

BOARD OF TRUSTEES

Regular Meeting

Friday, February 24, 2006, 12:00 p.m.

Retirement Fund Conference Room

MINUTES

DEFINED BENEFITS

I. ATTENDANCE, QUORUM, AND CALL TO ORDER

After determining a quorum was present, the Retirement Fund Board of Trustees Regular Meeting for the Defined Benefits Plan was called to order at 12:25 p.m. Friday, February 24, 2006, in the Retirement Fund Conference Room. Chairman Joe T. San Agustin officiated.

Board of Trustees Present:

Joe T. San Agustin, Chairman
Wilfred P. Leon Guerrero, Vice-Chairman
Katherine T.E. Taitano, Treasurer
James J. Taylor, Secretary
Anthony C. Blaz, Trustee
Gerard A. Cruz, Trustee
George A. Santos, Trustee

Staff Present:

Paula Blas, Acting Director
Rosalia Bordallo, Acting Controller
Vince Camacho, Great West Retirement Services
Jackie Blas, Recording Secretary

Public Present:

Terry Dennison, Mercer Investment Consulting
Clint Ridgell, KUAM

II. REVIEW AND APPROVAL OF BOARD MINUTES

A. December 9, 2005 Regular Meeting, December 27, 2005 Special Meeting, January 13, 2006 and January 20, 2006 Regular Meetings

Chairman San Agustin stated that the December 9, 2005 and December 27, 2005 Board Meeting Minutes are being reviewed by Secretary James Taylor.

On motion of Trustee George Santos, seconded by Trustee Gerard Cruz, and without objection, the Minutes of January 13, 2006 and January 20, 2006 Regular Meetings were approved, subject to corrections. Motion passed.

III. CORRESPONDENCE

A. December 29, 2005 Letter from John D. Diego Regarding Request for Service Credit

Trustee Gerard Cruz, seconded by Vice-Chairman Wilfred Leon Guerrero, moved to refer the correspondence listed under Section III to the Members and Benefits Committee. Without objection, the motion passed.

Acting Director Paula Blas stated that the December 29, 2005 letter from John D. Diego regarding request for service credit was referred to the Members and Benefits Committee.

B. January 16, 2006 Memorandum from Eileen V.M.S. Quintanilla Regarding Retirement

Acting Director Blas stated that the January 16, 2006 memorandum from Eileen V.M.S. Quintanilla regarding retirement was referred to the Members and Benefits Committee.

C. January 20, 2006 Letter from Joaquin T. Cruz Regarding the 1991 Hay Study Implementation

Acting Director Blas stated that the January 20, 2006 letter from Joaquin T. Cruz regarding the 1991 Hay Study implementation was referred to the Members and Benefits Committee.

D. January 30, 2006 Letter from Joseph S.N. Taitano Regarding Request for Extension

Acting Director Blas stated that the January 30, 2006 letter from Joseph S.N. Taitano regarding request for extension was referred to the Members and Benefits Committee.

E. January 31, 2006 Letter from Ann A. Soares Regarding Defined Benefits Membership

Acting Director Blas stated that the January 31, 2006 letter from Ann A. Soares regarding Defined Benefits membership was referred to the Members and Benefits Committee.

IV. DIRECTOR'S REPORT - EXECUTIVE SUMMARY

William Don Parkinson vs. Government of Guam, Guam Memorial Hospital Authority and Guam Public School System - Acting Director Blas stated that Mr. Don Parkinson is putting together a proposed order to submit to the Court to retire the \$33 Million debt to the Retirement Fund. Acting

Director Blas stated that a hearing at Superior Court is scheduled for March 3, 2006. Chairman San Agustin stated that the proposed order will require that the \$33 Million debt will be paid in principal and interest over the next six years. Chairman San Agustin stated that the proposed order should also support the Fund's need for more autonomy. Chairman San Agustin stated that Mr. Parkinson is drafting the proposed language of the draft judgment that maybe resolved by next week Tuesday. Chairman San Agustin invited Vice-Chairman Wilfred Leon Guerrero to participate in reviewing the draft judgment. Chairman San Agustin stated that if at any point in time that any agency is late in their contributions, the order will stipulate that the Fund will stop issuing checks for all retirees.

