



Executive Staff:

Richard Stensrud  
Chief Executive Officer

Jeffrey W. States  
Chief Investment Officer

James G. Line  
General Counsel

Kathryn T. Regalia  
Chief Operations Officer

John W. Gobel, Sr.  
Chief Benefits Officer

Members of the Board of Retirement

James A. Diepenbrock, President  
Appointed by the Board of Supervisors

Keith DeVore, 1<sup>st</sup> Vice President  
Elected by Miscellaneous Members

John B. Kelly, 2<sup>nd</sup> Vice President  
Appointed by the Board of Supervisors

Dave Irish, Director of Finance  
Ex-Officio

Winston H. Hickox  
Appointed by the Board of Supervisors

Vacant  
Elected by Miscellaneous Members

William D. Johnson  
Elected by Safety Members

Nancy Wolford-Landers  
Elected by Retired Members

Robert Woods  
Appointed by the Board of Supervisors

William Cox  
Elected by Retired Members

Steven Soto  
Elected by Safety Members

## MINUTES

### RETIREMENT BOARD MEETING, SEPTEMBER 21, 2006

The special meeting of the Retirement Board was held in the Sacramento County Employees' Retirement System Administrative Office, U.S. Bank Plaza Building, 980 9th Street, 18<sup>th</sup> Floor, Sacramento, California, on September 21, 2006 at 12:06 p.m.

#### OPEN SESSION:

##### PUBLIC COMMENT:

1. None heard.

##### MINUTES:

2. Motion by Mr. Irish to approve the Minutes of the July 20, 2006 regular meeting and the August 16, 2006 special meeting; Seconded by Mr. Johnson. Motion carried (5-0).

##### ADMINISTRATIVE MATTERS:

3. Chief Executive Officer Richard Stensrud reported on various SCERS' activities and on developments affecting public retirement systems.

**ADMINISTRATIVE MATTERS: (Continued)**

Mr. Stensrud discussed recent news reports on the investment losses by the hedge fund manager Amaranth Advisors, including losses by some California retirement systems. Mr. Stensrud reported that SCERS had no funds invested with Amaranth. Mr. Stensrud also noted that SCERS utilizes a fund-of-fund approach to its hedge fund investments, through which an investment manager with expertise in such investments was responsible for identifying and monitoring investment firms that would do the actual investing. Mr. Stensrud noted that this approach differed from one where the retirement system was responsible for identifying and making direct investments in specific hedge funds, and then overseeing those investments.

Mr. Stensrud and Chief Investment Officer Jeffrey States reported that review, analysis and negotiation was ongoing regarding the final documentation for the investments the Board had approved in three value-added real estate funds. Mr. Stensrud and Mr. States noted that the negotiations had been completed with one of the funds (Allegis Value Trust), and the final documents had been signed pursuant to the authority granted by the Board in approving the investments.

Mr. Stensrud reported that the legislature had passed AB 2863 which, among other things, authorizes 1937 Act retirement systems to manage assets for the sponsors of retiree health care plans and 'other post-employment benefit' ('OPEB') plans. Mr. Stensrud noted that this legislation could prove to be very helpful to the sponsors of such plans in that it would allow them to get a higher investment return on their assets, resulting in lower cost to the plan sponsor. Mr. Stensrud noted that the next step would be to convince the Governor to sign the bill.

Mr. Stensrud and General Counsel James G. Line reported that they would be bringing to the Board a proposed structure for addressing SCERS' legal service needs. Mr. Stensrud and Mr. Line noted that the structure would be based on the plan approved by the Board in establishing the General Counsel position, and would include a description of those areas where Mr. Line and Mr. Stensrud believed it was appropriate to utilize the services of outside counsel, and their recommendations for who to engage to perform such services.

Mr. Stensrud reported that the last retirement planning seminar of the year would be held the following week at the Board of Supervisors' Chambers. Mr. Stensrud noted that like the other sessions that had been held over the summer and fall, the final program was fully subscribed.

