

**REGULAR MEETING OF THE BOARD OF ADMINISTRATION
RETIREMENT BOARD
WATER AND POWER EMPLOYEES' RETIREMENT PLAN**

MEETING – December 17, 2003

Present:

Javier Romero	President
Lilly Calvache	Vice President
Ron Vazquez	Chief Financial Officer
Dan Mirisola	Board Member
Michael Moore	Retiree Member
Leland Wong	Commissioner

Absent:

David H. Wiggs	General Manager
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Others Present:

Duamel Vellon	Retirement Plan Manager
Vikki Burks	Recording Secretary
John Charley	PCA (Pension Consulting Alliance)
Sara Bernstein	PCA (Pension Consulting Alliance)
Mike Wilkinson	Deputy City Attorney

The meeting was called to order at 8:42 a.m. after the Pledge of Allegiance.

[Pledge of Allegiance]

Mr. Vellon indicated there was quorum of the Board (Commissioner Wong joined the Board late in the meeting).

President Romero inquired if there were requests for public comments. Mr. Vellon responded affirmatively.

PUBLIC COMMENTS

Board President Romero recognized Mr. Vince Foley (President of the DWP Retirees Association).

Mr. Foley approached the podium and requested, when there is a change of time, date or place of a regular Board meeting, this change be highlighted on the Internet Web page, and on the notices placed on the bulletin board of the lobby at the JFB building. He stated, on the agenda of the Water & Power Commissioners Internet site, when there is a change of time or place, it is highlighted, bolded and in bright red letters noting this change. Mr. Foley thanked the Board and retired to the audience.

Mr. Vellon reported items 1 and 2 were submitted for consent approval as follows:

- 1. Approval of Minutes for the November 19, 2003 Regular Board.**
- 2. Termination from Monthly Rolls as of December 2003:
Retirement Resolution for December 2003.
Termination from the January 2004 Family Death Benefit Roll:
Jenna Pfefferle – attained 18 years of age.
Termination from the December 2003 Survivorship Roll:
Lois K. Thayer – deceased.**

President Romero noted some changes on the minutes for November 19, 2003. He suggested page 1.5 (the last paragraph) reads “October 16, 20034”, and it should read “2003”. Mr. Vazquez noted a typographical error on the same page (3rd paragraph on the 4th line) reads “news of theses” and should be corrected to “these”. President Romero stated on page 1.10 (second paragraph, 4 lines up from the bottom of the paragraph) reads “of the candidates interviewed, is there”, the “is” should be changed to read “if”. Mr. Vellon stated these corrections will be made.

Mr. Vazquez moved adoption of the above items 1 and 2 on consent, after the suggested corrections. Seconded by Ms. Calvache and carried unanimously after the following vote:

Ayes: Romero, Moore, Vazquez, Mirisola, and Calvache
Nays: None

- 3. Security Transactions for the month of November 2003.**
- 4. Report of Payment Authorizations as of November 2003.**
- 5. Short Term Investments as of November 30, 2003.**
- 6. Report on Long Term Investment as of October 31, 2003.**
- 7. Authority to Purchase Commercial Paper from the List of Approved Issuers.
(January/February/March, 2004)**
- 8. Distribution of Securities by Type and Class as of October 31, 2003.**
- 9. Statement of Investments Owned as of October 31, 2003.**
- 10. Equity Investments as of October 31, 2003.**
- 11. Notice of Deaths as of November 2003.**

Mr. Vellon recommended items 3 through 11 be received and filed. He pointed out item 7 is the quarterly authorization for staff to place commercial paper investments.

Ms. Calvache moved the above items 3 through 11 be received and filed. Seconded by Mr. Vazquez and carried unanimously after the following vote:

Ayes: Romero, Moore, Vazquez, Mirisola and Calvache
Nays: None

- 12. Consideration of Amendment to the Plan’s Investment Guidelines to provide for International Equity (Developed Markets) Growth/Value/Core segments and to modify the International index benchmark to include Canada (recommended**

by Plan Consultant PCA).

Mr. Vellon explained item 12 relates to the amendment to the Plan's investment guidelines, as drafted by PCA. He noted these would become attachments to the Plan's contracts. He added the proposed amendments were included in the agenda packet and were highlighted for emphasis. He stated Plan staff recommends adoption of these amendments.

Mr. Vazquez moved adoption of item 12. Seconded by Ms. Calvache and carried unanimously after the following vote:

Ayes: Romero, Moore, Vazquez, Mirisola and Calvache

Nays: None

13. Consideration of the Plan Consultant's (Pension Consulting Alliance) request for an increase in annual consulting fee for the 3rd year of their three-year contract (Expires November 2004).

Mr. Vellon explained item 13 represents the Plan Consultant's (Pension Consulting Alliance) request for an increase in annual consulting fee for the 3rd of their 3 years contract. He reported this item had been presented to the Board at the previous meeting. He further indicated the PCA contract was included the agenda packet, as requested by the Board. Mr. Vellon related representatives of PCA were present to answer Board members question.

Ms. Sarah Bernstein, of PCA, requested the Board match the fee (\$200,000) PCA received for year one of the year's contract, due to the amount of work required by the Board at this time. She stated the Board was not a client PCA could afford to continue working with, at the existing fee rate for the 3rd year. She requested Board members consider PCA's request and noted PCA representatives have thought long and hard regarding continuing this relationship and would need to resign from the account, given the level of workload that is required. Mr. Moore stated the materials PCA provided to the Board did indicate several areas represented new work was done, which had not been anticipated. He expressed he was now more comfortable with PCA's request and was ready to move on the item, once the Board has had a chance to discuss it further.

