

**MINUTES OF THE
TEXAS MUNICIPAL RETIREMENT SYSTEM
Regular Meeting of the Board of Trustees**

March 27, 2009

On March 27, 2009, the Board of Trustees of the Texas Municipal Retirement System (TMRS) convened for a regular meeting at 8:35 a.m. at TMRS Headquarters, located at 1200 North IH 35 in Austin, Texas, with the following members present:

Board of Trustees

Carolyn Linér, Chair
Ben Gorzell, Jr., Vice Chair
Pat Hernandez
April Nixon
Mr. Roel ("Roy") Rodriguez
H. Frank Simpson

Present also were:

Eric Henry, Executive Director and CIO
Ian Allan, Director of Internal Audit
Rhonda Covarrubias, Director of Finance
Eric Davis, Deputy Executive Director
Bernie Eldridge, Director of Human Resources
David Gavia, General Counsel
Nancy Goerdel, Director of Public Investments and Asset Allocation
Leslee Hardy, Staff Actuary
Holly Macki, Director of Fixed Income
Michelle Mellon-Werch, Associate General Counsel
Cindy Morse, Executive Assistant
Debbie Munoz, Director of Member Services
Eddie Solis, Director of Government Relations
Bill Wallace, Director of Communications
Scott Willrich, Director of Information Resources
Robert Klausner, Klausner & Kaufman
Russ Kuhns, R. V. Kuhns & Associates, Inc.
Ron Lewis, Ron Lewis & Associates
Pete Madsen, R. V. Kuhns & Associates, Inc.
Mark Randall, Gabriel, Roeder, Smith and Company
Gary Shilling, Shilling & Associates, Inc.
Nancy Williams, Ennis Knupp + Associates, Inc.

Guests:

David Crow, President, Arlington Professional Fire Fighters
Debbie Maynor, Texas Municipal Human Resources Association
Randle Meadows, City of Arlington Police Department

Jim Moore, Assistant Fire Chief, City of Mesquite
Bob Scott, Director of Finance, City of Carrollton
Angela Deats, Communications Analyst
Debbie Farahmandi, Investment Operations Specialist
Pete Krnavek, Manager, Information Systems
Maryann Malave-Jaini, TMRS Travel Team
Anthony Mills, Regional Manager – City Services
Lorraine Moreno, Regional Manager, City Services
Candace Nolte, Controller
Kate Reed, Investment Analyst
Kristin Qualls, Assistant Investment Officer
Sean Thompson, Membership Analyst

The meeting was called to order by Ms. Linér at 8:35 a.m., and Ms. Hernandez gave the invocation.

1. Consider and Act on Consent Agenda

Mr. Henry presented this item and asked the Board to adopt the Consent Agenda, including the Minutes from the February 20, 2009 Regular Meeting of the Board of Trustees. There was no discussion on this item. Mr. Rodriguez moved that the minutes be adopted as presented. Ms. Nixon seconded the motion, which passed unanimously.

2. Economic Advisor Presentation

Dr. Shilling began his presentation by stating that he would discuss what is going on in the markets now, as well as the longer term outlook. He said the country's current leveraged position was 30 years in the making and that we are now in the down phase of a super cycle. He indicated that the upside occurred in the 1980s and 1990s; the peak of the cycle was in 2000, but was hidden by the short revival. He said speculation has now shifted to investments like hedge funds, and also real estate, including owner-occupied homes. Housing prices have declined due in great part to excess inventory. He also mentioned that personal net worth has declined, which means most consumers can no longer tap into this asset in order to continue spending.

Dr. Shilling stated that he thinks we will see a shift in the 25-year decline in personal savings, to an increase in personal savings. He doesn't believe this to be a recession phenomenon, and said it is likely to continue for about 10 years. This has an effect on the overall economy. If savings increases by 1% a year, it will decrease Gross Domestic Product (GDP) growth by 1% a year. Mr. Shilling believes that a lot of the increased savings will be used to repay debt, including financing the federal debt – more coming from U.S. savers than from foreign countries. This is bad news for the foreign countries because they rely on U. S. consumer spending to purchase their exports. With the entrenchment of U. S. consumers, world exporters have seen dramatic declines. China, for example, is being affected by the drop in exports. Dr. Shilling emphasized that U. S. consumers are on a savings spree which will result in a dampening effect on growth.

Another issue that results in slow growth is the unwinding of the financial markets and the return to regular lending. Lending to small businesses will be tightened. This bank retrenchment leads to tighter lending markets and slower economic growth. In addition, lower commodities prices will have an impact on foreign government spending, as their economies are dependent upon commodities exports leading to slower growth. Dr. Shilling also mentioned that increased government regulation is impacting economic growth. Government involvement usually means increased inefficiency, and less risk-taking and innovation.

