

MEETING OF THE TRUSTEES

CITY OF CHATTANOOGA GENERAL PENSION PLAN

February 16, 2012

The regular meeting of the City of Chattanooga General Pension Plan Board of Trustees was held on February 16, 2012 at 8:30 a.m. in the J. B. Collins Conference Room. Trustees present were Daisy Madison, Katie Reinschmidt, Dan Johnson, Terry Lamb and Steve Perry. Others attending the meeting were Valerie Malueg, City Attorney's Office; Teresa Laney, First Tennessee Bank; Scott Arnwine, Consulting Services Group; and Madeline Green, Andrew Dunn and Douglas Kelley, City Personnel Department.

The meeting was called to order by Chairwoman Daisy Madison. A quorum was present.

The minutes of the meeting held on November 17, 2011 were unanimously approved.

The following benefit and plan expenses were discussed and unanimously approved by the Board. Two comments of note – 1) the City and the GPP share equally in the paying the premium for disability insurance but the benefit payments are paid by the insurer, The Hartford; 2) the funds withdrawn to pay pension benefits are being reported to the board after the fact based on authorization granted previously.

GENERAL PENSION PLAN

PART I – PARTICIPANT SUMMARY

SUMMARY OF PENSION APPLICATIONS

<u>NAME</u>	<u>DEPARTMENT</u>	<u>TYPE/OPTION</u>	<u>MONTHLY AMOUNT</u>	<u>EFFECTIVE DATE</u>
Aaron, Jimmy V. (Formerly Vested)	General Services	Rule of 80 - Option B	\$897.45	February 1, 2012
Bowles, Sherman	Public Works	Normal-Option E	\$693.58	January 1, 2012
Burr, Suzanne	Library	Normal-Option A	\$1,630.31	January 1, 2012
Cuzzort, Robin	General Government	Normal-Option D	\$432.24	January 1, 2012
Deal, Danny D. (Two-Year DROP - \$46,510.37)	Public Works	Rule of 80 - Option D	\$1,456.31	December 1, 2011
Early, Patricia D.	Human Services	Normal-Option D	\$600.43	January 1, 2012
Erlandson, Jeffrey (Formerly Vested)	Public Works	Immediate Early- No Option Elected	\$347.40	January 1, 2012
Fowler, Martha	Public Works	Normal - No Option Elected	\$1,172.95	January 1, 2012
Goodson, Lincoln	Public Works	Normal-Option A	\$1,539.18	January 1, 2012
Gordon, Teresa Ann	COUNTY 911	Normal-Option A	\$1,267.23	January 1, 2012
Heath, Vanessa (Two-Year DROP - \$39,525.78)	Personnel	Rule of 80 - Option B	\$1,311.49	January 1, 2012

SUMMARY OF PENSION APPLICATIONS (cont.)

<u>NAME</u>	<u>DEPARTMENT</u>	<u>TYPE/OPTION</u>	<u>MONTHLY AMOUNT</u>	<u>EFFECTIVE DATE</u>
Hill, Eddie	Public Works	Normal-Option B	\$641.33	January 1, 2012
Jenkins, Countess B. (Formerly Vested)	Neighborhood Services	Normal-Option A	\$504.70	November 1, 2011
Lopez-Cepero, Brian	Finance	Normal - No Option Elected	\$830.51	January 1, 2012
Martin, Phillip D.	Public Works	Normal-Option B	\$1,294.13	January 1, 2012
Meives, Karen A.	Police	Normal - No Option Elected	\$627.46	January 1, 2012
Ray, Randall E.	Finance	Normal-Option B	\$2,018.06	January 1, 2012
Saylors, Bobby R.	Parks & Recreation	Normal-Option C	\$556.98	January 1, 2012
Stewart, Charles D. (Formerly Vested)	Public Works	Rule of 80 - Option D	\$1,083.47	January 1, 2012
Whiteside, Shwanna	COUNTY 911	Rule of 80 - No Option Elected	\$1,654.36	December 1, 2011

