



MINUTES

RETIREMENT BOARD MEETING MINUTES

SECOND BOARD MEETING

April 27, 2016

9:00 a.m.

Retirement Board Conference Room

The Willows Office Park

1355 Willow Way, Suite 221

Concord, California

Present: Debora Allen, Candace Andersen, Scott Gordon, Brian Hast, Jerry Holcombe, Louie Kroll, John Phillips, William Pigeon, Todd Smithey, Jerry Telles and Belinda Zhu (Deputy Treasurer, present and voting in Russell Watts' absence)

Absent: Gabe Rodrigues, Russell Watts

Staff: Gail Strohl, Chief Executive Officer; Timothy Price, Chief Investment Officer; Karen Levy, General Counsel; Wrally Dutkiewicz, Compliance Officer; Christina Dunn, Administrative/HR Manager; Timothy Hoppe, Retirement Services Manager; and Alexis Cox, Member Services Manager

Outside Professional Support:

Harvey Leiderman

Paul Angelo

Eva Young

Ed Hoffman

Representing:

Reed Smith LLP

Segal Consulting

Segal Consulting

Verus Consulting Group

1. **Pledge of Allegiance**

Gordon led all in the *Pledge of Allegiance*.

2. **Accept comments from the public**

There were no comments from the public.

3. **Approval of Minutes**

It was M/S/C to approve the minutes of the February 25, 2015 Board meeting. (Yes: Allen, Andersen, Gordon, Hast, Phillips, Smithey, Telles and Zhu)

4. **Presentation from Segal Consulting: Review of Economic Actuarial Assumptions** – Paul Angelo and Eva Young

Angelo reviewed the Economic Assumptions noting the expected return on assets is the most important assumption and salary increases are the next important. He reviewed the difference between demographic assumptions and economic assumptions. He also reviewed a selection of actuarial assumptions.

Pigeon was present for subsequent discussion and voting.

Angelo reviewed the Economic Actuarial Assumptions for the December 31, 2015 Actuarial Valuation highlighting the following recommendations:

Inflation – Future increases in the Consumer Price Index (CPI) which drive investment returns and active member salary increases, as well as COLA increases to retired members.

Recommendation: Reduce the rate from 3.25% to 3.00% per annum. Segal also recommends decreasing the assumed COLA for those tiers with a 4.00% maximum COLA from 3.25% to 3.00% per year.

Angelo noted the CPI is used throughout all entities and is not specific to CCCERA. Trustee Allen asked if the National Association of State Retirement Administrators (NASRA) publishes other numbers besides the median. Zhu asked if the 3% median inflation assumption is a nationwide number. Angelo noted the CPI is a national number, not a local number.

Investment Return – The estimated average future rate of return, net of investment expenses, on current and future assets of CCCERA as of the valuation date. This rate is used to discount liabilities.

Recommendation: Maintain the investment return assumption at 7.25% per annum. He also recommends moving from net of administrative expenses to gross of administrative expenses.

Individual Salary Increases – Increases in the salary of a member between the date of the valuation and the date of separation from active service. This assumption has three components: inflationary salary increases, real “across the board” salary increases, and merit and promotional increases.

Recommendation: Reduce the current inflationary salary increase assumption from 3.25% per annum to 3.00% per annum and reduce the current real “across the board” real wage growth assumption from 0.75% to 0.50%. This means the combined inflationary and real “across the board” wage inflation will decrease from 4.00% to 3.50%. The merit and promotional increase assumption ranges from a 0.75% to 9.50% for General and 0.75% to 10.0% for Safety. The merit and promotional increases will be reviewed as part of the triennial experience study of non-economic assumptions.

Angelo reviewed investment earnings assumptions noting it is also known as the discount rate. He discussed how the earnings assumptions are set: inflation, real returns by asset class, reduced by assumed expenses, and reduced by risk adjustment. There was a lengthy discussion on the assumed expenses and the risk adjustment. He described how Segal arrives at the assumed inflation as compared to other entities, i.e. Social Security and investment consultants.

He reviewed when the earnings assumption should be changed. There was a discussion on how the change in our asset allocation will affect the assumptions over time. Angelo reviewed the trend of risk adjustment and corresponding confidence level. There was also a discussion on the standard deviation decrease from 12.44% to 10.80%.

Angelo reviewed how the investment return assumptions are used in GASB 67 and 68 financial reporting noting they use a smoothed value basis and not a market value basis. He stated CCCERA currently sets the investment return assumption for funding on a net of administrative expenses basis and he is recommending we set the investment return assumption for funding on a gross of administrative expenses basis. This would be the equivalent of about \$7 million annually, or 1.0% of payroll and .77% would be allocated to the employer and .23% would be allocated to the member.