4. Andy Yeung of The Segal Company presented the firm's recommended economic actuarial assumptions for SCERS' actuarial valuation as of June 30, 2006. Mr. Yeung discussed the specific assumptions and outlined how each assumption was determined. Mr. Yeung reported that based on the firm's analysis of past experience and expected trends, The Segal Company was recommending no changes to the economic assumptions used for the previous year's valuation. Those assumptions include: (a) a 7.75% investment return assumption; and (b) a 3.5% inflation assumption. Mr. Yeung noted that the current economic assumptions had been

**ADMINISTRATIVE MATTERS: (Continued)**

adopted by the Board after review by The Segal Company and an independent assessment by consulting actuary Bartel & Associates. Mr. Yeung reported that The Segal Company was not recommending any changes to the non-economic (i.e., demographic) assumptions at this time.

Discussion followed. Motion by Mr. Hickox to adopt the recommended economic actuarial assumptions; Seconded by Ms. Wolford-Landers. Motion carried (6-0).

5. Chief Executive Officer Richard Stensrud presented a proposed Interest Crediting and Excess Earnings Policy ('Policy') for the Board's consideration. Mr. Stensrud noted that the proposed Policy was developed based on the goals, priorities and methodologies identified by the Board after several lengthy discussions. Mr. Stensrud noted that the proposed Policy was designed to provide guidelines for the Board based on the identified goals and priorities, while allowing the Board to exercise its discretion under the law in such matters if the Board determined that such action was reasonable, prudent and in the best interests of the retirement system. Mr. Stensrud noted such flexibility was important for allowing the Board to make sound fiduciary decisions if prevailing circumstances should change.

Mr. Stensrud noted that the fundamental objective of the proposed Policy was to maintain a sound funded status of the retirement system through the reasonable and prudent application of available earnings, including establishing contingency reserves sufficient to make a meaningful contribution toward mitigating future earnings shortfalls and unexpected expenses. Mr. Stensrud outlined the key elements of the proposed Policy, including: (a) The priority of fully funding the core vested benefits and establishing substantial contingency reserves before funding would be provided for non-vested benefits or for other purposes permitted by the 1937 Act; (b) The equal application of any funds in excess of the target earnings rate ('unallocated earnings') toward any earnings shortfall from a previous period and establishing contingency reserves and that this equal application of unallocated earnings would continue until such time as target funding levels are reached; and (c) A lower interest crediting rate for the active member contribution reserves than the other actuarial reserves. With respect to this last matter, Mr. Stensrud recommended that the Board select one of three possible benchmarks for setting the interest crediting rate for the active member contribution reserves: (1) the 6-Month Treasury Bill rate; (2) the 2-Year Treasury Note rate; or (3) the 5-Year Treasury Note rate.

Substantial discussion followed, including whether, and under what circumstances, the Board would consider providing funding toward non-vested benefits such as support for retiree health care costs. Discussion also was held regarding the appropriate benchmark for setting the interest crediting rate for the active member contribution reserves, including consideration of the difference between the rates at different points over the last several years. Mr. Stensrud and General Counsel James Line confirmed that the elements of the Policy are not subject to bargaining, but rather, rest within the discretion of the SCERS Board.

**ADMINISTRATIVE MATTERS: (Continued)**

Mr. Hickox made a motion to adopt the proposed Policy, utilizing the 5-Year Treasury Note rate as the benchmark for crediting interest to the active member contribution reserves; Seconded by Mr. Irish. Motion carried (5-2) (Ayes: DeVore, Diepenbrock, Irish, Hickox, and Soto)(Nays: Wolford-Landers and Johnson). Ms. Wolford-Landers dissented because she felt the Policy set too high a threshold before consideration would be given to funding non-vested benefits. Mr. Johnson dissented because he felt the appropriate benchmark for crediting interest to active member contribution reserves should be based on a shorter time period.

**CLOSED SESSION:**

**DISABILITY MATTERS:**

6. Hamilton-Travis, Rochelle: Matter was continued to the October Board Meeting.
7. Hasapis, Robert K.: Action was taken on the Application for Disability Retirement per confidential memorandum from the Chief Benefits Officer dated October 5, 2006.
8. Lloyd, Judith T.: Matter was continued to the October Board Meeting.
9. Watkins, Comer: Action was taken on the Application for Disability Retirement per confidential memorandum from the Chief Benefits Officer dated October 5, 2006.
10. Webber, Raymond: Action was taken on the Application for Disability Retirement per confidential memorandum from the Chief Benefits Officer dated October 5, 2006.