BENEFIT REVISIONS/CONVERSIONS-PENDING BOARD REVIEW/APPROVAL

<u>NAME</u>	<u>TYPE/OPTION</u>	<u>PREVIOUS AMOUNT APPROVED BY BOARD</u>	<u>REVISED AMOUNT</u>	<u>EFFECTIVE DATE</u>
-------------	--------------------	--	---------------------------	---------------------------

No Activity

SELECTION OF OPTIONAL BENEFIT REPORT – VESTED OR AGE 62 AND OLDER PARTICIPANTS

<u>NAME</u>	<u>OPTION</u>	<u>DATE</u>
Anderson, David Lee	Option B	January 4, 2012
Beck, Perry	Option B	January 11, 2012
Failing, Hugh	Option B	January 3, 2012
Francis, James J.	Option B	January 10, 2012
Landguth, Michael	Option B	January 11, 2012
Lea, Sharon	Option B	November 23, 2011
Morris, Richard C.	Option B	November 30, 2011
Trotter, W. Gene	Option B	January 25, 2012

DISABILITY BENEFIT REPORT

<u>NAME</u>	<u>MONTHLY DISABILITY BENEFIT AMOUNT</u>	<u>EFFECTIVE DATE</u>
Anderson, David L. (non-job related disability)	\$2,077.78	November 30, 2011
Holt, James S. (job-related disability)	\$1,102.50	April 17, 2011
Roshell, Gary L. (non-job related disability)	\$1,117.50	November 22, 2011

LUMP SUM DISTRIBUTIONS (FOR RATIFICATION-CHECKS PROCESSED)

<u>NAME</u>	<u>DEPARTMENT</u>	<u>EMPLOYEE NUMBER</u>	<u>TERMINATION DATE</u>	<u>REFUND AMOUNT</u>
Atkins, Alvin	Public Works	63203	September 29, 2011	\$2,248.87
Classen, Charles	Public Works	65898	December 15, 2011	\$1,247.33
Cole, Curtis	Public Works	63381	October 20, 2011	\$556.41
Cookson, Nicholas	Public Works	65630	December 9, 2011	\$1,479.91
Correll, Matthew	Public Works	68014	October 6, 2011	\$26.56
Cousin, Carla	Finance	68016	October 7, 2011	\$21.20
Galeano, Nelson	Planning	66250	November 18, 2011	\$1,590.76
Hall, Patrick	Planning	64234	November 18, 2011	\$2,429.45
Petty, Cindy	Finance	61534	January 11, 2012	\$6,474.21
Santiago, Christina	Finance	67720	September 16, 2011	\$105.84
Schrodt, Gail	Personnel	67122	January 3, 2012	\$692.66
Stearman, April	Police	63054	November 23, 2011	\$2,053.44
Hawkins, Genevieve (Estate) (Date of death November 25, 2011 - \$250.00 Death Benefit/retired from City school system)				\$250.00
Hixson, Ronald (Estate) (Refund of remaining employee basis – retiree Ronald Hixson died on December 5, 2011)				\$108.44
Jernigan, David (Refund of remaining employee basis – retiree Lewis Jernigan died on November 14, 2011)				\$52.09
Leffew, Deborah (Refund of remaining employee basis – retiree Lewis Jernigan died on November 14, 2011)				\$52.09

LUMP SUM DISTRIBUTIONS (FOR RATIFICATION-CHECKS PROCESSED) – cont.

