

TOWN OF HANOVER TRUSTEES OF TRUST FUNDS

Meeting Minutes

Thursday, August 26, 2010 at 7:30 a.m.

In attendance: B. Doyle (Trustee), P. Gardent (Trustee), J. Pierson (Trustee); M. Wrenn (Bank of America/Merrill Lynch); J. Wesson (Bank of America/Merrill Lynch); B. McClain (Town Administration)

Discussion of Investment Policy

Mr. Wrenn highlighted the advantages of a total return spending policy vs. the income-only spending policy currently mandated by the State of New Hampshire for Trustees of Trust Funds. These advantages included better potential returns on the portfolio as investment decisions are made with an eye towards broader diversification; this greater diversification also provides for less risk. With an income-only spending policy, the tendency is overweight the portfolio in bond funds to have a reliable and predictable income stream. If the manager does opt to invest in equities, the choices are skewed towards those stocks that pay dividends to again secure some sort of steady income. Under the income-only spending policy, realized capital gains and short term capital gains are considered principal gains, and, as they are not considered income, they are not distributed. With a total return spending policy, a portion of the overall fund appreciation would be eligible to be spent. Trustee Doyle remarked that there will also be more straightforward reporting with a total return spending policy, as the portfolio would be reported using more standard unitized fund accounting. Mr. Wrenn agreed and noted that the State's MS-9, Report of Trust Funds, would need to be completely revised – and this would be a good thing!

The Trustees asked what the State's current thinking was on allowing Trustees of Trust Funds to adopt a total return spending policy. Mr. Wrenn reiterated that under current State law, only income was eligible to be spent from common trust funds (those invested in perpetuity). The State is still evaluating the recent transition from the Prudent Man investment approach (where the manager was to evaluate each individual investment holding) to the Prudent Investor approach (where the portfolio is evaluated as a whole to make sure diversification is proper). Mr. Wrenn reported that the State is letting this transition percolate for a few years and then will be more receptive to allowing a total return spending policy for Trustees of Trust Funds. He noted that the State several years ago allowed all other entities that hold trust funds in the State to adopt a total return spending policy; the only types of funds currently prohibited from adopting such a policy are the Common Trust Funds held by Trustees of Trust Funds.

Mr. Wrenn suggested writing a letter in the future to Ms. Terry Knowles in the State's Charitable Trust Unit urging the State to allow Trustees of Trust Funds to adopt a total return spending policy. Mr. Gardent asked Mr. Wrenn to provide articles and other bulleted information that could be used as the basis for a letter from the Trustees. Trustees acknowledged that such a change would be slow in coming and agreed that a letter to Ms. Knowles was in order. They will await material from Mr. Wrenn as the "trigger" to compose and send the letter. Mr. Gardent noted that the only funds impacted by this issue are the "Hanover Common Trust Funds" which are endowment funds. The Bridgman Fund as an expendable fund is not impacted by this rule.

Investment Portfolio Suggestions

Mr. Wesson indicated that he hoped he would get some resolution from the Trustees on moving forward with the changes to the investment portfolio as originally proposed in April 2010. He confirmed that at the end of April 2010, Bank of America/Merrill Lynch (BAML) sold Columbia Funds; however, the current fee forgiveness for investment in such funds would be extended for five years.

Mr. Wesson started to walk through the Zephyr Analysis and the presentation he had prepared, focusing on page #9: Current Portfolio vs. Sample Enhanced Portfolio. The proposed portfolio represents BAML's "best thinking" portfolio for non-profits with holdings less than \$5mm. Trustee Gardent confirmed that the Trustees would not be charged any load fees under the proposed portfolio.

Trustee Doyle had a fundamental question in response to the transition in the portfolio holdings regarding the Trustees' comfort with increased risk. The current investment portfolio does not include any emerging market or real estate funds, and the proposed portfolio does; consequently, the standard deviation of the proposed portfolio is higher. Trustee Doyle's question to the Trustees is: "Do we want to take on more potential volatility to achieve more potential investment gains?"

- Yes or no
- If yes, one would expect the income available for spending from the Common Trust Funds to be reduced somewhat due to the prohibition of a total return spending policy as discussed above

Trustees agreed returns certainly matter, but the volatility in the portfolio is a significant issue. After some general discussion, they concluded that less volatility is preferred given the current income-only spending restrictions and the fact that there is no influx of new monies to these funds.

Mr. Wesson and Mr. Wrenn accepted the Trustees' verbal approval to move the investment holdings over to the proposed portfolio with affirmation that they will look to lesser volatility in the fixed income holdings and will be mindful in trying to keep income of the Common Trust Funds consistent from year to year with some modest growth. Mr. Wesson and Mr. Wrenn acknowledged the concerns the Trustees expressed regarding volatility and will exercise their discretion within the context of the investment portfolio.

Trustee Gardent mentioned that the Investment Policy states an investment objective of exceeding the long-term rate of inflation as measured by the CPI by 3.0%. Mr. Wesson agreed to add this metric to their presentation against which to measure portfolio performance. Mr. Wrenn offered to send a quarterly investment performance update to keep the Trustees current now that they were making semi-annual (vs. quarterly) presentations. The Trustees asked for a one-page Executive Summary highlighting the quarter's investment performance vs. the appropriate benchmarks. Mr. Wrenn agreed to e-mail a report in later January with the December 2010 results; and they would plan on attending an April 2011 meeting to present March 2011 results.

Review and Approval of Annual State Reports (MS-9, Report of Trust Funds, and MS-10, Report of Common Trust Investments)

Ms. McClain noted that the Town's independent auditors have reviewed the MS-9 and MS-10 and that these reports are tied back to the various investment statements. She also confirmed that the MS-10 is prepared by Mr. Wrenn, and she ties the MS-9 back to this report as well.

The Trustees discussed the MS-9, Report of Trust and Capital Reserve Funds, and the MS-10, Report of Common Trust Fund Investments, for the period ending June 30, 2010 and signed the forms for submission to the State, as presented.

Transaction Authorization

Trustees approved the following transactions:

- Withdrawal of \$190,000.00 from the Land and Capital Improvements Expendable Trust Fund (for partial funding of the Hayes Property purchase)
- Deposit of \$158.00 to the Etna Library Expendable Trust Fund

Other Business

There was a general discussion of the annual recommendation to the Hanover School District on the appropriate level of spending from the Bridgman Fund for the upcoming fiscal year. The School District appreciates knowing the Trustees' recommendation early on so that it can be factored into the budget that will be presented at the March District Meeting. Trustees asked Ms. McClain to send a statement along the following lines to the School District:

The Trustees of Trust Funds continues to encourage the Hanover School District to treat the Bridgman Fund as a quasi-endowment and to utilize only the earned income to support eligible projects in any given fiscal year. Based upon current market values, the Trustees recommend a FY2012 expenditure from the Bridgman Fund of \$35,000. If financial markets head into a significant downturn, the Trustees urge the School District to respond accordingly and to revisit the need to draw funds from the Bridgman Fund.

Ms. McClain will try to schedule the next Trustees meeting for sometime in mid to late January 2011.