

**MINUTES OF THE  
TEXAS MUNICIPAL RETIREMENT SYSTEM  
Special Meeting of the Board of Trustees**

**October 29, 2008**

On October 29, 2008, the Board of Trustees of the Texas Municipal Retirement System (TMRS) convened for a special meeting at 11:30 a.m. at the San Antonio Marriott Rivercenter Hotel, 101 Bowie Street, San Antonio, Texas, with the following members present:

**Board of Trustees**

Roel ("Roy") Rodriguez

Ben Gorzell, Jr.

April Nixon

H. Frank Simpson

Pat Hernandez

Absent: Carolyn Linér, Vice Chair

Present also were:

Eric Henry, Executive Director and CIO

Ian Allan, Director of Internal Audit

Rhonda Covarrubias, Director of Finance

Eric Davis, Deputy Executive Director

Bernie Eldridge, Director of Human Resources

David Gavia, General Counsel

Nancy Goerdel, Director of Public Investments and Asset Allocation

Leslee Hardy, Staff Actuary

Holly Macki, Director of Fixed Income

Michelle Mellon-Werch, Associate General Counsel

Cindy Morse, Executive Assistant

Debbie Munoz, Director of Member Services

Kristin Qualls, Investment Analyst

Eddie Solis, Director of Government Relations

Bill Wallace, Director of Communications

Bob Klausner, Klausner & Kaufman, PA

Nancy Williams, Ennis Knupp

Jeanna Cullins, Ennis Knupp

Mark Randall, Gabriel, Roeder, Smith and Company

Joe Newton, Gabriel, Roeder, Smith and Company

Russ Kuhns, R. V. Kuhns & Associates, Inc.

Jonathan Kowolick, R. V. Kuhns & Associates, Inc.

Peter Madsen, R. V. Kuhns & Associates, Inc.

Guests:

Jim Moore, Assistant Fire Chief, City of Mesquite

Greg Vick, Assistant City Manager, City of Farmers Branch

Jim Parrish, Director of Human Resources, City of Amarillo

Bob Scott, Director of Finance, City of Carrollton

Darlene Lanham, TMPA

Steve Potter, Northern Trust Global Investments

Michael Vardas, Northern Trust Global Investments

Donald Pollack, Northern Trust Global Investments  
Jason Pasquinelli, Northern Trust Global Investments  
Richard Clark, Northern Trust Global Investments

The meeting was called to order at 11:30 a.m. and the invocation was given by Pat Hernandez.

**Consider and Act on Temporarily Conducting Committee Business at the Board Level**

Mr. Henry explained that many of the items being heard before Board Committees such as investment matters and the enterprise risk management process merit the full Board's review. Thus a recommendation to temporarily suspend the use of Board Committees is being made at this time. Mr. Simpson moved that Committee business be temporarily conducted at the Board level. Mr. Gorzell seconded the motion, which passed unanimously.

**Consider and Act on Adoption of Minutes from the Investment Committee and the Finance & Audit Committee Meetings on September 25, 2008, and the Board of Trustees meeting on September 26, 2008**

Mr. Henry presented the Minutes for the September Committee and Board meetings. Mr. Simpson stated that on page 3 of the Investment Committee Minutes, his comments during the meeting were to request additional information in staff presentations relating to board decisions. Mr. Rodriguez asked if any revisions are required and Mr. Simpson said no. Ms. Nixon moved that the Minutes be adopted as presented without any revisions. Ms. Hernandez seconded the motion, which passed unanimously.

**Executive Session**

At 11:34 a.m., the Board entered into Executive Session, pursuant to Texas Government Code, §551.074 to discuss personnel matters. No action was taken during the Executive Session and the meeting was opened to the public again at 12:48 p.m. All members of the Board who had been present when the Board went into Executive Session were again present.

**Governance and Strategic Planning Session**

Ms. Williams began her presentation by stating that there were three things she wanted the Board to discuss: (1) Board Orientation and Education Policy; (2) Role and Responsibilities of the Board; and (3) Strategic Plan. Ms. Williams stated that no action is needed on these items until December.

