

TUCSON SUPPLEMENTAL RETIREMENT SYSTEM BOARD OF TRUSTEES

Meeting Minutes from Thursday, January 25, 2007, 8:30 a.m., City Hall

Members Present: Brian Bjorndahl, Chairman
John Moore, City Manager's Appointee
Suzanne Machain, Designee for Cindy Bezaruy, Human Resources Director
Scott Douthitt, Finance Director
John O'Hare, Employee Representative
Gage Andrews, Employee Representative
Paul Miner, Retiree Representative

Staff Present: Frank Kern, Board Counsel
Joe Ladenburg, Deputy Finance Director
Robert Leko, Finance Administrator
Allan Bentkowski, Investment Manager
Michael Hermanson, Retirement Manager
Doris Rentschler, Finance Analyst
Claire Beaubien, Administrative Assistant

Guests Present: Jean Wilkins, CTRA Representative
John Behrens, Finance Analyst
Gary Lowe, Co-worker of Tim Coleman
Lynn Jung, Supervisor City Courts
Tim Coleman, Disability Retirement Applicant
Sarah Ketterer, Causeway Capital Management LLC
Eric Crabtree, Causeway Capital Management LLC
Brett Gallagher, Julius Baer Investment Management LLC
Teri Smith, Julius Baer Investment Management LLC

A. Call to order

Chairman Brian Bjorndahl called the meeting to order at 8:30 a.m.

B. Consent Agenda

1. Approval of December 16th, 2006 Board meeting minutes
2. Service & disability retirement facts and figures report - January 2007

Paul Miner **motioned** to approve the consent agenda with corrections. Scott Douthitt provided a **second** to the motion. **Motion passed 7-0.**

C. Applications for Medical Retirement*

1. Sue Reyes (reconsideration)
2. Patricia Duarte
3. Timothy Coleman
4. Beth Paulson
5. Sally Dalton

1. The Board reconsidered Sue Reyes' application for disability retirement. Chairman Bjorndahl observed that Dr. Krasner's report simply reaffirmed his prior report, providing little assistance to board members with their decision on disability retirement. Scott Douthitt **motioned** to deny Ms. Reyes' application for disability retirement, John Moore provided the **second** to that motion. During discussion, John O'Hare commented that Ms. Reyes' attending physician offers an opinion that directly opposes Dr. Krasner's report. John O'Hare asked Ms. Reyes if her doctor might be able to provide the board with a more detailed report, specifying how her illness affects her ability to function in her job. Paul Miner stated that his concerns over the amount of drugs Ms. Reyes needed for daily comfort. Scott Douthitt **withdrew his motion**, to table consideration

of this application so that more details could be requested from Dr. Krasner Dr. Karen Smith (Ms. Reyes' attending physician). John Moore **seconded** the motion. **Motion passed 7-0.**

2. Patricia Duarte's application was then considered; the City's physician, Dr. Krasner, reported that Ms. Duarte's condition was not severe enough to prevent her from performing the basic functions of her position. However, after Doris Rentschler reviewed the restrictions Dr. Krasner recommends to be imposed on Ms. Duarte, Ms. Jung (Ms. Duarte's supervisor) opined that Ms. Duarte would be able to perform her duties. Scott Douthitt **motioned** to deny the disability application for Ms. Duarte. Suzanne Machain **seconded** the motion. **Motion passed 7-0.**
3. Timothy Coleman's application was considered. According to a report written by Dr. Van Doren, Mr. Coleman should not have been assigned to the position he was holding at the time of his leave. City Physician Dr. Krasner reported that Mr. Coleman is able to perform his duties, with some restrictions specified. Mr. Coleman discussed his disappointment with how he had been treated by the City over the past two years. Chairman Bjorndahl empathized with Mr. Coleman's situation and Scott Douthitt **motioned** to approve medical retirement, **seconded** by John O' Hare. **Motion passed 7-0.**

Items 4 and 5 – (not considered): Information regarding Beth Paulson's application and Sally Dalton's application had not been received at the time of the Board meeting.

