

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

MINUTES – December 20, 2006

Present:

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|----------------|----------------|
| Javier Romero | President |
| Eugene Canzano | Board Member |
| Cindy Coffin | Board Member |
| Michael Moore | Retiree Member |

Absent:

| | |
|-----------------------|-------------------------|
| Ronald Deaton | General Manager |
| Forescee Hogan-Rowles | Commissioner |
| Ron Vazquez | Chief Financial Officer |

Others Present:

| | |
|----------------------|-----------------------------------|
| Sangeeta Bhatia | Retirement Plan Manager |
| Monette Carranceja | Assistant Retirement Plan Manager |
| Mark Blunk | Assistant Retirement Plan Manager |
| Irene Colon Gonzalez | Recording Secretary |
| Sarah Bernstein | Pension Consulting Alliance |
| Mike Wilkinson | Deputy City Attorney |

President Romero called the meeting to order at 9:35 a.m. after the Pledge of Allegiance.

[Pledge of Allegiance]

Ms. Bhatia indicated a quorum of the Board was present.

PUBLIC COMMENTS

President Romero inquired if there were any public comments. There were no public comments.

- 1. Termination from Monthly Rolls as of December 2006:**
 - Retirement Resolution for December 2006**
 - Resolution terminating Alexis K. Adams from the January 2007 Family Death Benefit Roll – attained 18 years of age**
 - Resolution terminating Robert G. Henson from the December 2006 Permanent Disability Roll – reached termination age of 65**
 - Resolution terminating Ruth J. Watkins from the January 2007 Survivorship Roll as a result of her death**

Mr. Moore moved adoption of the above item 1 on consent. Seconded by Mr. Canzano and carried unanimously after the following vote:

Ayes: Romero, Coffin, Moore, and Canzano

Nays: None

- 2. Report of Payment Authorizations as of November 2006**
- 3. Notice of Deaths for November 2006**
- 4. Report on Status of Insurance as of November 30, 2006**
- 5. Summary Investment Returns as of November 30, 2006**
 - a) Market Value of Investment by Fund and Month as of November 30, 2006**
 - b) Market Value of the Retirement, Death & Disability Funds as of November 30, 2006**
 - c) Investment Returns as of November 30, 2006**
- 6. Note from Macias, Gini & O'Connell LLP regarding partnering with Essary, Dal Porto & Lowe LLP**

- 7. Discussion of notification from Lexington Partners regarding amendment to LCP VI Partnership agreements**

Mr. Moore noted that Item 4 reflects a number of the professional liability insurance policies have expired. He then inquired if the policies are currently up to date. Mrs. Carranceja responded that staff sent letters to 5 of the managers (Lexington, Paradigm, Northpointe, Merrill, and Landmark) on December 8, 2007. She indicated that three of the firms have been working with the Department's Risk Management; however, staff will be following up with a phone call to Lexington and Northpointe today.

Mr. Moore referred to Item 6 and expressed it was not clear as to what is happening between Macias Gini & O'Connell and the Essary, Dal Porto & Lowe firm. He inquired if the firms were partnering or if it was a joint venture. Mrs. Carranceja stated that Mr. James Godsey (Macias Gini & O'Connell) sent staff an email informing them that it was simply a purchase of a small tax firm in Sacramento. However, there is no impact to the Department, and there is no change in ownership of the firm. She explained that, according to the contract, the firm is required to submit a formal letter and staff would be following up on this also. Mr. Moore inquired if Essary would become a subsidiary of Macias or just a partnership, in terms of working together with an income-sharing arrangement. Mrs. Carranceja responded that staff would be asking the firm these questions in more detail and get back to the Board. Ms. Bhatia indicated that staff just recently received a business card from Essary as a notification of the partnership and no other formal notification.

Mr. Canzano moved the above item 2 through 7 be received and filed. Seconded by Ms. Coffin and carried unanimously after the following vote:

Ayes: Romero, Coffin, Canzano, and Moore

Nays: None

8. PCA's Quarterly Performance Review as of September 30, 2006
- Future Performance Report presentation suggestions

Ms. Bernstein approached the Board table. President Romero recognized Ms. Bernstein.