**Board Orientation and Education Policy**

Ms. Williams said that getting this policy in place will be a great step forward. She mentioned that a suggestion has been made to add a meeting with the actuary to the Board orientation process. Mr. Gorzell thanked Ms. Williams and said that his orientation was a very thorough process. He recommended that each new Board member meet with the Investment Advisor and the Actuary.

**Role and Responsibilities of the Board**

Ms. Williams reminded the Board that she is going to add a preamble to this policy. Some duties of the Board were not set forth in statute, so clarification is needed for this policy. Ms. Williams said it was suggested that hiring investment managers be added to the Board's responsibilities. Another suggestion was to add the hiring and review of Counsel and Internal Auditor to the Board's responsibilities.

### Strategic Plan

Ms. Williams stated that the Board will not change their goals very often; however objectives will change annually. Ms. Williams read several items that could be included in the Strategic Plan, including the Advisory Committee Charter change and role. Ms. Nixon stated that the “communication” item was her suggestion and that she felt an item on the current plan covers her suggestion, as long as the communication initiatives continue. Mr. Henry explained our current communication activities and said that this communication campaign with cities will continue. He reported that it is critical to continue the seminars with added focus on funding and funding workshops. Mr. Henry also discussed the “pension spiking” item. He stated that the Board did take action on this in the past. Mr. Simpson stated that his intent was to educate cities on the impact of Updated Service Credit (USC). The other issue dealt with TMRS’ financial backing of municipal bonds. Mr. Rodriguez stated his opinion that this is something the Board should wait on. Mr. Gorzell stated that we have a lot of investment portfolio work to do, and this item takes the System in a different direction and, as a result, should be tabled. Ms. Nixon and Ms. Hernandez both expressed their preference to delay this item. Mr. Kuhns was asked if other funds are doing this. He stated that other funds are investing in infrastructure, but no funds are backing or underwriting bonds. The infrastructure investments are akin to real estate investments. Mr. Klausner discussed legal issues around similar targeted investments in other states. The Board’s pleasure seemed to be to table this item until spring. Mr. Henry suggested this be part of the asset allocation discussions. He pointed out the distinction between investing in infrastructure and bond underwriting.

### Report on Investment Performance as of September 30, 2008

Mr. Madsen discussed the fund’s asset allocation and year-to-date performance. Based on the current allocation, TMRS is in the top 4 percentile, and possibly the top performing plan in the United States based on the high portion of the portfolio in bonds. Mr. Kuhns showed the rolling 1-year periods, and stated that TMRS’ timing is right, and what we are doing is positive.

### Report on Financial Markets and Fixed Income Investments

Ms. Macki gave the Board an update on the fixed income portfolio. She began with a timeline of recent events affecting financial markets since September 1. Both the fixed income and equity markets have been extremely volatile. The Federal Reserve’s short term funding activities has provided some relief to the markets. The one-year performance of the market is the worst performance across many indices. Ms. Macki then showed the current progress on the Blackrock mandate to decrease duration of the fixed income portfolio and, where possible, increase yield. She stated that if we had not shortened duration, the portfolio would have had a larger unrealized loss. Ms. Macki closed her presentation by saying shortening duration has served us well and that we have been able to exploit buying opportunities.

### Report by Equity Index Fund Manager

At 1:56 p.m., the Board took a short lunch break. The meeting resumed, with the same people present prior to the lunch break, at 2:15 p.m.