John O'Hare requested, and staff agreed to implement a more intensive information request from the treating physicians for future disability applications, recommending that the current form documents be revised.

D. Annual Manager Report from Causeway Capital Management

Chairman Bjorndahl welcomed Eric Crabtree and Sarah Ketterer from Causeway Capital Management. Eric thanked the Board for allowing them the opportunity to present the annual review of their performance. He began by introducing his colleague, Sarah Ketterer, CEO and founder of their strategy in the early '90s. Causeway is a value manager in 24 markets using a bottom up philosophy. Causeway looks for the highest quality companies with the best risk adjusted expected returns with an average annual turnover of 30-35% per year. Eric reported that there were no dramatic changes in the past year except for the addition of two new research fundamental analysts. An additional analyst will be added this spring after graduation from business school.

At the end of calendar year 2006, total assets approached \$50 million. Causeway had a dividend yield premium of 2.7% relative to 2.4% for the benchmark. Causeway has 70 holdings which is halfway between the 60-80 range they maintain. Causeway's objective is to find the most undervalued stock without regard to markets, and not to simply have representation in a country. In 2006, the Japanese market was the single worst performer of the developed markets. Because of their poor performance, opportunities exist in Japan for undervalued stocks. Sarah remarked that telecommunications was the single worst performing sector globally; precisely the opportunity that Causeway chose to invest because of several well capitalized, cash-flow generative companies that were being over penalized by the market. Energy was a good performer for Causeway although it was a weak industry globally. Causeway also invested in Diversified Financials in Japan which dragged performance. They believed in this sector because they felt Japan was unlikely to make dramatic reductions to the maximum lending rate. Unfortunately, Japan literally shut down an entire industry which induced the sale of the financials in Japan. One of the most positive holdings Causeway has is Petrochina with an 81% return for the year. This company is one of China's largest onshore exploration and development companies. John O'Hare asked Eric how many clients Causeway had gained or lost over the past year. Eric replied that Causeway manages \$18 billion in the product and the total number of clients gained over the last year was less than a handful because their traditional strategy was closed in 2004. The City of Tucson was one of the last clients allowed into the fund. Over the last two years, Causeway has lost two clients. Gage Andrews asked if currency fluctuation was a factor in their investment strategy. Sarah replied that it is a consideration applied at the stock analysis level. Sarah remarked that currently, the yen is very weak versus the

dollar; and the Euro is very strong versus the dollar. Causeway is not expecting the dollar to rise much during 2007. Chairman Bjorndahl thanked Eric and Sarah for their presentation.

E. Annual Manager Report from Julius Baer

Chairman Bjorndahl welcomed Brett Gallagher and Teri Smith from Julius Baer Investment Management. Teri Smith began the presentation by reminding the Board how Julius Baer manages the portfolio. She stated that they believe a diversified core portfolio, driven by dynamic sector and company fundamental analysis, is the key to delivering consistently superior, risk-adjusted, long-term performance in the international markets. They employ both bottom-up and top-down processes, depending on the sector and industry and whether it is a developed market or an emerging market. She reported that the Board of Directors had recently elected to raise the limits on emerging markets from 25% currently to 35% going forward. The reason: there are many emerging markets moving toward being developed markets. During 2006, the fund posted a 32.07% return versus the benchmark return of 26.34%. Brett stated that the emerging market is the biggest sector of the fund. They believe emerging markets have opportunities for the taking. However, Emerging markets are subject to nationalizations and devaluation that can create a "roller coaster" return pattern. For example, in Thailand, there was a military coup last year resulting in capital controls, regulating how money could be brought into and out of the country, resulting in poor stock market returns. Ecuador is talking about repudiating their debt, Venezuela has called for nationalizing utility companies. All of these events are relatively unpredictable, but ones that Julius Baer anticipates.

