MINUTES
PENSION TRUST COMMISSION
2ND FLOOR CONFERENCE ROOM
NEW CITY HALL
JULY 28, 2016 – 9:00 A.M.

Bart Hadley, called the meeting to order at 9:00 a.m. in the New City Hall 2nd Floor Conference Room. Notice of meeting and agenda was posted on the City Hall notice board as required by law.

ROLL CALL

PRESENT: Bayones, Teri; Dentler, Carl; Ellwanger, Paul; Hadley, Bart; Hill, Andy; Livingston, Steve.

ABSENT: Kindt, Bill.

ALSO PRESENT: Tim Wilson, City Attorney's Office; Denise Ezell, City Clerk's Office; J.I. Johnson and Krystal Urbanski, Financial Services; Perry Warren, Morgan Stanley,

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II. Introduction of Visitors

III. Approval of Minutes from April 28, 2016 and June 2, 2016.

Motion by Hill, **Second** by Dentler, to approve the minutes of April 28, 2016 and June 2, 2016. **Aye**: Dentler; Ellwanger; Hadley; Hill; Livingston; Bayones. **Nay**: None. **Motion Passed**.

IV. New Business

A. Receive Quarterly Employees Refunds Made From Retirement System and Receive Quarterly Statement of Receipts and Disbursement and take action if necessary – Krystal Urbanski, Finance.

Urbanski stated starting with the balance sheet the cash in and money market funds $1,097,387.75, investment U.S. government obligation $1,968,894.85, mutual funds $33,149,319.79, stocks $10,823,526.80, judgments $1,556,524.04 and interest and account receivables $138,577.75 which brings our total assets to $48,734,230.98. Our total liabilities $173,805.96 and total liabilities and equity $48,734,230.98. On the revenue the city contributions $577,002.32, employees contributions $363,514.54, miscellaneous revenue $150, realized gain/loss on Morgan Stanley $(221,614.30), dividends on Morgan Stanley $145,211.55, unrealized gain/loss on Morgan Stanley $944,438.39, interest $76,756.19 for a total revenue of $1,935,458.69 and year to date total revenue $2,819,019.71. Our expenditures were benefits of participants $1,055,712.37, refunds $204,077.70, other $1,052.33, investments fees $66,632.86, audit fees $3,776, bank charges $152.84 and total expenditures $1,331,403.10. This was a net increase/decrease of $604,055.59. Our fund balance as of June 30, 2016 was $48,555,351.12. The last page shows your refunds.

Hadley asked is it typical to have more earnings in the 4th quarter or did we do that much better this quarter. Two-thirds of our entire years earning was in the 4th quarter.

Urbanski stated we had a big difference in our realized/unrealized gain the previous quarter.

Johnson stated that is correct.

Hadley asked are there any questions. Thank you.

B. Receive quarterly financial report from Morgan Stanley and take action if necessary – Perry Warren, Morgan Stanley.

Warren stated we will begin on page 4. This is your calendar year performance. On June 30th the portfolio was up 1.53%. We are currently lagging in our index and that is due to our stance on interest rates. We believe all we will make on bonds over time is 2.5%. On June 30th the 10 year treasury fell to 1.488% and that is down from 2.269% on December 15th. From December 31st to June 30th interest rates fell from 2.2% to 1.48%. We are position for rates to stay the same or go up. Aggregate bonds are up 5.31% year to date. They went up because interest rates fell which will cause us to lag. Our duration is a lot less than the aggregate bond. We feel that interest rates are going to stay the same or go up. Over time we are not going to make 5.31% in bonds. We are 70% stocks and over the last year to date the S&P was up 3.84% as opposed to the aggregate bond being up 5.31%. I believe we are position for the long run to see our performance outperform the index as interest rates remain the same or go up. All this information is from June 30th. If you look at this same information on June 21st the 10 year treasury was at 1.8% and we were ahead.

Warren stated on page 18 you see the volatility we have. During the last few day of June we had the Brexit exit the EU and that is the reason we had a low yield. Everyone was buying our 10 year treasuries because they didn't know what was going to happen with other currencies. As of July 21st you see the portfolio in just 21 days went to 3.8%. Then from 3.8% to 4.06% on July 27th. Instead of the value being $46,438 million the value was $47,991 million. This is a little over $1.5 million in 27 days. It is because interest rates are now 1.5% and if they go back to 1.8% it will be even a bigger impact. This is the volatility that we have all the time.

Warren stated now to page 5. This shows the performance since November 15, 2007 to June 30, 2016. We started with $34,679 million and since then we have pulled down nearly $3.7 million and we made $15,455,905. Since this report the account the account has gained another $1.5 million in value. As of this report the balance was $46,438,020. Which gives us a return of 4.23%, During the last 12 months we have pulled out $1.6 million and we were down in value $915,000 which puts our return at negative 1.88%. That number will be used on the actuarial report.

