

PUBLIC SAFETY PERSONNEL RETIREMENT SYSTEM

FUND MANAGER MEETING

March 31, 2010

MINUTES

Members Present: Mr. Mike Galloway, Chairman
Mr. Tim Dunne, Member
Ms. Lori Roediger, Member
Mr. Brian Tobin, Member
Mr. Gregory Ferguson, Member

Others Present: Mr. Jim Hacking, Administrator
Ms. Tracey Peterson, Assistant Administrator, COO
Mr. Ryan Parham, Assistant Administrator, CIO
Mr. Marty Anderson, Chief Equities Analyst
Mr. Paul Corens, Investment Analyst
Mr. Mark Selfridge, Investment Analyst
Mr. Mark Steed, Investment Analyst
Mr. Shan Chen, Investment Analyst
Ms. Michele Weigand, Investment Contracts Paralegal
Ms. Gail Nova, Administrator Manager
Ms. Bridget Feeley, Internal Audit and Compliance Officer
Mr. Paul Hemmes, Training/Audio Visual Specialist
Mr. Allen Martin, NEPC
Mr. Marc Lieberman, Kutak Rock
Judge R. Carter Olson
Mr. Brian Delfs - Excused

1. Call to Order

The meeting was called to order by Chairman Galloway at 1:03 PM.

2. **Consent Agenda** (Documentation concerning the matters on the consent agenda may be reviewed at the PSPRS office). Any matter on the Consent Agenda will be removed from the Consent Agenda and discussed as a regular agenda item, and **Action** taken, upon the request of any Fund Manager member or advisor. The Fund Manager may approve, modify or reject approval of any of the following items:

- a. Approval of the Minutes of the Fund Manager Meeting on February 24, 2010.
- b. Acceptance of Transfer Between State Retirement Systems of Reginald Relf.
- c. Acceptance of Transfer Between State Retirement Systems of Thomas Hamilton.
- d. Acceptance of Transfer Between State Retirement Systems of Steve Marrone.
- e. Acceptance of Transfer Between State Retirement Systems of Robert Hoskin.
- f. Acceptance of Transfer Between State Retirement Systems of Michael Hoeve.
- g. Acceptance of Transfer Between State Retirement Systems of Kevin Florey.
- h. Acceptance of Transfer Between State Retirement Systems of Michael Shipley.
- i. Acceptance of Transfer Between State Retirement Systems of Stephen Desens.
- j. Acceptance of Transfer Between State Retirement Systems of Newell Peterson.
- k. Acceptance of Transfer Between State Retirement Systems of Robert Topolosek.
- l. Acceptance of Transfer Between State Retirement Systems of Matthew Tanner.

- m. Acceptance of Transfer Between State Retirement Systems of Robert Churchey.
- n. Acceptance of Transfer Between State Retirement Systems of Bruce Smith.
- o. Acceptance of Transfer Between State Retirement Systems of Frank Milstead.
- p. Acceptance of Transfer Between State Retirement Systems of John O'Connor.
- q. Acceptance of Transfer Between State Retirement Systems of Jeffrey Bell.
- r. Acceptance of Transfer Between State Retirement Systems of Patrick Kelly.
- s. Acceptance of Transfer Between State Retirement Systems of Brittany Stansbury
- t. Acceptance of Transfer Between State Retirement Systems of Kyran Brennan.
- u. Acceptance of Transfer Between State Retirement Systems of Terry Wilson.
- v. Acceptance of Transfer Between State Retirement Systems of Joni Burgler.
- w. Acceptance of Transfer Between State Retirement Systems of Larry Chambers.
- x. Acceptance of Transfer Between State Retirement Systems of Mario Escudero.
- y. Acceptance of Transfer Between State Retirement Systems of Martin Broderick.
- z. Acceptance of Transfer Between State Retirement Systems of Ronald Smith.
- aa. Acceptance of Transfer Between State Retirement Systems of Norma Campbell.
- bb. Acceptance of Transfer Between State Retirement Systems of James Pool.
- cc. Acceptance of Transfer Between State Retirement Systems of Ana Valencia.
- dd. Acceptance of Elected Officials' Retirement Plan of termination of benefit of Eugenia Hummel.
- ee. Acceptance of Elected Officials' Retirement Plan of normal benefit of Richard Henry.
- ff. Authorization and approval for the Trust (through its Chief Investment Officer) to enter into a Joint Defense Agreement with Desert Troon Limited and its affiliates (in a form approved by the Trust's legal counsel) with respect to litigation threatened by Millard and Scott Seldin against the Trust.
- gg. Authorization for Kutak Rock LLP to extend its agreement with Lightstone Solutions, LLC to provide investigation services for the Trust for an additional year, and to expand such services to include annual media monitoring of each of the Trust's outside investment managers.

