

**CITY OF PONTIAC, MICHIGAN
POLICE AND FIRE RETIREE PREFUNDED
GROUP HEALTH & INSURANCE PLAN
“VEBA MINUTES”
AUGUST 23, 2012**

Trustees Present

Lon Britton
Leon Jukowski, Mayor
John Naglick, Secretary
Craig Storum

Trustees Absent

Matthew Nye, Chairman (*excused*)

Others Present

Denise Jones, Rodwan Consulting
Chris Kuhn, Gray & Company
Laurance Gray, Gray & Company
Matthew Henzi, Sullivan, Ward, Asher & Patton
Ellen Zimmermann, Retirement Administrator
Jane Arndt, M-Administrative Assistant
Dustin Blitchok, The Oakland Press (*arr. at 8:55 a.m.*)

The meeting was called to order at 8:49 a.m.

AGENDA CHANGES

CONSENT AGENDA

- A. Approval of Regular Meeting Minutes: July 26, 2012
- B. Approval of Special Meeting Minutes: August 9, 2012
- C. Financial Reports
 - 1. Consolidated Statement of Changes – July, 2012
 - 2. Accounts Payable:
 - a. Bradford Marzec \$7,357.52
 - b. Comerica 4,043.94
 - c. Gray & Company 1,250.00
 - d. Rhumblin 4,375.00
- C. Correspondence:
 - 1. Correspondence from Bradford & Marzec Re: Investment Outlook & Portfolio Summary 05/13/12
 - 2. Correspondence from Rhumblin Re: Monthly Performance Report from July 2012
 - 3. Correspondence from Pluscios Re: Unaudited Account Statement – June 2012

RESOLUTION 12-035 By Storum, Supported by Naglick
Resolved, That consent agenda for August 23, 2012 be approved.

Yeas: 4 – Nays: 0

TRUSTEE/COMMITTEE STAFF REPORTS

Trustee Storum indicated that the Board may need to change the dates of the meeting in the future to accommodate for Chairman Nye’s attendance.

Trustee Britton indicated that he would like to save the personnel committee discussion for the Police & Fire Retirement System meeting.

CONSULTANTS

Re: Gray & Company – Second Quarter 2012 Performance Review

Mr. Kuhn told the Board that the economy showed signs of slowing during the second quarter. David Sowerby monitors the Purchasing Managers' Index (PMI). The index consists of a simple survey sent each month to CFO's. The index provides insight into economic activity, such as changes in orders. When manufacturing is above 50 on the scale the economy is growing and the market is optimistic. When it dips below 50, like it did in June, 2012 for the first time since the Great Depression, business activity is slowing and companies may begin to lay off employees. Normally, when the PMI declines the equity market sells off.

The GDP began sliding back down this quarter at 1% to 2% from 2% to 3% at the beginning of the year. The unemployment rate also began sliding up in May and June. The underemployed and unemployment rate is 14% to 15%. There is not a lot of good news in the economy.

There is a lot of uncertainty due to the recession in Europe. China's economy has slowed from a couple of years ago from 10% down to 7% which has attributed to the slowing global economy.

Inflation indicators were lower at the end of the quarter. Commodity prices were down at -5% for the quarter and -14.3% for the year. Oil and gold were pushing commodities prices higher during the first quarter but are now declining. He explained the composition of the commodities index and that a significant gain in pork bellies cannot offset the rest of the index.

The Fed is keeping rates at zero. There will not be any rate increase for the next couple of years.

The yield curve recorded record lows and was in risk off mode during the second quarter with investors selling off debt. Yields were down 0.5%. Yields have come back up since June 30, 2012 when the 10 year Treasury was at 1.5%.

He indicated that when the market is in risk off mode it hurts equity market performance. The S&P 500 was the best performer with returns of -2.75%. Mid cap was the weakest performer in the group. Normally when large cap is the best performer, mid cap is next and then small cap. The reverse is true when small cap is the best performer. Mid cap performance would be second and then large cap. It is unusual for mid cap to be the worst performer. The markets were more value oriented.

Sector performance was reviewed with most sectors in the red. The defensive oriented sectors outperformed with telecommunications at 14.15%. There was a 21% spread between the best and the worst performer (financials at -6.83%).

Yields fell substantially during the quarter which was good for fixed income. The Barclays Long Government was up 10.32% for the quarter and up 31.41% for the year. Barclays Government return was 2.63%; Barclays Government/Credit was 2.56% and Barclays Credit was 2.46% for the period. A falling yield curve drives fixed income prices up. Barclays Mortgage trailed at 1.08%.

