

**REGULAR MEETING OF THE RETIREMENT BOARD OF ADMINISTRATION  
WATER AND POWER EMPLOYEES' RETIREMENT PLAN**

**MINUTES**

**JANUARY 27, 2010**

**Board Members Present:**

Javier Romero, President  
Cindy Coffin, Vice President  
Barry Poole, Board Member  
Michael Moore, Retiree Member  
Jeff Peltola, Board Member  
S. David Freeman, Interim General Manager

**Board Members Absent:**

Appointed DWP Commissioner - Vacant

**Staff Present:**

Sangeeta Bhatia, Retirement Plan Manager  
Mary Higgins, Assistant Retirement Plan Mgr.  
Jeremy Wolfson, Chief Investment Officer  
Julie Escudero, Utility Executive Secretary

**Others Present:**

Alan Manning, Assistant City Attorney  
Mike Wilkinson, Deputy City Attorney  
Neil Rue, Pension Consulting Alliance  
Sarah Bernstein, Pension Consulting Alliance

President Romero called the meeting to order at 10:04 a.m. following the Pledge of Allegiance.

Ms. Bhatia indicated a quorum of the Board was present.

**Public Comments**

No public comments were received.

- 1. Request for Approval of October 28, 2009, Audit Committee Meeting Minutes**
- 2. Request for Approval of December 16, 2009, Special Board Meeting Minutes**
- 3. Termination from Rolls**
  - Termination from January 2010 Retirement Roll**
  - Termination of Caroline S. Brown from the January 2010 Survivorship Roll-Deceased**

Mr. Moore asked that the third line of the first paragraph on page 1.2 of Item 1 (October 28, 2009, Audit Minutes) be amended to read as follows:

*"...indicated the actuarial valuation of the Retiree Health Benefit Fund used for the audit was provided by Financial Services because the Retirement Board does not have the oversight of that contract."*

*Mr. Moore moved for approval of Consent Items 1 through 3 as amended; seconded by Ms. Coffin and carried unanimously after the following vote:*

*Ayes: Romero, Coffin, Poole, Moore, and Freeman  
Nays: None*

**4. Notice of Deaths for December 2009**

5. a) **Summary of Investment Returns as of December 31, 2009**
- b) **Market Value of Investments by Fund and Month as of December 31, 2009**
- c) **Market Value of the Retirement, Death, and Disability Funds and Retiree Health Care Fund as of December 31, 2009**

**6. Report on Status of Insurance as of December 31, 2009**

**7. Report on Organizational Changes at Fred Alger Asset Management Company**

*Mr. Moore moved for approval Items 4 through 7 as Received and Filed; seconded by Ms. Coffin and carried unanimously after the following vote:*

*Ayes: Romero, Coffin, Poole, Moore, and Freeman  
Nays: None*

*(Mr. Peltola joined the meeting at 10:06 a.m.)*

**8. Presentation by Courtland Partners, Ltd. – Third Quarter 2009 Real Estate Portfolio Performance**

Mr. Romero acknowledged Lourdes Canlas and Jacinta deRivera from Courtland Partners.

Ms. Canlas provided a brief introduction of their presentation. Mr. Freeman suggested that instead of reviewing the presentation material that had been provided to the Board, the Board Members might be more interested in discussing whether the Board should try to recoup its losses in this sector or divest. Mr. Moore added he was interested in having that discussion.

Garrett Zdolshek, Managing Director of Courtland's Cleveland Office, addressed Mr. Freeman's concerns. Mr. Zdolshek began by reviewing the market conditions and the increased foreclosure activity. Ms. Canlas pointed out the continued increase in foreclosures affected consumer spending and employment which negatively impacted the Plan's portfolio. Mr. Zdolshek explained the characteristics of cap rates. He stated the cap rates bottomed-out at approximately 5%-6% at the market's peak in 2008, and then had begun to rise. He said he believed they will continue to increase and value will continue to decline.

Ms. Canlas stated the Plan has invested 35% of its real estate portfolio in the West which has experienced a high foreclosure rate and has affected the portfolio.

