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

MINUTES – FEBRUARY 11, 2004

Present:

Javier Romero	President
Lilly Calvache	Vice-President
Dan Mirisola	Board Member
Ron Vazquez	Chief Financial Officer
Michael T. Moore	Retiree Member
Gerard McCallum II	Board Member

Absent:

Frank Salas	Assistant General Manager

Others Present:

Duamel Vellon	Retirement Plan Manager
Lesley Kuo	Investment Officer
Mike Wilkinson	Deputy City Attorney
Neil Rue	Pension Consulting Alliance (PCA)
Sarah Bernstein	Pension Consulting Alliance (PCA)

President Romero called the meeting to order at 8:14 a.m. after the Pledge of Allegiance.

[Pledge of Allegiance]

Mr. Vellon indicated there was a quorum of the Board present.

PUBLIC COMMENTS

Mr. Vellon inquired if there were any public comments and there were none.

Mr. Vellon introduced item 1 of the agenda, as the presentations of the prospective Small Cap Domestic Equity Managers. He stated Trust Company of the West (TCW), who was the first candidate, withdrew their presentation to the Board. Mr. Vazquez, noting the presence of ITS representatives, felt the Board should first address item 3.

President Romero then ruled that item 3 be discussed next.

3. Consideration of solution to Federal Tax over withholding on the first retirement allowance paid to retirees in 2004 (February 1 for January).

Mr. Vellon introduced item 3 and explained the situation as simply a system problem in the February 1st of 2004 payroll which resulted in the taxable amount being overstated for the retiree pensions (the gross amount was shown to be the same as the taxable amount, which should be less than the gross amount due to an excludable portion). He indicated many retirees noticed this difference and contacted Mr. Moore and several members of the Retirement staff. He continued retirees called the Retirement Plan due to the taxable amount being overstated resulting in the Federal Tax withholding being overstated (for most retirees, between $10 - $25 was over withheld, but for others, a more significant amount). Mr. Vellon stated in a meeting between him and ITS staff, 3 options were decided upon: 1) (Mr. Vellon's recommended option to the Board) an adjustment can be made in the March 1, 2004 payroll to make up the difference for taxes over withheld (e.g. withholding $10 less for the March 1st pension to compensate for $10 over withheld from the February 1st pension); Year-to-Date totals for taxes withheld will be unaffected by this method 2) (Mr. Vellon not recommending this option to the Board) separate checks are issued for the taxes over withheld on the pensions. He noted, regarding the 2nd option, Mr. Vazquez suggested this may not materially impact retirees, and the Board would not make adjustments (Federal withholdings remaining unaltered until the end of the year, when the amount of taxes over withheld for the year would be credited back to the retirees through a refund). Mr. Vellon then proposed the Board support an adjustment in the March 1, 2004 payroll, according to the method suggested in the 1st option mentioned above. He explained the urgency for the placement of this matter on a future agenda for Board discussion because there would be a limited window of time for ITS to make the necessary adjustments for the March 1, 2004 payroll.

Mr. Mirisola entered the meeting at 8:16 a.m.

President Romero expressed both his and the Board's appreciation and acknowledgement of Ms. Cecilia Weldon, Chief Information Officer, and her staff for their exemplary work and effort in resolving the 1099R matter and supporting the decisions of the Retirement Board during these difficult times.

President Romero then expressed he was very comfortable with the proposed adjustment for the March 1st pension, pending ITS and Board member comments regarding this.

Mr. Moore expressed he would be very comfortable with the method of correction for over withholdings of taxes on the February 1st pension if it was simply to make an adjustment over a course of one or two pay periods, but not with a method which would require the issuing of separate checks. Mr. Vellon indicated he too did not support the alternative method of issuing separate checks, which was suggested by ITS.

Mr. Vellon explained if the Board was comfortable with the method which would make adjustments to the March 1st pension, no further action would be needed from the Board, and he would proceed with implementing this method. Mr. Moore inquired if a letter would be sent to affected retirees, indicating the adjustment method used to correct the over withholdings of taxes. Mr. Vellon responded he was proposing that any letter of explanation sent out to affected retirees should be combined with any letter the Board was planning to send, including the one Mr. Moore suggested be sent out to retirees (this last letter being slated for Board discussion at the February 18th Board Meeting). Mr. Moore indicated his approval of Mr. Vellon's proposal.

Mr. Vazquez inquired if the pension check to be adjusted would be mailed around March 1st. Mr. Vellon responded in the affirmative. Mr. Vazquez then inquired the run-date for these checks. Mr. Vellon responded between the 12th and 16th of February.

President Romero inquired of Mr. Vellon if the instructions, regarding the corrections to tax over withholdings, were clear. Mr. Vellon responded in the affirmative. President Romero, Ms. Calvache, and Mr. Vellon expressed their appreciation of the efforts and support of Ms. Weldon and Ms. Linda Wah, Assistant Director of ITS, in this matter.

[The regular order of the agenda resumed]

1. Interviews and possible selection of an Investment Management Firm or Firms (From those responding to the Plan's Request for Proposal – Small Cap Value Domestic Equity Managers)

a. Trust Company of the West

Trust Company of the West withdrew their presentation to the Board.

Mr. Richard A. Wells, Portfolio Manager, and Mr. John D. Race, Co-Founder and Partner, of DePrince, Race & Zollo approached the table.

b. De Prince, Race & Zollo, Inc.

President Romero recognized the representatives from De Prince, Race & Zollo, Inc.

Mr. Wells provided the Board with background information on De Prince, Race & Zollo, Inc. He noted, prior to their establishment of this firm, the 3 Partners (Mr. Race, Mr. Gregory M. DePrince, and Mr. Victor A. Zollo) were at Sun Trust Capital Management where these three men had wonderful careers, during which they were able to take Sun Trust from approximately $500 million in assets to $14 billion in assets. Mr. Wells further noted since the Partners desired to focus on institutional business such as the Retirement Plan, they started DePrince, Race & Zollo (which is 100% independently owned and operated). He stated the ruling principle behind the establishment of the firm would be the maintenance of the small size of the firm and the reasons for this were: 1) (the primary reason) to provide the best performance 2) to provide the best client service possible. Mr. Wells elaborated the firm has set-up very strict asset caps and currently has approximately $3.3 billion under management, of which approximately $1.2 billion is under management in the Small Cap Value discipline. He expressed DePrince, Race & Zollo is strongly committed to capping-off a product before it is too big (to successfully manage it) and this is something very few other managers would commit themselves to do.

Mr. Wells stated, regarding DePrince, Race & Zollo, the firm is located in Orlando, Florida, and handles a wide variety of accounts (different types of funds such as a number of public funds, corporations, endowments, and foundations) within a very broad geographic range (a mixture of clients ranging from San Joaquin County Employees' Retirement System in California to the SPX Corporation in North Carolina). He indicated, from the inception of the firm's Small Cap Value product in 1995, the firm outperformed in 33 of the 39 negative months (over 85% of the time having a cumulative outperformance of roughly 162%). Mr. Wells explained, presently, the firm has 3 other products and approximately 25 professionals working with them.

Mr. Wells, while mentioning the firm's success in down markets through its valuation work, proceeded to focus on dividend yields, explaining their downside protection. He said the firm's portfolio is presently yielding between 2.5-3.0%. Mr. Wells stated, regardless of the actuarial assumption, just a 3% dividend return each year would automatically achieve between 30-40% of the required level of earnings. He noted this is immensely important to note when considering higher yielding stocks. He then stated Mr. Race would talk about the firm's (equity) philosophy and the daily buy/sell decisions.

Mr. Race (who also ran the firm's Small Cap Value discipline) explained, regarding the firm's philosophy, along with an emphasis on dividends, the firm is "bottom-up," which means the firm examines the companies which are trading in the very bottom of their relative range, works up through the industry and then through the economy. He stated what the firm is constantly doing is rotating companies in and out of the portfolio based upon risk parameters. Mr. Race noted another distinguishing quality is the firm's commitment to either speak or meet with senior management in every company the firm buys (i.e. either the CFO or CEO), to determine both the company's status and credibility. He stated, regarding the firm's buy decision, the firm is looking for companies with 1% dividend yield and a $1.5 billion market cap. Mr. Race explained when the universe of 8,000 Small Cap names is screened, there are roughly 1100 names which meet this criteria. He continued that the firm puts these companies through a valuation process and determines if the stock is trading at the top third of its relative dividend yield over the last 10 years and the bottom third of its price-to-book, price-to-earnings, or price-to-cash range. Mr. Race stated, when this valuation process is used, the original 1100 companies are condensed to roughly 400, which are then assigned to 5 full time analysts (working in the Small Cap area), who look for at least 2 fundamental catalysts (things which will cause improvement in execution, yet meet the firm's operational time frame). He stated at the end of this process, the list of companies is further distilled to about 100, and then the firm evaluates which of these have the best upside versus downside (2 times the upside relative to the downside). He commented the sell decision is just the opposite of the buy decision.

