POLICE & FIRE PENSION INVESTMENT BOARD

November 15, 2012

Summary Minutes

The information in these meeting minutes is intended to assist Police and Fire Pension members in understanding the activities of the Investment Board. The information is not intended to provide investment or financial advice to any individual or organization and should not be relied upon for that purpose. While we attempt to keep the content accurate we cannot guarantee that all information is current, accurate or complete.

Members present: Doug McDaniel - Personnel Director (Board Chairman)
Michael Donnelly – Mayoral Appointment
Mark Westphalen – Mayoral Appointment
Gerry Finnegan – Mayoral Appointment
Russell Fosler – Police Electee (Board Secretary)
Steve Niemeyer – Police Electee
Jeremy Gegg – Fire Electee
Steve Hubka – Finance Director
Guy Pinkman – Fire Electee

Members absent: none

Personnel Dept.
Resource Staff: Paul Lutomski – Police and Fire Pension Officer

Others present: Max Callen – Smith Hayes Financial Services Investment Consultant
Todd Peterson - Smith Hayes Financial Services Investment Consultant
Mark Dolton - Smith Hayes Financial Services Investment Consultant

Doug McDaniel calls the meeting to order at 9 am and requests those having recently attended conferences to brief the board.

Russ Fosler attended the NCPERS conference and briefed the board on conference topics regarding plan administration and investments.

Doug McDaniel calls for a vote to motion to approve the minutes of the August 16, 2012 meeting.

Michael Donnelly makes a motion to approve the minutes.

Russ Fosler seconds the motion.

Motion is approved.

Doug McDaniel asks Smith Hayes to present.

Mark Dolton presents regarding markets sectors returns, potential tax changes, general economic statistics and expectations.

Max Callen reviews portfolio allocations and 3Q2012 quarter , 1 year and 3 year returns.

Recommendation is to continue with plan developed in August:

Sell Hedge Funds and accept proceeds from JPM Alternative Property Fund wind down.

Purchased on Nov 1, 2012:

iShares Midcap Value Index	$1,980,000
Perkins Midcap Value	$1,425,000

To be purchased:

American Funds Capital World G&I	$1,500,000
Mutual Global Discovery	$1,500,000
Nuveen Global Infrastructure	$ 850,000
ING Global real estate	$2,589,000 (from Alt Prop Fund proceeds)
Invesco Balanced-Risk Allocation	$5,180,000 (from hedge Fund proceeds)

Max Callen continues discussion from prior meetings regarding Mr. Westphalen's dividend investment idea.

1. Create a list of domestic stocks that have increased their dividend every year for at least the last 10 years.
2. Enter each stock on that list into Morningstar with a hypothetical $10,000 investment on a recent month end, reinvesting dividends and calculating the value as of that month end date
3. Rank the investments in descending value order and select the top 25 performers.
4. Make a portfolio of these stocks by investing $5 million equally weighted ($200,000 for each stock) by selling assets currently in the sector rotation allocation. Do not rebalance. Hold for 4 years and sell.

Money for this strategy would come from $3.7M sector rotation holdings and the rest from domestic equity large value.

Replicating this strategy and various other similar models; total return, Free cash flow, PE rate, he discusses each and lists alpha, beta, div yield, total return, standard deviation, etc. and the 25 names used.

Smith Hayes would set up a separate account with just these stocks and reinvest the dividends so the account total would be tracked.

Board discusses.

Doug McDaniel asks for a motion.

Mark Westphalen makes a motion to implement the dividend model ranked by free cash flow.

Steve Hubka seconds the motion.

Board discusses. Mike Donnelly makes a friendly amendment to limit investment to the amount in sector rotation. Gerry Finnegan clarifies that the stocks will be equal weighted rather than cap weighted.

Motion with friendly amendment passes.

Todd Peterson reviews Watch List funds. In summary, all funds currently on the Watch List are not a major concern.

The next agenda item is new business.