**SIGNIFICANT EXPOSURE TO LITIGATION: [Government Code Section 54956.9(a)]**

11. Lloyd v. SCERS, et al., Sacramento County Superior Court, Case No. 06CS1009: Consultation with counsel.

**OPEN SESSION:**

**INVESTMENT MATTERS:**

12. Neil Tremblay and Mike Martel of State Street Global Advisors (SSGA) provided a portfolio performance review of the Strategic Overlay Strategy which was started in February. They reviewed the objectives established for the program and explained how the overlay strategy had performed during its first six months. Discussion followed, including questions about the tracking error in performance between the equity futures used to provide the overlay and the various market indexes that were being replicated. Staff and SSGA were asked to reconsider

**INVESTMENT MATTERS: (Continued)**

the treatment of the hedge fund of funds investments within the overlay strategy to determine whether allocating them entirely to cash was consistent with the portfolio characteristics for the hedge fund investments. SSGA was also asked to work with Mercer to provide a clearer presentation on the risk and return benefits to SCERS' overall portfolio. The presentation report was received and filed on a Motion by Mr. DeVore; Seconded by Ms. Wolford-Landers. Motion carried (7-0).

13. Chief Investment Officer Jeffrey States reviewed the changes being proposed to the Investment Policy and Objectives. Mr. States noted that the draft was substantially the same as the one discussed with the Board in July. Mr. States reported that the most important changes in the proposed language were the addition of a description of the strategic overlay strategy in the section on asset class structure and the addition of language regarding investment manager terminations in emergency situations.

Discussion followed, including a request that language be added regarding the definition of cost of living. Mr. States noted that the document would be reviewed for any necessary corrections or editing changes.

The Investment Policy and Objectives was approved with suggested changes on a Motion by Mr. Woods; Seconded by Ms. Wolford-Landers. Motion carried (7-0).

14. Chief Executive Officer Richard Stensrud presented a proposed Resolution delegating authority to the Chief Executive Officer and the Chief Investment Officer, in consultation with SCERS' investment consultant, General Counsel and Board President, to terminate an investment manager if it was determined that immediate action was necessary to protect SCERS' interests, but it was not possible to obtain a quorum of the Board.

Mr. Stensrud noted that the proposed Resolution was in response to Board discussions regarding possible situations where an inability to act quickly could result in detrimental impact to SCERS' assets or interests. Mr. Stensrud noted that the Board had indicated that it would be reasonable and prudent to develop an alternate means for taking appropriate action in such situations, but that it would also be necessary to assure that any grant of authority had the requisite controls and accountability.

Mr. Stensrud noted that the proposed Resolution was designed (a) to assure that the authority was only activated in situations where it was truly warranted; (b) to assure that the decision-making process included the appropriate experts; (c) to assure that the decision-making process included Board participation and control; (d) to provide flexibility in gathering decision-makers and fashioning remedies; and (e) to provide prompt and full reporting to the Board if the authority was exercised.

**INVESTMENT MATTERS: (Continued)**

Discussion followed. Motion by Mr. Johnson to adopt Resolution No. 2006-09 delegating authority to terminate investment managers and take other appropriate actions in emergency situations; Seconded by Mr. Hickox. Motion carried (7-0).

15. Chief Executive Officer Richard Stensrud presented a proposed Resolution delegating authority to staff to waive contractual limitations on restricted relationships in a real estate transaction if they determined the relationship was not material to the proposed transaction and did not operate to the detriment of SCERS.

Mr. Stensrud noted that SCERS' real estate manager contracts contain a prohibition on certain types of situations where the investment manager, its employees or a related entity might play a role where the firm or individual's duties or interests might not be consistent with its duties to SCERS. Mr. Stensrud noted that this language had not been viewed as an absolute bar on such situations and that the contractual limitation had previously been waived when it had been determined that the situation was not material, and did not operate to the detriment of SCERS.

Mr. Stensrud explained that such a situation could arise at a point in a real estate transaction when it might not be possible to get the Board's approval in a timely manner. Accordingly, Mr. Stensrud recommended that the Board adopt proposed Resolution 2006-10 delegating authority to the Chief Executive Officer or the Chief Investment Officer, in consultation with SCERS' real estate consultant and General Counsel, to determine if a given situation is material and detrimental to SCERS, and if not, to waive the contractual limitation. Mr. Stensrud noted that the proposed Resolution required that any such action be promptly reported to the Board.