Mr. Vazquez inquired if PCA would be involved in negotiating fees with the custody search if the request was increased to \$200,000 from \$100,000. He pointed out Dr. Bernstein stated this was not included in the original contract with PCA. Dr. Bernstein responded in the affirmative this. Mr. Vazquez then inquired if PCA anticipates if the Board is going to be able to complete their asset restructuring, including real estate and alternative investments within the coming contract year, based on where the Board stands now and the pace the Board is going. Dr. Bernstein responded real estate or alternative investments, two new asset areas, will not yet be addressed at the end of 2004 and may continue through to 2005.

President Romero indicated it was the Board's perception real estate or alternative

investments would be included in the contract as asset classes the Board wanted to participate in. He expressed his understanding real estate or alternative investments would require a separate and considerable fee, based on conversations he had with Mr. Neil Rue, of PCA. President Romero stated Mr. Rue also mentioned his workload has been significant. He added he agreed with this, however, the Board has had a lot of work also. He indicated he had suggested Mr. Rue and the Board pursue the fee increment provided a new Request for Proposal (RFP) search be initiated by the Board inclusive of real estate capabilities. He added this would avoid any further controversy or misinterpretations as to whether real estate is involved or not in the present contract. He clarified Mr. Allan Emkin and PCA would be allowed to participate in the search if the Board approves the search. He explained the current contract with PCA expires November 2004. President Romero suggested the Board conduct a search approximately six months prior to the ending of the PCA contract to include real estate. He added the Board would get a better idea as to the industry fee for real estate asset class consulting. He added, Mr. Emkin may be successful in continuing the relationship or there may be someone more fee aggressive.

Mr. Moore agreed this could be done in the remaining year of the contract with PCA. He agreed with President Romero's suggestions and added the search should include real estate and alternative investments, possibly towards the middle of next year. Ms. Calvache inquired if real estate could be included in the contract if contract extension or fee increase were to be given. Dr. Bernstein responded this would not be possible. Ms. Calvache then requested clarification as to whether or not the Board will search for a consultant approximately six months from now.

Mr. Vellon clarified President Romero was proposing this search be done approximately six months from now. He stated the Board typically has six months or more prior to the expiration of the contracts. He noted Plan staff typically present the contracts with RFP's to the Board within 6 or 7 months form expiration in case the Board wants to do an RFP. He further noted President Romero is proposing when the RFP is issued by the Board, it must include real estate, so everyone can be comparing apples with apples in the analysis of all RFP responses received.

Mr. Moore indicated he was quite comfortable with President Romero's suggestion and assumed, since the RFP's will be done mid-2004 this is something the Plan staff would do rather than PCA. He then moved approval of the fee increase requested by PCA. Seconded by Ms. Calvache and carried unanimously after the following vote:

Ayes: Romero, Moore, Vazquez, Mirisola and Calvache

Nays: None

Mr. Vellon explained, PCA claims of increased workload was understandable considering the amount of Board activity and multiple searches. He added he was not in favor of renegotiating a contract in the middle of the duration of such contract, because it sends the wrong message. He pointed out there has also been a lot of pressure on the Plan staff as a result of the Board's heavy pace and level of activity. Mr. Vellon noted if PCA has been producing 200% work, Plan staff have been producing 400% work and for this reason he always requests the Board's support for

any personnel/staff transaction submitted to the Board in the past and in the future. President Romero reiterated he has always recognized Mr. Vellon's performance and he, and his staff, will always have his support.

14. Consideration of Plan Investment Manager's failed trade relative to the sale October 23, 2003, of a bond not held in Plan Portfolio (Ford Motor Cusip No. 345370BJ8) and subsequent sale of a DWP owned bond (Ford Motor Cusip No. 345370BV1) on October 30, 2003, using the lower price of October 23, 2003.

Mr. Vellon explained item 14 represents a particular trade wherein one of the investment managers sold a security not owned by the Board, which was considered a fail. He explained, in connection with the fail, the investment manager intended to sell about \$25 million worth of securities for the purchase of about \$25 million worth of new securities. He noted this is considered a fail because the Board didn't have the bond sold, and the Board has to pay for securities bought by the investment managers. Mr. Vellon further explained, as part of the custody contract with Bank of New York (BNY), they generally advance the funds to the Board to settle these trades, but in order for them to finance these BNY must charge a fee for those failed transactions. He added this actually occurred but the particular manager actually paid for the fee to cover the fail. Mr. Vellon indicated while the plan did not pay for the fail, subsequent to the staff findings the manager took one of the securities owned by the Board's portfolio and sold it, but at a price of seven days before the trade. He stated there was a transaction between the manager and a broker and the staff analyzed it and the information and findings were included in the agenda packet. He indicated the Plan staff had concluded the transaction resulted in a shortage of about \$1 million for the Plan, based on Plan staff estimates. He added this matter has been discussed with President Romero and with one of the City Attorneys, Attorney MaryJoe Curwen, with the request this be discussed in close session, but she advised against this, therefore, their direction was to put it in the agenda packet for an open discussion and this is the reason the item is before the Board.

President Romero stated the Board apparently is owed \$1 million, based on the bond price information within the seven days. He pointed out the error is not the Board's responsibility and the market was moving in the Board's favor and the Board should pursue the matter.

Mr. Moore stated he disagreed with President Romero's approach on the matter as it seemed to him the way the matter was handled was how it would normally be done in the industry and the investment managers intended to sell the Board's bond but gave the wrong designation, which resulted in the selling of the wrong bond so it had to be cleaned up. He stated assuming the investment manager's intention to sell the correct Ford bond, they made the Plan whole as though the transaction had been done correctly in the first place and is normally the way these transactions are handled within the industry. Mr. Moore stated he doesn't see the relevance of the closing date of the transaction or the actual remedy concluded a week later, because the issue for the Board was whether or not the Plan got the price for the particular security on the day the decision was made to sell it.

