

SAN BERNARDINO COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

The regular meeting of the San Bernardino County Employees' Retirement Board was held February 4, 2010, in the Board of Retirement Board Room, 348 West Hospitality Lane, First Floor, San Bernardino, California.

Those present were:

ELLEN WEISSER, Appointed Member (Chairman)
 DAWN STAFFORD, General Member (Vice Chairman)
 ANNETTE KERBER, Assistant Treasurer
 CHRISTOPHER LEGGIO, Appointed Member
 ROBERT MCDONALD, Retired Member
 DON NEELY, General Member
 MARVIN REITER, Appointed Member
 PAUL RUSS, Appointed Member
 DAVID WILLIAMS, Safety Member
 BRET HENRY, Alternate Member

Also present were:

TIMOTHY BARRETT, Executive Director/CIO
 LANCE KJELDGAARD, Chief Counsel
 CHRISTIE PORTER, Chief Member Services
 MICHAEL O'KELLY, Chief Fiscal Services
 BRIAN LONG, Investment Officer
 JAMES PERRY, Investment Officer
 DONALD PIERCE, Investment Officer
 CAROL FENN, Recorder

1. Chairman Weisser called the meeting to order at 9:00 a.m.

Reiter moved, Russ seconded, to move items 12 - 17 to the end of the meeting. Motion carried.

CONSENT:

Russ moved, Stafford seconded, to approve the consent items as follows:

2. Approve minutes of regular meeting of January 4, 2010.

3. Service Retirements:

	<u>Effective</u> <u>Date</u>
ANDERSON, Margaret M.	District Attorney (Def) 01/30/10
ANDERSON, Mary E.	Auditor/Controller-Rec. 01/30/10
BEEEMER, Richard A.	Sheriff 01/30/10

BRADEN, Gerald T.	Museum	01/16/10
BRICKER-BARRETT, Nannette M.	Library	03/13/10
CARRERA, Julie J.	Special Districts (Def)	12/21/09
CRUZ, Maria I.	SCAQMD	02/27/10
ERICKSON, Richard H.	Library	03/13/10
ERTER, Sharon	ARMC (Def)	01/19/10
GASTON, Ronald	Public Health	01/25/10
GLASSER, Stephen	Child Support Services	02/27/10
GRESSMAN, Carol L.	Behavioral Health (Def)	01/21/10
GRIFFITH, Margaret H.	Library	02/13/10
JOHNSON, John L.	Sheriff	02/27/10
MALONE, Paul	Mojave Desert AQMD	01/30/10
MOLDOVAN, Joan	Probation (Def)	01/04/10
OCHOA, Lori D.	Sheriff	01/16/10
ORR, Melanie M.	ARMC	02/13/10
PATRICK, Gayle	Preschool Serv. (Def)	01/19/10
REDMAN, Deborah H.	SCAQMD (Def)	01/14/10
SHELBY, Darryl	ARMC	02/13/10
SHELBY, Joann M.	ARMC	02/13/10
TEMBY, Patricia	Human Services	02/13/10
THOMPSON, Jaynie M.	Probation (Def)	04/08/09
TRUJILLO, Amy V.	Superior Court (Def)	12/31/09
TRUSS, Janice W.	Human Services	01/30/10
TURNER, Norice E.	Parks & Recreation	02/13/10
VILLANUEVA, Yolanda	Human Resources	01/30/10
ZABALA, Armando B.	ARMC (Def)	01/07/10

4. Staff Travel:

- a. Approve the attendance of Michael B. O'Kelly to the GFOA 104th Annual Conference, to be held in Atlanta, GA on June 6 - 9, 2010.

5. Disability Applications - Initial Decision:

- a. BOWLING III, Rufus

To approve staff recommendation that:

1. Mr. Bowling is permanently incapacitated for the performance of duties and disability retirement be granted.
2. Mr. Bowling's disability is service-connected based on herniated lumbar disc with pressure on nerve.
3. Medical review is recommended in 12-18 months as specified by the medical advisor.

4. Staff shall initiate disability benefit payments with an effective date of November 21, 2009, the day after the last date compensated.

b. HUGHES, Betty C.

To approve staff recommendation that:

1. Ms. Hughes is permanently incapacitated for the performance of duties and disability retirement be granted.
2. Ms. Hughes' disability is nonservice-connected based on heart disease, sleep apnea and major depression.
3. Ms. Hughes is not capable of gainful employment.
4. No medical review is necessary as specified by the medical advisor.
5. Staff shall initiate disability benefit payments with an effective date of August 13, 2009, the date of application.

