



Executive Staff:

Richard Stensrud
Chief Executive Officer

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

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

William D. Johnson, Second Vice President
Elected by the Safety Members

Diana Gin
Elected by the Miscellaneous Members

Winston H. Hickox
Appointed by the Board of Supervisors

Kathy O'Neil
Elected by the Miscellaneous Members

Julie Valverde
Ex Officio, Director of Finance

Nancy Wolford-Landers
Elected by the Retired Members

John Conneally
Elected by the Safety Members

Michael DeBord
Elected by the Retired Members

MINUTES

RETIREMENT BOARD MEETING, THURSDAY, APRIL 19, 2012

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 Thursday, April 19, 2012, and commenced at 1:00 p.m.

OPEN SESSION:

PUBLIC COMMENT:

1. Chief Executive Officer Richard Stensrud introduced attorney Lance Kjeldgaard, who will be providing assistance with day-to-day legal service needs while the General Counsel position is vacant. Mr. Stensrud noted that Mr. Kjeldgaard had been the long time General Counsel to the San Bernardino County Retirement System. Mr. Stensrud noted that Mr. Kjeldgaard would be present in the SCERS office for a day or two every one or two weeks, in addition to being accessible by email and phone.

Deputy County Counsel Diana Ruiz informed the Board that at the upcoming State Association of County Retirement Systems (SACRS) Spring Conference there would be a session focused on disability retirement and the role of the medical advisor.

MINUTES:

2. The Minutes of the March 15, 2012 special meeting were approved on Motion by Ms. O'Neil; 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. DeBord; Seconded by Mr. Johnson. Motion carried (7-0).

3. SCOTT, David W.: Granted a nonservice-connected disability retirement.
4. PIERCE, Victor A. III: Granted a service-connected disability retirement.
5. CRAIG, Holly M.: Denied a service-connected disability retirement. Granted a nonservice-connected disability retirement.
6. JONES, Sien H.: Denied a nonservice-connected disability retirement.
7. Approved the proposed items to be voted on by the membership at the State Association of County Retirement Systems (SACRS) Spring Conference.
8. Approved the renewal of SCERS' fiduciary liability insurance coverage.
9. Approved the extension of the agreement with The Segal Company to provide actuarial services.
10. Approved the proposed amendment of the investment management agreement with Huber Capital Management.
11. Received and filed the March 2012 Monthly Investment Manager Compliance Report and Watch List.

CLOSED SESSION:

12. Consulted With Legal Counsel – Pending Litigation
Government Code Section 54956.9(C)
1 Case.

OPEN SESSION:

ADMINISTRATIVE MATTERS:

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

ADMINISTRATIVE MATTERS (continued):

Mr. Stensrud reported that the Staff and General Investment Consultant Strategic Investment Solutions (SIS) were conducting investment manager searches for three assignments in the international equity framework, including ACWI ex-US, international growth and international value. Mr. Stensrud stated that it was anticipated proposed firms would be presented to the Board at the May Board Meeting.

Mr. Stensrud noted that due to the investment manager search process and the timing of the SACRS Spring Conference, the May Board Meeting would need to be rescheduled for the end of May. Mr. Stensrud stated that Staff would be contacting Board Members to coordinate a date for the May Board Meeting.

Mr. Stensrud noted that the IFE Market Makers conference would be held June 27 – June 29, 2012 in Carlsbad, California. Mr. Stensrud stated that openings were limited and that Board Members who wish to attend should contact Staff for assistance.

Mr. Stensrud also noted that the SACRS Public Pension Investment Management Program would be held July 16 – July 18, 2012 at UC Berkeley. Mr. Stensrud stated that Board Members who wish to attend should contact Staff for assistance.

Mr. Stensrud reported that the Staff and Alternative Assets Consultant Cliffwater were working on one proposed private equity investment and two proposed hedge fund investments that would be closing by May 1, 2012. Mr. Stensrud stated that Staff would be keeping the Board Members updated on the progress.

Mr. Stensrud reported that the joint assembly committee looking at pension reform had met on April 13, 2012 in Chino, California. Mr. Stensrud stated that he was asked to testify on behalf of the 1937 Act Systems on the subject of compensation in county retirement, how it has been impacted by the Ventura Decision, and ramifications for addressing potential pension spiking. Mr. Stensrud noted he was joined by Harvey Leiderman from Reed Smith LLP, who is the outside counsel for Contra Costa County, Orange County, and several other county retirement systems.