Candelaria Rios, et al. v. Joseph Ada, et al (Special Proceeding Case No. SP206-93) - Acting Director Blas stated that a hearing at Superior Court is scheduled for March 2, 2006. Acting Director Blas stated that the Court will hear both Mrs. Rios' motion for the issuance of a peremptory writ of mandate and a new motion for summary judgment filed by the Attorney General. Acting Director Blas stated that the Attorney General's motion appears to be generally consistent with the positions taken by the Fund. Acting Director Blas stated that the Fund will continue to oppose Mrs. Rios' motion on the grounds stated in the opposition brief that was provided at the January 13, 2006 Board of Trustee's meeting.

Investment Mandate Amendments: Section 8157 and Section 8158 - Acting Director Blas stated that the amendments to Section 8158 have been transmitted to the Legislature. Acting Director Blas stated that Speaker Mark Forbes may be scheduling a public hearing within the next couple of weeks. Acting Director Blas stated that the draft legislation for Section 8157 is with the Board for further discussion. Chairman San Agustin stated that the Attorney General's opinion on Section 8157 should be received by next week Thursday. Vice-Chairman Leon Guerrero stated that the Board had agreed to meet for further discussion on Section 8157 after this meeting.

Organic Act / Trust Agreement - Acting Director Blas stated that Secretary Taylor did a presentation on the Trust Agreement at the last Board meeting. Secretary Taylor stated that he had asked the Board to make a couple of decisions - whether the Board wanted to continue seeking Trust status in conjunction with Congresswoman Madeleine Bordallo or not, or determine it is not useful going down that line because it is unlikely to happen. Secretary Taylor stated that the Legal Counsel's position is that it is unlikely that the Legislature will give up that power. Chairman San Agustin stated that he will ask Mr. Parkinson to incorporate the Trust Agreement in the proposed draft judgment. Chairman San Agustin suggested giving Mr. Parkinson a copy of the proposed Trust Agreement. Secretary Taylor stated that he agrees with providing a copy except that there is some language in the Trust Agreement that needs to be updated or clarified.

Request for Proposal (RFP): Custodial Bank Services - Acting Director Blas stated that she communicated with Mercer Investment Consulting regarding the information needed from the Fund for the draft RFP. Acting Director Blas stated that a copy of the first draft of the RFP would probably be available by the first week in March.

Request for Proposal (RFP): Medical Consultant Services - Acting Director Blas stated that the draft RFP for professional services is still under review with the Members and Benefits Committee. Acting Director Blas stated that the Members and Benefits Committee is waiting to hear from the Fund's Legal Counsel who is reviewing the RFP.

Request for Proposal (RFP): Defined Contribution (DC) Investment Consultant Services - Acting Director Blas stated that the draft RFP for the DC Investment Consultant Services is still with the Investment Committee for review. Vice-Chairman Leon Guerrero asked whether there is a letter from Arriola, Cowan & Arriola regarding this matter. Acting Director Blas stated that Arriola's letter is regarding the Defined Contributions Plan (DC) Third-Party Administrator.

Request for Proposal (RFP): Investment Portfolio Monitoring Services - Acting Director Blas stated that the draft RFP for Investment Portfolio Monitoring Services was approved to be submitted to Legal Counsel for review. Acting Director Blas stated that, with revisions, the draft RFP was sent to Legal Counsel. Acting Director Blas stated that the RFP will be issued on March 6, 2006 which will run for forty-five (45) days.

Public Law 28-94: GTA Sale Proceeds - Acting Director Blas stated that the Rural Telephone Bank (RTB) Stock Redemption Certificate was delivered to Washington by Mr. Marcel Camacho. Acting Director Blas stated that the actual cash will be received by mid March. Chairman San Agustin reiterated that the Fund will receive the \$7.7 Million before the end of the month. Secretary Taylor stated that his understanding is that someone has made a determination that the Guam Telephone Authority (GTA) sale was going to cost the Fund a greater amount than the Fund is getting through this process. Secretary Taylor asked whether the Fund is going to record this as a receivable on the books. Chairman San Agustin stated that the unfunded amount has increased. Trustee Cruz stated that the unfunded amount increased because the sale did not happen at that point in time. Acting Director Blas stated that the GTA unfunded liability becomes an obligation of the General Fund and gets lumped into the overall unfunded amount. Secretary Taylor stated that it should not be a lumped into the overall unfunded amount because it is a different situation.