6. Disability Applications - Writ of Mandate:

a. HESS, Nina

Based on the Notice of Entry of Judgment:

1. Petition for Writ of Mandate is granted.
2. Petitioner is granted a service-connected disability retirement commencing on the same date as her previously granted nonservice-connected disability retirement, with interest at the legal rate on all retroactive amounts.
3. Petitioner shall recover costs in this action as set forth in an appropriate cost bill.

Motion carried.

CLOSED SESSION

DISABILITY APPLICATIONS - [Article 1, Section 1, California Constitution (Right to Privacy) and California Government Code Section 54957]:

7. Initial Decision:

a. LO CURTO, James

Russ moved, Neely seconded, to approve staff recommendation that:

1. Mr. Lo Curto is not permanently incapacitated for the performance of duties based on degenerative joint disease with bilateral hip replacement.
2. Disability retirement be denied.
3. If a disability retirement is determined at a future hearing stage, the effective date will be June 11, 2009, the date of application.

Motion carried.

b. WILLIAMS, Renita

Russ moved, Neely seconded, to continue to the March Board meeting. Motion carried.

8. Expedited Administrative Review:

a. BROCKMAN, Carol J.

Leggio moved, Russ seconded, to approve staff recommendation to approve and adopt the proposed findings and the recommendations of the hearing officer to deny service-connected disability retirement. Motion carried.

b. OJEDA, Ramiro

Stafford moved, Russ seconded, to approve staff recommendation to approve and adopt the proposed findings and the recommendations of the hearing officer to grant service-connected disability retirement. Motion carried.

CONFERENCE WITH LEGAL COUNSEL

9. Anticipated Litigation: Government Code Section 54956.9(c) - One Case

OPEN SESSION

10. O'Kelly reviewed the annual retiree cost of living adjustment. McDonald moved, Stafford seconded, to approve the

annual retiree cost of living adjustment of 2.00%, effective April 1, 2010. Motion carried.

11. Allan Martin, New England Pension Consultants, reviewed their Quarterly Investment Performance Review for the period ending December 31, 2009.

The Chairman called a recess at 10:15 a.m. The meeting resumed at 10:28 a.m.

18. Long provided an update on the Apollo European Principal Finance Fund - Webb V Co-Investment.

19. Administrative Committee Report.

- a. Neely reported on the meeting conducted January 19, 2010.
- b. Leggio moved, Russ seconded, to approve the memorandum of understanding with San Bernardino County regarding County services. Motion carried.

20. Leggio moved, Russ seconded, to approve the attendance of Don Neely and Dawn Stafford to the Information Management Network (IMN) 2010 Securities Lending Summit, to be held in San Diego, CA on February 7 - 10, 2010. Motion carried.

21. Leggio moved, Russ seconded, to approve the attendance of Tim Barrett, Christopher Leggio, Ellen Weisser and Bret Henry to the IMN Distressed Investment Summit, to be held in Huntington Beach, CA on March 1 - 3, 2010. Motion carried.

22. Leggio moved, Russ seconded, to approve the attendance of Brian Long, Don Neely and Dawn Stafford to the Institutional Investor Global Real Assets Investment Forum, to be held in New York, NY on March 2 - 3, 2010. Motion carried.

23. Leggio moved, Russ seconded, to approve the attendance of Don Neely to RREEF Americas Real Estate Fund Conference, to be held in San Francisco, CA on March 17 - 18, 2010. Motion carried.

24. Leggio moved, Russ seconded, to approve the attendance of Don Neely, Paul Russ, Dawn Stafford, and Ellen Weisser to the Institutional Investor Institute and Hedge Fund Institutional Forum Public Funds Roundtable, to be held in Austin, TX on April 21 - 23, 2010. Motion carried.

25. Leggio moved, Russ seconded, to approve travel for Brian Long to attend 2010 Advisory Board meetings for Neuberger Berman Secondary Fund, Partners Group European Secondary Fund, Timbervest Partners Fund II and Timbervest Crossover Partners. Motion carried.

26. No reports of conferences attended were made.

27. Staff Reports:

- a. Barrett discussed items on his written report covering significant administrative events during January.
- b. Kjeldgaard reviewed guidelines regarding gift of travel.
- c. O'Kelly discussed the Administrative Expenses - Second Quarter Budget vs. Actual for Fiscal Year 2009/2010

12. Barrett reviewed the revised SBCERA Statement of Strategy. Weisser recommended an additional revision. Kerber moved, Russ seconded, to approve the SBCERA Statement of Strategy as revised. Motion carried.

13. Barrett reviewed the revised SBCERA Business Plan. The Board recommended some additional revisions. Kerber moved, Russ seconded, to approve the SBCERA Business Plan as revised. Motion carried.