Warren stated page 8 is the asset scan. You will see this every meeting because it affects us. You see the pie of $47 million that we have. It shows 8.66% in cash. I have about 1% in cash but this report scans through all the mutual funds and they hold cash. We have 69% in equities and this is where we need to be for the long term. Since we bounced back as of June 30th we will be selling stocks as we go higher and it allows us to buy bonds at a lower rate. When our yield on the bond portion goes to 3.5 or 4% then we can get back closer and have more money in bonds. In order to have an attempt to make the actuarial number that is where we need to be. That is why we have this volatility. In the tic-tac-toe boxes you see we had only 4% of our bonds with any extended of duration. The rest are moderate and limited duration. That means our affective duration before our hedge on interest rates is at 3.87 years and aggregate bonds duration is over 5 years. If interest rates rise the portfolio on aggregate bonds will not draw 5%. We are positioned in hedge equity and are more neutral. That is where we want to be. When interest rates fell from 2.25% to 1.48% it negatively impacted our returns. We didn't get the price appreciation that the aggregate bond did. Over time I think things will be better because we already have a good start to this quarter. We are seeing a lot of fluctuation. Page 7 shows you the actual cash we hold in the account. We have $443,682 in cash, $32,930,968 in equities and are yielding 1.2% off the equities, $11,666,229 under fixed income and that is a 2.6% yield. That is how I come up with the 2.5% in bonds and that is what we are currently yielding. To make more or less the price has to move up and down. You have 2 alternatives that pay dividends and between the 2 the rate is 5.8%. We have $1,285,000 which is our hedge with interest rates and it doesn't pay. We benefit from this when rates rise.

Warren stated page 13 is a chart we look at every time. We believe at some point rates won't go lower but will rise and we will be in a good position. That is our stance.

Warren stated on page 14 we definitely see a lot of the volatility. Each year you have a calendar year return and if you look at where we have been you see a lot of volatility. In January it was down 4.78% and in March it was up 4.87%. If we had it all in bonds it would diminish the volatility over time because interest rates move up and down and all you make is the coupon.

Warren stated this is where we are. It is frustrating to me but on the long term I'm convinced we are where we need to be. We just need more time to get there. At the next meeting I would like to give a more detailed report.

Hadley stated that would be good. When do you put this packet together?

Warren stated I put this one together last Friday.

Hadley asked would it be possible to get this to us so that we can place it in the packet for the members to review before the meeting.

Warren stated I can email it to you.

Hadley stated that would be beneficial. Just email it to Ezell.

Warren stated go to page 6. Over the last 5 years the index has averaged 6.96%. The reason we haven't is because we were 35% stock. I don't know if the 6.96% is achievable because rates have fallen over the last 5 years. I believe the number will be lower. That is the reason I feel that where we are allocated going forward we will get closer to the number.

Livingston stated I don't understand the chart on page 17.

Warren stated I'm sorry that is new. This chart shows the Herd Mentality of people and what happens with the market. The average investor gets out when he ought to be getting in or he gets in when he ought to be getting out. I don't think we are anywhere near being overly confident with the market nor have an enthusiasm for the market. If you look at the asset scan we have less than 1% in cash. The managers have 7% waiting for pullback to find a better place to put the money. Lots of people look at the market for just the numbers. The chart on page 16 is pretty telling. We had a bear market for 13 years. You hear people say the Dow Jones is hitting new highs. It is hitting new highs because during those 13 years earnings grew. A lot of investors say when the market is going to drop it's just going to drop. We have had a lot of excuses this year for it to do so. We've also had some corrections that haven't rolled over and died and it probably won't because earnings are pushing the market up. I don't believe anybody believes we are at the enthusiasm stage for the market.

Livingston asked do we not agree with this chart.

Warren stated we are not at the greed and conviction. You can be at that stage for a while and that is why these bull markets run.

Hadley asked are you saying that the bull markets are at the greed and conviction.

Warren stated that is why they persist. When it goes from greed and conviction to indifference that is when it rolls over and people sell out. I would say we were at the enthusiastic stage if the managers that are managing the money had less cash.

Hadley asked is it the fact that they have cash.

Warren stated they are not at the enthusiastic stage where they believe they have to have all their money in the market because it is going higher. If I had dreamed that interest rates would decline from 2.2 to 1.48% I wouldn't have given up that much in the return over the last 6 months. In all the time I've been investing all you make over time is the coupon on your bond portfolio. You will have bull runs where interest rates fall and you have out performance but at the end of the day you just clip your coupon unless you sold your bonds. Over the long term we are going to be in good shape. We will be forced to sell stocks as they rise and add money to our bonds.