Mr. Vazquez inquired regarding DePrince, Race & Zollo's buy decisions and the companies it worked with, did the firm buy more than 100 stocks. Mr. Race explained the firm has a well diversified portfolio of roughly 70 – 75 names. He explained the firm attempted to obtain a minimum position in a company of 1% to a maximum of between 4-5%.

Mr. Race explained the sell decision was actually the opposite of the buy decision, since if one of those 3 criteria (i.e. yield, relative valuation, or fundamental catalysts) were violated, then the firm would sell the stock of a company. He also stated one of the firm's internal goals, which has not yet been stated, was for the portfolio's yield to be at least 50% higher than the Russell 2000 in the broader Small Cap market.

Mr. Vazquez inquired of Mr. Race, regarding the process involved in the buy decision, is this process a recurring one. Mr. Race responded the firm looks at the portfolio every day, on a relative valuation model. Mr. Vazquez further inquired if any of those stocks do not fall down into the final group of 100 the firm would be considering, would the firm then sell these stocks. Mr. Race replied in the affirmative. Mr. Vellon inquired if this was a strict discipline of DePrince, Race & Zollo. Mr. Race responded this is a strict discipline which the firm has. Mr. Vellon further inquired whether managers have discretion regarding this aspect of the firm's sell decision. Mr. Race responded the firm uses discretion and explained the discretionary part is the catalyst, which is the major, artistic aspect of the sell decision. He stated the firm does not deviate from the discipline. Mr. Race noted roughly 70% of the time, the fundamental catalysts do work out as the firm expected them to, but the rest of the time, the catalysts do not work out. Mr. Race explained when they do not work out (e.g. when there is a credibility gap with management) this is when the firm will sell the stock (this occurs 10-15% of the time).

Mr. Vazquez inquired what is the firm's turnover rate. Mr. Race responded a little over 80%, and this is indicative of the firm following its buy/sell discipline rigidly, and the firm having ample liquidity in the companies it buys. He commented, these factors make the firm somewhat unusual for a value manager, since the firm is not buy and hold. Mr. Race indicated the reason for this is the inefficiency of the Small Cap market. Mr. Vellon inquired how the firm defined the 80% turnover mentioned. Mr. Race responded this is the combination of the buys and sells together, divided by the value of the portfolio.

Mr. Race stated he desired to explain the 3 equally balanced factors through the Friedman Billings & Ramsey brokerage firm. Using a chart, he stated the dividend at the time DePrince, Race & Zollo bought stock in this company was about 7.5-8.0% (meeting the firm's dividend requirement). Mr. Race commented since this was a brokerage firm, it was valued on price-to-book and the firm was looking for a value which is a multiple less than the market. He stated, since the brokerage is traded on an average of a 40% discount to a 20% discount, the firm is buying this company at the very bottom and, therefore, buying very efficiently. Mr. Race then put forth the question, what are the catalysts in this example. He explained they are: 1) a gigantic investment banking calendar with $400 million in revenues last year and (the firm believes) potentially $800 million in revenues for the current year and 2) this company's business is a REIT (i.e. this company buys mortgage back securities) and explained the company borrows at what is effectively LIBOR and it invests what is borrowed in variable rate mortgage pools which have a spread over and above its LIBOR-based borrowings (presently, the spread is 200 basis points, which is a significant contributor to earnings). The combined entity, last year, earned $1.55, and though Wall Street now tends to be conservative with low estimates, the DePrince, Race & Zollo model indicates this company will earn $2.50, which demonstrates substantial growth. Mr. Race continued the stock of this company has done well, it is trading toward the upper end of its range, and the firm is waiting for 1-2 more quarters of very good earnings before it discards this stock.   Mr. Race then inquired if the Board, at this point, understood the process carried out by the firm before execution: using the 3 equally balanced factors, contacting a company, meeting with a company's management, and forecasting a company's earnings.

Mr. Vazquez inquired of Mr. Race, regarding the firm Friedman Billings, if this was one of the brokers used in DePrince, Race & Zollo's inclusion policy. Mr. Race responded in the affirmative and explained DePrince, Race & Zollo uses them in the brokerage business. Mr. Vazquez then inquired what was meant by "small and emerging firms" in DePrince, Race & Zollo's inclusion policy. Mr. Race replied the firm has discovered it is typically beneficial to trade in Small Cap with brokerage companies who provide the best execution. He continued, the smaller brokerage companies are more dedicated to the Small Cap

Arena. He indicated what the firm is trying to do is to execute with brokerage companies who the firm believes will produce the best execution.

Mr. Race then used a graph to show that in every year, whether it was a negative year or a positive year, the firm has added value through trading (i.e. the implementation of the firm's buy/sell discipline does work). He displayed by way of a bar graph the firm's equity characteristics, the dividend exhibiting great value, the beta exhibiting deep value, and the P/E (Price to Earnings) on 2004's earnings exhibiting extremely deep value. Mr. Race expressed the firm believes it not only has excellent dividend overlay but it also provides the deepest value. He commented the firm believes all these characteristics together will produce the performance the Board is looking for. He stated that the firm's portfolio has a P/E of roughly 14 times and an expected growth rate of earnings of 25% (though this ranges between 25-35%). He explained one would be buying at a very cheap price and yet getting well above the market growth rates (this being the reason for the firm's optimism for 2004). Mr. Race expressed, at this point, he would let Mr. Wells finish the firm's presentation.

Mr. Wells stated performance is what many clearly look at in a firm. He explained, moving from left to right on a bar graph, it is seen the firm has out-performed in virtually every type of market, since the inception of its discipline, with the exception of this past year. He indicated that out of all of the firm's calendar year returns, there were only 2 time periods of under-performance (in 1998 and in 2002). Mr. Wells explained these 2 years were very similar because there were very speculative markets in both of these years, but after these periods, what occurred of importance was a dramatic out-performance moving forward. Mr. Wells explained the firm started to see the turn around in the 4th quarter of 2002 and is doing very well in the current quarter. Mr. Wells noted it is now turning back to a period which is very favorable for the firm. Mr. Wells concluded by expressing the firm also believes it correlates well with some of the Board's other managers (e.g. the Board's Small Cap Growth Managers) and there would be very little overlap with anything these other managers have and what the firm has. He noted the firm out-performs in value markets and indicated page 27 contained the firm's stated fee schedule (an alternative to this being a type of performance based fee). Mr. Wells elaborated what the firm would propose would be a flat 40 basis points for the product and if the firm out-performed the Russell 2000 Value Index by 300 basis points, the firm would receive an additional 40 basis points and, therefore, the fee's highest level would be 80 basis points (in his opinion, these prices were very aggressive). Mr. Race commented this performance based fee schedule would tie the firm's fortunes to the Board's.

President Romero inquired, for clarification purposes, is the firm's non-performance based fee non-negotiable. Mr. Race responded in the affirmative and commented since 75% of the firm's account base is managed on a favored nation basis, everyone, whose account(s) the firm handles, is on this fee schedule.

Mr. Moore inquired, regarding the firm's philosophy relative to yield investing (the conventional wisdom is for companies, if they are growing, to reinvest in there own business, for example through acquisitions) if the representatives were indicating their firm's discipline (requiring selected companies to produce dividend yields) was adhered to, these companies would not grow too quickly and would make the kind of decisions which small companies at times make. Mr. Race responded Mr. Moore had articulated the very reason for the firm's adherence to its discipline and noted a study was done by a big hedge fund in New York, called AQR, which compared companies who paid out dividends with those who did not. He indicated the former actually had longer term, higher growth rates than the latter because of their stewardship of the money they managed. Mr. Race added the firm's discipline involves a simple return of excess cash to a company's shareholders, a principle which has worked over time.

Mr. Vellon inquired, since both Mr. Wells and Mr. Race were listed as portfolio managers to handle accounts, what would their account load be like and who would take care of the business when they would be involved with presentations. Mr. Race responded this is a good question and explained Mr. Wells as a portfolio manager would be handling the client service and he (Mr. Race) would run the entire Small Cap pool. He explained every account would be individually maintained at the bank through which it is being handled, and he and Mr. Wells would handle every account in the same way, much like an omnibus account. Mr. Race noted the firm's definition of portfolio manager leans more toward the client service side and if selected, both he and Mr. Wells would come to the monthly Board meetings, in demonstration of this. He further noted the firm had 4 very competent analysts at the firm's headquarters to provide management support (for portfolios) whenever he and Mr. Wells would be engaged in other business for the firm.

Mr. Vellon inquired in the pursuit of high yield stocks, does the firm use industry weight controls or does the firm weight its handling of stocks exactly at the index. Mr. Race responded the firm does not have a minimum weight but rather over-weights. Mr. Vellon inquired about the firm's use of cash. Mr. Race replied the cash used will never be more than 5%. Mr. Vellon then inquired of Mr. Race, though the firm adheres closely to its buy/sell discipline, if he would be given the freedom, as a portfolio manager, to hold onto a particular stock if he felt it was advantageous to do so. Mr. Race explained the firm attempts to take as much of the emotion out of the process as possible and elaborated, if a company's stock is moving-up, past where the firm believes its value should be, the firm will sell it. Mr. Race noted the firm believes every stock is a cyclical stock (i.e. every stock is going to have periods of good value and periods of bad value) and bearing this in mind, the firm desires to take the risk off the table; therefore, the firm deems risk as high valuation, high P/E (Price to Earnings).

