PUBLIC SAFETY PERSONNEL RETIREMENT SYSTEM
BOARD OF TRUSTEES MEETING

February 29, 2012

MINUTES

Mr. Brian Tobin, Trustee, Chairman
Mr. Gregory Ferguson, Vice Chairman, Trustee
Mr. Jeff McHenry, Trustee
Ms. Randie Stein, Trustee
Mr. Richard Petrenka, Trustee
Mr. Lauren Kingry, Trustee
Mr. Jim Hacking, Administrator
Mr. Ryan Parham, Assistant Administrator / Chief Investment Officer
Mr. Jared Smout, Deputy Administrator
Mr. Marty Anderson, Deputy Chief Investment Officer
Mr. Pascal Stalder, Deputy Chief Investment Officer – Risk
Mr. Anton Orlich, Lead Investment Analyst
Mr. Paul Corens, Senior Investment Analyst
Mr. Mark Selfridge, Senior Investment Analyst
Mr. Shan Chen, Senior Investment Analyst
Mr. Mark Steed, Lead Investment Analyst
Ms. Michele Weigand, Senior Contracts Specialist
Mr. Fred Stork, Assistant Attorney General
Ms. Bridget Feeley, Internal Audit and Compliance Officer
Mr. John Hendricks, Accounting Manager
Mr. Don Stracke, Senior Consultant, NEPC, LLC
Mr. Jay Rose, Partner, StepStone Group
Mr. Marc Lieberman, Partner, Kutak Rock
Mr. Daniel S. Smith, President, Desert Troon Companies
Mr. Daniel R. Hammons, V.P. / Chief Financial Officer, Desert Troon Companies
Mr. Doug Cole, HighGround
Ms. Dianne McAllister, Public Policy Partners

1. Call to Order; Roll Call; Opening remarks ......................................................, Mr. Brian Tobin
.......................................................................................................................... Chairman

The meeting was called to order at 1:02 p.m. by Chairman Tobin and he welcomed Mr. Fred Stork, Assistant Attorney General, who is assisting PSPRS on a part time basis. The Governor’s appointment of Mr. William Davis as the seventh member of the Board was announced. Mr. Davis was introduced. Due to an impasse over the state budget, a number of confirmations are being delayed in the State Senate, including Mr. Davis’ confirmation. As a result, Mr. Davis will be attending today’s meeting as a member of the public.

2. Appropriate Action for approval of the 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 upon the request of any member of the Board of Trustees.
a. Acceptance of Elected Officials' Retirement Plan of survivor benefit of Marilyn Falbo
b. Acceptance of Elected Officials' Retirement Plan of survivor benefit of Patricia Ann Georgeff
c. Acceptance of Elected Officials' Retirement Plan of early benefit of Michael D. Jones
d. Acceptance of Elected Officials' Retirement Plan of normal benefit of Raymond P. Lee
e. Acceptance of Elected Officials' Retirement Plan of suspended normal split benefit of Cherie Mangum
f. Acceptance of Elected Officials' Retirement Plan of early benefit of Claude Mattox
g. Acceptance of Elected Officials' Retirement Plan of normal benefit of George H. Nault
h. Acceptance of Elected Officials' Retirement Plan of survivor benefit of normal split benefit of Natalie Rodriguez
i. Acceptance of Elected Officials' Retirement Plan of termination of normal benefit of Michael Ryan
j. Acceptance of Elected Officials' Retirement Plan of termination of early benefit of Alberta M. Smith
k. Acceptance of Elected Officials' Retirement Plan of termination of normal benefit of Dean Weatherly
l. Acceptance of Transfer Between State Retirement Systems of Paula Krueger
m. Acceptance of Transfer Between State Retirement Systems of Dart Craytor
n. Acceptance of Transfer Between State Retirement Systems of Gloria Egurrola
o. Acceptance of Transfer Between State Retirement Systems of Mary Garcia
p. Acceptance of Transfer Between State Retirement Systems of David Adams
q. Acceptance of Transfer Between State Retirement Systems of Stephan Heenan
r. Acceptance of Transfer Between State Retirement Systems of Kenneth Buckner
s. Acceptance of Transfer Between State Retirement Systems of John Dietel
t. Acceptance of Transfer Between State Retirement Systems of Vivienne Kirk
u. Acceptance of Transfer Between State Retirement Systems of Harry Scott
v. Acceptance of Transfer Between State Retirement Systems of Misael Avila
w. Acceptance of Transfer Between State Retirement Systems of John R. Jones
x. Acceptance of Transfer Between State Retirement Systems of Barbara Wilding
y. Acceptance of Transfer Between State Retirement Systems of Jessie Jimenez
z. Acceptance of Transfer Between State Retirement Systems of Dennise Leon
aa. Acceptance of Transfer Between State Retirement Systems of Randy Green
bb. Acceptance of Transfer Between State Retirement Systems of Brittany Beauchamp
c. Acceptance of Transfer Between State Retirement Systems of Steven Heatherington
dd. Acceptance of Transfer Between State Retirement Systems of Chad Austin
e. Acceptance of Transfer Between State Retirement Systems of David Calles
ff. Acceptance of Transfer Between State Retirement Systems of Jeffrey Glover
MOTION: 2-86-12  At 1:03 p.m.
Motion: To approve the Consent Agenda.
Moved by: Mr. Ferguson
Seconded by: Mr. Petrenka
Discussion: None
In Favor: Unanimous
Motion: Passes

