

**CITY OF PONTIAC, MICHIGAN
POLICE AND FIRE RETIREMENT SYSTEM
AUGUST 26, 2010**

A regular meeting of the Board of Trustees was held on Thursday, August 26, 2010 at the Shrine Room, Main Level, City Hall, Pontiac, Michigan. The meeting was called to order at 9:00 a.m.

TRUSTEES PRESENT

Mayor, Leon Jukowski
Brian Lee, Vice Chairman
Matthew Nye
Craig Storum, Chairman

OTHERS PRESENT

Cynthia Billings, Sullivan, Ward, Asher & Patton, P.C.
Stuart Tompkins, Sullivan, Ward, Asher & Patton, P.C.
Chris Kuhn, Gray & Company
Laurance O. Gray, Gray & Company
Ellen Zimmermann, Retirement Systems Administrator
Jane Arndt, M-Administrative Assistant
Drew Fortney, PFFU Union Representative

CONSENT AGENDA

- A. Minutes of Regular Meeting: July 29, 2010
- B. Communications:
 - 1. Correspondence from Artio Global Re: Q3 CIO Letter
- C. Financial Reports:
 - 1. Financial Reports – July 2010
 - 2. Securities Lending – Not Available
 - 3. Accounts Payable – August 2010
- D. Application for Deferred Retirement
 - 1. Douglas MacQuarrie - PPOA 14 years, 3 months Age 37 (2023)
- F. Final Benefit Calculations
 - 1. John Henson #2511 \$4,635.75
 - 2. David Desrochers #2512 3,476.55
 - 3. Trinidad Martinez #2517 3,855.93
 - 4. James Conn #2519 3,739.15

RESOLUTION 10-049 By Lee, Supported by Jukowski
Resolved, That the consent agenda be approved.

Yeas: 4 - Nays: 0

CONSULTANTS

Re: Sullivan, Ward, Asher & Patton – Joju Rimal Lease

Mr. Tompkins described the situation with the Joju Rimal Lease; as part of the CAPROC settlement, the System acquired an interest in CAP Mortgage. All the other mortgages obtained in the settlement have been taken care of except Joju Rimal.

The building is located at 1685 Baldwin Road in Pontiac, Michigan. The building's tenant, the State of Michigan, had a long-term lease with a sixty day notice of opt out.

The mortgage has come due a couple of times and each time the lease was extended. The mortgage is due September 1, 2010. A letter was sent out the latter part of May and two notices with no response. Upon investigation, it was learned that the State of Michigan has moved out of the building. Joju Rimal has failed to make their August 1, 2010 payment. Ultimately, they will not make the payment due September 1, 2010.

The System has a couple of options including initiating foreclosure proceedings in Oakland County, let the borrower hold onto the building and do nothing, or, sell the building through CB Richard Ellis. He spoke with Mr. Gray who feels that the Fund cannot sit back and do nothing.

There have been two appraisals done on the building with all fees paid for by the borrower. There have been no associated costs with this investment to date.

Mr. Tompkins recommended that a notice for the August 1, 2010 payment be sent out giving seven days notice and send another notice out regarding the mortgage payment due on September 1, 2010 with a seven day notice.

Foreclosure litigation can be initiated. The loan documents allow the Board to appoint a receiver. He also suggested that CB Richard Ellis be the property manager during the litigation.

Judicial foreclosure allows the borrower six months to redeem the property before the Fund acquires the property back. It should be sold if that is the case. The last appraisal said the building is worth \$1.5 million. Based on the settlement the Fund is still owed \$2.2 million.

He told the board that the State of Michigan moved to another property in Pontiac. It was a political move. The Fund now owns this property.

Trustee Jukowski asked who owns the property and if they have any other assets. Mr. Tompkins said that Joju Rimal is a single purpose LLC that was formed for this property. The property was secured at the decreased value.

Mr. Gray agreed that CB Richard Ellis is a good firm but feels the Fund should reach out to a few more firms.

Trustee Jukowski asked how many square feet are in the building. Mr. Tompkins said that it is a Class C building with 225,000 square feet. He discussed the downturn in commercial real estate.

Trustee Nye asked what happens if the Fund sits on the property. Mr. Tompkins said the Fund would be responsible for paying the utilities, taxes and general upkeep of the building.