Mr. Freeman asked if it would be wiser to sell considering the market conditions or invest more to take advantage of the situation. Mr. Zdolshek stated he believed the time was right to reassess the Plan's portfolio which, he believed, could yield 8% or 9% in returns in the next few years compared to the current yield of 6% based on the market value of the portfolio. He stated the portfolio was in a better range historically than in past years and he believed it was a good time to increase the portfolio's real estate holdings from the current one percent to five percent over the next few years.

Ms. Coffin asked if investors were trying to divest. Ms. Canlas responded that three open-ended funds have investors queued to sell and she explained the various reasons. She added that ample opportunities exist for investors with available capital, which was one reason Courtland was recommending the Board invest in a Value-Add Fund, Bristol Value Fund II, scheduled for discussion later in the meeting.

Mr. Freeman expressed his concern with the feasibility of earning an eight percent return rate and asked if that figure was conservative enough.

Ms. Higgins stated the Plan's actuary is currently conducting a three-year experience study, and the eight percent assumption rate is part of that study which will be presented to the Board at a future meeting.

Discussion ensued regarding risk and asset allocation

Mr. Zdolshek indicated Courtland is reviewing open-ended funds and Core investment opportunities and will be providing recommendations to the Board in the near future.

Ms. Bhatia added an overview of the asset allocation study is scheduled for the next meeting.

#### **9. Presentation by Courtland Partners, Ltd. – Investment Opportunity in Bristol Value II Fund**

Mr. Zdolshek introduced this item and indicated Courtland Partners was recommending the Board consider allocating \$25 million to Bristol Value Fund II.

Jeffery Kott, managing director from Bristol Group, Inc. (Bristol), reviewed Bristol's background and performance. He explained they engage in off-market transactions at a substantial discount, and reposition and redevelop the properties to create strong cash flows.

Mr. Kott reviewed some of Bristol's transactions in Southern California.

Mr. Peltola asked what investment opportunities were available. Mr. Kott stated pension fund advisors were now selling some of their best assets at a substantial discount. In response to Mr. Peltola's question regarding the cash return if the economy does not recover, Mr. Kott indicated he believed buying at an eight to nine percent unleveraged return and adding moderate leverage would result in a decent cash return even if rents go down twenty percent. He said he believed the key was to buy low.

Mr. Freeman asked for the projected investment period for the \$25 million if the Board approved this recommendation. Mr. Kott estimated investing \$5 million this year and \$10 million in each of the next two years, but he added Bristol used a five-year investment period and they would only invest if they believed they would make a profit.

*Mr. Moore moved for approval of Courtland's recommendation to invest \$25 million in the Bristol Value II Fund; seconded by Mr. Freeman, and carried unanimously after the following vote:*

*Ayes: Romero, Coffin, Poole, Moore, Peltola, and Freeman*

*Nays: None*

#### **10. Discussion of Paradigm Asset Management Company's Performance**

Mr. Romero acknowledged Neil Rue from Pension Consulting Alliance, Inc. (PCA).

*(Mr. Peltola left the meeting at 11:17 a.m.)*

Mr. Rue reported Paradigm has performed poorly since inception, and the Board placed them on watch status in December 2008. He further stated that in October 2009, the Board had discussed terminating the contract with Paradigm but decided instead to extend their review period to determine if Paradigm's revised investment strategy would result in positive returns. Mr. Rue stated Paradigm continued to underperform, and in the last four to six months they exhibited no proof of improvement in their stock selection. Mr. Rue stated PCA was recommending terminating the contract with Paradigm and transferring the Plan's assets to Frontier Capital (Frontier).

Ms. Coffin asked why PCA was recommending terminating the contract now when it had only been three months since the Board decided to extend the review period. Mr. Rue explained the Board agreed to extend the review period to six months from the initial change in strategy which occurred in July 2009, and he added the six months was now up. In response to a question from Ms. Coffin, Mr. Wolfson indicated Frontier showed exceptional performance in their fourth quarter report. Ms. Coffin asked if the funds could be placed in an index fund, and Ms. Bhatia stated they could and that was an option noted in Staff's memo.