<u>NAME</u>	<u>DEPARTMENT</u>	<u>EMPLOYEE NUMBER</u>	<u>TERMINATION DATE</u>	<u>REFUND AMOUNT</u>
Stone, Anita				\$329.39
(Refund of remaining employee basis – retiree Coretha Harmon died on January 8, 2012)				
TOTAL				\$19,718.65

PART II – ACCOUNT SUMMARY

ACCOUNTS PAYABLE

<u>COMPANY</u>	<u>AMOUNT PAID</u>		<u>PURPOSE</u>
	<u>THIS PERIOD</u>	<u>FYTD</u>	
CONSULTING SERVICES GROUP	\$17,887.75	\$35,849.00	Investment consulting services for period ending September 30, 2011
CONSULTING SERVICES GROUP	\$18,099.25	\$53,948.25	Investment consulting services for period ending December 31, 2011

ACCOUNTS PAYABLE

<u>COMPANY</u>	<u>AMOUNT PAID</u>		<u>PURPOSE</u>
	<u>THIS PERIOD</u>	<u>FYTD</u>	
FIRST TENNESSEE BANK	\$23,491.84	\$74,820.66	General Pension Plan expense for quarter ending December 31, 2011

COMPANY TOTAL	\$59,478.84	\$131,096.26	
----------------------	--------------------	---------------------	--

INVESTMENT MANAGERS

<u>COMPANY</u>	<u>AMOUNT PAID</u>		<u>PURPOSE</u>
	<u>THIS PERIOD</u>	<u>FYTD</u>	
DUFF & PHELPS	\$12,102.00	\$35,244.00	Investment management expense for quarter ending December 31, 2011
INSIGHT	\$13,655.39	\$42,525.10	Investment management expense for quarter ending December 31, 2011
NWQ INVESTMENT	\$23,079.36	\$50,349.00	Investment management expense for quarter ending September 30, 2011
PATTEN AND PATTEN	\$9,123.46	\$27,077.47	Investment management expense for quarter ending December 31, 2011

INVESTMENT MANAGERS (cont.)

<u>COMPANY</u>	<u>AMOUNT PAID</u>		<u>PURPOSE</u>
	<u>THIS PERIOD</u>	<u>FYTD</u>	
SMH CAPITAL ADVISORS	\$7,418.92	\$15,394.54	Investment management expense for quarter ending September 30, 2011
	\$7,754.45	\$23,148.99	Investment management expense for quarter ending December 31, 2011
WEDGE CAPITAL	\$20,414.56	\$61,220.29	Investment management expense for quarter ending December 31, 2011
MANAGER TOTAL	\$93,548.14	\$307,764.85	

ACCOUNTS PAYABLE – INVESTMENT MANAGERS (REVISION)

No Activity

ACCOUNTS RECEIVABLE

<u>COMPANY</u>	<u>AMOUNT RECEIVED</u>	<u>PURPOSE</u>
----------------	------------------------	----------------

No Activity

REPORT OF MISCELLANEOUS ACCOUNT TRANSACTIONS

<u>COMPANY</u>	<u>AMOUNT</u>	<u>FYTD</u>	<u>EFFECTIVE DATE/PURPOSE</u>
Northern Trust Investments	\$500,000.00	\$2,000,000.00	November 28, 2011 – withdrawal to cover benefit payments and miscellaneous expenses
Northern Trust Investments	\$300,000.00	\$2,300,000.00	December 23, 2011 – withdrawal to cover benefit payments and miscellaneous expenses
Northern Trust Investments	\$100,000.00	\$2,400,000.00	January 27, 2012 – withdrawal to cover benefit payments and miscellaneous expenses
MISCELLANEOUS TOTAL	\$900,000.00	\$2,400,000.00	

REPORT OF ACCOUNT(S) PAID

<u>COMPANY</u>	<u>AMOUNT PAID</u>		<u>PURPOSE</u>
	<u>THIS PERIOD</u>	<u>FYTD</u>	
THE HARTFORD	\$8,809.13		Long-Term Disability (50%) – November 2011

REPORT OF ACCOUNT(S) PAID (cont.)