High yield, at 1.83%, did not keep up due to the sell off in the equity market. Spreads widened a little bit which added to the underperformance in high yield.

International equity performance was all red numbers except for a few currencies. Most trailed U.S. performance except for Switzerland and the United Kingdom. The move to treasuries strengthened the dollar. Japan's currency was strong. Europe is continuing to affect the U.S. market and China which continues to see a decline in their economic growth.

The international bond market provided solid gains in countries perceived as safe, such as the United Kingdom, Germany and Japan. Unfortunately, weakening currencies offset the gains for U.S. investors along with the poor performance due to yields widening in problem markets. Investors are waiting on the European Central Bank to refine their bailout program. There has been lots of news but nothing meaningful.

Trustee Britton noted that the Greek Prime Minister has asked for more time.

Mr. Gray stated that Spain and Italy are also asking for more time. The Italian President is waiting to determine if he is going to run again. The German Chancellor does not want to sit around and continue to bail them out. The average person is upset with the politicians. The European Central Bank cannot wait to set their monetary policy.

Mr. Kuhn told that the Board that most people think Greece should not be in the European Union. They could set their own fiscal and monetary policy and inflate their way out of debt. Finland is thinking about exiting the European Union and they are one of the strongest economies.

He indicated that he does not have good news to report for this Fund. This portfolio is more sensitive to the market and was down -3.76% versus the policy index at -2.27%.

It was a difficult quarter for active management. They had a hard time protecting on the downside. It is not uncommon (but disappointing) to be down 10%; then down 5% then up 20% or up 18%. This did not happen in just this Fund but in most funds they work for.

Rhumblin performance for the second quarter was -4.05% versus the S&P Equally Weighted Index at -3.28%.

Small cap equity manager Broadview Advisors' performance for the period was -8.57% versus -4.14% for the benchmark.

Trustee Britton asked if Broadview's fee is 110 basis points.

Mr. Kuhn indicated that Broadview's fee is 80 basis points.

The Dodge & Cox International Fund saw the same under performance at -8.34% versus the benchmark at -7.13%.

Bradford & Marzec was not surprised they under performed at 1.67% versus the benchmark at 2.06%. They moved away from treasuries and longer duration securities so when the rates fell, it hurt their performance. Duration and interest rate sensitivity hurt them. When rates rise it should help their performance.

Hedge fund manager Pluscios reported performance of -1.39% versus -2.25% for the quarter which helped performance somewhat.

Trustee Britton asked how long Broadview has been in the portfolio.

Mr. Kuhn indicated that they have been managing assets for the Fund for less than two years.

Trustee Britton pointed out that they are 330 basis points behind year-to-date and this was a particularly bad quarter being behind 430 basis points. He asked if the manager should be put on watch.

Mr. Kuhn said that their March performance numbers were good, ahead of the benchmark by 2%. This quarter took a toll on their long-term numbers.

Trustee Britton stated that the Board cannot wait too long if they continue to under perform. He recommended that Gray & Company light a fire under them.

Mr. Kuhn noted that they can always be put on watch and taken off if the Board is concerned.

He reviewed the updated market values as of August 17, 2012. The portfolio's asset allocation is close to the target. The assets owed to the other funds totaling \$202,000 was taken from Rhumblin. They will do this at the same time as the transition to LS Investments. The contracts are ready.

Trustee Britton indicated that he would like to see the Fund in the northwest quadrant of the return versus risk chart.

RESOLUTION 12-036 By Storum, Supported by Naglick

Resolved, That the Board accept the Second Quarter 2012 Performance Report as presented.

Yeas: 4 – Nays: 0

Re: Rodwan Consulting – Actuarial Valuation Summary Report as of March 1, 2012.

Ms. Jones stated that the partial termination deferred vested members were not included in the other report. Adding these members changed the valuation of System assets.

The accrued liabilities were revised and computed to be \$74,965,444. Of that amount \$24,767,106 were attributed to the inactive vested members and \$49,198,338 to the other members with no change.

The funding value of assets as of December 31, 2011 was computed to be \$29,667,807 with the market value of assets at \$32,009,536. The funding value as of December 31, 2011 was used for the purpose of the March 1, 2012 valuation.

