

BOARD OF TRUSTEES
FOR THE
STATE RETIREMENT AND PENSION SYSTEM
OF MARYLAND

MINUTES OF MEETING

October 16, 2001

The Board of Trustees for the State Retirement and Pension System of Maryland met in the Boardroom of the SunTrust Building, 120 East Baltimore Street, Baltimore, Maryland, at 9:30 a.m. There were present Richard N. Dixon, Chairman, Dr. Nancy Grasmick (arrived at 9:33 a.m., departed at 11:55 a.m.), Arthur N. Caple, Jr., George R. Tydings (via teleconference), Debra B. Humphries (departed at 12:35 p.m.), William D. Brown, Carl D. Lancaster, Morris L. Krome, G. Bruce Harrison, Ali A. Alemi, Trustees, and Peter Vaughn, Secretary. Agency staff members also attending were Deborah Bacharach, Robert Feinstein, Assistant Attorneys General, Carol Boykin, Chief Investment Officer, Tracey Ray, Deputy Chief Investment Officer, J. Howard Pleines, Director of Legislation, Rick Harrison, Chief Financial Officer, Thomas Gighotti, Chief Internal Auditor, Gwen Mulkey, Executive Associate, and Gary Scribner, Chief Information Officer.

Francis Demuro, Attorney for Ms. Doris Gill, Paul Schlitz, Attorney for Mr. Ibomero Sharafeldin, and Robert Walters, were also present.

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| Minutes | 1 | On motion made by Dr. Alemi and seconded by Mr. Caple, the Minutes of the regular meeting of the Board of Trustees for the State Retirement and Pension System of Maryland, held on August 21, 2001, were approved. |
| Minutes | 2 | On motion made by Dr. Alemi and seconded by Mr. Brown, the Minutes of the regular meeting of the Board of Trustees for the State Retirement and Pension System of Maryland, held on September 20, 2001 were approved. |
| Investment
Committee Report | 3 | Mr. Arthur Caple, Jr., Chairman of the Investment Committee, reported on the meeting held October 12, 2001. Attachment A

Mr. Caple stated that the Committee recommended the Board approve the amended Real Estate Registry. On Motion made by Mr. Lancaster and Seconded by Mr. Caple the Real estate Registry was unanimously approved. |

Mr Caple also informed the Board that the Committee will study the process of approving the properties and will report back to the Board

Mr Lancaster delivered a summary of recent activities of the Real Estate Sub-Committee. He reviewed activities related to the upcoming purchase and sale of several properties, and he identified the properties that the sub-committee toured over the past few months

Mr Caple stated that a presentation was made to the Committee by Legg Mason Real Estate Capital, Inc. The proposed product is structured as a private REIT, and its emphasis is on mezzanine debt. The Investment Committee sent this proposal back to the Real Estate Sub-Committee and the Investment Operations Manual Sub-Committee for further review

Ms Humphries delivered a summary of recent activities of the Minority Sub-Committee. The focus of recent sub-committee discussions has been on the System's use of Maryland and minority managers and the degree to which we might consider giving preference to these two categories of managers. The sub-committee did not recommend any changes to the Investment Committee. As of the end of fiscal 2001, the system had 5.3% of its assets with Maryland managers and 2.9% with minority managers, bringing the total to 8.2% of its assets under management. Since that time, this trend has continued with the hiring of Ariel, a minority controlled investment management firm, to manage approximately \$200 million of the System's assets. With regard to the brokerage policy, we continue to see progress with our managers. The two areas, which appear to be more challenging, are OTC and international brokerage, because there are fewer Maryland and minority brokerage firms with these capabilities. Overall, we have more work ahead of ourselves, but we are pleased with the progress that has been made so far. We will also continue the practice of sending quarterly letters to the managers, reminding them of the brokerage policy and their status in complying with it.

