EMPLOYEES' RETIREMENT SYSTEM OF THE COUNTY OF MILWAUKEE

MINUTES OF THE SEPTEMBER 19, 2012 PENSION BOARD MEETING

1. Call to Order

Chairman Mickey Maier called the meeting to order at 8:30 a.m. in the Green Room of the Marcus Center, 127 East State Street, Milwaukee, Wisconsin 53202.

2. Roll Call

Members Present	Member Excused
Norb Gedemer	
D.A. Leonard	
Mickey Maier (Chairman)	
Dean Muller	
Dr. Sarah Peck	
Dave Sikorski	
Patricia Van Kampen	

Others Present
Marian Ninneman, CEBS, CRC, ERS Manager
Mark Grady, Deputy Corporation Counsel
Matthew Hanchek, Employee Benefits Administrator
Dale Yerkes, ERS Fiscal Officer
Daniel Gopalan, Assistant Fiscal Officer
Vivian Aikin, ERS
Mark Murphy, ABS Investment Management, LLC
Joe Hernandez, K2 Advisors
Brian Walsh, K2 Advisors
Ray Caprio, Marquette Associates, Inc.
Brett Christenson, Marquette Associates, Inc.
Marilyn Mayr, Prior Pension Board Member and Retiree
Yvonne Mahoney, Retiree
Joseph Szarka, Retiree
Robert Elliott, Attorney for James Tietjen
James Tietjen, Former Milwaukee County Employee
Steven Huff, Reinhart Boerner Van Deuren s.c.
Steve Schultze, Reporter, *Milwaukee Journal Sentinel*

3. Chairman's Report

The Chairman first welcomed D.A. Leonard as the new retiree elected member to the Pension Board.

In response to a question from the Chairman, Ms. Ninneman stated that there are now 7 members on the Board. The Board will be staffed at 9 after the employee election and at 10 after an appointment by the County Executive.

In response to a question from the Chairman, Mr. Grady stated that the appointment by the County Executive is going before the County Board at its next County Board meeting.

4. Minutes—July and August Pension Board Meetings

The Pension Board reviewed the minutes of the July 18, 2012 Pension Board meeting and the August 30, 2012 special Pension Board meeting.

The Pension Board unanimously approved the minutes of the July 18, 2012 Pension Board meeting. Motion by Mr. Sikorski, seconded by Ms. Van Kampen.

The Pension Board unanimously approved the minutes of the August 30, 2012 special Pension Board meeting. Motion by Mr. Gedemer, seconded by Mr. Leonard.

5. Reports of ERS Manager and Fiscal Officer

(a) Retirements Granted, July and August 2012

Ms. Ninneman presented the Retirements Granted Report for July and August 2012. In July, 24 retirements from ERS were approved, with a total monthly payment amount of $39,094. Of those 24 ERS retirements, 21 were normal retirements and 3 were deferred. Thirteen members retired under the Rule of 75. Additionally, 14 retirees chose the maximum option, and 5 retirees chose Option 3. Thirteen of the retirees were District Council 48 members. Seven retirees elected backDROPs in amounts totaling $418,175.

Ms. Ninneman continued with the August Retirements Granted Report, stating that 14 retirements from ERS were approved, with a total monthly payment amount of $22,274. Of those 14 ERS retirements, 8 were normal retirements, 3 were deferred, 2 were deferred early, and 1 was an early retirement. Seven members retired under the Rule of 75. Additionally, 9 retirees chose the maximum option, and 2 retirees chose Option 3. Seven of the retirees were District Council 48 members. Five retirees elected backDROPs in amounts totaling $386,970.

Ms. Ninneman then noted that August had the lowest volume of retirements in over a year, and that there were no significant backDROPs for either month.

In response to a question from the Chairman, Ms. Ninneman stated that ERS should continue to experience a lighter retirement volume in September and October.

(b) ERS Monthly Activities Report, July and August 2012

Ms. Ninneman presented the Monthly Activities Report for July and August 2012. In July, ERS and OBRA combined had 7,925 retirees, with a monthly payout of $12,311,767. In August, ERS and OBRA combined had 7,920 retirees, with a monthly payout of $12,260,997. To date, the number of retirements in 2012 is down from 2011.

Ms. Ninneman stated that ERS continues to field numerous calls, having received 674 calls in July and nearly 4,500 year-to-date. Legal and compliance issues were high in July and August, which can be attributed to ERS's research on individual cases and COLA adjustments, and review of ERS process and procedure related to the V3 system. ERS continues to perform audits on a monthly basis to ensure the V3 system is performing properly.

Ms. Ninneman then provided an update on ERS staffing. A new pension information specialist was hired last month. The new specialist has a very technical background and is quickly getting up to speed. The employee previously occupying the specialist position was promoted to ERS Assistant Manager, so ERS is staffed on the management side. Interviews were conducted for a clerical specialist, and ERS plans to post a position for an administrative specialist.

Ms. Ninneman then noted that Mr. Yerkes has decided to leave ERS and is currently working part time until his departure. Mr. Gopalan will handle the Fiscal Officer responsibilities until ERS fills the position.

(c) Pension Board Employee Member Election

Ms. Ninneman provided an update on the employee election. ERS is increasing employee awareness of the ERS Pension Board and the value of the pension. A candidate information session was held and 10 employees attended, resulting in 5 qualified candidates. Ms. Ninneman has been talking with ERS and OBRA members, providing information on the election and the candidates. An e-mail campaign begins this week and will continue through the campaign period. Signatures are verified and the candidates are campaigning. The voting period is expanded, and the election will run from September 28 through October 4. Ms. Ninneman also promoted the election and service on the Pension Board, which was well-received. County department heads agreed to watch for information and encourage the managers to promote employee voting.

Mr. Grady then stated that at its last meeting, the Board decided each employee would receive one vote for the special election. The candidate receiving the most votes would be awarded the longer term, and the candidate receiving the second most votes would be awarded the shorter term. Since that decision, Mr. Grady received complaints from County employees requesting that the Board reconsider. The employees want one vote for each open seat, citing that one vote for both seats is unfair because there may be two candidates who employees most want but, because of the way the votes break down with just one vote per employee, the two most popular candidates could split the votes and the candidate coming in third could be awarded a seat on the Pension Board.

In response to a question from Mr. Grady, Ms. Ninneman confirmed that there is still time to reprogram the Votenet system to accommodate the request to allow employees to vote twice, and to prevent employees from casting both votes for one candidate. There would not be a cost to these changes because the reprogramming would be done in-house.

In response to a question from the Chairman, Mr. Gedemer stated that the employees have a valid point; it is conceivable that the third most popular candidate would be awarded the second slot. Mr. Sikorski agreed.

The Pension Board unanimously approved two votes per employee in the special election to fill two employee seats. The candidate receiving the highest vote count will be assigned the longest partial term, and the candidate receiving the second-highest vote count will be assigned the shorter partial term. In the event of a tie, the tie will be broken in accordance with State statute as described in Rule 1020. Motion by Mr. Sikorski, seconded by Dr. Peck.