Ms. Bernstein reported for the third quarter ending the allocations to Domestic Equity and International were a little above target. She stated this was primarily due to holding assets that are designated for the new real estate, private equity, hedge fund-of-funds, and alternative investments.

Ms. Bernstein indicated there were a few items PCA would be bringing before the Board in January, such as notification of making sure the benchmarks are correct for the portfolio performance reviews. She noted, with regards to the Death and Disability fund, there was 8% cash in the Death Benefit Plan at the end of September and about 5% cash in the Disability Plan. Ms. Bernstein stated that PCA is working with the Retirement Office staff regarding the matter. She reported the current benchmark for both of those plans is just 100% fixed income, unlike the cash target of 1% in the Retirement Plan. She stated staff is working to decide how to manage this so that the benchmark is more in line with how the cash should be managed.

Mr. Canzano inquired about the LDZ Group. Ms. Bernstein responded that LDZ is a firm PCA has worked with for many years to assist in performance reporting. She explained that the firm does a lot of the backup work in making sure the manager and custodian numbers match and detect if they need any changes.

Mr. Moore noted the report reflects that the last quarter had a minus \$44 million net contributions and inquired if this was peculiar to the quarter and what was the net contribution on an annualized basis. Ms. Bhatia responded the information came from PCA and she is not sure what they are referring to. Ms. Bernstein stated she would come back with the details and breakdown.

Ms. Bernstein reported the actual returns for the policy for the quarter ending September 30, 2006 were slightly below the policy benchmark. In terms of peer performance, the WPERP portfolio climbed significantly from prior quarters. She listed contributing factors such as domestic equities where actual returns underperformed, international came out slightly ahead, and fixed income was in line. She added that alternative and real estate investments are not figured in yet.

Ms. Bernstein reported the domestic equity portfolio helped dampen the overall results of the portfolio for the one-year performance, international came in right on target, domestic fixed outperformed over the annual basis and contributed to bringing up the overall policy return to 10 basis points below the policy benchmark.

Ms. Bernstein reported, for the three-year performance, the total Retirement Plan slightly underperformed the blended policy benchmark. The domestic equities for that period came in right on line and domestic fixed was 40 basis points below the policy benchmark returns.

Ms. Bernstein noted there was not a manager with a five-year track record with DWP.

Ms. Bernstein stated that WPERP's policy, asset allocation, and managers are broadly moving in line with the overall markets and this is something the Board will hear every quarter. She further stated this is something that reinforces the importance of asset allocation over individual particular managers and the overall results for the pension plan.

Ms. Bernstein reported that the managers "on watch" for performance issues are still underperforming; however, Boston (emerging markets) has moved up to be right in line with their benchmark for the quarter.

Ms. Bernstein presented the Board with a new format for the quarterly performance review and explained the changes.

President Romero inquired, with regards to the underperforming managers, if there was anything in particular giving PCA great concern. Ms. Bernstein responded in the negative. President Romero commented that a few of the allocations have recently been completed, and inquired what time period does Ms. Bernstein see before the Board can realize the actual performance of the portfolio under the proposed allocation. Ms. Bernstein responded this was one of the additional benchmark issues PCA is planning to come to the Board with. She explained there are currently no real estate or alternative investments in WPERP's benchmark because they were not funded. She indicated those investments would be introduced in 2007 and it would take a few years to get private equity up to full allocation. President Romero inquired when is the new liability study scheduled. Ms. Bernstein responded it is scheduled for mid-year 2007.

Mr. Moore pointed out that the Board reviews the monthly figures as they are prepared by staff, who in turn draws primarily on Mellon; however, the report submitted for today's Governance Committee meeting by Deloitte & Touche looks at the investment side of operations. He also pointed out that one of the things the auditors suggested was that the Board not only looks at the returns, but also at the risks associated with the returns on a regular basis. Mr. Moore suggested the Board consider which of the risk measures should be included in the monthly report, versus what should be included in the quarterly report prepared by PCA. Ms. Bernstein responded she would look at the report and review the recommendations. Ms. Bhatia indicated that Deloitte & Touche would be presenting the report at the Audit Committee meeting today.

