Milwaukee County Employees' Retirement System (ERS)
Investment Committee Meeting
MINUTES

Call to Order

Chairperson Patti Van Kampen called the Investment Committee to order at 2:33 p.m. on Monday, March 7, 2016 in Room 203P of the Milwaukee County Courthouse, 901 N. 9th Street, Milwaukee, WI 53233.

Board Members Present:
Patti Van Kampen
Laurie Braun
Michael Harper
Vera Westphal

Others Present:
Brett Christenson, Marquette Associates
Christopher Caparelli, Marquette Associates
Larry Langer, Buck Consultants
Steven Huff, Reinhart Boerner Van Deuren, S.C.
James Carroll, Assistant Corporation Counsel
Scott Manske, Comptroller
CJ Pahl, Budget and Management Coordinator, Office of the Comptroller
Marian Ninneman
Tina Lausier

With Mr. Langer present from Buck Consultants, Ms. Van Kampen reversed the order of the topics for discussion.

2. Actuarial Data Relative to Expected Return Rate – Discussion

Presented by Larry Langer:

Last year investment return was left alone. The Basic Funding Equation is a grand budgeting tool of which investment income is a factor. Actuarial assumptions DO NOT change the ultimate cost of the retirement system. They ONLY change the timing of contributions into the plan. Over the short term, contributions are determined by the actuarial valuation process based upon estimated investment return, benefits and expenses using assumptions and methods recommended by the actuary and adopted by the Board.

The Funding Policy is one of the inputs in the actuarial valuation process. A summary of assumptions was provided, which are periodically reviewed – the last time they were reviewed was at the end of 2012.

Mr. Langer provided results of a survey of public pension investment return assumptions. The investment return for large pension systems has trended down from 8% median to 7.625% median. It was noted that these are much larger funds and have different investment strategies.

Current standards of practice suggest the use of an assumption that falls within the 40th and 50th percentile of projected returns, which would be between 7.36% and 8.48% from the chart provided. Based upon this, the 8% investment return assumption can be maintained. But Mr. Langer provided a moment of caution – over the next 5-10 years achieving 8% investment return will be very difficult.

After reviewing the charts provided, Ms. Braun asked if we were even more of an outlier. Mr. Langer responded that we have room to maintain the 8% over the long-term (30+ years). Other organizations, such as Marquette, may take a tighter look over only 10 years. Several other differences may be:

- Developed expectations are different
- Some asset classes are viewed differently
- Admin expenses may not be taken into account
- No adjustments for Alpha
- Inflation assumptions may differ

Mr. Christenson urged us not to get caught up in differences.

Mr. Langer's overall conclusion is the Board is not required to lower the rate, but of course you can choose to do so. The 7.5% assumption being considered is reasonable as well, and 4 alternatives to reducing to 7.5% was provided:

- Maintain the 8% until the anticipated experience review to be conducted in advance of the 2018 valuation.
- Consider alternative projections to give stakeholders a heads up to fund more to reflect both additional conservatism and the 2015 asset experience.
- Lower to 7.5% in a phase in.
- Use a select and ultimate assumption

Ms. Van Kampen asked what the impact would be on employee contributions with a lower investment return assumption. Mr. Langer responded that member contributions would see a similar percentage increase as contributions. Ms. Braun asked if a chart with more gradual change over the next 5 years would be available (i.e.: 8%, 7.9%, 7.8%, 7.7%, 7.6%, and 7.5%). Mr. Langer responded that it would be better to choose a percentage and blend the contribution figures. Ms. Westphal noted that once you start dropping the percentage to 7.5%, it may spur higher retirements (with backdrops) in order to still get the higher percentage. Mr. Langer further stated that the retirements do not have to be tied to the investment required rate of return. Mr. Manske provided comments to remember the impact on employee contribution percentages and look at investments and where they are going.

The next step is to refine the numbers by the actuary for presentation at the March Board meeting.

1. Updated Investment Guidelines – Discussion

The question is, what are the implications of the 75% equity limits (common stock) in the ordinances? Mr. Huff stated that there is no clarification on what is considered common stock and therefore what can be put in place to ensure compliance.

Documents provided background and analysis of the issue, including the minimum, target and maximum percentages for each asset class. Mr. Christenson stated that the cash overlay is less than $5 million, but the end of 2015 it was closer to $30 million due to county contributions received at the end of the year. Further, if you take a broad approach to what is considered "equity" or "common stock" it would include

Equity
Hedged Equity
Private Equity
Infrastructure

Which would leave Fixed Income and Real Estate out, and using the minimums these 2 classes would be only 22.5%. The minimums would need to be adjusted if this is the case. Ms. Van Kampen mentioned that, at the time the rule was put into place, it was meant to be conservative, but there weren't as many asset classes as we have today. Mr. Christenson added that the volatility of public common stock is generally higher, but equities actually have lower volatility.

Mr. Huff stated that this is an ordinance and that there is no grace period. Thus, the Board needs to be sure it is not violated. Unfortunately, without clear knowledge of what is considered "common stock" it is difficult to know if we are in compliance. Mr. Christenson stated that if clarification can be provided by each asset class, as to whether they are considered "common stock" or whether the 1st tier mutual fund is excluded from this classification, we would have a better idea of what is required. For instance, if Infrastructure is not considered "common stock" then we would be fine. Mr. Christenson will inquire with each fund as to how they interpret "common stock" and whether they consider the fund to be included in that classification. Ms. Braun would like to have a legal opinion before any interpretations are made. In response, Mr. Carroll stated that both would be reasonable, and thus a legal opinion would not provide further clarification. Mr. Christenson suggested to think of "common stock" as publically traded stock – let's take a conservative approach, and see what we get back from the investment managers.

Mr. Christenson stated that depending upon the clarification, he might suggest to move Fixed Income to 19% and Private Equity to 9% to give more of a cushion. Mr. Harper stated that he would prefer the change to be from Hedged Equity instead of Private Equity, and Mr. Christenson agreed that would be a better correction to make. Ms. Van Kampen asked if we can also find out what kind of month to month variance occurs with these funds in order to determine if fluctuations need to be a part of the discussion.

Moving on, Mr. Caparelli stated that 30 submissions were received to our RFP for a new investment manager to replace GMO in International Equity. It was also noted that GMO is one of the candidates that responded to the RFP with a different fund. Marquette will work through the screening process to narrow down the options for potential interviews in May. Detailed information on the potential funds will be provided for selection at the April Investment Committee meeting.

The next Investment Committee meeting is scheduled for Monday, April 4, 2016, at 2:30p.m., in Room 203-P of the Milwaukee County Courthouse at 901 North 9th Street, Milwaukee, WI 53233.

Meeting adjourned at 4:11 p.m.