3. Appropriate Action regarding the Minutes of the January 25, 2012 meeting of the PSPRS Board of Trustees.................................................................Mr. Brian Tobin

MOTION: 2-87-12  At 1:93 p.m.
Motion: To approve the Minutes of the January 25, 2012 meeting of the PSPRS Board of Trustees as presented.
Moved by: Mr. Ferguson
Seconded by: Mr. Mc Henry
Discussion: None
In Favor: Unanimous
Motion: Passes

Report by Mr. Richard Petrenka, Chairman of the Investment Committee regarding agenda items 4 through 9 which were discussed at the Investment Committee meeting held today, February 29, 2012, on or after 10:00 a.m., and possible Action on the Committee’s recommendations to the Board regarding same.

4. Investment Update Report by Desert Troon Companies and Investment Department Staff representatives and discussion regarding the assets of the Trust which are being managed by Desert Troon Companies ......................Mr. Daniel S. Smith, President .................................................................Mr. Daniel R. Hammons, V.P. / Chief Financial Officer .................................................................Desert Troon Companies

Mr. Parham reported that we have done business with Desert Troon Companies for about eighteen years. They have added to their management the assets formerly held by Apex Capital and Pivotal. We have taken a complex set of real estate assets from multiple sources and combined them under the management of Desert Troon. The Desert Troon’s properties are concentrated in the Southwest. Mr. Dan Smith summarized the history, organization, key personnel, ten years of asset history and the last two years of investments managed by Desert Troon for the Trust. The specifics of their history, market value, cash flow projections were discussed. Also members of the Board talked about a cross section description of the assets of DTRI (Fund 1), DRTIC (Fund 2) and the newly formed DT Fund 3. The ten year business plan, which was reviewed by Ernst & Young, was also discussed. Mr. Parham stated that Investment Staff is currently looking for a third party buyer interested in exposure in the Southwest in order to prudently reduce the real estate portfolio and to maximize capital.
5. Report by Investment Department Staff and discussion regarding the Month Ended and Fiscal Year-to-Date performance/portfolio with an overview of the Public Equities asset class  

Mr. Ryan Parham  
Chief Investment Officer  

Mr. Parham informed the members of the Board that the NEPC Quarterly Report will be delayed until the April meeting.

He reported that the total fund returned 2.05% as compared to the target benchmark of 2.87%; thus, the fund is underperforming by 82 basis points. This is due to underweight exposure to equities, which is in part to compensate for our 4% to 5% overweight to real estate and in part due to our reluctance to attain full beta replication for portable alpha during the switch from Mellon Bank to State Street. Although we had anticipated a quick transition, the equity market reports at that time were strongly suggesting economic conditions that could produce a downturn of 30-40%. In order to de-risk the portfolio, we reduced the exposure to equities. The downturn lasted several months which resulted in an underexposure to equities in November and December of 2011. Since then, we have been dollar cost averaging to attain our full beta exposure and complete the transition to State Street with less tracking error. In the next few months we will review our asset allocations and the asset class targets.

