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

MINUTES

JANUARY 13, 2010

Board Members Present:
Javier Romero, President
Cindy Coffin, Vice President
Barry Poole, Board Member
Michael Moore, Retiree Member
S. David Freeman, Interim General Manager

Board Members Absent:
Jeff Peltola, Chief Financial Officer
Appointed DWP Commissioner - Vacant

Staff Present:
Sangeeta Bhatia, Retirement Plan Manager
Monette Carranceja, Asst. Retirement Plan Mgr.
Mary Higgins, Asst. Retirement Plan Mgr.
Jeremy Wolfson, Chief Investment Officer
Julie Escudero, Utility Executive Secretary

Others Present:
Alan Manning, Assistant City Attorney
Mike Moy, Pension Consulting Alliance
David Sancewich, Pension Consulting Alliance
Sarah Bernstein Pension Consulting Alliance

President Romero called the meeting to order at 10:04 a.m. following the Pledge of Allegiance.

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

Public Comments

No public comments were received.

Mr. Romero introduced the following new Retirement Office employees:

Aurora Palma-Cabarrus, Senior Clerk Typist, Administrative Section
Melisa McElliot, Limited Clerk Typist, Benefits Group Scanning Section
Luisa Barrios, Limited Clerk Typist, Benefits Group Scanning Section
Nathan Ngo, Clerk Typist, Systems Integration Section

Mr. Romero called for a motion to approve Consent Items 1 and 2:

1. **Approval of Minutes for:**
   August 19, 2009, Audit Committee Meeting
   November 18, 2009, Special Retirement Board Meeting
   December 9, 2009, Regular Retirement Board Meeting

2. **Termination from Rolls**
   Termination from December 2009 Retirement Roll
   Termination of Mary Dell from the November 2009 Survivorship Roll
   Termination of Ronald Moisan from the December 2009 Permanent Total Disability Roll
   Termination of Tyler Vickers from the January 2010 Family Death Benefit Roll

Regarding Item 1, Mr. Moore asked that Item 9 of the November 18, 2009, Minutes *(Presentation by Pacific Alternative Asset Management Company-Hedge Fund of Funds Annual Performance Review)* be amended to read as follows:

"Mr. Moore asked about the significant amount of liquidity resulting from the economic stimulus and if the money to be withdrawn over time by the Federal Reserve would cause inflation."

Mr. Moore also asked that the second to the last paragraph of Item 11 of the November 18, 2009, Minutes *(Presentation by Pension Consulting Alliance, Inc. - Private Equity Second Quarter Performance Review as of June 30, 2009)* be amended to read as follows:

"Mr. Moore asked how leverage was being viewed . . ."

Ms. Bhatia stated that Staff had continued to review the December 9, 2009, minutes after they had been mailed and had made some minor corrections.

Ms. Escudero reviewed the minor changes. She also noted the following content changes:

- The record of votes for Item 3 *(California Association of Public Retirement Systems – Letter and Press Release Regarding Legislation Concerning Placement Agents)* was corrected to read:

  Ayes: Romero, Coffin, Peltola, and Moore

- The third paragraph of Item 5 (Presentation by Glass Lewis – Annual Proxy Season Review) was corrected to read:

  ". . . the Securities and Exchange Commission . . . proposed a higher threshold for proxy access of between 3% and 5% for mid-cap and small-cap companies with the lowest proposal being 1%. "

- The third paragraph of Item 14 *(Retirement Plan Manager's Comments)* was amended to read:

  "Ms. Carranceja further added Staff is getting prepared to implement the Retirement, Death and Disability component, and explained more ongoing testing was needed."