(d) Fiscal Officer

Mr. Gopalan first discussed the July and August portfolio activity reports, noting that July funding of $5 million came from the Mellon Capital Bond Fund. Additionally, Geneva Capital was funded by the ETF that was sold relating to the Reinhart Partners Capital Fund. August cash flow funding of $5 million also came from the Mellon Capital Bond Fund, and a Siguler Guff capital call was funded by $10,000,000.

In response to a question from the Chairman, Mr. Gopalan stated that Adams Street made a small capital call of just over $1 million.

Mr. Yerkes then discussed the cash flow report, noting that for third quarter cash needs, ERS picked managers from which timing is more intricate. ERS will receive $15 million from Morgan Stanley on the last business day of September and $10 million from IFM in the first week of October. Because ERS funds benefit payments to retirees on the second to last business day of the month, there will be a shortage of cash for one business day. Additionally, the $10 million funding of Siguler Guff is more than ERS has ever had called for private equity. Funds will be coming in from ABS in October and K2 in January, but now that ERS has more investments with partnerships rather than securities that are traded on the exchanges, it is more difficult to get those funds.

In response to a question from the Chairman, Mr. Yerkes stated that ERS is requesting additional funds of $10 million for September, and that the fourth quarter cash needs are $5 million for October, $15 million for November, and $15 million for December.

The Pension Board unanimously approved the liquidation of assets to fund additional cash flow of $10 million for September 2012, and cash flow of $5 million for October 2012, $15 million for November 2012, and $15 million for December 2012. The amounts should be withdrawn from investments designated by Marquette. Motion by Dr. Peck, seconded by Ms. Van Kampen.

Mr. Yerkes next requested that the Board approve the final 2011 Annual Report.

The Pension Board unanimously approved the final 2011 Annual Report. Motion by Mr. Sikorski, seconded by Dr. Peck.

Mr. Yerkes then discussed the 2013 preliminary budget. Because ERS wants to clarify what the Pension Board approves and what the County provides, the budget is now divided into 3 pages. The third page shows the money provided to the Pension Board by the County for administrative expenses. The second page shows what is paid directly by the ERS office. The first page is the combined budget and shows what was received in previous years.

The Chairman stated that the primary responsibility of the Pension Board is to control the investment manager and custodian fees directly related to the investments, but also to provide support for benefits administration.

In response to a question from the Chairman, Mr. Yerkes stated that the numbers for the 2013 preliminary budget came from increasing 2012 numbers by 3% across the board. Salary raises and stationary headcount assumptions were included.

In response to a question from Ms. Van Kampen as to why the 2012 projected amount is so much lower than the actual, Mr. Yerkes and Ms. Ninneman stated that four ERS positions were eliminated in the 2012 budgeting process. The Board felt that ERS would operate more efficiently if those 4 positions were restored and took action to include additional funds in the 2012 budget for those positions should that happen through the County at some point.

The Chairman then stated that the shortfall Ms. Van Kampen referred to is because the positions were never funded or approved by the County.

Mr. Yerkes stated that another difference between the 2012 projected amount and the actual relates to investment manager fees. When the 2012 budget was drafted, ERS was paying these fees directly out of the checking account. Now, however, most managers are simply deducting the fees from the value of the investment.

In response to a question from Mr. Leonard as to whether deducting fees directly gives the Board less control, Mr. Yerkes stated that the contract negotiated through the RFP process controls whether the fees are paid directly by ERS or deducted by the manager. ERS also checks the contract compliance of the managers.

In response to a question from Dr. Peck, Mr. Caprio stated that Marquette does not track fees, but does track performance and expense ratios.

In response to a question from Mr. Muller, Mr. Yerkes stated that the fees deducted from the accounts appear under Investment Manager Fees at the top of the report.

Mr. Gopalan then noted other items in the 2013 budget, such as salary and benefits and expected legal fees for VCP. There is also a $100,000 reduction in outside consultants because ERS re-categorized temporary employees and outside service into separate line items.

In response to a question from the Chairman, Mr. Gopalan confirmed there is no net change in cost for outside consultants.

In response to a question from Dr. Peck, Mr. Gopalan stated that amortization and depreciation refers to items that ERS purchases, such as the V3 software, and not cash expenses.

In response to a question from Mr. Muller, Mr. Gopalan stated that medical services relate to Medical Board disability claims.

In response to a question from the Chairman, Mr. Gopalan stated the preliminary budget could change based on the County's budget process and that no action is required from the Board on the budget right now.

In response to a question from the Chairman, Mr. Grady stated that the County Executive delivers his proposed budget on September 27, and that starts the County Board process.

The Chairman then stated that if anyone had additional questions about specific line items, the questions could be addressed at an Audit Committee or subsequent Board meeting.

6. Investments

(a) ABS Investment Management

Mark Murphy of ABS Investment Management distributed a booklet containing information on the custody services provided by ABS for ERS.

Mr. Murphy first provided an overview of ABS. ABS is a global equity long-short fund of funds benchmarked against the MSCI ACWI. Approximately half the investments made are outside the U.S., with a large portion in emerging markets. ERS is invested in the ABS global portfolio, which is $1.35 billion of the $3.75 billion of assets under management. An identical ERISA portfolio is approximately $935 million of the assets under management. ABS received about $200 million of net inflows year-to-date, and launched a long-biased emerging market portfolio in July.

Mr. Murphy next discussed the market environment. The market has been challenging and volatile, causing difficulty for long-short managers. Over the last 18 months, the MSCI remained basically unchanged despite many ups and downs. While the market went nowhere, there has been a flight to quality and liquidity and outperformance of the U.S. over emerging markets; close to 30% of the S&P has outperformed emerging markets. The emerging market index is almost completely dominated by Brazil, but includes other countries such as India, China, and Russia.

Mr. Murphy stated that volatility and manager market exposure are highly correlated. The current market environment is twice as volatile as it was before 2008. In a lower volatility environment, long-short managers have a higher net exposure. ERS is currently running 100% net long, so the long-short managers typically run 30% to 60% of that, on average half the market exposure of long-only managers. In a higher volatility environment, long-short managers do not have as much market exposure because there are not enough opportunities. Sector correlation has increased since 2008, and good and bad stocks are moving up and down together, making it more difficult for long-short managers to decipher between the two. There has been a dramatic drop in correlations over the past few months, but every time they come down a bit, they spike back up.

In response to a question from Dr. Peck, Mr. Murphy stated that a number of issues drive these correlations, such as whether Europe will stabilize, whether China will recover, whether U.S. debt is too high, and what the outcome of the U.S. election will be. These types of macro issues drive the market up and down. The current market is not an environment where fundamentals drive stock prices. Long-short managers are, for the most part, fundamental stock pickers, so they base most decisions on what they see as rich and cheap.

Mr. Murphy continued by stating that a hedge fund manager is paid to adapt to the market environment. The long-only manager is paid to be long. Fundamentals are what will bring correlations down, and they have to matter over the long run because managers have to have a longer holding period and be able to withstand volatility. If the managers have done their work and know their stocks well, eventually that will play out positively. This has been a challenging market because many managers had a shorter trading time than needed. However, the macro events mentioned earlier could change the current environment to a lower volatility market with lower correlation.

