
STATEMENT OF INVESTMENT POLICY AND OBJECTIVES

For The

CITY OF GAINESVILLE DISABILITY PENSION FUND

December 20, 2007

I. INTRODUCTION AND BACKGROUND

The City of Gainesville Disability Pension Fund is a benefit plan established by the City of Gainesville City Commission. The Fund is administered by the City Manager and is maintained to provide for the payment of a portion of health insurance premiums for persons eligible for Disability Pension coverage.

The City Commission has the responsibility to develop a policy for the investment of the assets of the Fund. The investment of the assets of the Fund must be consistent with the written investment policy adopted by the City Commission (Section 2-438 of the Gainesville City Code). The policies are structured to maximize the financial return to the Fund consistent with the risks incumbent in each investment and are structured to establish and maintain an appropriate diversification of the Fund's assets. To assist the City Commission in this function, they are authorized to engage the services of investment and actuarial consultants to provide expert assistance. The City Commission periodically undertakes studies to evaluate the potential consequence of alternative investment strategies on the long term well being of the Fund. In the view of its consultants and the City Commission, the investment program defined in this Statement will produce a result over the long term consistent with the Fund's primary objective of preserving and enhancing the purchasing power of assets.

In the implementation of the investment program, the Fund will employ investment managers who have demonstrated expertise with particular asset classes. Furthermore, the Fund's investment managers utilize a variety of investment approaches. This diversification of managers and investment approach should reduce the risk of loss and contribute to the attainment of a more consistent positive return. Nonetheless, there will be short term periods when the fund may experience negative returns. Such periods are not inconsistent with achievement of the targeted long term objective.

II. INVESTMENT POLICY AND OBJECTIVES

Based on analysis of the Fund assets and expected investment returns and risks associated with alternative asset mix strategies, the City adopted the following asset class targets, based on market value:

EQUITY	<u>% Range</u>	<u>% Target</u>
— Large Capitalization Value Manager	12.0 – 22.0%	17.0%
— Large Capitalization Growth Manager	12.0 – 22.0%	17.0%
— Small Capitalization Value Mgr.	6.0 – 16.0%	11.0%
— Small Capitalization Growth Mgr.	2.0 – 12.0%	7.0%
— International Manager	13.0 – 23.0%	18.0%
Total Equity	65.0 – 75.0%	70%
FIXED INCOME MANAGER	25.0 – 35.0%	30%
		100%
TRADITIONAL ASSET CLASSES		
EQUITY	<u>% Range</u>	<u>% Target</u>
Large Capitalization Value Manager	10% – 25%	17.5%
Large Capitalization Growth Manager	10% – 25%	17.5%
Small Capitalization Value Manager	2.5% - 15%	7.5%
Small Capitalization Growth Manager	2.5% - 15%	7.5%
Developed International Value Manager	5% - 15%	10.0%
Developed International Growth Manager	5% - 15%	10.0%
Emerging Markets Manager	0% - 10%	5.0%
Total Equity	65% - 85%	75.0%
FIXED INCOME MANAGER	0% - 10%	5.0%
TOTAL TRADITIONAL ASSET CLASSES	60% - 90%	80.0%
ALTERNATIVE ASSET CLASSES	<u>% Range</u>	<u>% Target</u>
REAL ESTATE		
Public REIT (Equity)	0% - 5%	0.0%
Private Real Estate (Fixed)	5% - 15%	10.0%
Total Real Estate	5% - 15%	10.0%
FUNDS OF HEDGE FUNDS & MANAGED	5% - 20%	10.0%
FUTURES		
PRIVATE EQUITY	0% - 5%	0.0%
TOTAL ALTERNATIVE ASSET CLASSES	10% - 35%	20.0%
TOTAL TRADITIONAL & ALTERNATIVE	90% - 100%	100.0%

The ranges are established as maximum weightings in each respective asset class. If the investment manager determines that a percentage of their allocation should be invested in cash, then they are permitted that flexibility and will be evaluated by their decisions accordingly.

Over time, it is the City's intention to direct cash flows toward the asset class(es) that are under-represented and away from the class(es) that are over-represented.

The General investment objectives of the City are as follows:

1. Establish a Prudent Investment Program

Although the Fund is not covered by the Employee Retirement Income Security Act of 1974 (ERISA), the assets of this Fund shall be invested in a manner consistent with the fiduciary standard set forth in ERISA, as though ERISA applied to the Fund; namely, (1) in accordance with the safeguards and diversity to which a prudent investor would adhere (2) and all transactions undertaken on behalf of the Fund must be for the sole interest of Plan participants and their beneficiaries in order to provide benefits and pay the expenses of the Fund. The Disability Pension Fund investment program must operate in compliance with all applicable State and Federal laws and regulations concerning the investment of trust assets

2. Achieve Growth in Purchasing Power

Primary investment emphasis must be placed upon the consistent protection of the funds assets and growth performance, i.e., the achievement of adequate investment growth must not be at the expense of the protection of the assets over the investment horizon.