Ellwanger asked can you go over the different benchmarks that are listed on page 6 and talk about those in relations to our portfolio.

Warren stated the ERSOCOL is the Employees Retirement System of the City of Lawton. That benchmark is 50/50. It is stocks that are not the S&P. The 50% stocks are 16% Russell 1000 Value, 16% Russell 1000 Growth, 6% MSCI AC World ex US gross, 4%Russell Midcap value, 4% Russell Midcap Growth, 2% Russell 2000 Value, 2% Russell 2000 Growth, 43%

Barclays Aggregate Bond, 5% HFRI Fund Weighted Composite and 2% CITI 90 Day Treasury. The aggregate bond makes 6% because prices went up due to it yielding 2.4%.

Ellwanger asked the benchmark is 50/50 but we are actually at 70/30.

Warren stated yes.

Ellwanger asked is the S&P 500 strictly stocks.

Warren stated yes.

Ellwanger asked what is Barclays.

Warren stated that is the bonds.

Hadley asked are there any other questions of Warren. Thank you.

C. Consider approving payment of an invoice from McAfee & Taft for services rendered to the Pension Trust.

Wilson stated we received this invoice on February 8th. Previously the board authorized Papahronis to do some work on the determination letter for the IRS and whether the sick leave buyback was pensionable. After reviewing the invoice all items except the 1 on May 17, 2016 for $66 are related items. I would ask you to approve the invoice less the $66 billed on May 17, 2016 which the City will pay for.

Motion by Livingston, **Second** by Bayones, to approve payment of an invoice from McAfee & Taft less the work performed on May 17, 2016 in the amount of $66. **Aye**: Ellwanger; Hadley; Hill; Livingston; Bayones; Dentler. **Nay**: None. **Motion Passed**.

Livingston asked have we heard from Dean on the defined contribution plan.

Hadley stated we have received the preliminary report. I spoke with Dean on Monday asking when we will receive the final report. He stated there were some minor changes to be made and they were almost done. I don’t believe any of the changes will affect the data. This Council Committee’s concept was beginning on some date in the future any city employee hired after that date would no longer be a part of this plan. They would have a defined contribution plan. The City would continue to contribute a certain percentage of the new hire wages to this plan and to the defined contribution plan. Currently the City contributes 10%. Generally speaking some of the numbers they were talking about was matching up to 3, then 4, then 5 and ending with 6% for all new employees. They would start out depositing 7% to this plan and then reduce it. There have been several different concepts on how they would implement the defined contribution. It might be a fixed amount or it might go up over time. Dean’s study indicates if the City contributes 7% to this plan it would not negatively impact the plan. In fact over time it might help the plan. The same is true if they choose to contribute 6%. If it drops below 6% it would have a negative effect on the current plan. I'm glad we have this data and I appreciate the board allowing us to have this study done. Without it all we could do is guess.

Wilson stated I know this isn't on the agenda for today but I'm assuming when we receive the final report Dean will present it to the board.

Hadley stated absolutely. I suspect we will be receiving the final report soon.

Wilson stated this Council Committee hasn't met in about a month. When they do I hope it will promote this board to have a meeting and make a recommendation to Council.

Hadley stated I would think we need to. I don't know if this information will have an effect on the committee. I suspect they will take it rather seriously and move forward with a plan to commit an amount that wouldn't negatively affect this plan. I think it would be important for this Authority to make a recommendation to Council whether it is 6 or 7%.

Wilson stated or leave it alone.

Hadley stated this plan is in pretty good shape and with the changes we made to the Tier II we are on track to keep improving as we move forward. We certainly believe as interest rates rise we will start doing better with our investments. I don't think anyone believes that interest rates will stay at 1 or 2% for forever. I believe this Committee is very serious about moving forward with a defined contribution plan to reduce future liability. The reason for a pension plan is for the employees and it helps with recruitment. I'm worried a defined contribution plan doesn't force employees to take care of themselves down the road. If 3% is the mandatory amount of contribution and given the option to increase that amount in the future I believe probably most won't do so and then will have nothing to retire on. That is a policy decision. I believe it would be beneficial for this Authority to make a recommendation to Council. The Committee didn't have a problem with doing the study but they didn't necessarily want to have it done. We needed this information to protect this plan. If we didn't have the study we wouldn't know that the plan needs at least 6% to stay solvent.

Livingston asked is there going to be anything that dovetails these two plans. We know we need 6 to 7% but in the future these numbers are not going to be accurate. Is he going to have anything out there that states what is needed in 10 years? At some point this plan will mature enough that there won't be anybody in it. Does he have charts that show this in his report?

Hadley stated I'm not certain. I think what he is saying is if we go to a defined contribution plan we no longer have those employees contributing to the plan. That will negatively affect the plan but we also have no future liabilities and that will positively affect our plan so it is a balance. We have to make certain this plan stays viable for at least 50 to 60 years at a minimum.

