SACRAMENTO COUNTY EMPLOYEES' RETIREMENT SYSTEM

MINUTES

RETIREMENT BOARD MEETING, WEDNESDAY, NOVEMBER 6, 2013

A special 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, November 6, 2013, and commenced at 10:00 a.m.

OPEN SESSION:

PUBLIC COMMENT:

1. None heard.

MINUTES:

2. The Minutes of the October 16, 2013 regular meeting were approved on Motion by Mr. Fowler; Seconded by Mr. Kelly. Motion carried (7-0).

CONSENT MATTERS:

Items 3-11

The Consent matters were acted upon as one unit upon a Motion by Mr. DeVore; Seconded by Ms. Wolford-Landers. Motion carried (8-0).

3. GARGANO, Lisa L.: Dismissed application for a service-connected disability retirement.

CONSENT MATTERS (continued):

4. PERISICH, Todd E.: Denied a service-connected disability retirement.

5. LANGSTON, Angela M.: Granted an interim nonservice-connected disability retirement pending the adjudication of applicant's claim of service-connected disability retirement.

6. UTLEY, Kathleen T.: Granted a service-connected disability retirement.

7. Approved the proposed amendment of the investment parameters for the portfolio overlay program managed by State Street Global Advisors.

8. Received and filed the Selected Fees and Costs for Outside Legal Services for the Quarter Ended September 30, 2013.

9. Received and filed the Portfolio Re-Balancing Report for the Quarter Ended September 30, 2013.

10. Received and filed the Trading Cost Report for the Quarter Ended September 30, 2013.

11. Received and filed the October 2013 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 reported that he had been meeting with key stakeholders regarding the strategic planning exercise contemplated for early 2014. Mr. Stensrud noted that the meetings have been going well and that the various stakeholders appear to appreciate the success achieved by SCERS and understand and concur with the issues for consideration in strategic planning. Mr. Stensrud stated that he will be continuing with the meetings. Mr. Fowler, who attended one of the meetings, noted that Mr. Stensrud was well prepared with appropriate information.

Mr. Stensrud reported that Staff was continuing to work on expanding the investment staff. Mr. Stensrud stated that an offer had been made to JR Pearce for an investment officer position and that Mr. Pearce had accepted the offer. Mr. Stensrud noted that Mr. Pearce was expected to join SCERS in late November.

Mr. Stensrud reported that Deputy Chief Investment Officer Steve Davis had recently passed the Chartered Alternative Investment Analyst (CAIA) exam. Mr. Stensrud also reported that Asset International Chief Investment Officer (aiCIO) has named Chief Investment Officer Scott Chan #87 on their list of the 100 most powerful CIOs in the world. Mr. Stensrud commended Mr. Davis and Mr. Chan for their accomplishments.

ADMINISTRATIVE MATTERS (continued):

13. Paul Angelo and Andy Yeung of Segal Consulting (Segal) presented the SCERS Actuarial Valuation as of June 30, 2013.

Mr. Angelo noted that no new economic assumptions had been approved by the Board. However, at the June 17, 2013 Board Meeting, the Board adopted an Actuarial Funding Policy, which, among other things, established: (1) The actuarial cost methodology; (2) The asset smoothing method; (3) The amortization policy, including the use of multiple amortization layers; (4) The length of the amortization period for different sources of unfunded accrued actuarial liability (UAAL) or surpluses; and (5) When it is appropriate to combine or re-start an amortization period.

Mr. Angelo stated that, with respect to amortization of UAAL, under the Actuarial Funding Policy the UAAL balance as of June 30, 2012 will be amortized over a declining 22 year period, and any subsequent change in UAAL will be amortized in a separate layer and over a separate period depending on the source of the UAAL – i.e., UAAL due to actuarial gains and losses or due to changes in actuarial assumptions/methods will be amortized over separate 20 year declining periods; UAAL due to plan amendments will be amortized over a separate 15 year declining period; and UAAL due to a retirement incentive program will be amortized over a separate 5 year declining period.

Mr. Angelo also stated that, with respect to the actuarial cost methodology, under the Actuarial Funding Policy the entry age funding method has been modified from the aggregate entry age method to the individual entry age method, which can be used under the new Governmental Accounting Standards Board (GASB) rules for both funding and financial reporting purposes. Additionally, with respect to asset smoothing, under the Actuarial Funding Policy investment gains and losses are recognized (‘smoothed’) over a 7 year period, subject to market value corridors which require that the actuarial value of assets (AVA) stays within a range of 70% to 130% of the market value of assets (MVA).