Mr. Vellon inquired lastly, given the limited availability of Small Cap companies, and the firm's turnover being at least 80%, is it likely the firm could occasionally purchase the same security and then sell it. Mr. Race responded the firm has bought and sold names 3-4 times and cited Calloway Golf and Helix Technology as examples. He noted one of the benefits of the new dividend legislation, which was passed last year, is the ever increasing number of companies who are now paying dividends.

The representatives of DePrince, Race & Zollo expressed their gratitude for being given the opportunity to make their presentation before the Board and left.

Mr. L. Kenneth Brooks, Managing Director of Robeco USA, Inc., and Mr. David M. Dabora, Principal and a Lead Small Cap Portfolio Manager of Boston Partners Asset Management, L. P., approached the table.

c. Boston Partners

President Romero recognized the representatives from Boston Partners.

Mr. Brooks gave an overview of Boston Partners, indicating that Boston Partners was primarily an asset management firm (i.e. the firm focuses on value investing). Mr. Brooks stated the firm's professionals have between10-20 years of investment experience and have worked together for a lengthy period of time. He stated, regarding the assets of the firm, currently the firm has $10 billion of assets under management and $800 million in this particular, Small Cap Value product (which would be capped out at $1 billion). Mr. Brooks stated on page 3, the representative client list (currently 17 clients) in this particular mandate is shown and essentially indicates the firm has a number of public funds, corporate funds, foundations, and endowments (the small group enables the firm to fulfill it desire of providing the personal attention requested by many of these clients). Mr. Brooks indicated the next phase of the presentation would be made by Mr. Dabora, who would talk about his investment team and the process of the firm's program.

Mr. Dabora indicated that the firm has a Small Cap team (consisting of 4 dedicated individuals and supported by 3 traders), 3 individuals (all of whom are Small Cap Specialists) providing him support (in the capacity of assistant portfolio manager II), and a pool of 15 fundamental and quantitative analysts. Mr. Dabora noted that the firm's main office is in Boston, Massachusetts, and it has 2 branch offices in San Francisco and Los Angeles, California (where the entire Small Cap team is located).

Regarding the firm's investment strategy, Mr. Dabora stated the firm is firstly a value investor (he noted the firm is somewhere in the middle of the value spectrum, having some stocks which are deep value/contrarian and others which are growth at a reasonable price). He indicated that from an overall portfolio perspective, the firm's stocks are value with a catalyst. Mr. Dabora stated that the firm engages in investment research, and they do their work themselves (with 18 individuals functioning as support staff for the firm's strategy). He noted that 90% of the firm's work is fundamental analysis and10% is quantitative work. Concerning the capitalization aspect of the firm, Mr. Dabora commented the stocks within the firm's portfolio generally have a market cap of $1.5 billion or less (the firm will automatically sell stocks once they reach $2.5 billion). He noted there are over 100 stocks in the Small Cap portfolio product, which makes this a well diversified portfolio (this lowers volatility and risk in the portfolio).

Mr. Vazquez asked of Mr. Dabora, what currently was the average number of stocks in the firm's portfolio. Mr. Dabora responded that the portfolio currently contained about 111 stocks and elaborated by stating that this number (a little over 100 stocks) has been the average number of stocks

Mr. Dabora stated that there were three components of the firm's philosophy: value discipline, internal research focus, and risk emergence (he commented that he had briefly mentioned these). He expressed that the firm's foremost commitment is to value investment and explained that his primary concern, as a portfolio manager, is to buy stocks which are traded at a discount from their intrinsic value. Mr. Dabora noted that the firm is also searching for companies with a "catalyst for change." He further noted that the firm's stock selection process provides consistency and aids in avoiding what the firm calls the "value trap" (i.e. the statistically inexpensive stock which has no hope for improvement).

Mr. Dabora commented that in light of what has been transpiring in Wall Street, firms like the Boston Partners have a distinct advantage.

Mr. Dabora continued to explain that the firm is value oriented; it does its own work, and it has a very diversified portfolio (indicated by over 100 companies within the portfolio). Concerning the minimization of risk, he commented that understanding the risk of every stock in the portfolio is the most effective way to do this. He commented that monitoring risk consumes the majority of his time and this activity provides a framework from which the firm purchases and sells stocks for its client portfolios. He stated that the heart of the firm's stock selection criteria are the following: 1) stocks must be undervalued 2) fundamental analysis in major areas such as a company's competitive position, management strategies, and profitability and 3) a catalyst (i.e. some sort of positive business momentum) to unlock the value of a stock must be present.

Mr. Vazquez inquired of Mr. Dabora, regarding risk control guidelines, if the firm sets a target price for each stock it holds. Mr. Dabora responded affirmatively and commented that the firm is constantly adjusting this target as new information becomes available.

Mr. Dabora, in regard to Mr. Brooks mentioning that the firm would shortly close its product, stated that this closure is one way the firm maintains the product's integrity. He noted that other integrity maintaining measures used by the firm were selling stocks at a $2.5 billion market cap basis, and zero deviation in product style.

Mr. Vazquez asked what the firm's benchmark was. Mr. Dabora replied that it was the 2000 Value benchmark.

Mr. Dabora stated that the firm's weekly research process is a repeatable process, using the firm's discipline. He explained that the beginning of this process examines the existing stocks in the portfolios based on value, fundamental analysis, and catalysts. He stated that the research process also includes monitoring the target prices for these stocks as well as screening the 2000 plus stock universe for new stocks (which would possibly be placed into the portfolios). Mr. Dabora indicated that the three main criteria used for placement of new stocks into a portfolio are: 1) a percentage movement toward the target price 2) a strong enough conviction that the stock will reach the target price given the risks associated with that particular stock and 3) liquidity.

Mr. Dabora then expressed, regarding the area of risk controls, that the firm has had these controls in place and they have worked very well for the firm. He indicated that these controls are: limited investment of 5% in any stock (the foremost control), limited exposure of 35% in a any sector, no market timing (being almost fully invested, at all times, is the goal), and individuals in the firm (outside of Mr. Dabora) who are also monitoring the portfolios to ensure that clients are benefiting from the firm's declared strategy.

Mr. Vazquez asked, regarding the risk control limits, how the firm arrived at the limit of 35%. Mr. Dabora responded that this limit has been used, by the firm, over the years to give their portfolio managers enough freedom to move toward an ascending value without the portfolio being overexposed in any one particular area. Mr. Brooks then inquired of Mr. Vazquez if he asked his question to determine whether the firm had models to set these limits. Mr. Vazquez responded that since this percentage seemed rather high to him, he desired to know where the firm obtained this as its limit. Mr. Dabora explained that the firm has industries where it would never even come close to approaching this level.

Mr. Dabora expressed that he desired next to briefly talk about the performance of the firm's product. He stated that since inception of the product, the firm has provided a consistent performance on both a short and long term basis, and he indicated that the firm has exceeded the product's performance goals by outperforming the benchmark. Mr. Dabora stated that the firm' s goal is to produce annual returns of 7-14% through a market cycle. He then indicated that valuation, Price/Earnings, Price/Book, and Price/Cash-Flow versus the 2000 validated the use of the firm's stock selection criteria. Mr. Dabora noted that fundamental analysis (also part of the stock selection criteria), using OR/OA (Operating Return on Operating Assets), revealed the poor profitability of a company to its operating assets. He further noted, regarding fundamental analysis, that ROE (Return on Equity), indicated whether there was a more profitable company (on average) with a slightly better growth rate than both the 2000 Value and the 2000. Mr. Dabora then explained that a catalyst (another part of the stock selection criteria), though more difficult to capture quantitatively, was seen in 69% of the companies within the portfolio, and their stocks were meeting or beating expectations (compared to both the 2000 Value and the 2000) in the last quarter. He indicated that the firm has a highly successful, proven investment strategy, which has a high probability for strong performance in the future.

President Romero asked, with respect to the stocks within the firm's portfolio, what the turnover was. Mr. Dabora responded that the turnover in the last 12 months had been slightly greater than 50%. President Romero asked further what the historical turnover had been for the portfolio's stocks. Mr. Dabora answered that the historical turnover had ranged from 50% to 120%. Mr. Vellon then indicated that, to his knowledge, the firm's historic turnover had also been higher than 120%. Mr. Dabora explained that before he managed the firm portfolio, the turnover had been as high as 180%.