<u>COMPANY</u>	<u>AMOUNT PAID</u>		<u>PURPOSE</u>
	<u>THIS PERIOD</u>	<u>FYTD</u>	
THE HARTFORD	\$8,808.69		Long-Term Disability (50%) – December 2011
THE HARTFORD	\$8,863.70		Long-Term Disability (50%) – January 2012
THE HARTFORD	\$8,873.94		Long-Term Disability (50%) – February 2012
LTD TOTAL	\$35,355.46	\$70,700.73	

**CITY OF CHATTANOOGA OPEB TRUST
 ADMINISTRATIVE ACTIONS**

Meeting of Trustees – February 16, 2012

PART I – ACCOUNT SUMMARY

ACCOUNTS PAYABLE

<u>COMPANY</u>	<u>AMOUNT PAID</u>		<u>PURPOSE</u>
	<u>THIS PERIOD</u>	<u>FYTD</u>	
FIRST TENNESSEE BANK	\$1,758.59		Custodial services for quarter ending December 31, 2011
COMPANY TOTAL	\$1,758.59	\$6,380.41	

INVESTMENT MANAGERS

No Activity

MANAGER TOTAL	\$0.00	\$8,618.00
----------------------	---------------	-------------------

ACCOUNTS RECEIVABLE

<u>COMPANY</u>	<u>AMOUNT PAID</u>		<u>PURPOSE</u>
	<u>THIS PERIOD</u>	<u>FYTD</u>	

No Activity

Consulting Services Group

New Small Cap Manager – presentations by Kennedy Capital Management and The London Company

Scott Arnwine –At the last meeting, the Board approved inviting representatives from The London Company and Kennedy Capital Management to the February 16, 2012 meeting for a presentation. The selected Small Cap Core managers will replace Russell 2000 index fund. Each of the companies will have time to make their presentation.

The London Company is represented by Tim McCoy, Director of Institutional Sales and Marketing and Mark DuVaul, Portfolio Manager. The London Company has been in existence for 18 years. Tim will present a summary of the breadth of experience of the investment team and Mark will discuss the investment philosophy of The London Company. References are made to various slides (pages) of the presentation.

Tim -- Experience of the investment team ranges from generalist to analyst to portfolio manager. The team invokes a private equity approach to investing; instead of predicting the future, the focus is on facts that exist today. The portfolio construction allows outperformance of index funds. The team operates with the conviction to downside protection and protection of client capital. Slide 4 provides the background of the firm, Slide 6 lists the 5 portfolio strategies, Slide 8 provides the results of performance against Russell 2000 using 5 year rolling averages, and Slide 9 shows consistency of performance.

Mark -- Slide 11 reiterates the company's focus on downside protection and, preservation of capital with a goal of consistent outperformance against their benchmarks. Slide 12 outlines their competitive advantages including a focus on return on capital rather than earnings per share. A balance sheet optimization tool is used in analysis to create value rather than predict earnings. Portfolio construction process implies optimization but with meaningful investment positioning. Slide 13 provides and outline of the process: idea – research (balance sheet optimization tool) – construct portfolio – sell decisions - soft stop loss rule. Slide 15 provides snapshot of the small cap portfolio characteristics. Mark highlighted the upside/downside statistic (want wide spread).

Questions from the Board:

- 1) *What is the typical turnover rate in the portfolio?* – usually low 20 - 25%;
- 2) *Do you expect a company to raise debt to buy back stock?* – look for this in analysis of a company, may be encouraged but not required, company should build in margins of safety in the balance sheet
- 3) *Changes in interest rate* – cost of debt low rate environment somewhat easy, as rates rise more difficult, look for cost of debt less than cost of equity
- 4) *Mergers and acquisitions on portfolio* – look at macro environment but focus on bottoms up fundamentals in management of portfolio, strong balance sheets, some stocks in portfolio do get acquired at attractive prices but not goal of portfolio construction
- 5) *Balance sheet optimization a strategy since inception* – yes, used elements of it from origin, became more formalized about 10 years ago

Tim wrapped up the presentation reiterating the strength of investment team, high client retention rate, and the process using current market information for the downside protection and preservation of capital.