Trustee Nye asked if there is any other downside. Mr. Tompkins said that in this market there are thousands of these buildings sitting vacant.

Chairman Storum asked if the Board is ready to make a motion to move forward with the foreclosure.

Mr. Tompkins recommended obtaining three more property managers to review per Mr. Gray's suggestion. He will send notices out to effectuate the foreclosure.

RESOLUTION 10-050 By Lee, Supported by Nye
Resolved, That the Board authorize legal counsel to send out notices to JoJu Rimal, LLC initiating foreclosure proceedings.

Yeas: 4 – Nays: 0

Trustee Jukowski & Mr. Tompkins left at 9:13 a.m.

Re: Gray & Company

2nd Quarter Performance Report

Mr. Kuhn said that the performance report normally contains a report on the capital markets. In this performance report they decided to write an educational piece. He described a portfolio management tool called VIX that manages volatility in the equity market.

There is strong negative correlation between the VIX Index and the S&P 500 Index. The VIX will go up when the S&P drops or the market is heading downward. It is difficult to use this tool on a monthly basis.

Chairman Storum asked if the people who are paying attention or using this tool could be driving the market. Mr. Gray said that this tool is typically used by hedge funds.

Mr. Kuhn said that some hedge funds have the VIX Index in their portfolio to help offset losses. They use the VIX Index to reduce their equity exposure. He is not suggesting this as a tool for the System. Pluscios will have this in their portfolio.

There is no clear direction. There are two very deliberate camps: one that feels there will be a double dip recession and the other that says not. He tends to lean toward the negative side.

They are looking at moderate growth in the economy. There are a lot of corporations that are confused and sitting on tons of cash. The stimulus program was designed to stave off a depression and is ready to expire. It will be interesting to see how the world reacts. Mr. Kuhn added that the housing decline will also have an affect on the economy. There are a lot of great mortgage rates.

The Fed funds rate is basically zero to accommodate future growth. They do not expect rates to go up anytime soon.

The whole world experienced a flight to quality gobbling up treasury bonds. It is a nice endorsement of the U.S. dollar / Treasury.

On the equity side everything was negative for the quarter. Globally, performance had done well prior to this quarter providing decent returns. However, there was a pull back this quarter. Performance for this quarter was -11.4% for the S&P 500; -9.9% for the Russell 2000; -14.8% for the MSCI EAFE and -8.4% for the MSCI Emerging Markets. There was nowhere to hide regardless of cap size or sector during this period.

Mr. Kuhn said that the three-year number for financials was down 25% which is an annualized number, not the cumulative. There was a lot of value lost that will never come back.

Mr. Gray told the Board that performance expectations in fixed income declined during the quarter. There is a lot of money flowing into long-term government bonds with performance for the quarter at 11.48%. High yield has a high correlation to the equity markets. Performance for the quarter was -0.11% with one-year returns at 26.77%.

Mr. Kuhn explained the terms “risk on” and “risk off”. In March, 2009 the market flipped to the riskiest investments, which is risk on: during the second quarter of 2010 it went back to risk off. Even secure companies are being punished.

Mr. Gray said that with this severe market sentiment the Board needs to understand their manager performance relative to the index.

Chairman Storum asked about using conservative managers versus ones that take more risk. He said this pertains to the small/smud cap manager presentations they are going to hear this afternoon.

Mr. Gray said there can be an impact on the portfolio with risk adverse securities.

The PIG (Portugal, Italy and Greece) countries caused a lot of global economic duress during the second quarter. Germany has been affected as well. Germany has been making a lot of money from auto sales; China is buying a lot of Mercedes and BMW's. However, the Chinese government's attempt to slow economic growth from the low double digits to the high single digits could have an impact on Germany.

Mr. Gray told the Board that Bob Hubbard prepares the Selected Index Returns Report. Over the last decade the stock market performance has been flat. A lot of attention is being paid to risk modeling. Statistically this performance is not supposed to happen. There are reasons why some things get too expensive.

The Fund's portfolio is pretty straightforward. Net of fees the one-year returns at 11.49% are in line with the benchmark at 12.14%. The Total Fund performance net of fees for the quarter was

-4.95% versus -4.88% which was pretty close to the benchmark. Ten-year returns are 3.53% versus 3.78%. The Total Fund standard deviation is slightly less than the policy index.

