

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

REVISED - MINUTES OF MEETING

August 21, 2007

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, beginning at 9:07 a.m. There were present: Nancy K. Kopp, Chairman; Peter Franchot, Vice-Chairman; William D. Brown; John W. Douglass; T. Eloise Foster; James M. Harkins; Sheila Hill; F. Patrick Hughes (by telephone); Morris L. Krome; Theresa Lochte; Patrick O'Shea; and, Robert W. Schaefer, Trustees; and R. Dean Kenderdine, Secretary.

Agency Staff members attending were: Deborah Bacharach; Anne Budowski; Margaret Bury; Melody Countess; Brian Feilinger; Robert Feinstein; Charles Geis; John Greenberg; Ira Greenstein; Carla Katzenberg; Dennis Krysiak; Vincent Marsiglia; Larry Martin; Sherlynn Matesky; Howard Pleines; Harvey Raitzyk; Kenneth Reott; Janet Sirkis; Barbara Swain; and, Patricia Wild.

Also attending were Dylan Baker; Lisa Campbell; Anne Gawthrop; Leon "Rocky" Joyner; John Kenney; Melissa Moye; and, Michael Rubenstein.

Present only during the appeal case portion of the agenda were Gloria Bauman; and Frank E. Troska and Michael E. Davey, Esquire.

Minutes 1. On motion made by Mr. Brown, and seconded by Mr. Hughes, the Board approved the Minutes of the July 17, 2007 regular meeting.

Investment 2. Mr. Robert Schaefer, Chairman of the Investment Committee, reported
Committee on the meeting held on August 10, 2007.

Mr. Schaefer reported that the Committee unanimously approved the July 13, 2007 open meeting minutes as submitted.

Mr. Schaefer indicated that the Investment Division has hired three new employees: Ms. Faina Kashtelyan, Senior Quantitative Analyst; Melissa Lee and Michael Ruetz, Senior Investment Analysts. He also noted that Shinelle Davis has been promoted to an Assistant Director position, focusing on cash management, corporate governance, and proxy related issues.

Mr. Schaefer stated he has appointed a working group to study Investment Committee operations and to develop methods that would promote more efficient and effective operations between the Committee and the Board. Messrs. Bill Brown, Pat Hughes, Dean Kenderdine, John Kenney, Wayne Shaner, Ms. Sheila Hill and Dr. Melissa Moye are members of this working group.

Mr. Schaefer noted that the Committee heard finalist presentations for the Core Plus Fixed Income Manager Search from Aberdeen Asset Management Inc., Principal Global Investors and Pyramis Global Advisors.

Mr. Schaefer stated that Mr. Greenberg presented the second quarter TUCS results, indicating that the System was in the 75th percentile for the most recent quarter, 76th percentile for six months ending June 30, 2007 and in the 53rd percentile for twelve months ending June 30, 2007. The System's one year return of 17.64% was only 5 basis points below the 17.69% median notwithstanding the fact that, compared to its peers participating in TUCS, the System has a significant overweight in fixed income.

Mr. Schaefer noted that the Committee received an updated version of the Investment Policy Manual that will be presented for adoption at a future Investment Committee meeting.

Mr. Schaefer stated that in response to a request from the Committee at the April 2007 meeting, staff provided a summary of final terms and conditions for the System's investment in the new fund begun by Relational Investors LLC.

At Mr. Schaefer's request, Mr. Kenderdine informed the Committee of AIG-VALIC's request to extend their contract with the System for an additional six months to afford them the opportunity to go before the General Assembly and request a change in the law to decouple the Supplemental Retirement Accounts Program from the Optional Retirement Plan. Mr. Kenderdine also reported that the University of Maryland System expressed their desire that the Board decline to extend AIG-VALIC's ORP contract. With respect to such a legislative change, they are opposed because it would place the University's Board of Regents in the position to act as a fiduciary, requiring the Regent's hiring of their own consultants, and other responsibilities.

On motion made by Mr. Schaefer and seconded by Major Krome, the Board declined to extend AIG-VALIC's ORP contract.

Mr. Schaefer noted that the Save Darfur Act of 2007 authorizes the Board of Trustees, in the exercise of its fiduciary duties, to decide whether to divest its investments in any company doing business in Sudan. In accordance with this Act, staff presented a divest/hold analysis of Schlumberger Ltd., an oil field service company that is currently operating in Sudan.