President Romero stated he didn't really know what the industry standard was, so he couldn't comment either way, but, according to the Plan's CFA, Ms. Lesley Kuo, she believes the Board is owed \$1 million as well. He stated he was inclined to believe Ms. Kuo and it doesn't hurt to explore and pursue it, and at best, the Board will be a little richer. He reiterated it is not the Board's fault if a bond the Plan didn't own, was sold.

Mr. Vellon stated the bond was going down precipitously when the investment manager sold the wrong bond, and then recovered equally quickly. He reiterated the transaction occurred seven days later, but it was not sold at the price reflective of the market recovery. He stated this was the best finding of the Plan staff, which he supports. He clarified it is the Board's decision to do something or not do anything.

President Romero stated he doesn't think the Plan should bare the cost of a money manager's error.

Mr. Mirisola inquired what happened to the difference in the money between December 23, 2003, which they charged the Board as though they sold it on that date for a loss, and the money on October 30, 2003. Mr. Vellon explained BNY bought a security worth \$25 million, which the Board has to come up with the cash and when the other side was matched there was a fail and the cash wasn't there to cover the purchase. He added BNY gave the Board an advance to cover the fail, but charged the investment managers, not the Plan, so the transaction was ultimately completed.

Mr. Mirisola stated TCW thought they were selling the right Board bond, which they were not, and it was not in the portfolio, so BNY made up for the difference to cover the securities. He inquired what happened to the difference between the money BNY made up and the price they got for the security on the bond on October 30, 2003.

Mr. Moore reiterated his impressions was, when the investment managers tried to make right the problem, they went to the same brokerage firm to whom they had sold the original bond, Goldman Sachs, the same firm that was involved in the first transaction. He indicated his answer to the question is the transaction, was somewhat a wash, because the two bonds had approximately the same maturity and same size coupon and that's the reason why they were able to cut the deal that way.

Mr. Vellon responded he did not know who the broker was the first or second time. He added, in light of the reference to industry standards and practices, maybe what Board members can refer this to an auditor and ask them to investigate this and what the opinion might be, and if they feel there is no problem and are satisfied with managers actions. He indicated, in terms of the findings of Plan staff, and in looking at the timeline presented today, staff strongly believes there was a shortage of approximately \$1 million dollars against the Plan.

Mr. Mirisola stated there should be a review to determine if there's really a loss. He added there's a lot of questions with how the whole transaction went down and he appreciated Plan staff recognizing the discrepancy.

Mr. Vazquez commented in the letter from TCW, addressing this matter, it says the day they had purchased the original security was in 1993 and 1994 and now they understand the security was subsequently changed for a different security. He inquired if this portfolio was under their control and direction and did they recommend this exchange for a different bond issue or was this something the Plan did. He noted he didn't really understand how they were managing this fixed income portfolio for the Board and they were bringing the Board recommendations and if they brought a recommendation to purchase this security initially, and if the Board ok'd it it's fine, but why were they unaware of the transaction where this security was exchanged for another Board security is one thing he would like to know. Mr. Vellon responded that's probably the crux of this matter. He added when staff looks at the transaction, they check for the recent past to see if it is owned (the securities) or if a mistake was made. He noted staff generally does not go 11 years ago (to 1993) to see what was the portfolio like. He wondered if the allegation that they have in trying to persuade the Board to indicate that there's nothing here. He expressed he was also puzzled by the same question raised by Mr. Vazquez as to how come they didn't know about the security. He added he was concerned about what would have been the situation if they had settled a transaction a year, at a price of a year ago. He indicated it doesn't appear this can be right and again suggested those are questions maybe objective parties should look at. He reiterated he has the same questions raised as to how come they are selling a bond that was not part of the portfolio since 11 years ago.

Mr. Vazquez stated it was his understanding the industry practice, to the extent that one commits to a transaction with another party and one fails to deliver, one needs to make up whatever loss they have encountered as a result of the fail. He inquired of Ms. Kuo how would a settlement for a transaction like this would work and when would it typically settle. Ms. Kuo explained normally the transaction involving corporate bonds settles in T+3 (trade date plus 3 days) and that's normal. She explained that's what the manager did on October 23rd and it settled on the 28th, at T+3. Ms. Kuo explained on October 30th they realized they made a mistake so they did a "cash settlement", meaning they sold on that day and settled on that day and that's what they have reported. She added the exchange of bonds took place in January 1998 and in five years they did not realize they were selling the wrong holdings.

Mr. Vazquez inquired if the new 8.9% security had been in the portfolio for five years. Ms. Kuo responded this has been the case ever since 1998.

Mr. Vazquez then recommended referring this matter to Mario Ignacio of his staff. He explained Mr. Ignacio deals with the investment on a routine basis, and with brokers, and he would like him to report to this Board on what he recommends the Board should do to pursue this matter.

Mr. Moore inquired if there was not a representative from TCW present at the meeting today. President Romero responded their letter suggests their position was pretty clear as to where they stand. He added no one wants to pay \$1 million, but he felt there should be a due diligence the Board should at least investigate and not be too quick in a decision.

Mr. Vazquez noted in the second to the last paragraph of their letter, the managers state basically one can't look at the closing price on Bloomberg to get a fair value, or the actual value at what the market was when they sold the security. He added what they do is come up with approximately \$1.40 difference. He wondered why they come up with this theoretical statement. Mr. Vellon stated he believes they're throwing that in there, in the event this turns out to be the case they probably would like to use a different price, and he felt this may be a reasonable position to have. Mr. Vellon stated this could be viewed as workable point, wherein, if it's not \$1 million loss, it may be \$700,000, but the fact is something is not right in terms of the Plan.

President Romero stated this is another reason why he sees a lot of value, and staff's suggestion to have an outside auditor look into it and maybe this is a practice the Board has been doing for years. He added this is another reason the Board needs a comprehensive audit.