The Gabriel Roeder Smith actuaries completed a cash flow analysis for the System. Based on previous surveys, we had anticipated being cash flow positive over the next 12-18 months. However, recent legislation has changed the behavior of our beneficiaries such that more participants are retiring than expected and that has increased our liabilities and our cash flow requirements. This, in turn, necessitates our having more liquidity in our total fund configuration than we had originally thought necessary. We have deleveraged and stabilized the portfolio but we must work with the current cash flow situation. The money for the capital calls must come out of liquid assets such as equities.

6. Presentation by Investment Department Staff and StepStone Group representatives and discussion and possible Action regarding an investment of up to $50 million in Denham Commodity Partners Fund VI, L.P. or appropriate feeders, blockers, or associated or parallel funds of same managed by Denham Capital Management L.P.  

Mr. Paul Corens  
Senior Investment Analyst  

Mr. Jay Rose  
Partner, StepStone Group  

Mr. Corens informed the members of the Board that Denham Commodity Partners is a global energy manager concentrating on energy from oil and gas exploration, power generation from traditional sources, and natural resource mining. He added that StepStone and Albourne recommend this investment.

Mr. Rose stated that StepStone recommends this investment due to worldwide population growth, economic advancement of emerging and developing countries, and urbanization of the emerging and developing countries. Denham is a best in class fund which has an excellent risk department and teamwork. They are in the top quartile in terms of their annualized rate of return.
MOTION: 2-88-12  At 2:30 p.m.
Motion: To accept the Investment Committee recommendation to invest up to $50 million in Denham Commodity Partners Fund VI, L.P. or appropriate feeders, blockers, or associated or parallel funds of same managed by Denham Capital Management L.P.
Moved by: Mr. Petrenka
Seconded by:
Discussion: None
In Favor: Unanimous
Motion: Passes

7. Presentation by Investment Department Staff, and NEPC, LLC representatives and discussion and possible Action regarding an investment of up to $40 million in Centerbridge Special Credit II, L.P., or appropriate feeders, blockers, or associated or parallel funds of same managed by Centerbridge Partners, L.P. ..........Mr. Mark Steed ............................................................. Lead Investment Analyst ............................................................. Mr. Don Stracke ............................................................. Senior Consultant, NEPC, LLC

It was stated by Mr. Steed that PSPRS has had an ongoing relationship with Centerbridge since 2009. Centerbridge invests in stressed and distressed credit and has an 18% IRR. This investment is a substantial opportunity for the System and StepStone and Albourne agree. The Centerbridge Special Credit II, L.P. has a three year investment period and a fund life of seven years.

MOTION: 2-89-12  At 2:34 p.m.
Motion: To accept the Investment Committee recommendation to invest up to $40 million in Centerbridge Special Credit II, L.P., or appropriate feeders, blockers, or associated or parallel funds of same managed by Centerbridge Partners, L.P.
Moved by: Mr. Petrenka
Seconded by:
Discussion: None
In Favor: Unanimous
Motion: Passes

8. Presentation by Investment Department Staff and NEPC, LLC representatives and discussion and possible Action regarding the approval of certain proposed revisions to the Asset Allocation targets which are stated in Appendix I Asset Allocation Policy; replacing and superseding those targets .........................Mr. Ryan Parham ............................................................. Mr. Allan Martin ............................................................. Partner, NEPC, LLC

This item was tabled until the April 4, 2012 Board of Trustees meeting.

