

MINUTES OF THE REGULAR MEETING
OF THE BOARD OF TRUSTEES OF THE EMPLOYEES' RETIREMENT SYSTEM
OF THE STATE OF HAWAII
HELD ON TUESDAY, APRIL 10, 2012
CITY FINANCIAL TOWER, 201 MERCHANT STREET, SUITE 1935
HONOLULU, HAWAII

ROLL CALL

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

Trustee excused: Mr. Emmit Kane

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

Staff: Mr. Wesley Machida, Administrator
Ms. Kanoe Margol, Assistant Administrator
Mr. Rodney June, Chief Investment Officer
Mr. Vijoy Chattergy, Investment Specialist
Ms. Gerri Konishi, Member Home Loan Assistant
Ms. Donna Curry, Program Specialist
Ms. Jaime Hirata, Recording Secretary
Ms. Wanda Kugiya, Secretary

Guests: Mr. Neil Rue) Pension Consulting Alliance
Ms. Kay Ceserani

Mr. Michael Humphrey) Courtland Partners Ltd.
Ms. Lou Canlas

Mr. Thomas (Tom) Pulley) Fortress Investment Group LLC
Mr. Lou Jug

Mr. Jim Proud) Heitman Capital Management
(via conference call)

Ms. Alexandra Hill) Blackstone Real Estate Partners

QUORUM

A quorum being present, Chair Matsumoto called the meeting to order at 9:04 a.m.

AMENDMENT OF THE AGENDA

On a motion made by Ms. Lee Loy, seconded by Ms. Ferguson-Miyamoto, and unanimously carried, the Board amended the agenda to include the following item in Executive Session:

- pursuant to HRS § 92-5(a)(8), to consider and, if appropriate, to make a decision regarding the ERS's investment in BlackSand Capital Opportunity Fund I, L.P.

RECESS

Chair Matsumoto called a recess at 9:05 a.m. The meeting will reconvene after the Investment Committee meeting.

RECONVENE

A quorum being present, Chair Matsumoto reconvened the meeting at 10:37 a.m.

PRESENTATION

PRESENTATION BY COURTLAND PARTNERS ON THE ERS' REAL ESTATE PORTFOLIO PERFORMANCE MEASUREMENT REPORT FOR 4TH QUARTER 2011

Mr. Michael Humphrey and Ms. Lou Canlas of Courtland Partners Ltd. (Courtland), ERS's real estate investment consultant, presented the ERS's Real Estate Portfolio Performance Measurement Report for 4th Quarter 2011, for period ended December 31, 2011:

- Market Value: \$903,309,939
- Income: 1.7%
- Appreciation: 2.5%
- Total Gross Return: 4.2%
- Total Net Return: 3.8%
- Internal Rate of Return: 6.3%
- % of Total Plan Assets: 8.4%
- Target % of Total Plan Assets: 7.0%

EXECUTIVE SESSION

On a motion made by Ms. Lee Loy, seconded by Ms. Ferguson-Miyamoto, and unanimously carried, the Board entered into Executive Session to:

- pursuant to HRS § 92-5(a)(8), to consider the status of the Royal Ka'anapali Golf Course.
- pursuant to HRS § 92-5(a)(8), to consider and, if appropriate, to make a decision regarding the ERS's investment in BlackSand Capital Opportunity Fund I, L.P.
- 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 Lehman Brothers, Inc. and Lehman Brothers Holdings, Inc.; appropriate action.

- pursuant to HRS § 92-5(a)(8), to consider and, if appropriate, to make a decision regarding, investment in Blackstone Real Estate Partners Fund VII, L.P.
- pursuant to HRS § 92-5(a)(8), to consider and, if appropriate, to make a decision regarding, investment in Fortress Japan Opportunity Fund II, L.P.

EXECUTIVE SESSION TO CONSIDER THE STATUS OF THE ROYAL KA'ANAPALI GOLF COURSE.

EXECUTIVE SESSION TO CONSIDER AND, IF APPROPRIATE, TO MAKE A DECISION REGARDING INVESTMENT IN BLACKSAND CAPITAL OPPORTUNITY FUND I, L.P.

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 LEHMAN BROTHERS, INC. (LBI) AND LEHMAN BROTHERS HOLDINGS, INC. (LBHI)

(Mr. Aburano left the meeting and did not return for the remainder of the meeting.)

EXECUTIVE SESSION TO CONSIDER AND, IF APPROPRIATE, TO MAKE A DECISION REGARDING INVESTMENT IN BLACKSTONE REAL ESTATE PARTNERS FUND VII, L.P.