Mr. Vellon expressed the Plan is past due from having an auditor look at these transactions as part of their standard reviews. President Romero inquired if the issue of having an auditor was on the agenda two months ago. Mr. Vellon responded in the affirmative and clarified the Board members wanted more practical evidence to justify an auditor may be needed. He expressed this particular transaction represents a perfect example why the Plan needs an auditor.

Ms. Calvache commented she didn't have a problem with Mr. Ignacio checking into this matter, but she believes Ms. Kuo was very thorough in her investigation and testimony. She suggested maybe Mr. Ignacio can work with Ms. Kuo because she is good at what she does, and she's very thorough. Mr. Vazquez agreed and indicated basically he wanted Mr. Ignacio to say if we sold the security in the Department's portfolio and failed to deliver on it, what would be the normal remedy, exactly how it works and how it should work in this case. He inquired of Ms. Kuo what her experience was on the remediation of these types situations. Ms. Kuo responded she has experience with reconciliation and how the industry works. She indicated she use to work with different kinds of mutual funds and pretty much understands their practices and whether their practices are acceptable or not. She reminded Board members right now the mutual fund industry is under investigation by the SEC relative to various charges. Ms. Kuo indicated "normal practice" needs to be reasonable in terms of whether it protects the best interest of the shareholders and at times it may be questionable. She expressed the Board may want to investigate and see what the "normal practice" will be in terms of the best interest of their shareholders, investors, or clients.

Mr. Vellon inquired Mr. Vazquez if it was possible for Mr. Ignacio to work with Ms. Kuo so they can submit a joint report to the Board. Mr. Vazquez agreed to so proceed.

President Romero thanked Ms. Kuo. He stated Mr. Vellon has said what an outstanding job she has been doing and how she has been impacting the Plan significantly in her short tenure. He added, during his limited discussions with her she is very intelligent and knowledgeable and wanted the record to show she is appreciated.

Mr. Mirisola stated Mr. Vellon had consistently requested the Board conduct separate

audit for investments and it's something he agrees the Board should do. Mr. Vazquez stated it should be a Board item and he would like to see the scope and layout to see precisely what the Board would be looking at.

Mr. Moore stated, at the meeting where the audit was discussed, the issue was what was the scope so a meeting could be set to see what was going to be done and how differentiating the role that they would play would be from some of the other people who assist the Board, including internal auditors and outside advisors.

President Romero recognized Mr. Lou Mastro of BNY who requested the opportunity to comment.

Mr. Mastro approached the podium and stated, just as an idea, maybe something the Board may want to consider, along with many other Retirement Plans that he works with is, the Boards asks the investment managers to do a monthly reconciliation with the banks custody records and that information would be sent back to the Plan staff to sign off, and determine if they agree with the records. He stated this was something the Board may want to consider when hiring new managers, to avoid having this situation occurring again in the future. It could also save the Board excess work or doing an audit going forward.

Mr. Mirisola inquired what was BNY's reporting procedure on a fail and how long after the fail do they notify the client. He inquired if they would report right away, make a phone call, send a letter and at what point and how would the Plan be notified about the fail.

Mr. Mastro stated the Board has access to BNY's system, so the Board receives them on a daily basis. He indicated he understands the overdraft is probably what prompted the focus on this specific situation as if there had been no overdraft; the fail could've gone for a long time.

Mr. Mirisola indicated BNY then doesn't have a formal reporting mechanism.

Mr. Mastro stated BNY has a failed trade report that's one of the automatic reports generated everyday.

Mr. Mirisola then inquired if the Board received a failed trade report in this instance.

Mr. Vellon stated the Plan staff reconciled against the broker confirmations and they also did their usual checking. He explained Board members have seen tools that are available to the Plan and the staff realized this was a failed trade and called the managers and told them the Board doesn't own the securities. He indicated that's how the trigger actually worked. He proceeded to give credit to the staff because they were on top of it right from the beginning and this should be testimony to the type of professionals on staff.

Mr. Kuo stated at 12 o'clock before the cutoff time for the proceeds for the overdraft, staff (Mr. Hong and Ms. Poon) caught the transaction and called TCW indicating there

will be overdraft and they needed to cover it. She added it took TCW two days just to negotiate with the brokers and come up with the transaction subject of discussion today.

Mr. Mirisola stated we have a motion from Mr. Vazquez to refer this to Mr. Ignacio and Ms. Kuo for a joint report. Ms. Calvache seconded the motion and it carried unanimously after the following vote:

Ayes: Romero, Moore, Vazquez, Mirisola, and Calvache

Nays: None

15. Consideration of Plan Actuary's report relative to the calculation of Actuarial employer contributions:

a) Reconsideration of smoothing technique for recognition of Plan gains/losses.

Mr. Vellon explained item 15 represents the Plan Actuary's report relative to the Board's request concerning the possible replacement of the method currently being used as smoothing technique for the Actuarial valuation of Plan Assets.

President Romero recognized Mr. Paul Angelo of the Segal Company.

Mr. Angelo stated the LADWP Plan's current focus is on realized gains, which was a fairly common method from the 1950's through to the 1980's. He reported these methods have evolved and the Segal Company is recommending methods which are much more in current practice today and much more consistent over the last two years as far as a total approach of the way the Board manages the portfolio for total return. He stated the cost of the plan comes in two parts; pay the current normal costs and make a mortgage payment to pay off the unfunded liability. Mr. Angelo reported the way the asset number is determined affects how much the accrued liability is unfunded, which in turn determines the level of the amortization payment. He explained, if the normal cost is one component and the amortization of unfunded liability is the other component, and the unfunded actuarial accrued liability (UAAL) is determined by accrued liability which comes right out of the computer, based on the benefits formula, from the demographic data and the actual amount of assets which Segal does not use the raw market value, they use the smooth method and the selection of this smoothing method is a key part of the Board's policy decision, part of the funding method set forth by this Board. He noted a higher actuarial liability would mean a lower UAAL and a lower amortization cost, as well as a lower total cost.