5. **Consider and take possible action to adopt the economic assumptions recommended by Segal Consulting to be utilized in the December 31, 2015 actuarial valuation report**

It was M/S to establish the assumed inflation rate at 2.75% and the assumed investment return at 7.00% and defer the GASB discussion with respect as to how to handle the administrative expense load. The Board discussed the motion noting there may be an increase in contribution rates for both the employers and the employees as well as the effects of recently changing the asset allocation which includes a 7.25% assumed investment return.

A substitute motion was M/S to follow Option A recommendations for both funding and financial reporting as stated in Slide 25 which sets the inflation rate at 3.00% and the assumed investment return at 7.25%. Angelo noted that in June when they do the demographic assumption review they will be recommending a longer mortality table which will increase costs. Leiderman asked the Board to focus on risk adjustment and timing and to look at what their comfort level is. (Yes: Hast, Pigeon, Smithey and Telles. No: Allen, Andersen, Gordon, Phillips and Zhu). Motion Failed.

The original motion was clarified: It was M/S/C to establish the assumed inflation rate at 2.75% and the assumed investment return at 7.00% and defer the GASB discussion with respect as to how to handle the administrative expense load. (Yes: Allen, Andersen, Gordon, Phillips and Zhu. No: Hast Pigeon, Smithey and Telles). Motion Passed.

It was M/S/C to continue the administrative portion to a future meeting for a deeper analysis. (Yes: Allen, Andersen, Gordon, Hast, Phillips, Pigeon, Smithey, Telles and Zhu).

6. **Presentation and recommendation from Verus on Updated Asset Allocation and Implementation Plan**

Hoffman reviewed an analysis of the asset allocation decisions based on updated capital market assumptions. He stated the forecast of the 10-year return in the current policy is set to generate 7.1%, in 2015 and 7.2% in 2016; it is 7.9% with the standard deviation going from 12.1% to 11.0%. He reviewed three different scenarios that would generate a higher return, 7.6%, 7.5% and 7.6%, with lower risk, 10.3%, 9.8%, and 9.6% respectively. Examples of changes in allocations would be a decrease in emerging markets from 14% to 10%, an increase in US Treasury, not investing in core real estate, an increase in value-add real estate and opportunistic real estate, and a decrease in private equity and private credit.

He reviewed risk diversifying strategies noting they are designed to have low correlations with traditional asset classes. Risk diversifying strategies currently in the CCCERA portfolio include AFL-CIO, PIMCO All Asset, and Wellington Real Return. He also reviewed hedge funds noting they haven't been a favorable place to invest in the past 5 years but that has changed. He stated operational due diligence is the key as each hedge fund is unique and they have partnered with Aksia to assist in the due diligence noting they have 100 people dedicated to reviewing hedge funds. He reviewed the different styles of hedge funds: alternative beta, event driven, long/short equity, Commodity Trading Advisor (CTA) and global macro, and relative value.

Pigeon was no longer present for subsequent discussion and voting.

Hoffman defined risk parity as a long-only portfolio seeking to generate returns through persistent exposure to global equity, global fixed income, and global inflation-protected assets noting it seeks balanced exposure for consistent performance across market environments. The risk parity approach uses leverage to adjust the volatility of each asset class to the same level and weights the asset class exposures so that each asset class contributes an equal amount of expected volatility to the portfolio. He gave an update on implementation milestones including establishing overlay and transition

management providers, establish liquidity strategy, transition assets among public equity and fixed income strategies to begin migrating current portfolio to target asset allocation, conduct education & searches for new mandates, and identifying holding strategies suitable for achieving risk/return characteristics until capital is called into illiquid strategies. He also reviewed the approach to private markets noting there are different models that need to be evaluated separately. He also noted the Verus office in San Francisco provides private market consulting and to avoid any conflicts CCCERA staff will be reviewing the models and making recommendations to the Board.

Hoffman and Price asked the Board for direction on which asset allocation model, A, B or C, to use for the investment policy statement. Price noted that his preference was for Option B.

It was M/S/C to give direction to staff to proceed with Option B. (Yes: Allen, Andersen, Gordon, Hast, Phillips, Smithey and Zhu. No: None. Abs: Telles).

7. **Consider and take possible action to adopt governance models as recommended by Verus, including delegation of authority of the following investment functions to CCCERA staff:**

Hoffman gave an overview of the items objectives noting there will be discussion on rebalancing, managing managers and obtaining direction from the Board to be able to develop policy language. He gave a recap of the current status of the preferred governance model noting the Board is moving from a Board-dominant model to a team-based model. He reviewed the investment policy development principles including the delegation of duties. He also reviewed the current structure of the investment policy statement and the potential structure highlighting the Governance section.

Pigeon was present for subsequent discussion and voting.