Paul Lutomski states that representatives from Prudential Real Estate visited yesterday with himself and Russ Fosler. He explained Prisa III is open to new investments for a short time. The pension has $5M in Prisa III and the fund is $1.9B total. He details a favorable Prisa III return expectation, explains why Prudential has the expectation. He explains the pension holds $2.3 M in the JP Morgan Strategic Property Fund which is a core real estate fund and as such is expected to earn less than Prisa III, which is a value added fund. He recommends selling SPF and investing the proceeds in Prisa III or the real estate fund recommended by Smith Hayes. The pension would still own $3.7 M in Rreef, a core fund.

Russ Fosler makes a motion to sell SPF and invest the proceeds in Prisa III.

The board, staff, and Smith Hayes discuss the motion, including return expectations, property location and usage diversification. SPF redemptions are processed quarterly. The SPF proceeds may not arrive before the Prisa III capital call, but the pension could sell a liquid investment and replace the liquid investment with SPF proceeds.

Doug McDaniel ask for a second to continue discussion.

Steve Hubka seconds the motion.

Board discussion. Russ Fosler mentions that Prudential purposefully issued a capital after the real estate market downturn to capitalize on lower prices.

Doug McDaniel calls for a vote.

Motion passes.

Doug McDaniel thanks the members and adjourns the meeting at 10:12 am.

Strategic Property Fund alls the
Max Callen: There are thousands of managers. Some fail and some succeed. You have to pick the right ones. As funds grow they may have to buy more securities becoming more like the market and posting market-like returns.

Gerry Finnegan: A fund family may start with eight funds. At the end of the first year they close four to new investing and keep the best open. At the end of the second year they close two and keep the best open. At the end of the third year they close one and keep the best one open and advertise it's returns and when it becomes available to the public it has a great track record. You have to be wary.

Steve Niemeyer attended the NCPERS conference in New York. Many topics were discussed. The overall feeling was more optimistic this time. Europe is still a big problem and may foreshadow similar US problems. Commodity prices are increasing, housing is leveling, consumer spending is increasing, municipalities are having pension problems. Changing from DC to DB is a topic and most NCPERS members are against it. Our plan is not as generous as most and we are better funded.

Doug McDaniel: We may be better, but we still have concerns.

Steve Niemeyer: Private equity funds were discussed. There are private equity fund of funds so the research and due diligence are done by the organizing partner.

Paul Lutomski attended the Public Funds conference in Newport, RI. Many topics were discussed. 75% was mentioned as the average public DB actuarial funding level. We are at 81% with 72% on a market basis. GASB 25 and 27 were replaced with 67 and 68 accounting display methods. We plan to ask our actuary to display the next report both ways. Investing a little more upbeat with cautious optimism and diversification the key. Emerging and frontier markets were mentioned as having less legacy costs for social programs, but also less technology legacy costs. For example, telephone in the US is landline, and cell with various cell transmission speeds. Rather than invest in and maintain the earlier technology emerging/frontier market companies with can start with the latest technology.

Doug McDaniel calls for discussion on approval of the minutes of the May 8, 2012 meeting.

Paul Lutomski states the department does not have a typist and therefore the meeting minutes will be shorter but still available.

Michael Donnelly notes a spelling error and recommends a disclaimer be added to the minutes.

Russ Fosler moves to approve the May 8, 2012 minutes with the spelling error corrected and disclaimer added. Jeremy Gegg seconds. All member vote in favor except Steve

Niemeyer who abstains because he did not attend that meeting.

Doug McDaniel asks Smith Hayes to present their recommendations.

Max Callen: Explains disclosures. We started a different format in May, market update, performance review, recommendations. 2Q2012 not a good quarter. Best sector was small value down 2%. Growth down more than value. CYTD pretty good. Sectors, best was telecom, worst was financial. PE 12.3 below historical PE of 14. Corporate cash is high in part because of tax and health care uncertainty. Budget deficit needs to be under control. If Bush tax cuts are allowed to expire top wage tax 37% to 43%, cap gains 15% to 23%, about a 50% increase, dividends 15% to 43%, FICA 4.2% back to 6.2%. Going back to those tax level would be a drag on the economy. The top 5% of people earn 31% of the income and pay 69% of taxes. The next 25% earn 34% pay 26% of taxes. The bottom 70% of earners pas 12% of incomes taxes. Not much inflation. Energy has come down. Best earning category was fixed income YTD. 10 year Treasury bond is 1.6%, well below historical averages. Last year we said rates could not go much lower but they did. High yield spreads are wide but defaults are half. HY a good space. Europe has one currency, an economic union, but several governments and that is a problem. Greece's borrowing costs as a percent of GDP are large, that is bad. US is pretty small. Emerging markets have good, low debt to GDP ratios.