President Romero inquired, regarding the firm's fees, if these were negotiable. Mr. Dabora explained that they were not negotiable due to the firm having a standard fee for all its clients. Mr. Brooks then noted that though the firm's fees were non-negotiable, the firm has been able to negotiate a performance fee with a particular fund (so hopefully the firm's fee policy would not prevent the Board from choosing the firm as a Small Cap Value manager). President Romero then inquired of Mr. Brooks, if a performance fee were not an option for the Board, would the fees still remain non-negotiable. Mr. Brooks responded affirmatively.

President Romero asked what the company had done as far as community involvement (e.g. mentoring programs, etc.) for women and minorities. Mr. Brooks indicated that, aside from the many things the firm did to assist women and minorities in its community, a number of its professionals were involved with the TOIGO Program (including himself) and participated in NAS conferences (the firm had also been sponsors of NAS). He confessed, however, that with regard to the community of Los Angeles, the firm was not involved (to his knowledge) with community assistance in the Los Angeles area.

President Romero then asked if the firm had a "Step-Out" Program for the firm's brokers. Mr. Dabora indicated that the firm had some clients that desire directed brokerage and; therefore, the firm usually accommodated up to 25% of the amount of trading to directed brokerage. He commented that in the Small Cap area, however, this would not do much to benefit the client or the Plan, so the firm encouraged clients to give the firm full discretion, regarding this matter.

Mr. Mirisola then inquired as to why a trend toward mid-value was seen in the firm's performance record (from March 2000 through 2003) and in over 70% of its portfolios (from March 2000 to at least November 2001). Mr. Dabora replied that the firm has two strategies: the "Small 1" and the "Small 2" strategy. He explained that the "Small 1" strategy (the one most often used) dealt with the portion of the Small Cap market that was far more liquid and generally had been less risky over time than the other strategy. Mr. Dabora noted that there was a large overlap between the two strategies but this particular strategy ("Small 1") did not have much of an emphasis in the Micro Cap area. He explained that the portfolio's largest stock would be $2.5 billion (which was in line with the largest stock within the 2000 Value or the Small Cap sector), but this is slightly higher than the benchmark.

Mr. Mirisola inquired of the firm's representatives if they had prior contact with any of the Board members (e.g. in private, in conferences, etc.). Mr. Dabora stated that he had not had any type of private contact with any of the Board members. Mr. Brooks stated that he had spoken to several of the Board members, attended a number of Board Meetings (and had possibly been seen by Board members at these meetings), and had left messages for Board members. Mr. Mirisola further inquired if the firm's representatives had prior contact with any of the Water and Power Commissioners of the City of Los Angeles (e.g. Kenneth Lombard, Leland Wong, and Mary Leslie). Mr. Brooks indicated that, aside from having seen Mr. McCallum at the last Board Meeting that Mr. Brooks was at, he had no prior contact with any Water and Power Commissioners.

President Romero asked the firm's representatives if they could discuss the firm's prior lost accounts and how these related to the Robeco organization. Mr. Dabora responded that the firm had not lost an account as a result of the Robeco transaction (Robeco's purchase of Boston Partners); however, its only account losses, within the last two and a half years, were related to changes in the firm's portfolio management (the new portfolio manager being Mr. Dabora). He indicated that since these losses, the firm has been very successful and, more recently, negative account activity has been negligible. President Romero then inquired regarding the identity of the Robeco organization. Mr. Brooks explained that Robeco is a bank in the Netherlands, which purchased Boston Partners, and whose activities have no impact on the investment process at Boston Partners (in particular, the firm's strategy, portfolio product, or portfolio managers). He noted that Robeco's senior management assured him that the organization understood that Boston Partners knew more about market place activities (especially investment management) than Robeco. Mr. Brooks commented that one should not expect to see Robeco making changes to the Boston Partners firm. Mr. Rue commented that it would be fair to say that Robeco is a holding company of investment management firms, and consequently, they own other investment management firms as well as Boston Partners.

President Romero then thanked the Boston Partners representatives for their presentation. The Boston Partners representatives expressed their appreciation to the Board for inviting them to be interviewed, thanked the Board, and then left.

Ms. Linda C. Carstens (CFA), Senior Vice President and Client Advisor, and Ms. Caroline Evascu (CFA), Vice President and Equity Portfolio Manager, of State Street Research & Management Company approached the table.

d. State Street Research & Management

President Romero recognized the representatives from State Street Research & Management Company.

Ms. Carstens indicated that Small Cap investing had been the firm's growth engine for its equity effort throughout the 1990's. She noted that the firm introduced its first successful Small Cap product in 1988 (the firm's Small Cap Energy product), a Small Cap Growth product in 1993, and a Small Cap Value product in 1995. Ms. Carstens noted that today, these three products together represent 40% of the firm's institutional assets. She stated that the firm's Small Cap Value product comes in a retail mutual fund version, the Aurora Fund, which is the firm's most sought after and successful mutual fund product. Ms. Carstens stated that the firm's product was created by two talented investors, Rudy Cluger and John Burbank; and due to their impending retirement, the firm, using foresight, had Mr. Burbank select Ms. Evascu (an example of the firm's ability to attract new, youthful talent and to involve them with the firm's product) and Mr. Paul E. Haagensen, who is the Co-Portfolio Manager of the firm's product. She then indicated that Ms. Evascu would complete the presentation.

Ms. Evascu indicated that the firm's heritage was in fundamental research, and she felt that this asset class (domestic equity) lent itself well to fundamental research since these stocks are neither pursued nor valued as they should be by Wall Street and the media. She then explained what set the firm apart from its competitors: 1) the use of its dedicated process to examine companies (involving a search for a theoretical case of 100% up-side over three years) and then the purchase of stocks at a significant discount to this value 2) involvement in "contrarian" situations where sectors were out of favor (where the firm was able to purchase stocks at the bottom) 3) involvement in turnaround situations (the firm invested in situations where fundamental research revealed that the firm's management would be able to correct faulty stocks) 4) the use of the firm's bottom-up process to pick stocks so the firm's sector weightings were a byproduct of this process 5) the allowance of the firms selected stocks to run (e.g. a stock, with a market capitalization of $1 billion but worth $ 4 billion [in the eyes of the firm], being held until it reached fair value) and 6) the long, patient trading of the firm (at times, six to nine months used to build a position, but then this stock would be owned for an extensive period of time [three to four years]), reflected in the portfolio's turn-over statistics (generally between 20–40%).

Mr. Vellon commented that the portfolio's turnover percentage had been 57% and even over 100% at times in the past. Mr. Rue explained that this percentage came from the firm's RFP (Request For Proposal), with the portfolio turnover in the 20%-50% range in the 12 months ending at 2002. He noted, however, that over the last year, the turnover had been over 100%. Ms. Evascu then commented that over the last year, this turnover percentage had probably been a response to the market being up by 50% and taking profits. Mr. Rue then noted, however, that this data (in the RFP) was somewhat outdated, since it covered the 12 months ending September. President Romero then inquired, regarding the 20-40% portfolio turnover mentioned, if these statistics had historical validity if they were to be cited. Ms. Evascu responded in the affirmative and commented that these statistics were the targeted range for the portfolio.

Ms. Evascu noted that though she and Mr. Haagensen had portfolio manager titles, with firm analysts assisting them, all members of the portfolio management team were working as research analysts (they had a mandate to talk to two to three managements per day). She also noted that the firm's Central Research group (which collaborated with the firm's Cap Value and Growth portfolios) and High Yield team (which was involved with the many synergies between the two asset classes) provided great internal resources for the portfolio management team.

Ms. Evascu stated that she believed the firm had in place a wonderful buy process and explained that when the firm searched throughout the Small Cap universe, the firm looked for three characteristics: inexpensive valuation, free cash flow, and multiple catalysts (or price appreciation drivers). She explained that free cash flow gave the portfolio management flexibility (e.g. for involvement in turn-around situations and situations where it would have been desirable to hold stocks for extended periods of time [two to three years]). Ms. Evascu indicated that in terms of multiple catalysts, the team searched for these so that there would be a higher probability that the firm's price targets would be reached. She pointed out, however, that the area of valuation was where the firm truly set itself apart from others. Ms. Evascu noted that the most desirable valuation measure or metric to use was EV/EBITDA (Enterprise Value to Operating Cash Flow). She explained that EV (Enterprise Value) was the market capitalization of a stock plus the debt on the balance sheet and EBITDA is the gross cash flow of a company. Ms. Evascu indicated that the firm preferred this metric for the following reasons: 1) it was important to the team that the cash flow the team identified accrued to the equity and just not the debt of the stock and 2) it provided the team with the perspective of a strategic buyer (when companies acquired other companies, they were more likely to use EV/EBITDA than any other metric). She stated that the aforementioned were the types of things the team was doing in order to proactively look for names.

