

MINUTES OF THE REGULAR BOARD MEETING OF THE
BOARD OF TRUSTEES OF THE EMPLOYEES' RETIREMENT SYSTEM (ERS)
DECEMBER 10, 2012
CITY FINANCIAL TOWER, 201 MERCHANT STREET, SUITE 1935
HONOLULU, HAWAII

Trustees present: Mr. Colbert Matsumoto, Chair
Mr. Vincent Barfield
Ms. Piliialoha Lee Loy
Mr. Jerome Rauckhorst
Mr. Wayne Yamasaki
Mr. Kalbert Young

Trustees excused: Mr. Emmit Kane, Vice Chair
Ms. Jackie Ferguson-Miyamoto

Attorneys present: Mr. Brian Aburano, Deputy Attorney General
Ms. Diane Kishimoto, Deputy Attorney General

Staff present: Mr. Wesley Machida, Administrator
Ms. Kanoe Margol, Assistant Administrator
Mr. Vijoy Chattergy, 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. Paul Anderson) Gateway Investment Advisers
Mr. Michael Buckius

Mr. John Lender) Pension Consulting Alliance
Mr. Neil Rue

CALL TO ORDER/QUORUM

A quorum being present, Mr. Colbert Matsumoto, Chair of the Board of Trustees of the Employees' Retirement System (ERS), called the regular meeting of the Board of Trustees of the ERS (the Board) to order at 10:04 a.m.

APPROVAL OF BOARD MEETING
MINUTES

- JULY 17, 2012
- AUGUST 13, 2012

On a motion made by Trustee Lee Loy, seconded by Trustee Barfield, and unanimously carried, the Board approved the minutes of the July 17, 2012 and August 13, 2012 Board meetings.

PRESENTATION BY PENSION
CONSULTING ALLIANCE ON
THEIR REVIEW OF THE ERS'S
COVERED CALLS PROGRAM

Mr. John Linder and Mr. Neil Rue of Pension Consulting Alliance (PCA), ERS's general investment consultant, presented PCA's review of the ERS's Covered Calls Program:

The program was fully funded as of December, with one manager (Gateway Investment Advisers) under two mandates: replication (matching the rules-based benchmark) at 80% of allocation and non-replication (seeking to outperform the benchmark) at 20% of allocation. The program is meeting expectations. The replication mandate has tracked the benchmark with a modest lag. The non-replication mandate has done very well in adding value.

PCA recommended that the Covered Calls Program be allowed to run before new managers or new strategies are added; however, PCA recommended that the ERS consider shifting the allocation of 80% replication / 20% non-replication to 50% / 50%.

PRESENTATION BY GATEWAY
INVESTMENT ADVISERS ON THE
PERFORMANCE OF THE ERS'S
COVERED CALLS INVESTMENT
PORTFOLIO

Mr. Paul Anderson and Mr. Michael Buckius of Gateway Investment Advisers (Gateway), presented a performance review of the ERS's investments in the covered calls portfolio managed by Gateway for the ERS.

On a motion made by Trustee Lee Loy, seconded by Trustee Barfield, and unanimously carried, the Board approved changing the allocation of the covered calls portfolio managed by Gateway to 50 % replication and 50 % non-replication.

PRESENTATION BY PENSION
CONSULTING ALLIANCE ON RISK
MANAGEMENT AND STRATEGIC
CLASSES

Mr. Linder and Mr. Rue presented PCA's report on risk management and strategic classes. PCA recommended the following:

1. Consolidate public equity classes into a broader growth oriented class that also contains assets exposed to growth risk (high yield, credit, opportunistic debt, other market dislocators; and
2. Revisit objectives for the fixed income class:
 - eliminate/materially reduce exposure to credit/growth risk
 - maintain very broad opportunity set
 - keep risk in this class low
 - longer-term possibilities, consider event risk participation strategies.

PCA will be presenting structural recommendations for the growth class in the first quarter of 2013 and for the fixed income class in the second quarter of 2013.

RECESS

Chair Matsumoto called a recess for lunch at 11:39 a.m.

RECONVENE

Chair Matsumoto reconvened the meeting to order at 12:08 p.m.

ENTRY INTO EXECUTIVE SESSION

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

- Pursuant to HRS § 92-5(a)(8), to consider and, if appropriate, to make a decision regarding the draft of the internal audit report by KMH LLP;
- To approve executive session minutes of the July 17, 2012 and August 13, 2012 Board meetings; and
- Pursuant to HRS § 92-5(a)(4), to consult with the ERS's attorneys on questions and issues pertaining to the ERS's powers, duties, privileges, immunities and liabilities with respect to the possible filing of a claim against Toyota Corporation in Japan, and setting policies and procedures regarding the filing of securities claims in non-U.S. courts; discussion and appropriate action.

The Administrator reported that it would not be necessary to consult with counsel at this meeting regarding legislative proposals affecting the ERS.

