



Executive Staff:

Richard Stensrud
Chief Executive Officer

Jeffrey W. States
Chief Investment Officer

James G. Line
General Counsel

Kathryn T. Regalia
Chief Operations Officer

John W. Gobel, Sr.
Chief Benefits Officer

Members of the Board of Retirement

James A. Diepenbrock, President
Appointed by the Board of Supervisors

Keith DeVore, 1st Vice President
Elected by Miscellaneous Members

John B. Kelly, 2nd Vice President
Appointed by the Board of Supervisors

Dave Irish, Director of Finance
Ex-Officio

Winston H. Hickox
Appointed by the Board of Supervisors

Alice Jarboe
Elected by Miscellaneous Members

William D. Johnson
Elected by Safety Members

Nancy Wolford-Landers
Elected by Retired Members

Robert Woods
Appointed by the Board of Supervisors

John Conneally
Elected by Safety Members

William Cox
Elected by Retired Members

MINUTES

RETIREMENT BOARD MEETING, THURSDAY, SEPTEMBER 17, 2009

The regular meeting of the Retirement Board was held in the Sacramento County Employees' Retirement System Administrative Office, 980 9th Street, 18th Floor, Sacramento, California, on Thursday, September 17, 2009, and commenced at 1:03 p.m.

OPEN SESSION:

PUBLIC COMMENT:

1. Dolores Kattenhorn addressed the Board regarding her husband's disability retirement application.

MINUTES:

2. The Minutes of the August 20, 2009 regular meeting were approved, and the Minutes of the June 18, 2009 and July 16, 2009 regular meetings were deferred on Motion by Mr. Irish; Seconded by Mr. Woods. Motion carried (8-0).

CONSENT MATTERS:

Items 3-5

The Consent matters were acted upon as one unit upon a Motion by Mr. Kelly; Seconded by Mr. Irish. Motion carried (8-0).

3. DINKINS, Shawn: Granted a service-connected disability retirement.

CONSENT MATTERS (continued):

4. JACKSON, Daryl M.: Adopted the findings and recommendation of the referee and denied the service-connected disability retirement.
5. Received and filed the August 2009 Monthly Investment Manager Compliance Report and Watch List.

CLOSED SESSION:

LEGAL MATTERS:

6. CONFERENCE WITH LEGAL COUNSEL – ANTICIPATED LITIGATION
Government Code Section 54956.9(b)(1) and (3)(A)
Significant Exposure to Litigation: 2 potential cases

The Board consulted with counsel.

7. CONFERENCE WITH LEGAL COUNSEL – EXISTING LITIGATION
Government Code Section 54956(a)
Securities and Exchange Commission vs. WG Trading Investors, L.P., et al
U.S. District Court, Southern District of N.Y., Case No. 09CIV 1750

The Board consulted with counsel.

8. CONFERENCE WITH LEGAL COUNSEL – EXISTING LITIGATION
Government Code Section 54956(a)
Free Enterprise Fund vs. PCAOB
U.S. Supreme Court, Case No. 08-861 (Amicus)

The Board consulted with counsel.

OPEN SESSION:

ADMINISTRATIVE MATTERS:

9. Chief Executive Officer Richard Stensrud provided an update on developments affecting public retirement systems and on miscellaneous system and staff activities.

Mr. Stensrud noted that the voting period for the SCERS Board election would begin on September 21st and close on October 2nd, with the results of the election expected to be available on October 5th.

ADMINISTRATIVE MATTERS (continued):

Mr. Stensrud advised the Board that in October he would be presenting a proposed extension of the custodial banking services with State Street Bank.

Mr. Stensrud advised the Board that SCERS had been consulted regarding the retirement impact of several furlough and work schedule reduction measures being discussed by the County and certain bargaining units as a way to provide budgetary relief, while preserving jobs.

Mr. Stensrud advised the Board that a work schedule reduction was planned for the doctor who serves as SCERS medical advisor on disability applications. Mr. Stensrud reported that such a schedule reduction could cause the medical advisor to vacate the position and if so, there would be a detrimental impact on SCERS' ability to process disability applications in a timely manner. Mr. Stensrud reported that for that reason, SCERS had offered to help fund the position and thereby secure the continued services of the medical advisor. Mr. Stensrud noted that there was sufficient capacity in the SCERS budget to cover the funding needs and that specific funding for this purpose would be built into future budgets.

Mr. Stensrud provided an update on the re-initiation of the search for an internal Investment Officer.

Mr. Stensrud reported that due to the recent announcement that Chief Investment Officer Jeffrey States would be leaving SCERS to pursue another professional opportunity at the end of October, absent a strong indication to the contrary by the Board, he planned to suspend consideration of the various proposals that had been submitted in response to SCERS' Request for Proposals (RFP) for Investment Consulting Services. Mr. Stensrud explained that given the important working relationship between a Chief Investment Officer (CIO) and the investment consultant, he felt it would be prudent to defer a decision regarding the selection of the investment consultant until the new CIO was in place. The Board concurred.

