Minutes of the Regular Monthly Meeting
Board of Trustees
Employees' Retirement System of the City of Norfolk
November 10, 2010

The regular monthly meeting of the Board of Trustees of the Employees' Retirement System of the City of Norfolk was held in the City Hall sixth floor conference room in the City of Norfolk, Virginia. The meeting began at 12:00 p.m. on Wednesday, November 10, 2010, with Chairperson Stephanie Calliott presiding. The following was the result of the roll call:

Attending the Meeting	Not Attending the Meeting
S. A. Calliott	R.V.K. Williams
C. R. Neikirk	K.W. Crowder
E. G. Tucker	
N. E. Nelson	
D.V. Hill	
L. A. Bernert	
Y. T. Allmond	

Ms. Mary L. G. Nexsen, Deputy City Attorney, attended the meeting.

The minutes for the meeting held on October 13, 2010 were approved.

New Business

A. Applications for vested service retirement:

Lynne P. Teller, Active No. 15684, December 1, 2007, with refund of $1,661.01. [Water Utility Fund]

Anthony L. Hayes, Active No. 18140, November 1, 2010, with no refund due. [Human Resources]

Stephen A. Schwartz, Active No. 19168, November 1, 2010, with no refund due. [Police]

Janice D. Dailey, Active No. 26768, December 1, 2010, with no refund due. [Human Services]

B. Applications for early service retirement:

Gwendolyn L. Thomas, Active No. 26208, December 1, 2010, with no refund due. [Juvenile Detention Center]

John M. Haithcock, Active No. 26416, December 1, 2010, with no refund due. [Police]

C. Applications for normal service retirement:

Gernoah N. Purnell, Active No. 19726, December 1, 2010, with no refund due. [Utilities]

Rudolph L. Dailey, Active No. 24060, December 1, 2010, with no refund due. [Public Works]

Gwendolyn W. Brehon, Active No. 24061, December 1, 2010, with no refund due. [Human Services]

Edward Savage, Jr., Active No. 24288, December 1, 2010, with no refund due. [Public Works]

William E. Dangle, Active No. 27224, December 1, 2010, with no refund due. [Police]

George T. Glazner, Active No. 19715, January 1, 2011, with no refund due. [Fire-Rescue Services]

Raymond E. Stephens, Active No. 25120, January 1, 2011, with no refund due. [Public Works]

Guzin Akan, Active No. 25732, January 1, 2011, with no refund due. [Public Works]

Robert M. Randall, Active No. 23199, February 1, 2011, with no refund due. [Planning]

D. Recommendations by the Medical Board that following be retired:

Mark A. Wethington, Active No. 24576, with no refund due. This member requested accidental disability retirement. [Finance & Business Services]

The Board approved Mark A. Wethington's request for accidental disability retirement. This approval is for one year. In one year, Mr. Wethington will undergo review of a functional capacity evaluation. [Approved 6; Abstain 1]

Russell K. Davis, Active No. 27018, with no refund. This member requested ordinary disability retirement. [Utilities]

The Board approved Russell K. Davis' request for ordinary disability retirement. This approval is for one year. In one year, Mr. Davis will undergo medical review. [Approve 4; Disapprove 2; Abstain 1]

NOTE: Mary Lou Nexsen will research how the Social Security Administration reviews same type of disability as related to retirement.

E. Death of retired members:

Raymond B. Chapman, Ret. No. 01452, death occurred April 4, 2010. Spouse elected monthly benefit of $343.57.

Janice L. Baum, Ret. No. 02521, death occurred September 12, 2010. No benefit payable due to no surviving spouse or dependent children.

Aloysius J. Dalpiaz, Ret. No. 02177, death occurred September 16, 2010. No benefit payable due to no surviving spouse or dependent children.

Marjorie G. Tillett, Ret. No. 03032, death occurred September 21, 2010. No benefit payable due to no surviving spouse or dependent children.

Paul Schumack, Ret. No. 04626, death occurred September 21, 2010. No benefit payable due to no surviving spouse or dependent children.

Mildred W. Copeland, Ret. No. 03336, death occurred October 1, 2010. No benefit payable due to no surviving spouse or dependent children.

Frances L. Kruger, Ret. No. 03382, death occurred October 3, 2010. No benefit payable due to no surviving spouse or dependent children.

William D. Kline, Ret. No. 03814, death occurred October 18, 2010. Spouse elected monthly benefit of $1,239.11.

Marie M. Lester, Ret. No. 03158, death occurred October 19, 2010. No benefit payable due to no surviving spouse or dependent children.

F. Death of spouses:

Violet L. Daughtry, Spouse No. 00312, death occurred September 26, 2010. No benefit payable.

Kathleen P. Hitt, Beneficiary No. 01166, death occurred October 26, 2010. No benefit payable.

