

MINUTES OF THE REGULAR BOARD MEETING OF THE
BOARD OF TRUSTEES OF THE EMPLOYEES' RETIREMENT SYSTEM (ERS)

FEBRUARY 10, 2014

CITY FINANCIAL TOWER
201 MERCHANT STREET, SUITE 1200
HONOLULU, HAWAII 96813

Trustees present: Ms. Piliialoha Lee Loy, Chair
Mr. Vincent Barfield, Vice Chair
Ms. Jackie Ferguson-Miyamoto
Mr. Patrick Frane
Mr. Emmit Kane
Mr. Colbert Matsumoto
Mr. Jerome Rauckhorst
Mr. Kalbert Young

Staff present: Mr. Wesley Machida, Executive Director
Ms. Kanoë Margol, Assistant Administrator
Mr. Vijoy Chattergy, Chief Investment Officer
Mr. Andrew Chen, Investment Specialist
Mr. Ian Wetzel, Investment Specialist
Ms. Donna Curry, Program Specialist
Ms. Gerri Konishi, Member Home Loan Assistant
Ms. Jaime Hirata, Recording Secretary
Ms. Raechele Joyo, Secretary
Ms. Wanda Kugiya, Secretary

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

Guests present: Mr. Andy Betz) Macquarie Funds Group (USA) Inc.
Ms. Kay Ceserani) Pension Consulting Alliance, Inc.
Ms. Judy Chambers
Mr. Neil Rue

QUORUM/CALL TO ORDER

A quorum being present, Chair Lee Loy, called the regular meeting of the Board of Trustees of the Employees' Retirement System (the Board), to order at 10:07 a.m.

AMENDMENT OF THE AGENDA

On a motion made by Trustee Ferguson-Miyamoto, seconded by Trustee Matsumoto, and unanimously carried, the Board amended the agenda to add the following:

- Executive Session, pursuant to HRS § 92-5(a)(4), to consult with the Board's attorneys on questions and issues pertaining to the Board's powers, duties, privileges, immunities, and liabilities regarding joining a possible securities fraud action against Saipem S.P.A; appropriate action.

PRESENTATION BY PENSION
CONSULTING ALLIANCE ON THE
EMPLOYEES' RETIREMENT
SYSTEM'S INVESTMENT
PORTFOLIO PERFORMANCE AND
RISK MANAGEMENT REPORTS
FOR 4TH QUARTER 2013

Mr. Neil Rue of Pension Consulting Alliance, Inc. (PCA), ERS's investment consultant, presented PCA's Portfolio Performance and Risk Management Reports of the ERS's investments for the fourth quarter of 2013. Highlights included:

- Aggregate portfolio value of \$13.5 billion as of December 31, 2013; record high for the portfolio.
- Portfolio increased by \$0.6 billion during the fourth quarter and by \$1.6 billion over the latest year.
- Portfolio outperformed the Policy Benchmark return of 5.2% and the Median Public Fund return of 4.8% for the fourth quarter.
- Portfolio outperformed the Policy Benchmark over fourth quarter and 1-year period by 20 and 50 basis points, respectively. Relative outperformance over the 1-year period is largely attributable to the Plan's active Domestic Equity and Fixed Income managers' combined performance exceeding their respective benchmarks, as well as an overweight to Domestic Equity and underweight to Fixed Income versus the policy target. Longer-term performance gaps have begun to narrow as a result of the near-term performance.
- Despite posting positive absolute return over the 3-, 5-, and 10-year periods, the total portfolio trailed the Median Public Fund on a relative basis due to the Plan's active domestic large cap equity managers' performance, primarily in the third quarter of 2011. Differences in strategic allocations also detracted from performance versus the Median Public Fund.
- Risk allocation is currently consistent with asset allocation.
- Growth risk is 75% of the policy portfolio's explainable risk.

In addition, the Board and ERS staff discussed with Mr. Rue, the purpose and the organization of information contained in the quarterly Risk Management Report prepared by PCA for the ERS. In the future, an executive summary of the risk management report will be included in the quarterly performance report to the Board. PCA will continue to provide comprehensive risk management reports to ERS staff.

(Trustee Young joined the meeting.)

PRESENTATION BY PENSION
CONSULTING ALLIANCE, INC. ON
REAL RETURN EDUCATION:
INFRASTRUCTURE

Ms. Judy Chambers of PCA provided an educational presentation on infrastructure within the real return asset class, and discussed the establishment of infrastructure in the ERS's investment portfolio. Highlights included:

- Review of the types of infrastructure and its characteristics.
- Benefits and concerns of infrastructure investments to pension plans.
- Expected risks and returns.
- Ways of investing in infrastructure.
- Current market conditions and forecasts of domestic and global infrastructure investments.
- Canadian participation versus U.S. participation.