Mr. Angelo reported, on the 2002 balance sheet, the Plan had a surplus, meaning the actuarial value of assets was greater than the accrued liability, which meant the total contribution was not equal to normal cost plus an amortization payment, rather, it was the normal cost minus an amortization credit. He referred to his charts nothing the Plan's total normal cost is 16% and of that, approximately 5.5% is paid by the members, leaving the net employer cost at 11%. He clarified, since but because the Plan had a surplus, being credited over a 15-year period, the Plan's net contribution was instead 8.66% and this has been the actual contribution made by the department for the plan

year ending June 30, 2002. He stated there is a minimum of the employee contribution match, greater than the required contribution and the contribution at this point is less than the normal cost.

Mr. Angelo commented about all the losses so far reported and heard about in 2003, common to every single Retirement System in the country. He indicated the DWP Plan has gone from \$75 million dollar over funding, to a \$417 million dollar shortfall, and, again, having unfunded liability is not an intrinsically bad thing, but now the normal cost is just over 11%, but now, instead of getting an amortization credit, the Plan has to pay 7.85% of the total cost which brings the rate to approximately 19.2%. He indicated if the Board changes nothing, the employee contribution rate would be 19.2%. He clarified, ultimately the cost to the Plan is determined by the amount of benefits that go out, plus expenses, offset by the amount of invested income. He outlined contributions plus invested income equals benefit payments plus expenses. Mr. Angelo reiterated the asset smoothing methods determine the unfunded accrued liability and amortization cost and the idea is to generally track the market value and eliminate some of the short term volatility and fluctuations and provide a smoother pattern of contributions and does not really affect the long term cost of the Plan. He stated in using the market value one would be riding the market value roller coaster, and it's too volatile. Mr. Angelo stated, in using the smoothing method and in distinguishing one method from another is to take the total return of the market value, look at the total return and its components and some parts of the return will be recognizable immediately and will not be smoothed and other parts of the return which will be run through the smoothing method and spread over five years. He indicated Segal recommends the Board change how it determines to split between the part that gets recognized immediately and the part, which gets smoothed over five years. Mr. Angelo explained some Plan returns in the market value have not been realized and this is the part, which gets run through the smoothing method.

Mr. Angelo stated Segal Company is proposing the Board consider either 4 or 5 year smoothing method and apply this method to the entire portfolio, and not use separate smoothing methods for bonds and a different method for equities. He stated this goes to the whole total portfolio concept. Mr. Angelo indicated Segal Company is still leaving the reserve and not recommending the Board take any action on the reserve approach today.

Mr. Vazquez inquired, regarding the reserve, would the Board be looking at the reserve and adding it to the market value of assets in the future or not. Mr. Angelo stated currently this is actually subtracted from the market value of assets. He explained if it weren't for the reserves, Segal would take the market value of assets of \$5.5 billion and add the deferred losses, then reducing the reserves, and once this is done, because of the way the statute is set up and the historical practices, there is a whole separate mechanism which requires taking part of the market value and excluding it from the valuation's assets.

Mr. Angelo stated the one approach would be to put the method in as though the method had always been in effect. He referred to this as "full retro". He indicated the other approach would be to go back one year, or "one year retro". Mr. Vellon inquired if

the assumption would be if the Board takes one of these approaches, this particular smoothing technique was for practice purposes effective, say June 2001. Mr. Angelo responded in the affirmative. Mr. Vellon inquired if the Board has not used the full market value of the fixed income, would this give the Board some cushion to reduce the blow of the employee contributions rate. Mr. Angelo responded in the affirmative. He indicated another way to go is to adopt this method prospective only, meaning the 19.2% contribution rate would be the answer this year. He explained if the Board agreed going forward to pursue this new method, but want to get there in a way, which would have no cost impact on the date of transition, this is something which can definitely be done and there would be no immediate change. Mr. Vellon inquired if Mr. Angelo would have a recommendation for the Board, as to which is the best approach. Mr. Angelo responded in the affirmative adding he prefer five years smoothing as it is the most commonly used method. Mr. Angelo stated he is giving the Board a “soft” recommendation for the adoption of five-year method.

President Romero inquired what the bottom line would be, either a four or five year, or a one year-two year retro or no change. Mr. Angelo stated he would urge the Board to adopt the new method going forward and that was his strong recommendation. Mr. Vazquez indicated he believed the Board should change, because this has been the actuary’s recommendation since 1999 and, looking at this from the Plan’s perspective as well as the Department’s perspective, in terms of contributions level, he would recommend the five-year mentioned. He then inquired of Mr. Angelo why again would he recommend the five-year as opposed to the four-year. Mr. Angelo stated, because of the economic cycle being five-year, so the idea was to capture enough years, so the highs and lows would offset each other.

Mr. Vazquez inquired of the partial retro, does this have the Plan going forward using a different method for one part and a different method for another. Mr. Angelo responded in the negative, adding the old method is completely gone and the only time the old method survives is if the Board chooses to do the no immediate change. Mr. Vazquez again stated his recommendation would be to move to a five year smoothing with a two-year partial retro.

Ms. Calvache stated she too agreed with this idea.

Mr. Mirisola stated he agreed with the idea, but was not sure about the partial retro. Mr. Vazquez stated, in looking at this from the Department’s perspective and also from what Mr. Angelo stated in his presentation, one of the reasons to look at different smoothing than the one the Board currently has, is to try to balance the contribution levels over a period of time and not have them swing widely and at an 18% employer rate for the current year. He explained it is too much of a swing for the Department to really be able to absorb, and it puts the City fund transfers in trouble. He inquired if there was a strong recommendation against a two-year retro. Mr. Angelo stated there is not a strong recommendation for it and this is where the Board has to make the decision.