Question – Is there anything on the horizon size wise or people wise of a regulatory nature that will change the process? -- No change anticipated in process, but the small cap fund will eventually close to new investors

Daisy asked for confirmation regarding slide 24 disclosures, fees, and company history

Kennedy Capital Management is represented by Donald Cobin, Portfolio Manager and Chuck Bryant, Managing Director, Marketing. Chuck will present information about the organization and Don will provide an overview of the investment process. References are made to various slides (pages) of the presentation.

Chuck -- Slide 3 gives an overview of the firm, its organization, the focus on small cap, mid cap, micro cap portfolios, the 6 managers and 3 traders, the 14 equity analysts with specific sector expertise to maintain diversity. There is greater risk in small cap portfolios, but greater rewards if it is managed well.

Don -- Slide 8 provides the snapshot of the process of the small cap portfolio construction. There are about 2,500 stocks in the universe to choose from. Potential investments are screened based on certain quantitative criteria and certain questions – what's our edge, does management know how to allocate capital, management is ethical, cash flow is evaluated, what is the intrinsic value vs. where the market is valuing it -- leaving about 100 stocks of interest. Slide 9 defines the cash flow return on investment (cash return on every dollar invested) as the focus of their portfolio evaluation to improve results for clients and

compares results to the Russell 2000 index fund. Slide 10 is intended to show that stocks in the Kennedy portfolio are undervalued compared to Russell 2000 and have a higher CFROI. This portfolio will close with another \$200-300 million in investment. Liquidity is a driver in this decision to close the fund.

Questions from the Board were parallel to those asked of The London Company. Responses are as follows:

Slide 12 - gives returns over past 10 years;

Slide 29 - gives risk profile of the portfolio over the last 12 quarterly returns; the upside/downside risk/reward is shown on the right hand side of the page

portfolio turnover (change in position) is 65-85%, name turnover (complete exit of name) is 50%

Slide 11 addresses risk control. The investment policy committee evaluates portfolio performance looking for changes in metrics and how it may change risk relative to company or client guidelines, sector weightings (provided on Slide 13), and the culture of compliance. Slide 15 summarizes the annual returns compared to the Russell 2000. Slide 16 graphically shows the outperformance over time vs. Russell 2000.

After the presentations Scott Arnwine recapped strengths of each company. He indicated that he has no reservations about investing with either one or both companies. Katie Reinschmidt has some knowledge of Kennedy and provided good feedback on one of the analysts. The Board continued discussion comparing companies on upside/downside results and the proportionate size of company in the GPP portfolio.

The question was raised - Is there a disadvantage in splitting the investment between the two? More discussion followed with the opinion that there is no apparent difference between the two and the fees are similar. There is \$8M to be invested.

Dan Johnson made a motion to split the available small cap funds equally between Kennedy Capital Management and The London Company. The motion was seconded by Steve Perry. Daisy Madison called for a vote; the motion carried.

Schedule – Election of Officers

Although this is an agenda item, the Board decided to defer the voting on officers until the next meeting. Valerie Malueg indicated that annual election of officers is required by bylaws of the Board.

Schedule - General Pension Plan Board Meetings

This agenda item concerns the frequency of the Board meeting and performance review. To change it requires board action. The suggestion has been made that the Board meet on quarterly basis when CSG is present. Special board meetings can always be called when necessary and still be in compliance with the bylaws. ***Steve Perry made a motion to change the meeting schedule to quarterly, Dan Johnson seconded the motion. Daisy Madison call for a vote. The motion carried.*** Future meetings will now be scheduled quarterly with special meetings called as necessary.

Report from Counsel

Valerie Malueg raised an issue regarding the Public Funds Listing. This is an investment securities monitoring program involving a large listing of public funds. It is essentially a cost free monitoring for fraud. The gist is similar to an internal audit – providing another set of eyes into the fiduciary responsibility of the Board. The Board has nothing to lose by participating.