In response to a question from the Chairman, Mr. Murphy stated that ABS has seen changes in turnover within its manager portfolios. Managers with high conviction in their individual names and the ability to ride through this volatility will survive. Managers who are less successful riding the volatility will need to adapt to the market or risk being removed from the ABS portfolio.

In response to a question, Mr. Murphy stated that ABS does have managers with small positions in precious metals and commodities, but exposure is low.

Mr. Murphy next provided an overview of the ABS global portfolio. ABS's goal was to create equity-like returns with much less volatility than the market, and ABS has accomplished this on 5- and 7-year returns. Since inception, ABS has created equity-like returns with much less volatility but with a shorter run on 1- and 3-year returns, resulting in underperformance. ABS expects the numbers to improve, with September proving to be a good month.

In response to a question from Mr. Caprio, Mr. Murphy stated that ABS should realize returns of 2-2½%. Exposure is in the low 40%, which is less than half the market exposure compared to long-only managers.

Mr. Murphy then discussed fund performance. The majority of ABS managers are at the low end of their 12-month return and in a rut. Managers are finding the market environment over the last 12 months very difficult and are performing atypically below average. First quarter 2012 was a risk-on environment and the market went up. ABS had a low net exposure of about 35% and did not capture a lot of that upside. While the U.S. and Europe managers performed well, emerging market managers did not because those markets were too defensively positioned in general for the move up. Second quarter 2012, however, was a risk-off environment. May was a bad month, and another spike in correlations and volatility occurred. By June 4, the MSCI was negative for the year, so everything gained from the first quarter was lost in the second. June was the second worst month since September of 2008, when Lehman went bankrupt and AIG was bailed out. Third quarter 2012 was another risk-on quarter, with a strong rally in the market, and losses experienced by June 4 are being regained.

In response to a question from Ms. Van Kampen, Mr. Murphy stated that the process for adding managers is bottom-up in that ABS chooses strong, stable managers who do not add risk that ABS already has. This sort of diversification helps to balance the portfolio as the market environment changes.

Mr. Murphy continued by stating that the portfolio is diversified across many strategies and styles. There are 28 managers in the portfolio, with about 75% of them managing less than $2 billion, which is good for equity long-short hedge fund managers. The smaller and more nimble, the easier it is to move the exposure around.

Mr. Murphy then discussed market opportunities and market outlook. Within the broad indices over the last 18 months, treasuries, bonds, and the S&P 500 have performed the best. Emerging markets have performed the worst, and ABS has a lot of exposure to emerging markets. Within the world sectors, the areas that performed the best include healthcare and consumer staples, but hedge funds do not typically trade in these areas. More common areas are technology, consumer, industrials, and materials, which have performed poorly. Within the market cap, the S&P 500, the large-cap stocks have performed the best compared to the mid- and small-caps, which have underperformed. Emerging markets all underperformed the U.S., but comparing debt to GDP in the developed world versus the emerging market world, the developed world has low growth expectations. The percentage of GDP coming from emerging markets over the last 20 years has doubled from 20% to 40%, and continued growth is expected. The percentage of emerging markets in the MSCI ACWI has increased from 2% to 13%, and that will definitely grow over the foreseeable future. Everything to which ABS has exposure should perform well going forward.

Mr. Murphy continued by stating that several large events will occur over the next two quarters, such as the U.S. elections and the fiscal cliff. Additionally, there has been a lot of capital on the sidelines. The high correlation and volatility and this flight to quality have made it difficult for long-short managers. Bottom-up stock pickers are excited about what is coming and adapting to the new environment. Hedge fund managers are being paid to protect the downside and have done well there, but they also need to embrace a potential upside.

Mr. Murphy then discussed portfolio positioning. Currently, a gross exposure of 133% and a net exposure of 42% are in-line with historical norms. The net exposure is focused in growth-oriented sectors, such as technology and industrials, with an emphasis on emerging market demand both locally and within larger cap, U.S., and European multi-national firms. While exposure levels are relatively steady, managers are cautious because of the downside possibility.

Mr. Murphy concluded by stating that ABS is the second largest equity long-short fund of funds in the business. Over the long run, ABS has produced favorable equity returns with less volatility than the market. Though recent performance has not been as strong, ABS will continue to improve its performance. Managers are excited about their positions, and

ABS does not expect any changes to the portfolio. Equity long-short is the best way to approach global equity investing compared to long-only.

In response to a question from the Chairman, Mr. Murphy stated that ABS is keeping the weight to emerging markets, especially given the underperformance of emerging markets.

In response to a question from Mr. Muller, Mr. Murphy stated that the numbers on page 8 of the ABS report are net of fees.

(b) K2 Advisors

Joe Hernandez and Brian Walsh of K2 Advisors distributed a booklet containing information on the custody services provided by K2 Advisors for ERS. Mr. Hernandez introduced himself as part of the investor relations team based in Chicago, and then introduced Brian Walsh as the head of the research team.

Mr. Hernandez first provided an overview of K2, noting that ERS hired K2 to help dampen equity volatility and further diversify the ERS portfolio. K2 has approximately $9 billion in assets under management. Of that $9 billion, 95% comes from institutional investors. Of that 95%, about 40% comes from public pension systems like ERS. K2 is based out of Stamford, Connecticut with offices in several locations and 116 employees globally. K2 has been a pioneer in transparency, managing not just the hedge fund managers but the positions they hold. As a result, K2 has been a leader in the industry among fund of hedge funds firms.

Mr. Walsh then noted that TA Associates, which is a private equity firm, held a minority position in K2 Advisors. As of this morning, Franklin Templeton, a publicly traded firm, has taken over that position. K2 will continue to remain a stand-alone company, and investment processes, people, and so on will continue to operate as they do today. With this change, however, K2 will have more global exposure, opportunity, and resources, which will reflect in the portfolio.

In response to questions from the Chairman and Dr. Peck, Mr. Walsh stated that the percentage of ownership for Franklin Templeton is 49%, but that is expected to grow over time. The employees own the remaining 51%, with the two firm co-founders as the majority with 20 other partners. TA was an equity partner, but the relationship was more financial. The relationship with Franklin Templeton will also be more operational with the benefit of independence. Franklin Templeton does not want to get involved in picking managers and constructing portfolios, but does find value in having a business like K2. In turn, K2 can draw on Franklin Templeton resources, which are expansive.

In response to a question from Dr. Peck, Mr. Walsh confirmed that Templeton is a significant international manager, and K2 would have access to their 500 investment professionals globally, their legal team, and their IT group. K2 can still operate autonomously because Templeton will not be involved in the investment process or the day to day management of K2. None of the partners are receiving anything in terms of financial remuneration as part of this transaction and there is no change in roles. Additionally, K2 chose Franklin Templeton. TA had no role or vote in the decision.