Mr. Angelo noted that Sacramento County had entered into a bargaining agreement with the Sacramento Deputy Sheriffs’ Association (DSA) which would provide salary increases, which would have otherwise been deferred, to sheriff’s deputies who agreed to retire by June 30, 2015 and therefore those salary increases would be used for the calculation of retirement benefits. Mr. Angelo noted that the additional salaries would not necessarily increase liabilities, but that the earlier than expected retirement dates of many of the DSA members participating in the program would increase liabilities. Mr. Angelo noted that this additional unfunded liability would be amortized over a shorter, five year period.

Mr. Angelo noted that at the September 2012 Board meeting, the Board adopted a two-year phase-in of the impact of the change in assumptions for the employer contribution rate starting with fiscal year 2013/2014. He noted that the employer contributions for 2014/2015 will increase due to the second year of the phase-in.

ADMINISTRATIVE MATTERS (continued):

Mr. Angelo reported that the aggregate employer rate increased from 25.0% of payroll to 27.57%. The increase in the recommended employer contribution rates is due to the following: (1) The ongoing phase-in of net investment losses via the smoothing process (primarily from the market collapse in 2007-2009), which pushed the employer rates upward by 1.26% of payroll; (2) The final year of the two year phase-in of the cost impact of the change in economic assumptions, which pushed upward on employer rates by 0.77% of payroll; (3) The change in the Entry Age actuarial funding methodology, which pushed employer rates upward by 0.60% of payroll; (4) Addressing the UAAL over a lower than expected payroll, which pushed upward on employer rates by 0.32% of payroll; (5) The cumulative effect of demographic changes and other actuarial losses, which pushed upward on employer rates by 0.42%; and (6) The retirement incentive for DSA members, which pushed the rate upward by 0.14% of payroll. These upward pressures on cost were partially offset by lower than expected salary growth, which pushed employer rates downward by 0.94% of payroll.

Mr. Angelo reported that the aggregate member contribution rate calculated in this valuation decreased from 6.42% of payroll to 6.39% of payroll. Mr. Angelo explained that the primary driver of the decrease in the employee contribution rates were demographic changes which pushed downward on the employee normal cost by 0.13%, offset to a degree by the change in the entry age actuarial funding methodology, which pushed upward on rates by 0.09% of payroll.

Mr. Angelo stated that, notwithstanding the 2007-2009 market collapse, the funded status has been strong and stable over time, and remains strong at 82.8% (down slightly from 83.3%). While the UAAL on an actuarial value of assets basis has increased by approximately $105,000, on a market value of assets basis, the level of UAAL has decreased by more than $341,000. The difference between the two numbers reflects the impact of the smoothing process, in that the actuarial value of assets does not yet reflect all of the strong investment performance subsequent to the 2007-2009 market collapse. In contrast, while total plan liabilities have increased by approximately $373,000 from last year, because of the investment performance, the market value of assets increased by approximately $714,000 from last year.

Mr. Angelo reported that due to an anomalous result of the smoothing process, left unchecked, the phasing-in of the remaining losses will result in a very uneven smoothing pattern over the next 6 years. Specifically, the next two years would feature the phasing-in of smoothed losses, followed by two years of phasing-in smoothed gains, followed by a year of smoothed losses, and then a year of smoothed gains. Mr. Angelo noted that given this pattern of alternating years of relatively equal smoothed gains and losses, Segal recommends that the Board consider utilizing their option under the Actuarial Funding Policy to alter the recognition of gains and losses. Mr. Angelo noted that specifically, Segal recommends combining the deferred gains and losses into a single 6 year smoothing

ADMINISTRATIVE MATTERS (continued):

'layer,' resulting in a very small, level smoothed loss in each of the next six years. Mr. Angelo noted this would reduce the volatility of gain/loss recognition and result in a more stable funded ratio and more level employer contributions. It would also recognize the net losses over the same time period as under the normal, separate smoothing layers.

Discussion followed, including consideration of the Segal recommendation to combine the deferred gains and losses into a single six year amortization layer, and the net impact from an actuarial perspective of members paying a greater share of normal cost, but receiving offsetting salary increases.

Motion by Mr. DeVore to receive and file the Actuarial Valuation as of June 30, 2013; approve the recommendation to combine the deferred gains and losses that would be recognized over the next 6 years into a single 6 year smoothing layer; and adopt the proposed employer and employee contribution rates for the 2013-14 Fiscal Year; Seconded by Ms. Wolford-Landers carried (8-0).

INVESTMENT MATTERS:

14. Patrick Thomas of Strategic Investment Solutions presented the Investment Performance Report for the Quarter Ended September 30, 2013.

Mr. Thomas reported that the Total Fund (TF) return for the first quarter, including the impact of the overlay program, was 5.5% gross of fees. The TF return was 1.0% above the policy index and the allocation index of 4.5%. The overlay program had a positive impact of 0.4% during the quarter.