Manager meeting report - Mr Caple noted that this segment of the Agenda included an update on Chapman's response to the Alan Bond situation. She also noted the pending purchase of Zurich Scudder by Deutsche Bank. Progress Investment Management Group also announced their new Chief Investment Officer.

Mr Caple informed the Board that the Committee discussed the possibility of replacing Bob Patzwall with Larry Bach for the Maryland Venture Capital Trust ("MVCT") Board. Mr Patzwall does not wish to serve another term. The Committee decided to identify a public member of the Committee who would be willing to serve. If that fails, Mr Caple recommended asking a member of the Investment Committee to serve. Mr Caple stressed that he appreciated Mr Bach's

2

offer to serve, but the Committee preferred to have an Investment Committee member serve to insure balanced independent input from all of the System's MVCT Board members

Mr Caple noted the promotion of Art Lynch to the position of Deputy Chief Investment Officer of Equities, and the addition of Bob Burd to the investment staff

Mr Caple made a motion, seconded by Mr Dixon to use approximately \$8 million in the equity cash account to fund the two new value managers (TCW and Ariel) to \$200 million each. The Motion passed unanimously

Mr Caple stated that Ms Boykin provided the Committee with responses to several questions, which were raised by the Board at its September meeting, as a result the terrorist attacks on America

Mr Caple stated that Mr Lancaster asked for an earlier mailing date for the Investment Committee Agenda and that Staff would do their best to mail them 10 days in advance instead of one week in advance

Martha Hershberger 4

The Board considered the report of Susan Officer sitting as Administrative Law Judge for the Office of Administrative Hearings, in connection with the appeal of Martha Hershberger. Ms Hershberger appealed the Medical Board's denial of accidental disability benefits. The Medical Board reasoned that they did not believe that her disability was the natural and proximate result of an accident that occurred in the performance of duty.

The Administrative Law Judge, upon consideration of the record, and following a hearing, affirmed the Agency's decision and concluded that Ms Hershberger's disability was not the "natural and proximate result" of a work-related accidents that allegedly occurred on August 29, 1996 and April 9, 1991. Therefore, her application for accidental disability benefits should be denied.

The case of Ms Hershberger was considered on the record at the member's request. Ms Jill Leiner, attorney for the Agency, addressed the Board and argued that the Board should adopt the Administrative Law Judge's recommendations. The Board deferred further consideration to executive session.

Ibnomer Sharafeldin 5

The Board considered the report of Kenneth Watson sitting as Administrative Law Judge for the Office of Administrative Hearings, in connection with the appeal of Ibnomer Sharafeldin. Mr Sharafeldin appealed the Medical Board's denial of accidental disability benefits. The Medical Board reasoned that they did not believe that his disability was the natural and proximate result of an accident that occurred in the performance of duty.

The Administrative Law Judge, upon consideration of the record, and following a hearing, affirmed the Agency's decision and concluded that Mr Sharafeldin's disability was not the "natural and proximate result" of work-related accidents that allegedly occurred on October 24, 1995, July 16, 1996. Therefore, his application for accidental disability benefits should be denied.

Mr Paul Schlitz, attorney for Mr Sharafeldin, presented his arguments opposing the Agency's position and the Administrative Law Judge's recommendations. Ms Jill Leiner, attorney for the Agency, addressed the Board and argued that the Board should adopt the Administrative Law Judge's recommendations. The Board deferred further consideration to executive session.

Doris Gill

6

The Board considered the report of AJ Novotny, Jr sitting as Administrative Law Judge for the Office of Administrative Hearings, in connection with the appeal of Doris Gill. Ms Gill appealed the Medical Board's denial of accidental disability benefits. The Medical Board reasoned that they did not believe that her disability was the natural and proximate result of an accident that occurred in the performance of duty.

The Administrative Law Judge, upon consideration of the record, and following a hearing, affirmed the Agency's decision and concluded that Ms Gill's disability was not the "natural and proximate result" of a work-related accident that allegedly occurred on June 9, 1995. Therefore, her application for accidental disability benefits should be denied.