With the changes to the minutes noted, Mr. Moore moved for approval of Items 1 and 2; seconded by Ms. Coffin, and carried unanimously after the following vote:

Ayes: Romero, Coffin, Moore, and Poole
Nays: None

Mr. Romero called for discussion on Received and Filed Items 3 through 8:

3. Report of Payment Authorizations
a) November 2009
b) December 2009

4. Notice of Deaths for November 2009

5. a) Summary of Investment Returns as of November 30, 2009
b) Market Value of Investments by Fund and Month as of November 30, 2009
c) Market Value of the Retirement, Death, and Disability Funds and Retiree Health Care Fund as of November 30, 2009

6. **Report on Status of Insurance as of November 12, 2009**

7. **Report on Organizational Change at MFS Investment Management**

8. **Report on Organizational Changes at Wells Capital Management**

With regard to Item 6 *(Report on Status of Insurance as of November 12, 2009)*, Mr. Moore asked if the situation regarding the lack of insurance documents from Loomis, Sayles and Co., as well as Pyramis, had been rectified. Mr. Wolfson responded that even though the status report listed those two files as being closed as a result of three unsuccessful attempts by Risk Management to receive the required documents, Retirement Staff continues to follow up because the managers do not get paid until they are in compliance.

With regard to Item 8, *(Report on Organizational Changes at Wells Capital Management)*, Ms. Bhatia commented that because additional organizational changes at Wells Capital had occurred after Staff's report was submitted, Staff would be bringing this item back as an action item with a possible recommendation to place Wells Capital on watch status.

> *With no further discussion, Mr. Moore moved to accept Items 3 through 8; seconded by Ms. Coffin and carried unanimously after the following vote:*
>
> *Ayes: Romero, Coffin, Moore, and Poole*
> *Nays: None*

(Mr. Freeman joined the meeting at 10:14 a.m.)

9. **Presentation by Pension Consulting Alliance, Inc. - Hedge Fund of Funds Quarterly Report as of September 30, 2009**

Mr. Romero acknowledged David Sancewich and Sarah Bernstein of Pension Consulting Alliance, Inc. (PCA).

Mr. Sancewich reported both funds in the portfolio *(Aetos and PAAMCO)* continued to outperform. He noted the portfolio outperformed the median fund for all time periods by a significant margin net-of-fees and has added value since inception. The portfolio was up 2% over the last month and up 1.4% over the latest one-year period. He noted the portfolio, over the latest since-inception period, added value versus equities; however, it underperformed the Barclay's Aggregate largely due to the 2008 market instability.

He reviewed the allocation breakdown and pointed out that Aetos and PAAMCO add value differently. He noted Aetos was overweight in event driven funds, while PAAMCO had a larger weight in opportunistic funds.

Mr. Freeman asked how much of the total portfolio was invested in hedge funds, and Mr. Wolfson answered it was 1%. With regard to the remaining 99% of the portfolio, Mr. Wolfson referred back to Item No. 5 on this agenda and the chart titled Market Value of Investments. He explained that chart represents a snapshot of the entire portfolio and staff provides this information to the Board monthly. Mr. Freeman suggested staff present this information in a larger, easier to read format.

Mr. Freeman said he wanted to ensure staff was closely watching how the retirement funds are allocated, and asked if this information was conveyed monthly. Ms. Bhatia stated Staff and Pension Consulting Alliance, Inc. (PCA) routinely submit several reports to the Board and funding was currently at 90%.

Mr. Moore added that PCA provides quarterly reports, the investment managers provide annual reports, and the actuary provides funding information annually due to the complex process involved. He stated he is comfortable with the asset allocation and the regular information the Board receives, and he noted the diligence of the Board in getting the Plan to where it is today.

Mr. Sancewich reviewed the additions and terminations within each firm. He concluded by reporting that both Aetos and PAAMCO are currently on watch due to their short-term performance; however, PCA plans to update the Board in February and will most likely recommend at that time that Aetos and PAAMCO be removed from watch status.

10. Discussion of Changes to Bank of New York Mellon's Securities Lending Program

Mr. Wolfson provided the background for this item by explaining that the financial crisis of 2008 had impacted the securities lending program, and the representatives from the Bank of New York Mellon (BNY) were here to review the impact and the steps they have taken to address it.

The Board recognized Mike Ferguson and Mike McDermott.

Mr. McDermott explained the function of BNY's securities lending service, where assets are held in safekeeping with BNY Mellon providing an opportunity for BNY to lend the assets to approved borrowers on a temporary basis in exchange for collateral in order to generate spread and earnings.