10. Paul Angelo and Andy Yeung of The Segal Company presented an updated report on the impact of alternative asset smoothing periods and market value corridors on the projected future employer contribution rates and projected funded status of the retirement system. Mr. Angelo and Mr. Yeung also discussed other matters under consideration for the upcoming actuarial valuation as of June 30, 2009.

Chief Executive Officer Richard Stensrud made some introductory remarks.

Mr. Stensrud noted that the two primary actuarial parameters addressed in the Segal study are asset smoothing and market value corridors. Mr. Stensrud noted that the two parameters work in concert, but have a somewhat different impact. Mr. Stensrud explained that in setting the length of the smoothing period, the Board can affect how long it will take for employer contribution rates to transition to the new, higher level necessary to

ADMINISTRATIVE MATTERS (continued):

compensate for the investment shortfall. Mr. Stensrud further explained that in determining the appropriate market value corridors, the Board can affect whether the transition in contribution rates will occur in a relatively straight line or increase more sharply in the years immediately following the market downturn.

Mr. Stensrud noted that the purpose of the Segal study and the related materials was to assist the Board in assessing whether the modification of certain actuarial parameters would be reasonable and prudent steps with respect to the management of the retirement system. Mr. Stensrud noted that in particular, the Board would need to consider whether potential changes in the actuarial parameters would: (a) Maintain the sound funded status of the plan; (b) Fairly spread the cost of the plan across present and future stakeholders; and (c) Help manage and mitigate future employer contribution rate volatility in light of the substantial downturn in the investment markets.

In presenting the updated study, Mr. Angelo and Mr. Yeung discussed a number of topics with the Board, including:

- The principles of pension funding, including the relationship between investment earnings and contribution rates.
- The principles of asset smoothing, including the difference and relationship between the market value of assets and the actuarial value of assets, and why contribution rates are based on the 'smoothed' actuarial value of assets.
- Options to the five-year smoothing period currently utilized by SCERS and reasons why a longer smoothing period might be warranted. Those reasons included not only helping to manage the impact of the current market downturn, but also broader systemic reasons such as greater levels of market volatility than in the past and the greater impact of such volatility on plans such as SCERS that are mature, well funded, and have higher benefit levels.
- The ramifications of going to a longer smoothing period, including: (a) That the longer phase-in of losses would increase the total cost due to the time value of money; (b) Possible concerns about inter-generational cost equity; and (c) The fact that gains as well as losses will be smoothed over longer periods, thus delaying cost reductions when the market recovers.
- The principles of market value 'corridors' and how corridors impact the smoothing process.
- The ramifications of and impact of different market value corridors given the magnitude of the investment losses that will have to be smoothed due to the significant market downturn, and how the corridors utilized will be the most important determining factor on contribution rates over the next three to four years.

ADMINISTRATIVE MATTERS (continued):

- Reasons why wider corridors might be reasonable and prudent, including the fact that ‘front-loading’ cost increases could be unfair to current contributors if the market recovered and ‘bought down’ the long-term cost.
- Actuarial Standards of Practice (ASOP) No. 44, which requires that the actuary utilize an asset valuation method that is designed to produce an actuarial value of assets that bears a reasonable relationship to the corresponding market values. They explained that this means that the actuarial value of assets must fall within a reasonable range around the corresponding market value, and that any differences between the actuarial value of assets and the market value must be recognized within a reasonable period of time.
- The impact of ASOP No. 44 on the smoothing period and market value corridors that would be reasonable and prudent for SCERS.
- The assumptions about future investment experience utilized in developing the projections regarding future employer contribution rates and SCERS’ future funded status. They noted that the assumptions about future investment experience were conservative and if the future experience proved to be better, the projections would improve.
- The various graphs and charts in the analysis illustrating the projected employer contribution rates and plan funded status under different smoothing periods and market value corridors.

Mr. Angelo and Mr. Yeung noted that subject to the requirements of ASOP No. 44, selection of an asset smoothing policy and market value corridors was a matter of funding policy, with the choice of parameters dependent on the policy objectives of the Board.

In response to a question of what would be reasonable and prudent in light of SCERS’ specific circumstances and permissible under ASOP No. 44, Mr. Angelo and Mr. Yeung replied that with respect to market value corridors, given SCERS’ funding situation, it would be reasonable to allow for a more gradual transition to the ultimate contribution rate level necessary to address the recent market losses, and if so, they would recommend changing the market value corridors from 80%/120% to 70%/130%. Mr. Angelo and Mr. Yeung further noted that consistent with the objective of allowing for a longer transition time to the ultimate contribution level, it would be reasonable to consider extending the smoothing period to seven years from the current five years.

Extensive discussion followed, and it was the conclusion of the Board that changing the market value corridors to 70%/130% and the smoothing period to seven years would: (a) Maintain the sound funded status of the plan; (b) Fairly spread the cost of the plan

ADMINISTRATIVE MATTERS (continued):

across present and future stakeholders; and (c) Help manage and mitigate future employer contribution rate volatility in light of the substantial downturn in the investment markets.