In response to a question from Dr. Peck, Mr. Walsh stated that K2 is one of the few fund of funds that has grown in the last several years, and steadily. There are no real constraints in terms of the assets. K2 has a lot of excess capacity. The only real constraint for the investment team is the number of investments in that only so many can be understood well, so it becomes somewhat of a market dynamic. Sometimes managers have less capacity for new lenders and sometimes more. In a post 2008 world, they have become more open than closed. However, K2 added 35 employees since 2008 and is well-staffed. Mr. Hernandez also added that K2 expects to grow responsibly.

Mr. Walsh then provided a market overview. Current market volatility is driven by macroeconomic factors, which is not an easy market for managers. The market environment is not expected to change, which is why a hedged approach makes sense. Correlation of stocks, or the degree to which stocks trade together, spiked about a year ago, making it harder to make money. When stocks do not trade together, when they are less correlated, it is easier to make money, and that is currently happening in the market. The market is showing less correlation, so the environment is better for long-short equity managers.

In response to a question from Mr. Muller as to how to interpret the graph on page 4 of the report, Mr. Walsh stated that the more peaked it is, the more that stocks are trading together. The peak in December of 2011 shows that stocks are almost entirely trading together with the S&P on any given day, making it difficult to find a winner or a loser. If things are moving based on company fundamentals, finding winners or losers is a lot easier, so the market environment is currently in a good place.

Mr. Walsh then reiterated that nothing will change with K2's process and philosophy. K2 will still try to find the best possible managers and styles.

Currently, there are 115 managers at K2 and an investment staff of 35, and K2 has never been bigger. Transparency has always been a challenge for everyone's hedge funds; managers want to tell less, clients want to know more. However, K2 requests that all managers provide their positions every month, which is an important tool in understanding managers and avoiding problems, so K2 uses that transparency to measure manager risk and the amount of actual added value they provide.

In response to a question from the Chairman, Mr. Walsh stated K2 uses a tactical asset allocation approach to risk. Because of the transparency, more opportunity and security selection success in technology, and because K2 can measure it so closely month to month, K2 can invest more of the portfolio in technology long-short. It is style as well as risk level. The portfolio tends to have a market exposure of 20% to 40%. Currently, it is approximately 38%. In 2008, K2 brought it to 0, so K2 has always been fairly tactical.

Mr. Walsh then discussed fees. K2 has preferential terms with 60% of the funds in the K2 long-short portfolio, negotiating discounts on fees benefiting the portfolio with 5 of the 21 current managers. It is difficult to extract fee discounts from hedge funds. However, managers appreciate that interest rates are low and returns are not stable, and managers also know to value their clients. These fee discounts are provided uniquely to K2.

In response to a question from the Chairman, Mr. Walsh stated that the market typically sees the traditional 2 and 20 type of fee program. In the K2 portfolio, though, it is approximately 1.4 and 20.

Mr. Walsh then discussed portfolio and manager performance. Since ERS hired K2, K2 has outperformed hedge fund indices with less volatility and less risk. K2 even outperformed with less risk compared to the hedge of hedge funds benchmarks, which is an important achievement. ERS investment in the long-short fund is up 2.53% as compared to the HFRI, up 1.94%, and the HFRX, down almost 10%. Primary contributors include Maverick, a long-short global equity manager, up over 20%. Coatue, focusing on technology companies globally, is up almost 17%. Additionally, Impala, focusing on cyclicals globally and one of the best performers over the last several years, is up about 7%. Performance detractors include Elm Ridge, who is on watch, down over 11%. Quest, a cyclical manager, is down nearly 5%. Triskele China, redeemed from the portfolio, is down 4.4%. While Triskele China is a good manager, the timing was wrong. K2 is shifting more to managers who try to create their own outcomes and has a number of managers who engage with management to spin off underperforming assets and businesses or restructured capital. K2's outlook on the strategy shifts that were made and the results coming in is very positive.

Mr. Walsh continued by stating that year-to-date performance through September 14 is up a little over 7%. This is primarily driven by the fact that managers are finding more long than short opportunities. K2 is not very directional, so if the market is up 15%, it is not the sole driver of portfolio performance. It is a combination of about 35% to 40% market exposure plus security selection. The changes in the environment are a factor for the portfolio.

In response to a question from Dr. Peck, Mr. Walsh stated that typical turnover is about 15% to 20% per year, though higher in the last few years. K2 managers have liquidity, so K2 can get in and out of them relatively quickly. Managers are not truly fired; they are usually just listed as approved and unfunded if there is a need to build the portfolio out differently.

Mr. Walsh concluded with an overview of K2's portfolio strategy allocation as of August 1, 2011 and August 1, 2012. The domestically-focused long-short equity manager allocation was approximately 40% in 2011. That was decreased to 34% in 2012, which was counterintuitive because the U.S. is performing better than many other regions. Sometimes, though, those other regions under stress present more long and short opportunities. The activist allocation increased from 15% in 2011 to 22% in 2012, but exposure is really in the U.S. Those managers have a particular style, encouraging management to do things to benefit shareholders and shareholder value.

In response to questions from Dr. Peck, Mr. Walsh stated that K2 expects the activist allocation to perform better because it is difficult for companies to grow earnings, something a company cannot control. Companies have to take action to achieve the same profitability levels. In the old days, there used to be more mergers and acquisitions, but today companies are more likely to try to get control by shedding businesses that do not have the same returns on equity. Activists engage in a more positive way with management to try to make change.

In response to a question from the Chairman, Mr. Murphy stated that the 4% cash allocation is due to timing. K2 typically redeems from managers after month end and receives it over the course of the month, so the cash cannot be reinvested until month end.

In response to a question from Mr. Leonard, Mr. Walsh stated that companies sitting on a lot of cash are a big focus of activist managers because that cash earns nothing. What the activists want is for the companies to either return that money to shareholders as a dividend, buy back stock, or take some type of corporate action with that cash to generate a return.

In response to a question from Mr. Muller, Mr. Walsh stated that K2 is completely transparent and can provide the underlying positions to the Board.

(c) Marquette Associates Report

Ray Caprio and Brett Christenson of Marquette Associates distributed and discussed the second quarter report and the August 2012 monthly report.

Mr. Christenson first discussed key points in the second quarter report; specifically, the total ERS plan allocation versus other public pension funds. The median public pension fund has 33% allocated to U.S. equities as of June 30, compared to ERS's allocation of 23.5%. ERS is currently underweight 9.5% to the U.S. stock market. The median public pension fund has 13.7% of its assets in international equities, compared to ERS's allocation of 18.3%. ERS is almost 5% overweight in international. The net underweight to long-only equities, then, is about 5%. ERS is positioned more conservatively here than its peers in terms of risk because equities are the riskiest asset class. ERS is also underweight to bonds by 7.3%, with a 28% asset allocation compared to the median public pension fund at 35%. Marquette would like to see that slowly come down even more; bonds are going to be a significant drag on performance going forward due to the low yield environment and ERS's 8% assumed rate of return. In hedge funds, ERS has a 10% allocation, with the median at just under 10%. In private equity, ERS's target was increased to 6% and is now close to the peer group at 6.6%. In real estate, ERS at 8% is very similar to its peer group at 6.5%. Overall, the real positioning is the underweight to fixed income and the underweight to equities.