MOTION 3-87-10	At 1:04 PM.
Motion:	To approve the Consent Agenda as listed.
Moved by:	Greg Ferguson
Seconded by:	Tim Dunne
Discussion:	None
In Favor:	Unanimous
Motion Passes:	Passes

3. Investments - Stocks, Bonds and Others

- a. Report by the Chair of the Investment Committee, Mike Galloway, regarding the discussions that were held and the recommendations that were made in the Investment Committee meeting that was held on Wednesday, March 31, 2010 at 10:00 a.m., with discussion, and possible **Action** by the Fund Manager to approve, disapprove, or suggest modification regarding the following items:
 1. Presentation by Staff, StepStone Group and representatives of DFJ Mercury and discussion regarding a possible investment of up to \$20 million in DFJ Mercury Fund II or any appropriate feeder, blocker or parallel fund of same.

Mr. Steed gave a brief summary of the presentation given by Staff and StepStone Group at the March 31, 2010 Investment Committee meeting. Dan Watkins, Blair Garrou and Edward Hill, all Managing Directors at DFJ Mercury discussed their investment strategy and responded to Fund Managers questions.

MOTION 3-88-10	At 1:11 PM.
Motion:	To approve investment of up to \$20 million in DFJ Mercury Fund II or any appropriate feeder, blocker or parallel fund subject to legal due diligence.
Moved by:	Lori Roediger
Seconded by:	Tim Dunne
Discussion:	
In Favor:	Unanimous
Motion Passes:	Passes

2. Presentation by Staff, New England Pension Consultants (“NEPC”) and representatives of GAM USA Inc. and discussion regarding a possible investment of up to \$75 million in GAM Trading Strategy commingled fund (or any appropriate feeder, blocker or parallel fund of same).

Mrs. Roediger reported that the Investment Committee recommends an investment of up to \$75 million in GAM Trading Strategy commingled fund.

Mr. Anderson gave an overview of Staff and advisor due diligence to arrive at this recommendation. Jennifer Drake, Investment Manager and Kristin Hovencamp, Director – Institutional Sales of GAM USA Inc. presented an overview of their Firm and their investment strategy.

MOTION 3-89-10	At 1:25 PM.
Motion:	To approve investment of up to \$75 million in GAM Trading Strategy commingled fund (or any appropriate feeder, blocker or parallel fund of same) subject to due diligence and contract negotiations.
Moved by:	Tim Dunne
Seconded by:	Lori Roediger
Discussion:	
In Favor:	Unanimous
Motion Passes:	Passes

3. Presentation by Staff and discussion regarding a possible increase to the committed investment in Millennium Technology Value Partners II from up to \$20 million to up to \$30 million with this additional \$10 million to be allocated to co-investment opportunities.

Mr. Parham gave an overview of the co-investment opportunities in Millennium Technology Value Partners II.

MOTION 3-90-10	At 3:12 PM.
Motion:	To approve a \$10 million additional investment for co-investment purposes to Millennium Technology Value Partners on completion of any due diligence by Staff.
Moved by:	Tim Dunne
Seconded by:	Lori Roediger
Discussion:	
In Favor:	Unanimous
Motion Passes:	Passes

4. Presentation by Staff and Albourne Partners and discussion regarding a possible investment of up to \$20 million in Hawker Capital Harrier Master Fund or any appropriate feeder, blocker or parallel fund of same.

Mr. Anderson gave an overview of Staff and advisers research and due diligence to arrive at their decision to recommend this Fund. John Shearman of Albourne Partner summarized Hawker's investment strategy, style, capabilities and risk management process.

MOTION 3-91-10	At 1:35 PM.
Motion:	To approve investment of up to \$20 million in Hawker Capital Harrier Master Fund or any appropriate feeder, blocker or parallel fund of same subject to all of the due diligence and legal compliance.
Moved by:	Lori Roediger
Seconded by:	Tim Dunne
Discussion:	
In Favor:	Unanimous
Motion Passes:	Passes

5. Presentation by Staff and discussion with advisers and legal counsel regarding adoption of the following amendment [new paragraph 6] to Section V of the Amended Statement of Investment Policy:

