



Executive Staff:

Richard Stensrud
Chief Executive Officer

Steve Davis
Chief Investment Officer

Robert L. Gaumer
General Counsel

Kathryn T. Regalia
Chief Operations Officer

John W. Gobel, Sr.
Chief Benefits Officer

Members of the Board of Retirement

Rick Fowler, President
Appointed by the Board of Supervisors

John B. Kelly, Vice President
Appointed by the Board of Supervisors

Keith DeVore, Vice President
Appointed by the Board of Supervisors

Steven L. Baird
Elected by the Miscellaneous Members

Michael DeBord
Elected by the Retired Members

James A. Diepenbrock
Appointed by the Board of Supervisors

Diana Gin
Elected by the Miscellaneous Members

Ben Lamera
Ex Officio, Director of Finance

Chris A. Pittman
Elected by the Safety Members

John Conneally
Elected by the Safety Members

Martha J. Hoover
Elected by the Retired Members

MINUTES

RETIREMENT BOARD MEETING, WEDNESDAY, DECEMBER 21, 2016

A regular meeting of the Retirement Board was held in the Sacramento County Employees' Retirement System Administrative Office, 980 9th Street, 19th Floor, Sacramento, California, on Wednesday, December 21, 2016, and commenced at 10:04 a.m.

OPEN SESSION:

PUBLIC COMMENT:

1. Mr. Kelly read resolutions commending and honoring Mr. DeBord and Ms. Gin upon their departure from the SCERS Board and for their years of outstanding service to Sacramento County, SCERS, and its members and stakeholders.

Motion by Mr. Diepenbrock to adopt the resolutions honoring Mr. DeBord and Ms. Gin; Seconded by Mr. Pittman. Motion carried (7-0).

MINUTES:

2. The Minutes of the November 7, 2016 special meeting were approved on Motion by Mr. Diepenbrock; Seconded by Mr. DeBord. Motion carried (7-0).

CONSENT MATTERS:

Items 3-11

The Consent Matters were acted upon as one unit upon a Motion by Mr. Diepenbrock; Seconded by Mr. Baird. Motion carried (7-0), Mr. Diepenbrock abstained on Items 6 and 7.

3. GONZALEZ, Alfredo: Granted a service-connected disability retirement.
4. SAAR, Sheryl: Granted a reciprocal nonservice-connected disability retirement.
5. WATERS, Tammy: Granted a nonservice-connected disability retirement.
6. BAGLEY, Stella: Denied a service-connected disability retirement.
7. GREEN, Virginia: Denied a service-connected disability retirement, but granted a non-service connected disability retirement.
8. SCALES, Joanna: Denied a service-connected disability retirement.
9. Approved the proposed resolution approving changes to the SCERS Bylaws.
10. Received and filed the November 2016 Monthly Investment Portfolio Activity Report.
11. Received and filed the October 2016 and November 2016 Monthly Investment Manager Compliance Report and Watch List.

ADMINISTRATIVE MATTERS:

12. Chief Executive Officer Richard Stensrud provided an update on developments affecting public retirement systems and on miscellaneous system and staff activities.

Mr. Stensrud introduced Alan Matré who will be joining the Board of Retirement in January 2017 as a newly elected Miscellaneous Representative.

Mr. Stensrud also introduced Annette St. Urbain who has been hired by SCERS as a Special Assistant Administrator working on special projects. Mr. Stensrud noted that Ms. St. Urbain was previously the Chief Executive Officer of the San Joaquin County Employees' Retirement Association.

13. Richard A. Green and Leah Jue-Cochran of Macias Gini & O'Connell presented the Report to the Board of Retirement, the Report on Internal Controls and Compliance, and the Independent Auditor's Report for the Fiscal Years Ended June 30, 2016 and 2015.

ADMINISTRATIVE MATTERS (Continued):

Mr. Green noted that his firm provided three reports from their audit. Mr. Green first presented the Independent Auditor's Report, which is the auditor's opinion on the basic financial statements. Mr. Green then presented the Report on Internal Controls and Compliance.

Mr. Green stated that the audit showed no deficiencies, nor any instances of non-compliance with laws or regulations. Mr. Green stated that the audit produced an unqualified or 'clean' opinion on the basic financial statements. Mr. Green explained that this was the highest assurance possible on the state of the financial statements. Mr. Green further explained that this means that the financial statements were fairly presented in accordance with generally accepted accounting principles.

Ms. Jue-Cochran presented the Report to the Board of Retirement. Ms. Jue-Cochran reported that there were no instances of difficulties encountered or disagreements with SCERS during the course of the audit. Ms. Jue-Cochran also reported that SCERS has corrected all known and likely misstatements identified during the audit and none of the misstatements were material, either individually or aggregate.