Mr. Schaefer stated that the Investment Committee voted to defer divestment citing: (1) the Sudan Divestment Task Force's recent decision to move Schlumberger from the "Highest Offender" category to an "Ongoing Engagement" category, due in part to the company's efforts to address the consequences of its operations in Sudan; (2) the

company's argument that it is a beneficial influence in Sudan in several respects and believes that its way of conducting business benefits the people of Sudan; (3) the company has been providing humanitarian assistance in the form of science education work in Sudan, both at the secondary school and university level; (4) the company has recently begun a 12-month series of projects in a displaced persons camp where Southern Sudanese and a small number of Darfurians are living temporarily, with a focus on education, health and water supply; and, (5) if Schlumberger, an industry leader, leaves the country, the void may be filled by competitors who are not as inclined to address and mitigate the consequences of their operations in Sudan.

After the Committee's motion to defer divestment from Schlumberger for 90 days was presented, on motion made by Treasurer Kopp, and duly seconded, the Board of Trustees amended the motion to provide for a deferral of up to 90 days. On motion made by Mr. Schaefer, and seconded by Mr. Hughes, the Board approved the amended Investment Committee's motion to defer for up to 90 days the consideration of staff's recommendation relating to divestment of the System's assets from Schlumberger Ltd. Comptroller Franchot is recorded as opposing the motion.

Administrative
Committee

3. Major Morris Krome, Vice-Chairman of the Administrative Committee, reported on the meeting held on August 7, 2007.

Major Krome noted that the Department of Budget and Management set the FY2009 budget target for the Retirement Agency at \$23,283,000, which is 3.9% greater than the FY2008 appropriation. However, the Agency must absorb all salary increases so the actual increase is 3%.

Major Krome stated that Mr. Tom Iannucci from Cortex presented his review of the Board's compliance with its charters and policies. He found a high level of compliance. Staff will review the recommended changes and come back in September with final recommendations for the Administrative Committee to review and recommend to the Board.

Major Krome stated that Wicomico County Board of Education again requested that the salary increase offered under the County's Early Notification Program (ENP) be included in the definition of "earnable compensation". He indicated that the Committee, with additional input from legal counsel and the actuary, concluded that the ENP salary is not part of "normal salary" and should not be included. The Administrative Committee advised Mr. Kenderdine to notify Wicomico County of that decision and the County's right to appeal.

On motion made by Major Krome, and seconded by Mr. Harkins, the Board of Trustees expanded the suspension of benefits rule for retirees who return to employment with the same employer to include Cabinet Secretaries, Heads of Independent Agencies, Deputy Secretaries and

Assistant Secretaries. All other retirees remain subject to the current pension recovery policy.

On motion made by Major Krome, and seconded by Mr. Harkins, the Board of Trustees assigned PINs 061657 and 077692 (Internal Auditor II, Grade 16) as Special Appointments.

On motion made by Major Krome, and seconded by Mr. Harkins, the Board of Trustees assigned Special Appointment status to PIN 083718 (Administrator II, Grade 17), which is to function as a Special Assistant to the Executive Director.

On motion made by Major Krome, and seconded by Mr. Schaefer, the Board approved the following legislative proposals for presentation to the Joint Committee on Pensions, noting Secretary's Foster's opposition to altering corridor funding at this time due to the current budget deficit.

Corridor Funding: Eliminate the corridor funding method currently applicable to the State portion of the Employees' Combined Systems and the Teachers' Combined Systems with a return to full actuarial funding as quickly as practical for those Systems.

Real Estate: Enable the fiduciaries of the Retirement System to consummate sales and purchases of real estate for the System's investment program without requiring Board of Public Works approval or Department of General Services review.

Fee Caps: Exempt the System's investment programs from its current fee caps that apply to (1) externally managed real estate and alternative investments; and, (2) the System's other externally managed assets.

Archaic Investment Language: Remove archaic language from pension law that states, "Not more than 25% of the assets that the Board of Trustees invests in common stocks may be invested in nondividend paying common stocks."

State Police Survivor Benefits: Increase the State Police survivor benefit for widows and widowers of retired State Police to 80% of the retirees' benefit, and eliminate the Special Supplemental Survivor Benefit.

Retire/Rehire Program: Require local school systems to pay any offset of pension benefits resulting from late reporting or non-reporting of retirees who were to participate in the so-called Retire/Rehire Program under Chapter 499 of the Acts of 2005 and Chapter 443 of the Acts of 2007.

Remove Reemployment Restrictions: Seek additional modifications to the reemployment restrictions within State pension law, including permitting State and participating municipal retirees receiving a full

service retirement (30 years) to return to work with the same employer without an earnings limitation.