Mr. Stensrud reported that SCERS was recently able to open the recruitment for the vacant Investment Officer position. Mr. Stensrud noted that SCERS has received already received a number of résumés. Mr. Stensrud stated that he would keep the Board Members updated on the progress of the recruitment.

Michael DeBord reported that he and other members of the state retirees' association had prepared a report on the retirement security and effectiveness of defined contribution plans as compared to defined benefit plans. Mr. DeBord noted that he had recently made a presentation regarding the report at the state retirees' association conference and that he had extra copies of the presentation for those who might be interested.

At the suggestion of Mr. Stensrud, Agenda Items 15 and 16 were taken up before Item 14.

INVESTMENT MATTERS:

15. Chief Executive Officer Richard Stensrud introduced a presentation on counterparty risk in prime broker relationships, which served as a foundation for a proposed policy that would be presented to the Board.

Legal counsel Lance Kjeldgaard explained that the counterparty risk in prime broker relationships is generated when investment money is comingled with money from other clients and/or used by the prime broker as collateral for other investment activity. Mr. Kjeldgaard explained that problems can arise in recovering the funds if the prime broker fails to honor its contracts with other parties, or if the prime broker fails completely and goes into bankruptcy. Mr. Kjeldgaard noted that in such cases the creditors of the prime broker could be given priority over the underlying investors with respect to recovering funds. Mr. Kjeldgaard noted that this is what had occurred when Lehman Brothers had failed. Mr. Kjeldgaard stated that this risk primarily exists with money held by prime brokers outside the United States. Mr. Kjeldgaard noted that this risk cannot be eliminated, but it can be mitigated, it should be monitored, and guidelines for it should be established.

Jamie Feidler of Cliffwater, LLC presented an overview of hedge fund broker-dealer exposure and counterparty risk management. Mr. Feidler explained the exposure and risk involved, why the exposure and risk exists, and how Cliffwater, hedge funds, and SCERS handle this exposure and risk.

Deputy Chief Investment Officer Scott Chan reviewed the policy outlining the way SCERS Staff, Cliffwater, and hedge fund strategic partner Grosvenor Capital Management would evaluate, monitor and address the counterparty risk of hedge fund managers who utilize prime brokers in the execution of their investment strategy. Mr. Chan noted that Staff had developed a series of questions to determine the trigger points for raising concerns over the amount of counterparty risk a fund was undertaking. Mr. Chan stated that any instances of deviation or exceptions to the policy would be noted as part of the monthly compliance report presented to the Board.

Motion by Ms. Valverde to approve the proposed policy regarding the assessment of counterparty risk in prime broker relationships; Seconded by Mr. DeBord. Motion carried (7-0).

16. Chief Executive Officer Richard Stensrud presented the proposed issuance of a request for proposals for real estate consulting services.

Mr. Stensrud noted that in October 2010, the Board had approved Requests for Proposals (RFPs) for general investment, alternative assets, and real estate consulting services.

INVESTMENT MATTERS (continued):

Mr. Stensrud stated that SCERS received multiple responses to its targeted RFP for real estate consulting services, but it was determined that the first priorities would be the selection of the general investment consultant and alternative assets consultant. Mr. Stensrud explained that this was because those parties would be the principal advisors on SCERS' overall asset allocation and approach to alternative assets, respectively, and until those matters had been addressed, SCERS would not be able to properly gauge its specific needs regarding real estate consulting services. Mr. Stensrud noted that, as a result, the selection of a real estate consultant had been put 'on hold.' Mr. Stensrud explained that with the asset allocation and respective allocation levels now established, and with the developing opportunity set in the real estate asset class, it was opportune to engage a real estate consulting services specialist.

Mr. Stensrud reported that the proposed RFP for real estate consulting services had been revised to reflect that a full-time, ongoing real estate consulting relationship might not be necessary. Mr. Stensrud explained that the consultant would be needed to assist in developing a strategic plan for the real estate sub-asset class and that the strategic plan would then determine the extent of real estate consulting services required. Mr. Stensrud noted that the proposed RFP asks bidders to submit a bid based on the delivery of fixed projects, assuming that there will not be an ongoing relationship, as well as a retainer bid that includes additional services that could be provided over time.