*(Mr. Peltola returned to the meeting at 11:21 a.m.)*

In response to questions from Ms. Coffin, Mr. Wolfson explained that Frontier has already submitted some of their insurance documents for final approval and their contract was nearing completion. He described the two approaches staff could take if the Board decided to transition the funds to Frontier prior to execution of their contract. He said the first approach, which would also have the lowest transition cost, would be for staff to halt trading with Paradigm and transition Paradigm's funds, plus the funds from the current passive account, to Frontier concurrently. He said if problems arose which caused delays in executing Frontier's contract, the other approach would be to move Paradigm's funds in the interim into the temporary passive account which currently holds the funds from NorthPointe, and then transfer them concurrently.

Mr. Freeman expressed his concern for where the money will be deposited upon termination of the contract. Ms. Bhatia explained to Mr. Freeman why Frontier was hired. She added that upon termination of the contract, a decision regarding the investments of those funds would need to be made.

Following considerable discussion among the Board Members, consultant, and staff, the following motion was made:

*Mr. Freeman moved for approval of the recommendation to terminate the contract with Paradigm Asset Management Company and transfer the funds from Paradigm to Frontier Capital on the condition that Frontier first signs the contract on the basis of our terms and conditions; seconded by Mr. Moore, and carried unanimously after the following vote:*

*Ayes: Romero, Coffin, Poole, Moore, Peltola, and Freeman  
Nays: None*

#### **11. Discussion of Western Asset Management Company's Global Investment-Linked Securities Investment Policy**

Mr. Wolfson gave the background for the item which asked for the Board to approve manager-specific investment guidelines for the Real Return Global Inflation-Linked Securities mandate

managed by Western Asset Management Company (WAMCO). He pointed out that it was industry practice to have specific investment policies for specific investment managers.

Neil Rue from PCA commented that the Plan currently has no manager specific guidelines but it might need to develop customized guidelines for each manager in the future to provide more flexibility. He added that in the case of WAMCO, they were now necessary given they manage a new mandate, and the current investment guidelines are too broad.

Mr. Rue reviewed the parameters of the updated guidelines.

*(Mr. Peltola left the meeting at 11:42 a.m.)*

Mr. Wolfson advised the Board that the targeted benchmark for the duration of portfolio security holdings should be plus or minus 30 percent ( $\pm 30\%$ ) and not “plus 30 percent” as shown on page 11.4 of staff’s report.

Mr. Moore asked for clarification of the diversification guideline that limited obligations of other national governments to 50 percent per issuer. Mr. Wolfson explained the figure was based on the United States benchmark of 40 percent. He stated limiting WAMCO to 50 percent in another country would give them flexibility to have a similar benchmark. Mr. Moore suggested the guideline be changed to reflect that the position of the United States securities be capped at 50 percent, but Mr. Rue explained that would limit WAMCO to be overweight the United States by only 10 percent and it would prevent WAMCO from investing more than 50 percent in the United States if that was ever their decision.

Mr. Moore asked why the aggregate of the active long currency exposure was limited to five percent of the portfolio, and Mr. Rue explained the mandate benchmark was hedged back to United States dollars and the overage could only be five percent. He further explained that any long bet would always have an offsetting short bet, and the reference to active exposure meant it was relative to the benchmark.

At the suggestion of Ms. Bhatia, Mr. Rue indicated a reference further explaining the limitation and the levels of exposure will be provided in the guidelines.

*(Mr. Peltola returned to the meeting at 11:48 a.m.)*

Mr. Moore stated WAMCO was not hired to trade currency and he stressed his concern that WAMCO might interpret the current language as a way to make money. He emphasized their mandate was to invest in TIPS and other inflation hedged securities and not to trade currency. He encouraged PCA to include an explanation as suggested by Ms. Bhatia.