Dr. Shilling said that the final area that is going to slow growth is protectionism. He said that we saw financial protectionism in governments guaranteeing bank deposits and loans, and now we are starting to see it in goods and services, too. He indicated that when looking at slower economic growth, we are likely to see growth in the 2% range rather than 3.6% we have seen previously. He indicated that we will probably see less robust bull markets and more and deeper bear markets.

Dr. Shilling also mentioned that he believes we are moving toward deflation due to weak global demand, but strong supply. We have excess liquidity, but the money is not being lent. Dr. Shilling admitted that his view is in the minority.

With regarding to state and local level issues, he reported that unemployment rates are going up. Pension funding ratios have declined and are not likely to rise back to the levels they were at previously.

3. Executive Session

At 9:50 a.m., the Board entered into Executive Session, pursuant to Texas Government Code, §§551.071 and 551.074 to consult with Legal Counsel to receive legal advice, and to discuss personnel matters, including reviewing and considering the duties, performance and compensation of the Executive Director. No action was taken during the Executive Session and the meeting was opened to the public again at 12:33 p.m. All members of the Board who had been present when the Board went into Executive Session were again present.

When the public meeting resumed, Ms. Nixon moved that the salary of the Executive Director be increased by 7.5%. Ms. Hernandez seconded the motion, which passed unanimously.

4. Discuss Board of Trustee Self-Evaluation

Ms. Williams then led the Board through a trustee self-evaluation. Ms. Williams began her presentation by stating that self-evaluation is a best practice in Board governance. She indicated that she would start by asking the Board a series of questions about things that every Board needs to consider on an annual basis to ensure they are operating efficiently.

She asked if the Board feels they are doing a good job of new member orientation. Mr. Gorzell said yes, and remarked that having access to the investment consultant and actuary was beneficial. Ms. Williams asked if the Board feels they are getting the right education on the right topics. The Board answered in the affirmative. Mr. Rodriguez stated that staff makes educational opportunities known to the Board via the Board Portal and emails. Ms. Williams asked if the board meetings lead to open and effective communication. The Board stated yes,

that the long, one-day, more frequent meetings were working. Ms. Williams asked if there was enough time for discussion during the Board meetings. Mr. Gorzell recommended that the Board or staff recap the actions taken. Ms. Williams asked about adequacy of Board meeting minutes. Mr. Simpson requested that more emphasis be placed on Board discussions. Ms. Williams asked if materials are provided on a timely basis. The Board agreed that posting materials on the portal has helped. The Board also expressed approval of the current practice of discussing items at one meeting and acting on the item at the next meeting. Ms. Williams asked if they were getting adequate information and support for the budget. The Board answered affirmatively. Ms. Williams asked if there was a need to change the strategic plan. The Board replied that there is no need to change the strategic plan.

Ms. Williams stated that she had no more questions and commended the Board and staff on their current practices and stated that she had no recommendations at this time.

5. Education Session on Updated Service Credit Provisions and Issues

Due to time constraints, this agenda was postponed until the April 24, 2009 Board meeting.

6. Investment Report as of February 28, 2009

Mr. Henry presented this item and highlighted the year-to-date performance in the aggregate and for the two stock funds. It was pointed out that on an income basis, the fund is still yielding above 5%.

7. Discussion on Draft Proposals Concerning Asset Allocation

Mr. Simpson asked if R. V. Kuhns had any difference of opinion with Dr. Shilling's economic outlook. Mr. Kuhns stated that they believe in diversification, as well as alternative classes, for the right reasons. Diversification in non-correlated or less correlated classes, and striving for a realistic target makes sense.

Mr. Madsen began the discussion by stating that we need to know risk, return and correlation numbers in order to put into their optimizer to determine the proper allocation. So the information presented is based on long-term relationships, not economic forecasts. Their estimates tend to be conservative. Mr. Madsen moved to a discussion on the standard deviation of different asset classes. One standard deviation happens two-thirds of the time, which is a measure of risk. He then moved to a discussion of correlation. He showed on a historical basis, the correlation of certain asset classes for the past 30 years.

Mr. Madsen discussed an extensive efficient allocation exercise that R. V. Kuhns went through with TMRS staff. He discussed the different factors that went into the computer model, explaining that they built upon the current portfolio showing the impact on both risk and return of adding various asset classes. Mr. Madsen showed the impact of adding real estate, real return, absolute return (hedge fund of funds) and private equity.

Mr. Madsen then discussed the Monte Carlo simulation results over a 5-year and 10-year period. Mr. Gorzell asked Mr. Madsen to walk him through one standard deviation on the suggested portfolio. Mr. Gorzell asked what plan was in place to move into this allocation. R. V. Kuhns

answered that moving into an allocation would be done over time, by dollar cost averaging into different classes.