The computed annual required contribution rate was computed to be \$3,616,743 for fiscal year 2013/2014. They used the thirty-year level dollar amortization which is the maximum permitted for reporting under GASB. There are no longer any active members or a viable funding policy.

Trustee Storum asked if the Fund will be solvent out fifty years.

Ms. Jones stated that thirty years is the maximum amortization period allowed.

Trustee Storum confirmed that the Fund would be solvent indefinitely.

The total insurance claims reported in 2011 were \$3,129,737. The required contribution is roughly \$500,000 more.

The liability shifted for active members shifted to inactive vested members and increased the actuarial accrued liabilities significantly from \$4,934,246 to \$24,767,106. Retirees and beneficiaries liability went from \$58,097,372 the previous year to \$49,198,338. The smoothed valuation assets went from \$34,821,105 net of receivables to \$29,667,807. The decline in premium rates helped the Fund save money. Last year's computed annual required contribution rate was 58.72% of payroll or \$3,915,371.

Trustee Naglick asked about the lawsuits against the City and whether the assets were received and applied to the VEBA would lower the required contributions.

Ms. Jones indicated that receiving the contributions would lower the City's required contributions.

Trustee Britton asked if the \$3.9 million as of June 30, 2012 is the amount that is currently in front of Judge O'Brien.

Ms. Jones stated that the required contributions for 2011/2012 are \$3.473 million, for 2012/2013 they would be \$3.915 million and for 2013/2014 they would be \$4.031 million. These numbers do not reflect the receivables.

Trustee Naglick asked if those funds were received would it decrease the amounts retroactively.

Trustee Britton stated the actuary cannot go back. If the Fund is unsuccessful obtaining the contributions the liability will increase. Judge Bowman has not ruled. The contributions will be an ever-changing number.

Trustee Storum referred to the liability associated with the inactive vested members and how it increased significantly due to the closed System.

Trustee Naglick asked if the 2014 required contributions of \$3.6 million. This report has all the information and the actuary seems comfortable that the information is accurate. If the Fund ever collects on the judgment is the Board comfortable with the number.

Trustee Storum stated that this report indicates that the Fund is now providing benefits for every member throughout their lives versus being solvent for fifty years.

Trustee Naglick stated that the report also uses the current level of benefits with good accurate information. He feels more comfortable taking this information to the Judge/Court.

Ms. Jones stated that the number of contributions included all members who made contributions toward their healthcare. It is a gross number. The amount due from the City is less because the retirees are paying.

Trustee Britton asked if it was the gross number to the City because many retirees are contributing toward their healthcare. He asked if the amounts from the VEBA include those eligible people.

Mr. Henzi indicated that \$59,000.00 is collected from eligible retirees each month. It is a key fact to know when sending the invoice to the City.

Trustee Naglick stated that it is important to know that the information is correct when taking to City Council to put on the tax rolls.

Ms. Jones reviewed the comments. Comment 4 indicated an investment return rate of 7.5% with a decreasing medical inflation rate. Contributions are highly sensitive to these rates. If contributions will not be going into the Fund it may be better to use a lower investment return rate of 5%.

She reviewed the actuarial accrued liabilities using a 5% investment return assumption. The total actuarial accrued liabilities would be \$137.1 million with an unfunded actuarial accrued liability of \$107.5 million. The total computed contributions would be \$7.6 million.

Trustee Storum said this shows that if the City does not make contributions, it more than doubles the contribution requirements. It is not necessarily the best scenario.

Ms. Jones indicated that if the contributions are not going to be funded they could be told to use a 4% to 5% investment return rate.

She reviewed the benefit provisions including the new healthcare premiums effective July 1, 2012. She noted that members who retire after August 22, 1996 are covered by the VEBA Trust.

The actuarial assumptions used for this valuation report were an investment return rate of 7.5% with a medical inflation rate of 10% graded down to 4% in 0.5% increments over a twelve year period. They used the same demographic assumptions that were used for the Pension System.

The actuarial cost method does not come into play because they are now using the real numbers.

Trustee Storum noted that the Medicare Part B Premium no longer applies and was part of the benefit provisions.

Ms. Jones stated that it will not affect the numbers and will be removed from the benefit summary.

As of December 31, 2010 the market value of assets totaled \$32,889,041.

She indicated that the average valuation assets at \$34.5 million were higher than the valuation assets of \$29.6 million.

There were 231 retirees included in the valuation with reported benefits paid of \$3,129,737 in 2011.