*Mr. Freeman moved for approval of the resolution to adopt Western Asset Management Company’s Global Inflation-Linked Securities investment policy upon clarification of the language pertaining to the limit for the aggregate of active long currency exposures; seconded by Mr. Poole, and carried unanimously after the following vote:*

*Ayes: Romero, Coffin, Poole, Moore, Peltola, and Freeman  
Nays: None*

## **12. Discussion of Revisions to Investment Policy Relating to 144a Securities in the Death and Disability Investment Portfolios Managed by Wells Capital**

Ms. Bhatia provided background for this item which concerns revisions to the investment policy as requested by Wells Capital (Wells). She explained Wells is currently permitted to invest Death and Disability Funds in Rule 144A Securities without registration rights but only up to two percent of the fund's market value at the time of purchase. She stated Wells has indicated they are no longer able to hold up to two percent because of the nature of the market and they have requested they be allowed to invest up to ten percent of the market value in Rule 144A Securities with and without registration rights. Ms. Bhatia stated PCA has recommended the Board approve the change which they believe will have no significant impact to the Fund; however, she indicated staff was concerned that the change would alter the intended risk profile of the fund. She explained staff has no immediate alternative at this time; therefore, staff has proposed the Board approve the resolution for now while staff continues to monitor the change and explore viable alternative options which they will present to the Board, if necessary.

*Mr. Freeman moved for approval of the revision to the investment policy relating to 144A Securities in the Death and Disability Investment Portfolios managed by Wells Capital; seconded by Mr. Moore, and carried unanimously after the following vote:*

*Ayes: Romero, Coffin, Poole, Moore, Peltola, and Freeman  
Nays: None*

## **13. Discussion of Request to Extend the Holding Period of Debt to Equity Conversion for the Wells Capital High Yield Portfolio**

Mr. Wolfson provided background for this item which concerns a request from Wells Capital to extend the holding period for 2,500 shares of equity in the Tropicana Hotel and Casino which they received as a debt-to-equity conversion as part of a bankruptcy restructuring. He stated the current investment policy allows for a fixed income manager to hold this type of equity for a maximum of six months, but Wells indicated it will take approximately five additional months to liquidate the shares.

*Mr. Moore moved for approval to extend the holding period of debt to equity conversion for the Wells Capital High Yield Portfolio; seconded by Ms. Coffin, and carried unanimously after the following vote:*

*Ayes: Romero, Coffin, Poole, Moore, Peltola, and Freeman  
Nays: None*

## **14. Discussion of Recommendation to Place Wells Capital Core Fixed Income Manager on Organizational Watch**

Mr. Wolfson provided background on this item which recommends that Wells Capital Core Fixed Income Manager be placed on watch status due to recent significant organizational changes.

*Mr. Moore moved that Wells Capital Core Fixed Income Manager be placed on organizational watch, seconded by Ms. Coffin, and carried unanimously after the following vote:*

*Ayes: Romero, Coffin, Poole, Moore, Peltola, and Freeman*  
*Nays: None*

**15. Discussion of Recommendation to Place Wells Capital High Yield Fixed Income Manager Performance Watch**

Mr. Wolfson provided background for this item which recommends that Wells Capital Sutter High Yield Team be placed on watch status for not meeting the WPERP short-term investment performance criteria for the quarter ending December 31, 2009.

*Mr. Moore moved that Wells Capital High Yield Fixed Income Manager be placed on performance watch; seconded by Ms. Coffin, and carried unanimously after the following vote:*

*Ayes: Romero, Coffin, Poole, Moore, Peltola, and Freeman*  
*Nays: None*

**16. Discussion of Update on Governance Issues**

Ms. Bhatia stated this item had been brought back to the Board to discuss the update from the City Attorney's Office concerning the authority of the Retirement Board.

Assistant City Attorney Alan Manning reported he and Deputy City Attorney Mike Wilkinson recently met with Pete Echeverria, the head of the Civil Division of the City Attorney's Office. He indicated that Mr. Echeverria was waiting to receive a memorandum from the City Attorney assigned to DWP to help him resolve this issue. Mr. Manning added that Mr. Echeverria was aware of the importance of the issues raised by the Retirement Board Members.

Mr. Freeman expressed his concern for the difference of opinion.

Mr. Peltola stated the three requested positions in the Retirement Office budget were now approved. Ms. Coffin responded that the more pressing issue was the determination of the Retirement Board's authority.

