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>> Sean Kaldor: Okay we'll start in one minute. We'll call to order the February 2nd, 2012, meeting of the San José Police and Fire retirement plan board of administration. We have present today board members Kaldor, Santos, Bill, Krytzer, Lanza, Rounds, Sunzeri and Taylor. We also have board member Bacigalupi present by teleconference. Can you hear us okay, Dave?

>> David Bacigalupi: I can hear you fine, thank you.

>> Sean Kaldor: Couple of agenda items before we begin on the agenda. First, we have been asked to speak up, enunciate. As they went through the recordings from the last meeting to make sure the minutes were accurate, there's a little trouble understanding the exact motions and language. Please create clear proposals and speak clearly on the topics. Second, in this agenda I tried to move things along a little bit, and pop the -- some recommendations received you notice in the consent calendar we put some minor contracts. I think these are things that in general come up each month, we read them everyone looks at each other said yep, looks good to me, why are we talking about this? I tried to put something in the calendar to accelerate things. If you ever see something on the consent calendar that you'd like further discussion on, just let me know and they'll be popped right out. Finally, Local 230 asked me if the new members would be interested in learning a little bit more about the San José fire department. They offered, this is a classic book we all received in the academy, the Guardians of the Garden City. It's interesting reading. I'm getting confirmation that it was an under $50 gift, so there would be no violation of the $50 gift policy. If it's over $50 I will let you know immediately, and it will be a loaner for 12 months, and then we'll ask for them back. Great. Under orders of the day, are there any -- do we have any changes to the orders of the day? I don't believe so There are no disabilities so we don't have a time certain time for hearing the retirements so we'll start with agenda item 1.1, update on investments from the CIO.

>> Carmen Racy-Choy: Thank you, and good morning. I'll provide updates on three investment items. The first is the calendar year gross return, a very preliminary number. The second item I'll provide an update on the asset liability study. And finally, I'll provide an update on where we stand with Alborne. Our new hedge funds consultant.

>> David Bacigalupi: Could you speak into the mic please?

>> Carmen Racy-Choy: All right, I'll try to speak a little bit closer. First of all, the calendar year gross returns very preliminary still is positive .6. We thought we'd disclose it because other larger pension funds have disclosed theirs. But please the reason we say very preliminary is because some of our managers haven't really reported numbers yet, so we've assumed that their performance is in line with their benchmark, which obviously that assumption will fail with certainty. But we hope that the final number would be close enough to the preliminary one. Second, I'd like to provide an update on the asset liability study. Staff has brought forward to the investment committee at the end of January, a draft of our recommendation. The investment committee has spent a significant amount of time discussing the study and have asked for additional asset mixes. The committee has also asked for additional stress testing on the asset mixes. And so staff will bring those back to the investment committee, in February. The investment committee also received a preliminary presentation from alborne. At the February meeting they will actually receive a draft -- a one-pager, that basically summarizes the goal of the hedge fund allocation. This will be approved by the investment committee first and then will come to the board for approval. And once the board has approved, then Alborne will initiate the manager selection process. A couple of heads-up. We will have to modify the custodian agreements and potentially we'll have to modify Macias, Gini, the auditor agreements due to the addition of hedge funds because typically they require specialized expertise and in all likelihood the fee may go up. So we are in the process of negotiating these and as we complete them we will bring them up first to the investment committee and then to the board. Are there any questions?

>> Sean Kaldor: No? Okay. Thank you. We'll move on to new business. Item 2.1. An educational presentation by Cheiron on changes to the GASB reporting requirements.

>> Gene Kalwarsky: Good morning. Bill's going to take you through the GASB changes. Government accounting standards board issues statements governing accounting and financial disclosure for public plans. And Statement 25 sets financial reporting requirements for pension plans and 27 sets pension and accounting standards for the employers. And statements 43 and 45 set similar requirements for OPEB plans. But now we have some changes on the horizon, and Bill will take you through them.

>> Bill Hallmark: So GASB started this process of reviewing their pension standards back in 2009 with a invitation to comment. They followed a year later with some preliminary views of where they were going. And both the invitation to comment and preliminary views indicated a very substantial change in the approach for accounting. Last year they issued exposure drafts and we're expecting final statements this June. And if they keep the same effective date, the final changes would be effective for your fiscal year ending 2013. Normally the valuation we produce right now, as of June 30th, 2011, would provide your accounting disclosures for the fiscal year ending 2013. So that's a bit up in the air, depending on where GASB comes down. What they're working on right now is just pension. So the retiree medical piece, the accounting will stay the same. They have put on their calendar to start a project to review the retiree medical accounting as well. But they have not started that project yet. Given the substantial changes we wanted to get some information to you to start the process of understanding the significant changes, and what the effect might be on San José. The first key thing is: Divorce of accounting from funding. Historically, the annual required contribution, as defined by GASB, was kind of a de facto funding standard. It did not actually require you to contribute that amount. But there's no other national standard, and that became the de facto standard by which all systems were compared. GASB's been very uncomfortable with having their standard be a funding standard, when they are an accounting board. And so they have explicitly said this new standard is not a funding standard. They have eliminated the term, arc or annual required contribution. And completely gone away from it. And you will see when we go through this that their new standard is not a good basis for funding. They've made a change so that the balance sheet drives the expense instead of the other way around. I'll go through that in a minute. They've tried to make the methods more uniform so that comparablity between plans is improved and tried to get more timely information for users of financial statements. The results is going to be significantly more volatile annual expense. So what do I mean by the balance sheet drives the expense? Historically, we were on the top set of -- top of the chart here, where each year we would determine the annual required contribution, as a part of the valuation. And compare that to employer contributions. And any difference went on the employer's balance sheet. And became the net pension obligation, or the net pension asset. Now with the new standard they have reversed the process and we start with the balance sheet or what's called the statement of net position, determine your net pension liability, and determine some deferrals, and the difference from your net position one year to your net position the next year is

what goes on your income statement or statement of activities. And it's the difference between what is the new pension expense and employer contributions. We'll go through the components of that but that's a very significant change in thinking, it's more aligned with the thinking in the private sector and how accounting works. But in the public sector, it's a complete reversal of the thought process. The net pension liability is the first thing that's calculated. And it all has to be done on an entry age actuarial cost method, regardless of what you actually use for funding. The discount rate is the expected return on assets to the extent the assets are sufficient. And an index rate for 30-year high-quality tax-exempt municipal bonds to the extent assets are not sufficient. We'll go through what they mean assets are sufficient, but the net result is, there won't be a change for San José. You will qualify as the assets being sufficient so we'll use the expected return. Couple key things, though they get overlooked in this, is that the actuarial liability has to be projected from the valuation date to the end of the fiscal year. You don't use the liability that we calculate as of the valuation date. And you have to use the market value of assets as of the end of the fiscal year. So when I say, we use the -- currently use the 2011 valuation to give you your accounting numbers for the fiscal year ending 2013, when this goes through, you won't know your numbers for fiscal year ending 2013 until after fiscal year end 2013.

>> Sean Kaldor: Just a brief question. What is the cutoff for that, assets being sufficient?

>> Bill Hallmark: Let me go through that. Good -- good segue. That is actually a graph for the Federated plan, not for your plan. But your plan would look very similar here. The red line shows the projected assets under the GASB proposal. And the yellow bars represent the annual benefit payments. An the way the assets are projected is, you use the current assets in the plan, plus any future contributions for current employees. So you get the future normal cost contributions for current employees. You also get, to include your amortization payments. So you've got a 16-year amortization period. You get to include all those payments. And so as long as you have, you know, really a closed amortization and, you know, a reasonably short if you had a 100 year amortization it may not work. You will end up having more assets than benefit payments at all points in time. And so that's the depletion test. If you fall short of that then you have to use this blended discount rate. But under your structure, you would not. This is just to emphasize the projection. If we were trying to do the 2012 fiscal year year-end statements, we would calculate the total pension liability, which is the actuarial liability using the entry age

method, same number we put in our report, as of June 30th, 2011. We'd add on the normal cost or in accounting terms they call that the service cost, the same thing. Adjust for expected benefit payments and interest and get a projected total pension liability, at the end of the fiscal year. That is one component of what would go on the City's books. Then you have to wait and find out what the actual market value of assets is at the end of the year, and do the subtraction to match your net pension liability that you report. I should say here, I am focusing mostly on what happens to the City's financial statements. Because the most significant changes are on the employer's financial statements as opposed to the plan's financial statements.

>> Russell Crosby: So when you've been saying you you and you, it's not really these guys here and the trust fund, it's what's going to happen at the city end?

>> Bill Hallmark: It is what's going to happen at the city.

>> Russell Crosby: Yeah.

>> Bill Hallmark: What happens for the trust fund You have to report the total he liability and assets of the plan and a bunch of historical disclosures and things. But the material changes, the really material changes beyond like the discount rate, only really affect the City's reporting.

>> Sean Kaldor: So this would be a new section in our financial report that would include these specific numbers and the city would be using those numbers instead when they report them --

>> Russell Crosby: We have them already. We already develop them and transmit them to the city. They are not going to be using them in the same way. They are going to have to wait until the end of the year to do the liability calculation that's going to reside on their books.

>> Sean Kaldor: Thank you.

>> Bill Hallmark: So you get the change in the pension liability each year. But there are deferred recognition periods for certain things. We -- in the funding side we talk about amortizations and we have a 16-year amortization period. And we have a five-year asset smoothing. For accounting, investment gains or losses are recognized over five years. So that's very similar to your asset smoothing method. But normal in the funding side, when we recognize it over five years, but each of those pieces then gets amortized over 16 years. Here when those pieces come out they get fully recognized immediately. That adds a significant amount of volatility to these numbers compared to what we've seen in funding. The other thing that happens immediately is any changes to plan benefits. The impact of those is immediately recognized, no arrangement sayings, no nothing. That hits the City's expense in that year. Actuarial gains or losses and assumption or method changes get split, so that the portion that's attributable to people who are no longer working at the city gets recognized immediately. And the portion that's attributable to active employees gets recognized over their expected working lifetime. This definition of expected working lifetime and how this recognition is supposed to work is a little vague in the exposure drafts, and a lot of questions were asked. But it's going to be -- work out to something on the order of five to seven years. So it's a very short recognition period. This is an illustration of how the expense calculation works. And I've broken it into some categories to try and help you get a little meaning behind the pension expense. I have our model set so I can show you how it varies going forward. But it can lose intuitive meaning when you see the volatility. So to start with, I call the top category operating activities. That's the cost, the service cost, the cost of the benefits being earned in the year, adjusted for any plan amendments. And member contributions and administrative expenses. Now, you'll notice, in the 2011-12 fiscal year column, there's already things we don't know. We don't know exactly the dollar amount of member contributions. We don't know the exact dollar amount of administrative expenses. So we only have one item we can plug in there. Financing activities is essentially the interest on the total pension liability, less the projected earnings on plan investments. So that's effectively equal to the interest on the unfunded liability. So that's kind of your interest cost or financing cost for the current situation. Then everything below that is the recognition of gains and losses. And those end up being very large numbers. Here we've tried to mock things up for you. This isn't exact, because we historically have not split your gains and losses between active and inactive employees. And things like that. But the point here is if you looked at the first two items in the 2010-11 you get around $140 million and then the gains and losses recognition doubles the loss from there. So those recognitions will be very significant. And again on 11-12 we won't know the

number until after the end of the year. Let me show you the model here. This is the projection for funding that we've done. Showing the contributions as a percent of pay on the bottom. Those yellow bars I'm going to keep for comparison purposes. So here's the mockup of your GASB expense. The pension expense is the blue line on the bottom graph. And you can see, it starts really high, 100% of payroll with some of the recognitions of losses and changes in assumptions and those sorts of things that have to be recognized immediately. Your investment gains the last couple years as those are recognized drive the expense through the floor. So you actually get an income. And then because I'm assuming all assumptions are met, it rises up slowly and seems fairly level going out. Now, the top bars show the net pension liability, which is essentially the unfunded liability of the plan. And then, the gray bars show after you adjust for the deferred recognition, what actually ends up on the City's balance sheet. So that's if all assumptions are met. Let me just switch this to historical. So if we repeat the experience of the last 20 years, look at how big the variability is here. It goes from an income of over 300% of payroll in 2020, to an expense of over 200% of payroll. So the volatility of this number is quite significant. And this is why actuaries say we are not going to be using this for funding. So your funding numbers are going to stay with the same sorts of methodologies we've used, and the GASB numbers will not affect what we do on funding. But you'll have to get used to significantly more volatile numbers for accounting purposes than are used for funding purposes.

>> Sean Kaldor: Amount I reading that right, that -- am I reading that right that says if this is actually used for funding you'd be pulling money out of the plan massively for the next few years?

>> Bill Hallmark: On an accounting basis, if you can, and during the '90s the private sector did experience this where they had huge pension income from their pension plans.

>> Vincent Sunzeri: Could you provide some of the factors that could go into mitigating some of that variability?

>> Bill Hallmark: In terms of accounting variability or on the funding?

>> Vincent Sunzeri: Holistically on the plan.

>> Bill Hallmark: What you're seeing here is predominantly the effect of variable investment returns. And recognizing those immediately. And so the size of the pension plan particularly, a mature pension plan, if you take the gain or loss on investments and put it immediately as a part of your expense, now we're spreading it here over five years. That dwarves anything else that is being done by the plan.

>> Russell Crosby: Which speaks to why we've been pushing low volatility portfolios.

>> Bill Hallmark: Right. So on the funding side, we have the five-year smoothing and the 16-year amortization to try and spread those out over a period of time. Which gives us a lot more stability in the annual funding cost than what you're seeing here.

>> Vincent Sunzeri: Are there factors that you would want to add to that? Certainly the change in the investment returns would be the most significant, but what other factors would you add to that, as well?

>> Bill Hallmark: Well, gains and losses on the actual benefits will also have an immediate effect and add to the volatility. So it does put more premium on making sure that those assumptions are -- are accurate. Because in this projection, we're not projecting any games or losses on the benefits side. And so that would get added to this volatility.

>> Carmen Racy-Choy: So in reality, the real accounting volatility that the City's going to experience is higher than this chart. Because this chart doesn't include any changes in benefits, which would have to hit their financial statements immediately.

>> Sean Kaldor: Are there any other questions? I have just one. You talked about active versus inactive on actuarial gains and losses. How do we split active versus inactive and do that? I mean how do you conceptually --

>> Bill Hallmark: That's been a subject of debate. Technically, out of our valuation process, we can -- let's see, where was that? Here we go. Out of our valuation process we can get the campaign or loss on each individual. But one of the interesting dynamics is, when somebody retires, or does not retire, there is, you know, if somebody does not retire in a given year, there's a small gain. When they do retire, there's a larger loss than that gain. And what our assumption says, when we put the whole plan together, we expect those to balance out, right? If you're splitting actives and inactives, do all the gains for that detriment go into the active pool and get amortized and get all the losses than go into the retiree pool and get reflected immediately, it appears that that's what the intent is. But there's been some suggestion about, instead of figuring out on an individual basis, that you could divide it based on the prior year's liability or some other methods. But I think technically, what GASB's described is you look at where they are on the valuation date, and their gain or loss for the prior year, and you put it in whichever bucket it goes in.

>> Sean Kaldor: Okay. Thank you.

>> Drew Lanza: If this question doesn't make any sense, just ignore it. If you do a Monte Carlo simulation going forward using historic rates of return over, say, the last 60 or 70 years, does the result of that converge to 7.5%?

>> Bill Hallmark: Well, the-- whether it converges into 7.5% in the Monte Carlo depends on the assumptions you put in the Monte Carlo.

>> Drew Lanza: Using the Monte Carlo analysis with historical rates of return.

>> Bill Hallmark: Looking at the -- you would put in the assumed return the average return for historical?

>> Carmen Racy-Choy: Let me help out.

>> Sean Kaldor: Is this our next agenda item?

>> Carmen Racy-Choy: Because this -- the actuarial valuation doesn't -- it assumes that you will earn the actuarial rate of return. So the asset liability study is where you make assumptions about whatever every asset segment will earn, looking forward.

>> Drew Lanza: Right.

>> Carmen Racy-Choy: Typically also the way you establish the forecast is you do look at the historical returns. And you might have a positive opinion, or a negative opinion about the segment. You add that to the historical returns, and you project going forward. The reason we simply don't take the historical numbers and use them is because all of the studies show that if you do that, you are worse off than if you go on your best estimates for every asset segment. So having said that, given if you have a high equity allocation, the historical returns, depending on the period that you're analyzing, are typically significant. So if you have a high allocation to equity and you look at a period where equity returns have been phenomenal, you will get definitely a return in excess of 7.5. But if you take for example a period where the equity to returns were slower, then you're obviously not going to make 7.5. So it's really dependent upon the period of data you're using.

>> Drew Lanza: Right.

>> Carmen Racy-Choy: And it's also very much dependent on your asset allocation. And it kind of even regardless of the number, I think the key is to understand the best way to try and understand whether the actuarial rate is set appropriately, is through forecast on the capital market assumption process, not necessarily by historical returns.

>> Drew Lanza: That makes sense. And that was one of my concerns, was that the periodicity is not captured in the underlying analysis. You know where you are inside the cycle right now, but that doesn't seem to get captured in the forward look.

>> Carmen Racy-Choy: That does get captured in the asset liability study in the sense that typically when we look, when we're setting the forward-looking return assumption, we do take into account where we are in the cycle.

>> Drew Lanza: Right, 7.25, 7.5? Right.

>> Carmen Racy-Choy: That's why using forecast is a superior way than using historical numbers.

>> Drew Lanza: Okay, good answer, thanks.

>> Sean Kaldor: Any other questions? Okay. We'll move on to item 2.2, just remind everyone please, best you can speak close to the microphone so we can capture everything. 2.2, discussion and action regarding retirement board of administration's fiduciary insurance coverage, terms and conditions.

>> Conrad Taylor: Mr. Chairman, if I may, I wanted this on this agenda. And one of the reasons why is, I think we have a proposed ballot coming forward. And with that proposed ballot, whether it's going to be -- issues on that ballot are going to be legal or illegal, there's going to be lawsuits coming from many venues. Taxpayers, retirees, actives. Possibly the city, possibly other retirement plans. What gave me great concern is that I know we have an insurance policy. But what does it actually cover? I don't think -- we either pay for something that we don't really know what it covers. Second, does it cover attorney fees? And are these attorney fees only why we sit on this board? What if we go off the board are we still covered and what happens if this lawsuit goes five to seven years out are we still covered with these attorneys fees and do we have to start coming out of our own pocket. Another concern that came about was talking with Mr. Crosby. Historically he has seen that if lawsuits do go upon a board, that everybody is blanketed and your personal credit could be affected or frozen. That's a great concern I think of everybody on this board. Second he also advised that many of the trustees on the boards that have done this have gone out and seeked their own legal council. Now, I don't know if we have attorneys being covered, but now we have to go out and seek our own legal counsel and start coming out of our own personal pocket for this is of great concern. So I would like Mr. Richeda to respond to this. Some of these questions I think everybody on the

board are going to once we hear these answers I think we're going to have great concern of whether we're still sitting on this board.

>> Vincent Sunzeri: If I can add to that Mr. Chair, as well.

>> Sean Kaldor: Dick, then you, please.

>> Richard Santos: Somebody over here first, if you don't mind.

>> Mollie Dent: I just wanted to say, I think you need to look at both the fiduciary insurance for the board, but also the nonrecourse insurance that each of the board members have. So there are two different sets of policies you will need to look at.

>> Russell Richeda: And just quickly, Conrad, I think you also want some review of your protections under the tort claims act, which is a separate -- which is a statutory set of protections which are applicable to you.

>> Mollie Dent: We can take a look at the governmental immunities if you want us to. There are governmental immunities under the tort claims act that may apply.

>> Russell Crosby: I think that's important. As I stressed to Conrad, my experience is total private sector with ERISA plans and there are different rules between ERISA plans and government plans about trustee exposure and a whole bunch of other things. So I think that the angle from the government side is very important on this one.

>> Mollie Dent: We can take a look at -- I mean you can have Mr. Richeda look at it too if you want to. But we deal you know obviously quite a lot with the government tort claims act in the city attorney's office for a variety of city functions.

>> Russell Richeda: And I would affirm that I believe it would be more --

>> Richard Santos: Closer to the microphone.

>> Russell Richeda: It would be more in the board's interest to have the city attorney's office review your obligations under the tort claims act that happened are having an outside attorney do that.

>> Why would you say that?

>> Russell Richeda: Because the city attorney's office speaks for the city. You don't just want a legal analysis about the law, you want confirmation from the entity that would be providing the protections from you. And can you get that through the city attorney's office.