The Board approved withdrawal of the following non-contributing members:

Name of Member	Active Number
Scott M. Warren	31159
Felicia J. White	31265
Lavonne R. Cuffee	31396
Ashley Folston	31877
Tressa Lucas	31895
Sharon Maben	31938
Alex C. English	32215
Mallory M. Chandler	32239
Brandy L. Jeschonek	32536
Stacy Adams	32579
Amy M. Fries	32684
Sherry Longshore	32924
Sandra L. Aquilar-Perez	32955
Joseph R. Robinson	32963
Heather A. Vargas	32964
Total Members - 15	

The following report of payments from the Trust Fund received and filed:

Chantal N. Brooks	(1)	$	250.00
Theodore O. Wilder	(2)		291.24
Baker's Crust	(3)		290.38
Retirement Payroll (Est. for November. 2010)		$	5,500,000.00
Total		$	5,500,831.62

(1) Medical examination for Mark Wethington

(2) Reimbursement for attending the Fall Meeting of the Association of Municipal Retirement Systems of Virginia in Danville, VA on October 25-26, 2010

(3) Lunch for Board Meeting held on October 13, 2010

Committee Reports

Administration and Planning:
There was no meeting.

Investment Management:
Mr. Neikirk informed the Board that the Investment Committee did meet today. Jessica Portis with Summit Strategies Group participated via conference call.

The first item on the agenda was the discussion of the assumed rate of return (discount rate). The System's current assumed rate of return is 7.5%. Chris Neikirk provided the trustees with a handout with sensitivity tables that showed the projected rate of return based on Summit's capital market assumptions with the System's prescribed asset allocation. The tables provided:

- Projected Return at 87.5% Fixed Income and 12.5% Real Estate
  - Using Summit's long-term assumptions produces a 4% expected return given the 3.5% fixed income long-term return and the 7.5% annualized real estate return.

- Projected Return at 60% Equity and 35% Fixed Income and 5% Real Estate
  - This portfolio composition provided a future expected return of approximately 6.4%.

Jessica discussed the Capital Markets Monthly – September 2010 Report. Summit always tries to make sure the methodology used to develop assumptions is logical and defendable. The assumptions for fixed income are based on the notion that bonds earn their yield. All fixed income expectations take into consideration the current yield for a representative asset. This methodology is used to determine the expected returns for each of the bond types. In aggregate, the core fixed income return assumption is currently 3¼%, and this is a reflection of current yields in the fixed income market (Page 8). On Page 9, Summit described the components of equity returns as follows:

1. stocks are going to earn dividends over time,
2. stocks have real EPS growth that needs to be incorporated; historically this number has been a percentage of US GDP growth,
3. the valuation (using P/E ratio as a measure) of stocks relative to history is used to determine if they are under- or under valued currently. Based on where they reside relative to their historical average a discount or premium is applied to the expected return, and
4. inflation assumption of 2.5% for each asset class

As an example, Summit showed the methodology utilized to derive the current assumption for Large Cap which is 7.5%.

Methodology for real estate is very similar to fixed income. The expectation is that real estate assets have a cap rate in terms of what will be generated from a yield perspective. A ten year expected return of 7.5% is anticipated for Core Real Estate.

The majority of Summit's clients are having similar conversations on the assumed rate of return. There have been a few articles in the press recently citing initiatives by large public funds considering a reduction of their assumed rate of return. Jessica provided a recent example surrounding CALSTERS, which is considering reducing their rate from 8% to 7.5%.

The Actuary (Cheiron) provided a letter dated October 28, 2010 on the *Estimated Financial Impact of Changing Interest Rate.* Last month the Trustees compared the

System’s rate of return with other municipal systems in Virginia and 7.5% was the median. On Page 2 of the letter, the projected Fiscal Year 2012 contribution rate is depicted in a graph with assumption rates of 7.5% ($45,497,000), 7.25% ($48,926,000), and 7.0% ($52,224,000).

The Chair reminded the Board that they have fiduciary oversight responsibility to review the rate of return, and make a recommendation. The City leadership decides on what action to take from the Board’s recommendation. The current rate of return of 7.5% was approved years ago.

The Trustees have been discussing the possibility of changing the assumed rate of return for some time. In formulating a decision, they reviewed and researched the following:

- Data provided on 10 other cities in Virginia as well as the Virginia Retirement System
- Data on 1 to 25 years historical returns achieved on various asset classes; both short- and long-term returns were examined.
- The expected return of the System’s target portfolio based on Summit’s Capital Market Assumptions. The blending of 60% equity, 35% fixed income and 5% real estate assumed returns produced a 10-year expected return of 6.4%.
- The information provided by Cheiron on the *Estimated Financial Impact of Changing Interest Rate* at 7.5%, 7.25% and 7%
- Five different articles were distributed to the trustees:

1. Washington Post Video (September 21, 2010)
   Title: Rowe says Public Pensions need to cut Return Assumptions

2. Wall Street Journal Weekend Edition, (September 18-19, 2010)
   Title: Pension Gaps Loom Larger
   Funds Stick to ‘Unrealistic’ Return Assumptions,
   Threatening Bigger Shortfalls