Discussion ensued with no resolution to this item. President Romero requested this item continue to be placed on future agendas until it is resolved. He requested the City Attorney update the Board at the next meeting.

**17. Discussion of Plan Amendments Required to Maintain the Plan's Tax Qualified Status**

Ms. Higgins indicated this item concerned amending the Retirement Plan to include technical legislative requirements necessary to maintain the Plan's tax qualified status. She indicated the deadline for the Board to adopt the proposed Plan amendment was the end of April 2010. She indicated the Plan amendment also needed to be approved by the DWP Board of Commissioners and then brought back to the Retirement Board for final adoption.

In response to a question from Mr. Romero, Ms. Higgins clarified the technical changes were only necessary for the Plan's tax qualified status and did not include any meet and confer items.

## **Out of Order (Item 16 continued)**

*Mr. Freeman requested it be noted that he dissented from the Board's insistence to pursue a City Attorney opinion regarding the governance issue concerning the Retirement Board's authority.*

## **Item 17 – continued**

Mr. Moore asked about the possible impact on retirees. Ms. Higgins indicated very few people would be affected. She added no one would be directly affected by the 415 limits because the Plan includes a companion piece called the Excess Benefit Plan which provides for the Department to pay the amount a retiree is entitled to beyond what the Plan can provide. She indicated there is a potential impact to the Department but none to the retirees. She added that because of "grandfather" provisions, there would be very little immediate impact from either the 415 or 401(a)(17) limits on retirees or people soon to retire or to the Plan sponsor. She indicated staff is conducting a full audit on this and will report back to the Board at a later date.

Ms. Bhatia added she and Ms. Higgins met with Mr. Peltola and Michele Nagin to discuss the IRS requirements, specifically the Excess Benefits Plan. She stated they are in the process of determining exactly who is impacted, and as of now, no one has been instructed to be reimbursed by the Excess Benefits Plan but that it is up to the Plan to work out with the Department.

*Mr. Moore moved to amend the Water and Power Employees' Retirement Plan to incorporate required legislative and regulatory provisions; seconded by Ms. Coffin, and carried unanimously after the following vote:*

*Ayes: Romero, Coffin, Poole, Moore, Peltola, and Freeman*

*Nays: None*

## **18. Retirement Plan Manager's Comments**

Ms. Bhatia reported that Mr. Peltola requested the Retirement Office staff make a presentation to the DWP Board of Commissioners' Investment Committee regarding the Plan's asset allocation process. She indicated the presentation was scheduled for the following week. She stated testing continues on the Retirement, Disability and Death Benefit module of the PenFax system, which should be in place in a few weeks. She said the module calculates retirement estimates. Ms. Bhatia reported on the insurance status for the pending investment manager contracts.

Ms. Bhatia noted Alan Manning would provide an update on the Lexin case, and copies of his memo were distributed to the Board Members at the beginning of the meeting. Mr. Manning stated the California Supreme Court dismissed charges against five of the six San Diego pension board members who had been charged with violating state conflict of interest laws. He explained the intermediate Appellate Court had established rules that would have made it difficult for trustees who were members of retirement systems to perform their job without exposing themselves to violation of conflict of interest laws. He stated the Supreme Court ruling reversed the earlier Appellate Court decision. He added the City Attorney's Office will continue to answer questions and provide training regarding conflict of interest.


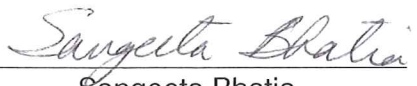



**19. Future Agenda Items**

Mr. Moore requested an item to discuss how the Board should monitor legislation and how to proceed if the Board wants to take a position on a legislative matter.

Mr. Romero asked for further discussion of reciprocity.

The meeting adjourned at 12:33 p.m.

 _____ Javier Romero Board President	<u>3/10/10</u> Date	 _____ Sangeeta Bhatia Retirement Plan Manager	<u>3/10/10</u> Date
 _____ Julie Escudero Utility Executive Secretary	<u>3-10-10</u> Date		