

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

MINUTES

DECEMBER 14, 2011

Board Members Present:

Javier Romero, President
Cindy Coffin, Vice President
Mario Ignacio, Chief Accounting Employee
Barry Poole, Regular Member
Robert Rozanski, Retiree Member

Board Members Absent:

DWP Commissioner - Vacant
Ronald O. Nichols, General Manager

Staff Present:

Monette Carranceja, Assistant Retirement Plan Manager
Mary Higgins, Assistant Retirement Plan Manager
Jeremy Wolfson, Chief Investment Officer
Julie Escudero, Utility Executive Secretary

Others Present:

Marie McTeague, Deputy City Attorney

President Romero called the meeting to order at 9:36 a.m.

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

Public Comments

Ms. Escudero reported no Public Comments were received.

Mr. Romero introduced new employee Erin Carone, Senior Clerk Typist in the Retirement Office Administration Section.

1. Request for Approval of Minutes:

- a) **September 28, 2011, Regular Meeting**
- b) **October 12, 2011, Regular Meeting**

2. Termination from Rolls

- a) **Termination of Monthly Allowance from the November 2011 Retirement Roll**
- b) **Termination of Monthly Allowance from the December 2011 Retirement Roll**

Mr. Rozanski moved that the Board approve Items 1 and 2: seconded by Ms. Coffin.

Ayes: Coffin, Ignacio, Poole, Romero, and Rozanski

Nays: None

Absent: Nichols

THE MOTION CARRIED.

3. Report of Payment Authorizations

- a) **October 2011**
- b) **November 2011**

4. Notice of Deaths

- a) **October 2011**
- b) **November 2011**

5. **Investment Reports for October 2011**
 - a) **Summary of Investment Returns as of October 31, 2011**
 - b) **Market Value of Investments by Fund and Month as of October 31, 2011**
 - c) **Market Value of the Retirement, Death, and Disability Funds and Retiree Health Care Fund as of October 31, 2011**
 - d) **Summary of Contract Expirations**
6. **Report on Status of Insurance as of November 9, 2011**
7. **Report on Bond Holding in the Wells Capital Management Sutter High Yield Portfolio**

Mr. Rozanski moved that the Board accept Received and Filed Items 3 through 7; seconded by Ms. Coffin.

*Ayes: Coffin, Ignacio, Poole, Romero, and Rozanski
Nays: None
Absent: Nichols*

THE MOTION CARRIED.

8. Discussion of Retirement Office Budget for Fiscal Year 2012-2013

Ms. Higgins reported the Retirement Office budget is being presented earlier than usual this year because the Department was requested to follow the City's budget calendar.

Ms. Carranceja reviewed the highlights of the Retirement Office 2012-2013 budget. She reported the overall budget increased by \$500,000 from last year's budget of \$32.5 million to \$33 million, primarily due to the \$1 million increase in investment fees. She emphasized that even with the increase in investment fees, the Retirement Office budget reflects a decrease in operating expenses from \$2.68 million to \$2.2 million. She reported the staffing levels in the 2012-2013 Annual Personnel Resolution (APR) maintain the 2011-2012 staff levels at 59 budgeted positions. She noted the attached resolution approves the budget, authorizes expenditures, and authorizes employment in accordance with the APR.

Ms. Higgins mentioned efficiencies implemented in the Retirement Office contributed to some of the decreases in the administrative budget.

Mr. Rozanski asked if the proposed three-year smoothing schedule would affect the Department's contributions. Ms. Higgins responded that because changes are implemented mid-year, some impact may occur halfway through 2012-2013.

Mr. Rozanski asked if an amendment would be presented to the Board if any changes were made to this budget, and Ms. Higgins responded that the Board would have to take an official action to change the budget that it adopts.

Mr. Rozanski moved that the Board approve Resolution No. 12-40 adopting the Retirement Office Budget and APR for FY 2012-2013; seconded by Ms. Coffin.

*Ayes: Coffin, Ignacio, Poole, Romero, and Rozanski
Nays: None
Absent: Nichols*

THE MOTION CARRIED.

9. Discussion of the Presentation by Simpson & Simpson, CPAs, of the Annual Audit Report and Related Financial Statements, as of June 30, 2011, as Discussed at the December 14, 2011, Audit Committee Meeting

Ms. Carranceja reported the Retirement Plan's CPA, Simpson and Simpson, presented the Audit Report and the Related Financial Statements at the December 14, 2011, Audit Committee meeting held earlier, and no material findings were presented.

Mr. Poole added that at the Audit Committee meeting, Simpson and Simpson touched on the 40% excise tax that is imbedded into the new health care law. He noted that clarification is needed on whether the 40% tax on retiree benefits is above the \$11,850 threshold or on the entire retiree health benefit. He stated the request for clarification has not yet been made, but information will be provided to the retirees when it becomes available. Ms. Higgins suggested this item can be discussed in January when The Segal Company presents the Death and Disability Valuations.

