EMPLOYEES' RETIREMENT SYSTEM OF THE COUNTY OF MILWAUKEE

MINUTES OF THE JANUARY 21, 2009 PENSION BOARD MEETING

1. Call to Order

Chairman Dr. Dean Roepke called the meeting to order at 8:40 a.m. in the Green Room of the Marcus Center, 127 East State Street, Milwaukee, Wisconsin 53202.

2. Roll Call

Members Present:
Linda Bedford (Vice Chairman)
Mickey Maier
Jeffrey Mawicke
Marilyn Mayr
Dr. Sarah Peck
Dr. Dean Roepke (Chairman)

Members Excused
Donald Cohen
Roy Felber

Others Present:
David Arena, Director of Employee Benefits, Department of Administrative Services
Gerald Schroeder, ERS Manager
Mark Grady, Principal Assistant Corporation Counsel
Gordon Mueller, Fiscal Officer
Dale Yerkes, Assistant to the Fiscal Officer
Vivian Aikin, ERS Administrative Specialist
Sushil Pillai, V3 Project Manager
John Holland, Business Analyst, ERS
Bess Frank, Ad Hoc Oversight Committee
Steven Huff, Reinhart Boerner Van Deuren s.c.
Leigh Riley, Foley & Lardner LLP
Craig Dean, Loomis & Sayles Company, L.P.
Brian Wrubel, Marquette Associates, Inc.
Brett Christenson, Marquette Associates, Inc.
Ray Caprio, Marquette Associates, Inc.
Frank Vitiello, President, Vitech Systems
Barrett Rodriguez, Vitech Systems
Ken Loeffel, Retiree
Yvonne Mahoney, Retiree
Joe Szarka, Retiree
Marlene Szarka, Retiree
Steve Schultze, Reporter, *Milwaukee Journal Sentinel*

3. Chairman's Report

(a) Election Status

The Chairman stated that there are five ERS members who submitted candidacy materials for the two employee member Pension Board seats up for election in February 2009. He provided the names of each candidate and reviewed the election timeline.

(b) Vitech Go-Live

The Chairman reported that the V-3 System go-live implementation was successful. He noted that the President of Vitech is in attendance at today's Pension Board meeting.

4. Minutes of the December 17, 2008 Pension Board Meeting

The Pension Board reviewed the minutes of the December 17, 2008 Pension Board meeting.

The Pension Board unanimously agreed to approve the minutes of the December 17, 2008 Pension Board meeting. Motion by Mr. Maier, seconded by Ms. Mayr.

5. Reports of Employee Benefits Director, ERS Manager and Fiscal Officer

(a) Retirements Granted

Mr. Schroeder presented the Retirements Granted Report for December 2008. He reported that 11 retirements were granted in December, noting that 4 retirees elected backDROPs in amounts totaling $339,755.

(b) ERS Monthly Activities Report

Mr. Schroder stated that 243 ERS members retired in 2008. He reported that there were 53 fewer retirements in 2008 than in 2007 and that 2008 benefit payments were $7.5 million less than in 2007. He noted that 94% of pensioners are receiving their benefits through direct deposit. He indicated that another batch of letters requesting the use of direct deposit was sent out, and an additional 105 retirees agreed to use direct deposit.

Mr. Schroeder reviewed the Retirement Office's 2008 accomplishments. He stated that all Pension Board meeting minutes dating back to 1938 were copied to an electronic format. He noted that the V-3 System imaging project resulted in 250,000 documents being scanned into electronic format. He pointed out that the imaging project will continue in 2009. He discussed two primary goals: to reduce

the Retirement Office's reliance on paper files and to move the paper files off site. In response to Dr. Peck's question, Mr. Schroeder stated that the most commonly used records are being scanned in for electronic access.

Mr. Schroeder reviewed the progress of the Retirement Office procedures writing project. He reported that the 20 most important procedures have been documented. He noted that the Retirement Office plans to draft an additional 20 to 30 procedures this year. He indicated that brochures on basic topics have been and will continue to be drafted. They are available in the Retirement Office's reception area and will be sent to retirees.

