

MINUTES OF THE SPECIAL BOARD MEETING OF THE
 BOARD OF TRUSTEES OF THE EMPLOYEES' RETIREMENT SYSTEM (ERS)
 THURSDAY, OCTOBER 11, 2012
 HAWAII PRINCE HOTEL WAIKIKI, MAUNA KEA BALLROOM
 HONOLULU, HAWAII

ROLL CALL	Trustees present:	Mr. Colbert Matsumoto, Chair Mr. Emmit Kane, Vice Chair Mr. Vincent Barfield Ms. Piliialoha Lee Loy Mr. Wayne Yamasaki Mr. Kalbert Young	
	Trustees excused:	Ms. Jackie Ferguson-Miyamoto Mr. Jerome Rauckhorst	
	Attorney present:	Ms. Diane Kishimoto, Deputy Attorney General	
	Staff present:	Mr. Wesley Machida, Administrator Ms. Kanoë Margol, Assistant Administrator Mr. Vijoy Chattergy, Interim Chief Investment Officer Mr. Ajay Umanikar, Investment Specialist Ms. Donna Curry, Program Specialist Ms. Gerri Konishi, Member Home Loan Assistant Ms. Jaime Hirata, Recording Secretary Ms. Wanda Kugiya, Secretary	
	Guests present:	Mr. Richard Lim (Director)) State of Hawaii Department of Business, Economic Development, & Tourism
		Mr. Nandana Kalupahana (Committee Clerk)) State of Hawaii House Committee on Finance
		Mr. Pawan Chaturvedi (via conference call)) Altius Associates
		Mr. Michael Humphrey Mr. Dan Moore) Courtland Partners
		Mr. Pete Fawcett Mr. Jim Proud Mr. Paul Rezens Mr. Ryan Tripton) Heitman Capital Management
		Mr. Jeff Cavanaugh Ms. Deirdre Perez) Invesco Real Estate
		Mr. Jim Hutchinson Ms. Allison McFaul Ms. Kristin Schneider) LaSalle Investment Management

Mr. Neil Rue
Mr. John Linder

) Pension Consulting Alliance

QUORUM/CALL TO ORDER

A quorum being present, Chair Matsumoto called the special meeting of the Board of Trustees of the Employees' Retirement System of the State of Hawaii (the Board) to order at 8:42 a.m., in the Mauna Kea Ballroom at the Hawaii Prince Hotel Waikiki.

ENTRY INTO EXECUTIVE SESSION

On a motion made by Trustee Barfield, seconded by Trustee Kane, and unanimously carried, the Board entered into executive session:

- Pursuant to HRS § 92-5(a)(8), to hear a status report regarding the Royal Ka'anapali Golf Courses and to consider, deliberate, and act on any proposals from Heitman Capital Management;
- Pursuant to HRS § 92-5(a)(8), to consider and, if appropriate to make a decision regarding private equity policy revisions;
- Pursuant to HRS § 92-5(a)(2), and (8), to hear the findings and recommendations of the ad hoc Chief Investment Officer Search committee; and
- To approve executive session minutes of the special meeting of October 25, 2011 and the regular meeting of May 15, 2012.

(Trustee Kane left the meeting.)

EXECUTIVE SESSION TO HEAR A
STATUS REPORT REGARDING THE
ROYAL KA'ANAPALI GOLF
COURSES AND TO CONSIDER,
DELIBERATE, AND ACT ON ANY
PROPOSALS FROM HEITMAN
CAPITAL MANAGEMENT

(Trustee Kane returned to the meeting.)

EXECUTIVE SESSION TO
CONSIDER AND, IF APPROPRIATE
TO MAKE A DECISION
REGARDING PRIVATE EQUITY
POLICY REVISIONS

(Mr. Chattergy, Mr. Umaranikar, Ms. Kugiya, and Ms. Konishi left the room.)

EXECUTIVE SESSION TO HEAR
THE FINDINGS AND
RECOMMENDATIONS OF THE AD
HOC CHIEF INVESTMENT OFFICER
SEARCH COMMITTEE

(Mr. Chattergy, Mr. Umaranikar, Ms. Kugiya, and Ms. Konishi returned to the room.)

EXECUTIVE SESSION TO APPROVE
THE EXECUTIVE SESSION
MINUTES OF THE SPECIAL
MEETING OF OCTOBER 25, 2011
AND THE REGULAR MEETING OF
MAY 15, 2012

EXIT EXECUTIVE SESSION

On a motion made by Trustee Kane, seconded by Trustee Lee Loy, and unanimously carried, the Board exited from executive session.

APPROVAL OF BOARD MEETING
MINUTES – OCTOBER 25, 2011 AND
MAY 15, 2012

On a motion made by Trustee Kane, seconded by Trustee Lee Loy, and unanimously carried, the Board approved the minutes of the special Board meeting of October 25, 2011. Consideration of the minutes of the regular Board meeting of May 15, 2012 was deferred.