Ms. Evascu then proceeded to discuss how the team constructed the firm's portfolio since this (according to her) was a very effective risk management tool. She noted that though the firm typically owned between 200-300 companies in its portfolio, she emphasized that the top 70 were actually 60-70% of the portfolio's assets (which truly drove the relative performance of the fund). Ms. Evascu explained that when the firm found a promising company, it was placed in a "farm team" position. She further explained that the firm's "farm team" consisted of over 100 names (which were less than 30% of the portfolio's assets) and this concept was analogous to the "farm teams" of baseball's Major Leagues (i.e. to choose alternates and to sight promising talent). Ms. Evascu elaborated by stating that after the team purchased a stock (typically 25 or 30 basis points worth), it got to know the company's management, waited for a positive data point on its investment thesis, and (if the team found the company promising) it purchased a little more of the stock (if the team made a mistake in the portfolio, it desired to recognize this while the company was still on the "farm team" and to eliminate it there before it was placed into the top 70 company positions).

Mr. Vazquez asked if the average number of stocks in the firm's portfolio was 170. Ms Evascu responded that the current number was approximately 240 and explained that since the market did very well last year, the portfolio's performance increased by 50%, and thus, the farm team had more names in it than normal.

Ms. Evascu then commented, regarding the firm's sell criteria, that the firm obviously desired to buy low and sell high. She pointed out (in order to demonstrate the consistency of the process of the firm's product over time) that the firm had consistently been in the Small Cap value zone for the life of the firm's product, regardless of the product's performance and the make-up of the firm's portfolio management team.

Ms. Carstens then indicated, for all time periods since the inception of the firm's product, that the firm had a solid investment performance and its product outperformed in six of the eight years from 1996 to 2003. She explained that drastically different external environments contributed to the two years of underperformance (1998 and 2002). Ms. Carstens noted that when the firm's portfolio stocks were out of favor, the firm bought or averaged-in and lowered the overall cost on companies the firm liked in its portfolio.

Mr. Vazquez asked what was the size of the firm's portfolio. Ms. Carstens indicated that the firm had approximately $5 billion in assets under management, in the product, which included the aforementioned retail mutual fund and the firm's institutional clients (the firm had opened and closed both of these over time and was comfortable that it could invest all the cash-flow which came into the firm) but the firm was not accepting any new interest in the product. Ms. Evascu commented that the firm did not seek to set capacity on the assets under its management but actually looked at the product on a cash flow basis. She explained that as long as the firm found value opportunities in which to put the money to work, the firm felt comfortable with managing assets of this size (she felt that there were still some value opportunities left in the market).

Mr. Moore then commented that the materials furnished by PCA indicated the forecasted fourth quarter P/E was fairly high compared to what one would have expected for the firm's value portfolio; the last several years it seemed to be performing better than 30-35% (referring to the P/E), and at least in the last quarter of the 2003 calendar year, PCA classified nearly half of the firm's portfolio as growth as opposed to value. He then asked if the firm's representatives could address this. Ms. Evascu responded that the firm's portfolio sector weighting was a byproduct of the firm's "Bottom-up" stock selection process. She explained that financial service and utility stocks typically had low P/E's and they comprised almost 30-35% of the Russell 2000 Value index. Ms. Evascu continued to explain that the firm over-weighted cyclical industries as a byproduct of the firm's process. She commented that because the economy had been in a recession for the last few years, these companies have had low earnings so, on paper, they appeared expensive, and as one moved into a normalized economic environment, one expected these multiples to come down and for the firm's composite P/E to be much lower.

President Romero then asked if the firm's fees were negotiable. Ms. Carstens responded in the affirmative.

Mr. Vellon then inquired how Ms. Evascu expected to replace one of the founders of the firm's product (Mr. Burbank) and make presentations for the firm at the same time (how would she balance office work, investment management, and marketing the firm's product) and other related concerns (such as the volume of accounts she would be expected to handle). Ms. Evascu responded that for approximately one year, the firm had been working with a management team comprised of her, Mr. Haagensen, and Mr. Burbank and all three members of the management team had functioned as equals. She noted however, that Mr. Burbank's involvement, during this time, was continuously being phased out. She indicated that the management team spent over 50% of the their time on the road, engaged in research and company visitations; therefore, it was not difficult for the team (including her) to combine marketing with the research. Ms. Carstens then stated that the firm had other resources, which included two equity product managers, whose primary responsibility was to keep consultants, such as Mr. Rue, informed so that the portfolio management team did not have to; the team was then freed to travel to meet with significant clients. She further stated that Ms. Evascu spent the rest of the time either in the office or meeting at corporate halls.

Mr. Vellon then asked if the firm raised cash when it believed there were no opportunities to purchase certain securities and was it conceivable for the firm to do this. Ms. Evascu responded that the firm's intentions were to remain fully invested and the firm considered fully invested to be less than 5% cash. Mr. Vellon then inquired of Ms. Evascu if this meant that the firm would always be fully invested. Ms. Evascu responded in the affirmative and explained that the firm did not make cash decisions.

Mr. Mirisola then inquired of the firm's representatives why, from September of 2002 to the present, the firm built its portfolio with a very heavy tilt of 40-60% in the Small Growth area. Ms. Evascu explained that the portfolio was being overweighed with cyclical companies, those which had negative or zero earnings three years prior and then experienced very high growth after they came out of a recession; they appeared to have very high growth but in actuality they probably did not. She noted that some of these company stocks had attracted growth investors (the firm considered itself successful that it was selling to growth investors).

Mr. Mirisola then inquired of the firm's representatives (outside of Ms. Carstens' previous contact with Mr. Vazquez) if they had had any form of personal contact with any Board member, Water and Power Commissioner, or other Los Angeles City Official, privately or in public (e.g. at a pension plan related conference). Ms. Evascu responded that, to her knowledge, she had not. Ms. Carstens responded in the negative and then commented that her job was not marketing; therefore, she did not attend conferences and spent all of her time in relationship management activities. She indicated, however, that she was aware that the firm's sister company, State Street Research Realty (SSR Realty), had met with three members of the Board and had contact with Mr. Rue.

President Romero thanked the representatives from State Street Research & Management Company for their presentation. The representatives from State Street Research & Management Company thanked the Board and then left.

President Romero then called for a recess at 9:47 A.M.

[Recess]

The meeting reconvened at 10:05 A.M.

Mr. Paul E. Viera, CEO and Partner, and Mr. Trey Greer (CFA and CPA), Investment Management, of Earnest Partners approached the table.

e. Earnest Partners

President Romero recognized the representatives from Earnest Partners.

Mr. Viera stated that as of the end of last year, the firm managed slightly more than $8 billion in assets. He explained, in order to give the Board a final update on the firm's performance, that last year the firm's Small Cap Value portfolios finished up by 52%. Mr. Viera commented that he believed that the key aspect of the firm was that it was entrepreneurial. He explained that this meant the firm was not owned by a bank, brokerage firm, or insurance company (the firm was not involved in activities outside of investment management).

Mr. Vazquez inquired of Mr. Viera, regarding the $8 billion, which the firm currently had under management, what portion of this was in the firm's Small Cap product. Mr. Viera responded that $1.9 billion was in the firm's Small Cap product. Mr. Vazquez then asked if the firm had any cap on how large the product would become. Mr. Viera stated that the firm believed that the cap was going to be on the order of magnitude of an additional $600 million and when more than $600 million came into the product the firm would close it.

Mr. Viera stated that the firm was proud of its very eclectic client list, whose size was nearly 200. He noted that this client list included many big corporate accounts (e.g. United Technologies, Verizon Communications, General Motors, NFL Players Annuity) as well as many pension plans (similar to the Retirement Plan, so the firm was very familiar with state pension plans, municipal pension plans, and other similar plans). Due to the composition of the firm's client list, Mr. Viera believed the firm understood the issues involved with pension plans.

Mr. Viera stated that the firm viewed the obtainment of good investment results to be dependent on two things: a very strong investment process and outstanding personnel to run this process. He commented that he believed the firm's investment team was one of the finest to be assembled for three reasons: 1) the team consisted of established individuals (i.e. the firm's performance record was created by individuals at the firm 2) the team consisted of experienced individuals (the principals of the firm all had an average of over 20 years of experience in which they actually achieved good results in equity markets) and 3) the team was an eclectic group of individuals. With regard to this last reason, Mr. Viera explained that the firm's investment team consisted of those with diverse vantage points, ranging from personal experience in the 1973-1974 equity markets to those knowledgeable in the latest technological developments. He further explained that, on this team, there were individuals who came from management consulting backgrounds, individuals who were steeped in trading acumen, individuals who were accounting partners, and individuals with credit backgrounds.