"6. **Overlay Liability.** The Trust may engage in "Portable Alpha" and other investments utilizing derivative exposures as authorized by the Fund Manager upon the recommendation of staff and the Investment Consultant. Generally, Portable Alpha investments are comprised of two portions—the "*Beta*" portion, in which the Trust invests no capital at the outset but through the use of derivatives, agrees to realize the return (whether positive or negative) of a particular group of publicly traded securities over a given period [typically expressed as an agreement to experience a particular LIBOR based threshold (or index or indices)], and the "*Alpha*" portion, in which the Trust invests cash with the expectation (but not guarantee) of achieving a return in excess of a particular index or indices (or LIBOR based threshold). With respect to its investment in the *Alpha* portion, the Trust risks loss of its invested capital, as is the case with any investment. With respect to its investment in the *Beta* portion, however, the Trust's risks may equal as much as its investment in the *Alpha* portion, such that the Trust's total losses in connection with a Portable Alpha investment (or other derivative based investment) may potentially equal twice that allocated for that investment.

For example, if the Trust were to allocate \$100,000,000 to a particular Portable Alpha investment, and invest the full \$100,000,000 in the *Alpha* portion of said investment, and correspondingly, agree to experience, as the *Beta* portion of the investment, the return attributable to a \$100,000,000 investment in the S&P Index over a term equal to that of the Trust's investment in the *Alpha* portion, in the unlikely event the S&P Index fell to zero during the given investment period, the Trust would be obligated to pay \$100,000,000 as and for its obligations relating to the *Beta* portion, regardless of how the *Alpha* portion performed. Such losses are mitigated by careful monitoring of the *Beta* portion, periodic true ups of any liabilities attributable to the *Beta* portion, and generally, the ability to exit the *Beta* portion at periodic intervals in the event the index or indices to which such portion is tied appear(s) to be moving in an adverse direction (although such exit may be subject to various costs, including termination fees and penalties).

It is the Fund Manager's expectation that the Trust's liability attributable to the *Beta* portion of any Portable Alpha investment, or any investment in which there is a derivative overlay (the "Overlay") will be closely monitored by staff and the managers of such investment such that any liability attributable to the Overlay will be modest and reasonable in relation to the prospective gains of such investment. Based upon that

expectation, amounts authorized by the Fund Manager for investment in any particular Portable Alpha type security (or other investment involving one or more Overlays) may be allocated solely to the Alpha portion of such investment, with the Trust to pay periodically, with other and additional funds derived from the Trust's overall portfolio, any liability arising with respect to the Overlay portion of the investment. For purposes of illustration, if the Fund Manager were to authorize investment of \$100,000,000 in a particular Portable Alpha investment, all \$100,000,000 authorized may be invested in the *Alpha* portion of said investment, with any liability arising from the Overlay to be paid by the Trust from other Trust funds as are then available from the Trust's portfolio generally. Any monies paid by the Trust to cover an Overlay shall be accounted for by the Trust as attributable to the Portable Alpha or other investment to which such Overlay pertains. Further, when a Portable Alpha investment [or other investment utilizing an Overlay] is presented to the Fund Manager for its consideration and approval, staff shall estimate the expected range of liability that may be incurred by the Trust from the investment's Overlay so the Fund Manager can better understand the investment's potential risks."

Chair Galloway discussed the alpha and beta strategy and reported that the Investment Committee recommended that the policy change be approved with the caveat that the General Consultant, Legal and Investment Staff all agree on the methodology. If any one of the three disagree, then they have to come back to the Fund Manager to resolve the disagreement. Legal Counsel briefly discussed the liability and risks associated with the Overlay and the implications of this policy amendment. Mr. Lieberman read the following language drafted as a proposed addition to the amendment stated in the agenda item to comply with the Investment Committees recommendation: "Finally, the System's legal counsel, investment staff and external investment consultant must approve in writing (or by email) every Overlay, and in the event any one or more of them disapprove of a particular Overlay, the Overlay shall not be implemented unless first approved by the Fund Manager."

MOTION 3-92-10	At 3:20 PM.
Motion:	To approve the change in the procedures as written by Marc Lieberman and approve item 5 as written.
Moved by:	Tim Dunne
Seconded by:	Lori Roediger
Discussion:	
In Favor:	Unanimous
Motion Passes:	Passes

6. Presentation by Staff and discussion with advisers and legal counsel regarding the approval of a new Appendix V *Securities Lending Policy*; replacing and superseding the previous Appendix V of the PSPRS Amended and Restated Statement of Investment Policies.

This item was not discussed.

7. Report by Staff and discussion regarding the Month Ended and Fiscal Year-to-Date performance/portfolio update.

Mr. Anderson summarized the Month Ended and Fiscal Year-to-Date performance/portfolio update that was included in the meeting material.