MELLON CAPITAL LARGE CAP
GROWTH AND LARGE CAP VALUE
INDEX DUE DILIGENCE REVIEW

Mr. Neil Rue and Mr. John Linder of Pension Consulting Alliance (PCA), ERS's investment consultant, and Mr. Vijoy Chattergy, ERS's Interim Chief Investment Officer, reported on the onsite due diligence meeting conducted by Mr. Linder and Mr. Chattergy at Mellon Capital Management (Mellon) in connection with the selection of Mellon as the manager for Passive Large Cap Growth Equity and Passive Large Cap Growth Value Equity. Mr. Linder and Mr. Chattergy reported that there were no material findings that would preclude Mellon from successfully managing the assets of the ERS in the Passive Large Cap Growth Equity and Passive Large Cap Growth Value Equity strategies.

INVESTMENT MANAGER AND
CONSULTANT ORGANIZATIONAL
CHANGES

Mr. Chattergy reported on the organizational changes of the following firms:

- Altius Associates (private equity non-discretionary consultant) – the search for a replacement for Garth Troxell is ongoing; Altius expects to fill the position by the end of the year.
- First Hawaiian Bank (fixed income manager) – the client service officer for the ERS will be leaving the company; no change in the investment officer for the ERS's account.

INVESTMENT MANAGER
MEETINGS FOR 3RD QUARTER, 2012

Mr. Chattergy reported on the investment meetings he attended with managers under contract with the ERS and potential investment managers, as well as other service providers in the third quarter of 2012.

INVESTMENT OFFICE ACTIVITIES
– OCTOBER 2012

Mr. Chattergy reported on the status of the activities of the Investment Office during October 2012. Highlights included:

- Investment managers on “Watch Status”
 - Bank of Hawaii
 - Mercator
 - Oechsle
 - PIMCO
 - QMA
 - Systematic Financial
- 3 transitions for completion by end of October 2012
 - Rebalance non-US equities
 - Large-cap growth passive to large-cap growth active
 - Large-cap value active to large-cap value passive
- PCA will manage the Request for Information (RFI) for the transition manager pool. Selection and contracting tentatively scheduled for January/February 2013.
- Bank custodian contract expires March 31, 2013; ERS staff will manage the Request for Expression of Interest (EOI).
- Mr. Chattergy and Trustee Kane will attend the Blackstone Real Estate Partners LP Conference that will be held in New York, November 7-9, 2012.

INVESTMENT OFFICE MANAGER
MEETING AND CONFERENCE
SCHEDULE - 2013

Mr. Chattergy presented a proposed schedule of investment manager due diligence site inspections and investment conferences through the calendar end of 2013. ERS *Investment Meeting Policy*, directs ERS staff to conduct on-site meeting at the offices of its investment managers once every two years, and requires ERS staff attendance at several industry conferences.

2012 ERS INVESTMENT POLICY
AND PROCEDURES MANUAL

Mr. Chattergy presented the revised 2012 ERS *Investment Policies & Procedures Manual*. The revised manual includes a reorganization of content sections and formatting in a more logical and efficient structure, as well as all policies, guidelines, and procedures adopted by the Board since the previous comprehensive issuance of the document in 2006.

On a motion made by Trustee Barfield, seconded by Trustee Lee Loy, and unanimously carried, the Board approved the 2012 ERS *Investment Policies & Procedures Manual* as presented.

ERS SECURITIES LENDING
GUIDELINES POLICY REVISION

Mr. Chattergy presented to the Board for approval proposed revisions to the Securities Lending Guidelines, which are included in the ERS *Investment Policies & Procedures Manual*. The revisions were recommended by Northern Trust to ensure that ERS's guidelines conform to SEC rules and standards.

On a motion made by Trustee Barfield, seconded by Trustee Lee Loy, and unanimously carried, the Board approved the revisions to the ERS's Securities Lending Guidelines, as presented.

2012 ERS DERIVATIVES EXPOSURE
REPORT

Mr. Rue presented PCA's report on PCA's verification of investment manager compliance with the ERS's Derivatives Policy in the fiscal year ending June 30, 2012. PCA received and reviewed the annual "Certification of Compliance with ERS' Derivatives Guidelines section C.3.C" from twenty of ERS's funded managers. One manager, Mellon Capital responded to PCA's inquiry, but did not certify that it complied with the ERS's guidelines because the ERS's investment with Mellon Capital is in commingled funds, which are subject to the funds' own investment guidelines. Seven of the managers surveyed used derivatives during the period; of these managers, four had compliance caveats that have either been resolved or are being addressed.

2011 ERS COMMISSION
RECAPTURE PROGRAM

Mr. Rue presented a summary of PCA's review of the ERS's Commission Recapture Program activity for calendar year 2011. PCA recommended that the ERS expand the list of participating brokers and that the ERS provide written notification annually to each of the participating investment managers summarizing ERS's Commission Recapture Program requirements.

COMMISSION RECAPTURE
BROKER SEARCH

Mr. Rue presented an estimated timeline to expand the list of participating brokers in ERS's Commission Recapture Program in an effort to increase manager participation. Current brokers utilized are Knight Capital Group, BNY ConvergeEx (Lynch, Jones, and Ryan), and Rockdale Securities. PCA will manage the Request for Information (RFI) to expand the list of participating brokers. PCA plans to present their recommended finalist candidates to the Board by December 2012, with final contract negotiation with the selected finalist anticipated for March/April 2013. The Administrator noted that the Board has the option to interview the finalists.