Secretary Taylor stated that it should be determined whether there is an amount involved and whether it should be recorded as a receivable. Acting Director Blas stated that she does not think it needs to be recorded as a receivable. Chairman San Agustin stated that Secretary Taylor is asking whether the difference of the unfunded liability could be recorded as a receivable. Acting Controller Rosalia Bordallo replied, "no." Acting Controller Bordallo stated that if the amount was to be booked as a receivable, who is going to pay for it. Secretary Taylor stated that the Fund would pursue payment from the Government of Guam. Acting Director Blas stated that the amount gets lumped into the overall contribution rate that is paid to the Fund by the Legislature. Secretary Taylor stated that the Fund should ask its auditor on what the Retirement Fund needs to do on this matter. Acting Controller Bordallo stated that she is concerned with GTA if it is booked as a receivable, the audit could tell the Fund to write it off. Secretary Taylor stated that the Fund's position legally will be stronger if it is done that way. Chairman San Agustin stated to document it as a footnote recognizing it as an obligation. Acting Controller Bordallo stated that it is not GTA's obligation anymore. Secretary Taylor stated that it is a GTA related obligation. Fund Management is to review the matter with the auditor and report to the Board on the auditor's recommendation.

Public Law 28-38 - Acting Director Blas stated that the Fund is processing applications for retirement eligible employees. Acting Director Blas stated that the monthly interest payments for GPSS and GMHA are current.

Public Law 28-66 - Acting Director Blas stated that none of the money has been received from the \$1.4 Million appropriated from the General Fund to the Retirement Fund for Guam Memorial Hospital

Authority (GMHA). Chairman San Agustin asked about the \$660,000.00. Acting Director Blas stated that the \$660,000.00 was received from GMHA, not from the General Fund. Acting Director Blas stated that \$800,000.00 is still outstanding.

Century 21, Realty Management Company, Inc.: Parking Lot Lease - Acting Director Blas stated that the Parking Lot Use Agreement is with First Hawaiian Bank's attorney and Century 21 for their review and consideration. Acting Director Blas stated that nothing has been received from the bank. Chairman San Agustin stated that First Hawaiian Bank is currently using the parking lot but First Hawaiian Bank is not paying anything right now. Chairman San Agustin stated that there is no incentive for First Hawaiian Bank to push the agreement because they would have to pay. Chairman San Agustin suggested asking for a good-will payment.

John Rios' Request for Indemnification - Acting Director Blas stated that the documents requested by the Director and Officers underwriter's attorney have been submitted to them including a copy of the second indictment and dismissal. Acting Director Blas stated that their decision should be received within a couple of weeks. Chairman San Agustin stated that civil cases are covered to be indemnified. Chairman San Agustin stated that in case of conviction, criminal cases should not be indemnified. Chairman San Agustin stated that the agency should be notified and the agency should set a cap on expense. Chairman San Agustin stated that if the accused is convicted on a criminal case, the accused must reimburse the agency for the cost of defense. Chairman San Agustin stated that the Fund does not have a policy now. Trustee Gerard Cruz stated that the Board had requested for a policy. Acting Director Blas stated that Legal Counsel is working on establishing a policy.

Contributions - Acting Director Blas stated that all agencies are current with their FY2006 employee and employer contributions.

Financial Statement / FY2005 Audit - Acting Director Blas stated that the books for January 2006 have been closed and the FY2005 audit is ongoing. Acting Director Blas stated that the audit would probably be released by April 30, 2006.

FY2006 Retirees' Supplemental and COLA - Acting Director Blas stated that the January 2006 supplemental benefits for retirees and survivors were issued. Acting Director Blas stated that the February 2006 supplemental benefits should be issued by next week from the General Fund.

Defined Contributions Plan (DC) Third-Party Administrator - Vice-Chairman Leon Guerrero stated that the letter from Arriola, Cowan & Arriola may be related to the Bank of Hawaii courtesy visit. Acting Director Blas stated that at the last Investment Committee meeting she was asked to get three (3) quotes for legal services to review the Third-Party Administrator Request for Proposal (RFP). Acting Director Blas stated that she was concerned with whether any attorney had a conflict of interest. Acting Director Blas stated that the Chairman suggested having the Fund's Legal Counsel terminate their relationship with Great West Retirement Services in order to be able to review the Third-Party Administrator RFP. Chairman San Agustin stated that there may be a problem getting three (3) quotes because of the potential conflict of interest. Chairman San Agustin further stated that the Fund's Legal Counsel has a conflict of interest with the current parties involved.