Mr. Schroeder reported that 2008 was a good recruitment year for the Retirement Office. He stated that the educational level of Retirement Office employees was increased with the hiring of several employees with college educations. He noted that the Retirement Office focused on employee training to better serve ERS members. He explained how the Retirement Office re-initiated pre-retirement information sessions and developed a newsletter and telephone hotline for retirees. The Chairman asked Mr. Schroeder or an ERS representative to repeat the Retirement Office's accomplishments at the annual meeting. The Chairman encouraged the Pension Board to review the procedure binders prepared by the Retirement Office to become more familiar with the Retirement Office's operations.

(c) Board Elections – February 2009 – Update and VoteNet Demonstration Link

Mr. Schroeder stated that the Retirement Office has taken a more proactive approach to the upcoming election compared to prior elections. He discussed the election timeline. He indicated that a drawing for ballot positions was held on January 6, 2009. He noted that the January 23, 2009 ERS newsletter will contain pictures and biographies of the five candidates, in addition to other general election information. He stated that the Retirement Office has been sending e-mails describing how to vote and listing the kiosk locations. He pointed out that the Retirement Office expects 40% voter turnout, which would be a large percentage increase from the last election.

Mr. Schroeder presented handouts to the Pension Board showing what the voters will view when voting. He indicated that he provided all of the Pension Board members with a link to access an online voting demonstration.

(d) Cash Flow Report

Mr. Mueller presented the ERS cash flow report. He reported that the projected cash needs for the first quarter of 2009 remain the same. He reviewed the cash needs, noting that the $10 million needed for January benefit payments is coming

from Mellon Capital Management. He indicated that he still expects ERS to need $5 million for benefit payments in both February and March.

Mr. Mueller stated that he received an e-mail from the County stating that $4.5 million of the $10 million that ERS's budget had projected would be received from the County in June 2009 will go to the stabilization fund being established for the pension obligation bonds. Mr. Mueller stated that he will follow up on this new clarification. The Chairman asked that Pension Board representatives follow up on this matter.

Mr. Grady reported that the stabilization fund is part of the pension obligation bonds process. He stated that he will look into the matter further and will review resolutions passed by the County Board as part of the County's 2008 budget. Ms. Mayr requested that Mr. Grady and Mr. Mueller look into the legality of what she perceives as the County withholding funds from ERS. Mr. Grady responded that the County Board can reduce its contribution to ERS and amortize the shortfall over five years. He noted that he needs to look at the budget documents to determine what the County agreed to contribute to ERS. He pointed out the County Board has no obligation to contribute funds to ERS in the full amount requested by ERS for that year, as long as the County Board follows the contribution shortfall provisions contained in the Ordinances.

Ms. Bedford pointed out that all the pension obligation bond developments have occurred at the County Board level. She stated that the Pension Board needs to know more about the pension obligation bond process in order to be ready to properly invest ERS's assets when ERS receives the pension obligation bond proceeds. In response to a comment by Ms. Bedford, Mr. Grady stated that the pension obligation bond working group includes Corporation Counsel's office. Mr. Grady indicated that he contacted Marquette Associates, Inc., and consulted with the Chairman, to arrange for consultation by Marquette on how the funds received from the pension obligation bonds should be invested. Mr. Grady commented that the County Board knows that ERS needs to be ready to invest the funds once the bonds are issued.

Ms. Mayr questioned whether such a process is "shortcutting" the Pension Board because the flow of information is not going the way she perceives it should be, in that Corporation Counsel's office is going directly to the Pension Board's advisors. Mr. Grady responded that Corporation Counsel's office only discussed meeting logistics with Marquette and not investment substance. The Chairman requested that Dr. Peck add the discussion of pension obligation bonds to the next Investment Committee meeting agenda. Mr. Mueller stated that he will provide any additional information he receives on this issue to the Pension Board Chairman, who will then share the information with the entire Pension Board.