The Board expressed they were pleased with the new performance report format. President Romero requested the format be reviewed thoroughly for errors.

9. PCA – 2007 Proposed Manager Presentations and Policy Development Review Schedule

Ms. Bernstein informed the Board that the information provided includes some of the major highlights of 2007, such as structural reviews of each of the major asset classes and the undertaking of an asset liability study. She indicated the Board would need to decide on whether to do a basic or more detailed asset liability study.

Mr. Moore commented that Deloitte & Touche recommended there be a standardized and rigorous attribution analysis with regards to the manager and he would like to see this take place. Ms. Bernstein responded that PCA would work with the Retirement Office staff in making sure all the managers are presenting similar and sufficient material regarding performance.

Mr. Canzano moved the adoption of the proposed 2007 manager presentations and policy development review schedule. Seconded by Mr. Moore and carried unanimously after the following vote:

Ayes: Romero, Coffin, Canzano, and Moore

Nays: None

10. Resolution to ratify the Board's action pertaining to the adoption of the June 30, 2006 actuarial valuation report of the Disability Fund and recommendations of the Plan's actuary

Mr. Moore moved the approval of Resolution 07-40 to ratify the Board's action pertaining to the adoption of the June 30, 2006 actuarial valuation report of the Disability Fund and recommendations of the Plan's actuary. Seconded by Mr. Canzano and carried unanimously after the following vote:

Ayes: Romero, Coffin, Canzano, and Moore

Nays: None

11. Discussion of the status of the resolution regarding indemnification of Board Members in connection with divestment from investments in Sudan and possible action

President Romero stated it was his understanding that the LACERS Board met on this item yesterday. He then requested Ms. Bhatia present the Board with a summary of what transpired. Ms. Bhatia explained the drafted City Council resolution regarding Darfur, Sudan was brought before the DWP Governance Committee on November 8, 2006, and it was suggested the resolution be brought before the Retirement Board for discussion. Ms. Bhatia reported that the other two City pension plans have been meeting on the resolution, which is regarding the indemnification of Board members in

connection with taking action as a result of the Mayor's letter to divest from investments in Sudan. Ms. Bhatia indicated she received an email yesterday from the Fire and Police Pension Plan Retirement Plan Manager informing her that both the Boards of Fire and Police Pensions and LACERS reviewed the resolution and signed the draft ordinance that was put together by Attorney Manning and Attorney Wilkinson. She reported that they also inquired if the DWP Retirement Board had reviewed the resolution and taken any action, and suggested all three pension plans go together with a letter to the Mayor's Office.

Mr. Moore expressed he was not entirely comfortable with one clause in the last paragraph of the resolution regarding fiduciary responsibilities. He stated his only concern is that if litigation were going to be brought, it would be on the grounds that the Board had not met their fiduciary responsibility. Mr. Moore stated, at the same time, he was assured by the City Attorney's Office and fiduciary counsel that the Government Code Sections on employee immunity does provide some measure of protection. He expressed that, on that basis, he is now comfortable. Mr. Canzano inquired if it would be a possible defense that the Board was performing within the limits of their fiduciary duty. Attorney Wilkinson responded in the affirmative, stating that all the things the Board is doing today, including the formation of the Governance Committee, would put the Board in a very good position. He stated the Board could be sued, but it would not be successful with the kind of record and actions the Retirement Board has taken.

Mr. Moore moved the approval of the draft City Council Resolution regarding Darfur, Sudan. Seconded by Mr. Canzano and carried unanimously after the following vote:

Ayes: Romero, Coffin, Canzano, and Moore

Nays: None

12. Retirement Plan Manager's Comments

a) General Items

Ms. Bhatia informed the Board that staff has begun the transition of the Post Retirement Health Care funds. She stated the first installment of funds of approximately \$200 million was received last Friday. She reminded the Board that those funds are invested in cash and the remainder of the funds are expected in January. President Romero inquired why the funds are being received in installments. Ms. Bhatia explained that the amount received represented the amount that matured in December (approximately \$550 million) -- the idea was that the entire fund be moved at one time in the first week in January. Ms. Bhatia indicated that staff is looking at options, such as employing a transition manager, versus providing the cash to the fixed income and the equity managers. She indicated that the issue of where the fund would be invested was brought before the Board at the last meeting. She stated PCA has recommended in the interim, and pending an asset liability study, 60% be invested in equity and 40% in fixed income. She added that PCA also suggests selecting one investment manager for equity and one for fixed income for purposes of separate record keeping. President Romero inquired about the selection process of those managers. Ms. Bernstein responded instead of selecting one growth or value manager just take the core large cap manager, which is the index fund. She expressed that PCA is comfortable with