More specific investment objectives established by the City include the following:

- *The Fund should earn a return over time exceeding the assumed actuarial rate of 9.0%. In addition, the Fund should earn a return greater than inflation, as measured by the Consumer Price Index, by 5.5% per year. Meeting this objective indicates that the active management of the various portfolio components has added value over a passively managed fund. It is also consistent with the City's objective to enhance the purchasing power of the Fund.*
- *Individual investment managers will not be measured against the aggregate fund objective stated above. They will be compared to appropriate market indices, and the performance of other managers who utilize a similar investment style.*

III. TRADITIONAL ASSET CLASSES - INVESTMENT GUIDELINES

A. Liquidity Requirements

There is a requirement to maintain liquid reserves for the payment of medical benefits and expenses. The City will review these projected cash flow requirements at least annually.

B. Equities

The investment manager(s) are permitted to invest in equity securities (including convertible bonds) listed on the New York, American and principal regional and foreign (for foreign securities) exchanges. They may also invest in over-the-counter securities for which there is an active market maker regulated by the NASD. Any investment that does not fall into a category listed above is prohibited.

The equity portion of each portfolio manager shall not

- 1. Be more than 10% invested in the securities of any one company at market.*
- 2. Make short sales.*
- 3. Use margin or leverage.*
- 4. Be invested in commodities.*
- 5. Be invested in private real estate.*
- 6. Be invested in "investment art objects."*
- 7. Invest in Options, including the purchase, sale or writing of options unless options are "covered" by the corresponding security.*
- 8. Be invested in warrants, although warrants issued in connection with stocks held by the fund may be sold, held, or converted by the investment manager at its discretion.*

a) Large –Capitalization Value & Growth Stocks

Large capitalization stocks are expected to have the greatest weighting in the Insurance Trust Fund. They are expected to provide more consistent returns over time than our other equity styles. The objective is to maximize investment return over a market cycle by investing in large capitalization equities having the

potential to generate investment returns exceeding those of a passively managed large stock index.

Large-capitalization equity manager performance parameters include the following:

- Performance within the top half of a Universe of Large Capitalization Value or Growth Managers.*
- Performance that exceeds the Russell 1000 Value or Russell 1000 Growth Indexes ~~by 200 basis points.~~*
- Performance that exceeds the S&P 500 Stock Index (Market & Equal-Weighted) ~~by 200 basis points.~~*
- The risk associated with the manager's portfolio as measured by the variability of quarterly returns (standard deviation) should not exceed that of the ~~appropriate index market (S&P 500 Index)~~ without a corresponding increase in performance above the index*
- Achieve the performance parameters within a time horizon of a minimum of three to five years or a full market cycle*

b) Mid/Small Capitalization Stocks

Mid/Small capitalization stocks are expected to improve total portfolio diversification and provide opportunities for higher incremental returns in the long run. The objective is to maximize investment return over a market cycle by investing in mid/small capitalization equities having the potential to generate investment returns exceeding those of a passively managed mid/small stock index. ~~Mid/Small capitalization stock managers generally purchase companies with a market capitalization of greater than \$500 million~~

Mid/Small capitalization equity manager performance parameters include the following:

- Performance within the top half of a Universe of Mid/Small Capitalization Core/Value or Growth Managers*
- Performance that exceeds the Russell 2000 or Russell 2500 Growth Indexes ~~by 200 basis points~~*
- ~~The risk associated with the manager's portfolio as measured by the variability of quarterly returns (standard deviation) should not exceed that of~~*

the appropriate index without a corresponding increase in performance above the index.

- *Achieve the performance parameters within a time horizon of a minimum of three to five years or a full market cycle for the mid/small capitalization market*

c) *Developed International Stocks*

Developed International Stocks are expected to improve total portfolio diversification and provide opportunities for higher incremental returns in the long run. The objective is to maximize investment return over a market cycle by investing in international securities through American Depository Receipts (ADRs). These equities should generate investment returns exceeding those of a passively managed international index.

Developed international equity manager performance parameters include the following:

- *Exceed MSCI EAFE – Net Dividend or MSCI All Country World ex. USA ~~MSCI EAFE (GDP) – Gross Dividend Indexes~~ by 200 basis points.*
- *The risk associated with the manager's portfolio as measured by the variability of quarterly returns (standard deviation) should not exceed that of the appropriate index without a corresponding increase in performance above the index.*
- *Achieve the performance parameters within a time horizon of a minimum of three to five years or a full market cycle of the international market*
- *Emerging Markets exposure is limited to 20% of the developed international equity portfolio*

d.) *Emerging Markets Stocks*

Emerging Markets Stocks are invested in countries with higher growth rates and therefore are expected to offer higher returns with higher volatility. The objective is to maximize investment return over a market cycle by investing in emerging markets securities through American Depository Receipts (ADRs) and Global Depository Receipts (GDRs). The managers are permitted to invest in closed-end country funds and exchange traded funds. These equities should generate investment returns exceeding those of a passively managed emerging markets index.