Data Reporting: Require employers to pay a fee for failure to establish eligibility for membership in the Teachers' or Employees' Pension Systems by not filing or delaying the filing of enrollment documents.

Unused Sick Leave: Amend pension law to provide that unused sick leave reported to the Retirement Agency at time of a member's retirement is the days of sick leave not used during employment or paid for at time of retirement by the employer.

Limited Exemption from State Personnel Rules: Provide the Board of Trustees the authority to set the compensation for professional employees of the State Retirement Agency (includes investment, auditing and key administrative staff).

Teacher membership: Amend the definition of "Teacher" to focus on job duties related to classroom teaching and curriculum, rather than defining it on job titles; and amend pension law to place "teacher" members who are promoted or transferred into an ineligible position into the Employees' Pension System, Alternate Contributory Pension Selection.

Disability Benefits – DROP: Amend the State Police and Law Enforcement Officers' Deferred Retirement Option Programs to provide for special/accidental disability only if the disabling condition or accident occurs during participation in DROP.

Major Krome stated that Mr. Charles Geis, project manager for MPAS, indicated that he has made a personal assessment of the project and is pleased with both the performance and the progress made to date. While there has been some slippage in work completed, the contractor has submitted a revised work schedule that retains the current completion dates (go live July 2008) without additional costs at this time.

Executive
Director's Report

4. Mr. Dean Kenderdine introduced Mr. Ira Greenstein, the new Chief Information System Officer for the Agency and Mr. Dennis Krysiak, the Agency's Budget Director. Mr. Kenderdine also introduced Mr. Dylan Baker from the Department of Legislative Services who is the Agency's new budget analyst.

Mr. Kenderdine informed the Trustees that there are mailboxes for each of them outside his office for any mail received by the Agency for individual Trustees.

Mr. Kenderdine noted that due to security reasons, beginning September 4, Agency staff will be required to wear their State identification badges, with visitors obtaining passes at the desk in the

lobby. Also, the doors to the Agency will be closed after public meetings begin, but public access will be maintained by calling staff for entrance by the public to these meetings.

Mr. Kenderdine stated that three finalists have been interviewed to be the executive search firm hired to look for candidates to become the System's Chief Investment Officer. The selection should occur by the end of this week, with the goal to select a CIO by the end of this calendar year.

Presentation of
Experience Study
Findings

5. Mr. Rocky Joyner of Segal Inc. reviewed the changes to the actuarial assumptions that Segal was recommending as a result of the recent experience study. Those recommendations are as follows:

Inflation Rate – 3.50%.

Investment Rate of Return – 7.50%.

Payroll Growth – 3.50%. **Salary Scale** – continue the 10-year select and ultimate structure for salary increases; modify the rates for individual Systems to reflect observed experience as well as lowered expectations for future inflation.

Mortality Rates:

Post-Retirement Mortality – use RP-2000 Mortality Table as base; adjust table appropriately for actual experience of individual plans; reflect expectation of longer life spans.

Disabled Life Mortality - use RP-2000 Disabled Life Mortality Table as base; adjust table appropriately for actual experience of individual plans.

Pre-Retirement Mortality – use corresponding Post-Retirement Mortality Tables.

Disability Rates – adopt new rates based on recent plan experience; do not change Judges' rates and use LEOPS rates for Local Fire and Police System.

Withdrawal Rates – continue using select and ultimate rates for all Systems; modify rates to match observed plan experience.

Retirement Rates – modify all rates for all Systems to reflect the observed experience during the period.

Mr. Joyner also suggested the following changes:

Actuarial Smoothing Method – adjust method to smooth actual investment gains/losses over a 5 year period.

Actuarial Funding Method – change from "Aggregate Entry Age" to "Individual Entry Age".

Corridor Cost Method – modify corridor method to assure adequate plan funding.

Mr. Joyner also presented information on the impact of accepting all recommended changes with both 7.75% and 7.50% interest rate assumptions, and altering the amortization period from 25 to 30 years, while eliminating the corridor funding method.

On a motion made by Mr. Schaefer, and seconded by Ms. Hill, the Board accepted all of the actuary's suggested assumption and funding changes except the investment assumption rate, which is to remain at 7.75% at this time. The Board also voted to add to its legislative proposal to eliminate corridor funding, the adjustment of the amortization period from 25 to 30 years. Secretary Foster abstained from the vote. This motion was made and adopted with the explicit commitment to the elimination of the corridor methodology funding and the understanding that the investment assumption rate may be reviewed in the Spring of 2008.