Mr. Christenson then discussed the net of fee rankings on the total fund composite. ERS is currently on the Investor Force platform, and more and more public funds are moving to that universe. Approximately 110 public funds across the country are part of that platform. Year-to-date returns through June show the ERS Fund was up 4.4%. However, Marquette estimates that as of mid-September, that number is about 8.5%. August was a strong month, but the stock market is up almost 5% in September. The 10-year return of the Fund through June is 6.9%, and a 10th percentile ranking on a 10-year return is an excellent rank. The median return for that same period is 5.9%, so there is just a 1% difference. The 5-year return of the Fund through June is 1.6%, with a rank in the 71st percentile. The median is 2.2%. On a 3-year basis, the Fund is 10.4% and ranks in the 49th percentile, which is in line with the median, so returns are tight over these time periods. Overall, ERS is not far from its peer group. Short-term rankings have a lot to do with how managers are performing and how the Fund is positioned in each asset class. For example, the Fund is performing better than the benchmark in bonds, up 2.6% versus 2.4%, but ranks in the 70th percentile because many of its peers are taking a lot more risk in high yields and other income-producing bonds. The equity composite is up 8.8% year-to-date and underperforming the benchmark at 9.4%, but still beating the peer group. The 21st percentile rank is due to peers having a lot more in small- and mid-cap, which have not performed well. Another reason for underperformance is due to small-cap manager returns. International performance has been disappointing, up 2.7% year-to-date, with the benchmark up 3.1%. This is due to GMO's struggle, and GMO is being replaced this month. The year-to-date on hedge funds is 1.4%, and the managers are also struggling there. Real estate came in at 5.4%, infrastructure at 3.3%, and private equity at 5.1%, and Marquette is happy with those returns. Real estate is experiencing a nice rebound over the last two to three years, and that asset class has been up over 20% per year.

Mr. Christenson then discussed the investment managers as of August, reminding the Board that two managers are currently on alert, GMO and American Realty Advisors. GMO is being terminated. American Realty had a change in staff six months ago when the director of research left. Marquette's research team recently upgraded American Realty back into compliance because the firm remains stable. Marquette recommends that the Board take American Realty off alert.

The Pension Board unanimously approved taking American Realty Advisors off alert. Motion by Dr. Peck, seconded by Ms. Van Kampen.

In response to a question from Dr. Peck, Mr. Christenson stated that K2 should automatically be placed on alert. Over the past years, institutional hedge fund of fund managers have grown in assets to multi-billion dollar companies. Most of these managers only have 5 or 6 partners in the firm, so with companies worth an extremely high amount of money, the managers need to liquidate partners out. As a result, the managers have sold pieces of their business. K2's transition from TA to Franklin Templeton is positive because the transition will build synergy, but K2 should still be placed on alert until the firm's stability can be verified.

In response to a question from Dr. Peck, Mr. Christenson stated that the transition does cause concerns with K2's investment process. One obvious risk is that Franklin Templeton could try to increase profit by reducing K2 employees, but Marquette does not think that will happen. Anything for which K2 uses Franklin Templeton on the investment side will be additive and build efficiencies. However, when a major change like this transition occurs, it is good policy to place the manager on alert for monitoring purposes.

The Pension Board unanimously approved placing K2 Advisors on alert. Motion by Dr. Peck, seconded by Mr. Gedemer.

Mr. Christenson then discussed market value assets, at $1.7 billion as of August 31. Marquette estimates that the Fund is up almost 2% so far in September. The GMO large-cap is being replaced this month and withdrawals are in place. A number of the alternative managers, such as ABS, K2, Morgan Stanley, and IFM, also have withdrawals that should be coming in at some point. Key private equity investments include the Adams Street 2005 and 2009 funds. Two new managers, Adams Street 2012 and Siguler Guff, both made capital calls. It will take time to build this portfolio up to the 6% allocation. In the meantime, it makes sense to have an overweight in the equity portfolio and an underweight in private equity because the asset classes are very similar. Marquette will most likely continue to draw funds for cash flow from the fixed income index fund.

In response to questions from Mr. Muller, Mr. Christenson stated that the policy column on the report is the asset allocation, and 29% is allocated to fixed income. Marquette is maintaining plus or minus 5% according to guidelines, and a discussion should eventually be held as to whether that should be lowered. Until that decision is made, Marquette will position the portfolio slightly underweight to the benchmark because it is clearly going to be a major drag on return. The Fed will not raise interest rates until mid-2015. Keeping the bond portfolio at a super low risk with super high quality in order to reduce the amount of assets makes good sense in a low yield environment. The net cash outflows from this Fund are only about 6% a year, which is low. The only true illiquid asset class is private equity at 6%. Real estate and infrastructure are at quarterly liquidity, but everything else, whether a comingled fund or a separate account, can be accessed within a few days, so there is a lot of liquidity in the Fund.

In response to questions from Mr. Muller, Mr. Christenson stated that the investment policy will allow for plus or minus 5% on both U.S. and international, for a total of 10%, and allow as low as 20%-22% on fixed income. The real key is the amount of risk. Anything taken out and placed elsewhere, no matter where, adds risk.

Mr. Christenson next discussed investment manager returns through August, at 6.7%, though closer to 8.5% mid-September. JP Morgan is up 4.3% versus the benchmark, which is a good number because JP Morgan is so conservative that they are not expected to earn much more than 20 to 80 basis points after fees in any given year. Mellon Capital is right on the benchmark at 3.9%. In U.S. equities, Boston large-cap and Artisan mid-cap have been consistently strong for the Fund. Geneva Capital was just funded and is currently outperforming. Two managers, Fiduciary and AQR, are struggling. Small-cap managers struggle in a very similar way to hedge fund managers because they are so fundamentally based, and there can be a lot more volatility in small-cap than in other asset classes. In general, active managers here are struggling, though neither manager is extremely off their benchmark on a 2-year basis. Fiduciary is at 15.4% versus 15.5%. AQR has not performed as well on the 2-year-basis, but performed close to the benchmark on a 3-, 4-, and 5-year basis. Marquette is concerned with AQR numbers and may consider putting AQR on alert. In international, Barings is up 7.1%, just beating the benchmark. GMO is struggling, up only 3.9%. Small-cap is up 7.5% and emerging markets is up 2.9%. Emerging markets is also an area of concern. Active management with good outperformance is difficult to find in this space.

In response to a question from Mr. Muller, Mr. Christenson stated that in terms of bonds, the 3-year number will be under 4%. The bond market has been strong. Interest rates have come down and pushed the value of the bonds up, but the yield curve just cannot go any lower right now. There will not be any more appreciation in bonds from lower interest rates going forward. The two scenarios are that they stay where they are currently and

JP Morgan and Mellon yield 2.5% returns, or they start to go up and put some pressure on returns.