>> Mollie Dent: I'll say it this way. You can access the government tort claims act because you're an official of the city. That would be the only way that you would be able to access it. It isn't because you're on this board. It's because you are an official. It would be because you were an official of the city.

>> Russell Richeda: You want a confirmation that the city is viewing you as a public official subject to the protections of the tort claims act.

>> Sean Kaldor: Dick had a question.

>> Richard Santos: Thank you, Mr. Chair. I appreciate those comments from our legal staff. I think also I would recommend that when we have our retreat on March 7th that we invite insurance personnel there along with our legal staff to have this discussion with board members so we know more or less where we stand and the more information we got on this, I know we feel a little more comfortable. I appreciate Conrad that you brought these up. I really didn't think about some of these issues but I'm getting more confirmation. I think on March 7th we can get more and sit around and learn more, thanks.

>> Sean Kaldor: Vince.

>> Vincent Sunzeri: Under the comments that trustee Taylor made I just want to echo my concerns and where I think the importance for me personally is. As an official of the city my pay grade at $150 a meeting isn't very high. But when I start to think about my personal liability, in this situation, both from a financial perspective and secondly from a professional perspective, I'm governed under FINRA. And I can't afford to lose my job, folks. So I'm very -- I'm concerned about this. I take this position very seriously. I got involved because I think I can make a difference. But this is a very important thing and I want to know where we stand and what my risk of liability is.

>> Conrad Taylor: Mollie, will you be able to have that for us by March 7th?

>> Mollie Dent: I'll certainly do my best to get it for you. I understand you want it by then and if I have any difficulty I will discuss with it Mr. Richeda.

>> Conrad Taylor: What does that mean, covered by the city for the tort acts? Just in a nutshell what does that really mean?

>> Mollie Dent: Well, because I haven't looked at it from the standpoint of the board I'll try to give you an example from the standpoint of a police officer or a firefighter. Many times when there is an incident in which the city is involved, the city, as well as the individual employee, will be named. And so there are rules that relate to whether or not you can sue the city, and there are rules that relate to whether or not you can sue the individual employee. And those are in the tort claims act. And so for example, our -- many times, the employee provides the city provides the defense an indemnity to the employee. There are a rare case that we don't. But I would need to go through that analysis in terms of the scope of the work of the board. So when you're sued in your capacity as a city employee, like a police shooting or something, many times, the individual employee will be named.

>> Sean Kaldor: Damon.

>> Damon Krytzer: And at the moment that's at the City's discretion?

>> Mollie Dent: It's set out in the government tort claims act. So that's what I'll be looking at for you in terms of your role as board members. And I will say that I don't think we've had an occasion in San José where individual board members have been named. We've had suits where the board as a whole has been named. But I don't think -- and I'll check and see.

>> Sean Kaldor: Russell.

>> Russell Crosby: I was just going to say that I've already arranged to have the person from the insurer there for the March meeting so they will be there as well.

>> Sean Kaldor: Russ then you.

>> Russell Richeda: Two quick points. The tort claims act provides mandatory coverage in certain occasions. It's in the sphere of course and scope of employment. There's lots of litigated cases, on whether the act in question that generated the litigation was within the course and scope of employment of the individual being sued, and therefore, whether that individual has protections under the tort claims act. I don't foresee that issue being an issue for you. That is with respect to civil litigation, almost certainly the only kind of litigation that's going to be involved here. But I'm sure Mollie will put into the presentation that if you are dieted criminally, remember, San Diego city retirement board members were dieted criminally. I find that very unlikely here but there's that historical background, that coverage is discretionary.

>> Mollie Dent: Yes, I'll address it. Not all civil coverage is mandatory. There are course-and-scope issues for civil coverage as well.

>> Sean Kaldor: If you write that up clarify what's mandatory versus optional. Bacigalupi.

>> Mollie Dent: And I think we'll also have to take a look at the interface between insurance and the tort claims act.

>> Sean Kaldor: Dave.

>> David Bacigalupi: If you could also include Mollie history as far as impact on person credit ratings. Conrad mentioned something about freezing our credit abilities and stuff. And I think that would impact all board members, whether we're in the process of being defended or not. I mean, if a lawsuit drags on for multiple years and to have your personal credit rating or personal credit to be frozen as a result of a lawsuit, what the background on that, experience on that.

>> Mollie Dent: I don't know if I have that information. If I have it I'll certainly provide it. But I don't know that I will have any information on the personal credit. For example, of -- in other contexts where city employees have been personally named. I don't know that our office would really have the information on how it impacted their credit. But if I can find it, I'll let you know.

>> Sean Kaldor: Where do we go for that?

>> Russell Crosby: I'm sure there's something on that --

>> Mollie Dent: The insurer may know.

>> Russell Richeda: The credit rating agencies. Equifax, it may not be feasible for them to respond.

>> Mollie Dent: Looking at reported cases and finding out from the systems that were involved in those cases if there was any impact on individuals.

>> Russell Richeda: I think there's two related points that you might want to consider. First some public entities have additional policies of insurance independent of the policy you have. And separate from the tort claims act which is just statutory. You might ask Mollie to see if the City of San José has any -- it may just be self-funded.

>> Mollie Dent: We're self-insured.

>> Russell Richeda: The element of self analysis is to note the distinction between the board itself as the only entity being named in litigation as opposed to individual board members named as individual defendants in any litigation. I think the vast preponderance of practical examples is that only the board is named as a defendant. Not individual board members. That's not a law, that's not a absolute guarantee. But it's almost, I think, a -- it is almost always going to be the case, that the board itself is sued. And therefore, that has, I think, and impact on whatever neck effect a lawsuit might have on your personal fundamental stancheon.

>> Sean Kaldor: Dave, did you have any other concerns?

>> David Bacigalupi: No that's it thank you.

>> Sean Kaldor: We will put it on the agenda for the 7th. But if you can get our research or analysis before that, I feel the concern and hesitation and sincere fear about what might happen in this. And to the degree we can, if we can accelerate that it would be appreciated. There are any more questions or comments on this topic? Okay. That concludes item 2.2. We'll move to item 3.1, discussion and action on Cheiron's June 30th, 2011 pension actuarial valuation report for the Police and Fire retirement plan regarding, we'll do these all at once or -- do you want to do them all at once?

>> Russell Crosby: They are going to flow --

>> Sean Kaldor: In order.

>> Russell Crosby: Yes, in the order they are there, they will flow.

>> Sean Kaldor: Okay, so we'll get a presentation on them all at once. A, the plan's assumed discount rate for 2012-13 fiscal year. Including number 1, memo dated January 17th, 2012 from deputy City Manager Alex Gurza regarding the discussions at the January 5, 2012 board meeting. B allocation methodology for valuations of administrative expenses. And C, allocation for valuation of reciprocity cost.

>> Gene Kalwarsky: Thank you, this is part 4. As you recall, we came here in November presenting results of experience study and that's when the discussion began in earnest, I think we had some discussions previously but we came to that meeting with a preference within a range of 7 and 7.75, with actually the preference being 7.5. We showed you some preliminary cost impact analysis because we hadn't completed our valuation yet. But at that meeting the board and staff provided significant input. We obtained some new information, particularly capital market assumptions, which led the board to ask us to come back to the following meeting to update our analysis reflecting the information. So in December we came back with updated capital market assumptions, I'll show you what those are shortly, and we changed our preferred discount recommendation down to 7.25, because that was more in line with the assumptions set by the investment committee. We reported for the first time the June 30th, 2011 preliminary valuation results and that's where the board saw for the first time the significant reduction in cost driven largely by the payroll drop. But after much deliberation, I think it was a one-vote swing the board voted to go with the 7.5 discount rate and we were asked to come back in January with a formal final results in our report. We came to that meeting and showed you the report with the 7.5 discount but then again we got back into the deliberation of the discount rate and why one may want to have 7.25. And a few board members felt they understood for the first time what the issue was. And they voted to at least temporarily reject the report. They didn't want to accept it at that meeting, on the basis of wanting to again consider the discount rate at now, today's meeting. So that's what we'll take you through. These are the capital market assumptions that we received from Carmen, I believe these are set by the investment committee.

>> Carmen Racy-Choy: That's correct.

>> Gene Kalwarsky: And you could see at the 50th percentile the expected return is right around 7.25, it's 7.26. Recognize this is a passive portfolio, you have an active management but that entails investment fees. That is one factor in the rate being pushed to 7.25.

>> Conrad Taylor: Can I ask a question? This is an older model not the current one that's being worked on?

>> Carmen Racy-Choy: That's correct, it's the current asset mix.

>> Conrad Taylor: It's the current one that we have?

>> Damon Krytzer: New assumptions, the current asset mix.

>> Sean Kaldor: The new asset mix.

>> Carmen Racy-Choy: That's correct. So it's the existing -- up until a new asset mix is proposed by the investment committee, you can't take -- it's the current asset mix.

>> Conrad Taylor: It's the existing one. It's not one you're working on which we have, the numbers could change.

>> Carmen Racy-Choy: That's correct.

>> Conrad Taylor: Thank you gentlemen, sorry to interrupt.

>> Gene Kalwarsky: So that was one factor in our coming to the 7.25 recommendation at the January meeting. The second one was trying to assess the board's risk preference. If you simply pick the return that's at the 50-50 level by definition looking at this chart half the time you're going to undershoot it and half the time you're going to overshoot it. We raised the point with trustees if you want to be right more often than not you may want to

set the bar below the expected return so that tends to provide more justification for the 7.25 if not lower. Then we introduced for the board the concept of leverage ratios. We obtained the database from the center of retirement research at Boston college. A renowned group that does retirement research analysis, and these are -- represent -- the bars represent on the left there the actuarial liability relative to payroll, and I'll get into in a minute why that is important. And in between the yellow and green line is sort of the 50th percentile and that's just below, maybe five and a half the ratio of liabilities divided by payroll. Then the red areas would be the 75th to 95th percentile, goes as high as 10. And we were showing you that San José's numbers even though they're later than this data which is -- we tend to think this whole bar is increasing, San José's numbers are way up there as far as leverage ratios. Just hold for a moment. I've added a new slide that you don't have in your packet so you can understand and appreciate why high-leverage ratios are risky. On the right-hand side is a leverage ratio for assets, and in between the yellow and the green, we're eyeballing somewhere around 3. And the Police and Fire fund is, again, way up above all the other 126 plans. So I added a slide because I didn't think these slides were telling enough. And we could send this to this board after this meeting. I just developed them on the plane yesterday. But what I'm showing here on the left-hand side, let's start with the right-hand side first. Because those are your numbers. Those are your actuarial liabilities, your market value of assets, and your payroll. So if I divide that actuarial liability by payroll I get the first leverage ratio which is 13 -- no, it's 17.3. It's liability leverage ratio. And then if I take the assets of 2.6 billion there divided by payroll I get a leverage ratio of 13.8. And on the left-hand side, I'm taking roughly what the Boston college database produced for the 50th percentile, and the leverage ratios are much lower. So why is that important? In the next row, I'm showing, what if we have an unfavorable asset experience of 10% for both plans, what if we have an unfavorable liability experience of 1%, because typically your liabilities experience doesn't fluctuate too wildly, and you were to amortize that over 20 years? With the low leverage ratio, the impact of that unfavorable experience would be 3.15% of payroll. But with your leverage ratio, that same unfavorable experience would be 10.84% of payroll. So just saying that you're more susceptible to large swings in your contribution rate because you have so many assets and liabilities relative to a much smaller payroll, where the average plan has more payroll to absorb those swings. We also talked to you about, in all three meetings I think, that the notion of taking risk off the table. What we're looking up there at, is the distribution from a Monte Carlo simulation. On the topside I'm looking at a Monte Carlo distribution that would have a very high risk portfolio, high return and high standard deviation and the distribution of contribution results are in that gold bar area and the middle, the 50th percentile is the expected and that's somewhere just south of 60%. But you see also 20% of the time there are zero contributions. And then to the far right of the red there, you've got maybe 5% of the time you've got contributions in excess of 120%. And taking the risk off the table means is you flatten that curve, you slightly rise -- increase -- I'm at the bottom chart now -- you slightly increase the expected return of the 50th percentile but you flatten the tails. You don't have strows much and you have lower reserves to right. That is the conceptual picture of what taking the risk off the table means. Too many analyses, too many pension plans have focused on that middle bar expected, and the odds are you hitting that mark are almost nil. So those are the key slides that led us to say we're more comfortable with the 7.25. And we were there in January. The board wanted to go back to the 7.5. You had a vote, and now here you are, with the decision time, where we've got the June 30th, 2011 valuation results at 7.25 and 7.5 and the impact bottom -- bottom two lines are the key things, at least for the city, the contribution at the beginning of the year with 7.25 is 116.3 million versus 105.9 then you see the middle of the year figures, then the total member rate is either 12% or 11.3%. And that just what to tee up the conversation.

>> Sean Kaldor: Questions or comments?

>> Conrad Taylor: I have a few.

>> Sean Kaldor: Please.

>> Conrad Taylor: A Kim of questions. Would you have been more comfortable if we had already had an asset liability model which shows that we are working on it, we decrease the volatility and increased the ten year median rate of return to 7.5 or between 7.4 to 7.5 with a decreased volatility?

>> Gene Kalwarsky: Our feeling is that your capital market assumptions are going to constantly change, it's going to be a moving target. Higher next time or lower. We are more comfortable with taking the risk off the table the left-hand column there.

>> Conrad Taylor: If I could go back to the leverage chart, where you showed --

>> Gene Kalwarsky: That one or the next one?

>> Conrad Taylor: That one there. You are comparing our data to the 2009 data. Where would we have fallen in the in there if you had used the 2009 data?

>> Bill Hallmark: Your data would have been lower but still above the bars. I don't remember the exact numbers you had for 2009, but you still have high leverage ratios.

>> Conrad Taylor: Okay but they wouldn't be as --

>> Bill Hallmark: They wouldn't be as pronounced. What we would expect is that those bars would move up for 2010-11. But the experience of this plan in the reduction of payroll in particular has been much more severe than we've seen in other plans. And so I think those bars probably wouldn't move up as fast as you're seeing the dots move up. So you would be moving to a higher leverage position.

>> Conrad Taylor: And the database you said had 160 plans in it?

>> Bill Hallmark: 126.

>> Conrad Taylor: Are some of those plans less conservative than what we have or more conservative? I know it's an overall database because you're taking-d I would assume our plan is pretty conservative compared to other plans.

>> Bill Hallmark: Well I think one of the key differences between the database and your plan is, the database includes large plans that are dominated by general members and not Police and Fire. And Police and Fire plans in general will have higher leverage ratios because of the earlier retirements, and the longer period in

retirement. So I think that's one of the key factors you'll see here, is in general, safety plans will have higher leverage ratios.

>> Conrad Taylor: And do they have a database that this shows safety plans where we compare our plans --

>> Bill Hallmark: We do not have a good database to give you that comparison.

>> Gene Kalwarsky: But we're currently working with the folks there and in fact we've got a visit planned, that's going to be the next step. That's one of the next steps, that we will be comparing safety versus general.

>> Conrad Taylor: Okay so our --

>> Bill Hallmark: But again I want to emphasize, this is not a statement of being good or bad. It's a statement of the leverage. And sensitivity to risk.

>> Conrad Taylor: I understand that.

>> Bill Hallmark: Okay.

>> Conrad Taylor: I just want to compare apples to apples, safety plans to safety plans not safety plans to other plans and other plans that might not be as conservative as ours.

>> Gene Kalwarsky: This does have safety plans in there but it's mixed with general.

>> Conrad Taylor: Thank you.

>> Vincent Sunzeri: Couple of comments, one first on the discount rate. Earlier you talked about reducing volatility of the plan and really, the lower we drive down the expected discount rate, there is some correlation with the volatility going down as well. Would that be true, Carmen?

>> Carmen Racy-Choy: Yes, unfortunately there's no free lunch.

>> Vincent Sunzeri: So you know not too much of a stretch to go there. And I just want to reiterate, to the board that we thousand have our actuary is on board with recommending 7.25. Our investment committee has done new market assumptions, they're recommending 7.25. And I believe at our last board meeting our CIO recommended 7.25. That's the position I will continue to drive towards. The other point to me which is really important and aside from the discount rate is this leverage factor. And this is more to go back to the city, and I have to say I was a little starlted at the last meeting. Ourdeputy City Manager said they were surprised by the leverage. And clearly if you look at that chart that you had earlier, the higher payroll is less leverage. Certainly I'm not sitting here saying let's go back to hire a bunch of people to fix our leverage ratios because that's a whole different conversation. But what would you tell our city, finance managers, that they should be looking at, so the potential impact isn't as significant next time when a decision like this is being made?

>> Gene Kalwarsky: Well, you know, there's a few things you didn't mention that to give you a full picture. We didn't intend to say that the cut in payroll made the system only have bad news associated with it. If you recall, the ten year projections we did last year prior to knowing that the payroll cuts took place were significantly higher than what they are now. So the payroll cuts did impact greatly or reduced the amount of outlay the city had to pay. In fact if you look up this chart that I showed, write showed the percent of pay was 3.15 or the left with an average leverage ratio and then it was 10.84 with the high. Look at the very next row. The dollar amounts are the same, though. So it depends, to answer your question, the city finance folks, it depends on what number they're more fixated on, the rate of pay or the absolute dollar amount.

>> Vincent Sunzeri: And this is not so much a discussion in my mind on the rate of pay but more the change in the total dollar of payroll. And so as safety is either added or taken away, and that total payroll number is impacted by that factor, not by compensation levels per se, it appears to have a significant swing here.

>> Bill Hallmark: I want to clarify something here. We use payroll as almost a crude proxy for the tax revenues. Because if you look at some of the large systems in the database, you can't figure out what their tax revenues are, because they cover hundreds or thousands of employers. And what really matters here is the revenue base that's supporting the dollar contributions that go into the plan. And so payroll is a rough proxy for that. With the concept that payroll may represent a fixed percentage of overall revenues. But I think when you start talking about changes in pay, and pay increases, or pay cuts or positions and how that affects the leverage in the plan, what you really need to be thinking about is the overall revenues of the city that have to support the contributions to the plan and what's happening with those.

>> Sean Kaldor: Damon, no, okay. I do have some questions about the leverage also. The deputy City Manager included a letter which had the same chart in there from last month. But it had the three bars, and this time you're not reflecting the unfunded liability leverage. Is there a reason for that?

>> Gene Kalwarsky: Yes, it conceptually really didn't make sense because we were offsetting unfavorable experience with investments with unfavorable experience in liabilities. And the reality is what we're trying to show is what if you have bad experience and what's the impact? We can't net the two out. The third chart was showing -- it was almost in a way presuming that you would have bad, perhaps bad investment experience offset by good liability experience and then you subtract the two and you're somewhere in the middle. So conceptually it didn't make sense.

>> Sean Kaldor: So just -- so in the advisory, you've been writing to clients and talking about that, that it shouldn't really be a way of looking at the data?

>> Gene Kalwarsky: Not the UAL piece, right.

>> Sean Kaldor: Okay, and then looking at the same, what you do to fix this, what do we do as a board, right, we don't set benefits. I look at --

>> Gene Kalwarsky: I must make one caution, because the other question came up, we are comparing you to 2009 data, we aren't taking out the safety. We don't want you to overact to this just yet. This is something -- I know Bill is coming back on March 5th, I think an educational conference where some of this may -- we may have better data. We're just introducing the concept to you that look like you're on the high side of leverage. But we've got some more work to do.

>> Sean Kaldor: This is healthy then, we're trying to learn what it means and if you're you know working through all the implications or how to take it it's good to do this together.

>> Gene Kalwarsky: Okay.

>> Sean Kaldor: I'm looking at the market value of assets and it says wee highly leveraged. So I said what are we are 100% leveraged would be.

>> Gene Kalwarsky: Yes.

>> Sean Kaldor: If we had $4 billion in liabilities and 20 billion in assets, we are 4% funded we would be horribly leveraged.

>> Gene Kalwarsky: And what it would tell you is why keep the 20 billion in a 60-40 or 70-30 equity fixed income. If you could derisk the plan and not have as much equity then your probability of having investment fluctuation will go down. Theoretically, we haven't mentioned here but since you're willing to work with us on enhancing this, the better leverage ratio, instead of just being assets divided by payroll, it would be one standard

deviation of your assets divided by payroll. And that way if you were all on fixed income your standard deviation is small. If it were all hedge funds it would be high. So that's an enhancement to this ratio as well.