There being no further discussion, the representatives from PCA left the room.

ENTER EXECUTIVE SESSION

On a motion made by Trustee Rauckhorst, seconded by Trustee Barfield, and unanimously carried, the Board entered executive session pursuant to HRS § 92-5(a)(4), to consult with the Board's attorneys on questions and issues pertaining to the Board's powers, duties, privileges, immunities, and liabilities regarding the study regarding sharing of investment information and services by the Employer-Union Health Benefits Trust Fund (EUTF) and the ERS.

EXECUTIVE SESSION TO CONSULT
WITH THE BOARD'S ATTORNEYS
ON QUESTIONS AND ISSUES
PERTAINING TO THE BOARD'S
POWERS, DUTIES, PRIVILEGES,
IMMUNITIES, AND LIABILITIES
REGARDING THE STUDY
REGARDING SHARING OF
INVESTMENT INFORMATION AND
SERVICES BY THE EMPLOYER-
UNION HEALTH BENEFITS TRUST
FUND AND THE EMPLOYEES'
RETIREMENT SYSTEM

EXIT EXECUTIVE SESSION

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

AMENDMENT OF THE AGENDA

On a motion made by Trustee Kane, seconded by Trustee Ferguson-Miyamoto, and unanimously carried, the Board amended the agenda to amend item 3 of Executive Session to read as follows (the addition is underscored):

Executive Session, pursuant to HRS § 92-5(a)(4), to consult with the Board’s attorneys on questions and issues pertaining to the Board’s powers, duties, privileges, immunities, and liabilities regarding the study regarding sharing of investment information and services by the Employer-Union Health Benefits Trust Fund and the Employees’ Retirement System; appropriate action.

APPROPRIATE ACTION FOR THE STUDY REGARDING SHARING OF INVESTMENT INFORMATION AND SERVICES BY THE EMPLOYER-UNION HEALTH BENEFITS TRUST FUND AND THE EMPLOYEES’ RETIREMENT SYSTEM

On a motion made by Trustee Rauckhorst, seconded by Trustee Kane, and unanimously carried, the Board: (1) authorized PCA and Mr. J. Thomas Maloney of D’Amato & Maloney LLP, ERS’s tax attorney, to participate in the Director of Finance’s study regarding the sharing of investment information and services by the EUTF and the ERS, and (2) authorized and directed the Executive Director to take such actions as are necessary to provide for such participation and to obtain payment by the Department of Budget and Finance of any additional costs that may be incurred by the ERS as the result of such participation by the ERS’s investment consultant and tax counsel.

(The representatives from PCA returned to the meeting.)

LEGISLATIVE PROPOSALS AFFECTING THE EMPLOYEES’ RETIREMENT SYSTEM

The Executive Director reported that the ERS submitted two proposals as part of the Governor’s administrative package for the 2014 Legislature:

- House Bill (H.B.) 2263 and Senate Bill (S.B.) 2812
Relating to unused sick leave for public employees who become members of the ERS after June 30, 2014.
- H.B. 2264 and S.B. 2813
Relating to the investment authority of the ERS to repeal the limitation on the holding period for real estate acquired by the ERS by foreclosure, enforcement of security, or in satisfaction of debts,

and that as of February 7, 2014, the following ERS-related proposals have been introduced in the legislature:

- H.B. 1627 and S.B. 2086
Proposal to provide firefighters with medical and service-connected disability retirement benefits for certain medical conditions that are presumed to arise out of and in the course of employment;

- H.B. 1705
Proposal to provide firefighters with medical coverage through workers compensation and service-connected disability retirement benefits through a presumptive law for cancer, blood-borne infectious diseases and exposure to a biochemical substance.
- H.B. 1964
Proposal to make a technical non-substantive amendment to the ERS law.
- H.B. 2192 and S.B. 2949
Proposal to establish guidelines for the transition of the Hawaii Health Systems Corporation, a regional system, or a combination of two or more regional systems, into a nonprofit corporation. Proposes certain retirement benefits for employees of the Hawaii Health Systems Corporation who are ERS members.
- H.B. 2386
Proposal to require the ERS to submit annual reports to the State Department of Budget and Finance on the status of the ERS.
- H.B. 2404 and S.B. 2688
Proposal to clarify that all or a portion of the benefits payable by reason of the death of the members of the ERS or former employee of the State or counties shall be payable to the alternate beneficiary designated under a qualified domestic relations order.
- H.B. 2652
Proposal to provide for reemployment opportunities for retired police officers, firefighters, and Hawaii National Guard retirees as public school security officers while protecting and without interruption of retirees' pension and retirement benefits.
- S.B. 335
Proposal to allow counties to adopt a county general surcharge on state excise tax. Exempts general excise tax amounts received from food and over the counter drugs. Stops transient accommodations tax from going to counties, instead directing that portion to pay other post employment benefits and reduce unfunded actuarial accrued liability of the ERS.