Mr. Rue also presented PCA's recommendation for amendment of the ERS's Commission Recapture Policy to clarify directed trading requirements for passive versus active mandates.

On a motion made by Trustee Lee Loy, seconded by Trustee Kane, and unanimously carried, the Board approved the recommended amendments to the ERS's Commission Recapture Policy as presented.

WESTERN ASSET MANAGEMENT
COMPANY'S REQUEST FOR
EXEMPTION FROM POLICY
RESTRICTION RELATED TO
DOWNGRADED SECURITY

Mr. Rue and Mr. Chattergy presented the request by Western Asset Management Company (WAMCO) to continue holding a recently downgraded issue that will bring portfolio concentration of below B-rated bonds exposure to 2.176% over the 2.0005 policy threshold.

On a motion made by Trustee Kane, seconded by Trustee Lee Loy, and unanimously carried, the Board approved WAMCO's request to continue holding the downgraded security.

SUDAN DIRECT HOLDINGS
DIVESTMENT

Mr. Chattergy reported on the ERS holding of Caterpillar Inc. (CAT), which is classified as a *Scrutinized* company on the Conflict Risk Network (CRN) list of *Scrutinized* companies with direct holdings in Sudan. Pursuant to Act 192, SLH 2007 and the ERS Sudan Investment Policy, the Board has several options, including:

- Continue holding the scrutinized company based on the Board's discretion pursuant to Act 192, Section 4(a)(4); or
- Divestment of scrutinized company, pursuant to Act 192, Section 4(b).

On a motion made by Trustee Kane, seconded by Trustee Barfield, and unanimously carried, the Board approved to divestment of direct holdings of Caterpillar Inc.

PRESENTATION BY COURTLAND
PARTNERS ON THE ERS REAL
ESTATE INVESTMENT PORTFOLIO
PERFORMANCE FOR SECOND
QUARTER 2012

Mr. Michael Humphrey and Mr. Dan Moore of Courtland Partners (Courtland), ERS's real estate investment consultant, presented Courtland's report on the ERS's real estate investment portfolio performance for the 2nd quarter of 2012. Highlights included:

- Current market value of the real estate portfolio is \$941,481,498.00
- Internal rate of return (IRR) of 6.7%; up 20 basis points

RECESS

Chair Matsumoto called a 10-minute recess at 10:50 a.m.

RECONVENE

Chair Matsumoto reconvened the meeting at 11:15 a.m.

PRESENTATION BY COURTLAND
PARTNERS ON REAL ESTATE
MARKET CONDITIONS

Mr. Humphrey and Mr. Moore gave a presentation on real estate market conditions; representatives from the ERS's real estate investment managers participated in the discussion.

RECESS

Chair Matsumoto called a recess for lunch at 12:15 p.m. and announced that the meeting would reconvene in the Mauna Kea Ballroom at 1:00 p.m.

RECONVENE

Chair Matsumoto reconvened the meeting at 1:30 p.m.

ENTRY INTO EXECUTIVE SESSION

On a motion made by Trustee Lee Loy, seconded by Trustee Kane, and unanimously carried, the Board entered executive session:

- Pursuant to HRS § 92-5(a)(8), to hear, consider, deliberate, and act upon the portfolio performance review presented by Heitman Capital Management;
- Pursuant to HRS § 92-5(a)(8), to hear, consider, deliberate, and act upon the portfolio performance review presented by LaSalle Investment Management; and
- Pursuant to HRS § 92-5(a)(8), to hear, consider, deliberate, and act upon the portfolio performance review presented by Invesco Real Estate.

EXECUTIVE SESSION TO HEAR,
CONSIDER, DELIBERATE, AND
ACT UPON THE PORTFOLIO
PERFORMANCE REVIEW
PRESENTED BY HEITMAN
CAPITAL MANAGEMENT

(Trustee Young left the meeting at 2:45 p.m. and did not return for the remainder of the meeting.)

EXECUTIVE SESSION TO HEAR,
CONSIDER, DELIBERATE, AND
ACT UPON THE PORTFOLIO
PERFORMANCE REVIEW
PRESENTED BY LASALLE
INVESTMENT MANAGEMENT

EXECUTIVE SESSION TO HEAR,
CONSIDER, DELIBERATE, AND
ACT UPON THE PORTFOLIO
PERFORMANCE REVIEW
PRESENTED BY INVESCO REAL
ESTATE

(Trustee Lee Loy left the meeting at 4:25 p.m. The remaining Trustees did not constitute a quorum; however, pursuant to HRS § 92-2.5(d), the Board continued to receive presentations and questions from the presenters on the remaining items on the agenda.)

EXIT EXECUTIVE SESSION

There being no further presentations for items to be considered in executive session, the Board exited from executive session.

RECESS

There being no further business, Chair Matsumoto adjourned the meeting at 5:00 p.m.

**REDACTED
SIGNATURE**

Wesley K. Machida
Administrator

WKM: jh