Mr. Viera began to summarize the firm's investment process by explaining that the firm believed three actions (which the firm believed it did well and somewhat uniquely) had to be done well to obtain good investment results: 1) focusing attention 2) controlling the risk of the portfolios and 3) executing very good fundamental work. Regarding focusing attention, he explained that the firm used a screening method, which the firm termed "Return Pattern Recognition," to segment the Small Cap Universe of thousands of companies by industries (e.g. railroads, insurance, etc.) and then to ask what were the important characteristics of each industry. Mr. Viera further explained that once the firm ran its screen through the Small Cap universe, this universe shrank from a few thousand names to 150 names (referred to, by the firm as its "fertile fishing pond") which the firm could do in depth research on. Regarding controlling the risk of the firm's portfolios, Mr. Viera explained that the firm used a concept called "Downside Deviation," which allowed the firm to minimize the probability of meaningfully under-performing the benchmark. He stated that the firm could make a statistical representation to its clients, which affirmed that with 80% probability, the firm would be within one downside deviation unit of the firm's benchmark or better. Regarding executing very good fundamental work, Mr. Viera stated that this was the area in which Mr. Greer and the rest of the investment team spent most of their time. He commented that this area was truly about engaging in the fundamentals of the investment process. Mr. Viera stated that he believed what differentiated the firm with regard to the fundamental work was that the firm framed a question before it attempted to answer it. He explained that what the firm desired to do was to spend as much time as possible asking and developing a list of questions which needed to be answered (e.g. what has to be true or what cannot not be true in order for this to be a good investment?). Mr. Viera explained that the firm then went out, applied these questions to a prospective company, and, if the firm received favorable responses, the firm knew this was a company it felt comfortable owning. Mr. Viera then indicated that Mr. Greer would complete the firm's presentation by elaborating on each of the three elements of the firm's investment process.

Mr. Greer indicated the investment team used its screen to identify companies which exhibited the characteristics which had historically preceded their out-performance. He stated that some of the different types of characteristics (these also being industry dependent) which the firm looked for were valuation, Price to Earnings (P/E), market trends (how a stock performed to the broader market), operating trends (e.g. operating margins or inventory turnover), growth measures (e.g. earnings per share growth or revenue per share growth), profitability measures (e.g. return on assets), the economic environment, and the impact the economic environment had (on companies). Mr. Greer explained that the team examined the history of each company in the Small Cap Universe and identified the periods of time the company outperformed. He continued to explain that the team then identified what characteristics were in place just prior to each period of out performance, and compared these with the characteristics which were currently in place in each company. Mr. Greer indicated that those companies, in which a match occurred between the two sets of characteristics, were the ones whose stocks were selected for the team to do its fundamental research on. Mr. Greer then stated that the 150 companies, the ones left after the team had used the firm's screen in the Small Cap Universe, were taken and used to construct a trial portfolio. He indicated that this was done using common sense and statistics. Mr. Greer explained that common sense directed the team to include those 60 stocks which had the highest expected excess return (i.e. the ones the firm had the most conviction in), in a portfolio while still managing risk.

Mr. Greer indicated that it was at this point that the firm used the concept known as "Downside Deviation." He noted that tracking error simply examined the variability of returns around the Russell 2000 Value benchmark, so it did not matter if one was on the out-performance or under-performance side of the benchmark, since the portfolio composition would have been deemed equally risky (using tracking error). Mr. Greer indicated that the firm used “Downside Deviation” to preserve the ability to out-perform (i.e. the portfolio’s ability to out-perform) while minimizing the likelihood that a portfolio the firm managed significantly under-performed the benchmark. He expressed that the firm believed this was what their clients truly cared about, so this was what the firm focused on.

Mr. Greer then discussed a few of the tasks the firm executed in the last step (fundamental analysis) of the firm’s investment process (which also depended on the type of company the firm examined). He explained that the first task the firm did was to look at the competitive framework, which meant examining the attractiveness of the industry the company operated in (i.e. examining the level of competition in this industry, examining the level of growth in this industry, and ensuring that the company was well positioned within this industry). Mr. Greer explained that looking at the competitive framework also meant the firm desired to ensure that the company had some distinguishable advantage (e.g. a cost advantage, a series of long term contracts, a patent, technology, etc.), something which let it stand apart from its peers. Mr. Greer then explained the second task the firm did, regarding fundamental analysis, was to scrutinize the financials, which meant moving beyond the numbers on the income statement of the balance sheet and truly evaluating the quality of the company’s earnings (this included determining the assumptions the company’s management made and the methodologies they used). Mr. Greer noted that this information was found in the footnotes (of a company’s informational statements), so the investment team spent the bulk of its time examining the footnotes. He explained that the third task the firm did was to look at the business environment (i.e. everything that affected the world which might have been outside of company management control), such as the contingencies and world events which were meaningfully impacting the company. Mr. Greer then indicated that the final task the firm did was to assess the management team of a company (e.g. determining how good it was, how deep was it [did it go beyond one or two individuals at the top], and if the firm could have confidence in the corporate governance structure [i.e. if these individuals were looking after the shareholders or themselves]). Regarding the assessment of management, he further indicated that the firm evaluated a company’s “insider trading” activity to ensure that management’s financial activity matched what they said they did. Mr. Greer summarized by stating that if a company passed the firm’s screening process, the firm could then place this stock in a portfolio and manage downside risk, and if this company met the scrutiny of the firm’s entire investment team as well, then and only then did the firm actually put this company in a portfolio.

President Romero then asked the firm representatives what exactly were the firm’s issues with the Board’s insurance requirements. Mr. Rue then asked Mr. Viera if he desired him to summarize the firm’s issues. Mr. Viera responded in the affirmative and Mr. Rue indicated that the way in which the firm responded in their RFP was that the firm had Errors and Omissions insurance of $10 million, though the Board’s Errors and Omissions insurance requirement was much higher than this amount. He further indicated that the firm’s position was that if they were the successful candidate, then they would be willing to discuss the Errors and Omissions coverage requirement.

President Romero inquired if this was the only insurance issue the firm had. Mr. Rue responded that there may have been subrogation issues and explained that the firm did not discuss these issues since it (the RFP) asked the firm to only discuss the Errors and Omissions element (of the Board's requirements). President Romero asked that since, waiver of subrogation was a must as well as the Errors and Omissions to do business with the Board, would the firm be willing to comply with the Board regarding the insurance issues. Mr. Viera responded, regarding the subrogation issue, that he believed this would not be problem for the firm. He continued, regarding the Errors and Omissions insurance, that the level of coverage ($50 million) required by the Board would not be a mutually advantageous relationship for the firm and the Retirement Plan. Mr. Viera explained that though the firm would have made every attempt to meet this requirement, incurring some of the cost, it would have been uneconomic for the firm to move forward given the possibility of incremental insurance costs to Earnest Partners being $300-400 thousand (if this were the cost of insurance) in which case, the firm would have to respectfully decline being an investment manager for the Retirement Plan.

President Romero expressed that it would benefit the Board to know at the present what the firm's position was regarding the Errors and Ommisions insurance issue. Mr. Viera stated that the firm would first have to obtain a quote regarding the cost of the $50 million of Errors and Omissions insurance. He indicated that the firm currently had $10 million of Errors and Omissions insurance and if the cost of purchasing $50 million was going to be over $100 thousand then he believed, due to the firm's incremental cost, that the firm would decline. Mr. Viera expressed that the firm desired to make its position as clear as possible. President Romero then expressed his appreciation for the firm's representatives being candid regarding the firm's position. Mr. Viera commented that for certain companies in the world, such as ENRON and WORLDCOM, an insurance requirement such as the Board's was now a business necessity.

President Romero then inquired if the firm's holdings of 50-60 (companies) were the historical number of holdings or were the number of holdings for last year. Mr. Viera responded that 60 names was what the firm actually desired to hold. President Romero then inquired what the turnover was (in the firm's portfolio). Mr. Viera responded that historically it had been approximately 35% but last year the percentage was in the high 20's.

President Romero then asked the firm's representatives if they considered their company to be minority owned. Mr. Viera responded that the firm considered itself to be a very good company who happened to be minority owned.

Mr. Moore then asked if the firm's representatives could address the firm being substantially over-weighted in the healthcare industry since 1999. Mr. Viera explained that the firm had not been drawn to the healthcare industry for any particular reason other than the firm having seen relatively more value in the healthcare sector. He noted that the healthcare industry covered a wide range of companies, and the firm's healthcare holdings were indicative of this (including everything from certain pharmaceuticals, contract research organizations, and distribution companies). He added that he believed, with regard to the healthcare industry, it was one of the most diversified sectors and had one of the highest "r squared " out of any sector among the seven or more listed sectors.

Mr. Vellon inquired if it was true that the the waiver of subrogation requirement was not going to be a problem for the firm. Mr. Viera responded in the affirmative. Mr. Vellon then commented that the firms who had made presentations earlier at this Board Meeting had many more securities in their portfolio. He then asked what would be the firm's response to criticisms that the firm had been overly weighted in the comparatively small number of securities the firm held. Mr. Viera responded by explaining that the firm was attempting to outperform and not to diversify away returns. He noted that the firm believed it could control risk with only 60 names in its portfolio and give the Retirement Plan an excellent opportunity to obtain real value for the fee it would pay. Mr. Viera then expressed that he would criticize those who expected more names (to be in a portfolio) by asking them how they could possibly get any type of performance by holding a much larger number of securities.

Mr. Romero then inquired, regarding the firm's fees, if these were negotiable. Mr. Viera indicated that the firm would work with the Board if an issue arose over a few basis points; therefore, the firm's answer would be an absolute yes.