either one or two of the core fixed income managers and this would be discussed further with staff. However, this would mean not having exposure to all asset classes for this interim, but staying in the core areas and not investing in high yield and emerging markets with these funds before an asset liabilities study has been done. Ms. Bhatia informed the Board that staff would be reporting further about this at the next Board meeting. President Romero inquired if any funds would be transitioned. Ms. Bhatia responded that staff would be transitioning the securities. She explained that currently the securities are custodied with U. S. Bank and would be moved to Mellon bank and liquidated to fund the equity and fixed income managers.

Ms. Bhatia reported that Staff received a demonstration by JEA, the other finalist for the computerized pension system, on Monday. She stated staff is planning a site visit to witness an implemented system to achieve some sort of comfort level. Ms. Bhatia stated staff is also planning to have a demo done by Tier in the first week of January.

Ms. Bhatia reported staff has been informed by Prudential that there will be an opportunity soon to invest in the real estate fund selected by the Board. She stated staff is working with the City Attorney's Office and outside counsel to finalize the contract in order to get the funds invested before the end of 2006. Mr. Moore inquired how much would be taken out of what has been committed. Ms. Bhatia responded the capital call is for \$10 million out of the \$30 million.

Ms. Bhatia indicated that information was passed out regarding the acquisition of Glass Lewis by Xinhua Finance. Glass Lewis has sent staff a notification via e-mail. However, no staff member has received anything directly from the firm. She stated that staff saw the notification in *Pension and Investments* online. Ms. Bhatia informed the Board that she requested PCA look into these developments because staff had no indication this acquisition was occurring. She stated there was a concern because it brings up similar issues that were encountered in the selection process of the Proxy provider and the conflict of interest issues that were identified with ISS. Ms. Bhatia reported, according to the notification, the services to DWP should not be impacted; however, staff will keep a close watch. Ms. Bernstein indicated she had spoken with Glass Lewis and added if they were a manager they would be placed on watch for organization issues, but at this point there is no cause for changing firms. President Romero inquired if it was Ms. Bernstein's recommendation to place Glass Lewis on watch as a formality. Ms. Bernstein responded there was not a watch policy in place for proxy service providers. She recommended Glass Lewis remain and PCA would look at it more in depth and continue to monitor the firm. She stated she did not see any cause for stopping the process and switching proxy service providers at this point. Mr. Moore inquired about Xinhua Finance, if it is entirely private capital, and if there is any government involvement. Ms. Bernstein responded as far as she knows it is private, but those are the kinds of questions PCA would be looking into and would come back before the Board with a more in depth review in January.

13. Future agenda items

Ms. Bhatia informed the Board that staff would be providing the Board with ongoing updates on the developments in connection with the new system.

Mr. Moore commented with regards to the Sudan issue, Ms. Bhatia mentioned there might be a joint letter prepared. He then inquired if the Board needed to take any action to authorize it. Ms. Bhatia responded that she felt it would be good to have a Board consensus on the matter. She stated the other City pension plan managers were writing the letter and she was not sure if the Board members were involved, but she would get more information. Ms. Bhatia indicated the last few updates had been signed by President Romero, so if the Board members all agreed, she would begin working with the other City pension plans to find out what needs to be done. She inquired if the Board wanted to do a joint letter to the Mayor. President Romero expressed he felt it was a good idea. Mr. Moore agreed with President Romero, stating his preference would be that the president of each board signs the letter.

The Board meeting was adjourned at 10:31 a.m.

JAVIER ROMERO
President

SANGEETA BHATIA
Secretary

Irene Colon Gonzalez
Recording Secretary