Discussion followed. Motion by Ms. Wolford-Landers to adopt Resolution 2006-10; Seconded by Mr. DeVore. Motion carried (7-0).

16. Chief Investment Officer Jeffrey States presented a proposed Resolution authorizing the conversion of SCERS' investment in the Cornerstone Property Fund, an open-end, core real estate fund, to an investment in the Cornerstone Patriot Fund LP, a private real estate investment trust. Mr. States noted that he and Allison Yager of Mercer Investment Consulting had reviewed the Offering Memorandum and had determined that the investment guidelines for the two investments to be the same on most terms and conditions. Mr. States noted that SCERS' General Counsel had reviewed the Subscription documents as to legal form and sufficiency. Brian Murdy, Portfolio Manager for both the existing Cornerstone Property Fund and for the Cornerstone Patriot Fund was present to answer questions.

Discussion followed. Motion by Mr. Hickox to adopt Resolution 2006-11 authorizing the Board President to execute the Subscription Agreement and any other documents necessary to convert the investment in the Cornerstone Property Fund to an investment in the Cornerstone Patriot Fund LP; Seconded by Mr. Woods. Motion carried (7-0).

**INVESTMENT MATTERS: (Continued)**

17. Chief Investment Officer Jeffrey States presented a report on changes to the commission recapture program administered by State Street Global Markets for SCERS. Mr. States reported that several changes were taking place in the brokerage industry related to the commission dollars returned by brokers. Mr. States noted these changes will decrease the income SCERS receives from the commission recapture program. Mr. States noted that Mercer Investment Consulting had reviewed the changes and was recommending that clients continue their programs for the present. Mr. States' report was for information purposes and no action was taken by the Board.
18. Chief Investment Officer Jeffrey States presented follow-up information to the educational program presented in August regarding loosening the long-only constraint on investments. Mr. States noted that Mercer Investment Consulting had produced an analysis discussing the potential advantages and disadvantages of relaxing the long-only constraint. Mr. States further noted that Mercer was advising its clients to thoroughly understand the risks as well as the potential rewards in pursuing strategies such as '130/30' or '120/20.' Mr. States' report was for information purposes and no action was taken by the Board.
19. Chief Investment Officer Jeffrey States presented follow-up information to the educational program presented in August regarding the investment risks and opportunities associated with climate change. Mr. States outlined various steps that staff would be taking to help develop a SCERS-appropriate strategy for addressing such considerations. Mr. States' report was for information purposes and no action was taken by the Board.
20. The Chief Investment Officer's Monthly Investment Management Compliance and Activity Report for August 2006 was received and filed on a motion by Mr. Woods; Seconded by Mr. Johnson. Motion carried (6-0)

The meeting was adjourned at 3:06 p.m.

**MEMBERS PRESENT:** James A. Diepenbrock; Keith DeVore (arrived at 12:18 p.m.); Dave Irish (left at 2:56 p.m.); Winston Hickox (arrived at 12:09 p.m.); William D. Johnson; Steven Soto (left at 1:54 p.m.); Nancy Wolford-Landers; and Robert Woods (arrived at 1:09 p.m.).

**MEMBERS ABSENT:** William Cox; and John B. Kelly.

**OTHERS PRESENT:** Richard Stensrud, Chief Executive Officer; Jeffrey States, Chief Investment Officer; James G. Line, General Counsel; Kathryn Regalia, Chief Operations Officer; John Gobel, Chief Benefits Officer; Suzanne Likarich, Retirement Services Manager; Alice Jarboe; Andy Yeung, The Segal Company; Tom Lightvoet of Mercer Investment Consulting; Neil Tremblay and Mike Martel of State Street Global Advisors; Brian Murdy of the Cornerstone Patriot Fund; Janet Ianniello of Cornerstone Realty Advisors; and Teresa Kennedy, Office Specialist.

Respectfully submitted,

SACRAMENTO COUNTY EMPLOYEES'  
RETIREMENT SYSTEM

Richard Stensrud  
Chief Executive Officer

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) Amervest Company, Inc.; Dickstein & Merin; John R. Descamp; and The Sacramento Bee.