

STATE OF DELAWARE
STATE BOARD OF PENSION TRUSTEES
AND
OFFICE OF PENSIONS
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BOARD OF PENSION TRUSTEES
MEETING MINUTES OF JULY 25, 2008

The meeting of the Board of Pension Trustees was called to order by N. Shevock, at 9:06 a.m. in the Delaware Conference Room of the Office of Pensions in Dover.

Trustees Present

Nancy Shevock
Robert Allen
Jan King
Richard Cordrey
Helen Foster
Jennifer Davis

Trustees Absent

Philip Reese

Others Present

David Craik, Pension Office
Kim Vincent, Pension Office
Terri Timmons, Pension Office
Kathy Kunkle, Pension Office
Cindy Collins, DAG
Charlotte Lister, PAC
Karen Field-Rogers, OMB

1. OPENING COMMENTS

The meeting of the Board of Pensions Trustees was called to order by N. Shevock.

2. APPROVAL OF THE MINUTES

The Trustees reviewed the public minutes of the June 20, 2008 meeting.

MOTION made by R. Cordrey and seconded by R. Allen to approve the public minutes of the Board of Pension Trustees' June 20, 2008 meeting.

MOTION ADOPTED UNANIMOUSLY

The Trustees reviewed the executive minutes of the June 20, 2008 meeting.

MOTION made by R. Cordrey and seconded by R. Allen to approve the executive minutes of the Board of Pension Trustees' June 20, 2008 meeting.

MOTION ADOPTED UNANIMOUSLY

3. INVESTMENT COMMITTEE REPORT

Investment Committee Performance Report

<u>Fund</u>	<u>Previous Month</u>	<u>Fiscal Year To Date</u>	<u>12-Month</u>
Total Fund	-3.5 %	-1.3%	-1.3%
S & P 500 Index	-8.4%	-13.1%	-13.1%
60/35/5*	-5.0%	-5.4%	-5.4%
Delaware	-4.9 %	-3.5%	-3.5%
Benchmark**			

*Benchmark mix of 60% S&P500 Index, 35% Salomon Long Government and Corporate Bond Index, 5% T-bills.

**Benchmark mix of 37% Russell 3000, 1% NAREIT, 20% MSCIA, 38.5% Lehman Bond universal, 1.5% LBTIPS, 2% T-bills.

Total assets in the Fund at the end of June totaled \$7,076 million. The Fund lost 3.5% for the month compared positively to a benchmark return of (4.9%) and ahead of the 60/35/5 benchmark which was (5.0%).

During the month of June the Fund experienced negative results in all equity markets. U.S. stocks in the Russell 3000 lost (8.3%) including Large U.S. Growth stocks losing (5.9%) and Large Value Index returned a negative (9.6%). Small Cap stocks also had negative results of (8.3%) for small U.S. Equity market according to the Russell 2000 Index. The International Markets also experienced high losses along with the U.S. Market with the unhedged EAFE returning a negative (8.9%). The Bond Market was spared with Lehman LT Government/Corp Index at a slight .5% gain for the month.

The fiscal year, (unaudited) year-to-date return for 12 months for the Fund will be reported at a (1.3%) loss, compared positively to a loss of (3.5%) in the benchmark. Calendar returns, year-to-date, for 2008 are a negative (3.9%) which compares positively to a benchmark of (5.7%).

Increasing illiquidity in the U.S. financial markets has prompted the Investment Committee to make multiple liquidation recommendations to move more funds to cash. A poll vote was taken and approved based on the Investment Committee recommendation to terminate the Lehman Fixed Income Fund, a manager who carries mortgage securities in its portfolio as an enhancement to its index holdings. This drag has reduced returns. In addition, there is increased liquidity risk on all investment banking firms that also prompts this recommendation.