Mr Francis Demuro, attorney for Ms Gill, presented his arguments opposing the Agency's position and the Administrative Law Judge's recommendations. Ms Carla Katzenberg, attorney for the Agency, addressed the Board and argued that the Board should adopt the Administrative Law Judge's recommendations. The Board deferred further consideration to executive session.

Robert Walters

7

The Board considered the report of Donna M D'Alessio sitting as Administrative Law Judge for the Office of Administrative Hearings, in connection with the appeal of Robert Walters. Mr Walters appealed the Medical Board's denial of accidental disability benefits. The Medical Board reasoned that they did not believe that his disability was the natural and proximate result of an accident that occurred in the performance of duty.

The Administrative Law Judge, upon consideration of the record, and following a hearing, affirmed the Agency's decision and concluded that Mr Walter's disability was not the "natural and proximate result" of a work-related accident that allegedly occurred on August 1 1994. Therefore, his application for accidental disability benefits should be denied.

Mr Walters presented his arguments opposing the Agency's position and the Administrative Law Judge's recommendations. Ms Carla Katzenberg, attorney for the Agency, addressed the Board and argued that the Board should adopt the Administrative Law Judge's recommendations. The Board deferred further consideration to executive session.

On motion made by Dr Alemi and seconded by Dr Grasmick, the Board unanimously voted to meet in Executive Session to consider the appeals of Martha Hershberger, Ibnoher Sharafeldin, Doris Gill, and Robert Walters. State Government Article Section 10-503(a)(1)(iii) authorizes the Board to meet in closed session to exercise a quasi-judicial function.

EXECUTIVE SESSION

The Board met in Executive Session at 11:30 a.m. in the SunTrust Building to consider the appeals of Martha Hershberger, Ibnoher Sharafeldin, Doris Gill, and Robert Walters. All of the persons present at the beginning of the meeting were present in Executive Session except the following: Francis Demuro, Attorney for Ms Doris Gill, Paul Schlitz, Attorney for Mr Ibnoher Sharafeldin, and Robert Walters. The Board adjourned its Executive Session at 11:45 a.m. and returned to regular session to complete the agenda.

- Martha Hershberger The Board considered the record of Martha Hershberger. Following a discussion, on motion made by Debra Humphries and seconded by Dr Alemi, the Board voted unanimously to adopt the Administrative Law Judge's Proposed Findings of Fact and Conclusions of Law and denied Ms Hershberger's request for accidental disability retirement benefits.
- Ibnoher Sharafeldin The Board considered the record of Ibnoher Sharafeldin. Following a discussion, on motion made by Mr William Brown and seconded by Ms Debra Humphries, the Board adopted the Administrative Law Judge's Proposed Findings of Fact and Conclusions of Law and denied Mr Sharafeldin's request for accidental disability retirement benefits, with the vote of 9 to 1. Chairman Dixon, Dr Grasmick, Major Krome, Ms Humphries, Messrs Caple, Tydings, Brown, Lancaster, and Harrison registered yea votes. Dr Alemi registered a nay vote.
- Doris Gill The Board considered the record of Doris Gill. Following a discussion, on motion made by Mr William Brown and seconded by Dr Nancy Grasmick, the Board rejected the Administrative Law Judge's Proposed Findings of Fact and Conclusions of Law and granted Ms Gill's request for accidental disability retirement benefits, with the vote of 9 affirmative votes and 1 abstention. Chairman Dixon, Dr Grasmick, Major Krome, Ms Humphries, Messrs Caple, Tydings, Brown, Lancaster, and Harrison registered yea votes. Dr Alemi abstained.
- Robert Walters The Board considered the record of Robert Walters. Following a discussion, on motion made by Mr William Brown and seconded by Ms Debra Humphries, the Board voted unanimously to adopt the Administrative Law Judge's Proposed Findings of Fact and Conclusions of Law and denied Mr Walters's request for accidental disability retirement benefits.