Mr. Poole asked Ms. Higgins for information on the necessary refinement of the PenFax system that was previously reported. Ms. Higgins responded the issue involves service credit, and Staff is working on data clean-up involving conversion issues and issues related to data that was in the legacy system. She indicated that because of staffing issues, Staff is performing the data clean-up whenever possible. She emphasized that no one is being paid improperly, and the actuary had indicated this had no material impact on the liabilities that have been estimated for the Fund.

In response to a question from Ms. Coffin, Ms. Higgins said currently Benefits Specialists and Management Analysts are conducting the data clean-up. She added that because of staff shortages and the inability to fill vacancies, management does offer overtime to perform the data cleanup.

10. Discussion of Guidelines for the Election of Active Member Representatives to the Retirement Board

Mr. Rozanski moved that the Board approve Resolution No. 12-41 to adopt the guidelines for the election of the active members' representatives to the Retirement Board; seconded by Ms. Coffin.

Ayes: Coffin, Ignacio, Poole, Romero, and Rozanski

Nays: None

Absent: Nichols

THE MOTION CARRIED.

11. Presentation by Courtland Partners on Potential Real Estate Investment Opportunities

a) Almanac Realty Securities VI, L.P.

b) AG Core Plus Realty Fund III, L.P.

The Board acknowledged Michael Humphrey and Bill Foster from Courtland Partners (Courtland).

Mr. Humphrey reported Courtland was presenting two Value Add real estate investment opportunities; Almanac Realty Securities VI, L.P., and AG Core Plus Realty Fund III, L.P., and that Courtland was recommending the Board invest \$20 million in each. He stated Courtland's recommended Value Add real estate allocation for 2011 was \$10 million short of their \$26.5 million goal. That amount, coupled with their recommended Value Add real estate allocation for 2012 of \$25 million, totaled \$35 million. He stated Courtland was recommending a combined total of \$40 million here because of the current

market conditions, and because both of the recommended funds focus on net returns of between 12% to 14%, with a significant component of those returns coming from income.

Mr. Foster commented on the pros and cons of each manager . He said one reason they are recommending both managers is they complement each other. On the risk side, he stated both funds can take on higher leverage than Core opportunities, and both rely highly on key personnel.

a) Almanac Realty Securities VI, L.P.

The Board acknowledged John Ryan, Managing Director from Almanac Realty Securities VI, L.P. (Almanac). Mr. Ryan explained Almanac makes private placements into real estate companies and provides growth capital to public and private real estate companies. He stated they are very conservative, their investments are typically structured as convertible debt or convertible preferred securities, and they focus on underwritable cash flow.

He reviewed Almanac's philosophy, management team, total return comparison, investment objectives, and investment approach for Fund VI. He indicated they have targeted the total net return for Fund VI at an unlevered 12% possibly higher, and they look to generate at least one half of their total net return from current cash flow. He stated they maintain positions on the Board of Directors of their investments which provides control on how their funds are deployed.

Mr. Romero asked Mr. Ryan if Almanac's fees are negotiable. Mr. Ryan indicated their management fees have already been reduced with no other fees associated.

b) AG Core Plus Realty Fund III, L.P.

The Board acknowledged Aliana Spungen and Adam Schwartz from Angelo, Gordon & Co. (AG Core). Ms. Spungen provided a brief overview of the company. She stated the bulk of their assets is in real estate and credit, and all of their ownership is held by their employees.

Mr. Schwartz reviewed AG Core's investment team and investment approach. He explained their Core Plus strategy is targeted to deliver between a 12% to 13% net return and their aim is to realize half of that return from current cash flow. He added they have a leverage target of approximately 55% to 65%, and their investments include senior mortgages where they can fund value.

He reviewed their gross performance and their fund-level track record. He stated they currently have seven property investments in Fund III that have either closed or are under contract to close, which represents approximately 20% of their targeted fund size of \$1 billion.

Ms. Spungen stated their management fee is 75 basis points on uncalled capital, 1.25% on net-funded capital, and their incentive fee is 15% subject to an 8% compounded preferred return with a 50% catch-up.

After the representatives from the two firms left the room, Retirement Office Staff and Courtland Staff provided a recap of the two presentations.

Mr. Rozanski moved that the Board approve Resolution No. 12-42 to invest \$20 million in Almanac Realty Securities VI, L.P.; seconded by Mr. Ignacio.

Ayes: Coffin, Ignacio, Poole, Romero, and Rozanski

Nays: None

Absent: Nichols

THE MOTION CARRIED.



Mr. Rozanski further moved that the Board approve Resolution No. 12-43 to invest \$20 million in AG Core Plus Realty Fund III, L.P.; seconded by Mr. Ignacio.

*Ayes: Coffin, Ignacio, Poole, Romero, and Rozanski
Nays: None
Absent: Nichols*

THE MOTION CARRIED.

13. Presentation by Pension Consulting Alliance – Real Return Structure Review (OUT OF ORDER)

The Board acknowledged Neil Rue from Pension Consulting Alliance, Inc. (PCA) who presented recommendations for strategic structural changes for the Real Return Asset Class.

He explained the current portfolio structure is benchmarked against the Consumer Price Index (CPI) plus 4% (CPI+4%) but they are recommending this be changed to CPI+3% to reduce equity-type risk.

