved**, That the Board of Trustees concurs with the recommendation of the Medical Director that Gary Hutchinson continues to be disabled and that his pension be continued.

Yeas: 4 – Nays: 0

Ms. Zimmermann referred to the last meeting where she asked the Board to postpone the disability re-exam for Magdalena Martinez. She told the Board that Ms. Martinez has no plans to return for her exam and is currently confined to a wheelchair due to her diabetes. Chairman Storum wanted to confirm the information. He asked Ms. Zimmermann to investigate whether Dr. Roth has a colleague in Puerto Rico that could examine Ms. Martinez. Ms. Zimmermann replied that she would look into the matter.

### VISA Issue

Ms. Zimmermann informed the Board that there were a few trustees who have had problems using their Board-issued VISA cards. She told the Board that certain vendors require a security code which is the tax identification number in order to validate the card. She stated that if any of

the trustees is currently having any difficulties using their card to let her know and she will take care of the problem.

Stolen Property

Ms. Zimmermann informed the Board that someone had broken into her home and stole her work-issued laptop and that a police report has been filed. Chairman Storum asked if there was any confidential information on the laptop. Trustee Miller asked if the laptop was password protected. Ms. Zimmermann replied that it was not password protected and that no confidential data was stored on the laptop.

Plante & Moran 2005 Audit Fee Schedule

Ms. Zimmermann requested that the Board of Trustees approve the 2005 audit fee schedule for Plante & Moran. She told the Board that the 2005 fee is \$9,705 which includes \$1,200 for GASB 40 reporting that was not a requirement for the 2004 audit. Chairman Storum confirmed with Ms. Zimmermann that all government pension plans require GASB 40 reporting.

**RESOLUTION 06-020** By Lee, Supported by Miller

Resolved, That the 2005 Plante & Moran Audit Fee Schedule be approved.

Yeas: 4 – Nays: 0

**Re: Legal**

**RESOLUTION 06-021** By Hannan, Supported by Miller

Resolved, That the minutes of the closed session of February 23, 2006 be approved.

Yeas: 4 – Nays: 0

Trustee Reimbursement Policy

Cynthia Billings referred to changes made to the trustee reimbursement policy dated April, 2004. She stated that the references to per diem were deleted from the policy.

**RESOLUTION 06-022** By Miller, Supported by Lee

Resolved, That the Trustee Reimbursement Policy revised to incorporate previous changes adopted by the Board be approved.

Yeas: 4 – Nays: 0

Ferro Corporation Litigation

Nothing new to report.

United Rentals Inc. Securities Class Action Litigation

Nothing new to report.

Boston Scientific Corporation Litigation

Ms. Billings stated that lead plaintiff status was awarded to the State of Mississippi Retirement System on the basis that they had incurred greater losses. Ms. Billings commented that this is the first securities litigation for their counsel.

**Re: Union Representatitves - None**

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**NEW BUSINESS**

**Re: Software Update for IRS Minimum Distribution Rules**

Ms. Zimmermann requested that the Board approve the expenditure to update the pension administration software in order to comply with IRS minimum distribution rules that could limit the joint and survivor percentage payable to non-spouse beneficiaries. She explained that the current software being used in the Retirement Office has not been updated to incorporate the IRS changes. She requested that the Board approve Choice B at \$4,500 from the GRS proposal which would be split between the two pension funds in the usual proportion.

**Resolution 06-023** By Hannan, Supported by Lee

Resolved, that the Board of Trustees approve the purchase of an upgrade to the pension administration software at a cost of \$4,500 with the cost to be shared with GERS in the usual proportion.

Yeas: 4 – Nays: 0

**Re: GASB 40 Reporting Capability**

Ms. Zimmermann requested that the Board approve the expenditure to acquire the GASB 40 reporting capability through the custodian bank Mellon Trust at a cost of \$6,000. She explained that there is a charge to access analytics for GASB 40 reporting. She said that GASB 40 requires detailed reporting on the quality of securities within the portfolio. Without access to this program each individual manager would have to be contacted and interviewed at the end of the year in order to provide information to maintain an unqualified opinion on the financial statements. She told the Board that the expenditure would be allocated between the two pension funds in the usual proportion.

**Resolution 06-024** By Hannan, Supported by Miller

Resolved, that the Board of Trustees approve the purchase of the GASB 40 Reporting Module at a cost of \$6,000 to be shared with GERS in the usual proportion.

Yeas: 4 – Nays: 0

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**UNFINISHED BUSINESS**

**Re: Ordinance Clean up - Tabled**

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**SCHEDULING OF NEXT MEETING** – Regular Meeting April 27, 2006 at 9:00 a.m. in the Shrine Room at City Hall

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**ADJOURNMENT**

**RESOLUTION 06-025** By Lee, Supported by Hannan  
Resolved, That the meeting be adjourned at 10:30 a.m.

Yeas: 4 – Nays: 0

I certify that the foregoing are the true and correct minutes of the meeting of the Police and Fire Retirement System held on March 30, 2006.

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J. Edward Hannan, Secretary  
*As recorded by Jane Arndt*