8. Discussion on Proposed Revisions to Investment Policy Concerning Asset Allocation

Ms. Goerdel introduced a draft version of the revised Investment Policy Statement for review and discussion. Because of extensive changes to the policy, a decision was made to completely rewrite the policy and not just amend the existing policy. She stated that the policy is designed to have broader issues in the body of the document, and more detailed asset class policies in the appendix. Ms. Goerdel said that the move to total return from income return makes the policy more complex by its nature resulting in many additional sections, including manager termination, manager retention, benchmarks and rebalancing.

Mr. Simpson asked for additional time to review before he feels comfortable asking questions about the document. The draft policy will continue to be reviewed in the April and June Board meetings.

9. Actuary Report to Include (a) Discussion of Preliminary Valuation Results; (b) Impact of Negative Investment Returns on Municipality Accumulation Fund (MAF) and Employer Contribution Rates Under Proposed Legislation; (c) Review of Actuarial Changes Adopted and Considered Since 12/31/06 Valuation; and (d) Discussion of Potential Actuarial Issues Looking Ahead

Mr. Randall began his presentation by stating that this presentation to the Board is a follow-up to the presentation made at the February meeting. With regard to preliminary valuation results, Mr. Randall stated that under the Projected Unit Credit (PUC) method, the normal cost from year to year stays fairly level due to turnover and other factors. He indicated that what he is seeing in this valuation is that turnover and retirements have slowed down which has the effect of increasing rates. Mr. Randall then briefly reviewed the "lag" that exists in the process, explaining that lag is the time between when the valuation is completed and when the rate is implemented. He showed an example of the impact of a "lag" on the rate for a sample city.

Mr. Randall also discussed the impact of the 5% interest credited to cities for 2008 versus the 7% actuarial interest credit assumption, and the impact of the three actuarial assumptions that were adopted at the December 2008 Board meeting. Mr. Randall discussed the six groupings of cities that GRS looks at when reviewing the system. He gave examples of the expected impact of all of these matters on city rates.

Mr. Randall then discussed the impact on rates of a negative return by the fund, and the effects of smoothing. Mr. Randall showed the impact of a -5% total return, the effect the leverage of the ESF and CSARF have due to their guaranteed returns (assuming legislation passes) and the final impact on the MAF. Mr. Randall gave examples of a -5% return, without actuarial smoothing, for cities with no phase-in rate and with a phase-in rate. He then showed the same scenario, assuming a 10-year actuarial smoothing period.

Mr. Randall then discussed future potential actuarial issues. He discussed the impact of the TMRS bill not passing and the fact that there would be an immediate need to reduce the actuarial investment return assumption and the city interest crediting assumption. He mentioned the need

to develop a reserve policy in the future. And finally, he briefly discussed the upcoming 2011 experience investigation. Mr. Simpson asked, given the current economy, if we should move this up one year. In response, Mr. Randall discussed the pros and cons of doing so, but concluded that the current timetable is acceptable.

10. Legislative Update and Overview of 81st Legislative Session, including Discussion on Status of TMRS Legislation (HB 360 and SB 908), HB 1358, HB 1344 and Other Filed and Proposed Legislation

Mr. Solis and Mr. Lewis discussed the recent hearing on HB 360. Mr. Solis thanked the Board for its guidance in the interim regarding the Stakeholders Group. He reported that the bill passed out of committee with broad support from the members of the Advisory Committee on Retirement Matters and was referred to the Local and Consent Calendar. He reported that staff will attempt to move SB 908 simultaneously with HB 360. Mr. Solis stated that staff has continued to make it clear that HB 360 is the only bill supported by TMRS.

Mr. Solis also mentioned that he has been asked about TMRS' investments in the current economy and indicated that the education process is continuing. Mr. Henry stated that staff has been adamant regarding keeping HB 360/SB 908 clean. The Board asked to remain informed on other bills affecting TMRS.

11. Executive Director and Staff Reports, including Reports from Administration, Communications, Decision Support Actuary, Finance, Human Resources, Information Resources, Internal Audit, Legal and Member Services

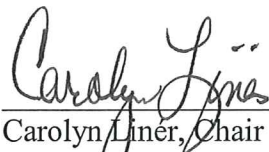
Mr. Henry introduced this item and asked if there were any questions or comments. As there were none, the Board moved on to the next agenda item.

12. Call for Future Agenda Items

Ms. Linér announced a call for future agenda items. As there were none, Ms. Linér adjourned the meeting at 3:30 p.m.



Eric Henry
Executive Director and CIO



Carolyn Linér, Chair
TMRS Board of Trustees