Treasurer Katherine Taitano stated that the Fund could have the same problem again. Acting Director Blas stated that she could send another RFP for legal services and pick up two (2) attorneys. Treasurer

Taitano asked why pick up two attorneys. Acting Director Blas stated that one would be conflicted out if needed and the other would be an alternative. Acting Director Blas asked whether the Board is in agreement with allowing the Fund's Legal Counsel to terminate services with Great West Retirement Services or to sign the waiver for the conflict of interest. Chairman San Agustin suggested revisiting the waiver. Treasurer Taitano stated that she would like for Legal Counsel Joanne Grimes to review the RFP. Acting Director Blas stated that the problem is not being able to determine if the firms are representing potential offerors. Trustee Cruz stated that the attorneys will not know who the offerors are. Chairman San Agustin stated that there could be an existing conflict. Trustee Cruz suggested for a separate attorney to do this. Chairman San Agustin stated that the Acting Director is offering two options: 1) to get three quotes for legal services to review the Third-Party Administrator RFP or 2) go with the Fund's Legal Counsel. Trustee Cruz stated that at the December 9, 2005 Board Meeting, Management was directed to go out and get three (3) quotes.

V. LEGAL COUNSEL'S REPORT

Acting Director Blas stated that there is no change in the Legal Counsel's report that was made at the January 2006 report. Chairman San Agustin asked what is being done on the Ralph Gutierrez case. Acting Director Blas stated that the Judge verbally denied Mr. Gutierrez's motion for dismissal. Acting Director Blas stated that the Judge has not issued a written decision.

Acting Director Blas stated that Mr. MacIntyre is disputing the effective date of his disability retirement benefits. Acting Director Blas stated that Mr. MacIntyre is appealing, but that the case has been pending, without any action, since September 2002. Acting Director Blas stated that Mr. MacIntyre has relocated off-island.

VI. TREASURER'S REPORT OF FINANCIAL STATUS

A. Cash Income/Disbursements: FY1999 – FY2005

Chairman San Agustin stated that he provided several charts to show the Fund's financial status. Chairman San Agustin stated that he is concerned with the Cash Return of Interest, Net of Fees. The Fund did well in FY2003 which was 4.57%. Chairman San Agustin stated that the 2002 Market Rate of Return was zero percent. Chairman San Agustin provided a chart showing the shortfall for FY1999 through FY2005. Chairman San Agustin stated that the Defined Benefits retirees are increasing and this causes increased demand on the monies in trust. Chairman San Agustin stated that the Funding Ratio was at its highest in 1998 at 72.6%. Chairman San Agustin stated that the Funding Ratio was at its lowest in 1989 at 39.9%. Trustee Cruz stated that the Market Return went up in FY2003 to 9.90%.

VII. STANDING COMMITTEE REPORTS

A. Members and Benefits Committee

Trustee George Santos reported to the Board of Trustees on his Committee's January 2006 end of the month report.

Trustee George Santos, seconded by Trustee Anthony Blaz, moved to approve the recommendation of the Members and Benefits Committee contained on Pages 4-7, based on the Committee's review and findings during their meeting of January 18, 2006 and subsequent meetings thereafter. Without objection, the motion passed.

B. Investment Committee

Vice-Chairman Leon Guerrero stated that he submitted a report of the due diligence meeting conducted on February 22, 2006. Vice-Chairman Leon Guerrero stated that the review covered the period ending December 2005. Vice-Chairman Leon Guerrero stated that the Fund is lagging other U.S. Public Funds due to legal restrictions on its investments. Vice-Chairman Leon Guerrero stated that the review covered the Bond Managers' performance. This included Aberdeen Asset Management (formerly Deutsche Asset Management) and Franklin Templeton Fixed Income (formerly Fiduciary Trust). Vice-Chairman Leon Guerrero stated that the Investment Committee is recommending retaining both Aberdeen Asset Management and Franklin Templeton Fixed Income.

Trustee Cruz had a question for Mr. Dennison on the recommendation to retain the General Motors Bonds. Trustee Cruz asked whether they still should be held. Mr. Terry Dennison, Mercer Investment Consulting, stated that General Motors Acceptance Corporation (GMAC) is separate from General Motors. Mr. Dennison stated that the second of the two bonds will mature in about eleven months. Mr. Dennison stated that with respect to performance, the Fund was up 6.0% for the year. For three years, the Fund was up 9.3% per year. Mr. Dennison stated that one of the concerns that they have is the stability of the Fund long term as the need to sell investments continues to grow. Mr. Dennison stated that the Defined Contribution benefits payroll will grow. Mr. Dennison stated that the Fund is looking at more negative cash flows. Steps need to be taken to improve the results of the asset performance. Mr. Dennison also stated that they are watching Aberdeen.