After general discussion by the Board on various investment managers, underperformance, and which managers to invite to an Investment Committee meeting, Dr. Peck stated her concerns about AQR and requested that the Board place AQR on alert.

The Pension Board unanimously approved placing AQR on alert. Motion by Dr. Peck, seconded by Mr. Leonard.

Mr. Christenson continued the discussion of the investment managers, stating that Marquette hopes to see good September numbers from the long-short managers. Additionally, real estate is performing well. On a 1-year, basis, American Realty is up 12.2% and Morgan Stanley is up 15.7%, both above the peer universe. UBS had a good second quarter at 2.3%, and IFM, the first infrastructure manager to call money, has a 10.6% 2-year return. In terms of real assets over the near term, real estate and infrastructure, there are good, consistent numbers over 8%. Year-to-date, IFM is up 4.9% and JP Morgan is up 2.9%. Hopefully, this will continue in the third and fourth quarter.

Mr. Caprio then discussed the securities lending program with which ERS has been involved with the custodian, BNY Mellon, for nearly 8 years. Securities lending is a way to generate income to the Fund through securities loaned by ERS through BNY Mellon as ERS's custodian. BNY Mellon lends securities to borrowers in exchange for cash collateral, which is then invested in the ASL ERISA fund, generating additional income. ERS's income from securities lending peaked in 2008 with about $500,000 of additional income. There is some risk associated with securities lending. In 2008, the ASL ERISA fund held an interest in Sigma Finance Corp. When Sigma Finance Corp. failed, the value of ERS's investment in the ASL ERISA fund became impaired, and the Sigma securities were transferred out of the ASL ERISA fund and into a liquidating trust. Because of the impairment, changes had to be made. In the short term, a switch was made to a very conservative, cash-like investment that was extremely liquid. The investors in securities lending using the ASL Fund had some ownership in the liquidating trust. ERS proportionate exposure to the Sigma securities was about $600,000, which was a small slice. Marquette decided to limit the risk by capping the amount of securities that BNY could lend out on the account's behalf. Additionally, any additional income generated was used to pay down ERS's share of the liquidating trust payable. Over the last 3 years, the payable has been reduced to about $300,000. Approximately $100,000 of income a year is generated on the lending, so the payable will likely be complete in the next year and a half. Recently, BNY made a change to the program by eliminating the comingled funds that ERS has been using, recommending that clients switch to a separately managed portfolio and develop separate investment guidelines, as with any other investment manager, or simply exiting from the program. Because of the income generated from the securities lending program and the potential impact to the County of withdrawing from such a program, Marquette recommends that ERS continue the program.

The Chairman then reiterated that the choice is to withdraw from the securities lending program and pay the $300,000 to complete the payable, or move to a separately managed account similar to what exists today and maintain it to work off the deficit.

After general Board discussion and in response to a question from Ms. Van Kampen, Mr. Caprio stated that ERS would have more control over the separately managed account using similar guidelines as the current fund because the guidelines for the separately managed fund could be more restrictive. Additionally, the guidelines could be changed at any point.

In response to a question from Mr. Muller, Mr. Caprio stated that the fund is currently at approximately $40 million.

The Pension Board unanimously approved moving to a separately managed portfolio after investment guidelines are reviewed by Marquette and Reinhart Boerner Van Deuren s.c. Motion by Dr. Peck, seconded by Ms. Van Kampen.

7. Investment Committee Report

Dr. Peck reported on the September 6, 2012 Investment Committee meeting.

The Investment Committee first reviewed the asset allocation study prepared by Marquette, including return and risk assumptions of the current investment portfolio versus other portfolios, to evaluate whether change is needed. The Committee does not yet have a recommendation for the Board.

The Investment Committee next discussed international equity active manager performance, including asset allocation and a new parity product introduced by Marquette. Further discussion of this topic will occur at a future meeting.

The Investment Committee then discussed the construction of the international equity portfolio in more detail. Marquette addressed potentially increasing emerging markets and international small-cap while reducing international developed markets.

8. Audit Committee Report

Mr. Sikorski reported on the September 5, 2012 Audit Committee meeting.

The Audit Committee first discussed whether members of the Deputy Sheriffs Association could vote in the upcoming employee election to fill two vacant employee member seats. Language in Ordinance section 201.24(8.2) confirms that DSA members cannot vote in the employee Pension Board election.

The Audit Committee next discussed the final phase in the IRS Audit, which is to escheat funds to the State for members ERS was unable to find. In situations where members have not cashed their checks, if the benefit was to have been paid more than five years ago, the payment will immediately escheat to the State. If less than 5 years, the benefit will remain in OBRA until claimed by the member, or until more than 5 years have passed from the date the benefit was first payable.

The Audit Committee then discussed the preliminary draft of the 2013 Pension Board budget.

The Audit Committee next discussed Rule 805, which states that resignation avoids a fault or delinquency on the member's part.

The Audit Committee then discussed Rule 1013, which defines when members can no longer make changes to the form of benefit elected. Reinhart Boerner Van Deuren will draft a revised rule to include when beneficiaries can no longer be changed when members elect a joint and survivor option.

The Audit Committee next discussed Rule 202 about optional membership and which groups of non-ERS eligible employees would opt into ERS. Further discussion of this topic will occur at a future meeting.

The Audit Committee then discussed the need for a new rule regarding beneficiary designations that states that the valid designation of a beneficiary revokes any prior designations.

The Audit Committee concluded the meeting with a discussion about overpayment recoupment. ERS asked for guidelines on how much authority staff has in requesting recoupment for members.

Mr. Huff then discussed proposed Pension Board Rule 1048, which states that if a beneficiary is designated for a particular benefit, and then another beneficiary is later designated for that same benefit, even without specifically revoking the first beneficiary, the act of naming a second beneficiary is the revocation of the first beneficiary. The later beneficiary designation controls. Additionally, the beneficiary designation is effective only for that particular benefit and does not affect the beneficiary designation of a different benefit. Both the Audit Committee and Corporation Counsel reviewed this proposed rule.

The Pension Board unanimously approved proposed Rule 1048 to codify the effect of subsequent beneficiary designations, attached to these minutes as Exhibit A. Motion by Mr. Leonard, seconded by Mr. Sikorski.

9. Administrative Matters

The Pension Board discussed additions and deletions to the Pension Board, Audit Committee, and Investment Committee topic lists. The Chairman then stated that anyone with future topic suggestions should voice them.

The Chairman stated that Barings, AQR, and emerging markets would be added as topics to the Investment Committee list.

Dr. Peck then stated that risk parity should also be added as a topic to the Investment Committee list.

The Board next discussed attendance at the Council of Institutional Investors fall conference.

The Pension Board unanimously approved Pension Board member attendance at the Council of Institutional Investors in Seattle from October 3-5, 2012. Motion by Mr. Sikorski, seconded by Ms. Van Kampen.

