

**Lower Saucon Township
Pension Advisory Committee Meeting
June 17, 2009
Minutes**

Roll Call:

Present: Jack Cahalan, Township Manager; Priscilla deLeon, Mary Curtin, Molly Bender, Cathy Gorman and Chuck Friedlander. The time was 11:00 AM. Linda Costa arrived at 11:33 AM.

1. Mr. Cahalan said Vic Koszi just retired from the Township Police Department. He left at the end of March and accepted employment from the casino. He was our representative for the Police Pension Plan and he and Cathy have been communicating with the Police Association representatives to find out if they will have a member to represent them for the Pension Advisory Committee. Vic was here on Monday and he is very busy at his new job. We notified you and announced that Fran LaBuda wished to resign from the Pension Planning Committee as he's undergoing medical treatment. We also sent him a card.
2. Mr. Cahalan said we can go over Chuck's report. Priscilla said doesn't Linda have to be here for that? Chuck said no, and there are two reasons. First of all, she's going to tell you about what's been going on in 2009. His snapshot is before 2009. When he was last here, it was very early in the year. The markets were still doing badly. He is going to digress a little bit and talk about what the goal is here and what actuarial funding is. This is not a year-to-year mission. It's a forty, fifty, sixty year project. He's making assumptions. He's looking at the youngest officer who might be twenty and may not retire for another twenty-five years and may collect for another twenty-five, thirty years of pension after that. The goal is to build the cost of pensions into that cost. On a municipal level, as your employees are generating good for the township, working for the township, the idea is to fund the benefits out of their salary to fund the benefits while people are working. The way funding methods work, we have a regular annual cost to fund the benefits on a level basis, but we also have additional payments and we generally spread those out over a certain number of years. Again, with the idea the market is going to jump up and down, what Actuaries do in terms of funding methods and assumptions is try to level this out over long periods of time. Obviously, we had a real bad market and a couple of things helped to change that. One of them was the big drop in the assets which we recognized over a four year period.

Linda Costa arrived. The time was 11:33 AM.

Jack said they are going to get Bill Bender on a conference call. Bill said he has the fortune of giving an update versus when Peter was here in February. Following up on last year's market, in January and February's market, we actually hit a low in the market on March 8. That is very significant because as we sit here today we think the markets hit the May 8 bottom which was around 6,500 on the DOW. If you follow the market, we feel that was the bottom. Since then, we hit what we call a perfect V which is a rapid recovery with the DOW today 2,000 points higher and we're at 8,500, which is exactly a 30% rally on the bottom. What does it mean for the year – the market actually began the year, the DOW, a little higher than it is right now. The S&P is up about 2% or so. Linda said she emailed the handouts from May. Bill said if you look at the 5th page of our May report through May, the indexes are there. The DOW was down 1.6% and the S&P was up 3%. There's still some red on the board from some of the small cap values and growth. If you come down on the index page, notice that the Russell 1000 Growth was up 10% year-to-date, but the Russell 1000 Value was down 2%. This means a little bit of the market is recovering and clear leadership coming from certain segments. There are other segments such as the financials that have continued to lag. How that relates to your pension, if you look at the first page just for a summary of the PSAB MRT through May, we are actually doing very well - year-to-date versus our index. Our plan managed account was up 6.2%. Looking at the indexes, there's not a lot up over 6% including the bonds. Our whole portfolio is up 6.2%. The index we measure against, which is based on our investment policy, would have been up 2.2%, so we are outperforming our state objective by 4% year-to-date through May. The way we've done that, is on the third page of our report where we show our re-balance to the committee every month. The