>> Sean Kaldor: So the -- okay, so those are some interesting points. The assets though I think as you took out the unfunded liability, looking at the assets, I don't quite get how do you fix that and why that would be a bad thing? You're right you could derisk the plan but we also have an obligation to do well as a plan. Not just to maximize the benefits for the members, they put the money in there. We don't just say, oh, we assume 0% return. Because we got so much cash now.

>> Gene Kalwarsky: Well, I think if you had $4 billion of liabilities, and let's say you're at $12 billion of assets, to continue to stay in risky portfolios make no sense.

>> Carmen Racy-Choy: Especially the practice, I mean, what you're seeing here is normal with a mature plan. And what a lot of plans do is, they take risk off the table by backing the retired liabilities with an immunized portfolio of fixed income instruments. The problem doing that is currently fixed income isn't yielding a lot so it's very expensive and it would actually increase the liability quite significantly. So the normal practice, which would have been ideal, is if 20 years ago or 30 years ago when a fixed income was higher, that practice was started, and some of the inactive liability that we currently have was immunized in that fashion. At this stage, the normal way you would deal with this, which is to take some component of your liability and match its cash flows with fixed income instruments, is almost exorbitantly unaffordable.

>> Gene Kalwarsky: We were just discussing here an interesting point. First it doesn't necessarily mean it's bad that you're up there. You just want to manage this. I want to give you an extreme example. Let's take two plans. One plan has no assets at all in your example and the other has a 20 billion. Well the plan that has no assets has no reason not to be in fully risky portfolios, and try to earn its way out of its mess, because there is little at risk. And so it would encourage that plan to maybe put more into equity. But the plan that is very overfunded, you're past the point of needing the risk on equity, and you ought to be derisking the plan from that other chart that we showed, no, not that one, the gold bars. You ought to be moving to the lower bar for a plan

that's grossly overfunded. Because there's no reason to take that right-hand escalation beyond 120% of payroll. So this is really a tool to manage your plan, as opposed to a report card saying oh you're bad because you're up here.

>> Sean Kaldor: So you're saying to take as little risk as you need to?

>> Gene Kalwarsky: Then that becomes a risk preference of the board. If I have no assets I can take all the risk because it's not going to impact me. If I'm way overfunded, 500% overfunded, what's the point of exposing yourself to that kind of risk?

>> Sean Kaldor: So if decision isn't just here is the 4 million, here is what your considerations should be, it should be the consideration of other factors?

>> Gene Kalwarsky: I'm give you another example. If the day comes that interest rates finally rise and we've got insurance company annuity rates that are 7.5%, you watch what happens to your leverage ratios, they'll drop way down if you immunize or annuitize your retire life liability.

>> Sean Kaldor: So we've gone into the discount rate discussion. I've got a few questions about that. Our friends in the Federated side, they adopted the decision to go to 7.5, they want to work towards that goal. Did you support that 7.5 position? Lower's always better.

>> Gene Kalwarsky: Yes, we did. But I think we also gave them a range. Here would it help to remind you what the projections look like for the 7.25, 7.5? We are just showing a static here, we have no model.

>> Sean Kaldor: That's okay. I want to keep going through this for the sake of time. So Federated 7.5. So 7.5, 7.25, are those both in the range for us?

>> Gene Kalwarsky: Yes.

>> Sean Kaldor: And then in your recommendation to San Diego just recently, you included useful information, they went to 7.75 --

>> Gene Kalwarsky: No, they're down to 7.5.

>> Sean Kaldor: They're at 7.5, I'm sorry, they were at 7.75, as we were, and they went to 7.5, which you also indicated would be good. But then you said there's a national trend to lower investment assumption, reduce risk, reflect increasing pressures from actuarial, economic, accounting and governing bodies. I think I'm more focused on what's the right thing for the plan rather than worry about political --

>> Gene Kalwarsky: That was just one slide saying, here are some other miscellaneous factors. It's consistent with what's going on last year, most of you know the CalSTERS dropped its rate.

>> Sean Kaldor: Yes. You mentioned the Boston college group right, that's the data we used for the -- can you put up the -- thank you, the leverage ratio. So using that same data, in the San Diego report, you talked about where people stand in terms of their discount rates and where they are. I looked at the same data and out of the 126 firms, three were at 7.25. The other one was at 7.

>> Gene Kalwarsky: I believe that's the Nasra study.

>> Sean Kaldor: No that's the Boston college study. If we go to Nasra and then on top of that we're doing the asset liability study and it looks like there might -- that study is not done right, we're holding off on that. The first cut on it looked like we might be able to get less risk and achieve 7.5%. That's not done so we'll keep working on it. It seems like we're being aggressively conservative. Conservative is always safer but there's a real cost to it. I think as Vince said last month, these decisions have a very real impact on the safety of the community. And Carmen mentioned I think last month or the month before, we're now going to be less than it was ocialgly thought to be, so let's spend some money in derisking the plan. I'm mindful to 120 million and as they go down to 105

that's not new found money to spend on derisking the plan because that's the safest place to be. I still think we need to be somewhat aggressive. We've come from 7.75, I think 7.5 is in the range, it's affordable and it still lets us move forward and then complete the sate plan liability study, when we have conclusive research that says here is our asset liability, our investment mix, everything, if it lines up with 7.25. If it lines up with 7.25, it lines unwith 7.25. Vince, Drew, Sean.

>> Vincent Sunzeri: So if you take a look at the most recent flash report from NEPC that does our reporting and you look at our ten-year number, the gross return is 6.6% as of October 31st. For ten years we're not hitting our number. We're not even at 7% for ten years. So if we think we're talking about things on a short term basis, frankly as a fiduciary, my priority is to make sure that those beneficiaries have the assets available throughout their lifetime and that we are funding the plan in a prudent fashion, we are derisking the plan as much as possible and there is a direct correlation to the plan that we select. If we go back to some of the conversations we had previously, we talked about the plan we had, Carmen talked about buying down risk if you will. You look at the current rurnts on the plan, either fiscal year to date, calendar year to date, they're either 1.1 or negative because of the current plan climate we're in. Again we're going to end up potentially in June where we're not hitting our current discount rate. We might not hit 7.5%, we may not even hit 7.%. I don't know what more empirical data you need.

>> Sean Kaldor: Drew.

>> Drew Lanza: Am I missing something here I mean some group of people need to craid off volatility, need to trade off certainty against return. And you said something at the last meeting about this Carmen. Are we supposed to be in a larger -- Gurza brought it up in the e-mail. Are we supposed to be in a broader conversation with the city council, about where to turn that knob? Am I missing something here.

>> Sean Kaldor: Pete why don't you speak to that and then Sean Bill next.

>> Pete Constant: I think the council has made a clear statement they've passed the fiscal reform plan and have stated that their expectation is that the retirement board select a rate of return that has at least a 50% likelihood of occurring. That is the council's position.

>> Sean Kaldor: Sean.

>> Sean Bill: So my interest in getting this back on the agenda was, you know, I think the board in general is all on board with the idea of derisking the plan over time. And it's a matter of you know doing it in a thoughtful and gradual way to get to where we want to go. And then, you know, Vince, your point about the 6.6% return would last ten years, that was interesting. One of my questions was going to be how often have we exceeded our assumed rate of return over the last ten, 15 years, but that kind of answers that question, actually. So I think, you know, from my perspective, you know, I want to be sensitive to how quickly we drop the discount rate, because obviously, it does impact the sponsors of the plan. The city, the employees, all, all are affected by this. But at the same time, you know as we lower that discount rate and your chart showed that we can kind of, you know, flatten out the curve a bit, and, you know, stabilize or reduce the volatility that -- of the contributions going forward. And so I do kind of come back around to what, you know, we discussed at prior meetings in terms of this being a little bit of an opportunity to maybe be a little bit more aggressive than what we normally would be inclined to do, in terms of dropping the rate. As we did have such a positive year last year. That said, we just got the update, for where we are currently. And again, you know, it's looking like it's possible that we'll miss our return again this year. So my sense is, you know, we're all trying to move towards making sure that this is a healthy funded plan, and it's in the best interests of all the beneficiaries of the plan that we continue to, you know, reduce the rate. I don't know where we ultimately want to get to the rate if you listen to Bob Arnott and those guys they say 4% going forward is your return or the CEPER studies, right? If you look at Stanford endowment, they're running like a 6.9% return but probably have a bit more sophisticated strategy than we do. My guess is that you know if we were to employ a thoughtful strategy in terms of our asset allocation, we probably could be somewhere above 7%. But, you know, I -- my preference and you know whether it's 7.5 7 and three eighths or 7.25, not be focused on away other plans are thinking of this you know independently, as a group of 9 people that you know what's best for the beneficiaries long term.

>> Sean Kaldor: So Carmen you're going through some numbers there. Did you have the 20-year return on the plan?

>> Carmen Racy-Choy: No we were going through some numbers on the Cheiron presentation.

>> Sean Kaldor: Do you know the long term, we're trying to make a long term decision here. Do you know in the past 20 years do you know what the return has been on the plan roughly?

>> Carmen Racy-Choy: I don't think we go that far in our financials.

>> Sean Kaldor: It's been in excess of 8% has it? Nationwide the aves is 8.2.

>> Carmen Racy-Choy: I don't know if the 20 year period is over eight but since inception I think it's over 8 or very close to it. But I think you have-d the concept again is when you have no assets or when you have very little assets, you can take a lot of risk. And this plan did do just that. And it did so very successfully. But at this stage of maturity, the plan simply -- and given where things are with the active population of the city, and the current payroll, I think the message is: We can't continue to take on the same level of risk.

>> Sean Kaldor: We took more risk back when we were in bonds?

>> Carmen Racy-Choy: We took more risk back when we were 60% and 70% equities. I mean, depending on how far pack you go, early on, you were I think predominantly in bonds. But you were also one of the first plans to move into equity. And you moved into equity in a big way. And that has paid off, because while the equity market was flourishing you were heavily invested in it. But again, the risk -- the leverage ratio back then was very different from what the leverage ratio is right now. And so you took risk at the right time. I think the message is, now is the time to derisk the plan. Really, for the sake of the existing inactive members and for the sake of the existing active members.

>> Sean Kaldor: Dick and then Sean.

>> Richard Santos: Just a couple of comments. I hear so many comments from 6.6 in ten years and that makes me feel very uncomfortable in those areas. Vince, is a committee is the investment committee are you guys suggesting or recommending that we have the 7.5 or the 7.25? Because I've heard various things then I want to follow up because I think there's other factors here like hiring and all the other factors and staffing, so many things that I'm sure relates to this. And I was assuming if we had many of these things ironed out they would be less volatile.

>> Vincent Sunzeri: So to try and directly answer your question, I can't say the committee has completely gotten to that perspective. Because we're dealing with the asset liability study. We did get there when we looked at the current asset mix. And the new capital market assumptions, this was a topic that was to come back to the investment committee for the January meeting. After five, six-hour meeting, and we got to that agenda item, there wasn't a single Police and Fire committee member remaining. So that topic was not discussed. But we did look at the capital market assumptions. We did work with our chief investment officer to -- and Federated as well, to get to new capital market assumptions. And that's how we got to the 7.25%.

>> Richard Santos: I read the memo and I understand 50% chance and that would be 7.5. But all these other factors tell me that doesn't seem achievable.

>> Sean Bill: 50% chance being achievable at 7.5?

>> Richard Santos: At the retreat, maybe we can get through some of these things to establish the future.

>> Vincent Sunzeri: So if we have a current plan and a current asset mix at capital market assumptions that put us to 7.25, my question to our chief investment officer and looking at a asset liable study, do I want to try to derisk the plan with a 7.25 rate or do I want to try and raise the rate to 7.5? Maybe the risk comes down a little bit. From

where we are. Frankly, I'd rather start with the 7.25 and derisk it as much as possible. Again, that to me is a driving force. There's nothing out here in terms of a priority, other than reducing the liability of the swings in the plan. You just look at the last two years what we're experiencing, we're seeing that right now, the swing from an 18% return to a current year where we're at roughly a 1% return. Where we have our actuaries telling us the most significant factor is the volatility of that number. Frankly don't we want to work on trying to mitigate that and reduce that as much as possible?

>> Richard Santos: That's what I'm hearing too, have your committee make some recommendations. The way I understand that payroll which has a portion of the responsibility there is going to start to increase because I understand we're hiring back, is that correct? Russell and others?

>> Conrad Taylor: That is correct. They're starting to recruit now. They're starting to do more hiring.

>> Richard Santos: So will that play a major role in this?

>> Pete Constant: Actually you know if I can jump in. They're not new positions they're replacement positions so payroll will not increase.

>> Richard Santos: But payroll did take a dip because of the layoffs.

>> Pete Constant: But the hiring that's being hired now are not new positions. They're filling positions from continual retirements. So the authorized strength is not intersing.

>> Richard Santos: There will be contributions.

>> Pete Constant: There will be contributions but payroll as a total number will not increase unless the council adds positions. Actual positions that get filled. So right now when someone retires, it's a one-for-one replacement. And they're hired at a lower rate so theoretically payroll could go down slightly with the minimal

decrease in payroll. But the city also has at minimum a $25 million deficit for next budget year. So whether any of those reductions in cost to meet the deficit are in Police and Fire we don't know obviously yet. But there are no new positions. So any hiring is just a replacement hire. Soilt won't affect payroll in any substantial way.

>> Sean Kaldor: So we have Sean then Vince Then Damon.

>> Sean Bill: Two points I would also emphasize are, if we were to drop our discount rate for the 7.7 and 3/8 or 7.25. That would unable touts have a higher probability of hitting that return we could get to a 60% rate or 55% rate or what you have. As we have seen from our last ten years of 6.6%, obviously it's difficult. The second point I would make, is that we've kind of had the wind at our back here for quite a long time. We're now at a 1.84% 10-year treasury, how much upside do you have? We all know what's going on in the global economy? The year et cetera equities are quite difficult to predict. So you know having a lower expectation of returns going forward to me, intuitively makes a lot of sense.

>> Sean Kaldor: Vince.

>> Vincent Sunzeri: Actually I was going to take the conversation the same direction and moving away from just the discount rate and look at the macro climate, frankly if you look at the macro climate we had sort of a Goldi lokes the growth of the economy continued to improve, and frankly for the last ten years, it's been very challenging, and you look at the situation that we are faced with today, the U.S. is significantly faced with a deleveraging environment. Most strategists are talking about a muddle through economy that will continue for quite a period of time. And Europe is a question of what the outcome's going to be. And no one knows. But Greece could unraffle the entire picture. Those -- ravel the entire picture now. Those markets are capital market assumptions what's taking place on a macro basis.

>> Sean Kaldor: Damon.

>> Damon Krytzer: The only other point I wanted to make, as well, was, something that Dick just mentioned. And I think frankly optimal to us is a combination of both. Increases in payroll and it's a lower rate. I mean, we're not talking about being in a situation where we're sort of sitting in a good position right now. We're pretty highly leveraged. We're not offsetting, so you know one is not offsetting the other. We need both either way. Even if that was the case, I would support 7.25 even though we were increasing the payroll quite a bit.

>> Sean Kaldor: Conrad then Drew.

>> Conrad Taylor: I 90 know we're talking about the ten year average and it's not to take that with a discount. But you also have to look at an anomaly with 2008. Where they had a huge market crash. We were almost -- the markets were at a financial -- the worse time they've ever seen since the great depression. If you would pull that out I bet our ten year number would be higher, that already occurred but you have to take that into consideration also, it was an anomaly. Like you said Vince we don't know what the future is going to leave but that was when the markets were on the brink of destruction. And that's included in the ten year mark. If you were to pull that out, I bet you our numbers would be much higher than what we're talking about.

>> I could take the same remark for the late '90s and the bull.

>> Carmen Racy-Choy: Prior to that there were four years of 2008, then you have to pull out those four years as well.

>> Sean Kaldor: Or the last two years of 14% and 18%.

>> Carmen Racy-Choy: So it's difficult to make arguments on pulling numbers out of historical context.

>> Sean Kaldor: True.

>> Drew Lanza: I think we all have the sense of something deep structurally is going on to pes 62 is the youngest retirement age for Social Security recipients. So I would ask you gentlemen to feed us back on the conversation you just heard, in the context of other retirement plans that you talked to. Your thoughts.

>> Gene Kalwarsky: We'll both have differing thoughts so Ith think we should both speak to this. You mention San Diego where we serve as the actuary. The 7.5 came out 7.5. That was our second go at it. Here is our second go. You were at 7.75 --

>> Sean Kaldor: We went from 8 to 7.75 now we are talking about 7.5 or 7.25.

>> Gene Kalwarsky: Since we got on we're likely to continue to consider pushing it down. Particularly when Carmen said you have had good years and you continue to buy your way down. After a year that you've had a bad market but discussion is very consistent with all our other funds and I might add that the discussion amongst actuaries, and federal policy makers, are talking about this as well. Somebody mentioned that these other studies of four, 5%, we mentioned to you before, there's a group of actuaries that are pushing hard to they use market value interest rates which are in the 4% range. And so in the federal sector, private sector plans have to use that now. So all the signs are that it's going in that direction and if you can ease your way down instead of one big jump, it makes sense. And that's my view. And I'll let Bill supplement.

>> Bill Hallmark: I think what you're struggling with is the same thing a lot of plans across the country are struggling with. A recognition that a lot of risk has been taken. But now that 2008 has happened, are it's expensive to make the adjustment. And even with the returns we've had, the struggle for plans today is looking at how to derisk in a way that's affordable for the sponsor, and balancing those issues. And so that's a lot of what I heard in the discussion here, is really, different views of what -- what's affordable today for this system. I think in terms of expectations going forward, if your median expectation is 7.25, you need to take that into account in your projections forward. If your median expectation is 7.5, you need to take that into account. The not just that median expectation but the variability around that expectation and what can you do to control the unaffordable consequences of that variability.

>> Sean Kaldor: I don't see any --

>> David Bacigalupi: Mr. Chair.

>> Sean Kaldor: Sorry, go ahead, Dave.

>> David Bacigalupi: Yeah, just a couple of comments. I hear different numbers being thrown out, that ten years we didn't make the numbers, 20 years we did, life of the plan we did make over 8%. You know, it's -- it goes back to the old saying, you know, depending on how you frame your statistics you can have the outcome almost of anything that you want. Which makes it difficult for a nonfinancial person like me to come to an -- you know come to a decision on this issue. One of my thoughts is that going from 7.2575 to 7.5, it does derisk the plan. Maybe not as much as 7.25. It is in a step fashion derisking the plan. If we see new information or additional information next year, the recommendation may be even stronger topes go to 7.25, it may be to go to 7. I hear the phrase, buying down the risk, during the good years. It makes me think back to what has somewhat created some of our pension crisis is, when we do knock-out returns before we increase benefits. Which is really good for the workers but somebody has to pay for those. Because somebody has to pay for those. The money that got those benefits increased, didn't continue. Returns didn't continue at that level and it's part of what led to where we are today. And you know, we as pension board members we want to do what's best for the plan. And obviously, derisking the plan is a good move. But how far do we want to go and at what speed? And you know, I -- you know I hear let's take the politics out of it. We don't want to be involved as far as you know putting more employees on the street. But I mean it's really hard to take the politics out of it. I mean we do the best we can. But you also have to look right now, the city has a real strong agenda to maintain the level of a pension crisis, and that would support their move to a ballot measure. And unfortunately, our staff works for the city, not for us. So I mean, who -- you know I don't want to make any accusations here. But there's pressure comes from the City Manager's office and from the city that we don't -- we may not even be aware of. And, you know, our staff deals with Cheiron. So there's all that into it, too. I think we should derisk the plan when we have the opportunity. I think this is a -- you know a good move. I'm not sure that we need to go all the way down to 7.25 this year. I may feel differently next

year. I may feel that 7 is a better number next year. But hearing all the conversation, I haven't heard anything that convinces me today that would make me support the move down to 7.25. I still think that 7.5 is a reasonable move in the right direction and that's what I would support.

>> Sean Kaldor: Thank you. Councilmember Constant.

>> Pete Constant: Question for Cheiron, on the new slide that you put up that we don't have. So can you talk a little bit about the implications hf this decision next year, what the delta will be, as far as the swing in volatility over that quarter percent difference? So in other words, if 7.5 were selected today and we underperformed by 5%, what would the difference have been in that half a percent?

>> Gene Kalwarsky: No one can predict what's going to happen next year with the returns. If we could, we wouldn't be here today.

>> Pete Constant: That's not what I asked. I asked for what would the difference be between 7.25 and 7.5, delta in differential in swing due to the volatility?