8. Report by Compliance Auditor and discussion regarding investment compliance, holdings and transactions as of February 28, 2010.

Ms. Feeley reported there were no investment compliance issues to report as of the end of February.

9. Report by Staff and/or legal counsel and discussion regarding recent developments and legal issues (including settlement discussions) involving the Trust's custodians, lenders, securities lending agents, vendors, investments or investment managers or partners (as well as any investments managed by the Trust's investment managers or partners). The Fund Manager may vote to discuss this matter in Executive Session pursuant to A.R.S. §§ 38-431.03(A) (3), (4) and (7), as set forth in item 5 (a) & (b).
10. Discussion regarding amending the Fund Manager Governance Policy, and the Investment Committee Charter contained therein, to allow the Committee to be comprised of three members (constituting a quorum) of the Fund Manager.

Mr. Galloway reported that he appointed Tim Dunne to the Investment Committee technically he unwittingly put three Fund Managers on the committee when there is only suppose to be two Fund Managers on any committee. To get by that today the Investment Committee made special admonitions prior to every motion of the committee. The Investment Committee is recommending the Charter be amended to allow for both the Investment Committee and Operations Committee to be comprised of three Fund Managers for two reasons: we have it now and if we expand the Board from five to seven members it's quite possible you will have it shortly anyway. The alternative is for the Fund Manager to direct that we maintain the two and remove a member from the Investment Committee.

MOTION 3-93-10	At 3:25 PM.
Motion:	To approve the increase of the potential for three Fund Managers on any committee.
Moved by:	Tim Dunne
Seconded by:	Lori Roediger
Discussion:	
In Favor:	Unanimous
Motion Passes:	Passes

4. Other Business

- a. Report by the Chair of the Operations, Governance Policy and Audit Committee, Brian Tobin, regarding discussions that were held, the recommendations that were made, and the action that was taken in the Operations, Governance Policy and Audit Committee meeting that was held on Wednesday, March 31, 2010 at 10:00 a.m., with discussion, and possible **Action** by the Fund Manager to approve, disapprove or suggest modification regarding the following items:
 1. Discussion and *possible recommendation for Action* regarding the results of the analysis of the program by the actuary, Gabriel, Roeder, Smith & Company ("GRS"), to include benefit enhancements and setting the premium for fiscal year 2011.

Mr. Tobin reported that there is no action to be taken this month.

2. Update by Karen Lewis regarding the FY 2009, 2010 budget as of February 28, 2010 with departmental projections to the end of the fiscal year to be followed by discussion and *possible recommendation for Action*.

The 2009-10 projected budget for the System as of February 28, 2010 is in line with the budget and no action was taken.

3. Discussion between the Committee, Staff and the IT department regarding second off site back up and *possible recommendation for Action*.

Back up of the database was discussed; the committee approved the plan which they will bring back to the committee next month.

4. Review and discussion of the March 2010 bill for legal services performed in February and possible **Action** by the Committee to approve the bill.

The March 2010 bill for legal service performed in February was approved for payment.

5. Written update on the progress of the Local Board Training program with *possible discussion and recommendation for Action*.

A written update was presented and Mr. Ferguson thanked the staff for the work they were doing and that the monthly newsletter is very informative.

6. Update by Bridget Feeley and discussion regarding compliance and internal audit with *possible recommendation for Action*.

Ms. Feeley stated there was nothing to report and she is working on a risk assessment.

- b. Presentation by the System lobbyists (Representatives of P3 and HighGround) with respect to status of the System's FY 2010 legislative initiatives with discussion and possible **Action** by the Board to approve, disapprove, or modify same.

Mr. Doug Cole of HighGround and Diane McAllister of Public Policy Partners summarized the progress of the PSPRS legislative initiatives.

- c. Presentation by representatives of Gabriel, Roeder, Smith regarding the Assumed Earnings Rate for the fiscal year beginning July 1, 2011 and possible **Action** by the Board to approve, disapprove, or modify same.

Mr. Brian Murphy of Gabriel, Roeder, Smith discussed this topic with the board.

MOTION 3-94-10	At 2:37 PM.
Motion:	Drop the DROP plan calculation by one quarter of a percent effective fiscal year 2011 (from 8.50% to 8.25 %) which will impact employers two years and three months from now.
Moved by:	Tim Dunne
Seconded by:	Brian Tobin
Discussion:	Judge Carter clarified that just the assumed earnings rate is being adjusted.
In Favor:	Unanimous
Motion Passes:	Passes

- d. Discussion regarding possible changes to the membership of the committee of the Fund Manager created to conduct interviews in order to select a new Administrator and possible **Action** to approve, disapprove, or modify same.