Mr. Green commended SCERS' Staff for their preparation and cooperation in conducting the audit.

Motion by Mr. Kelly to receive and file the reports; Seconded by Mr. Pittman. Motion carried (8-0).

14. Chief Operations Officer Kathryn Regalia presented the SCERS Comprehensive Annual Financial Report (CAFR) for the Fiscal Years Ended June 30, 2016 and 2015.

Mr. Diepenbrock asked whether SCERS is including the revenue earned from securities lending in the quarterly investment performance reports. Chief Executive Officer Richard Stensrud stated that the revenue from securities lending is included, and separately reported, in the financial information in the CAFR, but that it was not currently being reported in the quarterly investment performance materials. Chief Investment Officer Steve Davis stated that Staff would work with the investment consultant to add that information to future performance reports.

The Board commended Ms. Regalia and her staff on the quality of the CAFR.

Motion by Mr. Diepenbrock to receive and file the report; Seconded by Mr. Lamera. Motion carried (9-0).

ADMINISTRATIVE MATTERS (Continued):

15. Chief Executive Officer Richard Stensrud provided an overview on SCERS' Interest Crediting and Unallocated Earning Policy (Policy). Mr. Stensrud stated that while the investment performance in the first six months of the fiscal year (last six months of 2016) has been solid, with the return of approximately 5.1% running ahead of the target six month growth rate of 3.75%, when the deferred losses from the seven year smoothing process that must be recognized in the current interest crediting period are factored in, the available funding is not sufficient to meet the six month interest crediting target. Mr. Stensrud noted that the overall interest crediting rate is 3.27% for all valuation reserves. Mr. Stensrud noted that, pursuant to the Policy, the interest crediting rate for the active member contribution accounts would be approximately 0.96%.

Motion by Mr. Kelly to approve the proposed interest crediting rate for member contribution accounts for the six month period ending December 31, 2016; Seconded by Mr. Diepenbrock. Motion carried (7-1) (Mr. Baird in opposition).

INVESTMENT MATTERS:

Item 18 was taken up out of order at the request of Mr. Baird to accommodate a scheduling conflict.

18. Chief Investment Officer Steve Davis provided some background on the search performed by Staff and Verus Advisory, Inc. for an international equity developed markets growth manager. Investment Officer JR Pearce introduced Alex Torrens and Des Armstrong from Walter Scott Investment Management, the firm being recommended for the mandate.

Mr. Armstrong provided an overview of Walter Scott. Mr. Armstrong reviewed the firm's investment staff and investment philosophy.

Mr. Torrens discussed Walter Scott's research process and portfolio management.

Mr. Armstrong then reviewed the firm's portfolio characteristics and its investment performance over the past 30 years.

Discussion followed.

Motion by Mr. Diepenbrock to approve the engagement of Walter Scott Investment Management to manage an international developed market growth equity portfolio; Seconded by Mr. Baird. Motion carried (8-0).

ADMINISTRATIVE MATTERS:

16. Board Member Steven Baird read a statement noting that as an employee of the Sacramento County Department of Technology (DTech), he has a remote interest in the SCERS Board selection of a data conversion service provider and therefore will recuse himself from any discussion on the matter.

Chief Executive Officer Richard Stensrud introduced Brian Colker of Linea Solutions, consultant for the IT Modernization Program. Mr. Colker provided a presentation outlining the recommendation by Staff, representatives from DTech, and Linea Solutions that SCERS engage ICON Integration and Design, Inc. to provide data conversion services for the SCERS IT Modernization Program.

Mr. Colker reviewed the process performed by SCERS to create the Request for Proposals (RFP), analyze those proposals, and make a decision. Mr. Colker provided a comparison of the two finalists that SCERS considered, noting that the evaluation committee had confidence that both finalists had the skills to properly perform the work outlined in the RFP. Mr. Colker discussed the drivers that led the committee to choose ICON, including the belief that ICON's methodology and approach was better suited for SCERS. Finally, Mr. Colker reviewed the cost of the project and the next steps.

Discussion followed.

Motion by Mr. Kelly to approve the engagement of ICON Integration & Design, Inc. to provide data conversion services; Seconded by Mr. Diepenbrock. Motion carried (7-0), Ms. Gin abstained.

INVESTMENT MATTERS:

17. Chief Investment Officer Steve Davis introduced the educational presentation by Verus Advisory, Inc. and Staff regarding asset class construction and its impact on investment performance, funded ratio, and contribution rates.

Mr. Davis stated that this presentation would provide a detailed examination of sample portfolios with structures between SCERS' current allocation and the Verus Risk Diversified portfolio (a portfolio with nearly equal exposure to key risk factors). Mr. Davis also noted that the presentation would review SCERS' liquidity profile.