Mr. Dennison stated that no other managers were reviewed this quarter. Vice-Chairman Leon Guerrero stated that there are two fixed income managers. Mr. Dennison stated that two of five international managers have been funded. Capital International has an issue with the form of investment. There are two others, Grantham, Mayo, Van Otterloo (GMO) & DFA Investment Dimensions (DFA) – the GMO issue is getting a clarification from the Attorney General regarding the applicability of aspects of Section 8157. Mr. Dennison stated that there is no reason not to fund DFA. Mr. Dennison stated that the substance of the funding resolution was to substitute, temporarily, DFA for GMO. Acting Controller Rosalia Bordallo suggested amending the motion for the funding. Acting Controller Bordallo stated that the initial plan stated that Fisher Investments Institutional Group (Fisher) will get money from Aberdeen Asset Management (Aberdeen) and GMO will get money from Lazard Asset Management (Lazard). Acting Controller Bordallo stated that the Retirement Fund will liquidate the equity across the board. Trustee Cruz stated that the overall portfolio will be at a gain. Acting Controller Bordallo suggested that that the original motion be amended to state that the money could be taken from Lazard to fund DFA.

Vice-Chairman Wilfred Leon Guerrero, seconded by Trustee Gerard Cruz, moved to amend the original motion of funding Fisher Investments Institutional Group (Fisher) from the assets of Aberdeen Asset Management (Aberdeen) and Grantham, Mayo, Van Otterloo (GMO) from the assets of Lazard Asset Management (Lazard). Without objection, the motion passed.

Vice-Chairman Wilfred Leon Guerrero, seconded by Trustee Gerard Cruz, moved that Lazard Asset Management (Lazard) will be liquidated at a gain and that it is to fund the mutual funds and Grantham, Mayo, Van Otterloo (GMO). Without objection, the motion passed.

Chairman San Agustin stated that he is concerned with the actuarial rate of return of 7%. Chairman San Agustin asked what rate the Fund would need annually to cover inflation and its relation to the actuarial rate of return of 7%. Mr. Dennison stated that Mercer's forecast for inflation is 2.5%. Chairman San Agustin asked Mr. Dennison whether the Fund would then need a real rate of return of 9.5%. Mr. Denison replied, "yes." Chairman San Agustin asked whether the Fund is achieving that rate at this point. Mr. Dennison replied, "no." Chairman San Agustin asked if any managers reviewed have reached or exceeded the bench mark. Vice-Chairman Leon Guerrero stated that one of the managers reviewed did reach the bench mark for one year. Chairman San Agustin asked how the Fund could tie the bench mark to the target goal of 9.5%. Vice-Chairman Leon Guerrero stated that Aberdeen for one year met the bench mark. Mr. Dennison stated that the expenses relative to the benefit payments could be cut to zero and it will make very little difference.

RECESSED: 2:20 p.m.

RECONVENED: 2:40 p.m.

At this time, Mr. Dennison continued with his presentation. Mr. Dennison stated that Mercer was able to get information from Atalanta Sosnoff Capital Corporation (Atalanta) on the impact on portfolio structure. Mr. Dennison stated that he would have expected that the effects of the dividend restrictions would have been low with a growth manager. Mr. Dennison stated that the impact on core is larger than expected. For one year Atalanta's typical client accounts was up 19.7. For the Government of Guam (GovGuam) it was up 13.5; for three years Atalanta's typical account was 18.0, for GovGuam 14.7; for five years Atalanta's typical account was 3.6, for GovGuam 2.7; for ten years Atalanta's typical account was 11.5, for GovGuam 9.9.

Mr. Dennison stated that the other concern expressed was that because of the restrictions, they are not able to invest the way they think they should invest. Chairman San Agustin asked whether they would be able to meet the bench mark. Mr. Dennison replied, "no." Chairman San Agustin asked whether it would be possible to revisit the fee structure. Mr. Dennison stated that RCM Capital Management (RCM) chart was distributed on February 22, 2006. Mr. Dennison stated that if you look at RCM's unrestricted portfolio, they trounced the bench mark. Chairman San Agustin asked is it because of the restrictions. Mr. Dennison replied, "yes." Chairman San Agustin asked whether the bench mark is less than the actuarial rate of 7.5%. Mr. Dennison stated that another concern is that they can't make the portfolio look the way they want. Mr. Dennison stated that they are producing a lack of diversification between the different stocks. Mr. Dennison stated that he did an analysis of the holdings in the portfolio. Atalanta had four names versus eleven in their unrestricted portfolio.