Julius Baer focuses on Central and Eastern Europe or the European Union (EU) Zone. The single best investment opportunity of our generation is Toyota; as they attempt to get into the European market. In doing so, they have located a factory in the Czech Republic. Because the Czech Republic is part of the EU, they can send their cars anywhere in Europe without paying duties and tariffs that they would have to pay if they were shipped from Japan or the U.S. and then shipped to Europe. This has created a consumer class in that part of the world which did not exist before. Valuations in Eastern Europe are somewhat lower but the growth rates are much faster. In addition to their volatility, Asian and Latin American markets are not popular because they are export dependent. If there are slowdowns realized in the U.S. consumer spending or the U.K. consumer, a slowdown in China or Latin America will follow. Julius Baer seeks to avoid any country that is consumer dependent, with the exception of India. 2% of the portfolio is invested in India because India has its own dynamic consumer market. In the U.S., approximately 70% of our economy is accounted for by the consumer and consumer spending. The economy in India is approximately 60% dependent on consumer spending. China's economy, on the other hand, is affected about 35% from consumer spending. Western Europe, specifically Italian Banks, present vast opportunities because they are inefficiently run but have rich deposit bases. With better efficiency profits would be much higher. Julius Baer does not heavily invest in Japan, having only 8% of the portfolio as opposed to 25% by the benchmark. The other major country they are underweight in compared to the benchmark is the United Kingdom, with only 10% invested versus 25% by the benchmark.

Allan Bentkowski asked Brett about safeguards they employ to prevent getting into countries that could cause problems. Brett replied that they follow the macroeconomics existing in the country. Gage Andrews asked if Julius Baer takes sector bets. Brett replied that they look company by company from the bottom up to decide if they appear to be taking a prudent risk. For example, they wouldn't want to have 40% in banks because that doesn't meet a prudent risk test. Financials consist of 37% of the portfolios but that measurement also includes investment banks, credit companies and real estate companies. They like the financials because they are easily liquidated. Gage asked what their window was when an emerging market no longer becomes attractive. Brett replied that their first investments in Eastern Europe were bought in 1998. They could have bought the entire banking system in Eastern Europe for about \$20 billion. Today, they would have to spend \$150 billion to purchase the entire banking system in Eastern Europe. The growth rate in Poland or Spain is higher than in Eastern Europe. Chairman Bjorndahl thanked Brett and Teri for their time.

F. Investment Activity / Status Report - Portfolio composition, transactions and individual investments

1. Portfolio composition, transactions and individual investments

Allan Bentkowski reported that the fund hit an all-time high on 1/24/07 of \$661,742,000. All managers and asset classes are at or near their target allocations and within their ranges. Allan reported that the fund had a capital call from LaSalle Real Estate. \$866,462 was transferred from Alliance to LaSalle on 12/1/06. On 1/25/07, \$1,274,208 was transferred from Alliance to LaSalle. As of 1/25/07, \$5.3 million of the \$8.1 million has been funded or about 66% funded. On 12/29/07, \$1.5 million was transferred from Barclays Value to Fund 072. On 1/4/07, \$2.5 million was transferred from Barclays Alpha Tilts to Fund 72 (pension). Both transfers were made to meet the cash liquidity requirements generated by the End of Service Program and to fund the Library Dept. transfers to ASRS. During the current fiscal year, a total of \$12 million has been transferred out of the TSRS fund to the City's internal investment pool account.

G. 401(a) plan participation statistics

Mike Hermanson reported that the first year of enrollment had recently concluded for the 401(a) program. A total of 28 employees elected to participate during the 60-day open enrollment period that ended on December 30, 2006. Of the total participants enrolled, 21 elected bi-weekly deferrals and 25 elected to have terminal pay (vacation and sick leave payouts) deferred into this program.