committee and Merrill Lynch have over weighted large growth and under weighted large value. Our target for both of those is 14%, and they are only 9% large value at this time, but we're 13-1/2% large growth. Large growth is out performing considerably more than value, so we have gained on one end because we are in the right place with your money and that has benefited us. Last year we added a manager, Aletheia, to our mix. At the end of our 4Q08, Aletheia is up 21% versus 10%, so by our management and helping the plan, we've hired good managers who are meeting their index and we've allocated your money to the right place that's making us money, so those appear to be the reasons why we are beating the index. We did so without taking any more risk. He knows a lot of the questions in February were concerns, but what we didn't do was go and jump in feet first. We are still under weighted in equities. Our target for our balanced fund is 55%, we're currently at 50%. Our target for fixed income is 40% and we are over weighted by 44% and continue to want to protect the portfolio, although we've had a 30% recovery from the bottom, the market is still down 40% from the top. The growth from here is going to be slower. In our opinion, we're not going to see rapid growth for the next six months. The committee and Merrill have been taking a cautious approach. We are meeting on the 30th, we are in the midst of a manager search. We currently have a large amount of money with Wedge who has managed our balanced bond portfolio for ten years. They are a terrific bond manager. They are beating their index this year, up 2.6% versus .96%, and that is a good thing, but the exposure to one style. We think going forward, you hear a lot of talk about interest rates going way back up, inflation, risk, so he and Peter have asked the committee to consider a search to further diversify our bond managers so we are looking at a short term bond manager to add to our players and field of managers. We are also considering TIPS, Treasury Inflation Protection Securities, and we are looking, while the markets are stable, just to enhance the fixed income side of our portfolio. We are very satisfied with the managers in our mix. When you see NWQ of 30% versus 3%, that's a good manager. Wentworth is up 28% versus 6%. Aletheia is up 21% year-to-date versus 10%. We have a great variety of managers. Our long term track record speaks for itself and as far as 2009 is going, we're very happy, but we're not taking our eye off the ball. We are looking at some bond managers to enhance in the event that we see rates start to climb unexpectedly. We do continue, as Peter and Chris told you last meeting, to meet monthly instead of quarterly just to update the market as we are moving so quickly. We thought it was prudent to have more contact, not less, and the hands on approach of PSAB with us has been very helpful. Things are looking better. On the forecast, we think recession is expected to end, by that, seeing nominal growth, a GDP occur in the third or fourth quarter of this year. Earnings are looking better. We made it through the first quarter and earnings are doing very well. Earnings will start coming out next month, so we'll see things better based on how earnings are looking. You see oil going up and that concerns you, but we don't think it's going to \$100 or \$150 a barrel again. It's just a short term rise in commodity prices. We think it's probably stabilizing here in the \$70 to \$80 a barrel. Every day is a challenge. We come in and we certainly beat our index by quite a bit last year, so one would think if we took a conservative position, we might be way underperforming this year. That's not the case as we continue to outperform in PSAB and a 4% out performance for half a year, in our world, is not just good, it's very good. Typically, if you can beat the indexes by 1% to 2%, you'd be happy on an amortized schedule over time. We're very happy, but we remain cautious. We've not increased equities up to 50% or 60%. We're not managing this portfolio with over aggressiveness, so we're getting these numbers and being cautious. He hopes you get a better feel since February to June that it feels like things have improved quickly. Now that we're here, it's time to be cautious again and stay the course and look down the road a bit and say what can we do to stay on top of things and what can we do should things turn nervous again. He will open it up for questions and see what's on everybody's mind.

Jack said on the Chase, that's your second largest manager allocation, what's the story with them? Bill said that's a great question and a great observation. We have two growth managers, Chase and Aletheia. Before hiring Aletheia, we had all our money with Chase and they have been in the plan for ten years. Chase is much more conservative. If you were to go back in time to last year, where the markets were very, very erratic, Chase outperformed immensely. Chase doesn't take the more aggressive holdings. He attempts to have a style in growth that is conservative. He looks for value in gross stock. He's not surprised Mr. Chase is underperforming because what stocks are moving – more technology stocks. When we hired Aletheia, they are a perfect compliment to Chase. What happens is Aletheia is our manager who will do great when

the markets are running up and Chase is the person who protects us when times that the market is going down. We're not concerned about him, and what you are going to see here is Chase is going to be picking up as the year goes up. Chase owns Apple, Best Buy, Coca Cola, Direct TV, Disney, Corning, EMC, IBM, McDonalds, Oracle, great companies. It's just when you measure his holdings, he's not doing as well as Aletheia. What we will probably see is a little bit of catch up. He'll move up a little and Aletheia will slow down. We're going to hang in there with Chase for sure.