Mr. Dennison stated that the managers can not do much other than add value with the existing legal requirements imposed by the Retirement Fund. The way the manager constructed the asset allocation is so that over the long term, the sum of the expected returns is greater than 7.5%. In 2002, the Standard & Poor's (S&P) was down 20%. Mr. Dennison stated that the hedge funds can produce absolute returns. Mr. Dennison stated that to move to an absolute term structure will be quite a shift which will require a long visit with the Legislature.

Mr. Dennison reported on the cash flow considerations for fiscal year ended September 30, 2004. Mr. Dennison stated that over time, the assets plus contributions must equal benefits. Contributions were \$83.5 Million; the total income was \$40 Million; the benefit payments was \$170 Million and the

administrative expenses was \$2 Million leaving a negative cash flow of \$49 Million; and the required rate of return of 3.93% is the rate of return that is what the Fund needs to get the assets on keep the Fund arithmetically stable. Chairman San Agustin asked whether the Fund needs to have the 3.93% to meet the net cash flow. Mr. Dennison replied, "yes." Mr. Dennison stated that the trend analysis is that: 1) contributions are likely to decline as active members retire or leave government service; 2) benefit payments are certain to increase as active members retire and if any benefit improvements are enacted; 3) the combination of contributions declining and benefit payments increasing will require an increase in investment income and/or asset liquidations; 4) interest yield per invested dollar in fixed income securities is likely to be flat or declining as average coupon yields adjust to historically low intermediate and long rates; and 5) dividend yield per invested dollar is likely to be flat or increasing only modestly as companies either retain cash for corporate purposes or use cash for share buy-backs to enhance shareholder value. Given this analysis, Mr. Dennison stated that the Board needs to take effective action to increase investment returns and ensure the Fund receives an actuarially sound rate of return from the Legislative budget.

Mr. Dennison stated that the proposal is to amend Section 8157 to permit up to 50% of the equity portfolio in issues which do not meet the dividend and earnings requirements of the present law. Mr. Dennison stated that the likely impact would be increasing the overall rate of return of the portfolio. Mr. Dennison stated that in the analysis, the current Section 8157 requirements are significantly increasing the risk in the portfolio by forcing a concentration in few permitted securities or creating an inability to maintain style diversification. Mr. Dennison stated that the analysis addresses only the cash flow impact of the proposed changes to Section 8157. These proposed changes will increase overall investment returns.

Mr. Denison stated that the current dividend yield is calculated to be 1.66% as of September 30, 2004 which is somewhat higher than that of the S&P at that time. Mr. Dennison stated that in the worst case, amendment to Section 8157 could cause a reduction in the investment return. However, he noted this would be more the offset by the overall increase in the return to the portfolio.

(At this time, Chairman San Agustin walks away from the meeting to answer a phone call – walks back in).

Mr. Dennison stated that to fully replace the worst case fall in dividend income, the Fund only needs to see a 45 basis point (0.45%) increase in total fund performance to provide the equivalent funds available for benefit payments. Mr. Dennison stated that the Fund is already running a large negative external cash flow requiring systematic liquidation of securities to pay benefits. There is no creditable asset mix under current guidelines that can generate enough income to meet the benefit payment requirements. Under the current law, the Fund will continue to have a negative external cash flow. Mr. Dennison stated that in the fiscal year ending September 30, 2004, it was a good year for performance, more than a third of the 9.38% total fund return was consumed to make benefit payment, leaving only a 5.99% growth in wealth to rebuild reserves for bad years. The assets do matter as even greatest rate of return applied to a small asset base will only create a small amount of wealth. Chairman San Agustin asked if there was only 6% growth in wealth to rebuild the reserves – does the Fund have to grow that much. Mr. Dennison stated that even in a good year, we have less than 6% growth in wealth above the necessary withdrawals.

Mr. Dennison stated that he provided a hypothetical analysis. Case one shows a more positive performance in up markets. Case two shows a less positive performance in up markets which is where the Fund is today. Mr. Dennison stated that case one involves changing Section 8157. Case two shows that Section 8157 as it stands might reduce losses under limited circumstances. Mr. Dennison stated that the Fund overall will net gain and will show decline in assets. Mr. Dennison stated that relaxing Section 8157 would: 1) reduce the risk in the equity portfolios by allowing more diversification, reducing concentration in a few acceptable equity stock names; 2) reduce the risk in the equity portfolios by permitting more effective style diversification; 3) probably enhance the return of the portfolio, particularly in portions of the market-cycle where growth is in factor; 4) permit the Fund to get full value from its investment managers and the fees the Fund pays by allowing the use of first named equity rather than second best names. Chairman San Agustin pointed out that the Fund will not lose as much. Mr. Dennison reiterated that relaxing Section 8157 would reduce the risk of the equity portfolios by allowing more diversification. Mr. Dennison stated that he is concerned with the managers with different mandates being forced into buying the same things.