There was some discussion and questions were raised about the concept -- are the sponsors seeking a problem, a class action lawsuit? Is the operating procedure questionable?

Valerie indicated that the sponsors would like to present their program. Is the board interested in this?

Valerie has material to distribute to the Board if there is interest, but the Board needs to decide whether to pursue this program. The Board expressed no interest in pursuing this and Valerie will inform the sponsors.

CSG Performance Review – Fourth Quarter 2011

Scott Arnwine provided a quick summary of the investment performance for the quarter.

Overall 2011 was a difficult, volatile year, but by end of year, the S&P showed slightly positive results. Basically it was a flat year but they were the #1 performing country; better than

international which was down significantly. Long term treasuries, even after downgrade, were the best performing asset class. Utilities performed well.

The GPP portfolio showed good results in 4Q (up 6.2% and in the top quartile of performance of public funds in US). January was an up month (up 4.4%, not including our private equity, so expect a bit higher return). Managers performed in line or slightly below. NWQ struggled because they are heavily weighted toward gold mining stocks that did not do well (even though gold did well).

Daisy Madison mentioned that she is withdrawing funds from fixed income to meet monthly benefit payments. Does this practice need to be addressed again? Scott Arnwine indicated that the authorization was up to a specific dollar amount (\$4M) but that only about half of the authorized amount had been withdrawn.

The question was raised concerning corporate cash – are pension funds and endowments tremendously underinvested in US equities? Scott indicated that this is not evident in our class whereas alternative investments have been more prevalent. US equities are likely the best class to be in with large cap preferred over small cap and US preferred over international funds. There is still concern about a US treasury bubble. Floating rate investments are attractive as alternative since they are shorter term and US equities are favored.

Daisy Madison asked if the actuarial assumption of 7.75% is still a reasonable expectation? Over the last 3 yrs. the results have been 11.9%, but over the last 5yrs. only 1.3%.

Actuary RFP – Review

Daisy Madison indicated that the EFI contract expired prior to 2012.

Donna Kelley indicated that we normally send valuation data to the actuary at the end of February and expect valuation results sometime in April. An Actuarial RFP is sent periodically for competitive bid (the last one was sent five years ago). We sent one out at the end of 2011 and received 10 responses, some of which are highly competitive. The review is complicated by the fact that there is a transition period needed if a different actuary is chosen so that they can implement the data and plan provisions in their system. At the same time, budget timing, since it is moving closer to beginning of year, is problematic in getting the RFP completed in time for the transition period.

Therefore, ***Donna proposes an extension to the contract with the current actuary (EFI) for the current valuation of pension and OPEB.*** This will allow time to evaluate the proposals, select then next actuary, transition data if necessary, etc. for the next valuation cycle. It should be noted that all plan administration is handled internally and that the actuarial services are essentially for valuation.

Further, at the time of the last selection of the actuary, OPEB was not part of pension board, but has since been added to responsibility through City Council approval. The Pension Board is perceived as an agent of government with its own specified authority. Similarly, the Fire and Police pension operates independently (that is completely autonomous) and does not bring business to city council. Donna seeks clarification that the selection of the actuary is a Board responsibility and not City Council business.

Valerie Malueg will check to see who should be involved in selection of actuary or in entering into any contractual arrangement needed to conduct Pension Board business. She does not anticipate that approval beyond the Board is required for selection of the actuary.

Katie Reinschmidt made the motion to extend the EFI contract for the current valuation. The motion was seconded by Terry Lamb. Daisy Madison called for a vote. The motion carried.

The next Board meeting is scheduled for June 7, 2012 at 8:30 a.m. in the J.B. Collins Conference Room.

There being no further business, the meeting was adjourned.

Chairman

APPROVED:

Secretary