EXECUTIVE SESSION TO CONSIDER AND, IF APPROPRIATE, TO MAKE A DECISION REGARDING, INVESTMENT IN FORTRESS JAPAN OPPORTUNITY FUND II, L.P.

EXIT EXECUTIVE SESSION

On a motion made by Ms. Ferguson-Miyamoto, seconded by Mr. Barfield, and unanimously carried, the Board emerged from Executive Session at 1:09 p.m.

REQUEST FOR CONSENT TO
ASSIGNMENT OF INVESTMENT
MANAGEMENT AGREEMENT FROM
BISHOP STREET CAPITAL
MANAGEMENT (SUBSIDIARY) TO FIRST
HAWAIIAN BANK (PARENT).

The Administrator and the CIO reported that they received written notice from Bishop Street Capital Management, requesting consent to assignment of Bishop Street Capital Management's investment management agreement to its parent First Hawaiian Bank. The CIO noted the following:

- The Bishop Street Capital Management team that is currently serving the ERS account will remain the same; team would still be Bishop Street Capital Management, but would be under First Hawaiian Bank
- No indication of an organization lay-off; may be more of a cost saving measure or in consideration of employee satisfaction, or part of a branding/marketing strategy

Investment Committee Chair, Mr. Vince Barfield, and PCA, noted that they do not see this change as an immediate risk or issue, but advised that the Board and the ERS staff continue to watch both Bishop Street Capital Management and First Hawaiian Bank. The Administrator noted that in some respects, this change may be of an advantage to the ERS.

On a motion made by Ms. Lee Loy, seconded by Ms. Ferguson-Miyamoto, and unanimously carried, the Board approved consent to assignment of investment management from Bishop Street Capital Management to First Hawaiian Bank, subject to legal review and compliance with usual conditions for assignments of contracts.

INVESTMENT CASH LIMITATIONS
POLICY

The CIO reported that, at the February 13, 2012 Investment Committee meeting, the Investment Committee considered a proposed policy to limit the amount of cash holdings of public equity managers to ensure that such managers are fully exposed to respective markets within their prescribed strategy – policy also known as the “Cash Limitations Policy.” At the March 12, 2012 Board meeting, the Board reviewed the Cash Limitations Policy (the policy) and the recommendation from the ERS staff and PCA. The Board requested that the proposed policy be modified to reflect the Board’s concern about the appropriate notification and handling of potential investment manager breaches of the policy.

PCA and the CIO presented a revised proposed policy to the Board for the Board's approval. Mr. Rue noted that the proposed policy would ensure that the public investment managers remain fully invested at all times. This would allow total funds to remain more closely aligned to total policy target and that the management fees are aligned with the assigned mandates. PCA also recommended that cash holdings be limited to 5% or less of total investment manager holdings.

Staff recommended that the Board consider and approve the Cash Limitations Policy as presented by PCA.

On a motion made by Mr. Yamasaki, seconded by Ms. Lee Loy, and unanimously carried, the Board approved the proposed Cash Limitations Policy, as presented, for inclusion to the ERS Investment Policy and Procedures Manual, Section III.1.A – Domestic and International Equity Securities as follows:

It is expected that equity managers (domestic and international) will be fully invested at all times and that the cash equivalent portion of a manager's portfolio will not exceed 5% of the portfolio. Any exemption or variation from this guideline requires prior written approval from the ERS Chief Investment Officer.

LEGISLATIVE PROPOSALS AFFECTING THE ERS

The Administrator reported on the Administration's 2012 legislative proposals affecting the ERS as of April 10, 2012:

- Housekeeping (corrects inconsistencies and nonsubstantive errors in Act 163/SLH 2011)

House Bill (HB) 2487

The Senate Judiciary and Labor Committee (JDL) deleted the section that would have restore the age and service retirement requirements under section 88-73(b) and 88-74(c) and (d) for current members who become judges after June 30, 2012 to the same age and service retirement requirements as any other Contributory Plan members who became ERS members prior to July 1, 2012 and added the provisions of the anti-spiking bill with a defective effective date of July 1, 2050.

Senate Bill (SB) 2749

Senate JDL deleted the section of the bill that would restore the age and service retirement requirements under section 88-73(b) and 88-74(c) and (d) for current members who become judges after June 30, 2012 to the same age and service retirement requirements as any other Contributory Plan members who became ERS members prior to July 1, 2012.

- Anti-spiking

HB 2488

This bill is no longer an “active” bill as it has not crossed-over to the non-originating chamber

SB 2750

House Labor Committee (LAB) revised the amendment to section 88-81(g)(2), which describes the second test for “spiking.” The average final compensation ratios were changed from 120% to 135%. The Senate JDL added a defective effective date of July 1, 2050.