Emerging markets equity manager performance parameters include the following:

- *Exceed MSCI Emerging Markets (Gross) Index.*
- *The risk associated with the manager's portfolio as measured by the variability of quarterly returns (standard deviation) should not exceed that of the appropriate index without a corresponding increase in performance above the index.*
- *Achieve the performance parameters within a time horizon of a minimum of three to five years or a full market cycle of the emerging markets.*
- *Achieve the performance parameters within a time horizon of a minimum of three to five years or a full market cycle of the emerging markets.*

C. Fixed Income

Fixed income securities shall be invested entirely in marketable debt securities issued or guaranteed by either (a) the United States Government or its agencies, (b) domestic corporations (including industrial and utilities) (c) domestic banks and other US financial institutions. All securities must hold an investment grade rating by a major rating service. Any investments that do not fall under the criteria listed above are prohibited from being purchased. Securities ratings reduced beneath the three highest classifications after purchase should be sold by the portfolio manager within a reasonable period of time as determined by the manager. It is the manager's responsibility to notify the City in writing immediately after a security is downgraded below the policy guidelines. The written explanation should describe the manager's intentions regarding the disposition of the security being downgraded. Restrictions on fixed income include the following:

- 1 *Except for Treasury and Agency obligations, the debt portion of the Fund shall contain no more than ten percent (10%) of a given issuer irrespective of the number of differing issues. Other diversification standards should be developed and applied by the Investment Manager(s).*
- 2 *If commercial paper is used it must be only of the highest quality (A-1 or P-1)*
- 3 *Private placement debt is not permissible.*

Fixed income manager(s) performance parameters include the following.

- *Performance on a risk-adjusted basis that exceeds the Lehman Brothers Intermediate ~~Government/Credit~~ Aggregate Bond Index (LB Int AGG ~~G/C~~) by 50 basis points.*
- *Achieve the above objectives within a time horizon of a minimum of three to five years or a full market cycle.*

III. ALTERNATIVE ASSET CLASSES - INVESTMENT GUIDELINES

Alternative asset classes historically have low to moderate correlation to market indices. Alternative asset classes are expected to improve total portfolio diversification and provide opportunities for higher incremental returns over the long-term. Many of the asset categories are expected to generate absolute returns (positive returns regardless of market environment) versus relative returns (returns comparative to a given benchmark).

Alternative asset classes guidelines differ from traditional asset classes guidelines. Alternative asset managers may use leverage and derivatives, may short securities, generally have higher fees, typically have reduced liquidity, and performance is dependent primarily on advisor skill.

A. Real Estate

Real Estate Investment Trusts (REITs)

The investment managers are permitted to invest in real estate investment trusts (REITs) listed on the New York, American and principal regional and foreign (for foreign securities) exchanges. They may also invest in over-the-counter securities for which there is an active market maker regulated by the National Association of Securities Dealers (NASD).

Private Real Estate

The investment managers are permitted to invest in private real estate. Private real estate will be purchased through an institutional vehicle. The institutional vehicle provides diversification of property type and geographical location and provides a competitive price structure.

a.) Real Estate Investment Trusts (REITs)

Real Estate Investment Trust securities are expected to improve total portfolio diversification and provide opportunities for higher incremental returns in the long-term. The objective is to maximize investment return over a market cycle by investment in real estate through REITs. These equities should generate investment returns exceeding those of a passively managed REIT index.

REIT equity manager performance parameters include the following:

- Exceed National Association of Real Estate Investment Trusts (NAREIT) Equity REIT Index.
- The risk associated with the manager's portfolio as measured by the variability of quarterly returns (standard deviation) must not exceed that of the NAREIT

Equity REIT Index without a corresponding increase in performance above the index.

- Achieve the performance parameters within a time horizon of a minimum of three to five years or a full market cycle of the REIT market.

b) Private Real Estate

Private real estate investments are expected to improve total portfolio diversification and provide income and opportunities for higher incremental returns in the long-term. The objective is to maximize investment return over a market cycle by investment in real estate through private ownership. These private real estate investments should generate investment returns exceeding those of a passively managed private real estate index.