He reviewed the benefits of delegation. He discussed the potential adjustments to the rebalancing policy noting rebalancing can occur at any time as opposed to semi-annually to maintain policy targets.

It was M/S to approve the recommended change to current policy to include the potential adjustments reflected on the right column of page 9 and that the delegation would be to the Chief Investment Officer and staff for these adjustments with a detailed statement of policy and suggested ranges to be brought back to the Board.

There was a discussion on the differences between maintaining policy targets and effecting tactical tilts. Hoffman noted that tactical tilts are away from policy and would require Board approval.

An amended motion was M/S to approve the recommended change to current policy to include the potential adjustments reflected on the right column of page 9 and that the delegation would be to the Chief Investment Officer for these adjustments with a detailed statement of policy and suggested ranges to be brought back to the Board.

Pigeon was no longer present for subsequent discussion and voting.

The motion was restated. It was M/S/C to provide direction to staff and Verus to develop the policy change recommendations identified on page 9 of the Verus report on the right hand column for both maintenance of policy targets or effecting tactical tilts with the understanding that in bringing it back we are giving direction for Verus to develop proposed Board established ranges to be determined along with a definitive final policy document. (Yes: Allen, Andersen, Gordon, Hast, Phillips, Smithey, Telles and Zhu)

Hoffman briefly reviewed the current policy on hiring new managers. He reviewed a potential policy which would: 1) give staff the authority to hire new managers up to a pre-defined limit; 2) provide a detailed report to the Board prior to execution of investment manager agreement which would provide an opportunity for negative consent; 3) Board members may participate in on-site due diligence visits; and 4) assignments greater than \$100 million will follow the standard search process. He also reviewed investing in follow-on funds and if there should be a dollar limit on it. The Board felt there should be a dollar limit. The Board discussed the potential new delegation of staff hiring new managers and then reporting to the Board as well as the Board's involvement in hiring new managers. The Board asked what the process would be if they become aware of a fund they would like staff to review. Price reported it would be the same. They currently have a work flow process in place and will continue to use the process. He noted they would be reporting to the Board monthly.

It was M/S/C to provide direction to the Chief Investment Officer ("CIO") and Verus to develop a policy for investment manager hires that is both for manager selection in the implementation of established asset allocations as well as for investment in follow-on funds, and for each of those two categories, that the CIO would be given authority to hire new managers up to a predefined limit to be established in a recommendation from staff and Verus back to the Board, currently exemplified at \$100 million, that the hiring of new managers would provide for a detailed reporting to the Board prior to execution of investment manager agreements subset so that the Board has the opportunity to not approve. Board members should be allowed and may participate in any on-site due diligence visits, and any hiring of new managers above a predetermined limit would follow the standard search process. For follow-on funds, in addition to what is in writing, that the CIO would be given the authority to make additional new investments for follow-on funds with a predetermined dollar limit. In all respects, that this policy would be brought back to the Board so that we can have a definitive policy and established ranges and predetermined limits. (Yes: Allen, Andersen, Gordon, Hast, Phillips, Smithey and Telles. No: None, Abs.: Zhu)

Hoffman reviewed the current policy on manager terminations and the potential updates.

It was M/S/C to provide direction to Verus and the CIO to develop a policy update on manager termination which is the policy update reflected on page 13 of the Verus report with the following addition to Normal Circumstances a new Number 1: CIO to determine if manager under review and notify the Board; and thereafter Number 2: CIO has the authority to terminate a manager; and Number 3: a detailed report to the Board prior to termination provides opportunity for Board approval or disapproval. Under Emergency Situations, Number 1: the Chair and CEO would be notified immediately by the CIO by all available means; Number 2: the CIO given authority to terminate and find suitable short-term alternative; and bullet 3: CIO presents long-term remediation plan to Board as soon as practical, thereby providing opportunity for negative consent (i.e. veto). (Yes: Allen, Andersen, Gordon, Hast, Phillips, Smithey and Telles. No: None. Abs.: Zhu)

8. Presentation from Verus on Angelo Gordon personnel changes

Hoffman gave an update on personnel changes at Angelo Gordon noting they appear to have a large, stable organization. However, they will continue to monitor the firm.