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| Adoption of Post Retirement Health Benefits Trust Fund Agreement | 6. On a motion made by Ms. Hill, and seconded by Major Krome, the Board approved the Post Retirement Health Benefits Trust Agreement presented by counsel for the System. |
| Medical Board Reports | 7. On motion made by Ms. Hill, and seconded by Mr. O'Shea, the Board accepted the reports of the Medical Board in connection with applications of members for ordinary, accidental and special disability retirement allowances. The Medical Board's conclusions were reached after its review of the evidence provided by the claimants. |
| Supplemental Medical Board Reports | 8. On motion made by Ms. Hill, and seconded by Mr. Brown, the Board accepted the supplemental reports of the Medical Board in connection with applications of members for ordinary, accidental and special disability retirement allowances. The Medical Board's conclusions were reached after its review of the evidence provided by the claimants. |
| Toxie A. Banton | 9. The Board considered the recommendation of the Administrative Law Judge in connection with the claim of Ms. Toxie A. Banton for accidental disability benefits. The Administrative Law Judge's report, a report by the Medical Board, and all related documents submitted by the parties were presented.

Ms. Banton's case was heard on the record at her request. The Board deferred further consideration to Closed Session. |
| Frank. E. Troska | 10. The Board considered the recommendation of the Administrative Law Judge in connection with the claim of Mr. Frank E. Troska for special disability benefits. The Administrative Law Judge's report, a report by the Medical Board, and all related documents submitted by the parties were presented. |

Mr. Troska and his attorney, Mr. Michael Davey, appeared before the Board to ask that the Board adopt the Administrative Law Judge's recommendation to grant disability benefits. Ms. Carla Goldman Katzenberg, attorney for the Agency, addressed the Board and argued that the Board should reject the Administrative Law Judge's recommendations. Following discussion, the Board deferred further consideration to Closed Session.

- Gloria Bauman 11. The Board considered the recommendation of the Administrative Law Judge in connection with the claim of Ms. Gloria Bauman for accidental disability benefits. The Administrative Law Judge's report, a report by the Medical Board, and all related documents submitted by the parties were presented.

Ms. Bauman appeared before Board to oppose the Agency's position and the Administrative Law Judge's recommendation. Ms. Carla Goldman Katzenberg, attorney for the Agency, addressed the Board and argued that the Board should adopt the Administrative Law Judge's recommendations. Following discussion, the Board deferred further consideration to Closed Session.

CLOSED SESSION

The Board met in Closed Session at 12:52 p.m. in the Boardroom of the SunTrust Building at 120 East Baltimore Street to review the Watch List pursuant to State Government Article §503(a)(1)(i); to discuss the appeals of Toxie A. Banton, Frank E. Troska, and Gloria Bauman pursuant to State Government Article §503(a)(1)(iii); to consider a proposed real estate fund investment pursuant to State Government Article §508(a)(5); to discuss a contract claim and tenant-related litigation pursuant to State Government Article §508(a)(5) and (a)(8); and to select a Core Plus Manager pursuant to State Government Article §508(a)(5) and (a)(14).

There were present: Nancy K. Kopp, Chairman; Peter Franchot, Vice-Chairman; William D. Brown; John W. Douglass; T. Eloise Foster; James M. Harkins; Sheila Hill; Morris L. Krome; Theresa Lochte; and, Robert Schaefer, Trustees; and R. Dean Kenderdine, Secretary.

Agency staff attending were Deborah Bacharach; Margaret Bury; Robert Feinstein; John Kenney; Vincent Marsiglia; Howard Pleines; Janet Sirkis; and, Barbara Swain.

The Board ended its closed session at 1:20 p.m. and returned to regular session to complete the agenda.

REGULAR SESSION

During the closed session, the Board reviewed the Watch List; discussed funding for a commingled real estate limited partnership; discussed with legal counsel a contract claim and ongoing litigation; selected Core Plus managers; and decided on the following disability appeals.

Toxie A. Banton The Board voted to accept the Administrative Law Judge's Proposed Decision and deny Ms. Banton's request for accidental disability benefits.

Frank E. Troska The Board voted to accept the Administrative Law Judge's Proposed Decision and grant Mr. Troska's request for special disability benefits.

Gloria Bauman The Board voted to reject the Administrative Law Judge's Proposed Decision and grant Ms. Bauman's request for accidental disability benefits.

Adjournment There being no further business before the Board, the meeting adjourned at 1:22 p.m.

Respectfully submitted,



R. Dean Kenderdine
Secretary to the Board

RDK/js