The domestic equity composite returns for the quarter were -10.28% versus -10.34%; year-to-date returns at -4.83% versus -4.96% and one-year returns at 17.66% versus 17.31%.

In large cap there was a Northern Trust tracking error that is associated with the securities lending program.

Munder Capital's performance for the quarter beat the benchmark. Munder ranked in the 36th percentile with returns of -7.38% versus -9.59% for the quarter. Year-to-date returns were -0.83% versus -1.36%.

Loomis Sayles is a conservative manager. Their performance for the quarter was -9.43% net of fees versus the benchmark at -10.59% and their one-year returns were 18.52% versus 25.08%. They ranked in the 35th percentile versus their peers and were up 134 basis points for the quarter. They did not perform as well as the benchmark for the year due to the "flood to crud". Conservative managers will not buy low quality.

International managers did slightly better than the composite. Richard Hirayama at Wentworth is still healthy. He has talked about training other individuals to take over. Mr. Gray spoke with Miriam Ballert recently and she told him if something happens to Mr. Hirayama the Fund should pull back their investment. Their quarterly returns were -14.26% net of fees versus the benchmark at -13.97% and year-to-date at -11.04% versus -13.23%.

Thornburg is the new comer and has done very well with quarterly returns of -9.18% versus the benchmark at -13.97%. Year-to-date returns are -7.48% versus -13.23%.

The fixed income portfolio with Allianz, Artio, Goode and Northern Trust has returned good numbers. Allianz is now TCP Global which was transitioned at the end of June.

The real estate portfolio one-year numbers are all negative except for Mesirow. There are some great opportunities and the Board needs to be patient and let these investments work their way through.

Chairman Storum asked if Mesirow's one-year performance number was due to a sale. Mr. Kuhn indicated that at the MAPERS Conference he pointed out that they missed a cash flow number for Mesirow. Since inception their performance is negative.

Chairman Storum asked if it was due to a property sale. Mr. Kuhn said that they made a distribution. There was some appreciation in their portfolio in December, 2009.

Chairman Storum recalled that Joshua Daitch from Mesirow made a comment that their performance would be positive if it was not for the management fees. Mr. Kuhn said that he said that the fees were killing their performance.

Chairman Storum asked whether the line Total Fund excluding CAPROC should be removed from the Executive Summary Table.

Trustee Nye asked how much was written off. Mr. Kuhn stated that \$2.5 million was written off.

There was discussion regarding the Joju Rimal mortgage and how much money the System will be out. Mr. Gray said that Ms. Munson could provide the Board a rolling number.

Chairman Storum said that if the building was appraised at \$1.5 million and they sell it for \$400,000.00 the Fund will lose over \$1 million. He would be curious to see the write-off.

Trustee Nye asked where the mortgage is recorded in the report. Mr. Kuhn said that it is not in the report. It is under an unmanaged account.

Ms. Zimmermann said that the original note was at 9.125% and was re-negotiated one time. They paid an additional \$100,000.00 at the time of the extension.

Mr. Gray said it will be choppy for the rest of the year but should not be a severe downturn.

Mr. Kuhn told the Board to anticipate a move back to a more fundamental market going forward. Investors will be willing to pay more for good companies.

Fund of Fund Real Estate

Mr. Kuhn said that the System should be looking for a fund of funds real estate manager that can be paired with Mesirow and Metropolitan. Both of these managers are out raising new funds. The basket clause is full so he wants to make sure this investment is classified as real estate.

He distributed the most recent market valuations as of August 25, 2010. The increase in the cash account was to cover benefit payments including COLA payments. He reviewed the target allocation additions and reductions.

Their recommendation is to continue adding to the American Realty investment and the funding of Metropolitan and Mesirow.

Meeting Break at 9:58 a.m.

Meeting Resumed at 10:06 a.m.

Mr. Kuhn said that it is difficult to compare fund of fund real estate investments because they all have different strategies and starting dates or vintage years. They asked all the managers for a summary of their prior fund's performance and Morgan Stanley would not submit. There is a new team at Morgan Stanley and they do not want to have a performance track record with this group.

When looking at real estate fund of funds strategies, they are less quantitative and performance is less important. It is easy to plow through numbers with a small cap mandate. The professionals

and the stability of the firm are more important in this mandate. We are looking for a fund of fund with niche managers having similar strategies to Metropolitan and Mesirow.