The active participant page will be removed next year since there are no active members.

There are now 161 inactive vested members compared to 23 in 2010.

Trustee Naglick confirmed that they will all become retirees at age fifty.

Trustee Britton indicated that inactive vested members are calculated in the report. They are included prior to collecting a benefit so if they cashed out they would no longer be members. The Board is looking at that option due to the partial plan termination. If the number of inactive vested members goes down it would drive down the Fund's liability.

Ms. Jones confirmed that the benefit amount is estimated and if the premiums go down the estimate will go down.

Trustee Britton questioned whether this included the members who can repay contributions.

Trustee Naglick stated that would just affect the pension benefits.

Ms. Zimmermann told the Board that these people are also included in the VEBA valuation. If these members take their contribution incentive that will be offered they would move out of both the Pension System and the VEBA. Both the liabilities could be reduced.

Re: Sullivan, Ward, Asher & Patton

IRS Request for Form 990

Mr. Henzi reported that the issue is still pending and they are waiting for a reply from the IRS.

Request for Reinstatement of Health Insurance Policies

Mr. Henzi reported that the affected married retired members whose insurance coverage was canceled should have seen their health insurance reinstated. The Emergency Manager issued an Executive Order on July 30, 2012 (before Public Act 4 was suspended) indicating that the

premiums for a married couple would be changed to twice the single rate of \$91.00 and this would also apply to dental coverage.

The Emergency Manager agreed to put this in the Executive Order to make sure that, a year from now, his successor would know that is the deal.

Trustee Storum indicated that he is still paying the full premium.

Mr. Henzi indicated that Trustee Storum should be reimbursed.

Trustee Naglick stated that a person was assigned to look at the list and perhaps revise it. If retirees have dependents they would stay on the family plan.

Trustee Storum stated that if there are two people on a policy it would be \$413.00 per month versus \$505.00 per month.

Trustee Naglick indicated that the two-person policy is for a member and their spouse. When there is a child it falls under the family policy. He suggested that Mr. Henzi and Trustee Storum contact Nicole Rockov at Meadowbrook to review the list. When operationalized one member could take the single policy and the other could take the additional person.

Mr. Henzi said that he will get the list and share with the Administrator and the Chairman.

Trustee Britton stated that since the deduction is coming through the Board, the Fund should be able to cut the check for the reimbursement.

Mr. Henzi said that the way the premiums are being funded, the \$59,000 is being isolated by the Retirement Office and they can earn interest for three months then the City gets reimbursed for the gross.

Trustee Naglick asked if all the payment was remitted including the \$59,000.00.

Ms. Zimmermann confirmed that all monies including the \$59,000.00 were reimbursed to the City.

Trustee Britton recommended that the premiums come out of the members' pension checks. Per the HELPS Act the members are allowed up to a \$3,000.00 deduction from their taxes for medical premium payments.

Trustee Storum stated that his spouse is a GERS retiree and their medical premium payments are coming out of her check and so would not be eligible under the HELPS Act.

Mr. Henzi thought that members covered under the VEBA were the primary on the policy and that the premiums should be coming out of that member's pension benefit check.

The Board discussed how the medical premiums could be paid separately similar to COBRA.

LS Investments Contract – Customized Weighted Passive Strategy

Mr. Henzi reported that he reviewed the proposed investment manager contract. He consulted with Kevin Yousif from LS Investments and the contract is ready for execution today. He indicated that it is easier dealing directly with the investment manager.

RESOLUTION 12-037 By Storum, Supported by Naglick

Resolved, That the Board approve the Vice Chairman's signature on the LS Investments contract for their custom equal-weighted passive index strategy.

Yeas: 4 – Nays: 0

RESOLUTION 12-038 By Naglick, Supported by Jukowski

Resolved, That the Board move to closed session to discuss pending litigation.

Yeas: 4 – Nays: 0

The Board moved to closed session at 10:07 a.m.

Ms. Arndt, Ms. Jones, Mr. Gray, Mr. Kuhn and Mr. Blitchok left at 10:07 a.m.

The Board returned from closed session at 10:47 a.m.

Ms. Arndt, Ms. Jones, Mr. Gray, Mr. Kuhn and Mr. Blitchok returned at 10:47 a.m.

RESOLUTION 12-039 By Naglick, Supported by Storum

Resolved, That the Board approve the closed session minutes from July 26, 2012.