Mr. Moore commented that PCA's evaluation of the firm's portfolio characteristics seemed to indicate (in particular last year) that the firm had a fair amount of mid-value in the portfolio and a fair amount of mid-growth toward the end of the year. He asked the firm's representatives if they could address this in terms of variance from the benchmark. Mr. Viera explained that, with respect to size, one of the things which occurred was that the firm obtained very good performance so market caps rose 50% on the average; thus, if the names started the year with market caps of $1.3 billion they would have ended the year with market caps of $2.2 billion (he believed this could have been part of the size effect). Mr. Viera explained that, with respect to a certain part (of the portfolio) being classified on a growth basis, the firm examined companies and attempted to determine what was a good value. He then cited an example of companies which could be categorized as growth, depending on the way in which one analyzed them. He stated that the firm owned a number of homebuilders whose growth had been 20-25%, and by anyone's definition, they could have been categorized as growth companies. Mr. Viera noted that these companies traded at nine times their earnings; therefore, the firm felt it was highly beneficial to purchase companies such as these though they would prospectively grow 15-20%.

Mr. Moore commented, regarding PCA's assessment (of the firm's portfolio), that the firm's forecasted fourth quarter P/E ran from 12 to 16 and it had actually been going higher over the course of the last year. Mr. Viera responded by stating that the markets had also gone higher. Mr. Moore then inquired, regarding the firm's historical five years earnings per share, if what the firm indicated as being earnings per share value was actually earnings per share growth. Mr. Rue affirmed that it was actually earnings per share growth. Mr. Moore then commented that these earnings per share growth had been quite high for those low P/E's. Mr. Viera explained that the firm believed this was good. Mr. Rue commented that it was fair to say that based on the information the firm provided, the firm held companies which were significantly larger than the average company. Mr. Viera expressed that he believed this was a fair assessment and explained that one of the reasons for this was the firm's micro-cap strategy, which screened out at the onset, companies in the Russell 2000 which were under $250 million (approximately 30-40% of the names according to Mr. Greer).

Mr. Vazquez inquired what risk control did the firm have in terms of the size of the firm's holdings of a given stock. Mr. Viera responded that it was no more than five percent in any one company. He explained that most of the positions got bought between one and a half to two percent and if they went into five percent it meant good things were happening in a given company (in general, this had been the firm's experience). Mr. Viera further explained that the firm essentially had become hedge clippers and pruned 5.1% back to 4% and 4% was then allowed to grow to 5% (this was the experience of the firm in a number of its names over the last two years).

Mr. Mirisola inquired, regarding the value aspect of the firm's portfolio, if it was due to there being only 60 names in the portfolio, by way of clipping holdings in the portfolio's names, that the firm, in the end, appeared to be more of a Mid Value company than a very strong Small Value company (which was firm's original intention). Mr. Viera explained that he believed what was occurring was that the firm was attempting to be very selective about the names it purchased (due to its goal of out-performance). He further explained that to ensure proper selection (for out-performance) the firm had to obtain the companies whose stock prices were going to appreciate, which resulted in 60 names (for the firm's portfolio) with the effect of the size of the portfolio getting larger. Mr. Viera noted that the firm was currently in the mode of refreshing its portfolio through attempts to find some names, between $250 million to $1 billion in size, which could be substituted for some of the larger positions. Mr. Rue then commented that both of the firm' representatives had said that the firm was screening out a large number of names at a certain market cap so that there was going to be this bias due to the screening process. Mr. Viera affirmed Mr. Rue's comment and added that the firm's portfolio was always going to be larger than the 2000.

Mr. Mirisola then inquired of the firm's representatives if they had met with any members of the Retirement Board, any Los Angeles City Water and Power Commissioners, any City Council Members, or the Mayor. Mr. Viera responded negatively and then inquired if this was going to be a disadvantage for the representatives or the firm. Mr. Mirisola responded negatively and indicated that this was actually beneficial for both him and the firm.

Mr. Vellon commented that since Mr. Viera had successfully grasped the company's philosophy, its strategies, etc., what kind of contingency plan did the firm have if anything were to happen to him. Mr. Viera explained that as part of the firm's disaster recovery plan, a type of a succession scheme was in place so that the "baton" would be passed to a designated partner who would assume his position at the firm.

Mr. Moore then inquired, in light of the large amount of growth of the firm in the last several years, what implication would this growth have for the firm in terms of its ability to handle and manage capital. Mr. Viera responded that the firm desired to have the effect it had with all of its products and shut them down when the firm felt it could no longer do a good job with them. He continued to respond, regarding investment, that he was very comfortable with the investment team the firm had, so the team would be allowed to grow the firm and prove that the firm could still handle and manage the capital over the next five years. Mr. Viera indicated that he believed the real growth and change within the firm was in the firm's "client service personnel," (individuals who did reconciliation's and provided other client-related services) whose number would need to increase if the firm continued to experience growth. He explained that the firm's philosophy dictated that individuals for this group would be hired one year prior to their need within the firm in order for them to be properly trained in the specific way the firm desired to manage its affairs.

President Romero then thanked the representatives from Earnest Partners for there presentation. The representatives from Earnest Partners, expressed their appreciation for being allowed to make their presentation, thanked the Board, and then left.

President Romero expressed that according to their scatter plot, Earnest Partners went for the least risk with very good returns; their standard deviation was the lowest; their annualized returns were the second highest; their turnover was very minimal; and their fees were negotiable. He commented that to him, this company stood up far above the other firms which were interviewed so he was selecting Earnest Partners, subject to the insurance issues; and should these not be resolved, selecting State Street Research & Management Company.

Mr. Vazquez indicated that he agreed with President Romero, regarding his conditions for the selection of Earnest Partners (to him the most impressive firm interviewed and the one he was the most comfortable with in terms of their performance and what they had to present). He then expressed that, with regard to State Street Research & Management Company, he felt very uncomfortable with the amount they had under management in the Small Cap area, which was $5 billion between their institutional and their mutual fund. Mr. Rue commented that Mr. Vazquez had a fair concern. Mr. Vazquez stated that he believed this was what was driving them to 240 stocks and he believed the size of the assets they had under management in this particular style was sort of unwieldy. He noted that the other two firms (De Prince, Race & Zollo, Inc. and Boston Partners) both indicated that they would probably close their position in this particular portfolio to the extent that they obtained the Retirement Plan’s business, and this would put them at $1.5 to $2 billion, which was in line with Earnest Partners. Mr. Vazquez then expressed he would have to ponder a while longer over which of the other firms he would select as his second choice.

Mr. Rue apologized that he did not provide the Board with PCA’s sheet of correlations of active management; however, he did have information which showed that Earnest Partners and State Street Research & Management Company were very similar in terms of the statistics. He stated that, while these firms were not perfect substitutes, one could consider them as quasi-substitutes (as opposed to the other firms). Mr. Rue commented that Boston Partners looked surprisingly different from all the other managers.

Mr. Vazquez then inquired of Mr. Rue what was the Board attempting to complement by making this selection. Mr. Rue responded that the Board was attempting to complement its Small Growth Manager. Mr. Vazquez then inquired which of these would be most complementary to this (Small Growth Manager). Mr. Rue responded that the Board could pick any of the firms since each of them would be quite complementary to the Retirement Plan’s Small Growth Manager.

Mr. Mirisola indicated he liked Earnest Partners as well, for the reasons previously given, but that De Prince, Race & Zollo, Inc. was the only true Small Value Manager. Mr. Rue elaborated by stating that they were the deepest Small Value Manager. Mr. Mirisola then expressed that this firm was the deepest in the portfolio, which was what he liked. Mr. Rue explained they were the deepest in the sense that they were the only one who really keyed in on dividend yield. Mr. Mirisola responded in the affirmative and stated that they were making their money in the Small Value area and they were not risking themselves by moving into Mid Value or Mid Growth to obtain better performance, so he believed that they were more in line with the Board's asset allocation structure. He noted that this firm stayed within their mandate and yet outperformed the index, which was something that he liked. Mr. Mirisola stated that his first choice would be De Prince, Race & Zollo, Inc. and then his second would be Earnest Partners.

Ms. Calvache indicated that though she originally saw Boston Partners and State Street Research & Management Company as equals, with De Prince, Race & Zollo, Inc. standing out ahead of these (for the same reasons as Mr. Mirisola), Earnest Partners impressed her to the extent that her first choice was now Earnest Partners (with the same conditions Mr. Vazquez and President Romero had regarding the insurance) with De Prince, Race & Zollo, Inc. as her second choice.

Mr. Moore expressed that Earnest Partner was certainly the strongest candidate for him. He indicated that State Street Research & Management Company was still his second choice (though he was impressed with De Prince, Race & Zollo, Inc. based on their presentation and the materials they sent). He stated that his major concern obviously was still the insurance issue and the question he had regarding this was how much flexibility did the Board have in this area. President Romero responded that, after discussing this issue several times with the Department's Risk Management, the answer was still no (unless Risk Management had recently changed its position). Ms. Calvache indicated that it had not changed to her knowledge. Mr. Vellon indicated that no change in positon had been made by the Risk Manager.