Book first tab is allocation Appendix A, min and max percent per category with target allocation and actual allocation and if we are over or under that. The last column is the 2Q21012 return. Next pages are reports for each asset and category for quarter, 1 year and 3 year returns, ending June 30, 2012. 2Q2012 down 3%, 1 year down 3.7%. 3 year up 8.9% annually.

The next tab contains the Smith Hayes recommendations. They are:

1. **Income (Bond Holdings)**
    - Decrease bond holding slightly from prior targeted amount (3%).
    - Replace Calvert Income fund with the Barclay's Aggregate Bond Index.
    - Increase the allocation to the multi-sector bond managers.
2. **Equity Allocations**
    - Remodel the equity allocations to equal weight large cap / mid cap / small cap.
    - Introduce more index funds into the portfolio in most categories.
    - Have one active manager that has historically provided good downside protection and an index in most categories.
    - Reduce allocations to foreign and emerging markets.
    - Add a "total market index" in the sector rotation category.

3. Alternatives

- Replace the hedge fund allocations with the Invesco Risk Balanced portfolio.
- Increase infrastructure allocation slightly.
- Increase real estate allocation by purchasing a global real estate fund.

4. Benchmark Update

Change from current benchmarks to benchmarks that are investible as listed.

If the Smith Hayes recommendations are approved, the target allocations in Investment policy Appendix A would change as follows:

Category		Min %	Max %	Old Target	New Target
Cash		1.0%	3.0%	1.3%	1.0%
Income Investments		**15.0%**	**47.0%**	**26.1%**	**22.1%**
	US Investment Grade	0.0%	30.0%	5.50%	2.21%
	US High Yield	0.0%	15.0%	4.85%	4.42%
	US TIPS	0.0%	30.0%	2.50%	2.21%
	World Bonds	0.0%	20.0%	2.50%	2.21%
	Emerging Market Bonds	0.0%	15.0%	2.50%	1.11%
	US Multisector Bond	0.0%	30.0%	6.50%	8.84%
	Convertible Bonds	0.0%	10.0%	1.75%	1.11%
	Open Category				
Equity		**30.0%**	**70.0%**	**45.55%**	**45.0%**
	US Large Growth	0.0%	17.0%	2.80%	5.40%
	US Large Value	0.0%	17.0%	4.00%	4.05%
	US Mid Cap Growth	0.0%	17.0%	1.80%	4.05%
	US Mid Cap Value	0.0%	17.0%	3.00%	4.05%
	US Small Cap Growth	0.0%	17.0%	1.80%	4.05%
	US Small Cap Value	0.0%	17.0%	3.00%	4.05%
	US Active Sector Rotation	0.0%	17.0%	3.50%	4.50%
	Foreign Developed	0.0%	25.0%	5.80%	2.70%
	Foreign Emerging Mkt	0.0%	15.0%	11.00%	5.40%
	Global	0.0%	10.0%	9.00%	6.75%

	Open Category				
Alternatives		**10.0%**	**35.0%**	**27.00%**	**31.90%**
	Private Equity	0.0%	5.0%	0.40%	0.32%
	Hedge	0.0%	0.0%	5.80%	0.00%
	Natural Resources	0.0%	10.0%	5.40%	4.47%
	Go Anywhere Funds	0.0%	20.0%	4.80%	12.76%
	Infrastructure	0.0%	10.0%	4.20%	6.38%
	Real Estate	0.0%	10.0%	6.40%	7.98%

Max Callen explains for the Income group, the actively managed Calvert Income would be replaced with a US Bond Index and changes made to target allocation percentages per above.