Private real estate investment performance parameters include the following:

- Exceed the National Council of Real Estate Investment Fiduciaries (NCREIF) Index.
- Performance comparable to the Lehman Brothers Aggregate Bond Index
- The risk associated with the manager's portfolio as measured by the variability of quarterly returns (standard deviation) must not exceed that of the NCREIF Index or the Lehman Brothers Aggregate Bond Index without a corresponding increase in performance above the index.
- Achieve the above objectives within a time horizon of five to ten years or a full real estate market cycle.

B. Funds of Hedge Funds (FofHFs)

FofHFs are private investment funds investing primarily in the global equity and fixed income markets typically employing sophisticated trading strategies using leverage and derivative instruments. FofHFs invests in multiple, single manager hedge funds. The strategy designs a diversified portfolio of managers with the objective of significantly lowering the risk (volatility) of investing with an individual manager. The FofHFs manager has discretion in choosing which strategy to invest in for the portfolio. A manager may allocate funds to numerous managers within a single strategy, or with numerous managers in multiples strategies. The investor has the advantage of diversification among managers and styles with significantly less capital than investing with separate managers.

Low Volatility Funds of Hedge Funds (LVFofHFs)

The LVFofHFs manager selects hedge fund investment managers that invest in Relative Value Arbitrage/ Event Driven asset classes. Relative Value Arbitrage/ Event Driven asset class categories consists of hedge fund managers specializing in Convertible Arbitrage, Fixed Income Arbitrage, Distressed, Statistical Arbitrage, and Equity Market Neutral Strategies.

Mid to High Volatility Funds of Hedge Funds (MHVofHFs)

The MHVofHFs manager selects hedges fund investment managers that invest in Long/ Short, Global Macro/ Managed Futures, and Manager Futures asset classes.

a) ***Low Volatility Funds of Hedge Funds (LVFofHFs)***

LVFofHFs are expected to improve total portfolio diversification and provide opportunities to achieve higher incremental returns in the long-term. The objective is to provide absolute returns over a market cycle. The standard deviation for the combination of hedge fund managers' strategies are expected to have return volatility in the range of 2-5% over a market cycle.

LVFofHFs manager performance parameters include the following:

- Exceed Hedge Fund Research, Inc. Fund of Funds Conservative Index (HFRI FOF Conservative Index)
- The risk associated with the manager's portfolio as measured by the variability of quarterly returns (standard deviation) must not exceed that of the HFRI FOF Conservative Index without a corresponding increase in performance above the index.
- Achieve the performance parameters within a time horizon of a minimum of three to five years or a full market cycle.
- Compare to the Lehman US Aggregate Bond Index for return and risk over a time horizon of three to five years or a full market cycle.

b.) Mid to High Volatility Funds of Hedge Funds (MHVFofHFs)

MHVfHFs are expected to improve total portfolio diversification and provide opportunities to achieve higher incremental returns in the long-term. The objective is to provide absolute returns over a market cycle. The standard deviation for the combination of hedge fund managers strategies are expected to have return volatility in the range of 5-15% over a market cycle.

MHVfHFs manager performance parameters include the following:

- Exceed appropriate Hedge Fund Research, Inc. Fund of Funds Index
- The risk associated with the manager's portfolio as measured by the variability of quarterly returns (standard deviation) must not exceed that of the appropriate HFRI FOF without a corresponding increase in performance above the index.
- Achieve the performance parameters within a time horizon of a minimum of three to five years or a full market cycle.

IV D. REVIEW OF INVESTMENT MANAGERS

The City will meet quarterly with the consultants. Additionally, the City will review investment results monthly.

These reviews will focus on:

- *the managers' adherence to the policy guidelines;*
- *comparison of managers' results against funds using similar policies (in terms of the diversification, volatility, style, etc.),*
- *the opportunities available in both equity and debt markets; and*
- *material changes in the managers' organizations, such as philosophical and personnel changes, acquisitions or losses of major accounts, etc.*

VE. PERFORMANCE EXPECTATIONS

The most important performance expectation is the achievement of investment results that are consistent with the Plan's investment policy statement. A 5.5% real return is a reasonable expectation in light of this policy. The City recognizes that this real return objective may not be attainable during some time periods, it is a long term goal. In order to ensure that investment opportunities available over a specific time period are fairly evaluated, the City will use comparative performance statistics to evaluate investment results. Performance of the Plan will be compared to other funds utilizing a similar investment policy.

VI F. Policy Review

Periodic reviews of the Policy Statement will be made by the City to evaluate its appropriateness. Any modification of policy guidelines shall be approved by the City and acknowledged in writing by the investment managers.

Adopted _____ Signed _____
Date Finance Director

Investment Manager's Acknowledgment

I, the undersigned, acknowledge that I have received the policy statement for City of Gainesville Disability Pension Fund, dated _____ . I affirm that I have read and understand said Policy Statement, and do hereby agree to abide to the guidelines expressed in the Policy Statement

Name of Firm

Signed

Date