He reviewed the four optional changes, all of which would bring an expected value for the Real Return class of approximately \$400 million.

He stated PCA is recommending Option 4 which would add a new complementary Hedge Fund Manager thereby increasing the number of Hedge Fund Managers (for the Absolute Return Strategy) back to two, with an increased allocation for each from approximately \$35 million to approximately \$50 million. He added both would be customized to provide stability in that segment of the portfolio. He stated Option 4 would also add new Commodities and Timber mandates.

Extensive discussion ensued regarding adding exposure to Timber and Commodities, particularly Timber.

Mr. Rozanski moved that the Board authorize Staff to move forward with Option 4; seconded by Mr. Poole.

*Ayes: Coffin, Ignacio, Poole, Romero, and Rozanski
Nays: None
Absent: Nichols*

THE MOTION CARRIED.

Mr. Rue stated they would make this contingent upon the opportunities in the Absolute Return space. Mr. Wolfson added Staff will come back with a memo summarizing the discussion as well as a formal resolution.

12. Presentation by Pension Consulting Alliance – Third Quarter Performance Review for Period Ending September 30, 2011 (OUT OF ORDER)

Neil Rue from Pension Consulting Alliance, Inc. (PCA) reviewed the summary statistics for the third quarter performance and reported the Retirement Portfolio was down 9% and the Health Plan Portfolio was down 8%. He stated the median results were basically the same.

He reported the year-to-date performance for the Retirement Portfolio was up approximately 1%, and the Health Plan Portfolio was up approximately 2%.

He stated the value of the portfolio at the beginning of the third quarter was \$7.4 billion and ended at \$6.7 billion. He added that a significant amount of the third quarter's downside results were recouped, and the portfolio ended in October 2011 at \$7.1 billion. He stated since that time, volatility has returned and the market has been flat.

In reviewing the performance attribution, he indicated the portfolio underperformed the policy for the 12-month trailing period 0.8% versus 1.3% as a result of the deviation of weights between the different classes. He also noted the weighting for Private Equity and Real Estate were lagged one quarter so the market volatility of the third quarter will be reflected in the next quarterly report.

14. Annual Presentation by Western Asset Management Company

The Board acknowledged Joseph Carieri and Paul Wynn from Western Asset Management Company (WAMCO).

Mr. Carieri reported no significant issues in terms of the organization. He noted WAMCO manages portfolios for both the Retirement Fund and the Health Care Fund and stated the focus of this presentation would be on the Retirement Fund.

Mr. Wynn reviewed the performance and discussed the market conditions. He noted they were unable to achieve much diversification because of low interest rates resulting from the turmoil in European markets, and they underperformed their benchmark for the year ended June 30, 2011, by approximately 2%. He added they have recovered over half of what they lost during the first nine months of their tenure and remain optimistic as they rebound.

15. Retirement Plan Manager's Comments

Ms. Higgins reported Staff is in the last phase of implementing the new system module that will replace the legacy retired member system (RAP). This portion of the new system prints the retirement checks. Staff is conducting data validation and preparing for the final conversion of the data.

She reported Staff will be meeting with the Department's budget manager tomorrow to discuss the budget that was presented to the Board earlier in this meeting; Staff will provide feedback at the next meeting.

She reported, as directed by the Board, Staff successfully negotiated the new fee structure for the contract extension with Wells Capital High Yield and, as a result of those renegotiations, the Plan expects to save approximately \$250,000 per year. She noted the Wells team was very cooperative.

Mr. Wolfson provided an update on the Vontobel contract which affects the portfolio transition. He stated the transition has been somewhat on hold because Staff has been monitoring the market volatility. He reported Staff had identified two finalists from the Plan's bench of transition managers and made a decision. Staff is monitoring the market and trying to get in line with the benchmarks as soon and as cost efficiently as possible. He stated because Vontobel is being opened as a separate account, Staff is required to open some countries not previously opened, and Staff continues to face challenges with opening some of these emerging markets countries. This has caused a delay in the funding. He stated the current emerging markets managers are still managing the funds. Once the Board hires the second manager through the Request for Proposal (RFP) process and Vontobel is able to be funded, we will have the appropriate exposure to emerging markets.

Mr. Romero asked for a summary of the evaluating criteria for the transition managers.

Mr. Wolfson reported that Staff is currently working on five pending RFPs. The RFPs for International Developed Core that is being moved to Core Passive, the International Relative Value Active, and the Emerging Markets were recently advertised. He stated the Covered Calls Manager interviews will be held in January, and the Board chose to keep the current High Yield Manager.

Ms. Higgins closed by saying that Sangeeta Bhatia conveyed to all her wishes for a Happy Holiday Season.

16. Future Agenda Items

None requested at this time.

Mr. Romero closed by wishing the Board a Merry Christmas and Happy New Year. On behalf of the Board, he thanked Staff for all of their hard work throughout the year and stated the Board appreciates their efforts.

With no further business, the meeting adjourned at 12:11 p.m.



Javier Romero
Board President

2/8/12
Date



Sangeeta Bhatia
Retirement Plan Manager

2/8/12
Date



Julie Escudero
Utility Executive Secretary

2.8.12
Date