EXECUTIVE SESSION TO
CONSIDER AND, IF APPROPRIATE,
TO MAKE A DECISION
REGARDING THE DRAFT OF THE
INTERNAL AUDIT REPORT BY
KMH LLP

APPROVAL OF EXECUTIVE
SESSION BOARD MEETING
MINUTES

- JULY 17, 2012
- AUGUST 13, 2012

EXECUTIVE SESSION TO CONSULT
WITH THE ERS'S ATTORNEYS ON
QUESTIONS AND ISSUES
PERTAINING TO THE ERS'S
POWERS, DUTIES, PRIVILEGES,
IMMUNITIES, AND LIABILITIES
WITH RESPECT TO THE POSSIBLE
FILING OF A CLAIM AGAINST
TOYOTA CORPORATION IN JAPAN,
AND SETTING POLICIES AND
PROCEDURES REGARDING THE
FILING OF SECURITIES CLAIMS IN
NON-U.S. COURTS

EXIT EXECUTIVE SESSION

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

(Mr. Linder and Mr. Rue returned to the meeting.)

INVESTMENT MANAGERS ON
“WATCH STATUS”

Mr. Vijoy Chattergy, ERS’s Chief Investment Officer (CIO), reported that PCA recommended that Oechsle International Advisors LLC (Oechsle) and Pacific Investment Management Company (PIMCO) be removed from the watch list. Oechsle is an active international fixed income portfolio investment manager. PIMCO is an active core plus fixed income portfolio manager. Oechsle and PIMCO were placed on the watch list in March 2012 due to underperformance. While on the watch list, due diligence site inspections and quarterly conference calls with each manager were completed with no findings of irregularities. As of September 30, 2012, Oechsle and PIMCO had exceeded all of the ERS’s Investment Performance Watch Criteria. ERS staff and PCA recommended removal of Oechsle and PIMCO from the watch list due to improved performance.

On a motion made by Trustee Lee Loy, seconded by Trustee Barfield, and unanimously carried, the Board approved removal of Oechsle and PIMCO from the watch list.

POLICY FOR NON-MATERIAL
INVESTMENT-RELATED ACTION
REQUESTS

The CIO presented a draft policy (Non-Material Investment Related Action Requests Policy) for inclusion as a part of the ERS *Investment Policy, Guidelines, & Procedures Manual*. The proposed policy permits action on non-material portfolio management matters that periodically occur to be conducted at the staff level with *post-hoc* reporting to the Board. The policy would be inserted in Section B.5, under the responsibilities of the CIO.

On a motion made by Trustee Barfield, seconded by Trustee Rauckhorst, and unanimously carried, the Board approved the proposed Non- Material Investment Related Action Requests Policy , as presented, for inclusion as part of the ERS *Investment Policy, Guidelines, & Procedures Manual* in Section B.5.

REQUEST FOR PROPOSALS FOR
INTERNAL AUDIT CONSULTANT
SERVICES

The Administrator reported on the status of the ERS’s Request for Proposals (RFP) for consultant services related to the establishment of an internal audit function for the ERS. The Administrator reported that the ERS received two responses to the RFP that was issued in November 2012. The ERS’s existing contract with KMH will expire on January 31, 2013; therefore, the selection process will be completed in January, with early February as the target for commencement of the new contract.

REQUEST FOR PROPOSALS FOR
PRIVATE EQUITY INVESTMENT
CONSULTANT SERVICES

Mr. Rue announced that PCA would not be submitting a proposal in response to the RFP for private equity investment consultant services.

The Administrator reported on the status of the ERS’s RFP for private equity investment consultant services. The Administrator reported that the ERS received 13 responses to the RFP that was issued in November 2012; responses are due on December 19, 2012. The Administrator requested the appointment of an ad-hoc committee to evaluate the responses and recommend a list of finalists for the Board’s consideration and selection. Interviews of the finalists are

scheduled for late January 2013.

On a motion made by Trustee Yamasaki, seconded by Trustee Young, and unanimously carried, the Board created an ad-hoc committee to work ERS staff to evaluate the responses to the RFP and select finalists to recommend to the Board for consideration and selection. Chair Matsumoto appointed the following trustees to the ad-hoc committee to serve as its members:

- Trustee Barfield, Chair
- Trustee Lee Loy, Vice Chair
- Trustee Rauckhorst
- Trustee Young (alternate)

OPERATIONS REPORT

The Administrator reported on the status of ERS operations for the months of October 2012 and November 2012. Highlights included:

- Fiscal year 2010 Audit is expected to be completed early January 2013 and the fiscal year 2011 Audit is currently underway.
- Revised Overpayment procedures completed and approved by the Board at the November 13, 2012 Board meeting.
- Completed letters to former elected officials who lost this past election and addressed unique situations for certain individuals.
- 4th Quarter 2012 issue of the ERS's newsletter, Holomua, was sent to active members and retirees December 2012. The newsletter included a section from the State of Hawaii Employer Union Trust Fund (EUTF).

NEXT BOARD MEETING –
JANUARY 14, 2013

Chair Matsumoto announced that the next Board meeting is scheduled for January 14, 2013.

ADJOURNED AT 1:09 P.M.

On a motion made by Trustee Lee Loy, seconded by Trustee Rauckhorst, and unanimously carried, the Board adjourned the meeting at 1:19 p.m.

REDACTED SIGNATURE

Wesley K. Machida
Administrator

WKM: jh