3. The Huffington Post (October 15, 2010)
   Pension Benefits for Current Employees Could Face Legal Challenges

4. The Richmond Times-Dispatch (October 29, 2010)
   VRS gives Warning to Assembly on Pension Funding

5. Pension & Investments Magazine (November 1, 2010)
   Balancing Obligations: Face to face with William R. Atwood

Based on all the above information, input from financial professionals, and considerable discussion, the Investment Committee decided not to change the 7.5% rate of return assumptions. The Committee did agree to schedule an annual review of comparable data on assumed rate of return other public plans such as the Virginia

Retirement System, and some plans among Summit's consulting customers. This data will be reviewed in October yearly.

There has been some discussion on the duration of passive fixed income portfolios and whether there should be any action to shorten the duration to reduce interest rate risk. Summit provided a handout on the *Impact of Rising Interest Rates.* Jessica provided salient points related to the subject. Generally, people are doing and talking about making changes to their portfolio particularly in light of where rates are. Some clients have chosen to substitute fixed income with more alternative-based assets. People who want to maintain the traditional fixed income portfolio structure are making changes to the areas of the portfolio where there is the most risk. A passive strategy benchmarked against the Barclays Aggregate remains heavily dominated by treasuries and other government guaranteed assets which are experiencing very low yields. Some Summit clients are looking to shorten the duration of those particular portfolios adding areas to the portfolio that are higher in terms of the income they generate. Some clients have put in dedicated high yields mandates, others take a look at bank loans, and different ways they can supplement the effect of what is going to happen on the price side when interest rates begin to rise.

PIMCO is attempting to structure the portfolio to protect against rising U.S. interest rates. They have been managing fixed income assets for an extended period of time, and have been able to navigate other rising interest environments. One of the main things that PIMCO has done in recent history has been to position the portfolio in higher yielding assets. This could be (non-US) dollar-denominated debt; emerging market debt (which is trading at a higher yield relative to US securities); or high quality corporate bonds. PIMCO has chosen to underweight the longer duration assets and concentrated on shorter-duration assets so that as some of the securities mature, they can be reinvested at higher yields if interest rates rise.

Summit concluded short duration strategies may make sense for passive Barclays Aggregate strategies given there is no opportunity to enhance yield and the large weighting to government guaranteed assets; however, the System would be giving up yields at least for some time.

Among the fixed income portfolio, PIMCO comprises 64%. A portion of the PIMCO allocation will be used to fund another asset class (real estate). The remaining fixed income portfolio is comprised of 13% passive TIPS, and 23% passive Barclays Aggregate. The question becomes does the Board want to try and do something about the 23% exposed to Barclays Aggregate? After considerable discussion the Committee voted to not make any changes to the Passive Fixed Income portfolio.

Jessica reviewed with the Committee the *Investment Review 3rd Quarter 2010.* At the request of the Trustees, a new page was added to the quarterly review documenting rebalancing activity for the quarter as well as any other transactions (Page 3). The majority of cash raised was for monthly benefit payments as opposed to actual rebalancing purposes. Over the course of the quarter, the System used fixed income since this was where the portfolio was overweight. For the month of October the portfolio was overweight to international equities. In the month of November, cash will be withdrawn for benefits payment from the SSgA MSCI ACWI-ex US.

In reviewing the asset allocation, we have made a conscious decision to have a healthy allocation to international versus US. The 5% allocation that has been earmarked for real estate will put the portfolio in line with the median public fund and get the fixed income allocation closer to the median portfolio. Performance for the portfolio was discussed for the period ending September 30, 2010, including a comparison of peer rankings for the System.

October was a good month and resulted in a total market value of the pension fund of $825.3 million at month's end. The approximate funded status is 78.8% based on the last actuarial valuation of the liability. Two million dollars will be taken from the international portfolio within the next couple of weeks to fund benefit payments. Total performance was at 2.64% for the month with alpha coming from the PIMCO (fixed income) portfolio return of 1.06%, and TIPs performance return of 3.64%.

Ted Wilder informed the Board that at the December meeting Cheiron (Actuary) will present the June 30, 2010 Actuarial Valuation Results, and comment on the letter provided on estimated financial impact of changing interest rate. Also, KPMG is scheduled to present results of the June 30, 2010 audit.

Mr. Hill informed the Board that the City Manager has announced her retirement effective January 14, 2011. The City Manager's position is an ex-officio member of the Retirement Board of Trustees.

The Trustees reviewed the meeting schedule for Calendar Year 2011. Board meetings remain on the second Wednesday of the month at noon.

The Board's next meeting is on Wednesday, December 8, 2010 at 11:30 a.m. There will not be an Investment Committee meeting.

There being no further business, the meeting adjourned at 12:45 p.m.

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Chairperson

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Executive Director