

**Spokane Employees' Retirement System (SERS)
Board Meeting Minutes
May 30, 2012**

Bill Todd called the regular monthly meeting to order at 12:30 p.m. in the 5th Floor Conference Room at City Hall.

Present: Bill Todd, Jon Snyder, Jerry McFarlane, Mike Coster, Steve Sather, Dean Kiefer and Brian Brill

Staff: Leo Griffin, Christine Ellingson, Donald Brown and Tim Szambelan

Guests: Jayson Davidson, Bill Dowd, Bill Reid, Joan Hamilton, Joe Cavanaugh, Dean Vercruyssen, Mike Cavanaugh, Jim Tieken, Dave Hanshaw, Heather Lowe and John Bjork

Morrison Street Capital

Mr. Davidson presented Hymas Group's due diligence for Morrison Street Capital and their Morrison Street Fund IV. Mr. Davidson and Mr. Griffin are recommending a \$6.0 million commitment to Fund IV. The formal commitment, however, will only be finalized when additional due diligence has been conducted on the fund's auditor. The auditor due diligence is expected to be completed by June 8, 2012. The investment, once funded, will give the SERS portfolio a slightly different exposure to the mid-tier commercial real estate market. Historically, Morrison Street has focused on investments primarily within the Mountain and Western United States. Debt investments, particularly their Commercial Collateralized Mortgage Back Securities (CMBS) investments, have tended to have a broader national footprint. The property types for investment have historically included office, industrial, retail and multi-family.

In addition, the investment structures have included equity, preferred equity, mezzanine debt and CMBS. Based on the current market opportunities, this fund is expected to invest the majority of its assets in privately negotiated/structured preferred equity or mezzanine investments (targeting roughly 70% of portfolio) versus traditional equity investments. Therefore, the risk/return profile of this fund is expected to be highly differentiated from traditional equity-only real estate investment funds. Essentially, the fund is a hybrid lender with a majority of the assets structured around preferred equity investments, which operate more like a bond than traditional equity. As a result, we expect this to be a relatively conservative strategy relative to real estate equity-only strategies. The strategy is targeting returns in the high single to low double digits with the majority of returns derived from regular income payments (yield) and significant downside protection provided by attractive loan-to-value (LTV) ratios. The fund is expected to have a ten-year life and should be cash flow positive much earlier than traditional equity-only real estate investment strategies.

Mr. Griffin performed his on-site due diligence on the fund when he met with Rance Gregory, CEO and Brian Loescher of the Hyas Group in Hyas Group's Portland offices in December 2011. In March 2012, Mr. Griffin met with Rance Gregory and his senior management team in Morrison Street's offices in Portland, OR. Mr. Griffin stated the fund, given its size, takes advantage of market inefficiencies in the small-middle markets that tend to be less competitive than major markets.

Jon Snyder moved and Jerry McFarlane seconded the motion to accept the recommendation to commit \$6 million from equities (global split to be determined by Mr. Davidson and Mr. Griffin) to Morrison Street Fund IV, contingent upon final due diligence of the fund's auditor. The motion passed unanimously.

Capital Market Assumptions

Mr. Davidson presented a review of the Hyas Group's intermediate and long-term capital market assumptions. This review projects a slight bit of volatility in the ten-year assumptions but the 30-year assumptions were consistent with the last capital markets study conducted in 2007 and the return assumptions were largely consistent with long-term, historical averages. However, this is a forward-looking study. Based on SERS' asset allocation and Hyas Group's *intermediate-term* capital market assumptions, the SERS portfolio is expected to earn a 7.28% weighted average annual return over the next ten years. Using Hyas Group's *long-term* capital market assumptions, and based on SERS' asset allocation, the SERS portfolio is expected to earn a 9.08% weighted average annual return over the next 30 years. Mr. Griffin pointed out that the May 2007 Arnerich Massena Asset Allocation Analysis, which used a slightly different asset allocation for SERS, projected a 30-year return of 9.4%.