Metropolitan Real Estate Advisors was held over from a prior search. The Board is familiar with Jet Taylor and his team from New York. Their portfolio is constructed with 25% domestic distressed and 75% in value added real estate managers. In this market they are buying mortgages from banks for cents on the dollar, which are the types of situations you want your manager to take advantage of in a distressed market.

Morgan Stanley is part of the old Weyerhaeuser team. Their performance for pension funds has been one of the best in real estate and private equity. They have a new person on the team that came from GM Asset Management. They are a global manager but also a smaller niche manager. Some of their investments include international holdings in German office space and industrial space in the U.S. Southwest. Since there is less leverage, they are sticking to large major markets outside of New York City like Charlotte, North Carolina and international markets like Tokyo and Hong Kong.

Penn Square has a partnership with The Townsend Group which is a premier U.S. real estate manager. This gives them access to The Townsend Group's best ideas. Most of Townsend's clients have \$100 million real estate portfolios.

Portfolio Advisors is a global firm that specializes in the alternative space in private real estate and private equity. They provide a lot of back office support with an incredible database of managers.

Mr. Kuhn provided a comparison of the firms. All the firms are SEC registered. Penn Square does not have their own investment professionals: they use The Townsend Group's.

Trustee Lee asked if it is a negative that Metropolitan is the only firm that has a domestic mandate. Mr. Kuhn said that it is not necessarily a negative, pointing out that Metropolitan has a distressed sleeve.

Ms. Billings asked if the vintage year exposure makes a difference indicating that Metropolitan vintage year exposure is 2009 through 2011. Mr. Kuhn said that the System wants to get in now so they can take advantage of the next couple of years. The managers are all selected for Metropolitan but they have not begun their capital calls. The U.S. exposure for Metropolitan is all diversified. They can dip down into resale and land.

Chairman Storum asked if there are any timber investments in these portfolios. Mr. Kuhn said that there are no timber investments. The return expectations for these managers are in the high teens but the offering documents indicate that they are shooting for the low teens. They are all targeting median size funds with no \$10 billion funds. Metropolitan is targeting capital commitments of \$300 million. They like to work with smaller operators versus managers to save a layer of fees.

Portfolio Advisors has a waiver giving them the cheapest fees of the managers. He explained that their performance fee is lower and they have a lower preferred return.

He explained that a performance fee is paid when the investment reaches its preferred return. If there are losses the performance fee will not be assessed until the investment recoups the loss and reaches the preferred return.

Trustee Lee asked if there is any chance to negotiate the fee. Mr. Kuhn said that these funds are structured as LP's and there is no negotiation. He asked that the Board have Ms. Billings review the contracts to make sure that all the investments are qualified under real estate versus because there is no room left in the basket clause.

Trustee Lee asked if the allocation would be 1%. Mr. Kuhn said that currently 4.4% is allocated to Metropolitan and Mesirow. He would suggest staying on the conservative side with an investment of \$2 million to \$3 million.

Chairman Storum recommended that the Board move forward after Ms. Billings' review.

Mr. Kuhn said that they have a lot of confidence in these managers. There is some difference in fees. The fee matrix was a bit difficult to interpret. He will confirm the fee structure based on Gray & Company's matrix.

Trustee Nye asked if the fees really matter. Mr. Kuhn said that the Board needs to determine whether the fee is worth the reward.

REPORTS

Re: Chairman – None

Re: Secretary - None

Re: Trustees - None

Re: Administrator

Mr. Gray left at 10:37 a.m

Capital Calls

Ms. Zimmermann distributed documents containing capital call requests from Mesirow MFIRE and Metropolitan Real Estate. She asked that the Board ratify the capital calls.

RESOLUTION 10-051 By Nye, Supported by Lee
Resolved, That the Board ratify the Mesirow MFIRE capital call for \$150,000.00 and the Metropolitan Real Estate capital call for \$286,000.00 from the investment earnings of the fund.

Yeas: 3 – Nays: 0

Transfer Schedule

Ms. Zimmermann described the transfer schedule with monies due to the System from the City and monies due to the City from the System. The Board transfers money back and forth with the City. The City owes the Police & Fire Retirement System \$424,410.40 in Medicare Reimbursement and the System owes the City \$224,525.16 to Fund 733 for two years of administrative expenses. As of June 30, 2010 the System owes the City \$185,105.98 after the charges offset.