9. Consider authorizing the attendance of Board and/or staff:

- a. It was M/S/C to authorize the attendance of 1 Board member and 2 staff members at the California Public Plan Roundtable, PIMCO, May 9, 2016, Newport Beach, CA. (Yes: Allen, Andersen, Gordon, Hast, Phillips, Smithey, Telles and Zhu)

- b. It was M/S/C to authorize the attendance of 2 Board members and 2 staff members at the A Road Map for Growing Your Institution's Investment Assets, Commonfund, May 16, 2016, San Francisco, CA. (Yes: Allen, Andersen, Gordon, Hast, Phillips, Smithey, Telles and Zhu)
- c. It was M/S/C to authorize the attendance of 2 Board members and 2 staff members at the 2016 Adams Street Partners Client Conference, Adams Street Partners, June 1-2, 2016, Chicago, IL. (Yes: Allen, Andersen, Gordon, Hast, Phillips, Smithey, Telles and Zhu)
- d. It was M/S/C to authorize the attendance of 1 Board member and 1 staff member at the Equilibrium's Fifth Annual Forum, Equilibrium, June 16, 2016, San Francisco, CA. (Yes: Allen, Andersen, Gordon, Hast, Phillips,, Smithey, Telles and Zhu)
- e. It was M/S/C to authorize the attendance of 1 Board member and 1 staff member at the DBL 2016 Annual Meeting, June 16-17, 2016, San Francisco, CA. (Yes: Allen, Andersen, Gordon, Hast, Phillips,, Smithey, Telles and Zhu)
- f. It was M/S/C to authorize the attendance of 3 Board members at the 2016 Trustees and Administrators Institute, IFEBP, June 27-29, 2016, Las Vegas, NV. (Yes: Allen, Andersen, Gordon, Hast, Phillips,, Smithey, Telles and Zhu)
- g. It was M/S/C to authorize the attendance of 2 Board members at the International and emerging market Investing, IFEBP, July 25-27, 2016, San Francisco, CA. (Yes: Allen, Andersen, Gordon, Hast, Phillips,, Smithey, Telles and Zhu)
- h. It was M/S/C to authorize the attendance of 1 staff member at the Principles of Pension Management, CALAPRS, August 9-12, 2016, Malibu, CA. (Yes: Allen, Andersen, Gordon, Hast, Phillips, Smithey, Telles and Zhu)
- i. It was M/S/C to authorize the attendance of 3 Board members at the Public Pension Funding Forum, NCPERS, August 21-23, 2016, New Haven, CT. (Yes: Allen, Andersen, Gordon, Hast, Phillips, Smithey, Telles and Zhu)

10. Miscellaneous

(a) Staff Report –

Strohl read the following for the record:

The Board met in closed session pursuant to Govt. Code Section 54956.81 to consider the sale of a particular pension fund investment on December 9, 2015, Agenda Item No. 6. In accordance with Govt. Code Section 54957.1(a)(7), the Board reports as follows: It was M/S/C to sell the Willows Office Park to Graham Street Realty for a gross purchase price of \$8.55 million, subject to Graham Street's due diligence, and to authorize the CCCERA CEO to execute all necessary documents. (Yes: Allen, Andersen, Gordon, Hast, Phillips, Rodrigues, Smithey, Telles and Watts)

Strohl reported we have added an afternoon session for group counseling to accommodate members;; and, we are in the process of preparing the CAFR and asked the Board if they are comfortable with having their pictures in the CAFR.

Zhu was no longer present for subsequent discussion and voting.

Dutkiewicz reported he is continuing to update procedures and controls in the member services and benefits departments; and, we have re-engaged with our pension administration system vendor.

Price reported Verus made a modest revision in the positive direction to the 4th quarter report due to missing cash flow data. Strohl added the information was provided to Segal who then produced 5-year projected contribution rates that we provided to the employers. Based on the new data there may or may not be revised letters sent out.

Levy reported SACRS has published their 2016 edition of the lawbook, which includes the 1937 Act, PEPRA, and other statutes. It is available in electronic format and will be sent to all Trustees. Hard copies are also available. A memo was previously presented to the Board outlining the changes in the law effective January 1, 2016.

(b) Outside Professionals' Report -

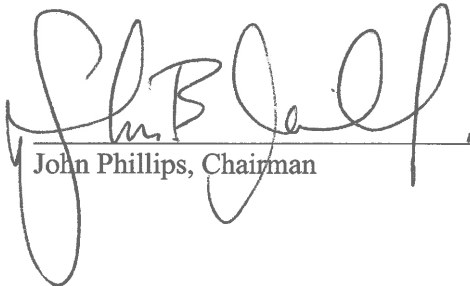
None

(c) Trustees' comments –

Phillips reported he has formed an Ad Hoc CEO Compensation Committee. Phillips is the Chairman, Hast is the Vice Chair, and Gordon is a member. They will be meeting several times prior to June.

Andersen reported the Internal Operations Committee of the Contra Costa County Board of Supervisors met on Monday and Gordon was the only applicant to the CCCERA Board and they recommended he be re-appointed.

It was M/S/C to adjourn the meeting. (Yes: Allen, Andersen, Gordon, Hast, Phillips, Smithey and Telles)



John Phillips, Chairman



Scott Gordon, Secretary