9. Report by NEPC representative(s) on the Second Fiscal Quarter (Fourth Calendar Quarter) Performance of the System ............................................................. Mr. Allan Martin

This item was tabled until the April 4, 2012 Board of Trustees meeting.
10. Report by Investment Department Staff representatives and discussion regarding Portfolio Exposures. Mr. Pascal Stalder, Deputy Chief Investment Officer – Risk

Mr. Stalder referred to the FY 2012 currency exposure and indicated that the largest category is U.S. currency. A discussion was held about the relative volatility contributed by the different asset classes over the past twelve months. Mr. Stalder compared each asset class to the others. He pointed out that there is low correlation between asset classes and that the asset class with the greatest volatility is equities. Real estate and private equity volatility have been underestimated as contributing to the portfolio volatility over the last twelve months.

Presentation by Mr. Gregory Ferguson, Chairman of the Operations, Governance Policy and Audit Committee regarding agenda items 11. through 24. which were discussed at the Operations, Governance Policy and Audit Committee meeting held today, February 29, 2012, on or after 11:00 a.m., and possible Action on the Committee’s recommendations to the Board regarding same.

11. Presentation of the Month-to-Date Budget Report for FY 2012 and possible Action on same Mr. John Hendricks, Manager of Finance and Accounting

It was reported by Chairman Ferguson that we are over budget for the line item relating to the office renovation due to the reconfiguration of the PSPRS second floor space for additional staff offices. But the major contributor to the over budget situation is legal fees, some of which is litigation-related but most of which is the result of investment activity and our still not having on staff an in-house investment counsel.

12. Status report on the filling of vacant staff positions and possible legislation that may affect the filling of vacant positions Mr. Jim Hacking, Administrator

Mr. Hacking said the filling of the vacant position for in-house investment counsel will be discussed in Executive Session later today.

13. Written update on the progress of the Local Board Training Program and discussion and possible Action regarding the same Mr. Robert Ortega, Local Board Training Coordinator and Human Resources Manager, Mr. Don Mineer, Local Board Training Specialist

A written report was presented in the materials provided the Board of Trustees.
14. Review, discussion and possible Action regarding the February 2012 Kutak Rock billing for legal services performed in January 2012.................................Mr. Jim Hacking

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<tr>
<th>MOTION: 2-90-12</th>
<th>At 2:47 p.m.</th>
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<tr>
<td>Motion:</td>
<td>To accept the recommendation by the Operations, Governance Policy and Audit Committee to approve the February 2012 Kutak Rock billing for legal services performed in January 2012.</td>
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<tr>
<td>Moved by:</td>
<td>Mr. Ferguson</td>
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<td>Seconded by:</td>
<td>Mr. Tobin</td>
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<td>Discussion:</td>
<td>None</td>
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<td>In Favor:</td>
<td>Unanimous</td>
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<td>Motion:</td>
<td>Passes</td>
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15. Discussion and possible Recommendations regarding the setting of the employer paid premium for FY 2013 for the Fire Fighter and Peace Officer Cancer Insurance Plan .........

.................................................................................................................................................................Mr. Jim Hacking

This was tabled until the April 4th meeting.

16. Status report regarding the fiduciary insurance for the PSPRS Board of Trustees ..........

.................................................................................................................................................................Mr. Jared Smout

.................................................................................................................................................................Deputy Administrator

It was reported by Mr. Smout that in speaking with the head of the Risk Management Department of the Arizona Department of Administration, we are covered regarding fiduciary insurance. Kutak Rock is looking into further details with respect to possible gaps in coverage. The staff will again present this agenda item during the April Operations, Governance Policy and Audit Committee meeting.

17. Status report on the legal challenges to the various provisions of SB 1609 ............

.................................................................................................................................................................Mr. Jim Hacking

Mr. Hacking listed four separate law suits resulting form SB 1609. The retired judges are challenging the EORP cost of living adjustment (COLA) changes; the active judges are also challenging the EORP COLA changes and the increased member contribution rates. The retired police officers are challenging the PSPRS COLA changes; and the active police officers are challenging the PSPRS COLA changes and increased member contribution rates.