Chairman San Agustin asked whether by having more diversification, could the Fund reduce the number of investment managers. Vice-Chairman Leon Guerrero asked Mr. Dennison if he is saying that during good times the Fund do not make as much and during bad times the Fund does not lose as much. Mr. Dennison stated yes. Chairman San Agustin asked if the Fund reduces the number of investment managers would it reduce the Fund's expenses. Mr. Dennison replied, "yes." Mr. Dennison stated that the investment expenses as opposed to the administrative expenses are \$3.5 Million, whereas the benefit payroll is \$170 Million. Chairman San Agustin requested for an update for FY2005. Mr. Dennison stated that the data could be produced by Acting Controller Bordallo. Chairman San Agustin commended Mr. Dennison on his analysis. Mr. Dennison stated that the information on impact is most severe with growth equities. The impact on core equity is larger than expected.

C. Audit Committee

None

D. Governmental Liaison

None

VIII. TRAVEL REPORT

A. Joe T. San Agustin, Chairman: January 11-13, 2006 - Scottsdale, Arizona

Chairman San Agustin stated that he has submitted his travel report for the Board's information on the Public Funds Summit, sponsored by the Opal Financial Group. He attended the Summit on January 11-13, 2006 in Scottsdale, Arizona.

IX. OLD BUSINESS

A. Rationale on Asset Re-Balancing

Vice-Chairman Leon Guerrero stated that the Investment Committee took care of Item IX A above. Trustee Cruz asked whether the Fund needs to drawdown for February. Acting Controller Bordallo replied, "no." Acting Director Blas stated that the Fund may need money for March if the \$7.7 Million does not come through.

B. Government of Guam Retirement Fund Board Resolution No. 2006-001

Vice-Chairman Leon Guerrero recommended moving forward with the proposed legislation. Acting Director Blas stated that this would include Section 8158 and Section 1857.

Vice-Chairman Wilfred Leon Guerrero, seconded by Trustee Gerard Cruz, moved to approve Resolution No. 2006-001. Without objection, the motion passed.

C. Negotiation Committee Report for Director/Chief Executive Officer Position

Vice-Chairman Leon Guerrero stated that the Negotiation Committee recommends moving forward with transmitting the Retirement Fund's Omnibus Bill to the Legislature for public hearing and reannouncing the Director's position both locally and nationally. Chairman San Agustin stated that the position should be announced before proceeding with the proposed legislation. Vice-Chairman Leon Guerrero informed the Board that the reason why the sole applicant did not take the job was because he was offered a quarter of a million dollar job off-island. Acting Director Blas stated that the Director's position will be announced locally and nationally.

Vice-Chairman Wilfred Leon Guerrero, seconded by Trustee Gerard Cruz, moved to accept the Negotiation Committee's recommendation to move forward with transmitting the Retirement Fund Omnibus Bill to the Legislature for public hearing, and to announce the Director/Chief Executive Officer position again, both locally and nationally. Without objection, the motion passed.

Trustee Anthony Blaz asked why announce nationally. Trustee Blaz recommended to announce locally again and see if anyone would apply. Acting Director Blas stated that it was advertised for three weeks locally. Vice-Chairman Leon Guerrero stated to advertise simultaneously locally and nationally. Trustee Blaz withdrew his objection to announce nationally.

D. John Rios' Request for Indemnification

Chairman San Agustin stated that Item IX D above was covered under the Director's Executive Summary.

At this point, Trustees George Santos and Anthony Blaz were excused from the meeting (1:55 p.m.)

X. NEW BUSINESS

A. Milliman Analysis Regarding Defined Benefits Plan Freeze

Chairman San Agustin stated that the benefit is much better for the active members. Trustee Cruz stated that payments will not be the same. Chairman San Agustin stated that the Defined Benefit (DB) members are paying 9.50%. Trustee Cruz stated that if the normal cost is reduced, then the required contribution rate will go down. Chairman San Agustin stated that the unfunded liability will not increase. Secretary Taylor stated that the only option an employee has been given is that they could take what they have contributed and roll it over to the Defined Contribution Plan (DC). Secretary Taylor stated that the freeze provides the employees with the possibility of keeping both – keep

existing DB and be able to move to DC. Trustee Cruz stated that no more money is going to be contributed to the DB side from the employee, only the government share which will be for the unfunded liability. Trustee Cruz stated that the unfunded liability will be reduced at a quicker rate if there is no growth in the DB obligations. Trustee Cruz stated that changing to this method will increase the projected life of the DC Plan.