Mr. Dunne wished to swap Barrett Baker for Gordon Clark from the new membership committee of the Fund Manager created to conduct interviews in order to select a new Administrator and the board wished to add the name of Charles Flannigan of Assistant Director of the Department of Corrections has volunteered to join the committee.

MOTION 2-95-10	At 3:45 PM.
Motion:	To amend the selection committee to replace
Moved by:	Greg Ferguson
Seconded by:	Tim Dunne
Discussion:	None
In Favor:	Unanimous
Motion Passes:	Passes

- e. Discussion regarding Fund Manager requests to participate in training, educational and due diligence opportunities with possible **Action** by the Board to approve, disapprove, or suggest alternative training and education seminars and/or due diligence opportunities.

Mr. Galloway stated the FTSE conference does not pay for the hotel which is 190 Euros per night. There was no further discussion.

- f. Discussion and possible **Action** by the Fund Manager regarding HB 2003 and the implications for PSPRS and Staff. The Fund Manager may vote to discuss this matter in Executive Session pursuant to A.R.S. § 38-431.03 (A) (1) as set forth in item 5(c).

MOTION 3-96-10	At 3:49 PM.
Motion:	To go into Executive Session to include Judge Carter Olson will remain for his knowledge of the matter.
Moved by:	Lori Roediger
Seconded by:	Greg Ferguson
Discussion:	None
In Favor:	Unanimous
Motion Passes:	Passes

The Administrator was directed to act on what was discussed and to coordinate that with the Vice Chairman, Brian Tobin.

- g. Discussion with the Fund Manager and instruction to legal counsel regarding ongoing or threatened legal action involving the Arizona PSPRS Trust, the System, or the System's sister plans (EORP or CORP), including Campbell, Swink, Hosea, Miller, Martin, ApexCapital, Staeck, BNY Mellon, Pivotal Group, Desert Troon, Seldin, Parker, Loftus, JP Morgan Chase, Toyota, and Countrywide matters and possible **Action** regarding same. The Fund Manager may vote to discuss these matters in Executive Session pursuant to A.R.S. §§ 38-431.03(A) (1), (2), (3), (4), and (7), as set forth in items 5(a) and (b).

5. Executive Session for Legal Matters in Accordance with A.R.S. §§ 38-431.03(A) (1), (2), (3), (4), & (7). The Fund Manager may vote to go into Executive Session to discuss matters pursuant to A.R.S. §§ 38-431.03(A)(1), (2), (3), (4), and (7) including to obtain legal advice from the Board's attorney on any matter listed on the agenda, including:

- a. Discussion and consultation with legal counsel regarding legal issues, and settlement discussions, if any, arising in connection with the Arizona PSPRS Trust's real estate, private equity, hedge and other investments, including those managed by the Pivotal Group, ApexCapital Management, and Desert Troon Limited, pursuant to A.R.S. §§ 38-431.03(A)(3), (4) and (7).
- b. Discussion and consultation with legal counsel and Staff regarding ongoing or threatened legal action involving the Arizona PSPRS Trust, the System or the System's sister plans (EORP or CORP), including contemplated internal investigation and interview guidelines, investment

related matters, EEOC charges, and cases, including Campbell, Swink, Hosea, Miller, Martin, Cross, ApexCapital, Staeck, BNY Mellon, Pivotal Group, Desert Troon, Seldin, Parker, Loftus, JP Morgan Chase, Toyota, and Countrywide matters, pursuant to A.R.S. §§ 38-431.03(A)(3), (3), (4), and (7).

- c. Discussion and consultation with legal counsel and Staff regarding implications of HB 2003 on PSPRS and Staff, pursuant to A.R.S. § 38-431.03 (A) (1).

6. Call to the Public:

Jim Mann, Executive Director of the Fraternal Order of Police spoke regarding the impact to budgets of the counties and municipalities within the next two years.

This is the time for the public to comment. Members of the Fund Manager may not discuss items that are not specifically identified on the agenda, except to address criticism from the public. Therefore, pursuant to A.R.S. § 38-431.01(H), the Fund Manager’s reaction to any public comment is limited to addressing criticism or recommending that the Fund Manager or Staff respond or study such comment or schedule the subject matter for further consideration at a later date after appropriate notice.

7. Set Next Meeting Date

The next meeting is scheduled for Wednesday, April 28, 2010.

8. Adjournment

The meeting was adjourned at 4:19 PM.

Mike Galloway, Chairman

Brian Tobin, Vice Chairman

Gregory Ferguson, Member

Tim Dunne, Member

Lori Roediger, Member