18. Status report with respect to the distribution of the Annual Member Statements ...........

.................................................................................................................................................................Mr. Jared Smout

Mr. Smout reported that state statutes require that Annual Member Statements be available for members who request them. In the past we have given the statements to the employers who then distribute them to the members. With the advent of the internet, PSPRS now has these statements available on-line for anyone at any time. The final time these statements were distributed to the employers was last June 30th. This year, and in subsequent years, the Member Statements will be available on-line. A
notice regarding this has been sent out.

19. **Status report with respect to the Lease Extension Agreement with Dinan & Company, LLC** ...............................................................................................................................................................Mr. Jim Hacking

Mr. Hacking informed the Board of Trustees that Dinan & Company is renting two thirds of the first floor of the PSPR building. A market comparison of square footage rates for commercial office space in the Camelback corridor was completed and a proposal was presented to Mr. Dinan. He accepted the proposal and we have now executed a five year lease extension so that the lease agreement will run through the end of September 2017.

...............................................................................................................................................................Mr. Jim Hacking

The Governance Manual revisions are being worked on and will be e-mailed to the members of the Operations Committee prior to the next meeting.

21. **Status report on the confirmation process with respect to the Governor’s newest nominee to the Public Safety Personnel Retirement System Board of Trustees, William C. Davis and with respect to the re-nomination of Gregory S. Ferguson to the Board of Trustees** ...............................................................................................................................................................Mr. Jim Hacking

Mr. Hacking reported that the Governor has appointed Mr. William Davis to the Board of Trustees. Although Mr. Davis has had his confirmation hearing before the Senate Finance Committee, the remainder of the confirmation process has been delayed due to an impasse between the Governor’s Office and the Senate leadership over the FY’13 budget. He also told the Board that Mr. Ferguson has been reappointed and, because he is already serving on the Board, he will just continue to serve, pending the completion of the confirmation process in the Senate.

22. **Status report on the Public Safety Personnel Retirement System staff compensation review** ...............................................................................................................................................................Mr. Jim Hacking

As a result of a Request for Proposal to review our staff salary ranges and the Investment staff’s Incentive Compensation Program, three well known external compensation consulting firms have responded. However, this matter has been put on hold, at least temporarily, as a result of the HB 2571, the Personnel Reform initiative coming from the Governor’s Office.

In its current form, HB 2571 would place all PSPRS staff positions under the Arizona Department of Administration (ADOA). Since the inception of PSPRS, the System’s staff has never been under the control of ADOA.
23. **Report, discussion and possible Recommendation** regarding investment compliance, holdings and transactions as of January 31, 2012; and operations compliance, internal audit examination and procedures. 

Ms. Bridget Feeley, Internal Audit and Compliance Officer

There are currently two compliance issues pending. The internally managed fixed income portfolio exceeds the 5% threshold and since January 31, 2012 the total real estate portfolio is in excess of the 12% Board approved range maximum. Internal reviews of member refunds, travel and expense reimbursements, and an update of the internal audit plan as requested by the Operations, Governance Policy and Audit Committee have been completed. Ms. Feeley said once the Systems Development team has completed updates to our internal computer program, an audit of the program’s access control will be conducted.

24. **Discussion and appropriate Action** regarding Board of Trustee member requests to participate in training, educational and due diligence opportunities.

Mr. Brian Tobin

There were no requests.

25. **Discussion and Recommendation** regarding the filling of the position of In-house Investment Counsel.

Mr. Jim Hacking

To be discussed in Executive Session.

26. Call to the Public

This is the time for the public to comment. Members of the Board of Trustees 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 Board of Trustees’ reaction to any public comment is limited to addressing criticism or recommending that the Board of Trustees or Staff respond or study such comment or schedule the subject matter for further consideration at a later date after appropriate notice.

No members of the public came forward to comment.

27. Set the next meeting date. (Currently scheduled for Wednesday, April 4, 2012.)

The date remains the same.