The Chairman stated that Mr. Mueller is the only person with access to the ERS credit card. Mr. Mueller indicated that the ERS credit card is in his name and the card is used generally to pay for large expenses such as conference fees. He asked that the Pension Board authorize the Chairman to sign a credit card application for ERS. Mr. Mueller pointed out that this would provide an increased internal control over ERS's finances. The Chairman suggested eliminating Mr. Mueller's credit card and having ERS obtain a new card with the same $25,000 limit as currently exists. In response to a question from Mr. Mawicke, Mr. Schroeder stated that he will be the only person authorized to use the credit card, except that Ms. Olson will be authorized to sign in his absence. Mr. Mueller states that he matched all invoices to each credit card expense and will continue to do so in the future.

The Pension Board voted 5-1, with Ms. Mayr dissenting, to authorize the Chairman to sign a Wells Fargo credit card application for an ERS credit card with a $25,000 limit with Mr. Schroeder and Ms. Olson as the only authorized users of the credit card. Motion by Mr. Maier, seconded by Dr. Peck.

6. Investment

(a) Marquette Associates, Inc. Report

The Chairman introduced the consulting team from Marquette Associates, Inc. ("Marquette"), ERS's new investment consultant. He indicated that the consulting team consists of Brian Wrubel, Brett Christenson and Ray Caprio. Mr. Wrubel stated that Marquette is performing an in-depth systems review of ERS's existing investment program by analyzing ERS's investment policies and guidelines and reviewing the performance of ERS's investment managers and their contracts. He estimated that Marquette will present its observations and recommendations on the ERS investment program at the March Pension Board meeting. He noted that Marquette will focus on ERS's asset allocation, investment management fees and the quality of the investment managers. He stated that Marquette's systems review will provide a blueprint for the Pension Board going forward.

Mr. Wrubel discussed the performance of the stock and bond markets in 2008. He presented an overview of the fixed income market environment. He noted that the Barclays Capital Aggregate Index was formerly known as the Lehman Aggregate Index. He described the bond rally in December 2008 and the volatility in the marketplace in general in 2008. He indicated that fixed income managers have a number of decisions to make in deciding how to construct their portfolios.

Mr. Wrubel explained how the flight to quality increased the price of investment grade triple-A-rated securities. He noted that junk bond prices have decreased and

their performance is more in line with the performance of the stock market. He discussed the fixed income yield curve and indicated that the S&P 500 dividend yield exceeded the 2.7% yield on 30-year Treasury at the end of 2008.

Mr. Wrubel reviewed the performance of the equity markets. He indicated that October and November were brutal months in all market areas and sectors. He discussed the performance of each of the market sectors. He reported that every major world stock market significantly decreased in value. He explained the components of the MSCI EAFE index. He reviewed the performance of the international markets. In response to a question from Dr. Peck, Mr. Wrubel stated that Morocco outperformed other international markets because it is a newer and smaller market, which means that less money has flowed in, so the market has less to decrease in value. He also pointed out that Morocco is a hard market to get into.

Mr. Wrubel stated that real estate also performed poorly, especially in the fourth quarter because of capital depreciation and writedowns. He indicated that most hedge funds had bad years in 2008. He discussed various hedge fund strategies and reasons why particular strategies performed poorly. He noted that short selling and macro strategies had positive returns in 2008.

Mr. Christenson discussed the history of bear markets and compared the current bear market to prior bear markets. He stated that a global recession happens less frequently. He indicated that 2008 was the second worst calendar year on record for the S&P 500, next to 1931. He pointed out that 2001 and 2002 were also two of the worst years in the history of the S&P 500.

Mr. Wrubel stated that Marquette hopes that these are "tail events" and that the market is at the end of the spectrum. He indicated that Marquette wants its clients to be more towards the middle of the spectrum with consistent positive returns. Mr. Christenson discussed the performance figures and durations of the 16 bear markets throughout history. He noted that the current market is looking for certainty. He pointed out that it is very unusual to have a 10-year negative return, which occurred in the 1940s and almost happened in the 1970s. He stated that a traditional portfolio of 60% equity and 40% fixed income investments only returned 0.6% over the past 10 years.