She explained that the Mayor is not adverse to the Retirement System processing their payroll. Currently, the total owed the City in Fund 733 for Administrative Charges is \$748,417.21 for both retirement systems. The net owed the City after costs for both Retirement Systems are offset is \$137,757.15. She reviewed the various costs for Medicare, medical, dental, life and optical insurance premiums and the additions and deductions from retiree pension benefit checks to cover or be reimbursed for these costs.

There was a discussion regarding the reimbursement of Medicare premiums to retirees. This amount is reimbursed to the retirees in their pension benefit checks and is reimbursed back to the Systems by the City.

Chairman Storum felt that the System has leverage with the City using the current reimbursement process.

Mr. Gray returned at 10:49 a.m.

Trustee Reimbursement Policy Revision

Ms. Zimmermann indicated that she would like the Board to update the Trustee Reimbursement Policy to include a resolution for mileage reimbursement as an acceptable expense when traveling to and from the monthly meeting.

RESOLUTION 10-052 By Nye, Supported by Lee

Resolved, That the Board approve the revision to the Trustee Reimbursement Policy for mileage reimbursement to and from the monthly Board meeting.

Yeas: 3 – Nays: 0

Acting Finance Director Appointment

Ms. Zimmermann informed the Board that the Emergency Financial Manager has appointed temporary employee John Naglick as the Acting Finance Director for sixty days in accordance with his Executive Order.

Deborah Munson – CFA Exam

Ms. Zimmermann told the Board that Ms. Munson passed her CFA Level 1 Exam. This year only 42% of those taking the test passed. Ms. Munson requested that the Fund pay for her Level 2 Exam.

RESOLUTION 10-053 By Lee, Supported by Nye

Resolved, That the Board approve the cost for Accountant, Deborah Munson to take the CFA Level 2 Exam.

Yeas: 3 – Nays: 0

HELPS Act

Ms. Zimmermann said that she is waiting for the opinion regarding pre-tax deductions for retirees. The HELPS Act is part of the federal Pension Protection Act of 2006 which allows eligible retired public safety officers the option of excluding up to \$3,000 to be deducted from their retirement benefit for qualified health insurance premiums and long-term healthcare. The deductions must be a direct trustee-to-insurance-provider transfer.

There was discussion whether this disbursement is tax exempt. Ms. Billings said that as a public safety officer retirees are eligible for a tax deduction and is excludable on their tax return at the end of the year. The deduction from their monthly pension benefit is not tax exempt.

Chairman Storum said that the City agreed that it was a pre-tax deduction. Ms. Billings said that according to IRC 402 the pension disbursement is taxable. The City cannot negotiate a benefit that would be in direct violation of the tax code.

PFFU Early Out Provision

Chairman Storum said that Trustee Nye asked about whether the number of firefighters taking the extended early out provision would affect the actuarial valuation of the System. Ms. Zimmermann said that the original study included up to fifty firefighters. She felt that as long as the number does not exceed fifty members the valuation will not change.

Trustee Nye said that the City and the Union are holding a meeting today to sign this provision into the contract.

Re: Legal

Northern Trust

Ms. Billings reported that they joined the lawsuit with BLBG in Chicago. They filed a complaint with the Court and are waiting for Northern Trust's reply which is due the second week of September.

Almost Family, Inc. Securities Litigation

Ms. Billings reported that the System's application for lead plaintiff status is pending.

Fossil, Inc.

Ms. Billings reported that under advisement of the Court, limited discovery is proceeding.

UBS/AG Securities Class Action

Ms. Billings reported that the hearing on the Defendants' Motion to Dismiss has not been set. They will continue to advise the Board with respect to this matter.

Airgas Securities Litigation

Ms. Billings reported that Ms. Zimmermann went through a seven-hour deposition on July 27, 2010. They will continue to update the Board with respect to this matter.

IRS Application for Determination Letter

Ms. Billings reported that the matter is currently pending with the Internal Revenue Service.

Correspondence to EFM Regarding Benefit Calculations

Ms. Billings was directed to send another letter to the EFM regarding final payouts for PFFU retirees as the Board felt the response from Larry Marshall was not adequate.