Mr. Jim Hacking

Mr. Cole of HighGround summarized the PSPRS bills -- SB 1115 and SB 1116, which have passed the Senate and have been heard in the House committee. They are expected to pass without any problems. However, the PSPRS HB 2087, which would make explicit the Board’s authority to enter into employment agreements with key staff, has been put on hold because of HB 2571; that bill would prohibit state agencies from entering into employment contracts. SB 1120, which would have accelerated the
effective date of the new COLA mechanism for CORP and EORP, has been held in the House and been reassigned to the Appropriations Committee. SB 1211, which would require a refund of contributions (with interest) made by members when they are in the DROP was approved in the Senate. However, its prospects in the House are uncertain. The actuaries have determined that this proposal would add 1.7% to employer contribution requirements.

29. Discussion and consultation with legal counsel and Staff regarding proposed legislation, ongoing, contemplated or threatened legal action involving the Plans, including vendor disputes, public record requests, personnel matters and actual or potential litigation and claims based on contract, tort or statute, including matters involving Bank of America, BNY Mellon, judges Thompson and Hall, retired judges Fields and Lankford, Huggins, retired police officers Rappleyea and Everson, Cross, Martin, the Pivotal Group, APEX Capital Management 1, U.S. Bank, the Seldins, and Stroh Ranch Development. The Board 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 item 30.

30. The Board of Trustees may vote to go into Executive Session (which will not be open to the public) to discuss matters pursuant to A.R.S. §§ 38-431.03(A) (1), (2), (3), (4) and (7), as applicable, including to obtain legal advice from the Board’s attorney on any matter listed on the agenda, including:

a. Discussion with legal counsel regarding the filling of the position of In-house Investment Counsel and the effect HB 2571 may have on the ability to recruit such Counsel and/or retain key staff.

b. Discussion regarding the filling of the position of In-house Investment Counsel.

c. Status report from Ben Cooper of Steptoe & Johnson LLP regarding the three (3) lawsuits challenging provisions of Senate Bill 1609.

d. Discussion with Michael Sillyman of Kutak Rock LLP regarding the settlement offer in the John Martin v. Corrections Officers Retirement Plan lawsuit.

e. Discussion with legal counsel (and possible recommendation to the Board of Trustees) about legal developments, claims and issues (including settlement discussions) involving investment-related public record requests as well as the Plans’ contracts and investments, including legal matters concerning the Plans’ custodians, lenders, securities lending agents, investment contracts, vendors, advisors, investment managers or joint venturers (as well as any investments managed by the Plans’ investment managers or joint venturers). The Board may vote to discuss these matters, wholly or in part, in Executive Session pursuant to A.R.S. §§ 38-431.03(A) (2), (3), (4) & (7). Matters discussed may include claims or potential claims by or against (or issues concerning) Bank of America, BNY Mellon, Stroh Ranch Development, The Pivotal Group, Apex Capital Management 1, U.S. Bank and/or Millard and Scott Seldin.

f. Discussion and consultation with legal counsel and Staff regarding ongoing or threatened legal action involving the Plans, including internal investigations, public record requests, and actual or potential litigation and claims based on contract, tort or statute, including those involving Huggins, Cross, Martin,
judges Thompson and Hall, retired judges Fields and Lankford, and retired police officers Rappleyea and Everson, pursuant to A.R.S. §§ 38-431.03(A) (2), (3) and (4).

**MOTION: 2-91-12**  
At 3:35 p.m.  
Motion: To recess Open Session and enter Executive Session  
Moved by: Mr. Ferguson  
Seconded by: Mr. McHenry  
Discussion: None  
In Favor: Unanimous  
Motion: Passes

**MOTION: 2-92-12**  
At 5:23 p.m.  
Motion: To reinstate the Ad Hoc Committee for the search for in-house investment counsel. The members of the committee are Mr. Kingry, Ms. Stein, and Mr. Tobin.  
Moved by: Mr. Ferguson  
Seconded by: Mr. McHenry  
Discussion: None  
In Favor: Unanimous  
Motion: Passes

31. Adjournment

The meeting was adjourned at 5:30 p.m.

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Brian Tobin, Chairman

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Gregory Ferguson, Trustee,  
Vice Chairman

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Randie A. Stein, Trustee

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Jeff Allen Mc Henry, Trustee  

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Richard J. Petrenka, Trustee

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Lauren Kingry, Trustee