Yeas: 4 – Nays: 0

RESOLUTION 12-040 By Jukowski, Supported by Naglick

Resolved, That the Board accept the Actuarial Valuation Report as of March 1, 2012 as presented.

Yeas: 4 – Nays: 0

UNFINISHED BUSINESS

Re: Non Payment of Contributions – Fiscal Year 2011 – Refer to Legal (Closed Session)

Re: Non Payment of Contributions – Fiscal Year 2012 – Refer to Legal (Closed Session)

Re: Contribution Invoices July – December 2011

Trustee Britton recommended that the invoices for contributions include only the new invoices going forward.

RESOLUTION 12-041 By Naglick, Supported by Storum

Resolved, That the Board take the 2012 first quarter reimbursement of contributions off the table.

Yeas: 4 – Nays: 0

Re: Tax Exempt Status – Refer to Legal

Re: Q1 2012 Healthcare Reimbursement Request

Trustee Storum asked if the invoices for the 2012 first and second quarter healthcare reimbursements had been vetted by Ms. Zimmermann. Ms. Zimmermann did vet them for both quarters.

RESOLUTION 12-042 By Naglick, Supported by Jukowski

Resolved, That the Board approves the reimbursement of retiree healthcare coverage for the first quarter of 2012.

Yeas: 4 – Nays: 0

Re: Q2 2012 Healthcare Reimbursement Request

RESOLUTION 12-043 By Naglick, Supported by Jukowski

Resolved, That the Board approves the reimbursement of retiree healthcare coverage for the second quarter of 2012.

Yeas: 4 – Nays: 0

Trustee Naglick stated that the only discussion was whether the Board supported the reimbursement of \$1.1 million to the City. The flash report did not include this reimbursement.

Mr. Kuhn stated that the funds will come from Rhumblin with the balance from Dodge & Cox and Broadview.

Trustee Naglick indicated that he needs the funds by August 31, 2012.

Trustee Storum asked whether Pluscios is currently overfunded.

NEW BUSINESS

Re: Executive Order S-224 (Pre-65 Retirees: Retiree and Spouse Individual Coverage)

Ms. Zimmermann stated that this is for the trustees' information and was not included in the special meeting agenda.

Trustee Britton asked about the specific contents of this Executive Order.

Mr. Henzi stated that Executive Order S-224 eliminated the directive that retirees have to have their medical premium deduction mandatorily taken out of their pension benefit checks.

Trustee Naglick added that it also included language regarding two-person coverage and that two single coverage amounts would be mirrored for members when the amount is less than two-person coverage.

Re: Health Insurance Deductible Transfers

Ms. Zimmermann reported that the deductibles for pre-65 retirees will transfer over to Blue Cross.

Trustee Britton asked why it does not pertain to retirees with Medicare Advantage.

Trustee Naglick indicated that the \$150.00 deductible for the retirees who are on Medicare will not transfer. The government agency, CMS, manages Medicare and based on a Federal regulation they do not allow deductibles to carryover.

Trustee Britton asked if there has been any thought to reimbursing the retirees on Medicare.

Trustee Naglick stated that the question could be raised with Steve Hitchcock the Emergency Manager's legal counsel via Mr. Henzi.

Trustee Britton suggested sending out a letter for members to send in a one-time claim for their deductible.

Trustee Naglick asked if the August, 2012 check deductions went into the VEBA. They will be creating an invoice for the July, 2012 deductions.

Trustee Storum recommended that the Administrator double check to insure that the actives' deductions are going into the VEBA.

Mr. Henzi indicated that Ms. Munson received the deductibles in the System.

SCHEDULING OF NEXT MEETING & ADJOURNMENT

Regular Meeting – September 27, 2012 – City Council Conference Room, Second Level, City Hall @ 8:30 a.m.

There was discussion that going forward that there may be a moving date for the Board meeting to accommodate Chairman Nye's attendance.

Trustee Storum stated that Chairman Nye is working on some issues in order to trade time so he can attend meetings.

ADJOURNMENT

RESOLUTION 12-044 By Jukowski, Supported by Naglick
Further Resolved, That the meeting be adjourned at 10:56 a.m.

Yeas: 4 – Nays: 0

I certify that the foregoing are the true minutes of the
Police & Fire Retirement Pre-funded Group Health and
Insurance Plan “VEBA Trust” on August 23, 2012.

John Naglick, Secretary
As recorded by Jane Arndt