Actuarial
Valuation Results

8 Mr Eugene M Kalwarski of Milliman and Robertson, Inc reviewed the principal results of the June 30, 2001 actuarial valuation of the State Retirement and Pension System of Maryland Attachment B

Mr Harrison expressed his concern over the proposed State Police Plans Contribution rate being lower next year despite the large investment losses the System had during the year

Mr Caple expressed his concerns over the adequacy of benefits available to members of the Pension Systems

Mr Lancaster expressed his desire to have a mechanism in place to provide gain-sharing and to accumulate a reserve to help fund future benefits After further discussion, and lack of concensus the item was deferred to a future Board meeting

Executive Directors
Report

9 Mr Vaughn reported the sale of 2115 Jefferson street On 10/24/01 he will go to the Board of Public Works meeting to request approve for the sale The Agency has received an offer of \$21.5 million dollars which represents a 20% return on the asset

Mr Vaughn informed the Board that Legislative Auditors have concluded their audit for Fiscal year 2001 On October 5, 2001 they departed and gave no indication that any adjustments will have to be made to the financial statements

Mr Vaughn stated that the Maryland Charity Campaign mailing to retirees is finished All literature was sent to retirees by October 9, 2001 Maryland Charity agreed to pay the additional costs of \$7,500.00 incurred by our vendor to process the mailing

Mr Vaughn then informed the Board that Senior Officers of the Agency would attend the Joint Committee on Pensions where the following issues would be addressed

- 1 Investment review for the year
- 2 Board sponsored legislation
- 3 Benefits for Probation and Parole officers
- 4 Benefits for Clerks of the Court and Register of wills

Mr Vaughn announced that one of our Board members, Mr William Brown was recently elected to the Executive Committee of the National Council on Teachers Retirement Mr Vaughn asked the Board to join him in congratulating Mr Brown

Mr Vaughn finally informed the Board that Chairman Dixon has requested feedback regarding the location of the 2002 Planning Conference The Chairman wanted to know if a Baltimore or a Cambridge location would be

(6)

better Mr Brown requested a change in the date of the conference because it always conflicts for him with the beginning of the school year Treasurer Dixon said that the Conference date could also be changed

The Board accepted Mr Vaughn's report

Executive
Committee Report

10 Major Krome, Vice-Chairman of the Executive Committee, reported on the regular meeting held October 2, 2001 Attachment C

Major Krome informed the Board that Mr Ricky Harrison reported that there were several projected overruns in the area of ADC, contractual services and garage rent (based on additional contracted space on the 12 floor of the building) Mr Harrison also reported a projected cost saving based on renewal of certain contracts He also reported that the year to date estimated manager fees (both non-real estate and real estate) are running under the cap

Major Krome reported that two technical errors were discovered in a review of the proposed FY2003 budget submission Adjustments were made and monies reallocated so that the total target budget remains the same as approved by the Board of Trustees

Legislative Proposals

Tax Related Issues.

Major Krome noted that this legislative proposal related to several technical revisions needed because of changes to regulations made by the Federal Government that impact public retirement systems The first issue is related to increases to the compensation limits for certain members hired after July 1, 1996

Major Krome reported the second issue related to an expanded definition of eligible rollover distributions to include certain 457 plans and 403 (B) plans Additionally, eligible rollover distributions now include post tax monies Mr Vaughn noted that amending Maryland law would be a positive benefit as well as an enhancement to portability for all our members

Major Krome then reported the third tax issue relates to the purchase of service credits Current law permits members to purchase up to 10 years of certain types of service credits at full cost (employee and employer costs) Federal law, however, may limit the purchase of service for members hired after July 1, 1999 and for Plan amendments made after August 5, 1997 In certain instances, the purchase of service may be limited to 5 years for post seconding teaching and not more than 5 years of service for which an individual is receiving a retirement benefit from another plan During previous discussion on this matter, Mr Lancaster indicated that it seemed inappropriate to reduce the current rights of a member Both Mr Vaughn and Mr Feinstein explained that outside tax counsel advised that the Board cannot ignore federal law Major Krome stated that since there is some confusion the Committee recommends not including the 5 year limits until further research is complete Finally, federal law now permits members to purchase service with additional sources of funds (457 and 403(B) plans)