JOJU-RIMAL, L.L.C. – Refer to Consultants

FOIA Request from Financial Investment News

For the Trustees Information

TCP Global Investment Advisory Agreement

Ms. Billings reported that the advisory agreement contained the wrong fee schedule. She just received the revised signed copy.

RMK Update

Ms. Billings reviewed the changes to the RMK Contract. There were no controversial changes.

She described the various changes. They added two unit holdings Class A and B. They cut a discount with large investors. Class A management fees are 1.25% and Class B fees are 1.15%.

The three largest unit holders will control the list of independent appraisers and will approve the manager's incentive fee.

An annual audited report and unaudited quarterly reports will be provided starting December 31, 2010.

The initial closing date of the fund was changed to June 30, 2011.

She explained a disclaimer stating that unit holders may have tax liability on the undistributed income and gains based on where the tax domicile is located.

A Side Agreement was negotiated reducing gross negligence to negligence.

The governing law is under Luxemburg Law.

The previously agreed to honor the initial Side Agreement which included most favored nations, adherence to Michigan FOIA Laws and Michigan Anti-Discrimination Laws and to recognize

themselves as an investment fiduciary. She has requested confirmation that the side agreement will still be adopted.

Ms. Billings asked that the Board approve the documents as amended provided the side agreement is adopted.

RESOLUTION 10-054 By Nye, Supported by Lee

Resolved, That the Board approve the documents as amended in the RMK Timberland Contract provided the original side agreement is adopted.

Yeas: 3 – Nays: 0

Social Security Number Privacy Issues

Ms. Billings said that Human Resources requested social security numbers for retirees receiving healthcare benefits. She reviewed the Social Security Privacy Act and determined that the information can be made available for health care administration.

Motley Rice Portfolio Monitoring Report for the Second Quarter 2010

For the Trustees Information

Bernstein Litowitz Portfolio Monitoring Report for the Second Quarter 2010

For the Trustees Information

Miscellaneous Articles

- Robbins Geller Corporate Governance Bulletin, Third Quarter 2010 – The Importance of Alert and Active Institutional Investors

Loretta Herring Meeting

Ms. Billings told the Board that she was asked to meet with Loretta Herring. She described the issue regarding the Charles Herring pension benefit. He was a deferred vested member who passed away before he began to collect his pension benefit.

It was first determined that Ms. Herring was entitled to the annuity withdrawal and received the annuity withdrawal payout. It was later determined that she was, in fact, entitled to her husband's pension benefit. As a result, the Board asked that the annuity withdrawal be reimbursed to the System as she was not entitled to receive it pursuant to the terms of the Ordinance. Ms. Herring questioned that there was nothing in writing stating that she was not entitled to the annuity withdrawal payout.

Ms. Billings said that the Retirement Ordinance is not silent on this issue. A member may elect an annuity withdrawal with no pension or take the annuity withdrawal with a reduced pension rate. She cannot speak for the Board. Ms. Herring may file an appeal.

Chairman Storum requested that in the future Ms. Billings bring this type of issue to the Board. This should come to the Board not around the Board.

Re: Union Representatives - None

NEW BUSINESS

UNFINISHED BUSINESS

Re: Budget Fiscal Year 2010 – 2011 – Remove from Agenda

Re: HELPS Letter to Retirees – Refer to Administrator

Re: Disaster Recovery Plan/Actuarial Software Search – Carry Forward

Ms. Zimmermann stated that this is an ongoing process. She has included a report put together by a University of Florida student on pension software programs being considered by various pension systems. This gives us a general idea of what other pension systems are doing.

Chairman Storum asked if Ms. Zimmermann has had time to put together multiple bids for the disaster recovery plan. Ms. Zimmermann explained that she has not had time to work on the disaster recovery plan based on pertinent issues in the Retirement Office including rebalancing the portfolio.

SCHEDULING OF NEXT MEETING

Regular Meeting –Thursday, September 23, 2010 – Shrine Room, Main Level, City Hall @ 9:00 am

ADJOURNMENT

RESOLUTION 10-055 By Nye, Supported by Jukowski
Resolved, That the meeting be adjourned at 11:24 a.m.

Yeas: 3 – 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 August 26, 2010.

As recorded by Jane Arndt