Linda said that's what they were wondering also about Chase. She guesses that points out the highlights of the MRT. It's all about the process. We follow the process. We have a diligent process. We look to see if we have too much money in one place, are we going to spread it out, are we going to diversify it further, we review it every three months, or put somebody on watch. It's all part of the process and you watch it month by month and you see the process seems to flow very well and seems to smooth out. Bill said no doubt about it. He thinks every manager has periods of up and downs. We're looking at year-to-date reports and we look at that. We've seen that from Chase before, and then we look at the portfolio and call them in. So far, we don't have them on watch because we had more money in that account and it was very prudent on the committee's part to diversify. Two years ago, when growth was forecasted to outperform value, for five years prior, we were overweighed value which was good and we only had Chase. When Bob Doll came out and said, for the next five years, we think growth is going to outperform value, we said, we only have one growth manager. If growth is going to become the leader, we need to enhance your portfolio, and add another manager. We did a manager search and Aletheia was the winner of that search. That worked out because, as he just showed you, growth is clearly outperforming and when it was underperforming, we were okay with Chase, but now that growth is the leader, it was smart. Chase helps us very much in the down markets. That's why we're content to stay with that.

Priscilla said at the last meeting, we had a lot of discussion as there were a lot of minuses on the pages. We were very worried. She's pleased to see there are not as many minuses. You had said there would be a nervous level, and we don't meet again until September, so what is your plan A, and she knows you can't predict. Bill said our job is to help predict, to some extent. To the extent of what you all need to know, all of you should sleep at night and not worry because you have your money in a situation where others are taking a look at this constantly. Your only worry is that you hope the people who are looking at it are doing a good job. PSAB's trustees, and particularly the investment committee takes this so diligently that what are we doing in the event things go wrong, and his answer is going to be the exact same as what they did when things did go wrong. That is, keep in touch, make good decisions, terminate managers who are grossly underperforming, and also look to add managers who will bring back. The second thing we do, and Linda hit on the key is we have an investment policy. It has minimums, targets and maximums. Our job is to totally stay in line with the investment policy meaning we aren't going to panic and get out and go all cash. That's what individuals do. This is a pension and it's long term. So many of the people got out of the market and then when it went up 30, they said they are missing it and then they got back in. You can't time the market. The reasons for outperformance over the long term, which we've done, is consistency in the process. The worries of what are you going to do "if"? What we're going to do is communicate, evaluate, and take action. That's the answer. To tell you what we're going to do, he can't tell you until it happens. Right now, in the report of today, it does two things. It looks backwards and says "how did you do", "how are you doing"? The answer to those are "good" and "good". We're doing very well and much better. He went to a meeting with Chris Capp with the other Borough's and the actuary was there and he said he does this for 120 plans, and this is the best plan we have. That was last year when we were down 19%. He can't wait to see what he says this year when he finds out we're up over 6% in this continued difficult economy. The process is in place. What he'll tell you to answer your question is we're going to continue to do the process and that should allow all of you to stay focused on your other issues in your Township. Is this going to affect your MMO? He would say more than likely, yes. You have to deal with how much, do we have to do co-pays, and do we have to raise taxes? Your challenges are many. There was an article in last month's Forbes that talked about the public pension funds in America. This is a major problem. The questions you deal with in your own municipality, how do you look compared to the rest of the country? If New York looks to address its pension fund losses, Pennsylvania state pension, much worse than our Boroughs. We're

actually doing better than most. That doesn't mean it's good. Pensions across America have issues just like Social Security. Can't we afford, can't we keep them? What's government going to do later? We may end up freezing them, we may end up changing the way this looks over the next ten years. Right now, you have a fiduciary responsibility as does PSAB and we all are doing our job to manage this pension as best we can, and then we measure it and say how are we doing versus our objective. Of course, you can say how are we doing versus everyone else? In the period last year, we were in the top fifteen percentile of all plans that are in our universe, meaning that we did better than 85% of all plans. We measure ourselves against others. We measure ourselves against our policy. What we can't do is change the economics of our country. We try to deal with what we can, and let what's going to hit us, we'll deal with as best we can. This has been the worst since the Great Depression. He can give you statistics on comparisons. He can guarantee you it won't ever happen again. He has so many charts that show the next ten years should do better than the last ten years. The last ten years on the S&P have averaged a negative number. The ten years that follows historically averages much better, and should average 10% to 15% to come back to the average. He thinks there is more cash in America – close to \$7 trillion deposited in history. When cash is that high, the markets do very well. There are a lot of positives.