- S.B. 1038. SD 1 (proposed)
Proposal to require forfeiture of the employers contribution and interest portion of a member's retirement benefits upon a member's final conviction of or pleading guilty or nolo contendere to a felony. Establishes that the forfeiture of retirement benefits does not include a member's contributions to the ERS or vested retirement benefits. Applies forfeiture of benefits to ERS members who leave active employment if the conviction or plea includes bribery, corruption, forgery, perjury, or any other crime related to the duties of the member's employment.
- S.B. 2916
Proposal to require the ERS to require any State department or agency or counties to furnish to ERS certain payroll and personnel transaction information, including any changes or errors in payments that require correcting or updating.
- S.B. 3115
Proposal to authorize a one-time lump sum payment to pensioners who retired prior to July 1, 1990, with at least 20 years of service, and whose pension, annuity, or retirement allowance is \$25,000 or less.

The Executive Director also reported on the Board's Administrative and Legislative Committee's recommendations to the Board for positions on the legislative proposals:

- Oppose: H.B. 1627; H.B. 1705; H.B. 2192; H.B. 2652; S.B. 2086;
- Support: H.B. 2263, H.D. 1; S.B. 335; S.B. 1038, S.D. 1 (with suggested clarification on technical and operational concerns); S.B. 2812; S.B. 2813; H.B. 2264; S.B. 2916 (with suggested penalty imposed for non-compliance);
- No comment: H.B. 1964;
- Request clarification; suggest resolution: H.B. 2386;
- Deferred for further research, review, and cost estimates: H.B. 2404; S.B. 2688; and
- No position: S.B. 3115.

Furthermore, the Senate Committee on Health will hold a hearing on S.B. 2949 on February 10, 2014, and the Board's Administrative and Legislative Committee recommended that the Board oppose this proposal because it is considered a benefit enhancement. It was also recently discovered that the Senate Committee on Judiciary and Labor will hold a hearing on S.B. 1038, proposed S.D. 1 on February 11, 2014, and that there was also a possible chance that there would be a hearing on H.B. 2404 and S.B. 2688.

On a motion made by Trustee Matsumoto, seconded by Trustee Rauckhorst, and unanimously carried, the Board adopted the Board's Administrative and Legislative Committee's recommendation to oppose S.B. 2949.

On a motion made by Trustee Ferguson-Miyamoto, seconded by Trustee Matsumoto, and unanimously carried, the Board adopted the Board's Administrative and Legislative Committee's recommendations for positions on the following bills:

- Oppose: H.B. 1627; H.B. 1705; H.B. 2192; H.B. 2652; S.B. 2086;
- Support: H.B. 2263, H.D. 1; S.B. 335; S.B. 1038, S.D. 1 (with suggested clarification on technical and operational concerns); S.B. 2812; S.B. 2813; H.B. 2264; S.B. 2916 (with suggested penalty imposed for non-compliance);
- No comment: H.B. 1964;
- Request clarification; suggest resolution: H.B. 2386;
- Deferred for further research, review, and cost estimates: H.B. 2404; S.B. 2688; and

No position: S.B. 3115.

RECESS

Chair Lee Loy called a recess at 12:49 p.m.

RECONVENE

A quorum being present, Chair Lee Loy reconvened the meeting at 1:00 p.m.

ENTER EXECUTIVE SESSION

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

- Pursuant to HRS § 92-5(a)(8), to hear a status report from Macquarie Funds Group (USA) Inc. on the Hawaii Targeted Investment Program (HiTIP) and organizational changes; appropriate action;

- Pursuant to HRS § 92-5(a)(4), to consult with the Board's attorneys on questions and issues pertaining to the Board's powers, duties, privileges, immunities, and liabilities regarding false claims actions filed outside of Hawaii that relate to the Employees' Retirement System of the State of Hawaii; appropriate action;
- Pursuant to HRS § 92-5(a)(4), to consult with the Board's attorneys on questions and issues pertaining to the Board's powers, duties, privileges, immunities, and liabilities regarding joining a possible securities fraud action against Saipem S.P.A; appropriate action;
- Pursuant to HRS § 92-5(a)(4), to consult with the Board's attorneys on questions and issues pertaining to the Board's powers, duties, privileges, immunities, and liabilities regarding continuances of meetings; and
- To approve executive session minutes of the December 9, 2013 board meeting;

EXECUTIVE SESSION TO HEAR A
STATUS REPORT FROM
MACQUARIE FUNDS GROUP (USA)
INC. ON THE HAWAII TARGETED
INVESTMENT PROGRAM AND
ORGANIZATIONAL CHANGES

(The Executive Director and Ms. Donna Curry, ERS Program Specialist, and the representatives from PCA left the meeting.)