>> Gene Kalwarsky: You would slightly increase the liability leverage ratio but the other thing that would happen is if you look at the line that says unfavorable asset experience, 10 and 10, as you lower the discount rate and presumably the portfolio follows that, the odds that the unfavorable experience would be the same in both wouldn't make sense. The lower the discount rate, you know, I mentioned earlier we should be looking at one standard deviation of return. If you lower the discount rate the unfavorable experience becomes lower on the right so it improves your position as far as not having to have the volatile contribution rate.

>> Pete Constant: So this -- if I'm underring right, if the plan underperformance, the swing, because of the volatility, is going to be more significant with a higher discount rate, less significant with a lower discount rate?

>> Gene Kalwarsky: That isn't quite what I said. I said with a lower discount rate accompanied with a derisking of the portfolio, means a one start deviation is smaller -- standard deviation is we would be mainly in this chart be comparing 10% at a 7.5 with a maybe 9% on a 7.25. You notice up there we have lieblght experience only have 1% because we know the standard deviation for the liability assumptions is very small. And that's almost comparable to the asset deviation of 10. The lower standard deviation the lower we would have those unfavorable percentages up there.

>> Pete Constant: Okay. And then Carmen you mentioned the calendar year return was plus .6 gross, is that correct?

>> Carmen Racy-Choy: That's correct.

>> Pete Constant: And what about fiscal year to date since we're halfway through the year?

>> Carmen Racy-Choy: Fiscal would be negative 3.6.

>> Pete Constant: Okay, so negative 3.6.

>> Sean Kaldor: Through what date?

>> Carmen Racy-Choy: This is fiscal year to date, July 1st, 2011 to end of December.

>> Pete Constant: End of December. So we've talked a lot about historical returns and -- but what we do know is what we've done so far this year which is negative 3.what?

>> Carmen Racy-Choy: 6.

>> Pete Constant: 6 gross?

>> Carmen Racy-Choy: Gross. And this is preliminary of course.

>> Pete Constant: Preliminary, okay.

>> Sean Kaldor: So I'll ask a question and make a motion. I don't want to get -- do we have two people from the audience who want to speak? So I'll ask my question let them speak and hold the floor after that to make my motion. You talked about returns through December. Have we released any plan returns for the board members about November or December yet?

>> Carmen Racy-Choy: Not yet. We've discussed returns through October at the investment committee meeting.

>> Sean Kaldor: And so what have the markets done in January?

>> Carmen Racy-Choy: A good question but I think the volatility continues. Meaning, don't expect the negative return to be mollified. It has been a roller coaster period, and I think you can continue to expect that. So --

>> Sean Kaldor: That's my point. January's been a phenomenal month. Markets seem to be from the start of our fiscal year in general, markets seem to be up 1%, overall markets. I don't want to set a long term rate based on what's what happened last three months, four months, last two years we got 3% returned, long asset liability models and the economic assumptions that are coming up about where things are going . With that I'll open the floor to the members of the audience.

>> Robert Sapien, San José firefighters local 230 president. Interesting dialogue today. I want to say, I guess I'd start off by saying, I'm thankful that the idea at an earlier agenda item that GASB is not a funding requirement was explicitly stated because I know there's political interests in certainly that we've seen that want to make it a funding requirement. So I'll be using your slide quite a bit in the future I imagine. With regard to this discount rate,

I have to say, when the decision was made to go to 7.5%, frankly, it was important that we move towards derisking. But it's sobering from the user end. Don't forget, I represent fewer than 650 now firefighters. When I heard last month, folks saying, especially city staff, it was frankly disturbing that they were surprised by the volatility, when we know in reality that when we had over 700 members paying into the plan, who took a 10% reduction, and then reduced their numbers down to less than 650 members, that volatility's going to exist in this plan. Secondly, with the environment that the city has created for employees who were close to retirement, many were driven out of their jobs and into retirement, creating further impact on the leveraging of this plan. There's a lot of very politically driven panicky decisions being made. What we expect from this board is reasoned decisions based upon long term investments. I've been in the city for 22 years investing over time in this plan. My own dollars, as have my members. What I don't expect from you is to bring volatility in your action, a full half a percent change in the discount rate because of many factors, a lot of them concern me that I heard today, is not what we expect. We expect long term management of our plan that is reasoned and sound and that is not politically driven. You are gradually derisking the plan. We appreciate it. You drastically derisk the plan we pay for it.

>> Sean Bill: I like to ask, do you people the plan has been managed in a way that is sound?

>> The external farks have a 100% members in this plan, who are at the table willing to talk about reforms, to additionally take some stress off this plan. So a drastic move to lower the discount rate is unwarranted in my view. I do believe you're here doing the best you can to make this plan work. I just think we have to be reasonable, not succumb to political pressures. Let's move down the road in a reasonable fashion, a volatile setting of the discount rate that moves in big chunks just doesn't make sense to us. Thank you.

>> Alex Gurza: Good morning, Alex Gurza deputy City Manager. Want to thank the board members for the discussion this morning. I know it's a very difficult issue. I wasn't going to speak but I felt the need to spoke after Mr. Bacigalupi's comments. I don't want to quote him but figuring there might be pressure on uneive with cli that is absolutely not the case. The City Manager, City Manager's office does not apply pressure on you any individual trustees or the staff to make your best professional judgment. On very, very important decisions sich as the earnings assumption. We absolutely respect your role as fiduciaries, that make these decisions independent of

that pressure. We, on the other hand, are absolutely concerned as you are, of risk and volatility in the plan. I want to clarify what I meant by saying surprise. I think everybody that I've talked to didn't -- was not aware of this particularly leveraging issue. That slide that Cheiron indicated was not a slide that prior actuaries had advised the board of this nature of leveraging. We very unfortunately had to cut our payroll by cutting pay and cutting hundreds of positions. The Federated plan did not experience this same level of volatility because that level of volatility didn't exist. Again this was because we haven't had in the past to cut the number of positions and compensation to same degree. I think that was one of the reasons why that issue of leveraging hadn't come up previously. But again, what the exact discount rate should be, that is up to you to decide what that is. We are very, very aware however, that if you pick an earnings assumption that is not met, that creates a liability. And we just encourage you to continue to think of what is realistic, and continue to think of taking risk off the table. Thank you very much.

>> Russell Crosby: If I could, just a second, on David's comments, with all due respect, David, the information flow is just absolutely opposite to what you describe. The professional professional credentials and licensing that it doesn't matter whether we work for San José or some other trust fund. You're going to get the same answer, which is our best professional expertise, applied to the problem. The information flow isn't going from the City Manager, or Alex Gurza or somebody like that. It's the other way around. As we've learned these plans and discovered what's going on within them, it's to transmit that information to the city.

>> Sean Kaldor: So we don't tell them how to do their estimates or how to do forecasts.

>> Russell Crosby: Absolutely, we don't get any input from Alex or the City Manager on these forecast. It doesn't happen that way, the information is the other way around. Carr Membership.

>> Carmen Racy-Choy: I'd like to add that my area of expertise, I am an actuary. My area of expertise is investments and setting the discount rate. I work very closely while I was at Mercer investment consulting. They wanted to build an approach to -- to develop a standard recommendation across all of their clients on what the discount ought to be. And ultimately the model that we're using is very much the result of that experience. I

worked with a professor at a very famous, with a very famous actuarial program. And basically, the model currently whose numbers are in front of you, was the result of that cooperation. The best practice range for setting the discount rate, and I do believe I have stated that in past years, is somewhere between the median, which for this plan is currently 7.26 and the 25th percentile which would be 5.6 net. So this is the best practice range. The -- when I say best practice am I looking at public plans only? Absolutely not. Because we don't exist in a vacuum. The median, we were significantly outside of that range. So for the past three years staff has always encouraged the board to move towards the median. And we're very grateful, and we -- I think the board should be very proud of the fact that the discount rate has been moved in that direction. Is the median the ultimate right number? I mean, now you're very close to being at the median. The question that is being raised is, should you be somewhere in the middle of that range? Should you be maybe at the 60th percentile? The question is really for the board to decide whether you want to be in the middle of the range in order to give yourself and the city a little bit more leeway, or whether you always want to be stuck at the median. That is your decision, but this is my expertise in setting the discount rate. And this is my belief, the discount rate inappropriately set in the past. And the board is in the process of correcting that -- that issue. It is almost at the median level, absolutely. The question is, do you want to remain at the median? So every time there's a new capital market assumption, we have to go back and redo an asset liability study, and create a new structure, and transition assets. Which is very expensive. Or does it make sense to give both the plan and the city a little bit more leeway, and be a little bit below the median? I think what Cheiron is suggesting, to be more in the middle of that best practice range.

>> Russell Crosby: It is also important to note that this process started before Cheiron ever appeared on the scene. That both GRS and Segal RFPs that ended up with us having Cheiron. So it ain't the staff. It ain't Cheiron. It's the nature of the problem that you've got and you now have three actuaries who have come to the same set of conclusions.

>> Sean Kaldor: Vince.

>> Vincent Sunzeri: Call me naive, I'm not a politician. I'm a little offended by some of the comments that I might be or board members might be influenced by politics. I wasn't tapped on the shoulder to join this board. I'm a

taxpayers, I have parents who are retired on disability in the police department in other cities, active in safety and other cities. I look at the picture holistically, frankly. I work for a full-service financial firm that is global in nature. They are driving down their return assumptions. And I sit down with individual clients on a daily basis. And imagine, having to tell those people, because of the climate that we're in, they have to change their standard of living because returns rcht what they are. Folks, things are changing. People have to adjust to that. I think we have to live in reality instead of the illusion that we're going to be seeing exceptional returns. So my perspective on this is from a financial perspective, from the help of the plan, and the benefit of the ultimate beneficiaries of this plan that the assets are going to be there for the future.

>> Sean Kaldor: Sean.

>> Sean Bill: So you know I would be kind of curious to take the temperature of the board. I'd like to see you come towards a consensus. Last time, it was 7.25 in one camp, 7.5 in one camp. Is there a happy yeem? What is the classic, when you make a good deal, no one's happy, right?

>> Sean Kaldor: In responding to that my thought would be we have the information to go to 7.5, let's do that. We finish the asset liability model and it comes back in a month or two and we want to pretalk about the follow year's assumption we have a model and we know we can move to that I'm completely open to do that. Normally we would wait a whole year to do that right? But there's no reason we could bring it up maybe after the retreat, would that study be done by the time of the retreat? Is that an option?

>> Russell Crosby: Are you going to have the LM ready for the next investment committee meeting?

>> Sean Kaldor: For them to brit to the retreat.

>> Carmen Racy-Choy: But the investment committee could decide they want to do further analysis. I might say there is a good chance it might be but I can't promise.

>> Sean Kaldor: After the retreat or the following month, bring it back, here is the efficient frontier and where we think we can reduce risk and the best return for 50-50 then the analysis has been done.

>> Sean Bill: How do other board members feel? Is everybody still in the same camp, nobody has really budged it seems like to me.

>> No.

>> Sean Bill: Okay.

>> Sean Kaldor: So is there a motion on the table to change the discount -- oh, I'm sorry, please.

>> Frank Lovato, police officer in San José also chief financial officer of police officers pay 17, just under 17.5% to the retirement system. If we move to the 7.25 that's going to put their contribution rates at 20.2% roughly, that's a tremendous amount of money for them to go up. Each incremental step that you take causes our officers to pay more. Cheiron here has made reference to buying down the rate, that extra money that this retirement system has now found they have with assumption rate. There is no extra money for our police officers and firefighters have 50 police officers leave the City of San José and take jobs in other departments who pay contribution rates at about half that. We're going to continue to see those people leave. And it's going to continue to affect the volatility of this plan because they will be leaving because they can't afford the plan. Now as we sit at the table and try to come up with retirement reforms we are looking at solutions to this. This is an all encompassing group of people, we have to stay this slowly and incrementally trying to take the solution without taxing any one person too much. Thank you.

>> Sean Kaldor: 10.6 or lerch.3 and if we went to 7.25 it goes up to 12%. So I would be concerned where the he discrepancies is between the 20 and the twill.

>> Gene Kalwarsky: The OPEB. Bill and I were talking we're still not sure how the discount rate itself would have a 3% differential. We don't have any information in that regard.

>> Russell Crosby: Probably embedded you have the increase in OPEB which is a negotiated step that goes up.

>> Sean Kaldor: Just talking about taking out of their paycheck it's going to be a quarter of -- 20% of their pay after a quarter.

>> Gene Kalwarsky: It's just the 70 basis points you see up there.

>> Sean Bill: This is where this is a hard decision in terms of the fiscal impacts. You know the employee rate goes up on their contribution in, city rate goes from 50 up to 63% of payroll. From away I see here. I mean, certainly, big impacts.

>> Sean Kaldor: Sean, that's my thinking. Let's make sure we're doing this right. Ifpoint let's make sure it's absolutely the right thing to do. I'm sorry. Drew.

>> Drew Lanza: We've talked earlier about the notion of underlying velocity. I've heard the notion of going fast we might cause pain. Carmen we roughly reset this once a year, roughly?

>> Carmen Racy-Choy: Yes.

>> Drew Lanza: Okay and the new normal based on sort of what you're saying with professors and stuff, the new normal might be 6%, what is this historically, we could be heading towards a regime of long term 6% this could be happening.

>> Carmen Racy-Choy: I think.

>> Drew Lanza: Let's just assume that's right, okay, if we're going to tweak this a quarter% at a time to get from 7.75 to 6 that will take us a decade longer so the underlying if we believe which as I believe going back to what Vince said, if we believe the new normal is a substantially new which a lot of us do believe and if we're at 7.75 and the new normal is around 7, say 6, if we're going to move at a quarter percent per an up, it's going to take us five or six years to underlying velocity we have to match. It seems to me we don't want to move a percent at a time but a quarter percent may be too small. A half a percent can allow us to move from 7.75 to 6 in a couple of years. So to the extent we are trying to track to something I worry that a quarter percent at a time is too small a comment on that.

>> Go.

>> Carmen Racy-Choy: I would say the ideal for a pension plan is to be below the median, by to be somewhere around the 60th percentile which approximately for this plan would be 6.5, something around 6.5, 6.75. I think that's kind of the ultimate goal starting from 8%. I think the message has always been, just, that. How quickly we get there depends on the board. Staff is committed to continually bringing to the attention of the board this issue, until we get to a comfortable range. A question is: Is the median the comfortable range. That is for the board to decide. I think ultimately if the board stands on the fact that we would like to be at the median, with absolutely no margin for error, that is your decision and staff would respect that but ultimately until we hear from the board, an instruction that we will not go beyond this point, we're going to continue to come forward every year and bring this to your attention. Now, with respect to, is it a quarter or a half basis points better, that's hard for me to comment. I think definitely, if you move faster, I mean, everybody's mentioning the increase in contribution. And I totally understand that point. Because my contributions are also going up. But what -- the understanding needs to be that it's both the city paying more and the employees are paying more. And the reason they're paying more is because benefits need to be paid. And the funding situation for both plans is -- actually needs to be improved. Yes, there is a significant payment. Yes, both parties will see their contribution increasing. But this is what's actually going to do two things. One, ensure the benefit gets paid and two, stabilize the employee contribution. Way think all of the members do not want to see is a continuing -- a contribution that is spiraling out

of control. This -- what this is going to result in is the city doing the type of drastic action that you it did over the couple of years, in layoffs and in pay cuts. Staff would like to see a flat contribution rate. Whatever the right rate is, let's keep it flat, in order to avoid the type of actions that have been seen. And the only way to accomplish at a is through taking risk -- that is through taking risk off, lowering the discount rate and giving yourself a little bit of breathing room. So is it 25? Is it 50? I think I would agree with Cheiron, that even if you reduced it to 7.25, next year will bring back the topic of lowering the discount rate. So I think the key is, I don't know that this is something you will be hearing about. At least until we get to 7.

>> Sean Kaldor: Bettina. Beds I'm not a financial person and certainly have struggled with our own finances so I do agree that we should be lowering the rate, probably to the 7.25. But I think to Sean's point is a very logical one that I would support. Being able to explain exactly why we do that if that's the decision is the right way to go. And I think that if we as a board can explain and communicate fully why we're making this decision, then everybody wins. Even though there's sacrifice.

>> Sean Kaldor: Dick.

>> Richard Santos: Yes, there's so many buzz words, you know we all want to be comfortable. Stability and flat rates and all those good things. Tell me whatever we do, does that last only for one year?

>> Russell Crosby: Correct, this year and November.

>> Richard Santos: Bettina was saying and so was our chair, we got more information coming. I think 50-50 is the place to go at this time. We're all trying to de-risk all the issues here. It's tough. And so many things are pending. I still don't understand the hiring and so on. Because when you don't pay, it has effects. There are so many other variables that we ought to take a look at. We got the whole yier to look at that. I'll support the chairman's motion, as a second on this. I believe 7.50 is the right thing to do. We've got so many other things to do, the retreat, understanding so much more, I believe once we get a hold on what we believe as a board to be doing, we're going to be giving this leverage I know to make Moyer money and make more decisions.

>> Sean Kaldor: I think Dick alluded to me making a motion. I'll make a motion to be clear. Hearing what's been said and hearing the questions from Sean and Bettina and Drew and Vince and nrve this process, I'd like to make a motion that we stay at the 7.5 discount rate and as soon as the investment committee gives us a good analysis of what a future discount rate should be, we can put that on the agenda and consider the discount rate for next year and not wait until the though planning process.

>> Richard Santos: Second.

>> Sean Kaldor: Motion and second and now it's open for discussion. Damon Pete then Vince.

>> Damon Krytzer: There is not going to be one month we come to that we don't have new information one two three four months away. November is soon, in public plan world, right? Which means we're probably going to make a decision by February or March of next year as well. I feel like we have all the information that we needed to have to make this decision in the first place. So, you know, continuing to put this off further and further and further just doesn't really seem to be a great idea to me.

>> Sean Kaldor: Pete.

>> Pete Constant: I just wanted to make one comment that didn't come up. If you go to a 7.5 you're basically making a move where it's more likely than not that you will not achieve that result in returns. And what happens, while there is an impact to employees, that 70 basis points as been pointed out this year, when you miss your targets, there is another impact. And that is, the burden gets shifted to the taxpayers in an unfunded liability. And that transfer of risk is something that has occurred year after year after year. Here we have the city that's set a goal of a 50% likelihood. We have our professional staff. And we have the professional actuaries making a recommendation to minimize the risk of that transfer of liabilities. I just wanted to make that statement because that part hasn't come up yet in this discussion. Thank you.

>> Sean Kaldor: Vince.

>> Vincent Sunzeri: Well I think it's important to understand the work on the ALM is going to drive towards the starting that's selected here. So if in fact we're going to 7.5 she's going to create an ALM and an asset allocation based around that number. Which means you're going to have a plan that will have more volatility and more risk than if you select 7.25. If you select 7.25 the ALM work will be done based upon that number. So thinking that, pushing this back to the investment committee and the work on the ALM frankly you're making the decision for them what number is going to be focused on, not vice versa.

>> Sean Kaldor: So would that should that then I was looking at the ALM study and it had several different portfolio assumptions and found one that has less risk than we currently have in the plan but a 7.5 return. Maybe that decision doesn't have to happen at the investment committee but deciding really looking for that efficient frontier level needs to happen here right? So would it be more appropriate to come back to the board and say we looked at these various different portfolios and based on that this is where we should sit to minimize risk and maximize return. Is that should --

>> Carmen Racy-Choy: I think this is happening at the investment committee. The investment committee pointed out is, the problem with that position is it odes very low allocation to fixed income. The plan would experience severe losses considerably more severe than peer pension plans. And so the moment you increased the fixed income allocation to try and deal with this exposure, you reduce the expected return to around 7.25. Just to give you a sense, the Federated plan, they made the decision to go to the discount rate of 7.5. So through the ALM their allocation to liquid fixed income is 5%, 5. This is 20% below the average public plan allocation to liquid fixed income. And the reason is, if we are to get to a long term expectation of 7.5 at the median level the only way to achieve that is to reduced fixed income. Again, the exposure and the problem with that is it leaves the plan very exposed in a deflationary environment. And so it is a tradeoff. And this is what the investment committee is currently wrestling with.

>> Sean Kaldor: Vince.

>> Vincent Sunzeri: We're spending a significant amount of time in deliberating frankly I think we should do that. For what they adopted as their real asset return its 20%. I just attended a workshop with our consultant with 12 systems there. And Dallas was the only plan in the system that was even close to having a high return to real assets. Two things came out of it. Number 1, they were down in 2008, 23.8%. How much was our plan down in 2008, Carmen, do you recall?