Priscilla said what she's trying to get at is fiduciary responsibilities. She's an elected official so her job is even greater than the people sitting around the table because she has to look at the taxpayers. The thing is we looked at minuses, and we don't meet for three months. Either this committee makes these decisions and presents it to Council or the professionals make these decisions and present it to the committee and it goes to Council. We have to trust that you are doing the right thing. We have no comparison levels. We can't hire two firms and say "okay, you both do the job and then we're going to compare it at the end". We have to trust that your instincts are on the money. In hindsight, you can go back and say this should have happened and this should have happened, maybe the end of the month at your meetings, you could have said "do you guys want us to do something different"? Are we bound to a quarterly report.? There's nothing from keeping this committee to meet in between quarters. She just feels that the employees are looking at us and saying this is our pension money and we want to make sure it's done right. Bill said your choice, as of today, is to go with the process that PSAB offers. That process does take that personal, "here's what we should do" in our Township. You do leave it to another Board of Trustees. Your job as fiduciary with the system you currently have in place would be to keep the PSAB on their toes, which is what we're doing today. Your role as fiduciary elected official is to raise an eyebrow and question us as to anything you see that you don't like. Can we take and micromanage Lower Saucon – no. We have a process that has 200+ plans like yours combined into one. We do it as one overall plan. If your fire and police want you to go to 30% equities, we cannot take that up to the big plan and do that. We offer two choices – a 100% bond and a balanced. The balanced has a policy and we manage it accordingly. We report to all 200 Boroughs on our performance and he has to admit we're doing quite well. We're not losing plans, we're gaining plans. Compared to you doing it yourself...Priscilla said she's not talking about doing it ourselves. Bill said that's the only way we can manage it specifically with what you want to go at a given time.

Linda said let her make an offer. She doesn't know if we're on the same brainwave, but you get this report monthly. Priscilla said the township does, but the committee doesn't. Linda said do you get the Merrill Lynch report monthly? Jack said he hasn't seen that. Bill said that doesn't go out to all plans. Linda said some of them do, so she wasn't sure if Lower Saucon got them. How about if we give you a monthly copy of this Merrill Lynch plan and you can see where the allocations are. You can look and if you have a question, and it's not time for a quarterly meeting, you say Chase is negative 1.96%, what's going on there. How are you going to explain that? You either pick up the phone and give us a call or send us an email. That way you not only have net assets, but you have the Merrill Lynch report and you can look at the rebalancing and look at everything we're doing and see if there are any changes from last month. Priscilla said she's not being critical, she's just looking backwards and saying how could we have improved this. Bill said you really couldn't because at this point, you are four million out of 120 million some funds. If you don't like the way they are invested, there's nothing they can do as the policy is policy. Priscilla said before the township had its own policy, we had more control. She's not trying to be critical; she's just trying to protect the employees. Linda said this will give you more information and this way you'll know

on a month-to-month basis what is happening. If anybody questions you, you can say, look they did rebalance. They went into large growth and it's doing good. They pulled out of something that wasn't doing well. This will give you more information.

Mary said she thinks Priscilla is saying she's not quite getting enough information. You don't know when it's time for you to ask the question, and if you get that, you could see the pluses and minuses. Linda said what you can do is compare - here's April and here's May. Priscilla said on the other hand, we're bound by the policy but we could make some noise to the board and say we're really unhappy or we're satisfied. Linda said ask the question as to what's bothering you. Is it Chase, and if it is Chase, what are we doing about Chase. As Bill said, we pull out the ten year, we look at the trend, and we say are they doing better or should they be put on watch. There's no harm in raising the question. Priscilla said she's going to ask Jack and Cathy to look at it as they are the ones distributing it and they should see if it raises your eyebrow too. We're volunteers and she might look at it immediately, but Cathy and Jack are here and should be looking at it when you they get it. Linda said we'll send you a hard copy so you can Xerox it and see what's red and what's green. Molly said she felt a little bit better as we can start tracking it and it will give us a little more insight on what is going on. Meeting on a quarterly basis is only four times a year. Twelve times would be a lot better. Linda said don't hesitate to ask questions either.