Mr. Christenson stated that Marquette focuses on preserving capital without giving up any upside results. He indicated this is achieved by focusing on costs, reviewing the quality of managers and monitoring the portfolio's asset allocation.

Mr. Caprio discussed Marquette's systems review process. He reported that the team is in the information gathering stage and is gathering data from multiple sources. He indicated that Marquette will evaluate ERS's investment managers'

fees and the managers' total returns, both gross and net. At that point, Marquette will make its formal recommendations to the Pension Board.

Mr. Caprio reviewed the current asset allocation against ERS's investment policy. He noted that ERS's fixed income allocation is at 51.7%, compared to the 42% target. He stated that the fixed income allocation is above the target because of the appreciation of bonds combined with the depreciation of the stock market. He indicated that ERS's total equity allocation is currently at 42%, which is below the 51% target.

Mr. Caprio presented ERS's performance figures from January through September 2008. He stated that ERS ranks in the 36th percentile when compared to the universe of funds with greater than $1 billion in assets, and in the 47th percentile when compared to the universe of total public funds. Ms. Riley asked why ERS's performance rankings are so low, especially when ERS generally performs better than its peers in poor market conditions. Mr. Christenson stated that this is an unusual market and there have been lower returns than usual on fixed income.

In response to a question from Dr. Peck, the Marquette representatives agreed that ERS should be careful about rebalancing its portfolio due to market volatility. Mr. Caprio indicated that ERS has had some very good investment returns following years with poor returns. Mr. Christenson stated that most equity asset classes tend to have very similar returns when the market is in chaos, as it was in 2008. Mr. Caprio reviewed the performance of ERS's investment managers, noting which managers outperformed their benchmarks. He discussed the domestic equity style diversification chart, pointing out how the portfolio compares to various benchmarks and noting the common holdings between investment managers. He stated that ERS paid 28 basis points in investment manager fees in 2008, which was less than the industry average.

Mr. Christenson indicated that Marquette will look in great depth at the fees and quality of each of ERS's investment managers. He noted that this review will identify each investment manager's risk and its risk controls.

Mr. Grady inquired how Marquette will handle consulting on the funds received from the issuance of pension obligation bonds. Mr. Christenson stated that the investment of the pension obligation bond funds will supersede all other topics. He indicated that Marquette recommended that the topic of how to invest the pension obligation bond money should be the primary topic of discussion at the next Investment Committee meeting. He noted that Marquette will develop a strong recommendation on how to invest the funds, which will focus on minimizing brokerage transaction costs. He pointed out that extreme volatility is a problem when investing a large amount of funds. He suggested investing over a period of time to achieve dollar cost averaging.

The Chairman stated that ERS has a commission recapture arrangement with Able Noser. Mr. Wrubel indicated that this topic will be also addressed at the next Investment Committee meeting.

(b) Investment Manager Report – Loomis Sayles & Company, L.P.

Mr. Dean distributed a report on Loomis Sayles & Company, L.P.'s ("Loomis Sayles") management of ERS's core fixed income and high-yield fixed income strategies and presented it to the Pension Board on behalf of Loomis. Mr. Dean stated that Marquette Associates, Inc. has an excellent reputation in the investment community and people. He indicated that Loomis manages two portfolios for ERS: Portfolio A is ERS's investment grade portfolio and Portfolio B is ERS's high-yield portfolio. He noted that Loomis has managed Portfolio A since 1991 and has only had two years with negative performance, 2008 being the worst. He reported that this year was also the worst performing year of the four negative years Loomis has had since it began managing Portfolio B in 1983.

Mr. Dean stated that Loomis is doing fine as a firm and has over $100 billion in assets, which are primarily in fixed income. He reported that Loomis is very stable with low turnover and has no plans to reduce staff levels. He noted that one portfolio manager has left to pursue other opportunities, while Loomis added one quantitative research professional. He stated that Dan Fuss was named by *Smart Money* magazine as one of the six best money managers in the world.

Mr. Dean noted that this is the worst market he has seen in his 35 years in the investment industry. He indicated that September, October and November were the worst months in the stock and bond markets. He pointed out that the worst spreads were in the corporate and government bonds. He noted that the fixed income markets turned to chaos after the Lehman Brothers collapse. He stated that the credit market was frozen at the end of 2008, but the bond market was starting to begin to function.