Actuarial Experience Study – Bill Dowd & Bill Reid, SageView Consulting

Mr. Dowd and Mr. Reid discussed the Experience Study for the five-year time period ended December 31, 2011. An Experience Study is conducted every five years to test the actuarial assumptions against actual System experience. The results of the study are used to make recommendations for changes going forward in an attempt to provide the best estimate of expected future experience as it relates to contribution rates and the funded status of the System. The actuaries discussed demographic and economic assumptions, valuation and actuarial costing methods, and presented an impact of their recommendations.

The investment return assumption rate of 7.5% was also discussed. A 2011 study performed by Wilshire Associates reflects that although some pension plans have lowered their assumption rates, the mean, median and mode assumed rate of return remains at 8%. At 7.5%, SERS is in the bottom quartile nationwide for assumed rates of return for governmental pension plans; three quarters of pension plans have assumed rates of returns that are higher than SERS. Mr. Dowd pointed out that the investment consultant's analysis reflects a projected investment return of 9.08% over the next 30 years given SERS' sophisticated asset allocation. The actuary recommended to the Board that the assumed rate of return on investments remain at 7.5%.

SERS uses the Projected Unit Credit (PUC) actuarial cost method, which is one of the methods currently allowed by the Governmental Accounting Standards Board (GASB). However, the GASB is poised to issue a new Pension Pronouncement in June 2012 which Mr. Griffin stated will bring more “consistency” to governmental reporting disclosures. The latest draft of that Pronouncement was studied by Mr. Griffin and Mr. Dowd and contains a requirement of Entry Age Normal (EAN) for the actuarial cost method. Mr. Griffin stated SERS used the EAN costing method up until the late 1980s when the Plan changed to PUC. Mr. Dowd and Mr. Griffin recommended to the Board a change from PUC to EAN.

The recommended changes to the actuarial assumptions are outlined as follows:

- Demographic
 - Retirement
 - Decrease early retirement rates
 - Termination before Retirement
 - Decrease termination rates
 - Disability
 - No change
 - Mortality
 - No change
- Economic
 - Salary Increases
 - Increase salary increase rates for members with less than 5 years of service (step increases)
 - Reduce salary increase rates for members with more than 5 years of service to 0% in years 2013, 2014 and 2015.
 - In 2016 and thereafter, use current salary increase table for members with more than 5 years of service.
 - Investment Return
 - No Change
- Valuation Methods
 - Actuarial Cost Method
 - Change to Entry Age
 - Asset Valuation method
 - No change

If the Board approves the above assumption changes, the revised funded ratio as of December 31, 2011 will be 70.6% and the recommended contribution rate by the actuary is 16.5% (8.25% if split equally by the City and the employee participant). The current contribution rate is 15.5% split equally between the City and the employee participants at 7.75%.

Brian Brill moved and Jon Snyder seconded the motion to accept the recommendation of SageView to change actuarial assumptions as they appear on p. 25 of the Experience Study as a Summary of Recommendations [and as outlined above]. The motion passed unanimously.

Interest Rate on Employee Contributions

The Board deferred this item to the June meeting.

2012 1st Qtr Investment Performance Report

Mr. Davidson briefed the Board on the portfolio returns in what amounted to be a second, consecutive strong quarter on both a relative and an absolute basis. SERS' investment performance, for the second quarter in a row, is considered top quartile as measured against other pension plans nationwide. For the quarter ended March 31, 2012, SERS' investment return was 8.92%, which is slightly ahead of the Policy Index return of 8.83%. One-year performance was 2.18%, three-year was 15.77% and five-year 3.20%. SERS' five-year investment performance exceeded the policy index by 20 basis points and is above median when compared to other pension funds nationwide.

The watch status on the Hotchkis & Wiley Core Value Fund and the Santa Barbara Large Cap Growth Fund remains. A Large Cap Growth manager search to evaluate alternatives to the Santa Barbara Fund will be prepared and delivered at the August 2012 board meeting.

Mr. Davison discussed the liquidation timing for the Landmark Value Strategies Fund. We expect to receive the majority of the SERS allocation back at the end of 2012. An early exit was discussed between the Hyas Group and Mr. Griffin but it was determined that there was not much value in Landmark's proposed early exit terms.