He reviewed the market impacts that occurred over the past 12 -18 months and reported that many of the negative factors have begun to turn around. He highlighted the steps BNY has taken to reduce risk, increase controls, and increase transparency. He reported they moved to overnight-only investments with incremental collateral to help the Net Asset Values of the collateral pool and increase liquidity. He explained they also moved the term investments out of the collateral pool and tightened the guidelines of the collateral pool, in addition to offering an overnight-only collateral pool as an alternate investment. He reported BNY drastically reduced their approved issuer list and increased their due diligence of what counter-parties were borrowing, went from monthly reporting to daily reporting on cash collateral reinvestments, and added a sixth oversight committee called the Valuation Committee. He highlighted the change in the guideline which targeted reducing risk and stated the change is consistent with Rule 2A-7.

Mr. Moore asked if the investments are now more geared toward longer term. Mr. McDermott indicated BNY was not restricted to just an overnight pool. He mentioned their standard pools are currently for 13 months with a focus on liquidity, and the liquidity in the 6-month to one-year term has improved. He added there are more issuers for that type of investment. He further added the pool in which the Plan invests is 50% liquid versus the policy target of 25% liquidity. Mr. Wolfson clarified that Mr. McDermott was talking about separate accounts that can go beyond Rule 2A-7. Mr. McDermott added they were very limited beyond 13-months.

Mr. McDermott provided a market update, commented on the earning trends, and reviewed the spreads.

Mr. Freeman expressed his apprehension with the portfolio's risk factor and asked if the Board was concerned with being approximately 50% invested in the stock market. Mr. Moore responded that he was not concerned because the Board had undertaken a carefully thought-out asset allocation study, which it reviews periodically. He said the Board is currently in the process of making some allocation changes, and noted risk was reduced by changing to multiple asset classes which move differently and have a low correlation to each other. He reiterated that is how the Board has reduced the portfolio's level of risk, along with changing managers who have not performed.

Mr. Freeman said he was proud of what the Board has accomplished, but he was interested in taking a closer look at he Plan's stock investments and requested further discussion at the next meeting.

Mr. Freeman asked why the Health Care Fund's performance was worse than that of the Retirement Fund. Mr. Wolfson explained the Board had recently approved the transition of the Health Care Fund to represent a portfolio more similar to the Retirement Fund, and the returns on the Health Care Fund were representative of the recent transition.

Mr. Romero added that the Board has been very careful with its investments and had hired Pension Consulting Alliance, Inc. (PCA) to provide guidance, and he asked Sarah Bernstein from PCA for her comments.

Ms. Bernstein stated PCA has been the Board's general consultant for several years. She stated the Board continually studies the risks and reevaluates its entire portfolio both in regard to the overall asset allocation and the structures within. She said PCA is willing to provide an overview for discussion at the next Board meeting.

Mr. Wolfson stated the Board needed to determine where to move its collateral investments, and he reviewed the options available.

> *Mr. Moore moved that the Board choose Option 1 to remain in the current ASL Collateral Pool on a risk-adjusted basis; seconded by Ms. Coffin, and carried after the following vote:*
>
> *Ayes: Romero, Coffin, Poole, Moore, and Freeman*
> *Nays: None*

11. Update on Placement Agent Usage by Current WPERP Managers

Ms. Bhatia reported that in July 2009, the Board adopted a policy regarding the use of placement agents, and this item was being brought back to update the Board on the current use of placement agents by the investment managers. She also stated that Mr. Moore had asked staff to send a formal letter to all investment managers asking them to acknowledge receipt and their understanding of the policy. She indicated staff has prepared the letter and was ready to send it. Mr. Moore said he would like to see the letter and asked that it request the investment managers to specify the amount they paid to firms using placement agents. Mr. Wolfson replied that staff would amend the letter as requested.

Mr. Moore asked if Landmark XIV was still utilizing Merrill Lynch as a placement agent. Mike Moy, of PCA, stated he believed they were but he believed it was only for marketing their funds outside of the United States and did not involve the Plan's current investment.