>> Carmen Racy-Choy: Minus 18%, approximately.

>> Vincent Sunzeri: A plan that has a high real asset allocation went down more than our plan. And that's what we're talking about doing, moving in that direction. Number 2, on a liquidity basis, because of the fact they shifted they had less liquidity. They had to borrow $350 million to meet obligations. I don't want a plan in that situation, folks.

>> Carmen Racy-Choy: I just want to add, the assumption that they achieved an additional minus 5% because of the real asset allocation, is an assumption. Our real asset -- the volatility of our real asset portfolio is actually lower than our equity volatility. And we've constructed specialized benchmark, risk parity benchmark. And we actually asked first quadrant and Credit Suisse for linkage with inflation but reduces very significantly the volatility of that asset, of that asset segment. So does this mean that if the equity market crashes, our risk parity benchmark would not crash? No it would, but not to the extent of the equity markets. And this has been tested in the recent down turns, where the risk parity benchmark was actually significantly higher than equities and significantly higher than either the Dow Jones or the goldman Sachs assets. This is in order to keep the fund sound in a high inflationary scenario. We have implemented in a very thoughtful way that doesn't result in significant losses and stress environments. And I do believe that the numbers that will come back to the investment committee on the stress testing will actually show that.

>> Sean Kaldor: So Drew, is there anyone else that wants to comment before I call for the vote?

>> Drew Lanza: Good last question then. I was wondering if Russell Carmen and Cheiron would give us their recommendations for 7.25 versus 7.5.

>> Russell Crosby: Well I'll start. Asmen said and we've said, this is a long course. And you've got to get from where you were to some number south of 7. The faster you can do it, the better off you are in the long run. It is really a tolerance for contribution increases and other things going on. As long as I think from my standpoint, as long as we can see that it's a course, and that we're setting the stage for the next transaction and the next and the next after that, I certainly don't have a problem with wherever the board comes out. Because we're headed in the right direction. And if you went to 7.25 this year, for the valuation of last June, come the next one, we're going to be talking about 7.. And so on. And get to try to derisk these plans to get them down to a lower level that then the portfolios can address the volatility question as well and you're not going to have these kinds of swings in contribution rates go forward.

>> Carmen Racy-Choy: I will reiterate I think what Russell has just conveyed in the sense that we feel that the board is engaged very seriously in the process of derisking the plan. And as long as the course is set and we all see where it's ending up. Whether it's 7.5 this year or 7.25, in the overall scheme of things from staff's perspective that's your decision. The question is, how quickly can we get there? The faster we get there, the better it is for the health of the plan. Very simply, because of what it means is the pain, the employees are paying more, the City's paying more, the plans are going to be better funded and this ensures basically a better pension plan. So ultimately, the faster we get there the better. But the most important thing is to simply be engaged in the process.

>> Drew Lanza: Cheiron, do you have a concrete recommendation?

>> Gene Kalwarsky: Concrete. I first twoontd mention I don't think in my entire career I've heard the board discuss the discount rate as thoroughly as this one does. Wherever you end up it is a fafnl being question. that is outs of our purview so purely actuarially speaking we want the 7.25 but we've said to you that we can live with the 7.5 for nonactuarial reasons.

>> Sean Kaldor: Last comment from the public.

>> Thank you again, Robert Sapien for San José firefighters. You've moved your level to 7.75. I've gone to my members, I've already told them increases contributions we've already explained why, we've already explained why a gradual approach is prudent considering their willingness to come to the table and talk about reforms overall and do a multitude of things to get this plan where it needs to be. You've made your move and now you want to make another one for you know certainly as fast as we can make the plan great that's wonderful except to the discussion about what can people tolerate. We're pushing the limits on tolerance for our members. You heard the Police Officers Association say they're losing members left and right. I know I have members that are looking to go elsewhere. What they're really missing is trust in a system that's making changes that make sense. I would strongly encourage you to stand by the change you already made towards derisking the plan. I would ask that you go back and make your moves that are going to continue to derisk the plan. But to do that in the flip of leaves our members in the lunch.

>> Sean Kaldor: With that I'll calm for the question.

>> Mollie Dent: Just remind to you do a rolt call vote because of the teleconference.

>> Sean Kaldor: Understood. How do do I that? One at a time if you will respond. I'm going to call for a vote on the motion. I'll go down.

>> Conrad Taylor: Could you read the motion again?

>> Sean Kaldor: Sure if you secretary could.

>> Russell Crosby: Kaldor motion 7.5 vex rate and as soon as the investment committee can review the investment rate allocation model, review the discount rate and we can address its earlier as soon as the

investment committee and Cheiron are ready to talk about it prior to the next year's valuation. Seconded by Santos.

>> Sean Kaldor: Okay, go down in the order of the agenda. So Kaldor aye. Santos?

>> Richard Santos: I'm. L.

>> Sean Kaldor: Bacigalupi.

>> David Bacigalupi: Yes. Oorks rounds, Sunzeri,.

>> Vincent Sunzeri: Nay.

>> Sean Kaldor: Taylor.

>> Conrad Taylor: Nay.

>> Sean Kaldor: 5-four, passes. Sense we've been here a while and interesting discussion. Why don't we take a ten-minute break. There are some slight refreshments there. We'll reconvene, at by that clock, five-past. Thank you. [recess]

>> Sean Kaldor: As soon as Cheiron is completed in the back we'll start. We're just waiting for that.

>> Sean Kaldor: Let's get started. All right. Let's resume with item 3.1b which we've her mentioned on the agenda. Did you want to discuss valuation and administrative expenses?

>> Gene Kalwarsky: Yes, we're -- this is more of an informational item. Bill's going to lay out for you what the issue's been and what's been done historically. And I'm clearly certain that we're going to rely on counsel to offer

an opinion. There's no recommendation coming out of that and reciprocity is mower of an informational item. Don't expect any deep actuarial analysis like the prior session.

>> Sean Kaldor: Okay.

>> Bill Hallmark: So the issue here is in prior valuations there was no explicit assumption for administrative assumptions or transfers to the SRBR. We recommended and the board adopted explicit assumptions as an addition to the normal cost. The coat requires the nor cost to be split between the city and members in the 8-to-3 ratio. The question is should these costs go into that eight-to-three plight. As Gene indicated it's not really an actuarial question, it's more of a legal question. So we wanted to just provide some background on how those costs were embedded historically in the system to help enlighten the legal analysis. Essentially, to the extent the expected cost of these benefits was embedded in the investment return assumption, there was some sharing between the members and the city as a part of the normal cost. Any unexpected costs or deviations from those expected costs were clearly picked up by the city. The city also would pick up a portion of the expected cost through the UAL due to a change in the discount rate. So we went back to Segal's economic assumption analysis for the 2010 valuation, to see how they determined their assumption and whether there were adjustments for these things explicitly. The short and sweet of it is, for administrative expenses, they made an adjustment of 10 basis points in the development of the expected return. And then, they explicitly said they did not make any adjustment for the SRBR transfers. So that's the extent of what we have to say, really, about the historical practice and how those costs were split or not split. And so I guess I return it to cark Carmen or Molly.

>> Carmen Racy-Choy: Bill, just a question. Could you mention to the board approximately how much was being shared through that 10 basis point deduction in the -- in arriving at the net investment return assumption?

>> Bill Hallmark: Yeah, yes. We did some conviction calculation on the valuation results not the prior investment results. it changed the total normal cost by about $1.7 million and so then that would have been split 8-to-3. It also increased the UAL arrangementsization payment by I think it was 2.5 million which would be totally picked up by the city. Now that impact is going to vary depending on how well funded the plan is.

>> Carmen Racy-Choy: So I guess the question is, there's a $3 million now explicit assumption and the question is should this be split with using the 8-to-3 ratio. The past practice as Cheiron has provided, approximately under the past practice maybe 1.7 would have been split between the two?

>> Sean Kaldor: The administrative expense?

>> Carmen Racy-Choy: In administrative expensed and the rest which is approximately the difference between the 3 million and the 1.7 would be picked up by the city through unfunded liability process. And just to be clear, Cheiron and staff believed that picking up part of the administrative expenses through the unfunded liability is not a sound financial practice. You only want real losses and real gains to flow through that component. And where we have a reasonability expectation of what the expense is, you actually want to have an explicit assumption for it. So that's the rationale for the change. And what wasn't clear is just how the cost-sharing would power .

>> Sean Kaldor: Mollie.

>> Mollie Dent: So normally, a cost split would be split by the city in an 8/11, 3/11 ratio. Part of the administrative expense plight in that same ratio, the 1.sen million that was mentioned . There's clearly no problem for the board in moving forward with that. The issue of whether or not the board can by virtue of declaring a new normal cost, cause a shift in that expense from the employees -- from the city to the employees, is, I think, an open one. In the sense that it is a normal cost under the plan. So if you call it a normal cost, normal cost are split 8-3. But it hasn't been called a normal cost in the past, so I think there could be some risk to -- in terms of doing that. Job of I don't know to what extent there's any public testimony on whether it should be done or could be done, or whether anybody cares that it's done that way. I would also note that there are administrative expenses of course associated with the OPEB plans too and there because all costs are split 50-50 on the OPEB man's it's not going to matter. I'm assuming the $3 million number does not include the OPEB.

>> Sean Kaldor: Is that correct? I don't see anyone running up to the microphone or do we? [Laughter]

>> I think it's real important before this gets passed along, as a normal cost, and the obvious implications of that is to look at the bargaining history of how this benefit came about. I would strongly encourage this board to really understand how this benefit was developed in terms of the structure, as it relates to the plan, and then how it relates to member contributions. So I really hope that you dig deep and understand how this thing was put together.

>> Mollie Dent: So I want to say I was just speaking of the administrative expense at this point. I wasn't speaking to the SRBR which is the benefit. Because clearly, historically, the SRBR wasn't funded it was set up for money to go into excess earns.

>> Sean Kaldor: How was it set up then?

>> Mollie Dent: It was set up out of excess earnings and for the SRBR there is a mechanism in the SRBR where money actually goes back to the city in some years. Where there's no mechanism for money to go back to the employees in some years. I think there's some legal basis for splitting at least part of and maybe all of the administrative expense with the employees. I would not reach the same conclusion on the SRBR expense.

>> Gene Kalwarsky: Sean, can I just supplement something she said, the UAL so in the extent you can say the city has paid for it all .

>> Mollie Dent: That's correct, that very clearly is that it has been.

>> Carmen Racy-Choy: The practice continues. I think the reason we are discussing the admin costs, now that we're explicitly funding it, we nted to make sure there was discussion on how the sharing should happen.

>> Sean Kaldor: All right then I'll -- nope.

>> Alex Gurza: Alex Gurza again. On the administrative expenses you know, at least from my perspective, if it's going to be a normal cost then I don't know what the basis would be to share a normal cost in any other way other than the 8 to 3 split unless something else is arranged for that. In terms of the SRBR, I understand historically, the if the SRBR is going to continue I think forward and how it would be split since it would be a change.

>> Sean Kaldor: All right, so we need a motion. What I'm hearing is it sounds like administrative expenses are pretty straightforward. But SRBR, we're hearing legal advice that it's probably not best to change -- it's been a city expense funded through unfunded liability, probably not best to charge employees. Should we implement it that way and then if the city wants to come back and say no or work out with the unions or how do we --

>> Mollie Dent: Well, yes. Mr. Richeda is pointing out that SRBR isn't actually agendized. It's on the slide but we don't have it agendized. Because I think the discussion was already had on the SRBR.

>> Carmen Racy-Choy: Exactly. I think there was a conclusion that since the city was always fully paid the expense that would not be charged to the employees. So we've continued with the practice. Although there's now more explicit funding. On the admin expenses, I think the issue is that only a portion was shared and the other piece was picked up by the city. And so we want to confirm how the cost-sharing should now be happening on the 3 million.

>> Sean Kaldor: Why was the rest of it not shared previously?

>> Carmen Racy-Choy: Because the rest of it flowed through to -- it became a loss. The loss became an unfunded liability and the city picks up the unfunded liability. Since the practice of pushing a portion of the unfund -- basically pushing a portion of your admin expenses which is a very predictable expense, 20 years into the future, making it a loss, and making it getting amortized over 20 years is not a sound financial practice. The unfunded liability, I would say, process is there for real gains and losses. Like investment, to deal with investment gains and losses, and maybe even mortality gains and losses, if there are significant ones. It's not there in order to push into -- 20 years into the future in admin expense.

>> Sean Kaldor: I don't see anyone jumping around. Oh we do please.

>> Vincent Sunzeri: I just have a question on DB plans versus the DC plans. In the DC arena, at least my observation is that the employer tends to pick up most of the cost. And I'm not sure if that's in fact true or not. On the DB side, is there any kind of practice that's standard that you see on the admin expense?

>> Carmen Racy-Choy: I'm going to ask ciernl because they've seen a larger number of public plans, to address that component. But based on my experience, it really depends on the plan sponsor. There are a lot of plan sponsors for example that have said they never wantedto the employee contribution to go over 9%. So you design things around that. On the admin issue I think the key is if there is an agreement between the employees, and the city, to administer, to divide the expense in a specific way, that's what we need to administer. I'm not going to talk about general practice. But maybe Cheiron can provide further input.

>> Bill Hallmark: I think the administrative expenses are clearly an expense of the plan. Who pays for them depends on how the strurgs of the 34R57B were set up. And most I've seen define the member contribution independent of everything else. And so they'll set a specific rate that members pay, for example, or a method for calculating the rate members pay, based on their date, their age at hire. But it is independent -- it's not a proportion of the normal cost like it is here. So I think that's what's unusual in this situation, is defining the members' contribution as a proportion of normal cost that then creates the issue.

>> Mollie Dent: So that was going to be my question really.

>> Gene Kalwarsky: To supplement his answer. I agree with him totally and that's maybe 98% of the plans out there. But I have experience with some other funds that do have proportional sharing and in those funds it still is implicit in the interest rate. The interest rate is lower than otherwise so therefore there's an implicit sharing for those.

>> Mollie Dent: So that -- my more direct question was, to what extent is having it be an explicit normal cost like it's being recommended here versus it having been embedded in the discount rate which is how it was done in the past, are we the only ones that are doing it as an explicit enroll cost or is that commonly done?

>> Gene Kalwarsky: It's common and it's split. I'm saying those few funds that have an explicit portion that I'm aware ever it's not explicitly recognized.

>> Sean Kaldor: Russ, did you have --

>> Russell Richeda: Two points the board might want to consider. Right now the board doesn't have before it a very extensive history of the practice. They have the 2010 Segal report. Edon't know at this point to what degree that has been the case for let's say, the prior ten years or whatever the appropriate time period, or whether there's been a bouncing around. Because I'm concerned as Mollie about practice. You have a Muni code term that's been in the code for a long time. And to the degree there's a consistent administrative practice, there's at least some support under administrative law doctrines that that's what that section means. And it can be enforced against the plan. But if there's no real practice, then that doctrine doesn't necessarily apply. And I think at this point it's not exactly clear whether we have an engrained settled practice. But number 2 I seem to recall and probably people in the audience will recall more, that there was actual contracts, MOAs between the bargaining units many between the POA, the firefighters and the city. I think sometimes they were tripartite agreements governing administrative expenses, it had a cap et cetera. I never had a look at those. I don't know if there is something germane on this issue but it seems like there might be and perhaps that can be investigated and that might again provide some context to this.

>> Mollie Dent: I think we can look at the bargaining agreements but the code does say that administrative expenses are to be paid out of the fund. But it doesn't say who pays.

>> Sean Kaldor: Who funds the fund.

>> Mollie Dent: Which side of the fund to the fund pays.

>> Sean Kaldor: Alex did you want -- is the prudent course of action to as Russ is alluding to, what is the best way to treat this money or is it --

>> Mollie Dent: Well, I don't think we can -- i don't think the legal analysis would be.

>> Sean Kaldor: Or contract analysis.

>> Mollie Dent: What the practice has been? I think that -- we can look at it more, but I would understand the Segal letter to be documenting what their practice had been for however long they were the plan's actuaries, anyway.

>> Carmen Racy-Choy: Yes and I've read --

>> Mollie Dent: I wouldn't view that as any other information and I see Alex got up to speak so he may want to talk about what he knows about what's in the bargaining agreements about splitting of cost. But --

>> Sean Kaldor: Okay. Carr melon did you --

>> Carmen Racy-Choy: I just wanted to confirm that I've read prior recommendations on the discount rate coming from Segal and that they used the same methodology which means they netted a certain amount of basis points for expenses. So the practice that Cheiron has described, in the June 30, 2010 I believe recommendation, was consistent with the -- at least one or two prior recommendations.

>> Sean Kaldor: So it would be consistent to treat this as a true normal cost and charge it according to the 3/8 ratio split.

>> Mollie Dent: A portion, that would be the problem. And every year that portion would be different. Because a portion of that cost in the past would have been 100% assigned to the city, based on what the UAAL was and a purges would be split in the 8-3 ratio.

>> Carmen Racy-Choy: That's right. And based on the 10 basis points and the current valuation, I think Cheiron has expressed that that portion that was split would be physical 1.7 million so approximately 50% of the cost. And the other piece that would have been picked up by the city is --

>> Carmen the 1.8 million would be split 8 to 3. is that correct.

>> Carmen Racy-Choy: That's the portion being split as opposed to right now the 3.

>> Gene Kalwarsky: That difference is about $350,000.

>> Sean Kaldor: We can't just say going forward half of the administrative expenses will be split by that ratio because that changes over time, sometimes more, sometimes less?

>> Carmen Racy-Choy: I mean you could pick up the rule and ask the actuary to follow it but I'm not sure what basis you would have --

>> Drew Lanza: Was there a rule before, could this be codified or was this just --

>> Carmen Racy-Choy: I think the practice was the city and the employees were paying for only half, approximately, of the overall admin expenses. And I think Cheiron has recommended and you've approved in prior board meetings the fact that the full $3 million which you know should be paid up front, rather than just a portion of it. Now, the past practice on paying the $3 million was that approximately 1.7 of the 3 would be shared using the 8-to-3 ratio and the rest would flow through the -- would become a loss and flow through the unfunded liability and would be paid by the city. The question now is, this was the past practice. Now there are very good --

there's a very good actuarial rationale for front-ending the full 3 million and that's the right thing to do. I guess the question is, how should the cost-sharing be handled.

>> Sean Kaldor: Russ.

>> Russell Richeda: And what is the matter for me is we seem to be hearing the past notion of normal cost that we are employing really is not in accord with the kind of actuarial analysis and principles that you'd use to interpret that concept. In other words even if there had been a past practice, that practice exists uneasily with the way it properly should be. And so, of, does the board restain the discretion to modify what they'd been doing in the past even if it amounts to a past practice?

>> Mollie Dent: I understood what the actuaries were saying is that actually, plans that operate like ours do. There is no -- there is no right way to do it. Some of them do it through the discount rate and some of them do it as a normal cost. It isn't like one is right or wrong. If I misunderstood, from an actuarial standpoint. So that's where you do really get into a matter of the practice.

>> Carmen Racy-Choy: I don't disagree with that assessment. The reason we're front-ending the full 3 million is because it's not sound to pay up front the 1.7 million and take the other 1.3 million and defer it over 20 years and pay it through the mortgage approach. If the admin expenses, $3 million, the admin expense should be paid up-front. The -- and so there is a reason for the change actuarially. And the adopted recommendation has reasons, Cheiron recommended the change for a reason. So I wouldn't say actuarially it's all the same. But I think the question is just how should, now that we're front-ending the 3 million how should the sharing happen.

>> Mollie Dent: I'm not saying it was all the same. I'm saying there isn't a right or wrong way, some plans do it one way, some plans do it the other way. Sometimes the board goes forward with changing it to normal cost but when do you that that board decision and how that plays out in terms of being able to change a past practice, that basically results in a different splitting of the cost, is the problem.

>> Sean Kaldor: Vince.

>> Vincent Sunzeri: So I mean first of all the new structure to me is is a lot more elegant in terms of trying to understand what's happening within the plan. But I have a question and then I want to introduce another interesting aspect here. The question is pretty simple. What falls under administrative expense?

>> Carmen Racy-Choy: Good question.

>> Sean Kaldor: It would be the contracts with Cheiron correct, the contracts for all of retirement services staff.

>> Carmen Racy-Choy: Pretty much all the investment staff, all the accounting staff, all the benefits staff and all of your consultants. This is like kind of a broad brush, I'm sure there are a few smaller categories as well.

>> Russell Richeda: The premium for fiduciary liability insurance.

>> Carmen Racy-Choy: Absolutely.