Jack said what are the alternative investments, a brief description? Bill said an alternative investment is anything that is not in stock or bonds. Typically, private equity, you hear of hedge fund - this is a fund of funds. There are 200 different alternative investment managers in one fund. They came in and spoke to us at our last meeting two months ago and gave a presentation to the Board of Trustees. They are beating their index as well since we hired them. Their job is to take approximately half the risk of the market and further diversify the portfolio so we have less risk in the portfolio; therefore, we've hired a plan that is really above and beyond. For example, the Matoff, you have none of that in this because of the due diligence. We looked at Matoff and don't want to hire them because of the things he did wrong. The alternative investment in this plan is very diversified and none of that type of thing some of the bigger plans get into. It actually adds value, lowers our risk and enhances our return without being directly correlated to the stocks. Linda said isn't the endowment fund, the one we're in, a more conservative alternative investment? Bill said exactly.

Chuck said what do your economic models tell you about when unemployment is going to start turning around? Bill said he thinks the 3rd and 4th quarter as we've already seen it plateau. Unemployment is a lagging indicator, not a leading indicator, so the economy will turn before we see the unemployment start to come down. Unemployment is important. We've already seen it plateau and we think on a monthly basis, the next thing we are going to see is a decrease in unemployment. It's already up over 9%, which is a high. We should see it decrease by now and the end of the year. You're going to be surprised as you see that number slowly come down. Chuck said unemployment is pretty well correlated with the tax revenue they are using on the plan. The more people that are working, the more tax they pay. Bill said unemployment doesn't spur growth, doesn't spur spending, and doesn't help anyone. Priscilla said we don't have an issue with unemployment in the township. Bill said it affects you in the country. It affects the market. Cathy said you can't tell how many residents have been laid off. Priscilla said she's talking about township employees. Cathy said Bill is talking about overall, more regional as it's the EIT we collect. Chuck said that's his concern. Cathy said regarding the budget, instead of projecting a one percent increase like we did last year, she might do the same or less of a percentage.

Bill said thank you and the best thing you can do if you have questions is to get a hold of Chris or Linda. If anyone ever has any questions, or need us to update you, we are very proud of what we do for all of you, and we work very hard. We want to keep your confidence and don't ever want you losing sleep and worrying. Information is what they can supply to help do that. Let him, Chris, Linda or Peter know, anytime you are having one of those uneasy times, and they'll be happy to communicate with all of you to try to make you understand a very complicated world. They will do their best.