President Romero indicated in Mr. Angelo’s presentation he recommended a one-year retro would a compromise between a five-year and a one be suitable. Mr. Angelo stated that really both option two and three (in his chart) would land.

Mr. Mirisola indicated he does not mind a five-year smoothing and a two retro. Mr. Moore stated, ultimately the Department is on the hook for whatever it's going to take and the Board has to recognize they have to go to a smoothing it makes sense and particularly from Mr. Vazquez' perspective or anyone who has to worry about making these payments on a regular basis, but also the Board has to be mindful of the concerns of Mr. Vazquez has in terms of the fund transfer and the impact on the City of Los Angeles at a time of difficulty and a time when one is trying to work with the change in the way water rates are structured, so all these things are important. He added he is very comfortable with Mr. Vazquez' recommendation.

Mr. Mirisola stated he is in favor of it because the smoothing method will help the Board especially with the new asset allocation, it will be more consistent and recognizing all of the Plan earnings and losses, as opposed to picking out which we will recognize. He added, as fiduciaries, it is more realistic and a valid argument and the thing to do, but as far as the two-year retro, he thought it is valid because it takes into account some of the extreme losses and allows some of the earnings the Board didn't count in those years and he thought it would help to make it more realistic on how the actual earnings really are.

President Romero noted Mr. Wong's arrival at 10:07 a.m.

Mr. Vazquez moved adoption of the five-year smoothing technique with a two-year retro, seconded by Mr. Mirisola and carried unanimously after the following vote:

Ayes: Romero, Wong, Moore, Vazquez, Mirisola, and Calvache
Nays: None

- 16. Consideration of request from Attorney Michael Wilkinson regarding NAPPA (National Association of Pension Attorneys):**
- a) Annual membership (\$325)**
 - b) Mid-year meeting participation (estimated cost \$ to be provided)**

Mr. Vellon explained item 16 covers Attorney Michael Wilkinson's participation in NAPPA (National Association of Public Pension Attorneys) both membership and meeting activities. He noted the cost of the meeting is estimated at \$1700, and he recommends Board approval.

Mr. Moore moved approval of item 16. Seconded by Ms. Calvache and carried unanimously after the following vote:

Ayes: Romero, Wong, Moore, Vazquez, Mirisola, and Calvache
Nays: None

- 17. Consideration of Retirement Plan amendment to provide for charging the Plan expenses against the Trust, for payment of investment management fees due**

and payable under the newly adopted asset allocation structure. (For final approval after adoption by the Board of Water and Power Commissioners).

Mr. Vellon explained item 17 represents a Plan amendment the Board has been moving from one meeting to the other. He explained basically this particular amendment was approved by the Board, as a Plan amendment, it was given to the Board of Commissioners (who have approved the amendment) and then the amendment came back to the Board in conformity with the usual proceedings for Board final approval and it is on the agenda for Board consideration.

Mr. Vazquez moved approval of item 17. Seconded by Mr. Wong. The motion failed after the following tie vote:

Ayes: Wong, Moore, and Vazquez

Nays: Romero, Mirisola, and Calvache

Mr. Vazquez requested item 17 be put in the next Board meeting agenda.

18. Update (from the Board's Attorney) on item referred to the Board's Fiduciary Counsel (Re: number of votes required for a legitimate Board Action).

Mr. Vellon explained item 18 represents an update from the Board's Attorney on the Board; referral to the Fiduciary Counsel.

President Romero inquired if Attorney Wilkinson had referred this to the Fiduciary Counsel. Attorney Wilkinson confirmed it was referred to the Fiduciary Counsel. He indicated he didn't have a report, however, he received a letter dated November 24, 2003. President Romero inquired if Attorney Wilkinson had a timeline in mind. Attorney Wilkinson responded he had not received a response but he would make a follow-up phone call to the Fiduciary Counsel today.

19. Reconsideration of Fred Alger as Large Capitalization Growth Manager in light of recently published news (contract number 137).

Mr. Vellon explained item 19 represents a reconsideration of Fred Alger contract, as one of the Plan's Large Capitalization Growth Managers selected by the Board. He indicated they have a contract in place and they are supposed to be funded through the upcoming transition. He reported there is a request for comments of this item by representatives of Fred Alger.

Mr. Matthew Gotwols, CFA, Senior Vice President, and Ms. Teresa Phraner, Vice President of Fred Alger Management, Inc. approached the table.

Mr. Gotwols thanked the Board for allowing Fred Alger to speak before the Board. He introduced himself and explained his basic functions at Fred Alger. He informed the Board he sent a response to the inquiries regarding redemption as to a percentage of