Mr. Moore then inquired if this individual was the Department's own Risk Manager. President Romero, Ms. Calvache, and Mr. Vazquez all responded in the affirmative. Ms. Calvache indicated that Risk Management was headed Mr. Avery Neaman. Mr. Moore then inquired if this group was in Mr. Vazquez' organization. Mr. Vazquez responded in the affirmative. Mr. Moore then inquired if Mr. Vazquez was confident regarding the level his group was setting on this matter. Mr. Vazquez responded that these were very stringent levels but these levels were applied across the board. He then indicated that he would talk with the Risk Manager to see if the Board had any latitude in this matter.

President Romero asked if any of the firms who had made the insurance requirement a significant issue, for the record, eventually managed to comply. Mr. Rue commented that one had to keep in mind that, regarding Earnest Partners, the Board was dealing with a "boutique" firm, the other firms in the other spaces where the Board has dealt with (e.g. Merrill Lynch, etc.) were "big boys" and they had the capability to make a business decision on the Errors and Omissions, and they could probably cover it across their huge cost base, whereas Earnest Partners said they just couldn't cover it cost-wise. President Romero then expressed that his only concern with this was that these big players would then say that you did this for them (the Board lowered the insurance requirement for the Earnest Partners because they were a "boutique" firm) and this was not fair, so the Board should have to do the same thing for a larger company.

Mr. Vellon then inquired of Mr. Moore, for clarification, if his second choice was State Street Research & Management Company. Mr. Moore indicated that it was.

President Romero then asked Mr. McCallum if he had any comments. Mr. McCallum stated that he totally agreed that Earnest Partners was his first choice, with the same caveats in terms of insurance, and his second choice was De Prince, Race & Zollo, Inc.

Mr. Vellon indicated that for the second place position, there were three votes for De Prince, Race & Zollo, Inc., two votes for State Street Research & Management Company, and Mr. Vazquez was undecided for his second place firm.

Mr. Vazquez then inquired of Mr. Rue why, though State Street Research & Management Company was one of PCA's top 15 managers in terms of Small Value, this firm was not recommended by PCA for serious consideration as a Small Cap Value Manager. Mr. Rue explained that it was for some of the reasons which Mr. Vazquez had previously mentioned. Mr. Vazquez further inquired how 240 stocks in one's portfolio could still classify the firm as a Small Cap Value Manager. Mr. Rue affirmed that, due to the firm's portfolio size, it could not be classified as being purely Small Cap Value. Mr. Vazquez then expressed more of his concerns with three of the firms interviewed: State Street Research & Management Company was not in (PCA's) top 10 list of Small Cap Value Managers, and this firm's risk returns over a five year period were troubling; De Prince, Race & Zollo, Inc. and Boston Partners all have fees which are non-negotiable and relatively high, and these last two firms' incremental value for five year returns versus the benchmark are not much. Mr. Rue explained that the problem concerning State Street Research & Management Company was that it claimed its portfolio was purely Small Cap Value and focused on dividends. He continued to explain that this firm actually had a different concept of what value was and due to this, the firm, over the last year, had moved into the Small Growth arena by investing in the booming technology industry (this arena was where this firm's performance had shined to some degree, including investment in down-trodden growth companies). Mr. Rue explained, with regard to De Prince, Race & Zollo, Inc. and Boston Partners, these firms were a little more flexible, and this led to investment in either larger companies (including high yield companies), which brought them into either the Mid Value arena or to the Small Growth arena (both profitable areas to have currently been in).

Mr. Vazquez inquired of Mr. Rue if PCA would recommend State Street Research & Management Company as a candidate for the Small Cap Value Domestic Equity Manager, since PCA had not specifically ruled it out as one. Mr. Rue indicated that they were among the list of candidates to be considered. Mr. Vazquez then stated that he would select State Street Research & Management Company as his second choice, based on the risk returns, as opposed to De Prince, Race & Zollo, Inc. or Boston Partners.

After further discussion, Mr. Vellon then indicated that, for the second place position, there were now three votes for De Prince, Race & Zollo, Inc. and three votes for State Street Research & Management Company, with one (Mr. Mirisola) for De Prince, Race & Zollo, Inc. as his first choice.

President Romero then urged the Board to vote on the firms separately, stating that the Board should vote on the choice for the first place firm separately, and then the Board would determine the firm for the second place.

Mr. Mirisola motioned to hire Earnest Partners as the first choice for Small Cap Value Domestic Equity Manager, subject to the resolution of the insurance issues. Seconded by Mr. McCallum and carried unanimously after the following vote:

Ayes: Moore, Mirisola, Calvache, Romero, Vazquez, and McCallum
Nayes: None

Mr. Mirisola then inquired if the Board was hiring two firms for this mandate or just one. Mr. Rue responded that this (second choice) was a contingency. Mr. Vellon commented that if the first choice (Earnest Partners) could not meet the insurance requirement, the Board would then work with the second choice.

Mr. Rue then commented that State Street Research & Management Company under-performed in bad performing markets but when the markets gained some momentum (e.g. in the 1999 or 2003 period) this firm did well (searching for growing companies, a strategy which did not always work when markets were not performing well). He continued to comment, with respect to De Prince, Race & Zollo, Inc., that this firm under-performed in good performing markets, but they out-performed in very poor markets (for a four out of five year period). Mr. Rue noted that this was what focusing on dividend yield would do.

Mr. Mirisola expressed that his desire was that the Board hire a manager who could produce money while staying within the mandate of being Small Cap Value. He then stated that De Prince, Race & Zollo, Inc. and Earnest Partners (who had moved slightly away from the mandate) would be able to do this. Mr. Mirisola commented that Street Research & Management Company (who achieved their performance through growth) would ruin the Retirement Plan during a bad market, in the Small Cap Value area. He then inquired of Mr. Rue if he would foresee Earnest Partners suffering the same (severe) losses that the Retirement Plan's Small Growth Manager would during a market crash.

Mr. Rue responded that though Earnest Partners' performance results showed that they had out-performed in every single year, he believed that they had suffered greater losses than De Prince, Race & Zollo, Inc. (whenever the market environment had caused this to occur). Mr. Mirisola agreed with Mr. Rue and commented that Earnest Partners would suffer greater losses since this firm was improving its performance in the asset class by moving out (of this class).

Mr. Moore inquired how much the Board was considering for management under the Small Cap Value Manager. Ms. Kuo indicated that this amount was approximately $95 million.

Mr. Vazquez then indicated he would be comfortable with changing his second choice to De Prince, Race & Zollo, Inc.

Mr. Moore commented that the other point he thought he would make, with respect to Earnest Partners, was that given the fact that they had lower fees than De Prince, Race & Zollo, Inc., there was even some room to deal with this insurance issue within their fee schedule, and he believed the Board should be open to this as well. Mr. McCallum expressed his agreement with Mr. Moore's comment. Mr. Vazquez expressed his agreement with Mr. Moore's comment completely.

Mr. Mirisola then motioned to have De Prince, Race & Zollo, Inc. as a second (contingent) choice for Small Cap Value Domestic Equity Manager. Seconded by Ms. Calvache and carried unanimously after the following vote:

Ayes: Moore, Mirisola, Calvache, Romero, Vazquez, and McCallum
Nayes: None

Mr. Vellon indicated that the Board received the letter from PCA confirming that INVESCO and MFS would be on the watch list (which the Board had already decided upon) and that the Board had another memo, from February 3, 2004, indicating that Merrill Lynch should also be put on a watch list since they were losing a key person for the index fund (this would be put for discussion at a future Board Meeting).

Mr. Vellon stated that the Board received a letter from TCW indicating that they declined to participate (in the interview at this Board Meeting for the position of Small Cap Value Domestic Equity Manager).

2. Consideration of Northern Trust Request for Authorization of cross trading transactions.

Mr. Vellon introduced item 2 as a request for the Board to sign a document authorizing the use of cross trading transactions, opportunities which would save the Retirement Fund money. He indicated that Northern Trust was attempting to obtain the necessary authorization for them to do this under the SEC requirement.

Mr. Wilkinson, who was present at the Board Meeting, indicated that this was a document which could be signed by the Board and he was recommending Board approval of item 2.

President Romero indicated that he fully supported this and he expressed his desire to have PCA on the record that they supported this as well. Mr. Rue indicated that PCA was on the record as supporting this.

Mr. Vazquez then moved adoption of resolution 04-74. Seconded by Ms. Calvache and carried unanimously after the following vote:

Ayes: Moore, Mirisola, Calvache, Romero, Vazquez, and McCallum
Nayes: None

The Board meeting was adjourned at 10:30 A.M.

JAVIER ROMERO President	DUAMEL VELLON Secretary

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Acting Recording Secretary