>> Vincent Sunzeri: The reason I bring this up, how this changes also impacts to some extent the discussion on another topic which is staffing. All right? If it's shared then it's a conversation that changes a dynamic at the board level in my mind. If it's not a shared level of compensation, if it's completely funded and I'm not saying that's how it's going to go but if it's completely funded by the city it takes a lot of control away from decision-making on compensation levels for staff away from the board directly into the hands of the city. I don't know if that's a fair conclusion to jump to but that's how I might look at it.

>> Sean Kaldor: It seems we don't have enough clarity to take a long term decision on this. Could I float the idea that we might split the administrative cost in the same percentage it was last year, through three-8 and the other goes to the city and ask for a detailed analysis from the bargaining units and the city and determine what the long term split of the cost is? Does that seem a workable solution?

>> Mollie Dent: If you are looking at the historic split of cost then the 1.7 would be split 8/11, 3/11 and the on the decide if you are looking truly at the historic split.

>> Sean Kaldor: Mr. Gurza.

>> Alex Gurza: One thing I wanted to mention, there are no labor contracts that specifically states how are to be split, curchlt it's not Police and Fire that you have total assets as how much those were. So those were explicitly and still exist in some of the Federated contracts. But it doesn't specify and I have sample language in front of me, it doesn't specify how it was going to be split. I think you know what I would recommend the board is, to give time for this issue because clearly if you're going to make it a normal cost but yet then say it's not going to be split 8 to 3 I think I myself have questions about how that would be? How you have a normal cost, determine it's a normal cost but not split in the same way as any other normal cost. I think it bears further research and discussion.

>> Sean Kaldor: Would you be often to what I propose? At some point we need to write a bill to the employees and the city are we already past that date? Would that be one way to approach this year and then whatever ultimate decision is decided could be retroactively in the.

>> Alex Gurza: If I understand correctly what you are saying is at the end of the day there's no change between how it gets split between the city and the employees?

>> Sean Kaldor: We can talk and analyze long term now that it --

>> Alex Gurza: To be honest I think we'd need knead a little bit further time to further consider that.

>> Sean Kaldor: Thank you. Mr. Sapien.

>> Yeah, I would offer the same advice at this point, is there is quite a bit of history with this particular benefit and how it was implemented and who was and wasn't at the table. Certainly, nobody wants to put their head in the sand and act like it's not a cost, and we want to recognize it at some point but we want to do it right and understand the bargaining history behind it. I would encourage the board to proceed judiciously and make sure that we know exactly where it should be assigned. Thank you.

>> Sean Kaldor: Mollie, what's judiciously?

>> Mollie Dent: Well, fifort we're not talking about a benefit here. We're talking about an administrative expense. Just so that we understand. The SRBR is done. And we'll talk about reciprocity next but that's real simple actually. So we're talking just about the administrative expense. And whether or not you need -- and some decision does feed to be made on it in terms of how it's going to be allocated. It's not a huge dollar amount either way. So -- and I think that I don't think -- I don't think that just by putting it over in the normal cost column you automatically can overlook your past history and practice of how were doing it. It's a basis, definitely, for charging it in the 8-3 ratio, it's definitely a basis for doing that on a going-forward basis maybe. But it's not necessarily do you get rid of the baggage of the past history.

>> Gene Kalwarsky: One comment. We characterized the.

>> Sean Kaldor: I'm make the premium lops tesh correct way to treat it and if we need to change it retroactively and credit back someone being over or undercharged we'll do that in the following year.

>> Carmen Racy-Choy: So just to clarify, the 1.sen of the 3 million will be split using the 8-to-3 ratio wile the rest is paid by the city.

>> Sean Kaldor: And I'll ask you to clarify is that how it was done last year?

>> Carmen Racy-Choy: Last year the full expense wasn't front-ended. 1.7 million was front-ended and the other 1.3 or so --

>> Sean Kaldor: Conceptually -- then yes, that is what I'm saying.

>> Carmen Racy-Choy: Okay.

>> Damon Krytzer: I don't -- can anyone make a substantive agreement against that? Like I don't see one. I'd like to hear if there is one but -- okay.

>> Russell Crosby: We're just seeking instruction. We just want to know how to complete the evaluations and get them done so we can establish contributions for next year.

>> Sean Kaldor: So in the absence of clear insight that's my recommendation and I'm asking staff to come forward with us with clear recommendation, that we've thought of this and the other and here is what we recommend. Any further discussion? Call for the vote, the chair, Kaldor yes,
Santos? Bacigalupi? Bill? Krytzer? Lanza, rounds, Sunzeri, Taylor. Motion passes unanimously. 3.1 C.

>> Gene Kalwarsky: This goes the other way around. Bill's going to describe a benefit that we believe should be paid by the city but may have been paid by the members in the past so this works the opposite way.

>> Bill Hallmark: So one of the benefits of the plan is reciprocity for members who terminate employment with San José but get employment with a reciprocal employer. They get a benefit. And our reading of the code was the entire cost of that benefit is to be paid by the city. But in looking at the way the valuation had been done in the past it appears to have been split, 8 to 3. And so we raise the question to confirm our reading of the code, that it should be entirely paid by the city. I will note, it's a very small amount of money.

>> Mollie Dent: Right.

>> Sean Kaldor: Ask you to please keep speaking close to the microphone if you could for the recording.

>> Mollie Dent: And we did confirm that the direction is clear that the reciprocity is to be paid by the city. I'm unaware of any bargaining agreements that say dint but maybe Mr. Gurza knows that they do say something different.

>> Alex Gurza: I do have a little history in the project because implementing reciprocity was my first duty when I was an employee of the Department of specific agreement that the city would pay the entire cost of reciprocity and there's been no bargain since then to change that.

>> Sean Kaldor: Any -- is there any other questions of staff? Is there a motion?

>> Richard Santos: So moved. Motion to accept the allocation for valuation of reciprocity cost.

>> Sean Kaldor: The motion is made to accept the recommendation of Cheiron that it should be a city cost.

>> Drew Lanza: I'll second.

>> Sean Kaldor: Seconded by Lanza. Any discussion on the motion?

>> Just a clarification, this would be prospective change, no look-back of any plus or minuses in the past is that correct?

>> Mollie Dent: That's correct.

>> Sean Kaldor: Role call vote Kaldor aye, Saturdays, Bill acknowledges rks Rounds, suns, Taylor yes. Motion passes, unanimously. Item 3.2. Discussion and action regarding Cheiron's assumptions for the June 30th, 2011 other postemployment benefits plan OPEB actuarial valuation continued from our January 2012 board meeting.

>> Bill Hallmark: So at the January board meeting we presented our recommendations for the health assumptions for the OPEB valuation. The expected return discussion also applied today to that discussion. But in our presentation in January, the City's actuary, John Bartell had raised a couple of questions about our valuation and you had asked us to go back and resolve those with him. The two questions had to do with the health care trend rates for those who are eligible for Medicare and the assumptions for those employees who are not covered by Medicare or not eligible for coverage under Medicare. This chart shows our health care trend rates. The blue line shows what Segal's assumption was for the explicit subsidy and all claims. And then the green line shows their assumption for the part B health care trend. The orange line shows our assumption for the explicit subsidy which is the same as our pre-65 assumption, base the explicit subsidy is based on the pre-65 plans. And then the red line shows what we're assuming for med scare eligible in part B. So essentially we have a lower assumption than Segal did for the post-65 claims but a higher assumption over part B costs. And the explicit subsidy is somewhat higher. We had a discussion with Mr. Bartell and I don't see him today but we noted in that discussion that the explicit subsidy's based on the lowest active plan so we are using the higher trend rates for that part of the valuation. And for on the estimated claims costs, we had a discussion about the structure of your post-65 plans, what benefits they provide, how they're integrated with Medicare and so forth. And really the premiums for those plans are primarily covering co-insurance co-pays the piece that Medicare doesn't pay but those deductibles and co-pays are tied into Medicare's plans. So that's the reason we have a lower trend for those than for the pre-Medicare where there isn't sort of a government control on those costs. So I don't know that we came to complete agreement with Mr. Bartell but I think we ended up much closer, and I haven't heard any continuing objections. In terms of members not covered by Medicare, the issue is primarily for members hired prior to April 1, 1986. They can still become covered by Medicare due to either other employment, or employment -- their spouse's employment. We searched the data and 90th noted that 29 of 808 retirees who are over age 65 are not covered by Medicare. And I think Mr. Bartell was surprised at how small this number was, as were we. And so that concern has dispaided because given the small number it's not really material. So we're back with -- seeking

your approval of our assumptions so that we can come back with a final valuation report. This slides summarizes those assumptions and, for more details, we can go through the presentation we made last month if you need that.

>> Sean Kaldor: Would anyone like to see a review of the presentation from last month? I didn't think so. Are there any changes this month, versus last month?

>> Bill Hallmark: No.

>> Sean Kaldor: Is there any discussion on the presentation? Is there a motion? I'll make the motion to accept Cheiron's report and approve actuarial assumptions for the June 30th, 2011 OPEB valuation.

>> Richard Santos: Second.

>> David Bacigalupi: Second.

>> Sean Kaldor: Second Santos. Any discussion on the motion? Move for a vote, we'll go down the -- all those in favor, Kaldor aye, Santos aye, Bacigalupi, yes. Bill, yes. Criers, yes. Lanza disple yes. Rounds, yes, Sunzeri, yes, Taylor, yes. Unanimously passes. Any other items on the agenda for Cheiron?

>> Gene Kalwarsky: We've got more presentations to give you if you want. [Laughter]

>> Sean Kaldor: Thank you, gentlemen, we realize there's an ebb and flow, we understand these are actuarial rounds. Next year we'll move into our investment mode and such thank you for your presentations over the last few months.

>> Drew Lanza: Great job, guise.

>> Sean Kaldor: Okay later topics. 3.3, update on the analysis of the trustees role on an environment of discussion and negotiations on vested benefits.

>> Drew Lanza: That's Russ and myself, I'm hain to report almost every day swapping e-mails on this. Our goal is to bring this to the offsite for discussion and potentially for some votes. So let me just reframe what the high level question is. It's that question a lot of boards face which is if you think something's coming down the road at you should you get ahead of it? What we're worried potentially coming down the road is the city council, voters saying you need to change the way benefits are handled in one way or another. And the members of the plan saying, well we don't think that's exactly kosher. So the question that Russ and I are wrangling with is to bring to the offsite a list of potential actions we might take if we find ourselves in that kind of a position and then potentially bring up for a vote should we adopt the sort of guidelines or the what we would do if that should ever happen. So I don't want to get into a detailed discussion for that today. The job is for us to frame a picture, Russ has been paint a big, broad canvas for everybody, give a set of what might be the steps we would take, so we can discuss that. Different kinds of steps depending what we want to do and then maybe bring up for a vote should we do that ahead of time. So this is a big broad discussion. I don't want to get into that now. I think that is kind of it. I would commend the work Russ has been doing, it's been grade. He's been forwarding me a lot of people are wrestling with this issue. I think we'll be able to give you what are all the different potential options and put it in front of you so we will have a very broad debate. Again we don't want to have the debate here. Russ we're going to be ready for the offsite for this right?

>> Russell Crosby: Yes.

>> Drew Lanza: Great.

>> Sean Kaldor: Rick.

>> Richard Santos: Cal PERS for those who can go? I'm sure this can come up. Let's say tomorrow whether it be a the city or anyone else does an actuary and we do one and they differ and the voters can go out and say let's go ahead and do that based on that. Woo jeopardize the plan i'm looking forward to discussing this issue.

>> Drew Lanza: It will be fun, I guarantee it.

>> Sean Kaldor: Any further discussion? All right, thank you for your work on that. I know it takes a lot of time. Item 3.4, discussion and action regarding retirees association's request to raise dues deductions. Do we have an update from staff on where that stands?

>> Pete Constant: I might be able to jump in. I saw this on the council agenda I believe for the 14th. So it's moving along with that.

>> Sean Kaldor: Thank you.

>> Donna Busse: That's what I was going to say.

>> Sean Kaldor: What's resolved or what does the time line look like? Dp.

>> Donna Busse: It is an ordinance that the City Attorney has adopted to change the amount of the dues. Mollie you might want to go into detail.

>> Mollie Dent: A few of you have asked for the ordinance change. I hadn't actually agendized the ordinance itself because it's a pretty simple ordinance. I can bring the ordinance back in March if you want but there seems some urgency wanting it to go to council. So the schedule is to go to council on the 14th for first reading and on the 28th for second reading. So it actually is scheduled to be adopted before your next meeting. But what I'll do is, if the draft ordinances get published, I have no problem with circulating it to all of the board members if you want to look at it. And I'll formally agendize it for the 1st but it probably will be adopted by then.

>> Sean Kaldor: Okay, is there comment from the public?

>> Might help, I'm police vice president of the retirees association. Jim Spence couldn't be here, he's out of the country. what I wanted to address, first of all, Jay Wendling the former president was involved in discussions with staff about the language to the amendment. My understanding is from Jay, he can't be here today, illness, that he has had no input into the language. And his understanding was that we would be allowed to review the language, and have a little input before it went to the council. To my knowledge, that hasn't been done. Secondly My particular interest in this is, the side issue of how the process is proceeding. What we did, as the association, is we followed our bylaws. We held an election. We -- an election. We sent out a ballot to our membership. Our membership voted to increase our dues. This was all done in accordance to our bylaws. I have with me in the box there the envelopes that are signed by each member that voted and each ballot. Anyone that wants to look at them, can look at them. Further, I have in my hand, speaking of past practice, a June 24th, 1999, from Jerry Ellis to Ed overton requesting a change of dues from $3 to $10. This was accomplished with no significant hassle. August the 10th, 2007, from Jerry Ellis to tube Weber, request to raise the dues from $10 to $15 and it was done with no issue at that time. In a very ex pee peed yent manner. Both the previous ones were initiated. This one is being for some reason held up for whatever reason. My comment is that in doing it the way that staff wants to do it, by sending out in essence another ballot it will accomplish a couple of things. It will accomplish a cost to the fund to do that in manpower and resources. So I might be a minimal cost but we're talking about saving money here. The second thing it will do, I don't know if many of you are familiar with older retirees, a lot of people are going to say, hey I voted on that once, they're going to pitch it in the garbage can. What is the result of that? There's nothing I read in this gives me what happens to those people that decide not to respond to that. Does their nonresponse constitute a no-vote to the city that says that they're not going to do this? I don't know. I don't know what the reasoning is. My last statement is that our dues increase is a voluntary contribution by the membership. The increase as stated in the ballot is a one-year increase. Not a calendar year. It is from the date that we start taking out the dues to 12 months later. At the end of 12 months later it goes back to the $15. As far as the language that I've read, for the charter thing, I don't have a problem with that.

>> Russell Crosby: Mollie, perhaps you can address why the process is different in 2012 than it was in 2003 and 1999.

>> Mollie Dent: So I'll address a couple of things. When we start -- when we saw the request to increase the dues this year, the first thing I looked at was, what the authority was under the code for us to even be doing the deductions. And our code has a nonassignment provision. So the ordinance is to change the nonassignment provision, so that we can basically validate what we have been doing and have what we have been doing all along be consistent with the code. So I did send a -- the draft ordinance will be posted today. Everybody can comment on draft ordinances. And they can comment to our office, they can comment to city council, they can come to the council meeting. They can do -- so the whole process with ordinances is for there to be a first reading so that people can comment on it, and then a second reading after comments have been submitted. So I do think the retirees association has a copy of the draft ordinance, that is really a courtesy copy because it hasn't even been posted for the council agenda yet but it will be posted today. I misspoke when I said, it will be adopted by the time of your next meeting. It is up to the council whether they adopt it or not.

>> Like I said I had no issue with the draft ordinance. My issue was why we could do this with no problem in a month, these two prior times. Now this time we're playing with it for like three months now.

>> Mollie Dent: So there are two problems. Number 1, deducting the dues has not been consent in the past. And we need to get the authority for you all to continue to do that for organizations that you approve. But in terms of an increase in dues and I'll let staff speak to this specifically. When members sign up to have the dues taken out of their pension payment, they sign up for a specific dollar amount right now. So our authority from the member has, in the past, been for specific dollar amounts of the dues at the time they sign up. We need a piece of paper from the member saying, "I want the dues taken out of my paycheck at," whatever the dues level is as approved by the association. So that we have the authority to increase thx as they come through. And I think that's what staff is going to try to do.

>> Sean Kaldor: Does that sheet say -- like what are the things that you can sign up for, insurance and --

>> Donna Busse: Whists they retire there's a lift of things and it does have a specific amount for each one so they're actually authorizing a specific dollar amount for the deductions.

>> Sean Kaldor: The insurance amounts do they change every year? Do we have to go back to a specific member and --

>> Mollie Dent: It is not a specific amount for insurance you're choosing a plan when you choose insurance.

>> Donna Busse: We do notify them --

>> Sean Kaldor: You don't specifically call --

>> Donna Busse: Like Mollie is saying, they sign up for a plan.

>> Mollie Dent: Every year you sign up for your accuse basically.

>> Sean Kaldor: We don't need to notify then of a change then?

>> I think what we are looking for is to deduct them in whatever amount the association has approved for dues so we can in the future automatically increase them or decrease them as they go up and down.

>> Sean Kaldor: You don't have that for anything else now right?

>> Mollie Dent: We in effect do it for the health care. I don't know what else people sign up for.

>> Donna Busse: We don't change anything without their prior agreement.

>> Nobody sent me anything saying it's okay, if why raise it from 3 to 15. It's okay because the association did in the manner that we have done this.

>> Russell Crosby: I any the City Attorney is saying that's an unacceptable risk that can't go forward.

>> Mollie Dent: I think it's best to have the member's explicit consent to make the deduction.

>> Sean Kaldor: What if we make the change and they say I don't want to pay that much more?

>> Mollie Dent: The plan is to bring back some rules for you to adopt based on how these deductions will be made. I know the staff recommendation is they only want to deduct a different am, they don't want to deduct different amounts for different people. It becomes administratively expensive. If somebody says I don't want my dues to be $45, then I think we're going to say we're not going to deduct any dollars. The way the ordinance is drafted the board is is been going to adopt rules and regulations that gorge.

>> Sean Kaldor: Sounds like where we're allowed to do.

>> Donna Busse: We should be allowed to take dues out. Scwld right so it will be resolved one way or the other, then --

>> Mollie Dent: And we haven't stopped doing it.

>> Sean Kaldor: It is the change of the dues, right, if you say we're going to pay it for 45 or whatever it is, is that a acceptable solution?

>> That's correct. They've done that with the vote we just did. They accepted the additional 28 for one year as with the vote per our bylaws.

>> Mollie Dent: I think, a vote to raise everybody's dues is not necessarily a vote for the money to come out of your check. It's in the. Because some people voted against it, I'm sure.

>> Yes, obviously, about ten people voted against it and I can show you who voted for it because it's all right here.

>> Mollie Dent: But I think next month staff planned to come forward with a recommendation on how the process would work from their perspective. And I think the -- you need to have that recommendation and have that discussion at that point.

>> If I could interject per our bylaws it's a majority-rule thing. And the vote was to raise the dues. Any member, any individual member that wishes not to have their dues raised can withdraw from our membership, and that's their choice. My feeling is, I don't feel that it's up to staff to make that decision by sending out another vote, and then if like I said, a lot of older folks, and -- I find myself in that position sometimes, too, getting a second piece of paper saying, I got to vote again on this? I already voted on it, throw it in the trash and ignore it so they get dumped from our membership rolls when they actually voted to have the donation raised to $28.

>> Mollie Dent: The problem is they didn't sign retirement paperwork to have that taken out of the retirement check. We got a piece of paper from the member that says X dollars. That's what it says.

>> Okay.

>> Mollie Dent: It doesn't say Y dollars. So we --

>> Once again, mine says 3. But they're taking 15, okay? So it's inconsistent.

>> Mollie Dent: And we want to corrects that.

>> Okay, I do, too. But I also want to adhere to the bylaws of my association. My membership has told me, we want to take out an extra $28 for a specific fund for a year and I want to be able to do that.

>> Mollie Dent: It doesn't need to come out of your retirement check. We're not interfering with the retirees association being able to get the dues they want to get. And we're trying to facilitate the members being able to get if they want to have it done out of their retirement check, we're trying to facilitate that.

>> Then if I might suggest the letter that goes out requesting the dues amount not have an amount on it just that they want to be able to take the dues out.

>> Mollie Dent: That's what we're talking about.

>> But my understanding was the letter that was going out as a side note would be to increase it specifically the amount.