Mr. Davis reviewed total fund performance over the past ten years, and discussed how an important consideration in refining the asset allocation is to mitigate losses in dislocated market environments. Mr. Davis also discussed the ten year capital market return and risk assumptions developed by Verus and Cliffwater LLC for the asset liability study.

INVESTMENT MATTERS (continued):

Mr. Davis presented three investment models being studied by Staff and Verus, and discussed how they compare to SCERS' current policy and Verus' Risk Diversified portfolio. Mr. Davis noted that the second model met many of the objectives identified by the Board as priority goals and provided a deeper analysis comparing the current policy with the second model.

Margaret Jadallah of Verus then reviewed the investment model forecasts for the three models as well as their risk decomposition and sources of risk. Ms. Jadallah also discussed the economic diversification across the models and how the models would have behaved in various historical market scenarios and potential future stress event market scenarios. Finally, Ms. Jadallah reviewed the potential impact on SCERS' funded ratio and the expected employer contributions between the models based on a range of scenarios.

John Nicolini of Verus provided an overview of liquidity ratios and the projected ratios for SCERS' current allocation and the second model using various assumed potential growth rates.

Mr. Davis then provided a conclusion to the presentation noting that Staff and Verus plan to provide a recommendation for a new asset allocation at the next Board meeting.

Discussion followed. Mr. Diepenbrock asked why Staff and Verus favored the second model over the third model, which seemed to have slightly better return and risk metrics. Mr. Davis explained that the third model had a larger allocation to real asset strategies and Staff and Verus believed that the investment opportunities in those areas were limited and reaching the target allocation level would be hard to achieve. Mr. Davis also noted that the third model featured more illiquid investments, which negatively impacted the liquidity ratio.

Barry Dennis of Verus also provided commentary on the presentation and discussed the rationale in how the three models were developed.

Chief Executive Officer Richard Stensrud discussed the difference between developing an optimal asset allocation structure and determining the actuarial investment return assumption. Mr. Stensrud noted that the goal of the asset/liability modeling study was not to identify a target rate of return and then construct a portfolio designed to reach that goal. Mr. Stensrud explained that the goal was to develop a portfolio structure that meets the investment goals identified by the Board – increased risk diversification; reduced volatility; improved funded status; and protection against significant drawdowns. Mr. Stensrud noted that the options presented by Staff and Verus achieved those objectives. Mr. Stensrud further noted, however, that over the next five to ten years, neither the current portfolio or the alternatives under consideration are likely to meet the current actuarial investment return assumption of 7.50%. Mr. Stensrud noted that upon completion of the asset/liability modeling study, the Board would turn to considering whether the return assumption needed to be adjusted to better align with the expected results of the asset allocation model.

INVESTMENT MATTERS (continued):

Motion by Ms. Gin to receive and file the educational presentation by Verus Advisory Inc. and Staff regarding asset class construction and its impact on investment performance, funded ratio, and contribution rates; Seconded by Mr. Diepenbrock. Motion carried (8-0).

19. Jennifer Young of The Townsend Group presented the quarterly performance report on real estate investments for the quarter ended September 30, 2016.

Ms. Young provided a summary of the real estate market for the quarter. Ms. Young also provided an overview of SCERS' real estate portfolio, including the portfolio's funding status and composition.

Ms. Young reported that SCERS' total real estate portfolio returned 1.9% during the third quarter of 2016, which slightly outperformed SCERS' blended benchmark of 1.7%. Ms. Young stated that for the 12-month period ending September 30, 2016, SCERS' real estate portfolio return was 10.1% and that in the same period, the benchmark returned 10.8%.

Ms. Young reported that SCERS' core real estate portfolio returned 2.1% during the third quarter, outperforming the benchmark of 1.8%. Ms. Young stated that for the 12-month period ending September 30, 2016, SCERS' core real estate portfolio return was 7.0% and that in the same period, the benchmark returned 9.1%. Ms. Young further stated that the core separate accounts and the core commingled fund returned 1.9% and 2.4%, respectively, for the quarter.

Ms. Young reported that SCERS' non-core real estate portfolio returned 2.1% for the quarter, equaling Townsend's benchmark of the NFI-ODCE plus 100 bps benchmark of 2.1%. Ms. Young stated that SCERS' non-core real estate portfolio returned 12.7% for the 12-month period ending September 30, 2016, outperforming the benchmark return of 10.2%.

Ms. Young reported that SCERS' domestic public REIT portfolio returned -1.4%, compared to a third quarter return of -1.2% for the FTSE NAREIT (domestic) REIT Index. Ms. Young stated that for the 12-months ending September 30, 2016, SCERS' domestic public REIT portfolio earned 20.7% return, slightly underperforming the benchmark return of 20.9%.