Mr. Sikorski moved that the Pension Board adjourn into closed session under the provisions of Wisconsin Statutes section 19.85(1)(f), with regard to items 10, 11, 12, 13, and 14, for considering the financial, medical, social, or personal histories of specific persons which, if discussed in public, would be likely to have a substantial adverse effect upon the reputation of any person referred to in such histories, and that the Pension

Board adjourn into closed session under the provisions of Wisconsin Statutes section 19.85(1)(g), with regard to items 11, 12, 13, and 14 for the purpose of the Board receiving oral or written advice from legal counsel concerning strategy to be adopted with respect to pending or possible litigation. At the conclusion of the closed session, the Board may reconvene in open session to take whatever actions it may deem necessary concerning these matters.

The Pension Board voted by roll call vote 7-0 to enter into closed session to discuss agenda items 10, 11, 12, 13, and 14. Motion by Mr. Sikorski, seconded by Ms. Van Kampen.

10. Proposed Board Rule 1050

After returning to open session, the Board discussed proposed Rule 1050.

The Pension Board unanimously approved proposed Rule 1050 to codify offsets, as amended and attached to these minutes as Exhibit B. Motion by Mr. Sikorski, seconded by Dr. Peck.

11. Disability Matters

(a) Merlin Avery - ODR

In open sessions, the Chairman stated that Mr. Avery's application was received by the Medical Board and recommended for approval. The Chairman stated that he reviewed the application and did not have any questions. In response to a question from the Chairman, no other member had a question.

The Pension Board unanimously approved granting the ordinary disability pension application based on the Medical Board's determination. Motion by Mr. Leonard, seconded by Mr. Sikorski.

(b) Carl Lacy - ODR

In open session, the Chairman stated that Mr. Lacy's application was received by the Medical Board and recommended for approval. The Chairman stated that he reviewed the application and did not have any questions. In response to a question from the Chairman, no other member had a question.

The Pension Board unanimously approved granting the ordinary disability pension application based on the Medical Board's determination. Motion by Mr. Leonard, seconded by Mr. Sikorski.

(c) Janet Oglesby - ODR

In open session, the Chairman stated that Ms. Oglesby's application was received by the Medical Board and recommended for approval. The Chairman stated that he reviewed the application and did not have any questions. In response to a question from the Chairman, no other member had a question.

The Pension Board unanimously approved granting the ordinary disability pension application based on the Medical Board's determination. Motion by Mr. Leonard, seconded by Mr. Sikorski.

12. Pending Litigation

(a) *Mark Ryan, et al. v. Pension Board*

The Pension Board took no action on this item.

(b) *Renee Booker v. ERS*

The Pension Board took no action on this item.

(c) *Jo Ann Schulz v. ERS*

The Pension Board took no action on this item.

(d) *Stoker v. ERS*

The Pension Board took no action on this item.

13. Report on Compliance Review

The Pension Board took no action on this item.

14. Appeals—James Tietjen

Before adjourning into closed session, Robert Elliott, attorney for James Tietjen, provided an overview of the appeal and the documents presented into the record.

Mr. Elliott first stated that he believes Mr. Tietjen qualifies for a normal retirement benefit under section 4.1 of the Ordinances. If Mr. Tietjen qualifies for a normal retirement benefit, he therefore qualifies for the backDROP benefit. Mr. Elliott stated that the July 2, 2012 letter from ERS provides that Mr. Tietjen meets the requirements of section 4.1, but further provides that he is not eligible for a backDROP benefit because to be eligible for a backDROP, he had to retire while he was in active employment. Mr. Elliott noted that he was unable to find the term "active employment" in the Ordinances or Rules, except Rule 501 requires a member to be in "active service" to qualify for retirement benefits. Mr. Elliott argues that if ERS admits that Mr. Tietjen is eligible for a deferred vested pension benefit, he must be in active service as described in Rule 501.

Mr. Elliott continued by stating that in a response letter dated July 13, 2012 ERS stated that Mr. Tietjen did not qualify for a normal benefit under section 4.1 because he did not file the normal retirement and backDROP application forms. However, Mr. Elliott argued that the Ordinances and Rules do not indicate that eligibility for a retirement benefit is dependent on completion of the forms. Mr. Elliott's understanding is that the forms are required for the distribution of the benefit, but not for eligibility. Mr. Elliott further argued that ERS conceded in its July 2 letter that Mr. Tietjen qualifies for a normal benefit because his employment was terminated, he is over age 55, and he has more than 30 years of service. Therefore, it is Mr. Elliott's claim that Mr. Tietjen is entitled to his normal retirement benefit.

In response to a question from Mr. Huff as to the date Mr. Elliott considered Mr. Tietjen terminated, Mr. Elliott stated that Mr. Tietjen was not terminated appropriately. Mr. Elliott contended that the person who fired Mr. Tietjen on June 8, 2012, did not have the ability to do so. Therefore, Mr. Elliott concluded that Mr. Tietjen has never been terminated.

In response to a question from Mr. Huff as to when Mr. Elliott believes Mr. Tietjen applied for pension benefits, Mr. Elliott stated that it was his belief that Mr. Tietjen began the process on June 11, 2012. However, Mr. Elliott contended that ERS provided the wrong benefit information to Mr. Tietjen, stating that there would be a discount of 10%. Mr. Elliott noted that ERS later corrected this, but then would not accept Mr. Tietjen's normal retirement benefit application. A few weeks later, under protest, Mr. Tietjen filed an application for a deferred vested pension.

In response to a question from Mr. Huff as to the dates on which Mr. Elliott believes Mr. Tietjen applied for benefits and was terminated from County employment, Mr. Elliott stated that Mr. Tietjen applied for benefits starting on June 11, 2012. Mr. Elliott agreed that the County terminated Mr. Tietjen on June 8, 2012, but Mr. Elliott argued that the County did not properly terminate Mr. Tietjen.

In response to a question from Mr. Elliott, the Chairman and Mr. Grady stated that if the Board takes action on the appeal, it will occur in open session. Mr. Elliott could wait for the Board to return from closed session to hear any action the Board voted on. If there is a vote today, it will be confirmed to Mr. Elliott.

In response to a question from Mr. Leonard, Mr. Grady stated that a Personnel Review Board hearing is scheduled for October 2.

The Pension Board then discussed the matter in closed session.

Returning to open session, the Pension Board unanimously voted to deny Mr. Tietjen's appeal, consistent with the discretion assigned to the Pension Board by Ordinance section 8.17 to interpret the Ordinances and Rules of Employees' Retirement System of the County of Milwaukee ("County ERS"), based on facts and rationale discussed by the Pension Board to be adopted in final form at the next Pension Board meeting. Motion by Mr. Sikorski, seconded by Ms. Van Kampen.

15. Adjournment

The meeting adjourned at 11:30 a.m.

Submitted by Steven D. Huff,
Secretary of the Pension Board

EXHIBIT A

AMENDMENT TO THE RULES OF
THE PENSION BOARD OF THE EMPLOYEES'
RETIREMENT SYSTEM OF THE
COUNTY OF MILWAUKEE

RECITALS

1. Section 201.24(8.1) of the General Ordinances of Milwaukee County (the "Ordinances") provides that the Pension Board of the Employees' Retirement System of the County of Milwaukee (the "Pension Board") is responsible for the general administration and operation of the Employees' Retirement System of the County of Milwaukee ("ERS").