>> Russell Crosby: No, we've never --

>> Drew Lanza: It would be whatever dues are.

>> That's what the language would say. But what is the letter that's going to the membership going to say?

>> Donna Busse: You'll be able to review the letter, Jay has already asked that. I've been working on that. What we are asking for is agree to any amount that's approved by your membership, and to allow them also, allow us also to give you the addresses and phone numbers which they're also asking for so we wanted to get their consent for that as well.

>> Okay, but again you are asking for them to agree to a dues increase. It shouldn't asking ask for a dues increase. It should just say the dues specified by the association.

>> Donna Busse: That's fine. We can just say the dues specified by the association.

>> Okay.

>> Donna Busse: Then you also brought up the fact about the cost for us to do this mailing. What we are doing in could be junction with that which we proposed to the board was the option to opt out of the automatic deposit receipts, which pace for the mailing and then some.

>> I have no problem opting out, a lot of people don't want to do the computer thing.

>> Sean Kaldor: That's just an encouragement.

>> Donna Busse: That's how we're justifying the cost of the plan. It's going to benefit us as well.

>> Sean Kaldor: Looks like next meeting we'll have an update on this. So we'll agendize that.

>> Russell Crosby: Uh-huh.

>> Sean Kaldor: Item 3.5, update regarding legal services requests for proposals.

>> Mollie Dent: So a brief update. We concluded our interview processes, our office has been conducting due diligence, and background checks on some of the candidates. I'm hoping to be able to -- we have an appeal period that runs, once we come to a recommendation, then we have an appeal period that runs ten days, so I'm hoping to be able to notify the firms about what the panel's recommendation is going to be tomorrow. Because if I

can do that then we'll be able to move forward to the Federated board later this month. And come back to you on -- at the first meeting in March. So that's the goal.

>> Sean Kaldor: Any questions? Okay. Thank you. Item 3.6, discussion and action on letters to/from the City Manager regarding staff salaries. So.

>> We need (inaudible) on this one.

>> Sean Kaldor: The investment committee took one, direction on this, you might know olittle bit more about it than --

>> Vincent Sunzeri: It was on the agenda. I would say that Federated probably weighed in more on this topic than Police and Fire. In that they weren't very satisfied with the response. My sense on the Police and Fire side was they felt that there might be some room to kind of work with it. But we try to take a little bit bigger picture view of the situation and take it not just so much on compensation but to look at the overall structure of the department. And to think through a longer term perspective ideally what we would like to see. And I would suggest that this is a topic that we are hoping to push to the retreat and really dig in a lot further at that point in time.

>> Damon Krytzer: At some point someone has to -- but we're negotiating and two months in arrears off of letters back and forth that we're sort of signing but not all the -- look, at some point, like someone take ownership, right? And at some point we need to actually sit in front of a city and instead of sending these passive aggressive letters.

>> Vincent Sunzeri: Well it was also my understanding too that they were going to come back to us within a relatively short time frame and I thought that time frame was 30 days or so with their analysis --

>> Sean Kaldor: Salary, compensation analysis.

>> Vincent Sunzeri: Exactly. My suggestion at that time was it was a little premature to come back with a response until we had that information because frankly we'd just be pushed back until they had that data. So I don't think it would get United States anywhere.

>> Damon Krytzer: That's true. There's a couple moving parts to it right? One part of it is I mean this gets to the bigger issue of what kind of control do we have over the staff too over compensation, over hiring and firing and all of that stuff as well. I mean so there's shorter term and longer term issues here, right? I was pretty encouraged, actually, by this letter. In some ways, not so much but in some ways you know I mean it seemed like the synopsis was I'm not going to stand in the way. I don't know what that means, I I'm not going to stand in the way, it doesn't mean we're going to double salaries.

>> Sean Kaldor: At least not do anything.

>> Damon Krytzer: Cied of. Whether or not this is done at the board level or after the retreat, I mean we just need to sit down with the city and figure out what this means and kind of do all this over a few hours instead of over a few months vee ooh alerts.

>> Sean Kaldor: So to that point I had a crch with Matt Loesch, he was a chair of the Federated board and I received on January 27th an e-mail from Alex Gurza saying that this month's Federated meeting the board decided to have two members meet with city administration, we wanted to ask the Police and Fire board if they also wanted to have two members participate. Matt their chair will be one of the two representatives from the Federated board, and they had discussion who would be the appropriate second person. To your point if that's the way --

>> Volunteer Damon.

>> I'll do it.

>> Sean Kaldor: Sit down and have a dialogue rather than an exchange of lengthsy e-mails I'm willing to do that. If you guys want to do something different I'd be willing to do that also. But what they're willing to do on the Federated side seems like the city is willing to have that type of discussion.

>> Russell Crosby: If I may suggest, you now have an HR person, a compensation specialist who is sitting on your board that might be a person to have in the room for this event.

>> Sean Kaldor: Vince then Vivace.

>> Vincent Sunzeri: Ultimately, I think that the dialogue is good to see that we have that taking place. I'm not sure it's getting us too far, are we moving this a nickel or a quarter, is that going to solve the big-ticket issues. Back to the retreat at least the collective board or working in conjunction with Federated to come one a longer-term solution. And in my mind, as a trustee sitting here, with the absence of certain staff members, taking time to get things implemented because we lack the staff, creates a lot of liability for us as trustees. To some extent it is being deflected because we don't have control. But frankly, I want to have control. I want to have control to be able to compensate the people for an appropriate wage, to be able to go out there and recruit away we need. And I think we need to look at it from a bigger-picture perspective. I do like the fact that there will be a group interacting with the city. But I think we need to think long-term about this and see what is the appropriate structure for this board, given the fact that we are working on governance issues, given the fact that the structure has changed. And I believe that this was a significant part of the original recommendation from Cortex, recommendation number 1, diversify your board, recommendation number 2 is to talk about what that control should look like. And in my mind, it doesn't 19 entire -- doesn't mean the entire retirement services department but there are current key individuals that we need to be in the position to drive control.

>> Sean Kaldor: Dick, Damon, Drew.

>> Richard Santos: I think Vince has some very good points and as a group we've been saying I sure don't like it because it shows that we have not been the fiduciaries we'd like to be but I think we're all saying the same thing and I've been seeing it along. I would welcome Bettina's input on the committee only for me personally, did you try, war is easy but did you try? That's what I like to do. You're right about the City Manager's letter Damon. It's encouraging but it doesn't spell out anything. So let's give it a try. I'd like to see a committee. What we would like to do is go over there and have a discussion and then identify what we really going to do. Then of course we have a retreat and we can talk very strong in that meeting, what we need to do is finalize our legal representation. Once we know what that's going to be, then where he can move on from there, if we are serious being the fiduciaries, as doing so it's going to take a little time but right now the cards show that we should be doing that once we get everything else settled then we can go from there so thank you.

>> Sean Kaldor: Damon.

>> Damon Krytzer: So in a lot of ways I don't think we've -- we've been completely fair because again just to reiterate dpik's point. This doesn't say anything because we've never asked for anything. We've never put fort an ask of course we are going to period we haven't asked for how much money, how many -- what do we actually need? Like we've never spelled that out that ave seen. If I've missed it then it's vague enough for me to have missed and I should be part of the ask.

>> I thought it was specific. Go back to the letter that was originally drafted by Federated, we followed up and tached our letters, whether those were right compensation levels is debatable but there were compensation levels from that came back from Cortex and we asked to move wages to that level.

>> Damon Krytzer: Was staff comfortable with those levels? Is that our solution or -- that's our ask?

>> Vincent Sunzeri: Frankly, I don't think staff should be involved in that debate because it's line me asking -- to pay me more, certainly I'm going to want more.

>> Damon Krytzer: I'm not saying to pay me more. I'm saying do those levels allow staff feel like they can go out and do searches to fill the rest of the positions? Are we fully staffed at the staffing levels we've set out given the current market environment? If we get yes from them on this, then we're done, we're good?

>> Carmen Racy-Choy: I think you have a pretty good chance of filling most if not all positions at these levels.

>> Damon Krytzer: Okay. Then that's where we need to go from, right? And that we need to -- we need to get a counter to that. That's a real number.

>> Vincent Sunzeri: Right and I think Damon the counter was, now let's do our analysis and certainly there's other things that weren't taken into consideration given there's benefits and so forth. And that's why I felt like we were at a little bit of a discal-out here because we needed to get that data back first.

>> Damon Krytzer: So we don't have a bat in it either, we don't have our, what's our recourse by saying if we don't have a response by this date then we don't have that. So why don't we come up with a time line whether it's right here, I mean we can't really defer to the offsite, that's way the heck out there in time, right? So I kind of feel like we at least need to come one a concrete next-step at this meeting.

>> Sean Kaldor: Drew.

>> Drew Lanza: That's the same way, what I want to talk about. First reacting to Carmen. Compensation and what Dick alludes to, control. The City Manager is only addressing one of those two concerns. There is a larger bailiwick we are multiple paths in parallel. This is burn some cycles because we'll fru four paths, only pick one in the end. But for cycles. I think the way I've been working with Russ on this other issue which is similar in the sense that you sort of twoontd reach out to other parties and find out what other funds do put down your options and put down a broader debate has been pretty good. Mr. Chairman, I suggest you pick one of us and say go, right? Figure it out, talk to other pension funds, find out what the options are, give it to us as a laundry list or menu list and I think we'll have to talk about it at the offsite, we have to agendize it and everything else, dealing with the

correlated issues, one of which is compensation and the other of which is control. Look being broadly across what are owrps it's working well for us Russ, two guys can really get a lot of stuff done.

>> Sean Kaldor: This was talking about a custom of delegates meeting rks entire long federal structural and operation, an I don't know if the two people can go and see if we can try to do something to fix the problem in the next six months. The ad hoc committee specifically dedicated to this.

>> Drew Lanza: I wouldn't recommend a committee because if you are one or two people can do that and I think you're saying what Vince said, I think Vince said it really well, it's okay to do all of these things in parallel, this is such an important issue, let's send our delegates to do that. I can see there being three or four l distinct paths and we've all talked about it. If you delegate to it a committee it will take forever but if you delegate it to one or two people it will.

>> Pete Constant: I wanted to comment on the overall process talking about two different things, compensation level and the control level. So the compensation relates to classifications and pay rates and things like that which are under the City Manager's control but ultimately go to the city council for approval. And also, require budget actions by the council. So that's a whole process. Keep in mind that we are starting, I think, on March, I want to say 8th or something like like that is when the Mayor's Budget Message comes out that sets the course for the entire budget discussion between March, April, may and June to get us to a budget starting July 1st. Depending on the timing you have to be conscious of the budget action the council is taking. In the area of control, that is a whole 'nother issue which quite frankly is outside the City Manager's control to control the control, that rests with the city council and potentially the voters. Because I'm not sure if that's something that would just be an ordinance or if it would affect the charter. Because our retirement systems are referenced in both and I don't know the answer and that's something that we'd have to be have looked at. And if it's an ordinance thing then obviously the council has the ability to do that. Almost on any given Tuesday that could happen but there's a process and the time line that it takes. If it's a charter issue, then that takes a lot longer because anything with a charter takes a vote of the people. So just keeping in mind those are different paths that may be taken concurrently or excessive consecutively or in any other matter.

>> Sean Kaldor: Vince.

>> Vincent Sunzeri: To explore current compensation issues i'm morning willing to be part of a different team looking at a longer term solution. And anyone else that wants to join with me in that regard.

>> Sean Kaldor: Okay, so I hear a recommendation, I'll turn it into a motion. That Bettina and myself respond to the City Manager's office request to have a couple delegates try to work through the current compensation and that we'll establish an ad hoc committee to look at that time appropriate short and long term steps that are necessary for retirement services staffing. Getting all this Russell?

>> Russell Crosby: Yes.

>> Sean Kaldor: And I'd ask anyone interested in that committee to let me know your interest and come back to the next meeting for discussion.

>> Open for discussion.

>> Bettina Rounds: Because they do have a great wealth of knowledge of other public pension systems, and how other cities operate. In the same way that you, Drew were working with Russ. I think that there's real expertise out there that I certainly don't individually have, having been more of a generalist. But I would be happy to work with Sean and with Vince on both parallel paths with Cortex, and Tom Ianucci and get some of his council.

>> Sean Kaldor: That's good. I know that Cortex now is burking on general governance issues but it's all part of the steps it was the next issue, overall organization operation.

>> Damon Krytzer: I have a question before you so if remind me again, if they're in a committee can they actually speak outside of --

>> Sean Kaldor: Not till they're board members on issues that will affect a decision by the board.

>> Damon Krytzer: But I mean --

>> Sean Kaldor: As long as there's less than 4, but once it's a committee then they can't --

>> Damon Krytzer: If it's an ad hoc, right?

>> Mollie Dent: So if you have an ad hoc committee it still has to be less than a quorum of the board. They can have ad hoc --

>> Sean Kaldor: Again meetings that are without --

>> Mollie Dent: They can be -- the meetings do not have to be Brown Acted.

>> Sean Kaldor: Perfect, just a chance to talk without it being six weeks' notice.

>> Stymied by the law.

>> Mollie Dent: But other board members can't show up and they can't talk to other board members.

>> Russell Richeda: And Mollie, it's four or less.

>> Mollie Dent: Four or less yeah.

>> Vincent Sunzeri: I would also suggest if we on this longer term topic, we confer with Fred since it affects both boards.

>> Bettina Rounds: I would agree with that.

>> Drew Lanza: Is that a second to the motion?

>> Vincent Sunzeri: Yes.

>> Drew Lanza: I've noticed our committee members you guys on that committee to seek best practices and to go go go. Which is one of the reasons I really just wanted to limit it to Russ and I. The hard pes some of these committees seem to sort of take forever and that doesn't benefit.

>> Sean Kaldor: Are you completely grate with that. We need to meat quickly, storm, form, norm, perform and disband and go on to the next big topic. Okay pb any further discussion on the motion? The friendly amendment was accepted. And does the second accept the flind amendment? Okay any further discussion on the motion? I'll do a roll call vote on the motion, Kaldor aye. Santos, aye, Bacigalupi, yes. Bill, yes, criers, yes, Lanza disple yes, rounds, Sunzeri, yes, Taylor, yes. Motion pims. I'll follow, we'll coordinate schedules and follow up City Manager's office to set up meetings. Item 3.7, update on Cortex consulting project. Is (inaudible) we're still trying to get confirmation from all the trustees on the timing so we'll send out an e-mail the next couple of days with the quirmts of the date.

>> Sean Kaldor: So this is a joint meeting of the two. This is our second path the last set and we can return to the board disband that group and it will be your chance to look through a big stack of policies about how we work and play together. How things are handled administratively, roles and responsibilities, et cetera. Any questions on the update? Good. Thank you, Ron. Item 3.8, deferred from our last meeting. Update on prl audit, FLSA and overtime payment issues.

>> Donna Busse: There is no update. Payroll was supposed to get back to us. They have an update from March but we don't have an update from them.

>> Richard Santos: Seem like the retirees --

>> Sean Kaldor: To the degree this plan is owed money or we owe retirees money are we prioritizing those issues with the city? It's just been eight months nine months ten months. If we're owed a million bucks we are owed a million bucks.

>> When you say we?

>> Sean Kaldor: If plan.

>> The major of the situation it's the opposite case where there was an overcontribution. That's where the larger FLSA contribution is at. The issue here is just do we accept what the city has begin us even though our external auditors have found some issues with the information. When we went back to the city and said, here is where the issues lie their response is, we can correct it and we can provide corrected information. The problem now is with their budget cuts and all these different actions they don't have the staffing to go back in and do -- at least that's how it appears to me, they don't have the staffing to go back in and actually do the work. So at this point it leaves this plan at a point where do you want to implement the information that has been provided which has some minor issues with it, or how do we proceed?

>> Sean Kaldor: So we owe them money. Is that the --

>> It's not determined whether we owe them money or not. You have to look at, that is plan paid out more in overpayment than it received in overcontribution? If it has then there is no overpayment portion.

>> Mollie Dent: So I think that if we don't have maybe a path forward would be, if we don't have the information back by the March meeting, we need to understand what the magnitude is of the discrepancies. When Veronica says minor, you don't know exactly what that means. And then bring forward a recommendation to the board concerning whether they can move forward with the data that they do have. If it's -- if it is not a really substantive difference, you may have members that will come forward with different data and will allow to you correct it that way, too. I just don't have a sense, at this point, of what the problems are with what's been provided.

>> Sean Kaldor: I think not in a $4 billion plan, $1 billion doesn't concern me the city has the issues with its employees and their over-under contribution. But it sounds like the city's going through its own stuff. Russell do you have a recommending of maybe a next step? At some point with this bubbles up to how do we resolve this? Do we wait for them to do what they're doing and say it is what it is?

>> I say the issue is it affects different members at different rates. There will be some members that will be highly impacted and some that will be a couple cents impacted. Depends on the individual, depends the hours they worked, depends the error that's there. So again we're a month away from the update from finance. I guess what I would say is, it seems reasonable to see if they can provide some information, around then these types of questions can be addressed as far as can anything more be provided and should we take a different course.

>> Sean Kaldor: Which was Donna's point to start off. Councilmember Constant.

>> Pete Constant: Perhaps since this is an issue if I could get a synopsis of the time line and waiting period, perhaps this is something that can be best highlighted by me, in my updates to the city council, that this is a significant snag for this board.

>> Sean Kaldor: Thank you very much. Can we facilitate that request? Thank you. Any further discussion on this update? Okay. Thank you. Item 3.9, discussion and ac on revised physician disability determination formation, putting a nail in this one, deferred from the January meeting. When you get a disability packet if you get any other comments on those forms please just send them to Donna. We ran out of times to do that.

>> Richard Santos: Mr. Chair, this relates to our disability committee. Are you the chair of that Conrad?

>> Conrad Taylor: I am.

>> Richard Santos: Let's get a couple of days between. Let's make some recommendation let's do some kind of action before we point fingers of others we got to take care of the stuff in-house and do with it. Let's do that. I'll work with Conrad any time, thank you.

>> Sean Kaldor: All right, thank you, that will wrap up that one, part of the ongoing disability community. Item threne 10, yont board retreat, we've set a date for the retreat which is --

>> Russell Crosby: March 7th.

>> Sean Kaldor: I asked for input on the board items, I received input from one board member. I think the in please input send me in the next couple of days and we'll coordinate getting an agenda out, everyone knows it will be well in advance of the meeting give staff ability to prepare. All the things we're thinking about and a long term structural organizational financial assumptions and et cetera.

>> Pete Constant: Sean, if you make sure I'm included on those e-mails I didn't receive anything.

>> Russell Crosby: Yeah, I talked this morning that was one insight of our department. Had every intention.

>> Sean Kaldor: Can we coordinate a schedule?

>> Russell Crosby: Yes.

>> Sean Kaldor: Our apologies item 4.1, service retirements. Gonzalo Chayrez. Firefighter. Do I need to do a roll call on this?

>> Mollie Dent: Why don't you take them all and do a roll call at the end.

>> Sean Kaldor: That was item 4.1B, Phelan "D. Garrett, 26.28 years of service, as well as 4.2 A, Teresa D. Reed, instant fire chief, fire department, effective January 21, 2012, 24.71 years of service. Stop there.

>> Richard Santos: Motion to approve.

>> Second.

>> Sean Kaldor: Motion to approve and second. All those in favor, Kaldor aye, Santos, aye, Bacigalupi, eye, Bill, aye, crierdz, aye, Lanza, aye, rounds, aye, Sunzeri, aye. Taylor, aye, motion passes unanimously.

>> Richard Santos: Mr. Chair, I played with all of those, Gonzalo Chayrez was fantastic and Phelan "I worked with for three years. Congratulations to Teresa Reed, I was on her examination when she came on, I remember saying, do you want to be captain, she said no, I want to be chief. Congratulations, she just became Oakland fire chief. Wonderful employee, privilege to work with her. She was a fantastic employee. Thank you all for listening.

>> Sean Kaldor: We'll do the all of 3 and 4 as one. 4.3 A, approval to change retirements date for David Cavallaro, deputy Chief of Police, from December 10, 2011 to December 24, 2011 with 29.47 years of service. As well as 4.4 A, approval to rescind retirement application of Jerald Durk, approval of December 1, 2011 meeting. And approval to rescind retirement of application of Larry Esquivel.

>> David Bacigalupi: Move to approve.

>> Richard Santos: Second.

>> Sean Kaldor: I have a motion and second. Any discussion on the motion? We will go for approval, all those in favor Kaldor aye, sanlts, aye, Bacigalupi, aye, Bill, eye, Krytzer, aye, LAN zap, aye, Rounds, aye, Sunzeri, aye, Taylor, aye. Motion poms.