assets and as a percentage of sales relative to the Fred Alger Fund, which is an open-end retail mutual fund portfolio. He also added he sent out a letter mentioning some of the changes Fred Alger has made in the mutual fund sales marketing area, to ensure they have the best practices in the industry. He commented, as he stated last week, LADWP is an important relationship for Fred Alger and he hopes the Board will decide to go ahead with them, despite the unfavorable publicity the firm has received. He stated he and other members of Fred Alger remain stunned with Mr. Jim Connelly's actions in obstructing their internal review of mutual funds sales practices as well as instructing the investigations of the New York State Attorney General's office and the SEC. He continued his actions were unilateral, not systemic, and upon discovering what Mr. Connelly had done, Fred Alger notified the Attorney General's office, which resulted in Mr. Connelly's arrest and he forced resignation from the firm. Mr. Gotwols stated, as an update, Mr. Connelly is scheduled for his sentencing today, for his actions of tampering with physical evidence. He stated Mr. Connelly's issues are distinct from any issues at Fred Alger. He explained Mr. Connelly pled guilty to tampering with physical evidence in conjunction with the investigation conducted by the NY Attorney General's office and that is what he is being sentenced for. Mr. Gotwols noted no portfolio manager or analyst at Fred Alger has engaged in improper trading or conduct and none of these issues affect the Board's separately managed accounts. He noted it is important the late trading incident, which he had reported previously, occurred because of misleading information that was supplied by a former customer. He continued to explain the employees of Fred Alger were misled to believe the underline trades had been properly made before 4 p.m. and that they were only administratively processing such trades, which is consistent with long standing industry customs and practices. Mr. Gotwols noted, while this may not completely excuse what happened, they would want the Board to know that no one at Fred Alger knowingly tried to facilitate late trades. He stated they were not the only mutual fund that was misled by the client, a former client, in this manner and they understand that that particular customer is now out of business. He continued to explain as for internal review, which is summarized in the information sent out yesterday, Fred Alger's internal review has progressed. He indicated they reviewed all transactions year-to-date and found no other relationships with a potentially trade issues. He added Fred Alger is hiring a chief of compliance officer which will be an addition to their legal department; they have banned market timing in all their mutual funds; short term trading is not permitted in the Fred Alger fund after October 16, 2003 and they are implementing a 2% redemption fee for shares that are held for less than 30 days. He indicated last week Fred Alger added Dr. Joseph Ny, Dean of Harvard University Kennedy School of Government to their Board's foreseeing mutual funds. He noted, overall, the reasons why the Board hired Fred Alger earlier in the year remain intact and there have been no changes or reversion in investment philosophy throughout the firm's 40-year history. He emphasized the firm's investment process relies on independent research performed by their staff of experienced dedicated analysts and performance has been very good. He stated, in summary, his firm is committed to delivering excellent performance and service. Mr. Gotwols stated Fred Alger has learned and improved from the mistakes and are committed to the Board, employees of LADWP, and retirees, and hopes the Board will give them the opportunity to serve LADWP. He thanked the Board for their consideration.

President Romero expressed concerns Mr. Connelly was given too much latitude

without any checks and balances, reflecting a failure at Fred Alger. He noted Ms. Phraner did a good job in trying to maintain the Board informed, but no one from upper management at Fred Alger took the initiative to come before the Board.

Mr. Moore agreed with President Romero and noted Mr. Connelly had a high level position, reflecting a possible corporate culture. He referred to the level of transactions as a percent of the total assets showing 283% ratio churning at Fred Alger. He also indicated redemptions against sales exceeded 100%. He noted the Board has a responsibility as fiduciaries. He added the managers' use of soft dollars is another concern requiring Board attention and in light of what has transpired he could not support the continuation of Fred Alger.

Mr. Vazquez indicated he had been impressed with Fred Alger returns and integrity and he would continue to support them as investment managers for the Plan.

Mr. Mirisola agreed with Mr. Vazquez and expressed the need to move forward to avoid more opportunity losses for the Plan. He noted the Plan's consultant, PCA, had recommended a manager hired by the Board be placed in a "watch list". He expressed his preference for such action so the transition of assets could take place without more delays. He noted he saw no wrong doing at Fred Alger. He elaborated on the need to distinguish between individual activity through redemptions, versus the institutional transactions. He felt Fred Alger actions justify retaining them on a "watch list" basis.

Ms. Calvache expressed she cannot support continuing Fred Alger's contract under the present circumstances. Mr. Vazquez expressed the Board will probably not benefit from selecting another finalist firm to replace Fred Alger.

President Romero indicated it is important to distinguish market timing versus late trading. He added most managers may have been doing this and the Board needs to demand integrity. He noted Fred Alger reported they will have a compliance officer, but this was as a result of a requirement by the SEC. Mr. Gotwols agreed, but noted Fred Alger had thought of the idea before the SEC's requirement. He reiterated Fred Alger controls to prevent these situations.

President Romero suggested funding those hired and wait until the dust settled before funding those under investigation. Mr. Mirisola expressed concerns the Board had retained Merrill Lynch in two areas while they were also under investigation and the Board chose not to wait until the dust settled. He expressed the Plan will be hurt by not proceeding with the funding of Fred Alger, short of any further revelations.

President Romero explained the situation with Merrill Lynch was different.

After more discussion, Mr. Vazquez moved continuation of the existing contract with Fred Alger and to place them on a watch list. President Romero expressed there must be consistency in the issue relative to all managers selected such as Intech/Janus, MFS, Fidelity and even Mellon had some exposure relative to Dreyfus and advertising charges (per yesterdays papers).

Mr. Moore indicated the Board needs to move ahead, but he would be in favor of replacing the firms by the next Board meeting.

Mr. Vellon noted the draft resolution in the agenda packet needs to be modified to reflect the desires of the Board. Mr. Mirisola then seconded Mr. Vazquez motioned and prevailed after the following vote:

Ayes: Vazquez, Mirisola, Romero and Wong
Nays: Moore and Calvache

President Romero's vote was not clear and Attorney Wilkinson advised any abstentions must be recorded as a "yes" vote. Ms. Calvache changed her vote from "no" vote to a "yes" vote and the vote prevailed after the following vote:

Ayes: Vazquez, Mirisola, Romero, Calvache and Wong
Nays: Moore

Ms. Calvache inquired how would the Board monitor Fred Alger. Mr. Vazquez responded this would be done by PCA. Mr. Vellon noted the draft resolution will be amended accordingly and the transition process to fund them through BNY will continue. Mr. Charley explained how PCA monitors these cases.

Mr. Gotwols and Ms. Phraner were excused and left.

20. Reconsideration of Invesco as International Manger (Developed Markets), in light of recently published news (contract pending).

Mr. Vellon explained a draft resolution was included in the agenda packet for Board consideration. He noted the Board did not have a signed contract with Invesco and their allocation or funding will be above \$227 million due to increases in Plan market values.