Mr. Stensrud reported that in the interim until the real estate consultant was chosen, Staff had engaged Bard Consulting to assist in making real estate related decisions by providing a second opinion to the recommendations from the real estate managers.

Motion by Mr. Hickox to approve the proposed issuance of a request for proposals for real estate consulting services; Seconded by Mr. Kelly. Motion carried (7-0).

ADMINISTRATIVE MATTERS:

14. Paul Angelo and Andy Yeung of The Segal Company (Segal) made an educational presentation regarding actuarial funding policies.

Mr. Angelo explained that the actuarial valuation is built around certain key parameters that impact the determination of the plan's liability and the calculation of the annual contribution rates that will provide funding to address that liability. Mr. Angelo noted that those parameters – the actuarial cost method, the asset smoothing method, and the amortization policy – constitute the plan's actuarial funding policy. Mr. Angelo noted that SCERS has all three of the components of the actuarial funding policy in place, but that for various reasons, it was an opportune time to review them and to consider incorporating them into a comprehensive funding policy statement.

ADMINISTRATIVE MATTERS (continued):

Mr. Angelo explained the purpose of the actuarial cost (or funding) method. Mr. Angelo noted that SCERS is currently funded using the Entry Age Normal (EAN) method. Mr. Angelo noted that this method is the model practice for public pension plans, is considered a reasonable funding method under the Actuarial Standards of Practice and is acceptable under the current accounting standards promulgated by the Governmental Accounting Standards Board (GASB). Mr. Angelo noted that this method is most consistent with the policy goal of having the Normal Cost bear a consistent relationship to payroll, and that the recent GASB Exposure Draft of proposed rule changes would require all plans to report their liabilities using the EAN method.

Mr. Angelo noted, however, that, while SCERS' current EAN methodology will continue to be permitted under the Actuarial Standards of Practice for funding purposes, the approach will no longer be allowed for financial disclosure purposes if recently proposed accounting requirements are adopted by GASB. Accordingly, Mr. Angelo noted that Segal believes it would be advantageous to change SCERS' current practice so that the same Normal Cost can continue to be used for both financial reporting purposes and for funding purposes.

Mr. Angelo explained the purpose of the asset smoothing method. Mr. Angelo noted that in 2009, the Board conducted a comprehensive review of the asset smoothing method and decided to extend the smoothing period used to recognize investment gains or losses from five years to seven years. Mr. Angelo further noted that as of June 30, 2009, the Board decided to expand the Market Value (MVA) Corridor so that the Actuarial Value of Assets (AVA) would be allowed to vary within a range from 70% to 130% of the MVA, rather than the previous policy range of 80% to 120% of the MVA. Mr. Angelo stated that Segal believes it is reasonable for the Board to continue this asset smoothing policy adopted in 2009.

Mr. Angelo explained the purpose of the amortization policy. Mr. Angelo noted that except for a 10-year period used in the June 30, 2010 valuation to amortize the Unfunded Actuarial Accrued Liability (UAAL) for employees who participated in an Early Retirement Incentive Program (ERIP), the entire UAAL is amortized over a single "fixed" period that reduces by one year with each actuarial valuation. Mr. Angelo noted that the single period was re-set to 25 years as of the June 30, 2010 valuation and will be down to 23 years as of the June 30, 2012 actuarial valuation.

Mr. Angelo explained that many public systems have switched to a "layered" approach to amortization where each year any new amount of UAAL is amortized over a separate, fixed period. Mr. Angelo explained that this approach has the advantage of identifying the source of each dollar of current UAAL, as well as when each portion of UAAL will be fully amortized.

ADMINISTRATIVE MATTERS (continued):

Mr. Angelo stated that Segal recommends that SCERS continue to amortize its UAAL as of June 30, 2011 in a substantially single layer over its current fixed period of 24 years. Mr. Angelo further stated that Segal recommends that any new increases or decreases in UAAL be amortized over separate, multiple layers each with its own fixed amortization periods. Mr. Angelo explained that under this recommended approach, there will be a series of layers, one for the original UAAL as of June 30, 2011 and one from each year's gain or loss as well as from any other changes in the UAAL. Mr. Angelo noted that this would provide a history of sources of the plan's UAAL in any year.