Ms. Young reported that SCERS' international REIT portfolio returned 4.9%, compared to the third quarter return of 4.3% for the FTSE EPRA/NAREIT Global ex-US REIT Index. Ms. Young stated that for the 12-months ending September 30, 2016, SCERS' international REIT portfolio earned a 10.6% return, trailing the benchmark return of 11.7%.

Motion by Mr. Kelly to receive and file the quarterly performance report; Seconded by Ms. Gin. Motion carried (8-0).

INVESTMENT MATTERS (continued):

20. Jamie Feidler of Cliffwater, LLC presented the Alternative Assets Investment Performance Report for periods ending June 30, 2016 and September 30, 2016, including information regarding the absolute return, private equity, real assets, and opportunities portfolios.

Mr. Feidler reported that SCERS' absolute return portfolio was up 2.5% in the third quarter of 2016, which was above the absolute policy benchmark (90-day T-Bills + 5%) which was up 1.3%, and matched the HFRI Fund of Funds Composite Index of 2.5%.

Mr. Feidler stated that the SC Absolute Return Fund, LLC ("SCARF") was up 2.8% in the quarter, and outperformed both the HFRI Fund of Funds Composite Index and the 90-day T-Bills + 5%.

Mr. Feidler stated that for the quarter, SCARF B returned 1.9%, which underperformed the HFRI Fund of Funds Composite Index, but outperformed the 90-day T-Bills + 5%.

Mr. Feidler reported that SCERS' direct absolute return program was up 2.6% during the third quarter, which outperformed both the HFRI Fund of Funds Composite Index and the 90-day T-Bills + 5%.

Mr. Feidler reported that the net investment rate of return ("IRR") of SCERS' private equity portfolio was up 9.8% since inception compared to the Cambridge Associates Private Equity Index up 9.8% and the multiple of total value to paid in capital ("TVPI") is 1.23x since inception. Mr. Feidler noted that SCERS' private equity portfolio shows lower relative returns due to the early phase/cycle of investments (j-curve affect) compared to the index.

Mr. Feidler reported that, through September 30, 2016, SCERS' real assets portfolio IRR was 7.0% compared to SCERS' real assets portfolio benchmark (CPI + 5%) IRR of 7.2% and SCERS' TVPI was 1.2x.

Mr. Feidler reported that SCERS' opportunities portfolio generated a net IRR of 8.6% as of September 30, 2016 which has outperformed SCERS' long-term benchmark (SCERS' actuarial rate of return) of 7.5%.

Motion by Mr. Diepenbrock to receive and file the quarterly performance report; Seconded by Mr. Pittman. Motion carried (8-0).

The meeting was adjourned at 1:10 p.m.

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MEMBERS PRESENT: Rick Fowler (arrived at 10:14 a.m.), John B. Kelly, Steven L. Baird (departed at 10:58 a.m.), Michael DeBord, James A. Diepenbrock, Diana Gin, Ben Lamera, Chris Pittman, John Conneally, and Martha J. Hoover

MEMBERS ABSENT: Keith DeVore

OTHERS PRESENT: Richard Stensrud, Chief Executive Officer; Steve Davis, Chief Investment Officer; Robert L. Gaumer, General Counsel; Kathryn T. Regalia, Chief Operations Officer; John W. Gobel, Sr., Chief Benefits Officer; Annette St. Urbain, Assistant Retirement Administrator; Suzanne Likarich, Retirement Services Manager; Thuyet Dang, Senior Accounting Manager; JR Pearce, Investment Officer; John Lindley, IT Administrator; Barry Dennis, John Nicolini, and Margaret Jadallah, Verus Advisory, Inc; Jamie Feidler, Cliffwater LLC; Jennifer Young-Stevens and Robert Miranda, The Townsend Group; Richard A. Green and Leah Jue-Cochran, Macias Gini & O’Connell; Brian Colker, Linea Solutions; John Reed and Kelsey Johnson, Deputy County Counsel; Alan Matré; and Kevin Isawa

Respectfully submitted,

Richard Stensrud
Chief Executive Officer and
Secretary of the Retirement Board

APPROVED: _____
Rick Fowler, President

DATE: _____

cc: Retirement Board (11); Board of Supervisors (6); County Counsel; County Executive (2); Internal Services Agency (2); County Labor Relations; Employee Organizations (20); Sacramento County Retired Employees’ Association; SCERS Member Districts (10); Elected Officials (3); Superior Court of California, County of Sacramento; Amervest Company, Inc.; Mark Merin; John R. Descamp; and The Sacramento Bee.