>> Richard Santos: I know vice chair Bacigalupi and I worked with these and congratulations.

>> Sean Kaldor: And 5, less fortunate part of our agenda. 5.1, Carmelo gons, and second, notification of the death of Matthew T. veuj Vujevich with survivor benefits going to La Donna Vujevich spouse.

>> Richard Santos: Motion.

>> Second.

>> Sean Kaldor: All those in favor, say aye.

>> Richard Santos: Mr. Chair, I'd like to take a moment to bow our heads. I, they were old veterans, very exceptional firefighters back in those days you didn't have masks, I can go on and on. Thee guys put their butts on the line many, many times. Good human beings many.

>> Sean Kaldor: At Mr. Santos request we'll take a moment of silence. [Moment of silence.]

>> Sean Kaldor: Thank you.

>> Richard Santos: Thank you, Mr. Chair.

>> Sean Kaldor: Item sciks.1, investment committee, next meeting to be held February 29, 2012. We have the minutes in our packet and 6.1 B a report from the chair of the investment committee.

>> Vincent Sunzeri: So I have four items I want to cover. I'll try to go through it as briefly as possible. First talk about the the alM. Secondly the and finally our consultant. If you look at the time that we took to discuss the discount rate, it was pretty lengthy conversation. And that's pretty similar to what happens at the investment committee almost at a greater, more extended format. I think that's good, that kind of dialogue taking place. We're scrutiny scrunsing the with investments until we have the alM and frankly, I wasn't the rves quickly push it through. I thought it made sense to really ask some good questions. And some of the things that came up I'll just share with you that we're digging into was that surprisingly to me, the outcome and the asset allocations, were exactly what Federated had. We have two different populations, we have different age groups. Different mortality tables I would imagine. Kind of interesting to me that the outcome would be exactly the same. So that was one reason that raised some questions for me. There was some debate about how they were structuring the allocation, they're trying to simplify it and take it down to four different buckets, what do those buckets look like, should they be structure differently. So that was a bit of debate that took place. Probably the most significant thing however is in the alM if you compare where we are to what Federated adopted and I think what the vex staff is suggesting is they adopted asset mix C. Right now we have between real assets and absolute return or hedge funds, 15%. The asset mix C is moving it to 45%. Talk about moving discount rate in increments. This is a significant shift in asset allocation. And I was a little started by that. So we've asked them to do a little bit further studying on a stress-test basis. Part of the concern is that I think it's with an eye towards the threat of inflation down the road. It's a significant decrease in fixed income, a significant increase in real assets. And so the stress-testing geared on several different dates. Looking at 2008, 1994, 1998, 1990, how would the plan have performed in another downturn environment vs. an inflationary environment. So they're going to do some work on that. More importantly though the goal is talking about trying to derisk the plan and shifting the asset allocation return higher or that the investment return higher than where we were targeting in my mind was a bit of a challenge. But I feel confident that they're going to spend some time digging to this and coming back to the investment committee and talking about that in more detail. Second topic on the investment committee itself. Now I know what it's like to be a head coach of a basketball team. You got a lot of players, there's a lot of personalities that are different, some real superstars and you're kind of trying to nag all of that. You take what you have on Police and Fire and you combine it with Federated and everybody has a different goal and a different agenda. And I think it's great that there's

different thought and debate going ton. There are some challenges that I hope we can fix. There's also some significant benefits. We do have staff members or I'm sorry board members from Federated, that look at the world a little bit differently than some of the Police and Fire and that's good. What I think will be valuable, however, is changing the agenda up a little bit so that we're not all sitting through everybody's entire agenda. There -- the last meeting probably too long six hours so you think you're in a long meeting here, imagine how that meeting is, it's too much. Some of the topics that are taking place need to be reframed a little bit. Some of the presentations need to be shifted around in how they're presenting data and where they're focusing their efforts. I still see the benefit. What I'm going to address with Carmen and Laura when we have our call when we work on the agenda is shifting if we can Police and Fire possibly the early segment just us together for our individual topics, haven't joint topics that we cover, and then Federated can cover their own topics independently. There's no reason for all of us to sit through entire meeting. And that kind of leads me into the agenda. Because with respect to the agenda, we had a conversation or a conference call, that is Laura and I who was the chair on the Federated side, with Carmen to work through the agenda for the meeting and the day of the meeting one of the agenda items got moved to the very front. So painfully Federated had to sit through our entire conversation on aIM. We almost dumbed the same conversations-d duplicated the same conversations so I understand their frustration. For the agenda we did have CIO in a box presentation from McKena. It was a very frustrating presentation in my mind in that 70% of the dialogue was talking about the qualifications of their staff and how talented they are, which was enlightening but I didn't need to spend 75% of the time on that and when it got to talking about the portfolio is somewhat limited. So I think with that frustrated some of the committee members. I believe that hearing about outsourcing is still important because it's one of three different solutions. Although we may not go down that avenue we need to explore, we need to consider so that we're educated when we're making decisions. We had a discussion on staff as we talked about here, and id think what we just agreed to is pretty much in line with what we had talked about there, trying to think about things from a long term perspective. We also talked about, let's see, specific agenda items, Sykes, we have Sykes as our fixed income manager for core, plus they manage about $230 million for us, in that space they manage about $24 million on the bank loan portfolio. They also manage money for Federated. They've had significant turnover in some of the key levels of personnel. And they were simply coming to talk about that change. They had four individuals there. The CEO, CIO, couple of portfolio managers. That's exactly the kind of thing that should happen at those investment committee meetings. Where they're telling us what's going on. Sometimes it's not an action item, it's a process you have to go through to agree whether we're going to continue moving forward with them. And there were some regular flags raised that we need to look at going forward. We have contracted with Alborne and they had a discussion about structure. It was a helpful discussion. Somewhat elementariary I would say, but in the direction we want to go. Those two agenda items are consistent over both boards. Both boards are using Alborne, both boards are using Sykes, it makes sense to have them discussed together. We aced about the priority list and we're working through that. There were some items on the Fed agenda, Federated board agenda that we had to sort of sit through. Unfortunately when it got to the point of discussing the discount rate, as we got to a point of discussing that, the meeting had gone on so long that there were no committee members left from Police and Fire. I don't blame them. They also missed the flash performance report that had some interesting information in it. And what I find interesting is, we had our CIO talk about or give us an update on investment. There wasn't a single question. It took her ten, 15 minutes. And so you wonder why our investment committee meetings are taking so long. We need to have more dialogue, frankly. We need to have it a bigger part of this board meeting. Ultimately that's what it's coming down to is the management of this plan. And if everything is going to take place at the investment committee meeting we are going to have six hour meetings because it's going to interesting data trarchgly Three year numbers which she talked about at the previous board meeting, looks pretty good. It's actually showing some signs of weakness trend of our performance. Not a single person here asked a question about that. Of course because there was no handout here for that detailed information. So I think it's the onus is on us to also make these meetings frufl when we have our CIO there. In addition to that, the last part of the meeting, or actually the very beginning of the meeting but something I want to point out was we have vice chair Santos there at the very beginning and he brought up a point of due diligence. And that is should board members be participating in some of the due diligence that's taking place as we hire managers? Maybe with some of our existing managers not quite as critical but as we're moving towards the hedge fund space an area that could be fraught with some real risk, it's something that we should really discuss on who is the party that does the due diligence, in addition to our consultant? Is it staff? Is it a board member, so I appreciate him bringing that point up and I think it should be a topic for the future. Fourth point. Last point. Monday Tuesday I was at an NEPC workshop. It was, a very insightful workshop. There were 12 systems there collectively managing $100 billion in assets. You had because it was a workshop not a conference, a lot of dialogue. You got to see everybody's portfolio, how they were allocated. There were about eight or nine CIOs there, our CIO was not there. I'm not sure why. Probably could be scheduling conflicts but I think it's worth something to get into. When you have your pierce there peers there and you're bringing in certain experts, why is that taking place? They had some very significant plan sizes. the smallest was about $1.3 billion, the largest which was South Carolina retirement system, $28 billion. So there were some heavy hitters, San Bernardino, Arizona state. Some of these plans have had significant good performance. The one thing I will say which was very, very encouraging to me is every one of these plans of these 12 systems showed their funding ratio. We're the outlier. We were at the end of the curve in there were only two other plans that were 85% funded. Many of these plans were in the 70% range, there was one plan that was 43% funded. So as much as we talk about there being a crisis, frankly the plan looked a little bit better than some of the other systems out there. So that was interesting to see. They had some speakers there talking about overly strategies, windham capital talked, hedge fund managers there CIO of bridge water which is a very significant and well respected firm talking about the markets. They had Greenwich associates that does a tremendous amount of work on pension funds and went through a look at what is happening with peers out there, how assets are being allocated, where money is being moved. And then they ended with a good discussion on real assets. A significant amount of money in our aIM is being targeted to real assets. Frankly nobody was there. Of the 12 systems there was maybe one or two plans that was positioned there. And if we are looking at moving heavily in that area I wonder why we're the outlier. Either we have a brilliant CIO that's moving us significantly ahead of our peers or there may be something that's out of whack here. I think the scrutiny is important. I think we have some really, really talented people that are on the investment committee. I really appreciate the time that they commit to it. And I work really hard to refine the agenda, limit times on the agenda and prevent the overlaps that takes place. Questions.

>> Sean Kaldor: That was a very good report. I would ask if there are things that could be handled at the board level so you're not spending six hours and still not getting through things, there are things that we can certainly benefit from hearing, if you can elevate those things and let me know, we can elevate it to the short meetings.

>> Vincent Sunzeri: There is actually one other thing I want to mention which I think is interesting, taking this into consideration as you guys are making decision. Last year there was a discussion to change to a global equity

portfolio, you recall that, we approved that. Secondly, it was to move to a significant overweight in emerging markets and we sort of put the brakes on that and talked about hedging strategies. Took a while to get the hedging strategy put together and frankly we didn't move in that direction because we were quite concerned about moving to an overweight in emerging markets so we never did that during the year. Emerging markets were down 20% last year, one of the worst performing classes. I applaud this board for doing that number one. Number two when they did come back with the hedging strategy, the hedging strategy in my mind was too late. The hedging strategy had a cap of 24%. Talk about performance in January, emerging markets are up 12% in January alone. So I feel like the value that this board is bringing to the investment process is beneficial.

>> Damon Krytzer: And they were somewhat ripping our face off in (inaudible).

>> Sean Bill: Would I say to Drew's point I I'm still up in the air about the joint meetings. I find them somewhat painful in terms of the length. I don't feel like we've accomplished a whole lot. And I do think that, you know, we could move a lot quicker with a smaller group. Kind of what you were saying about how and Russ were able to get so much more done. You know if the four of us were meeting with the with the staff I don't think we would need to take nearly as much time as what's being spent in these meetings. Because when you add another board, it's almost like it's a geometric energies in discussion rather than arithmetic increase. It's kind of crazy.

>> Vincent Sunzeri: To that point Sean at the NEPC conference there was a committee on number is between 5 and 6 and once you go beyond that number the level of productivity really starts to drop off. You are right in some respects. However, there is some benefit fit makes sense for us to move in a coordinated fashion to work together. We may end up, we now have the same discount rate. Right? We may end up with the exact same alM and if in fact we are doing that we have already hired alborne, we're likely to end up with very similar investments there. Both should be able to weigh in rather than separating that out into two different meetings, collectively talk about that would make sense. The capital market assumption exercise in my mind that was very beneficial having both boards there, to vet that data and come to some decisions but there's a lot of stuff that needs to be separated out. And dealt with independently. So I do -- I do value your input on that and I appreciate that.

>> Sean Bill: And I do think to your point about the Federated board and the allocation that they've chosen a very difference allocation in terms of illiquidity. You have a different mentality on some of the other members of this board, right? You may want to have a slightly different assess allocation strategy than what Federated is comfortable with, you know.

>> Let me put this way dallas and borrowing $5 million bucks nefnlg time we have a downturn.

>> Damon Krytzer: Mechanical differences to me, you know where I stand on this. It's the difference in the thought process. And the decision making process. And that's where I think it's not -- it hasn't been super-productive. It hasn't been productive at all for me. Forget super-productive, that's the issue to me. I mean even if we had the same discount rate the same allocation, we arrive at things so differently.

>> Vincent Sunzeri: So I would ask, if Mr. Crosby wouldn't mind weighing in on the observation of the differences and the benefits you see or disadvantages you see of continuing the process of a joint committee meeting.

>> Russell Crosby: Well, I think there's value from an investment standpoint. You've already highlighted some of them in the alM and other areas. Plus when you look at the construct of the two boards, the Federated board has Stewart Odell. In the originally construct you had Mike flairm. Those were the only individuals in the whole mix who actually had run large pension investment portfolios, multiasset class with all the bells and whistles. That expertise if you will only resides in Federated in the form of Stuart Odell. Likewise, Marty Dirks also on the Federated board teaches portfolio theory, asset allocation. The topics of the day. Dkdz so do I, I teach at USF let me just ask instead of have you seen that come out yes as a financier at the investment committee level?

>> Russell Crosby: Yes I have een that out, in that the reasonable asset allocation, let's go down that road let's get going. They're going to have their manager structure done this month. I mean, that's at a level of a professional in the business, who is presenting through the CIO, a -- really a best practices portfolio. That board saw it, said oh yeah, we know this we see it we understand it we're ready to go, let's go, let's go fast down that road, let's get us to another level which is the manager structure as quickly as you can. That board is moving

along and would I submit that board is moving along because it has these people on it who have done pension portfolios in a multiasset class structure.

>> Damon Krytzer: I can't disagree with that at all. But today, our CIO said, can you believe they only have 5% in this one asset class?

>> Russell Crosby: Uh-huh.

>> Damon Krytzer: So I sort of also -- let's take this offline.

>> Russell Crosby: Meaning that's a good thing.

>> Damon Krytzer: Let's take this offline.

>> Sean Kaldor: It is your committee, can you make it as an agenda item within your committee. Sorry you can make it as an agenda item with your committee to talk about how best to structure the committee.

>> Russell Crosby: And quite frankly there's frustration on the Federated side too, they see it they understand it boom we're moving fast and these guys in Police and Fire are taking forever and they don't really get it. At a very high level that's kind of the views of the two organizations.

>> Vincent Sunzeri: And going back to the discussion of the Dallas Police and Fire where they have a high real asset allocation and they had to borrows $350 million. Frankly I'd rather be sitting on the San José Police and Fire board asking those questions, before it happens, and scrutinizing than shoving something through.

>> Russell Crosby: And that's why you went through whole liquidity analysis. At the end of that whole aIM is say do you have enough liquidity in this portfolio to pay those bests and that was the whole analysis which set yes.

>> Damon Krytzer: Which the consultant didn't agree with. I agree with you but our consultant didn't.

>> Vincent Sunzeri: Actually, that is an interesting. The Mikita consultant didn't even weigh in at all. You have a general consultant for your plan. They weren't a part of the process at all in developing the alM nor did they weigh in on the asset allocation. In our case part of our request is to have our consultant NEPC way in. Frankly if they are our consultant I want their opinion as well. I feel like we're moving prudently, I feel there are some challenges. In my view there are things separated out that wob would make it a little bit more productive. I'm not willing to scrap the great experiment yet .

>> Russell Crosby: Second to address the skill sets Seth between the two boards. You have to understand that there's a tiny tiny staff and to the extent we can keep you guys moving between the two boards in a parallel direction you have enough staff resources to make that happen. The minute you have, let's go in this direction, let's have a different direction you need another CIO. Maybe that's what we're heading towards.

>> We got our ALM a lot later than Federated. That's a good reason they would be further out in front.

>> Russell Crosby: You were 30 days behind.

>> No it was more than that.

>> Russell Crosby: No, they got theirs one month ahead of you and you saw yours and you said, I don't want to go forward with that. Christmas was in the middle. There was no December investment committee meeting.

>> Sean Bill: I understand, that's probably taken into account. I think the other thing is I think we do want our consultant to be a little bit more involved in this process and to kind of bless things if you will. You know?

>> Sean Kaldor: Dick, did you have a comment?

>> Richard Santos: Just a comment. I work with a different agency. When we meet with other agencies we may meet once a year as a protocol, we may pass one or two things, it's a long process our CEO joint issues we need to take a look at. Meantime I hope you guys run your committees because when I was there I could see it being bogged down.

>> Sean Kaldor: All right, any further discussion? That was a good update. I do appreciate the investment committee and all the work that's going into that. We can certainly bring some of those things to the board level and alleviate it at that level but thank you. Item 6.2, ad hoc committee for disability determination process. Scheduling the next meeting. Six.3, ad hoc governance committee, next meeting February 16th, following Federated board meeting. Tentative trying to line that up. I think they're shooting for 1:00. Anybody, Ron? 12:30 or 1:00. Right after their meeting. The minutes are included in here as far as the report we already discussed it earlier in the meeting that this will be our last ad hoc review of all the policies and bring it back to both our boards. The two boards are virtually identical in terms of the policies coming forward. Item 7 is consent calendar, items heard as one motion as a whole.

>> Russell Crosby: Could I suggest that item 2.1 -- or 7.2, the minutes be pulled, and have a separate discussion of those.

>> Sean Kaldor: Anything else?

>> Richard Santos: Just want to say it was my name about going to some training, add that CalAPRS, which I'll be going.

>> Sean Kaldor: Was it proved last month? Add it to this time. 7.2 and 7.3D any other --

>> Russell Crosby: That's the tomorrow round table.

>> Damon Krytzer: I'm registered for that as well.

>> Sean Bill: I am as well.

>> Sean Kaldor: I am as well. I think we were approved last month's agenda. Minutes, you know what, here it is.

>> There were some board members that were approved.

>> Sean Kaldor: Sean Kaldor, you need to be added Damon Krytzer and Sean Bill.

>> Sean Bill: I'd recommend you ail go. The conversation about independence, the fellow that's suing Contra Costa county is going to be speaking there.

>> Sean Kaldor: Hair Harvey leaderman. You are a co-chair of.

>> Sean Bill: Yes.

>> Sean Kaldor: Want to recognize Sean Bill.

>> Richard Santos: Were you able to bring it to San José? Thank you.

>> Sean Kaldor: Remind everyone when we're all there we have to speak about specific board issues that we might bring -- not to.

>> Richard Santos: Bring business to San José.

>> Sean Kaldor: I have a motion from Dick Santos to accept the consent calendar, with the exception ofsen.2. Do I have a second? Kaldor aye, Santos, yes, Bacigalupi, yes, Bill, criers, larch da some rounds, Sunzeri, Taylor. Passes unanimously. Item 7.2, approval of the minutes, I think Russell you notice that item 2.1

we just wanted to clarify. The intent last month was to accept cine's report except for the discount rate discussion, which we reopened. It needs to be clarified that the matter was passed, so notion by Santos to accept with that one modification second? We have a motion and second. Calling for the vote, Kaldor aye, Santos yeah, Bacigalupi, yes, Bill, Krytzer, Lanza, Rounds, Sunzeri, Taylor, motion poms. Moving on to item 8 you have in your board pacts, 8.1 education programs and courses 8.2 conferences and seminars, 8.3 researches and articles, 8.4, clamps training, tomorrow March 4-six, finally proposed agenda items, I've written one written in, to authorize the actuary leave of absence service for fire members. I'll explain what that is. in the contracts with the firefighters and the cops, if they take a leave of absence, for maternity leave for example, they can at some point buy back that time. They have to pay the cost for it. The analysis to do that they pay for and then they pay the money to the plan to cover it. When those benefits were impedimented, it was agreed upon that there would be a costing, they did say provide the benefit in general, they provided the benefit to -- they did the costing for the police but never ended up doing the costing for the firefighters, our assistant chief was told, you can't buy back your old time, whereas people have been doing it for years. So we just need to execute the costing of the benefit, one time thing right? So it can be implemented corked to the union agreement.

>> Richard Santos: Motion to include.

>> Russell Crosby: And Alex is going to trigger a letter to us to the board to request that, to complete that whole process of taking it to the city council.

>> Sean Kaldor: That's why I proposed it, because we just ran into an issue with the assistant chief trying to retire I and were told no, it needs to be cleaned up. Any other proposed agenda items next month?

>> Richard Santos: I think our plate is pretty full.

>> Sean Kaldor: Any general comments from the public? I appreciate people showing up and commenting.

>> I would have also the wharnt realtime program in San Francisco . Scald got you down for this? If there are any interests in classes please let Russell know. Other than that I'll call the meeting adjourned.

>> Richard Santos: Pretty good.