Mr. Angelo discussed the appropriate amortization periods to use for different sources of UAAL and the concept of negative amortization. Mr. Angelo explained that an amortization period of less than 15 years for investment gains and losses would result in too much contribution rate volatility. Mr. Angelo noted that an amortization period over 20 to 25 years for investment gains and losses would yield higher levels of negative amortization. Mr. Angelo noted that Segal generally recommends that the Board consider amortization periods in the range of 15 to 20 years for actuarial gains and losses.

Mr. Angelo stated that the Board may want to use a different amortization period for actuarial assumption and method changes because they are changes in the long term measurement of the plan. Mr. Angelo noted that Segal believes it would be reasonable for the Board to consider using an amortization period in the range of 20 to 25 years for assumption and method changes.

Mr. Angelo stated that Segal recommends that a shorter amortization period (15 years) be utilized for UAAL attributable to plan amendments since plan amendments are within the control of the plan sponsor. Mr. Angelo noted that Segal recommends an even shorter default amortization period for a retirement incentive offer (e.g., five years) so that the additional cost for such an offer is borne during the period when the plan sponsor contends it will benefit from offering it. Mr. Angelo further noted that GASB is calling for a short period for retirement incentives in its recent proposed rule changes.

Mr. Angelo discussed the amortization period that should be used when the plan has a surplus (i.e., is more than 100% funded). Mr. Angelo explained how Normal Cost is calculated when the plan has a surplus and noted that too short an amortization period would result in a partial 'contribution holiday.' Mr. Angelo noted that important lessons had been learned about the risks of such an outcome, and accordingly, Segal recommends that a 30 year rolling amortization period be used for any surplus.

Mr. Angelo stated that the impact of the recommended modification to the Entry Age Normal cost method would be to increase the average employer contribution rate by 0.4% of payroll. Mr. Angelo stated that the individual Basic member contribution rates would

ADMINISTRATIVE MATTERS (continued):

remain unchanged, while the COLA member contribution rates would increase by around 0.1% of payroll.

Mr. Angelo explained that it is not possible to quantify in advance the full future cost impact associated with adopting any of the alternative amortization periods because the plan's future changes in UAAL are not yet identified. Mr. Angelo noted, however, that the neighborhood of the potential cost impact could be estimated by looking at how the cost would vary if the remainder of the unrecognized investment losses from the 2007-2009 investment market collapse was amortized at 15 and 20 years, respectively. Mr. Angelo explained that over the next six valuations, the increase in the annual payroll cost required to amortize the net investment losses would be about 0.2% of payroll per year if amortized over 20 years, and about 0.6% of payroll per year if amortized over 15 years. Mr. Angelo noted that under the current amortization policy the projected cost would be somewhere in this range, since the amortization period would decrease from 24 to 19 years during this period.

Discussion followed.

It was agreed that a proposed actuarial funding policy would be prepared and presented for the Board's formal consideration at an upcoming Board Meeting.

Motion by Mr. Hickox to receive and file the presentation by The Segal Company regarding the components of an actuarial funding policy; Seconded by Mr. Kelly. Motion carried (7-0).

The meeting was adjourned at 4:06 p.m.

MEMBERS PRESENT: James A. Diepenbrock, John B. Kelly, William D. Johnson, Winston H. Hickox, Kathy O'Neil, Julie Valverde, and Michael DeBord.

MEMBERS ABSENT: Diana Gin, Nancy Wolford-Landers, and John Conneally.

OTHERS PRESENT: Richard Stensrud, Chief Executive Officer; Lance Kjeldgaard, outside counsel; Kathryn T. Regalia, Chief Operations Officer; John W. Gobel, Sr., Chief Benefits Officer; Scott Chan, Deputy Chief Investment Officer; Steve Davis, Investment Officer; Suzanne Likarich, Retirement Services Manager; Thuyet Ziyalan, Accounting Manager; John Lindley, IT Administrator; Pete Keliuotis, Strategic Investment Services, Inc; Jamie Feidler, Cliffwater, LLC; Paul Angelo and Andy Yeung, The Segal Company; Paul Hight, Sacramento County Risk Management; Tara Maeller, Sacramento Metropolitan Fire District; and Victor Pierce.

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.