Livingston stated as an actuary he has those numbers.

Wilson stated it might be beneficial to have him at the next meeting or call a special meeting when the report is ready.

Hadley stated we will probably make that happen.

Livingston stated I'm assuming the defined contribution plan will be sold as a money saver. Someone will think they have to contribute for a certain amount of years. I would like to know what that number of years will be. When will the plan reach a point to where they no longer need to contribute? What is a good number, when will the city began to save money and how much will they save. I would like to have a good actuarial number.

Warren asked did this report look at 5, 10 or 20 years if we stayed the course and didn't do the defined contribution. What does it look like if we compared them? When we made the changes to career averaging the benefits were down the road. As employees rolled off and you added new ones it was going to have a big impact down the road. How would this compare to the course we are on. That would be an interesting study.

Hadley stated you have 2 sides to that. Those who are on the career average were a 30 or 40% reduction in benefits. Every year we have employees on career average the liability keeps going down with the same amount going into the pension. Defined contribution reduces liability even more because anyone hired after a day certain this plan has no liability. The key is the funding side and are we going to have enough funding to maintain it for the Tier I and II employees. Having Dean here to discuss some of that would be beneficial. As long as the City commits to contributing at least 6% for all new hires this plan should stay solvent and this number cannot change at any point in the future. Depending on how quickly the Committee is going to act on this we may want to set a special meeting.

Ellwanger asked would any of the members from the Council Committee be invited to listen to Dean.

Hadley stated we can invite them.

Ellwanger stated they need to hear this from him.

Hill stated what I see going forward is Council is thinking a percentage. They want to see how soon they will be at zero. That is what we need to know because as quick as they can get to zero they are not going to want to do 7%. Where is the stopping point?

Hadley stated initially they were looking at immediate saving but now they are not interested in savings from a City's standpoint but the unfunded liability of the pension will continue to decrease and that is the overall benefit to the City and the citizens.

Wilson stated we are getting a little off topic with the open meetings act. This isn't an agenda item. It is more for the comment section of the agenda.

Hadley stated you are correct. We will agenda an item and bring this before you.

V. Old Business

None

VI. Consent Agenda

FOR THE BENEFIT OF THE AUDIENCE, ALL MATTERS LISTED UNDER THE CONSENT AGENDA ARE CONSIDERED TO BE ROUTINE BY THE PENSION COMMISSION AND WILL BE ENACTED BY ONE MOTION. THERE WILL BE NO SEPARATE DISCUSSION OF THESE ITEMS. IF DISCUSSION IS DESIRED, THAT ITEM WILL BE REMOVED FROM THE CONSENT AGENDA PRIOR TO ROLL CALL AND WILL BE CONSIDERED SEPARATELY.

A. Consider Memo of Information regarding the death retiree Duane Brunner.
B. Consider Memo of Information regarding the early retirement of Colette Gilbert.
C. Consider Memo of Information regarding the normal retirement of Sherry Anderson.
D. Consider Memo of Information regarding the death of the spouse of retiree Adron Graves.
E. Consider Memo of Information regarding the early retirement of Carmen Bothell.
F. Consider approval for the paid-in-full judgments to be released from the record.

<u>**Motion** by Bayones, **Second** by Ellwanger</u>, to approve the consent agenda. **Aye**: Hadley; Hill; Livingston; Bayones; Dentler; Ellwanger. **Nay**: None. **Motion Passed**.

VII. Comments

Hadley asked did anyone have anything else to say.

Livingston stated future Council needs guidance on the pension issue because it will become a budgeted issue. It will be knocked around in the budget when things get tough. It becomes easy to shave $100,000 off this and that. If you have a commitment you have something that is agreed upon and this gives you a lot more leverage.

Wilson stated there would have to be a code change to the retirement section stating that any new hire after a certain date will contribute a certain percentage.

Livingston stated code can be changed.

Hadley stated current council can’t bind future council to anything.

Wilson stated that is a good point. In 30 years you will have a whole new city staff on defined contribution and they are going to ask why do we care about the defined benefits guys.

Hill stated somebody mentioned unfunded liability. By law I guess the city has to carry that. Is there a benefit to not showing an unfunded liability?

Livingston stated I don't believe Council pays much attention to the unfunded liability. When selling a bond the bond guys look at it. Budget is the most important document everybody works with.

VIII. Audience Participation

None.

IX. Adjournment

There being no further business the meeting adjourned at 9:58 a.m.

Motion by Ellwanger, **Second** by Livingston, to adjourn. **Aye**: Hadley; Hill; Livingston; Bayones; Dentler; Ellwanger. **Nay**: None. **Motion Passed**.