EXECUTIVE SESSION TO CONSULT
WITH THE BOARD'S ATTORNEYS
ON QUESTIONS AND ISSUES
PERTAINING TO THE BOARD'S
POWERS, DUTIES, PRIVILEGES,
IMMUNITIES, AND LIABILITIES
REGARDING FALSE CLAIMS
ACTIONS FILED OUTSIDE OF
HAWAII THAT RELATE TO THE
EMPLOYEES' RETIREMENT
SYSTEM OF THE STATE OF
HAWAII

EXECUTIVE SESSION TO CONSULT
WITH THE BOARD'S ATTORNEYS
ON QUESTIONS AND ISSUES
PERTAINING TO THE BOARD'S
POWERS, DUTIES, PRIVILEGES,
IMMUNITIES, AND LIABILITIES
REGARDING JOINING A POSSIBLE
SECURITIES FRAUD ACTION
AGAINST SAIPEM, S.P.A.

EXECUTIVE SESSION TO CONSULT
WITH THE BOARD'S ATTORNEYS
ON QUESTIONS AND ISSUES
PERTAINING TO THE BOARD'S
POWERS, DUTIES, PRIVILEGES,
IMMUNITIES, AND LIABILITIES
REGARDING CONTINUANCE OF
MEETINGS

APPROVAL OF EXECUTIVE
SESSION MINUTES
- DECEMBER 9, 2013

EXIT EXECUTIVE SESSION

On a motion made by Trustee Rauckhorst, seconded by Trustee Matsumoto, and unanimously carried, the Board exited from executive session.

APPROVAL OF MINUTES
- DECEMBER 9, 2013

On a motion made by Trustee Ferguson-Miyamoto, seconded by Trustee Rauckhorst, and unanimously carried, the Board approved the minutes of the Board's December 9, 2013 meeting.

INVESTMENT MANAGER WATCH
STATUS (BRADFORD & MARZEC,
LLC)

Mr. Vijoy Chattergy, ERS Chief Investment Officer (CIO), reported that he and PCA recommended that Bradford & Marzec, LLC (BM), ERS's fixed income manager, be placed on "Watch List" status due to organizational changes triggered by four of BM's investment management professionals, including two senior portfolio managers, having left the firm as a group.

On a motion made by Trustee Barfield, seconded by Trustee Kane, and unanimously carried, the Board approved placing Bradford & Marzec, LLC on the Watch List status effective March 1, 2014, due to organizational changes.

The CIO noted that ERS's routinely scheduled due diligence site inspection of BM's offices in Los Angeles, California, will be expedited due to BM's organizational changes and the potential structural changes within the ERS's fixed income portfolio.

2014 HIERS INVESTMENT SUMMIT

The CIO reported on the site inspections of the possible host properties on Kauai for the ERS's annual HIERS Investment Summit and proposed that the Grand Hyatt Kauai be selected as the venue to host the 2014 Investment Summit, July 23-25, 2014. The CIO also proposed a budget of the expenses.

2014 BOARD MEETING DATES

ERS staff proposed that the May Board meeting date be changed from Monday, May 12, 2014, to Tuesday, May 13, 2014 so that ERS's consultants and other Board meeting attendees who reside out of state do not need to catch a flight to Honolulu on Mother's Day, Sunday, May 11, 2014. ERS staff also proposed that the November Board meeting date be changed from Monday, November 10, 2014, to Wednesday, November 12, 2014, because the Veteran's Day holiday falls on Tuesday, November 11, 2014.

OPERATIONS REPORT
- JANUARY 2014

Ms. Kanoe Margol, ERS Assistant Administrator, presented the monthly update on ERS operations and ERS website statistics (top 10 viewed pages) for January 2013. Highlights included:

- ERS hosted its first “Brown Bag Information Session” on January 23, 2014, in an effort to provide ERS members with additional opportunities to learn more about the ERS and their ERS benefits; 27 ERS members attended.
- Status of the ERS’s operating expense budget as of December 31, 2013; ERS staff will continue to provide the Board with a monthly update on the operating expense budget.
- Top ten viewed web pages of the ERS’s website included the benefits calculator still holding at number one since October 2013.

NEXT BOARD MEETING
- FEBRUARY 21, 2014

Chair Lee Loy announced that the next Board meeting is scheduled for February 21, 2014 (special Board meeting).

ADJOURNMENT

On a motion made by Trustee Matsumoto, seconded by Trustee Kane, and unanimously carried, Chair Lee Loy adjourned the meeting at 2:02 p.m.

**REDACTED
SIGNATURE**

Wesley K. Machida
Executive Director

WKM: jh