For the Equity group, in each sub-category, about half of the assets would be invested in a passive index, and changes made to target allocation percentages per above.

For the Alternative group, hedge funds would be replaced with the Invesco Risk Balanced Fund and the JP Morgan Alternative Property Fund would be replaced with the ING Global Real Estate Fund and changes made to target allocation percentages per above.

The Board discusses the recommendations with Smith Hayes. Discussion items include how the index funds are weighted relative to the market, the addition of index funds, and delayed transactions.

The proceeds from the JPMorgan Alternative Property Fund, which is currently being closed by JP Morgan, when received, are recommended to be invested in the ING Global Real Estate Fund. The proceeds are expected to total about $2.5 million and be received in the next six months. This fund will provide real estate exposure with liquidity.

Mark Westphalen moves to approve Smith Hayes real estate recommendation. Russ Fosler seconds. All members vote in favor.

Doug McDaniel asks if the Board wants to vote on each recommendation separately, or en-mass.

Gerry Finnegan want to separate changes to the benchmarks from the other recommendations.

Max Callen explains the three Income /Bond Holdings recommendations.

Mike Donnelly moves to accept all three of Smith Hayes' bond recommendations. Motion is seconded. All members vote in favor.

Max Callen explains the Equity recommendations. Some active managers allocations will be reduced and index funds will be added. There is no extensive change in equity allocations, but about half of assets will be moved from active managers to passive indexes. Discussion

that only 2 of the 19 funds on the Watch List will be replaced.

Gerry Finnegan moved to accept the Smith Hayes equity recommendations. Mike Donnelly seconds. All members vote in favor.

Max Callen explains the Alternative Asset recommendations. Real Estate is already done. By replacing the hedge funds with Invecso Risk Balanced we are moving more assets into the Alternative Asset Flexible Mandate, so your Investment Policy will have to be changed because the policy maximum is 10%. The JPMorgan Fund of Hedge Funds has quarterly liquidity. The investment was originally purchased with the intent that value be non-correlated to the equity market. The value of the investment is more correlated to the equity market than originally expected. If the Board approves the proceeds, when received, will be invested in the INVESCO Risk Balanced Fund.

Guy Pinkman moves to accept the remainder of the Smith Hayes Alternative Asset recommendations. The motion is seconded. All members vote in favor.

Max Callen revisits the 4th part of the Smith Hayes recommendation, changing to benchmarks that contain assets that con be invested in, an investible benchmark. It is more meaningful to compare against an investible benchmark so that when comparing active manager returns to benchmark returns the active manager return is not at a disadvantage due purely to the benchmark having no trading costs.

Max continues and recommends changing the benchmarks to investible indexes when possible. The new benchmarks are highlighted.

Asset Class	Benchmark Now	Recommended Investable Benchmark
Cash	91 day Treasury	91 day Treasury
I Income Investments		
US Investment Grade Bonds	Barclays 5-10 Yr Govt/Credit	Barclays Aggregate Bond
US High Yield Bonds	Merrill Lynch US High Yield Master	Merrill Lynch US High Yield Master
US Tips	Barclays US Treasury TIP	Barclays US Treasury TIP
World Bonds	Citi Non USD Gov't Bond	CitiWorldBIG Corporate A
Emerging Market Bonds	Citi ESBI-Cap Brad	BofA Merrill Emerging Market (Sovereign/Corporate)
US Multi-Sector Bond Funds	Barclays US Bond Universe	Barclays US Bond Universe
US Convertible Bonds	Morningstar Convertible	BofA Merrill Convertible (all conv., all quality)
II Equity		
US Large Cap	Russell 1000 Growth	Russell 1000 Growth