The Investment Committee requests approval of the immediate termination of the Lehman Fixed Income Account (approximately \$395 million). It also recommends Mellon be used as a transition manager. \$100 million of the proceeds will remain in cash. Approval is also needed to hire Mellon Capital to invest the liquidated funds into a Lehman Aggregate Fixed Income Index. Some transferred securities (illiquid) will not be liquidated and will be held to maturity in a separate structured bond account at DPERS' custodian bank Northern Trust. These securities will be managed by Mellon Capital. As market opportunities present themselves certain securities held in this account may be liquidated.

A discussion of the merits was held.

MOTION was made by R. Cordrey and seconded by R. Allen to approve the termination of the Lehman Fixed Income Account (approximately \$395 million) and approve that Mellon be used as a transition manager and that \$100 million of the proceeds remain in cash at Northern Trust with the balance of the account to be invested in the Mellon Fixed Income Index Fund.

MOTION ADOPTED UNANIMOUSLY

The Investment Committee recommends further liquidations to cash. DPERS has commitments to fund various private equity and hedge funds which will have capital calls up to \$300 million in the next 12 months. In addition, \$170 million is needed for benefit payments. Given the

volatility and liquidity issues in this market, the Investment Committee is recommending moving to cash enough funds to meet cash flow needs for the next 12 months. It is recommended that DPERS liquidate and hold in cash \$100 million from each of the Mellon TAA, \$100 million from Mellon GTAA and \$70 million from Mercator, an international equity manager. The combined effect of these liquidations and reallocation to cash will reduce the overall risk level of the fund.

MOTION was made by H. Foster and seconded by J. Davis to approve liquidating funds to meet the cash flow needs of DPERS for the next 12 months in order to fund various private equity and hedge fund capital commitments and hold in the cash account at Northern Trust. Approval to liquidate \$100 million from Mellon TAA, \$100 million from Mellon GTAA and \$70 million from Mercator.

MOTION ADOPTED UNANIMOUSLY

At the July meeting of the Investment Committee, John Moon, the portfolio manager and principal owner of Moon Capital, presented information on his firms' progress and results over the last three years since his departure from Oaktree Capital. Moon Capital is a long/short equity fund that is run with a very low net market exposure, generally under 10%. John's first two years on his own were lack luster but he has built his organization and infrastructure and it is hitting its stride. His returns are now exceeding the Oaktree Emerging Fund. The Investment Committee recommends an initial funding level of \$25 million to this product with possible additional investments in the future when funds become available from Oaktree Emerging Fund.

MOTION was made by H. Foster and seconded by R. Allen to approve the initial funding of \$25 million to Moon Capital with the possible additional investments from the Oaktree Emerging Fund when funds become available from Oaktree Emerging Fund.

MOTION ADOPTED UNANIMOUSLY

The Investment Committee also recommends committing up to \$35 million to an investment in Onset VI, a venture capital fund. From its outset, Onset works in the earliest stages of venture firms that incubate ideas into successful businesses. DPERS has invested in previous Onset Funds and received excellent returns from the Onset II, III and IV partnerships.

MOTION was made by J. Davis and seconded by R. Allen to commit up to \$35 million to Onset VI.

MOTION ADOPTED UNANIMOUSLY

During the July meeting of the Investment Committee, a presentation was made by Michael Gordon, a principal in Angelo Gordon, a current hedge fund manager for DPERS. The next meeting of the Investment Committee will be on August 19th.