Secretary Taylor stated that this is a financial analysis problem. Acting Director Blas stated that she asked Mr. Rich Nuzum for a more detailed analysis. Trustee Cruz asked whether there is a savings if the contribution to the DC participant goes up slightly. Secretary Taylor stated that the problem that the Fund has is that the Legislature sets the contribution for the DC Plan too low. Secretary Taylor stated that it should be at least 7.5%. Acting Director Blas stated that she asked Mr. Nuzum to use a 5, 6, 7 contribution rate for the DC Plan on his analysis.

Trustee Cruz stated that the Fund needs to work out the numbers. Mr. Dennison stated that the participants might discover that this would hurt them. Secretary Taylor stated that he would like to work with the figures. Vice-Chairman Leon Guerrero stated that the Fund needs to educate the employees of the implications. Chairman San Agustin asked whether the Fund could afford to stay on the same course. Acting Controller Bordallo stated that the supplemental and COLA payments are cash that could have been provided to the Fund to decrease the unfunded liability for future retirees. Mr. Dennison stated that this is a zero-sum game - everyone can't win. Chairman San Agustin stated that the alternative is to reduce future benefits. Chairman San Agustin stated that the Fund is stabilized at 1.2 Billion. Chairman San Agustin stated that the Fund is basically bankrupt. Chairman San Agustin asked how will the Fund get out of this bankruptcy. Acting Controller Bordallo stated to stop using the current employees' money to pay the current retirees. Current employees' money should be set aside for the exclusive use of the current employees when they retire.

B. Information Technology Security

Acting Director Blas stated that the Fund has adequate security. Chairman San Agustin stated that the Fund should have a written policy in place to protect the records. Chairman San Agustin asked if there is an Information Technology Policy in place. Mrs. Bordallo stated that the Fund once had a policy. Acting Controller Bordallo stated that if the Fund does not get the correct data from the agency, the data is bumped. Management was asked to begin the development of an Information Technology Security Policy.

XI. OPEN DISCUSSION / GENERAL PUBLIC INPUT

A. Courtesy Visit: Bank of Hawaii Officers – Dennis Lock and Janet Katakura

Chairman San Agustin welcomed Mrs. Marilyn Megofna and the visiting Bank of Hawaii Officers. Mrs. Megofna introduced Ms. Janet Katakura and Mr. Dennis Lock. Ms. Katakura stated that she has managed fixed income portfolio for twenty-three years in Hawaii. Mr. Lock stated that he has been coming to Guam since 1991. Mr. Lock stated that he is married to a Chamorro lady. Mr. Lock stated that he has held positions in Bank of Hawaii for twenty-four years. He is Vice President in Institutional and Pacific Islands Department with responsibilities primarily on client relationship on the custodial side of accounts. Trustee Cruz inquired about the due diligence with Palau. Mr. Lock stated that it was good. Vice-Chairman Leon Guerrero asked whether the Federal Government requires Palau

to invest the money from the Compact of Free Association. Mr. Lock stated that the money that they got from the Compact is the agreement with the Department of the Interior which is that they invest in the U.S. Treasury. Vice-Chairman Leon Guerrero asked whether it is used for operations. Mr. Lock stated that they have trust funds to supplement their taxes.

Chairman San Agustin introduced the Board of Trustees to Ms. Katakura and Mr. Lock.

XII. ANNOUNCEMENTS

A. Rescheduling of April 14, 2006 Board Meeting

Chairman San Agustin informed the Board of Trustees that the Board's regularly scheduled meeting on April 14, 2006 is being moved to April 21, 2006.

XIII. ADJOURNMENT

There being no further business before the Board for the Defined Benefits Plan, on motion of Trustee Gerard Cruz, seconded by Treasurer Katherine Taitano, and without objection, the meeting was adjourned at 3:40 p.m. Motion passed.

I hereby certify that the foregoing is a full, true and correct copy of the Minutes of February 24, 2006 Regular Meeting duly adopted and approved by the Government of Guam Retirement Fund Board of Trustees on July 14, 2006.

James J. Taylor, Board Secretary

RECORDING SECRETARY:

Jackie Blas