The Chairman called a recess at 11:27 a.m. The meeting resumed at 11:35 a.m.

14. Barrett reviewed the creation of the OPEB Trust and startup costs of the OPEB Trust pursuant to SB11.

The Chairman called a lunch recess at 12:15 p.m. The meeting resumed at 12:45 p.m.

Barrett stated that the SBCERA Board could choose, or not, to create an OPEB Trust pursuant to the new legislation, SB-11. If the SBCERA Board chose to create the OPEB Trust, the Board could also fund the start-up-costs and initial administrative expenses of the OPEB Trust if it determines this is in the best interest of the system members.

Barrett reviewed Government Code Section 31699.9(b), which states "The establishment of the postemployment health fund will enable the sharing of expenses of administration and investments, bringing economies of scale and better use of investment expertise to the retirement system. Consequently, the retirement system board may pay the startup and initial administrative expenses for the fund if the retirement system board determines that this expenditure is in the long-term best interests of the members and beneficiaries of the retirement system, and the employers that participate in the system. The Board may also assess participating agencies and trust for all or a portion of those expenses."

Barrett presented three start-up funding options. In Option 1, the start-up-costs and initial administrative expenses for an OPEB Trust with a strategy using an investment platform that included risk management software designed by the platform provider were estimated to be \$2,718,907. In Option 2, the start-up-costs and initial administrative expenses for an OPEB Trust with a strategy using an investment platform custom built by SBCERA without risk management software was estimated to be \$1.5 million. In Option 3, the start-up-costs and initial administrative expenses for an OPEB Trust with a silo investment strategy were estimated to be \$868,907.

Barrett reviewed an OPEB Platform feasibility study by HedgeMark International, which presented details of Options 1 and 2.

Barrett reviewed a proposed budget and feasibility study by SBCERA staff, which presented the details of Options 1, 2 and 3.

Barrett reviewed the background and assumptions underlying these options. The Governor's OPEB Commission identified \$118 billion in unfunded OPEB liabilities in California. GASB requires that these liabilities be identified and carried on the financial statements of public entities. Unfunded liabilities affect a public entity's ability to raise money, so it is in the best interest of public entities to prefund OPEB liabilities. The rating agencies have begun to ask for information about what public agencies are doing to deal with this liability - reinforcing that not prefunding these liabilities will ultimately affect an agency's credit rating. The Governor's OPEB Commission unanimously recommended that public agencies prefund OPEB liabilities. Because of the economic downturn very few, if any, public entities are prefunding OPEB liabilities currently. However, as the economy improves and the current low interest rate environment persists, public entities are expected to start raising money through bonding to fund these liabilities.

At the present time, public entities may only invest their OPEB funds with money managers or CALPERS. The proposed OPEB Trust has advantages over either of these existing alternatives. As to money managers, the OPEB Trust would not be making a profit, so the cost of investing OPEB assets would be substantially less than that charged by money managers. As to CALPERS, this OPEB Trust would be an alternative for public entities that do not want to invest with CALPERS. Succinctly stated, public entities who want an alternative to CALPERS but who don't want to pay the higher fees of money managers would be attracted to the SBCERA OPEB Trust.

Barrett discussed a proposed OPEB start-up budget, using each of the three options, to show that SBCERA would recoup the OPEB start-up-costs and initial administrative expenses over a five year period if the OPEB Trust raised \$5 billion. Consultant Allan Martin asked the Board what minimum amount of OPEB funds would have to be placed in the OPEB trust each year over a five year period in order for the SBCERA to recoup start-up costs of \$2.7 million. Barrett stated that the OPEB Trust could recoup the SBCERA start-up-costs and initial administrative expenses of \$2.7 million in five years if the OPEB Trust obtained only \$60 million each year for the five year period and assessed participating agencies 0.3% per year for recoupment. Barrett stated that if the economy improves there will be a window where interest rates remain

attractive and most, if not all, public entities will see a golden opportunity to float bonds and fund these unfunded liabilities. It is important to note that public entities need to get these unfunded liabilities off their financial statements. Barrett stated that CALPERS raised approximately \$1.5 billion in OPEB assets in the last couple of years, even though the markets have been bad. Therefore, it is reasonable to believe that the OPEB Trust could raise \$60 million per year for five years. This amounts to less than 1% of the estimated OPEB liabilities in California.