The Board was briefed on a recent ownership change for the current SERS custodian. Union Bank's custodial operations were purchased by U.S. Bank. It is not expected that this change will have any major impact on the SERS relationship. Mr. Griffin stated that U.S. Bank was a strong second place finalist when the custodial search was conducted a few years ago and the core team that services our account at Union Bank is moving to U.S. Bank.

Vanguard Short-term Investment Grade Admiral Fund

The Board was briefed on a recent change in Vanguard's pricing structure for the Short-term Investment Grade mutual fund. Mr. Davidson recommended transitioning the assets in the Vanguard Short-term Bond Fund Admiral share class to the Vanguard Short-term Bond Institutional share class due a lower fee structure now available in the Institutional share class.

Jerry McFarlane moved and Steve Sather seconded the motion to transition the assets in the Vanguard Short-term Bond Fund Admiral share class to the Vanguard Short-term Bond Institutional share class. The motion passed unanimously.

Board Election Results

The Board was informed that Bill Todd was reelected to his Board seat. His term will start July 2, 2012 and expire on July 5, 2015.

Mr. Griffin, Mr. Dowd, Mr. Reid, Mr. Davidson and Mr. Brown left the meeting at 2:25 pm.

Minutes of the April 25, 2012 Meeting

Mike Coster moved and Jon Snyder seconded the motion to approve the minutes of the April 25, 2012 meeting as distributed. The motion passed unanimously.

Service Retirements

Name	Age	Retirement Date	Years of Service	Option	30-day Notice
William Poffenroth	51	04/29/2012	14.8	E	N
Casey Booley III	51	04/29/2012	16.6	E	N
Rocco Treppiedi	59	05/02/2012	9.9	ST	N
Roy "Frank" Triplett	62	06/02/2012	35.0	E	Y
Gregory L. Martin	59	06/19/2012	33.5	ST	Y
Edward T. Bowers	61	06/23/2012	27.8	ST	Y
Patricia G. Hall	60	06/30/2012	17.8	E	Y
Travis Wilbourn	61	07/07/2012	23.0	D	Y
Richard L. Starr Jr.	65	07/07/2012	26.7	ST	Y

Steve Sather moved and Jerry McFarlane seconded the motion to approve the service retirements as presented on the May Retirement Transaction Report. The motion passed unanimously.

Withdrawals for May 2012

Name	Termination Date
Larry S. Bliesner	03/22/2009
Stephanie L. Hughes	03/14/2012
Kim A. Godfrey	04/27/2012

Steve Sather moved and Mike Coster seconded the motion to approve the request for withdrawal as presented on the May Retirement Transaction Report. The motion passed unanimously.

Deaths

Name	Date of Death	Age	Information
Evelyn Dinsmore	04/20/2012	94	No Further Benefit
Wilbert Hoff	04/27/2012	83	No Further Benefit
Helen Blackwell	05/15/2012	91	No Further Benefit

Death information was provided to the Board for review.

Director's Report

Expenditure Summary Report – April 2012

The Expenditure Summary Report was presented to the Board and discussed. Ms. Ellingson informed the Board that administrative expenses, through April 30, 2012, are 24% less than the same period last year.

Steve Sather moved and Dean Kiefer seconded the motion to approve the April 2012 Expenditure Summary Report. The motion passed unanimously.

Schedule of Investments – April 2012

The monthly investment report was presented to the Board for review. The estimated market value (MV) of the SERS portfolio on April 30, 2012 was \$240.2 million.

Inland Northwest Investors Update – Local Investment

Ms. Ellingson informed the Board that the last investment held within the Inland Northwest Investors, LP fund was written off by the fund and the fund itself was dissolved in spring, 2012. This fund was designed to target “local investments” with initial funding occurring approximately 17 years ago. The fund was scheduled to terminate circa 2005, but the sunset date was extended multiple times when problems arose with liquidating some of the investments. The fund has not provided any cash flow for a number of years. The carrying value of the fund was written off by SERS over five years ago.

There being no other business, the meeting adjourned at 2:36 p.m.

/s/

Leo F. Griffin, Retirement Director