Mr. Dean reported that Portfolio A was down 8.0% in 2008 and trailed its benchmark. He noted that Portfolio B outperformed its benchmark but still had a negative return. He stated that the government's investments have not worked to bring the markets out of a recession, mainly because banks have not been willing to lend to borrowers who present any risk. He indicated that Loomis had very little exposure to problem investments, but commented that many toxic assets still exist in the marketplace.

Mr. Dean reviewed what caused the problems in the marketplace. He stated that the real estate market needs to bottom out and that banks need to lend and build confidence before the economy recovers. He indicated that the markets will have

a snapback when the economy recovers, but noted that the question is when markets will recover.

In response to a question from the Chairman, Mr. Dean stated that Loomis is concerned with inflation and deflation as a result of the bailout money. Mr. Dean opined that the market went from the peak of greed to the peak of fear. He indicated that investors are skeptical and concerned about inflation. He noted that there will be more self-regulation or governmental regulation on Wall Street as a result of the market failures. He pointed out that the market will return to greed and market bubbles in the future.

Mr. Dean reviewed the fixed income market performance in 2008. He stated that this was a very tough period and the spread-widening was the worst in history. He reported that the change in the spread for investment grade securities went from 200 to 600 basis points between 2007 to 2008 and the spread change for high yield securities went from 600 to 2000 basis points over the same period. He pointed out that the Portfolio A returned -8.47% for 2008. He indicated that Portfolio A has had good performance in the year following a poor return year. He provided the example where Portfolio A returned -4.76% in 1994 and 25.28% in 1995. He also stated that Portfolio B had similar snapback years in 1991 and 1996.

(c) Investment Committee Report

Dr. Peck reported on the January 5, 2009 Investment Committee meeting. She stated that Mr. Christenson and Mr. Caprio attended the meeting. She indicated that the Investment Committee discussed asset allocation logistics with Marquette. She noted that Marquette provided an update on ERS's securities lending program, which lost approximately $600,000 in 2008. The Investment Committee also discussed how to go about rebalancing the portfolio in conjunction with the asset allocation study.

Dr. Peck indicated that the Investment Committee discussed alternative investments, which include hedge funds. She stated that Marquette presented an educational piece on fund of funds investments. She explained that a fund of funds is an investment which is invested in various hedge funds. She noted that funds of funds offer diversification and expert selection of hedge funds, but at a higher cost.

7. Vitech Project and Implementation Oversight Committee Reports

Mr. Arena reported that a great deal of time and effort resulted in the successful launch of the Vitech System. He thanked the Pension Board members for their support throughout the project. He indicated that the Vitech System was the second largest systems

conversion undertaken by Milwaukee County and has had minimal problems compared to the Ceridian project.

Mr. Pillai reported that phase one of the project is 98% complete. In response to a question from Ms. Mayr, Mr. Pillai indicated that the pension checks issued by the new system will contain a phone number if people have problems with their checks. In response to a question from Mr. Grady, Mr. Pillai noted that the Retirement Office staff is using the V3 system to calculate new retirements. Mr. Pillai stated that the project's contingency funds have not been used.

Mr. Pillai stated that he accomplished all of his project goals with the tremendous support he received from Mr. Arena, Mr. Schroeder and Ms. Olson. Mr. Pillai thanked Mr. Holland of Syslogic and Mr. Rodriguez of Vitech for their support. Mr. Pillai noted that Vitech assisted his team in overcoming issues to complete the project on time.

8. Chairman and Vice Chairman Selection Process

Ms. Mayr discussed the topic of Chair and Vice Chair selection process. She stated that a former Pension Board Chairman stayed in that position for 13 years. She noted that now there are Pension Board member term limits, which would prevent that scenario from occurring. She expressed her feelings that there should be a rule requiring an election every three years for the Chair and Vice Chair positions or, alternatively, each position should have a three-year term. She suggested that the Pension Board be structured to allow its members to vote for their officers at regular intervals. Dr. Peck agreed with Ms. Mayr's views.