Growth		
US Large Cap Value	Russell 1000 Value	Russell 1000 Value
US Mid Cap Growth	Russell MidCap Growth	Russell MidCap Growth
US Mid Cap Value	Russell MidCap Value	Russell MidCap Value
US Small Cap Growth	Russell 2000 Growth	Russell 2000 Growth
US Small Cap Value	Russell 2000 Value	Russell 2000 Value
US Active Model (sector rotation)	S & P 500	S & P 500
Foreign Developed	MSCI EAFE	MSCI EAFE
Foreign Emerging	MSCI Emerging Markets	MSCI Emerging Markets
Global	MSCI World Equity Index	MSCI World Equity Index
III Alternative		
Private Equity	N/A	N/A
Hedge Funds	HFRI Fund of Funds	N/A
Natural Resources	S&P North American Natural Resources	S&P North American Natural Resources
Go Anywhere Do Anything	MSCI World NR USD	MSCI World NR USD
Infrastructure	S&P 500 Utilities	MSCI ACWI Infrastructure
Real Estate	NCREIF Index	Dow Jones US Real Estate

Russ Fosler moves to accept the Smith Hayes benchmark recommendations. Jeremy Gegg seconds the motion. All members vote in favor.

Todd Peterson briefly discusses that there are 19 funds on the Watch List. The large number is due to adoption of Investment Policy Watch List guidelines in the last meeting. There are 2 funds that we had concerns about. The first was Heartland Value Fund with 1, 3, and 5 year bottom quartile returns and will be replaced by an iShares ETF with the approval of the equity recommendation. The other, Calvert Income Fund was replaced by its ETF, the Barclay's Aggregate Bond, with the Income recommendation approval. Others we are following closely include the VanEck Global hard Assets. American Funds Capital World Growth and Income has had 3 of 12 managers replaced. The new people had more emerging markets experience.

Max states that Mark Westphalen proposed a dividend portfolio in the last meeting using funds currently invested in sector rotation. INVESCO sells a similar product as a unit trust. To get an idea of the return from Mark's they looked at an INVESCO product. One year 18%. Three years it returned 17% annually. Five years 8% annually. The three year numbers would not

include 2008.

The next agenda item is to revisit Mr. Westphalen's investment proposal. Paul Lutomski explains the idea to the Board.

5. Create a list of domestic stocks that have increased their dividend every year for at least the last 10 years.
6. Enter each stock on that list into Morningstar with a hypothetical $10,000 investment on a recent monthend, reinvesting dividends and calculating the value as of that monthend date
7. Rank the investments in descending value order and select the top 25 performers.
8. Make a portfolio of these stocks by investing $5 million equally weighted ($200,000 for each stock) by selling assets currently in the sector rotation allocation. Do not rebalance. Hold for 4 years and sell.

Paul Lutomski states that if the Board creates their own criteria they may be open to more fiduciary responsibility than if they approve the purchase of an investment whose selection criteria is developed by an investment manager as the manager is then sharing the fiduciary responsibility.

Max Callen states Smith Hayes will implement the Board's criteria, or will come up with a criteria, for the Board's vote.

Mark Westphalen states the US economy may be flat for the next 4-5 years and if so he would like to invest in companies that have a proven record of dividend payment for a long period of time. He does not have the ability to back-test the strategy to see which companies would have made the list and how they would have performed. The Dividend Aristocrat is an index of every company in the S&P 500 that has consistently raised their dividend consistently for the last 25 years. He is not interested in buying that index.

Mark Westphalen makes a motion Smith Hayes investigate the proposal further. Mike Donnelly seconds and adds a friendly amendment to include the Invesco fund in the research. Amendment accepted. All members vote in favor.

Doug McDaniel asks if there is any other business.

Steve Hubka states the City budget set aside $1.4 million less than the actuary recommended. The City Council made a motion and approved it 4 to 3 that if valuations come in above 3.5% any additional amount generated by the existing tax rate go to the Police and Fire Pension Fund.

Paul Lutomski states the fund used to collect Smith Hayes 12B1 rebates and pay travel expenses will be closed and the balance deposited into the pension general fund. Doug McDaniel adds the amount is roughly $400,000 and this change will make the accounting more transparent and the Finance Department agreed.

Jeremy Gegg suggests the next meeting be scheduled for longer than 1.5 hours.

Doug McDaniel apologizes for the rushed meeting, states we will try to do better in matching time allotted and items to discuss.

Meeting adjourned at 10:57 am.