2. Ordinance section 201.24(8.6) allows the Pension Board to establish rules for the administration of ERS.

3. ERS members have the opportunity to designate a beneficiary or beneficiaries for various types of ERS benefits over the course of their membership.

4. A member may designate a beneficiary for the same benefit on multiple occasions, and the member may change who is his or her beneficiary at any time. Such changes could create conflicting beneficiary designations.

5. General contract construction principles direct that a subsequent designation of beneficiary acts to revoke a prior designation.

6. The Pension Board believes it is appropriate to adopt the following rule to clarify and codify that the subsequent designation of a beneficiary shall have the effect of revoking any prior designations with respect to the same benefit.

RESOLUTION

Effective September 19, 2012, pursuant to Ordinance section 201.24(8.6), the Pension Board hereby creates and adopts Rule 1048 to read as follows:

1048. Effect of subsequent designation of beneficiary

The valid designation of a beneficiary(ies) to receive amounts payable upon the member's death shall revoke any prior designations of a beneficiary(ies) made with respect to the same benefit. The revocation shall only be effective as to the particular benefit described in the designation.

EXHIBIT B

AMENDMENT TO THE RULES OF
THE PENSION BOARD OF THE EMPLOYEES'
RETIREMENT SYSTEM OF THE
COUNTY OF MILWAUKEE

RECITALS

1. Section 201.24(8.1) of the General Ordinances of Milwaukee County (the "Ordinances") provides that the Pension Board of the Employees' Retirement System of the County of Milwaukee (the "Pension Board") is responsible for the general administration and operation of the Employees' Retirement System of the County of Milwaukee ("ERS").

2. Ordinance section 201.24(8.6) allows the Pension Board to establish rules for the administration of ERS.

3. Periodically, for various reasons, members or beneficiaries will receive an overpayment of benefits from ERS.

4. The Pension Board believes that it is consistent with its fiduciary responsibilities to recover any overpayment made to members and beneficiaries to preserve ERS assets and ensure compliance with Internal Revenue Code requirements for tax qualified plans. Accordingly, the Pension Board desires to adopt Rule 1050 to allow ERS to offset members' and beneficiaries' future benefits to recover prior overpayments and provide for an adequate hearing prior to offset.

RESOLUTION

Effective September 19, 2012, pursuant to Ordinance section 201.24(8.6), the Pension Board hereby creates and adopts Rule 1050 to read as follows:

1050. Offset

1. *Recalculation/Cessation of Benefit.* Upon discovery of a payment in error, a determination shall be made regarding whether a benefit should have been paid under the Ordinances and Rules.

   (a) If the benefit should not have been paid, then the benefit shall cease, and a letter shall be sent to the member or beneficiary explaining the error and requesting repayment of the overpayment, plus interest from the date paid.

(b) If a benefit should have been paid but in a different amount, the member's and/or beneficiary's benefit shall be recalculated to reflect the accurate amount under the Ordinances and Rules. The corrected benefit amount shall be paid to the member and/or beneficiary going forward, and any necessary reduction to recover the overpayment shall be made in accordance with section (2) below.

(c) Eligible individuals may appeal these determinations pursuant to Rule 1016.

2. *Offset.* If a member and/or beneficiary receives benefits exceeding those to which the individual(s) is or are entitled under the Ordinances and Rules, future benefit payments to a member and/or beneficiary from ERS may be reduced until the amount of the overpayment, plus interest from the date paid, has been recovered by ERS. This right of offset shall not limit the rights of ERS to recover such overpayments in any other manner.

(a) *Amount of Offset*. If the Retirement Office determines that an offset is appropriate, the Retirement Office shall reduce the affected individual's ERS benefit payments by up to 100% until ERS has fully recovered the amount of the overpayment, plus interest from the date paid. This reduction shall begin at the time indicated in subsections (c) and (d) below.

In determining the amount of the offset, the Retirement Office, and the Pension Board on appeal, should consider all of the following factors:

(i) The reason for the overpayment (e.g., fraud, miscalculation, mistake). If the individual played a part in receiving the overpayment, the percentage of offset could be greater.

(ii) The life expectancy of the individual. The overpayment should be recovered, if possible, before the death of the last beneficiary.

(iii) The amount of the benefit versus the overpayment to be recovered (e.g., if it is a smaller benefit and larger overpayment, the offset would need to be greater).

(iv) The financial resources available to the individual to satisfy the amount of the overpayment, plus interest, from resources other than the individual's ERS benefit.

(b) *Interest Rate.* The interest rate payable on the overpayment shall be at the rate specified in and pursuant to Rule 403.

(c) *Offset Procedures.* Upon discovery of an overpayment, the Retirement Office shall notify the affected individual in writing and explain the nature and amount of the overpayment. The following information shall also be included in the notice:

(i) a request that the individual repay the overpayment in a lump sum payment;

(ii) a statement that if the member declines to repay the overpayment in a lump sum, ERS intends to reduce the amount of the individual's future benefit payments until the overpayment amount, plus interest, has been recovered;

(iii) the effective date of the offset;

(iv) the amount that was overpaid;

(v) the total recovery amount (i.e., the overpayment plus interest from the date paid);

(vi) if applicable, the corrected benefit amount that the member is entitled to receive;

(vii) a statement regarding the tax treatment of the overpayment (e.g., if a portion of the overpayment was rolled over, favorable tax treatment may not be available);

(viii) the reduced benefit amount that will be paid to the individual after the offset is applied;

(ix) a statement that the individual may appeal the Retirement Office's decision pursuant to the process described in subsection (d) below.

(d) *Appeals.*

(i) *Initial Appeal Process.* The member may appeal the offset decision and amount of the offset to the Pension Board at the Pension Board meeting immediately following the notice of offset at which it is possible to schedule the appeal (or the Pension Board could call a special meeting). If the member appeals to the Pension Board, the offset will not commence until a decision regarding the offset has been made by the Pension Board. If the Pension Board determines that the offset is correct and consistent with this Rule, ERS will implement the offset as soon as administratively possible. If the member does not appeal under this initial appeal process, the

Retirement Office will commence the offset as of the date specified in the notice.

(ii) *Rule 1016 Appeal Process*. After the initial decision of the Pension Board, the individual subject to offset may appeal to the Pension Board as described in Rule 1016. The individual may appeal under Rule 1016 regardless of whether the member utilized the initial appeal. However, if the offset commenced as of the date described in the notice, the offset will continue unless and until the Pension Board determines on appeal that the offset is improper. If the offset is determined to be improper, the individual will be repaid the amount previously withheld.

(iii) *No Appeal for Subsequent Offset*. If a beneficiary's payments are offset to recover an overpayment made to a member, the beneficiary shall not have an independent right to appeal if the member utilized the appeal rights granted by this Rule or Rule 1016.