On motion made and duly seconded the board voted unanimously to adopt the proposals for consideration by the Joint Committee on pensions

Suspension of Disability Retirement Allowances under 29-115

The legislative proposal attempts to revise the section of the current law related to the permanent suspension of a disability retirement allowance for those disability retirees who return to employment with a participating employer. The Executive Committee directed staff to revise the current law because they believed the current provisions are onerous to disability retirees.

The proposal makes several revisions to current law. (1) This section only applies to a disability retiree is under normal retirement eligibility who is employed by a participating employer at an annual compensation that is at least equal to the retiree's average final compensation at retirement (Current law also applied to retirees who returned to a participating employer at an annual compensation less than the retiree's average final compensation in a similar position held at retirement). (2) The section now provides for the temporary suspension (not permanent) and reinstatement of the disability benefit (with cost of living adjustments) after the disability retiree is no longer working for a participating employer. Finally, the proposal would make the temporary suspension mandatory rather than a decision of the Board of Trustees.

(3) That Section 29-115 to be amended to exempt accidental and special disability retirees from its provisions.

The Executive Committee recommends to the Board of Trustees that the Board approve the legislative proposal for §29-115 amendments.

On motion made and duly seconded the Board voted unanimously to approve the proposal for §29-115.

Optional forms of Retirement Allowance

The Board had previously requested changes to the re-calculations of Options 2 & 3 when the original beneficiary pre-deceases the retiree that would be cost neutral and still enhance the options available to both active and retired members.

The Committee reviewed a two-part proposal. The first part included changing the Option 5 and Option 6 language to allow a retiree whose spouse predeceased him and his allowance pop-up to a maximum allowance to elect a second beneficiary. This would apply to both current and future retirees who elect option 5 or 6. The Actuary has stated that this part of the proposal was cost neutral.

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The second part of the proposal was to allow current retirees who elected options 2 or 3 to elect to change to option 5 or 6. The retiree would be given one year to make this election. Based upon the number of retirees (20,000) who had elected option 2 or 3, the committee believed that it was not viable to request this proposal. Therefore, the Committee recommended that the Board approve the legislative proposal to only change the definition of Options 5 and 6 to permit a retiree whose benefit pop-up to maximum allowance to re-designate a second beneficiary of the spouse pre-deceased the retiree.

Mr. Lancaster believed that the proposal should include the option 2 and 3 language and requested that the Board include the provision in its proposal, amended to permit the retirees who had selected option 2 and 3 a one year election period to switch to option 5 or 6. This election period would commence with the date they requested an estimate. After discussion, on motion made and duly seconded, the Board approved requesting the General assembly approve changes to both option 5 and 6 language and option 2 and 3 language.

Major Krome reported that the Committee received requests from a member of the State Police Retirement System (SPRS) and the Law Enforcement Officers Pension System (LEOPS) to appeal the denial of their request to lengthen of participation in the Deferred Retirement Option Program (DROP). Those members are William W. Cihlar, (LEOPS) and James E. McKinley, (SPRS).

The first case involved Lt. Cihlar, a member of LEOPS who enrolled in the LEOPS DROP effective January 2001. As of January 1, 2001 Lt. Cihlar's maximum allowable participation period under State law was 24 months. On September 5, 2001, Lt. Cihlar requested to participate in the DROP for 5 years and also the right to be able to return to employment with the State of Maryland.

The second request was received from Sgt. McKinley, a member of the State Police Retirement System who applied for enrollment in the SPRS DROP effective September 1, 2001. As of September 12, 2001, Sgt. McKinley had 32 and ½ years of service in the SPRS. Under State law, members may participate in the SPRS DROP only if they have less than 28 years of service.