Mr. Thomas reported that on a comparative basis, the return for the quarter was 0.7% above the Public Funds $1+ Billion Median return of 4.8%. The TF return ranks in the 21st percentile in the InvestorForce Universe, which is the ranking universe used by SIS. All the major asset classes experienced positive returns for the quarter.

Mr. Thomas reported that at the asset class level, quarter outperformance occurred, gross of fees, in the domestic equity, fixed income, hedge fund, real assets, and opportunistic segments. Underperformance occurred in the international equity segment. The private equity segment was in-line with the benchmark.

Mr. Thomas reported that, for the calendar year-to-date, the TF return gross of fees, including the impact of the overlay program was 11.2%, which was 1.9% above the return of the policy index of 9.3% and 0.6% above the allocation index return of 10.6%. The TF calendar year return was 1.6% above the Public Funds $1+ Billion Median return of 9.6%, and ranks in the 23rd percentile in the InvestorForce Universe, which is the ranking universe used by SIS.

INVESTMENT MATTERS (continued):

Mr. Thomas reported that at the asset class level, year-to-date outperformance versus the policy benchmark has occurred, gross of fees, in domestic equity, international equity, fixed income, hedge fund, and opportunistic segments of the portfolio. Calendar year-to-date underperformance versus the policy benchmark occurred, gross of fees, in the private equity and real assets segments of the portfolio.

Mr. Thomas reported that the annualized TF return gross of fees for three years of 10.4% is 0.2% above the policy index benchmark for the same period. The annualized TF return gross of fees for five years of 7.3% is 0.2% below the policy index benchmark for the period. The TF gross of fees return of 8.6% since the inception of SIS' data in June of 1986 is 0.2% below the Total Benchmark return of 8.8% for the period.

Motion by Mr. Kelly to receive and file the quarterly report and to approve the recommendations made in the presentation; Seconded by Ms. Wolford-Landers. Motion carried (8-0).

15. Chief Investment Officer Scott Chan presented the recommendation to engage Mondrian Investment Partners and William Blair & Company to manage an emerging markets small cap equity mandate.

Mr. Chan noted that Staff chose two managers due in part to their high quality, but also to mitigate risk and provide greater diversification. Mr. Chan noted that Mondrian is more of a value defensive manager, while William Blair is more of a quality growth manager, and therefore complement each other well.

Deputy Chief Investment Officer Steve Davis introduced Ormala Krishnan and Paul Ross of Mondrian Investment Partners. Mr. Ross provided a brief introduction on Mondrian's thoughts on the emerging market small cap space. Ms. Krishnan reviewed the characteristics of emerging market small cap and Mondrian's investment approach. Ms. Krishnan provided an overview of Mondrian's organizational makeup and emerging market small cap team.

Mr. Davis then introduced John McLaughlin and Todd McClone of William Blair & Company. Mr. McLaughlin provided an overview of William Blair. Mr. McClone, joining over the phone, covered William Blair's philosophy and process. Finally, Mr. McClone provided a review of William Blair's portfolio analytics and performance.

Motion by Mr. DeVore to approve the recommendation to engage Mondrian Investment Partners and William Blair & Company to manage an emerging markets small cap equity mandate; Seconded by Ms. Wolford-Landers. Motion carried (8-0).

CLOSED SESSION:

16. Discussion took place regarding the purchase or sale of specific pension fund investments pursuant to Government Code Section 54956.81.

The meeting was adjourned at 1:25 p.m.

MEMBERS PRESENT: James A. Diepenbrock, John B. Kelly, Keith DeVore, Richard B. Fowler II, Diana Gin, Kathy O'Neil (arrived at 10:04 a.m.), Chris A. Pittman, Nancy Wolford-Landers (arrived at 10:01 a.m.), John Conneally, and Michael DeBord (arrived at 10:02 a.m.).

MEMBERS ABSENT: Julie Valverde.

OTHERS PRESENT: Richard Stensrud, Chief Executive Officer; Scott Chan, Chief Investment Officer; Kathryn T. Regalia, Chief Operations Officer; John W. Gobel, Sr., Chief Benefits Officer; Steve Davis, Deputy Chief Investment Officer; Suzanne Likarich, Retirement Services Manager; Thuyet Dang, Accounting Manager; John Lindley, IT Administrator; Lance Kjeldgaard, Outside Counsel; Patrick Thomas and Jonathan Brody, Strategic Investment Solutions, Inc; Paul Angelo and Andy Yeung, Segal Consulting; Ormala Krishnan and Paul Ross, Mondrian Investment Partners; John McLaughlin, William Blair & Company; John Kennedy, Nossaman LLP; Diana Ruiz, Deputy County Counsel; and Todd Perisich.

Respectfully submitted,

Richard Stensrud
Chief Executive Officer and
Secretary of the Retirement Board

APPROVED: ______________________________________
James A. Diepenbrock, 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.