Priscilla said just so the employee knows when you see that report, don't be shy if you have questions. She doesn't know if it'll do anything, but at least we're on record that we tried. Chuck said that's a lot more appropriate for you than for him. You can't watch the market every day. This is a forty, fifty, sixty year proposition. He doesn't care what the market does in 2009 or 2011, he cares what it does over the long range period. One of the things he was trying to get across when we were talking about the economic factors is that this increase in pension requirements, as the market drops, comes at the same time the income may be down because of lower tax revenues. Therefore, it's a long term process, but it's not inappropriate to try to push some of this forward to a day when you got more tax revenues. That's one of the reasons they use the actuarial method, they don't want to recognize the whole 2008 market drop and swallow it in one great gulp. We want to do this over a number of years. If you recall at the February meeting, the reason he wasn't there was because he didn't want to come in here without answers. The time is right now. What's happening to these plans is while the investments have had big losses, we've smoothed most of it off to future years, and second, we've had gains on the other side, specifically for the police plan. Vic Koszi and Chief Lesser were eligible for retirement two years ago. They didn't retire before 2009, so that's two year benefit payments for those plans that you didn't have to pay. Pays didn't increase as we expected. As a whole, actuaries like to be conservative. You'd rather have gains and losses, and obviously, the gains should balance the losses. One of the more conservative assumptions he's used is that people retire when they are eligible, but they don't and you get gains off of them. That's what offsets some of the gains. As with the non-uniform plan, we've had many people terminate employment. One was Martha Chase. They thought the plan would have to pay out more than it actually did. The reason was the estimate of lump sum was done seven years ago instead of updating it, they paid her the original amount. There are things that have gone the plans way. If you look at the first column, it's the actual 2009. We're looking at about \$162,000 for the police and \$95,000 for the non-union. The Township obligation is about \$35,000. He now has a new evaluation. Priscilla said Cathy's budget is now going to reflect the new evaluation. So it's going to reflect the 2009. Chuck said it can't. Priscilla said it will because you're not real. Chuck said you have a choice. Let's look at the results. He agrees with Priscilla. That's the most actuarial responsible. Priscilla said responsible, and that's what we're here to do. Chuck said if that number was \$500,000, and if we'd only have tax revenues to some extent and we wouldn't make any sense to do it over future years. Priscilla said what happens next year. We need to be realistic in the budget. In some respect, you can estimate, but we have real hard facts here and that's why we pay you to come up with the numbers. She will vote no to the budget unless we have those numbers in here, and she will say it publicly. Chuck said and that's the actuarial responsibility. Mary said the net township obligation for both of these funds will be paid out of the 2010? Chuck said we'll use these in normal cost percentage amortization and apply it to the new payroll. Cathy is going to estimate the payroll for 2009 and we apply that to the formula. The payroll for 2009 is about the same as it was for 2008. Because the non investment gains offset the losses, the numbers really aren't as bad as he thought they were going to be. The police number goes up by about \$26,000 for a total of about \$99,000. This went up because they added the services. The non-uniform is about the same as the gains upset the losses. We are looking at a township obligation, it's virtually identical to what it was based on the old numbers. That may change if your payroll changes. The police is up somewhat more, \$22,000, but when we add the service increment, we've also had the members contributing 1% of pay. There's a \$10,000 reduction there for that. The hit on the police is about \$26,000. The non uniform is about the same. Being that such an amount makes good sense to let's start funding that now. If that would have roped you into an increase of \$500,000, we'd have to rethink. The state is looking at things to try to ameliorate this burden like throwing out 2009 totally and using 2010. Other things they are thinking of doing is extending the amortization. (COULD NOT HEAR HIM THE NEXT 15 MINUTES OF THE TAPE).

Priscilla said the 1% that the police are paying, the \$26,000, is going to offset the township obligation? Cathy said 1% is the \$10,000 that they are contributing and we have to add another \$26,000 to what we have to pay in. Priscilla said in addition to the \$72,000? Cathy said right. This is where we are right now. If the police officers were not contributing 1%, it would be \$36,000 of contributions that would have to be paid in. Priscilla said didn't the law say the police couldn't contribute more than a certain amount, so this number could have been 5%. Chuck said the state aid this year is based on 2007. Assuming the pile of money is about the same, we should be about the same.

Priscilla said as liaison, she would strongly urge the committee, to use real numbers so that could be presented to the taxpayers. She is not insinuating that Chuck is using manufactured numbers. Cathy said the vast majority of municipalities are not using real numbers. Priscilla said maybe she's missing something. They are putting it off and she'd rather not put it off because we have fire people that need money from us. We might be paying for paid fire people. That's top priority in this township. She knows you won't be happy with her regarding the budget, as that's what she is going to be doing and what she is going to be saying, that's our top priority. Then we go down the line and we have to have real numbers. This is not going to be a good budget. Cathy said we might have to say this has to be cut or this has to be cut. Someone said "or raise taxes". Priscilla said this is not good to put it off a couple of years.

Priscilla said the taxpayers are still paying the greater majority in addition to all the other benefits they pay for everything else. Chuck said yes, the township and the state are still paying the vast majority.

Chuck said he will go back to his office and finalize these reports and send them out to you. Cathy said she emailed financial reports to everyone basically showing what the employer contributions are on the statements.

Cathy said no. 7, settlement notices, they received one. Any notice that comes in, she will put on the agenda. If someone files a cross action suit, all that documentation ends up going to the planning administrators and they end up tracking it. Most of these filings and lawsuits are from 2001.

A motion and a second was made for approval of the March 18, 2009 minutes. All in favor.

- 3. Set date for next meeting – Wednesday, September 9th at 11:00 AM**
- 4. Adjournment:** Meeting adjourned. The time was 11:45 AM.