H. Annual Disability audit report

Mike Hermanson reported the results from the annual disability audit recently completed. Members that have not reached normal retirement (age 62 or 80 points with age) must have an annual income review using their prior year's income tax returns for verification of income sources. Of the 150 disability recipients, four individuals exceeded the 80% average final compensation allowed by the City Code. Mike indicated the member names and the dollar amounts by which each individual should be reduced during 2007, in accordance with the City Code, asking the Board to approve the adjustments recommended. Scott Douthitt **motioned** to approve these recommendations, **seconded** by John Moore. **Motion approved 7-0.**

I. City of Tucson Part-time Librarian Discussion

Mike Hermanson discussed his meeting with Nancy Ledeboer, Jonathan Altman, Pat Corillo and Rob Reff on January 22nd. The subject of this meeting considered pension benefits available to several part-time librarians that have elected a deferred vested benefit and are contemplating a transfer of their TSRS service credits to the Arizona State Retirement System. Several individuals have requested modifications to our part-time calculation rules for the benefit amount because they aren't the same as the ASRS rules. Mike emphasized that it was important for Board members to know that TSRS members with a vested deferred retirement benefit have full control over the decision whether to their transfer service credits to ASRS. It is most important that these members be fully informed of the benefits available from either system, especially in light of the medical benefits available from their service in ASRS and from the possible medical insurance subsidy that could be available from ASRS, but that is not available from TSRS. Mike further advised the board that considering such a change in City Code could create precedence for TSRS to be applied to anyone with a deferred vested benefit.

As a common illustration, a librarian that has worked part time for 30 years with the City of Tucson (20 hours per week) would receive service credit in our system based upon the number of hours for which they received compensation and contributed to our pension plan. In this example, the member would 15 years of service credit available for transfer to ASRS. Under the ASRS system, different rules apply to part-time employees; in certain instances, as little as one hour worked in a month would qualify as a full month of service. Also, the method used by TSRS to calculate average final compensation for pension benefits are different than ASRS. For TSRS, full time pay is average, for ASRS, it is actual pay received. Under normal circumstances, requests for service credit transfers to ASRS are automatic, but Mike advised the Board that all such transfers for vested part-time members have been stopped to allow these members to be fully informed of the effects on their eventual benefits. Individual counseling meetings are being established to explain to members requesting such transfers. Both Mike Hermanson and Rob Reff, the ASRS local representative will be meet to

explain how each individual member benefits could be affected. Following counseling, a part time member desiring to transfer service credits will be asked to sign a memorandum of understanding.

J. GFOA CORBA Committee Report

Mike Hermanson reported that late last year, he had received an appointment to a standing committee with the Government Financial Officers Association – Committee on Retirement Benefits Administration (CORBA). Mike recently returned from Washington, DC from his first committee meeting on January 19th. Members of this committee are asked to write recommended practices for the retirement industry, recommend legislative actions to Congress and act as resources to congressional members on issues dealing with retirement benefits. Mike also distributed an announcement made on the City intranet that TSRS had received GFOA's Excellence in Financial Reporting Award for last years TSRS Comprehensive Annual Financial Report.

K. Study group update on post retirement benefit increase policy

Scott Douthitt reported that the study group requested information from the Actuary and are expect to receive information soon.

L. TSRS Board Member Election Report, welcome to Gage Andrews

Chairman Bjorndahl welcomed Gage Andrews as the newly elected member representative. Mike reported that the election results have been duly filed with the City Clerk's office.

M. Future Agenda Items

Allan reminded the Board that both Hewitt and a JP Morgan fund-of-funds hedge fund manager are expected to attend the 2/27/07 Board meeting. Hewitt would like to discuss LaSalle's Real Estate Fund V opportunity. Fidelity will be attending the 3/22/07 Board meeting.

N. Call to Audience

Chairman Bjorndahl presented retiring Board member Scott Douthitt with a farewell letter from the Board thanking Scott for his many years of service.

O. Adjournment - Scott Douthitt **motioned** to adjourn the meeting. Gage Andrews **seconded** the motion. Meeting adjourned 10:56 a.m.

Approved:

Brian Bjorndahl
Chairman of the Board

Date

Mike Hermanson
Retirement Manager

Date