12. Discussion of BlackRock Merger and Organizational Changes

Mr. Wolfson introduced the item and summarized that the Board had placed BlackRock on organizational watch in July 2009 due to its upcoming merger with Barclays Global Investors, which was finalized December 2009. He reported Staff had learned the Plan's portfolio manager would be relocating to San Francisco as Chief Operating Officer in June 2010, and would no longer be managing the Plan's portfolio. He explained BlackRock remains on watch through June 2010, and Staff will continue to closely monitor the account with BlackRock to determine if extending the watch status becomes necessary. He indicated Staff will bring this item back in June with an update and a recommendation regarding BlackRock's watch status.

Ms. Bernstein noted PCA staff would be performing an on-site due diligence visit of BlackRock's San Francisco office by the following week.

13. Discussion of Request by Frontier Capital Management for Exception to the Investment Policy

Mr. Wolfson reported that the Board hired Frontier Capital (Frontier) in July 2009 to manage a Small Cap Growth mandate. He stated Frontier has requested an exception to the Plan's investment policy to increase their cash allocation exposure from the guideline's 5% maximum to no more than 8%.

Ms. Coffin asked why Frontier requested an increase given that the policy guidelines were attached to the Request for Proposal documents. Ms. Bhatia explained as a general rule, the policy requires managers to maintain no more than 5% in cash, but the Board also has the authority to provide an exception to the rules based on a manager's individual investment style.

> *Mr. Freeman moved for approval of Resolution No. 10-52 to amend the Small Cap Growth Equity Investment Policy for Frontier Capital Management to raise their cash limit from 5% to no more than 8%; seconded by Mr. Poole and carried after the following vote:*
>
> *Ayes: Romero, Coffin, Moore, Poole and Freeman*
> *Nays: None*

14. CLOSED SESSION pursuant to Government Code Section 54956.9 (c) to confer with Counsel regarding possible initiation of litigation in one potential case.

The Board met in Closed Session at 11:17 a.m. and met back in Open Session at 11:43 a.m. with no action taken.

15. Retirement Plan Manager's Comments

Ms. Bhatia reported that a system error had occurred which affected employee paychecks for the pay period ending January 3, 2010. She explained some employees might have experienced variations in their deductions for that pay period, and Staff was working to identify the specifics but had sent a general letter to the estimated 1,000 affected employees. She added that depending on each individual situation, the affected employees would either be back-billed or issued a refund. She indicated that Information Technology Services has since implemented specific methods and controls to prevent this type of situation from recurring.

Ms. Bhatia reported she and Michelle Nagin attended a meeting with the City's Chief Administrative Officer (CAO) during the last week of December 2009 to discuss the Richman Initiative regarding potential pension reform. She stated CAO representatives would be meeting in closed session with the City Council to discuss changes to pension benefits for new employees, effective 2011. She added that subsequent to the Closed Session meeting, letters had been sent by the CAO's Office to the DWP unions, and another meeting was held by the CAO on January 8. Ms. Bhatia indicated the invitation to attend the CAO's meeting was as a member of the management employee union and not as a staff member of the Retirement Office. She said she understood that DWP considers the change in benefits a "Meet and Confer" item whereas the CAO considers it a "Meet and Consult" item because it pertains to new employees. Mr. Freeman added that the DWP Board President sent a letter to the CAO stressing the CAO should have first consulted with DWP management and the Retirement Board before looking at DWP's Retirement system, and they should consider the impact on new personnel, existing retirees, and the economy.

Ms. Bhatia reported on insurance issues with the new contracts for JP Morgan Asset Management, Inc.; Western Asset Management Company (WAMCO); and Frontier Capital Management Company. She noted conference calls have been scheduled with the Department's Risk Manager Avery Neaman, and each of these firms' managers, and Staff would provide the Board with an update at a later date. Mr. Romero voiced his concern given that the insurance requirements were included in the Request for Proposal documents. Ms. Bhatia explained that the contracts will not be executed and the mandates will not be funded until the requirements are met.