Major Krome stated that the Retirement Agency was following the law that establishes specific requirements for participation in DROP. He noted that agreeing to these requests would clearly violate the law.

The Executive Committee recommends to the Board of Trustees that the Board approve Mr. Vaughn's denial of a hearing for William W. Cihlar and James E. McKinley.

On motion made and duly seconded the Board voted unanimously to approve Mr. Vaughn's decision to deny a hearing for William W. Cihlar and James E. McKinley.

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Mr Gary Scribner presented the monthly Strategic System update. He informed the Committee that he addressed the Joint Committee on Pensions regarding the problems with the implementation of the Strategic System. Mr Vaughn noted that several legislators commented that there have been similar problems with IT projects in many other State agencies. While some problems exist, Mr Scribner believes that there is still a reasonable chance that the project could succeed. Colonel Mitchell noted that any future RFP should be drafted to include security provisions to protect the system from hackers. Mr Scribner and Mr Feinstein noted that our RFP for the Strategic System included those security provisions.

Mr Scribner informed the Committee that data backups from the Annapolis Data Center (ADC) are transported to the Agency and the Agency subsequently has the media transported to the offsite secure facility.

The Board accepted Mr Krome's report.

Audit Committee
Report

- 11 Mr William D Brown, Chairman of the Audit Committee, reported on the regular meeting held on September 20, 2001 Attachment D

Mr Brown stated that after completing the recruiting process for the Audit Supervisor position, the Internal Audit Division selected their Lead Auditor for the Position. After completing a search within the Agency to fill the Lead Auditor position, the IAD named the Auditor for the position. Recruiting will now begin to fill the Auditor II position.

Mr Brown informed the Board that Borwn & Company had not yet obtained a performance bond after their surety, Amwest Surety Insurance Company went bankrupt but is still working on a replacement bond.

Mr Brown noted that Universal had conditionally approved Brown & Company's bond request, pending certification by the Agency that all of the work done to date was completed satisfactorily and was on schedule. Since the primary results of Brown & Company's work will not be received until the end of the project, the Agency cannot make such an assertion.

Mr Brown stated that in the interest of time, he would request that the Board read the remainder to the Audit Committee report at their leisure.

Earnings
Limitation
Recovery

- 12 The report of the Agency for offsets of certain retirees was accepted by the Board. The Board, on motion made by Colonel Mitchell and seconded by Ms Humphries, authorized the reduction of the pensions of affected retirees as provided for under the current law [State Personnel and Pensions Article Sections 22-406 (b)(2) and 23-407 (b)(2)]. The pensions offset are based on calendar 2000 earnings that will be offset from pension benefits paid in fiscal year 2002. Attachment E

Medical Board
Reports

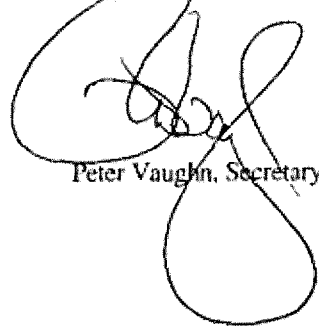
- 13 The Board, on motion by Mr Harrison and duly seconded, unanimously approved the reports of the Medical Board in connection with applications of members for ordinary, accidental and special retirement allowances. The Medical Board's conclusions were reached after its review of the evidence provided by the claimants. Attachment F

10

- Supplemental Board Reports 14 The Board, on motion by Harrison and duly seconded, unanimously accepted and approved the supplemental reports of the Medical Board in connection with applications of members for ordinary, accidental and special retirement allowances. The Medical Boards conclusions were reached after its review of the evidence provided by the claimants. The Supplemental Report of the Medical Board is shown as Attachment G
- Other Business 15

There being no further business, on motion made and duly seconded, the Board adjourned at 1:35 p m

Respectfully submitted,



Peter Vaughn, Secretary

11