Northern Trust representatives provided an overview of their company. They then proceeded to explain the impact of the current financial crisis on the securities lending program of the index funds that Northern Trust manages for TMRS. With regard to securities lending, these are unprecedented times. In past crises, the LIBOR spreads were in the 30-40 point range; today, those spreads are 300 points. An example of the securities lending transactions was given. Security loans are typically very short term. The weighted average life is 24 days – measured by

interest sensitivity. The weighted average maturity of the open loan is 169 days. Northern Trust representatives stated that because of the credit crisis it was necessary to declare a collateral deficiency in the collateral pools that support the securities lending program and to assess TMRS and the other shareholders of the index funds for the decline in the market value of the collateral pool. According to Northern Trust, the collateral pool is currently highly liquid and of high quality. Over time, Northern Trust hopes that the impaired securities in the collateral pool will mature at par. At the conclusion of the presentation, Mr. Henry stated, from his perspective, there are three directions that TMRS can go: (1) do nothing and remain invested in the funds; (2) take an in-kind pro-rata portion of the collateral pool and manage it ourselves; or (3) cash out our investment in the index funds and recognize the loss.

### **Executive Session**

At 3:15 p.m., the Board entered into Executive Session, pursuant to Texas Government Code, § 551.071 to consult with Legal Counsel and to receive legal advice. No action was taken during the Executive Session and the meeting was opened to the public again at 3:57 p.m. All members of the Board who had been present when the Board went into Executive Session were again present.

### **Consider and Act on Changes to Northern Trust Global Investments Contract**

Mr. Henry presented the background information. Mr. Simpson moved that the Board of Trustees direct the Executive Director to negotiate a change in the contract with Northern Trust Global Investments for management of the Russell 3000 and EAFE commingled index funds, to commit new funds to commingled or separately managed Northern Trust index funds that do not participate in securities lending and at fees not to exceed 2 basis points for the Russell 3000 Index fund and 3 basis points for the EAFE Index fund and to retain the current funds in the Northern Trust lending funds; the Board further delegates to the Executive Director the authority to take such action as necessary to protect the System's interests, including but not limited to withdrawing TMRS funds from the Northern Trust lending funds and talking collateral assets in-kind should the need arise. Mr. Gorzell seconded the motion, which passed unanimously.

### **Review and Discuss Actuarial Assumptions for December 31, 2008 Actuarial Valuation; Discuss Reserve Policy**

Mr. Randall began by stating that GRS typically would not begin working with a new client and recommend assumption changes. However, he believes that two assumptions need immediate attention for the next valuation: (1) immediately implementing the salary scale; and (2) explicitly valuing the COLAs. A third item, the discount rate, will continue to be reviewed in light of the reserving policy. Mr. Newton pointed out that with regard to COLAs, the Partial Lump Sum Distribution use rate needs to be taken into account. Mr. Simpson asked if this was the correct time to implement a change in the salary scale assumption. GRS responded that it was. The Board will be asked to act on the actuarial assumptions at the December Board meeting.

Mr. Randall next began discussing a potential reserve policy. One premise to remember is that over the long term, it is expected that the entire fund will earn 7%; if this is the case, the MAF can be granted more than 7% (perhaps 7.5%); and if this is the case, gain sharing could occur in the future. GRS will continue to work with staff and board on an appropriate level of reserves. By combining reserves and smoothing, we will be able to lower the reserve required to mitigate contribution volatility. The policy needs to be flexible. The smoothing policy will develop two asset figures – the actual and the smoothed value.

After discussing the modeling GRS has done on the reserve policy, Mr. Newton pointed out that based on this work, GRS' recommendation would be to use a discount rate in the range from 7% to 8%, likely at 7.5%.

**Municipality Accumulation Fund Analysis**

Mr. Randall briefly discussed the MAF analysis work that will be done going forward. This work will test to determine if there are any cash flow problems given certain assumptions. This information will be used to communicate with cities regarding their funding status.

**Review and Discuss Preliminary 2009 Operating Budget**

After some discussion, it was decided that this budget will be brought back to the Board at the December meeting.

**Consider and Act on General Counsel Job Description**

It was decided that this item will be brought back to the Board at the December meeting.

**Call for Future Agenda Items**

There were no proposed agenda items for future meetings. As there was no further action, the meeting was adjourned at 5:08 p.m.



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Eric Henry  
Executive Director and  
Chief Investment Officer



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Roel ("Roy") Rodriguez  
Chair, Board of Trustees