President Romero expressed concerns about funding Invesco and he suggested the Board use ETF to obtain exposure to the asset class in question, until a proper replacement can be selected. He felt the options appear to be to fund or wait.

Mr. Mirisola explained in the Invesco situation the Board selected a completely different product, not related to other segments of the Invesco organization. He added he feels comfortable with Invesco as Plan Investment Managers.

Mr. Moore expressed he had greater concerns with Invesco than what he had with Fred Alger. He distinguished Fred Alger is cooperating with the SEC, while Invesco is resisting and he could not support them either. He suggested exploring other alternatives to obtain International market exposure or to consider other alternatives.

Mr. Vazquez moved the Board not select Invesco, consistent with the recommendations of the Plan's consultant, PCA and to put on a future agenda the discussion on the cash

investments as well as the selection of Invesco's replacement. President Romero reiterated the need for consistency and he preferred not to select a replacement until the SEC investigation is completed. He felt terminating a manager while keeping the other is not fair. Mr. Mirisola agreed with President Romero. He asked Mr. Charley for clarification of their recommendation. Mr. Charley explained there are suitable replacements in the pool of managers interviewed, but it was up to the Board to terminate or not terminate the relationship with Invesco.

Dr. Bernstein noted the main difference between Fred Alger and Invesco is the latter is challenging the accusations, but PCA's recommendation as to not continue with Invesco remains unchanged. President Romero expressed concerns about the appearance of giving the finalists interviewed a second chance.

Mr. Moore again moved to replace Invesco as Plan Investment Manager. Seconded by Mr. Vazquez. The motion failed after the following tie vote:

Ayes: Vazquez, Moore, Wong
Nays: Mirisola, Romero, Calvache

Mr. Vazquez moved to defer action on this matter and to make it an agenda item at the January 2004 meeting, along with the consideration of what to do with the cash earmarked for Invesco, with a recommendation from PCA. Seconded by Mr. Moore and carried unanimously after the following vote:

Ayes: Romero, Wong, Moore, Vazquez, Mirisola, and Calvache
Nays: None

21. Reconsideration of MFS as Active Large Cap Value Manager in light of recently published news (contract number 140).

Mr. Vellon explained there is a draft resolution in the agenda packet for Board discussion. He noted a representative from MFS requested the opportunity to address the Board. President Romero recognized Mr. Jack O'Connor who approached the podium.

Mr. O'Connor recognized these were troubled times for MFS. He reiterated MFS has a culture of integrity. He elaborated on MFS multiple investment products, other than mutual funds. He explained MFS may be fined modestly on some charges and they would probably pay without admitting wrongdoing. He closed by stating the Board selected MFS in June on their track record and he encouraged the Board stay with MFS.

Mr. Vazquez inquired about the funding Plans for MFS. Mr. Vellon reported they will be funded out of the Boston Co. equity account and the transition is being coordinated with the Board's transition provider BNY/GTM.

President Romero noted his view on MFS is no different from Invesco and he would be

in favor of obtaining input from PCA. He reiterated the issue of fairness to all managers involved.

Mr. O'Connor indicated MFS is cooperating fully with the SEC.

Mr. Moore suggested to proceed the same as with Invesco and to consider alternatives to funding.

Mr. Mirisola moved to continue with MFS for all the same reasons as in Fred Alger's case. He noted the opportunity cost to the Plan, caused by the delays, can probably be estimated in the millions. There was no second to this motion.

President Romero suggested to perhaps proceed the same as Invesco and to continue working with PCA relative to funding them or not, or consider other avenues.

Mr. Vazquez moved not to Fund MFS at this point, pending the outcome of the SEC investigation and to have the Boston Company continue their management of the securities originally earmarked for the funding of MFS, and to continue the funding of the other three managers (Intech, Fred Alger, and Merrill Lynch). Seconded by Mr. Moore and carried by majority after the following vote:

Ayes: Romero, Wong, Moore, Vazquez, and Calvache

Nays: Mirisola

22. Consideration of selection process for the replacement of certain Domestic Growth/Value and International Growth/Value/Core investment managers.

Mr. Vellon reported the proposed draft resolution under this item was intended to establish a replacement process for any terminated investment manager. Mr. Vazquez clarified no investment manager had been terminated by the Board and it was the consensus no Board action was necessary at this time.

23. Retirement Plan Manager's comments.

a) DWP Plan Newsletter for retirees (December 1, 2003 Edition)

Mr. Vellon reported the Board members had already received a copy of the December 1, 2003 Newsletter for DWP retirees.

b) TCW Personnel Changes (letter of November 4, 2003)

Mr. Vellon informed the Board TCW reported a personnel change through their letter of November 4, 2003.

c) General Items

Recognition of Retirement Plan Staff

Mr. Vellon recognized the Plan staff at all levels in the Retirement Office for an excellent job and effort towards all the Board's manager searches, implementation, transition and related responsibilities. He expressed his wishes for the Plan staff, Retirement Office and the Board to have happy holidays.

President Romero also expressed his wishes to the Plan staff and the Board for their hard work and effort. He wished everyone have a happy holiday.

Mr. Vazquez commented, in regards to a request made to the Board and to the Retirement Plan Office by Mr. Foley, at the beginning of this meeting, he would like to ask Mr. Vellon to consider trying to highlight for those looking at the minutes, when there are changes in venue or changes in time, so that people are alerted in the posting.

Mr. Vellon responded the size of the characters used on the agenda is not, perhaps, the best size and the Plan staff would be happy to highlight changes for easier reference. He expressed concerns this was a very minor issue and a phone call to staff should have been sufficient. He added the Board agendas are often heavy and that these minor issues do not belong at the Board level. He recommended those kind of suggestions should not be something that should be encouraged.

The Board meeting was adjourned at 11:03 a.m.

JAVIER ROMERO

President

DUAMEL VELLON

Secretary

Vikki Burks

Recording Secretary