Ms. Bhatia reported that *Institutional Investment News* recently nominated Jeremy Wolfson as one of the 2010 rising stars in public funds investing, and the awards will be presented in February.

Ms. Bhatia also noted that Retirement Office Staff was asked to make a presentation on the Plan's investment policy at the upcoming meeting of the DWP Board of Commissioner's Investment Committee.

Mr. Poole asked Ms. Bhatia if Staff had received any information on the unresolved governance issue concerning the authority of the Retirement Board. Ms. Bhatia responded that the Department was given until January 15 to provide feedback, and this item will be on the agenda for the next meeting. She provided background on this issue for Mr. Freeman's benefit, as did Mr. Moore and Mr. Poole. Discussion ensued regarding the Retirement Board's authority including approving the Retirement budget and staffing levels. Mr. Freeman stated he believes the Retirement Board is in charge of the Retirement System.

Ms. Bhatia reported Staff is ahead of schedule regarding the distribution of the1099s which are expected to be printed and distributed to the retirees as early as next week.

Ms. Bhatia acknowledged the contribution of all of the employees in the Retirement Office as well as the support staff has received from the Retirement Board, and she provided the following review of the activities and accomplishments of 2009:

- The Retirement Board experienced the biggest change in the composition of the Board with respect to new ex-officio members and the election of a new active employee representative. Staff provided orientation material and scheduled training to help make a smooth transition for the new members. The Commission representative seat remains vacant.

- The Retirement Office handled a considerable amount of media scrutiny regarding the health of the Retirement Fund and the amount paid out to the more highly paid retirees.

- Staff appeared before the City Council and Council Committees with respect to the use of placement agent as well as the health of the Retirement Plan.

- A new Joint Labor Management Committee was formed and meetings have been going well.

- The Benefits and Systems Sections transitioned from the long-time use of Bank of America over to Wachovia Bank and all of the internal processes were restructured accordingly.

- The first module of the new computer system, Penfax, was implemented and the outdated RSS system was discontinued.

- The new FileNet document imaging system, which is separate but related to the new system, was created, and staff developed the necessary associated workflows and processes. Using this new system, Retirement Office Staff scanned approximately 20,000 index cards last year and generated the active member statements.

- The Retirement Office transitioned from the old sealer machine to standard envelopes for retiree communications which will result in future cost savings for the Plan.

- Data cleanup and testing for the new module continues, and the new module is expected to be implemented soon.

- Implementation of the new asset allocation structure, adopted by the Board after a comprehensive process and review, had been postponed due to the financial crisis; but approximately $2 billion has now successfully been transitioned into an index fund, including $55 pertaining to the Small Cap Growth mandate, completing the first phase of the strategic asset allocation process. The Retiree Health Benefit Fund also received an infusion of funds from this first transition.

- The Plan hired several new investment managers: Western Asset Management Company, Frontier Capital, JP Morgan, T. Rowe Price, Mesa West, Oaktree, and Lexington; and most of these contracts have been completed.

- The pilot program for commission recapture was implemented.

- Staff successfully renegotiated down several fees on existing contracts.

- The Board adopted the Placement Agency Policy which was implemented immediately.

- Staff has improved the format for reporting to the Board.

- Staff has maintained the discipline of providing the Board with the minutes of every Board meeting within the month, despite resource challenges.

- The Board also faced the major issue concerning the authority of the Board.

- The remodeling of the Retirement Office has been completed and almost every staff member now has ergonomic furniture and equipment.

- Regular monthly Retirement Seminars were conducted last year with a total of over 500 attendees.

- Management continues to encourage staff training, and 35 Retirement Office employees attended department-sponsored training last year.

- Staff continues to work on improving communication to Plan members, and the first new publication of the reformatted retiree newsletter is expected to be mailed later this month.

16. Future Agenda Items

No future agenda items were requested.

The meeting adjourned at 12:05 p.m.

Javier Romero 2/10/10
Javier Romero, Board President — Date

Sangeeta Bhatia 2/10/10
Sangeeta Bhatia, Retirement Plan Manager — Date

Julie Escudero 2.10.10
Julie Escudero, Utility Executive Secretary — Date