4. PENSION ADMINISTRATOR'S REPORT

Legislative Update

D. Craik reported that all of the following Bills have been signed by the Governor.

- HB 153, lower vesting for the County/Municipal Police Plan to 5 years of service.
- SB 282, allows the Board to charge a penalty for late payments from entities that submit monthly payments. There will be a recommendation at the 9/08 Board meeting for discussion.
- SB 337, Disability Insurance Program clean up legislation. An LTD recipient whose benefits are terminated because of a mental illness or substance abuse diagnosis may return to the pension system if the employee was vested as of 1/1/06. Other sections of the legislation will be coordinated with the Statewide Benefits Unit.
- SB 304, regards eligibility for the Disability Insurance Program for retired troopers who have returned to employment in a position that normally would be covered by the State Employees Pension Plan. Funding to come from Homeland Security.
- SB284, technical changes in all plans for the IRS compliance project.
- Budget Bill
 - a) Four new positions to establish a call center
 - b) OPEB related issues:
 - 1) Funding continued at a rate of 0.54% of payroll (same as FY08)
 - 2) Any reimbursement for Medicare Part D premiums will be deposited into OPEB trust.
 - 3) Subcommittee to be formed by State Employee Benefits Unit to provide a report to the Governor by 4/15/09 on employee health benefit design or program eligibility options which if implemented would reduce the OPEB liability.
 - c) Language to add clarifying language that DPERS' investment records are confidential and not public records.

\$1.8 million was also in the budget for the PeopleSoft upgrade.

Quarterly Administrative Report

D. Craik reported that there was nothing unusual to report on the quarterly statistics. The new pension applications are slightly higher for the 4th quarter than the 3rd quarter. August is usually the busiest month for new applications in the Pension Office.

The Disability Pension report reflected 8 new cases and 1 pending case. These numbers continue to come down due to the new disability program.

Medical Committee Update

D. Craik reported that a new physician is being recommended for the Medical Committee. Dr. Robert B. Brereton has a B.A. from the University of Delaware, graduated from Temple University School of Medicine and did his postgraduate residency in internal medicine at the Wilmington Medical Center. Dr. Brereton has recently retired after 34 years of private practice in internal medicine. D. Craik then recommended Dr. Brereton be appointed to the Medical Committee.

MOTION was made by J. King and seconded by R. Allen to approve the recommendation of appointing Dr. Brereton to the Board of Pension Trustees' Medical Committee.

MOTION ADOPTED UNANIMOUSLY

OPEB Trust Actuarial Assumptions

D. Craik stated that the Valuation process for reconciling OPEB will be similar to how we reconcile pensions but will be using a different discount rate. There is a group working with the auditors and the Pension Office expects to have more information for the September Board meeting.

5. PENSION ADVISORY COUNCIL REPORT

C. Lister reported that things have been quiet and that the Advisory Council will not meet again until November.

6. DEPUTY ATTORNEY GENERAL REPORT

Volunteer Firemen's Pension Fund Update

C. Collins stated that the private letter ruling request has been sent to the IRS. The IRS has asked for a follow-up and everything is going smoothly.

Diamond State Port

D. Craik and C. Collins met with executives from the Diamond State Port Corporation and the Port's respective labor representative to discuss and explain the Port's revised plan document. The revised plan document incorporates the IRS tax changes and the existing Rules and Regulations. D. Craik and C. Collins explained the tax qualification project and the Cycle C filing the Board intends to submit to the IRS to obtain determination letters for DPERS' plans, including the Port Plan. C.

Collins reported that the current plan was to arrange for a meeting with the Board in August or September to obtain approval of the new plan document from the Port's Board.

FOIA Requests

C. Collins stated that there were two pending FOIA requests in process awaiting further responses from the requestors.

7. PENDING ITEMS

D. Craik stated that there were no new pending items.

8. NEW BUSINESS

R. Allen reported the following from the Audit Committee:

- The contract for the new General Ledger System has been signed.
- The KPMG Auditors will be in the Pension Office starting July 28th.
- The Pension Office is working with a professional firm to do the layout for this years CAFR.

9. ADJOURNMENT

The next Pension Board meeting is scheduled to be held on September 26, 2008, at 9:00 a.m., in the Delaware Conference Room of the Office of Pensions.

At 9:50 p.m., there being no further business, MOTION was made by R. Allen and seconded by J. King to adjourn the meeting.

MOTION ADOPTED UNANIMOUSLY

Respectfully submitted,

David C. Craik
Pension Administrator

Nancy Shevock
Acting Chair for the Board of Pension Trustees