- Trustee Investment Requirement

HB 2489

This bill is no longer an “active” bill as it has not crossed-over to the non-originating chamber

SB 2751

House LAB amended the bill to increase from 1 to 2 the number of members of the Board who are not State or county employees who must have at least 3 years of experience providing financial services, including investments, to public, corporate or private institutional clients.

The Administrator reported that the costs associated with the changes to the ERS's computers etc. to implement the anti-spiking legislation, if it is passed, are included in the budget. On-going meetings with legislators, City & County, the unions, etc. are still priority in educating everyone about the ERS's legislative proposals. Overall goal is to do more presentations for the retirees and active members, provide support for employer trainings, and continue to meet with legislators.

RELOCATION OF ERS OFFICES WITHIN CITY FINANCIAL TOWER

The Administrator reported on the proposed plans to relocate ERS's offices within City Financial Tower (201 Merchant Street). The 12th floor of City Financial Tower has been vacant since 2004, following Central Pacific Bank's acquisition of City Bank; City Bank's lease expired in February 2009 and attempts to lease the 12th floor space have been unsuccessful due to the current configuration of the offices on that floor and the high costs that may be required to renovate the space for new tenants. One of the ERS' main goals is to maximize revenue. Therefore, relocating all of the ERS offices on the 9th and the 16th floors to the 12th floor have been proposed because City Financial Tower management, PM Realty Group, has advised the ERS that the 9th and 16th floors have greater potential to generate leasing revenue than the 12th floor. Total anticipated revenue from leasing the 9th and 16th floors would be approximately \$532,400 to

\$552,400 per year. Preliminary estimated budget to renovate the 12th floor for ERS staff is approximately \$1.33 million.

PMRG has informed the ERS that there is a potential tenant interested in the 16th floor that would like to move in July 2012 and that there have been a number of other inquiries. Due to the timing and high interest in the 9th and 12th floors, ERS staff recommended the Board consider and approve the relocation of the ERS offices on the 9th and 16th floors to the 12th floor, and consider and approve the initial estimated renovation budget of \$1.33 million for the 12th floor.

On a motion made by Ms. Ferguson-Miyamoto, seconded by Mr. Barfield, and unanimously carried, the Board approved (1) the relocation of the ERS offices on the 9th and 16th floors to the 12th floor of the City Financial Tower, and (2) a renovation budget of up to \$1.33 million for the 12th floor.

ADMINISTRATOR'S UPDATE ON THE ERS ACTION PLAN AS OF APRIL 10, 2012

The Administrator provided an update on the ERS Action Plan as of April 10, 2012:

- Ms. Kishimoto and Mr. Tom Maloney (ERS Tax Counsel) are working on the amendment of Chapter 6-28, Hawaii Administrative Rules, to modify the operating procedures to ensure compliance with federal tax law requirements; submitted to Governor's office for review and approval.
- Bank of Hawaii is currently providing ERS with banking services. Bank of Hawaii's contract expires this year. ERS is procuring a new contract. The results of the procurement will be reported later
- Custodian contract (with Northern Trust) is due to expire next year. A Request for Proposal for custodial services will be issued this year
- Internal audit project with ERS' internal audit consultant, KMH LLP (KMH), is progressing; KMH would like to present the Audit Committee with the proposed Internal Audit Plan, proposed Audit Charter, and Internal Audit Charter; plan to present the Audit Committee's recommendations at the May 15, 2012 Board meeting

APPOINTMENT OF MR. KANE TO ATTEND THE INTERNATIONAL FOUNDATION OF EMPLOYEE BENEFITS PLAN (IFEBP) PORTFOLIO CONCEPTS AND MANAGEMENT TRAINING AT THE WHARTON SCHOOL UNIVERSITY OF PENNSYLVANIA

There being no objections, Chair Matsumoto appointed Mr. Kane to attend the International Foundation of Employee Benefits Plan (IFEBP) Portfolio Concepts and Management Training, to be held May 21-24, 2012 at The Wharton School University of Pennsylvania, Philadelphia, PA.

NEXT BOARD MEETING –
MAY 15, 2012

MEETING ADJOURNED AT 1:39 P.M.

Chair Matsumoto announced that the next Board meeting is scheduled for May 15, 2012.

On a motion made by Ms. Lee Loy, seconded by Ms. Ferguson-Miyamoto, and unanimously carried, the Board adjourned the meeting at 1:39 p.m.

**REDACTED
SIGNATURE**

Wesley K. Machida
Administrator

WKM: jh