Mr. Grady stated that he could draft such a rule. He indicated that an election could be held at the end of the incumbent's term. The Chairman and Ms. Bedford pointed out that a Pension Board member could be serving a prior appointee's term and could be on the Pension Board for up to eight years. Ms. Mayr commented that the Pension Board might want a Chair for eight years for continuity purposes. The Pension Board agreed to have the Chair and Vice Chair stand for election every three years, but serve without term limits. Mr. Grady indicated that he will draft a rule and have Mr. Huff review the rule.

9. Annual Meeting Planning

The Pension Board discussed the annual Pension Board meeting agenda. The Chairman stated that he will ask Mr. Schroeder or an ERS representative to present during the Chairman's report. Ms. Mayr suggested that the meeting agenda should state the time the doors open and note that coffee and lunch will be available. Mr. Loeffel indicated that he included this information in the latest retiree newsletter and told the retirees not to come earlier.

Ms. Bedford asked if Scott Walker or Lee Holloway were invited to make opening remarks. The Chairman indicated that he asked Mr. Arena to extend an invitation to Mr. Walker and Mr. Holloway. Ms. Mayr suggested that the County Supervisors also be invited to attend the meeting and meet their constituents.

Mr. Loeffel questioned whether it would be better to have Marquette as the sole presenter instead of also having an investment manager speak. The Chairman noted that it has been popular with the retirees to have a manager speak. Ms. Bedford opined that she would not have chosen Artisan Partners to speak at the annual meeting in light of recent local publicity. Mr. Grady pointed out that Artisan is a local manager and manages two mid-cap strategies for ERS, which favors mid-cap investment strategies.

Ms. Frank stated that Mr. Schroeder should discuss the new Vitech System. The Chairman suggested giving the retirees a card with a pathway to the V3 System. Mr. Grady indicated that the V3 System is not yet ready for individual access. Mr. Arena stated that he will explain to the retirees that the self-service part of the V3 System will be accessible in the future.

10. Administrative Matters

The Chairman asked if there are any additions or deletions needed on the future topics list. Dr. Peck stated that the Investment Committee is looking at performing an asset allocation study, reviewing the Pension Board's options on how to invest the pension obligation bond money and monitoring ERS's brokerage fees. The Chairman indicated that the Audit Committee is not meeting at the present time due to insufficient members.

The Chairman distributed a handout on the International Foundation of Employee Benefit Plan's annual investments institute. He recommended the program and noted it is very worthwhile.

The Pension Board unanimously approved the attendance of any Pension Board member at the International Foundation of Employee Benefit Plan's Investments Institute conference on April 27 through 29, 2009 in New Orleans, Louisiana. Motion by Ms. Bedford, seconded by Dr. Peck.

11. Disability Pensions – Earned Income Statements

(a) Rule 1010 Suspension – Kenneth Clemence – Status

Mr. Schroeder reported that Mr. Clemence has complied with the requirements of Rule 1010 and that he has begun to receive his pension. He noted that there are no cases in suspension at this time.

(b) 2007 Income Review Status

Mr. Schroeder stated that the 2007 income review process has been completed. He indicated that the 2008 income review will begin after April 15, 2009, when disability pensioners file their income tax returns and provide copies to the Retirement Office. In response to Ms. Mayr's question regarding the income limitation, Mr. Grady stated that the disability pensioner's income from his or her disability pension and outside earnings cannot be greater than the amount the pensioner would have earned if he or she was able to work for the County.

12. Pending Litigation

The Pension Board noted that there are no updates in the pending litigation: *Milwaukee County, et al. v. Mercer Human Resource Consulting.*

13. Report on Special Investigation

In open session, Ms. Riley noted that there is nothing new to report regarding the special investigation.

14. Report on Compliance Review

In open session, Mr. Huff stated that there is nothing new to report regarding the compliance review.

15. Adjournment

The meeting adjourned at 11:40 a.m.

Submitted by Steven D. Huff
Secretary of the Pension Board