The Board discussed the three proposed funding options. Reiter noted that if the assumption about raising interest rates was correct, then the conclusion that the start-up costs and initial administrative expenses for Option 1 could be recouped over five years was also reasonable. Reiter further opined that if the OPEB Trust wanted to attract public agencies to participate in the OPEB Trust, that Option 1 with a strategy using an investment platform with embedded risk management software was a better choice than either of the other two options. Barrett agreed, stating that the OPEB Trust, like SBCERA, would have an investment strategy that managed downside risk rather than trying to capture the volatile upside return. Considering the current financial crisis, having risk management software to assist in managing downside risk was an advantage not provided by other options. Reiter explained that having risk management software to evaluate the interrelated downside risk of disparate asset classes was a selling point to attract OPEB money from public entities since many fiduciaries are now evaluating investments based on risk analysis as a standard part of their investment review.

Reiter asked what would be the benefit to the SBCERA members, beneficiaries, and employers if the Board adopted the OPEB Trust and funded the start-up costs. Barrett stated that adopting the OPEB Trust would result in fee compression, economies of scale, and reduced net cost through cost sharing. Reiter asked what the specific benefit would be to the SBCERA members, beneficiaries, and employers if the fee compression and economies of scale were not realized. Barrett stated that adopting the OPEB Trust would result in cost sharing for SBCERA on investment and legal expenses both as to staff and outsider contractors. Barrett continued that on a very, very conservative basis, the cost saving to SBCERA would be at least 15% of investment and legal staff costs, which he stated would be at a minimum \$175,000 per annum to

begin with and increase year by year over time. In addition, the cost sharing for outside legal fees, at least as to investments in which both SBCERA and the OPEB Trust both participated, would be around \$10,000 to SBCERA per contract. Depending on the number of transactions, conservatively this amounts to \$150,000 per year. Again, legal costs increase over time, so this cost savings on outside legal fees would increase over time as well. Reiter agreed that if SBCERA recouped its initial start-up costs over five years, then the ongoing cost savings were a definite specific benefit to the SBCERA members, beneficiaries, and employers

Barrett reviewed the proposed OPEB Timeline.

Kjeldgaard stated that pursuant to advice of outside counsel, the Law Firm of Hanson Bridgett, SBCERA may account for the expenditure of money for OPEB start-up-costs and initial administrative expenses from the fund assets pursuant to specific authorization under Government Code Section 31699.9(b) if the Board determines that this expenditure is in the long-term best interests of the members and beneficiaries of the retirement system, and the employers that participate in the system.

Kjeldgaard reviewed a memo by outside counsel, the Law Firm of Hanson Bridgett, discussing the legal risks for SBCERA in establishing and maintaining an OPEB Trust. Kjeldgaard also reviewed a memo by outside counsel, the Law Firm of K&L Gates, discussing the SEC issues and risks associated with managing other public agencies' money in an OPEB Trust. Kjeldgaard stated that these memos identified legal risks and showed how the legal risks can be mitigated, although not completely mitigated, either through careful drafting of the OPEB Trust or through on-going due diligence. Williams asked whether anything could be done to ensure there were no legal risks in the creation and maintenance of the OPEB Trust. In other words, could these risks be 100% mitigated? Kjeldgaard responded in the negative, the legal risks associated with establishing and maintaining an OPEB Trust can only be mitigated to a point and that there was no way to completely remove the legal risks. Kjeldgaard pointed out that the Board understands investment risks and mitigates those as well.

Kjeldgaard reviewed the proposed Declaration of OPEB Trust and the Resolution which would adopt the OPEB Trust and approve the OPEB start-up costs.

The Board asked that the Resolution include a requirement that quarterly reports be provided by the OPEB Trust to the SBCERA Board showing progress and the expenditure of funds, as well as a quarterly report from the SBCERA Executive Director showing how the start-up-costs and initial administrative expenses were being recouped.

Russ moved, Kerber seconded, to approve the startup costs of the OPEB Trust up to \$2,718,907, to adopt the OPEB Resolution, and to adopt the OPEB Declaration of Trust. Motion carried.

15. Barrett reviewed the OPEB Project Timeline. Step 1) Due Diligence and Fiduciary Duty Findings; Step 2) Establish the OPEB Fund; and Step 3) Review and Adopt OPEB Budget. Russ moved, Reiter seconded, to approve the OPEB Project Timeline. Motion carried.
16. Kjeldgaard reviewed the contract amendment with Delta Partners. Russ moved, Stafford seconded, to approve Contract Amendment No. 3 with Delta Partners. Motion carried.
17. Kjeldgaard reviewed the Legal Agreement between SBCERA and Platinum Advisors. Russ moved, Stafford seconded, to approve the Legal Agreement between SBCERA and Platinum Advisors. Motion carried.
28. The Chairman invited public comment. No public comment was provided.

There being no further business, the meeting adjourned at 1:38 p.m.

Respectfully submitted,

ELLEN WEISSER, Chairman

TIMOTHY BARRETT, Secretary

DATED _____