Mr. Stensrud noted that in addition to consideration of the smoothing period and market value corridors, he was recommending that the Board authorize application of the \$203.9 million in the Contingency Reserve in the June 30, 2009 valuation to help mitigate the investment earnings shortfall for the year. Mr. Stensrud noted that use of the Contingency Reserve for this purpose would be consistent with SCERS' Interest Crediting and Unallocated Earnings Policy. Mr. Stensrud also noted that the projections in the Segal analysis were premised on the assumption that the Contingency Reserve would be utilized in this manner.

Discussion followed and it was the consensus of the Board that the Contingency Reserves should be applied in the June 30, 2009 valuation.

Mr. Stensrud noted that a final consideration for the June 30, 2009 valuation would be whether there should be a change in the schedule utilized to pay off the unfunded actuarial accrued liability (UAAL).

Mr. Stensrud explained that SCERS' unfunded liability is paid off via a dedicated component of the employer contribution rate, with the portion of the contribution rate dedicated to this purpose determined each year based on the current amount of unfunded liability in the system. Mr. Stensrud explained that the unfunded liability is retired over time, much like a mortgage, pursuant to an amortization schedule that declines each year. Mr. Stensrud noted that as of June 30, 2009, the amortization period would be 24 years, and scheduled to decline year by year thereafter.

Mr. Stensrud noted that the maximum period currently permitted by the Governmental Accounting Standards Board (GASB) for amortizing unfunded liability is 30 years. Mr. Stensrud explained that if SCERS were to reset the amortization period for paying off the unfunded liability back to 30 years, and restart the declining schedule, the effect would be to reduce the projected employer contribution rates set forth in the Segal analysis.

Mr. Stensrud noted that the arguments for and against making such a change would be similar to the arguments regarding changing the smoothing period or market value corridors – i.e., it would help phase-in the cost impact of the extraordinary investment experience, but it would increase total costs because the unfunded liability would be paid off over a longer period of time, raising questions of intergenerational cost equity.

Mr. Stensrud also noted that GASB is contemplating shortening the maximum amortization period to something in the neighborhood of 20-25 years and that such a change was being supported by the leading actuaries who advise public retirement systems.

ADMINISTRATIVE MATTERS (continued):

Mr. Stensrud explained that in light of these considerations, including the decision to modify the smoothing period and market value corridors, he was recommending that the amortization period for addressing UAAL not be reset for the June 30, 2009 valuation. Mr. Stensrud further noted, however, that he was recommending that The Segal Company assist the Board in assessing SCERS' UAAL policy, including whether that policy would support resetting the amortization period in future valuations.

Discussion followed and it was agreed that the amortization period would not be changed in the June 30, 2009 valuation but that SCERS' policy regarding unfunded liability would be assessed prior to the next valuation.

Motion by Mr. Johnson to (a) Adopt 70%/130% market value corridors and a seven-year smoothing period; (b) Apply the funds in the Contingency Reserve in the June 30, 2009 valuation; and (c) Continue the current amortization schedule for paying off the unfunded liability in the June 30, 2009 valuation. The Motion was seconded by Mr. Hickox. Motion carried (8-0).

11. Paul Angelo and Andy Yeung of The Segal Company presented the recommended economic actuarial assumptions for use in the June 30, 2009 actuarial valuation.

Mr. Angelo and Mr. Yeung explained that the annual actuarial valuation measures the current and projected assets and liabilities of the retirement system, as well as the system's funded status. Mr. Angelo and Mr. Yeung noted that this information forms the basis for establishing the actuary's recommendations for the employer and employee contribution rates for the upcoming fiscal year.

Mr. Angelo and Mr. Yeung explained that in determining the projected assets and liabilities, the actuary utilizes actual investment and actuarial experience to-date, plus various assumptions about the projected future growth in assets and liabilities. Mr. Angelo and Mr. Yeung noted that the actuarial assumptions include both economic and demographic assumptions, with the economic assumptions reviewed annually, and the demographic assumptions reviewed every three years.

Mr. Angelo and Mr. Yeung explained that the economic assumptions include: (a) the investment return assumption, which is comprised of the assumed inflation rate and the assumed real rate of return net of inflation; (b) the assumed system expense rate; (c) the risk adjustment; (d) the salary increase assumption, which is comprised of the assumed inflation rate, the assumed rate of real 'across the board' pay increases, and the assumed rate of promotional and merit increases; and (e) the active member payroll growth assumption, which is a combination of the inflation assumption and the 'across the board' salary increase assumption.

Mr. Angelo and Mr. Yeung explained that the extraordinary market turmoil over the last eighteen months and the substantial, ongoing efforts to return the markets to good health

ADMINISTRATIVE MATTERS (continued):

made it difficult to determine whether it was necessary to make changes to long-term economic and investment return expectations. Mr. Angelo and Mr. Yeung noted that in this regard, most of the investment consultants advising public pension funds, including SCERS' investment consultant (Mercer Investment Consulting), had not made material changes in their real rate of return projections for the next five to fifteen years.

Mr. Angelo and Mr. Yeung explained that rather than speculate as to whether the recent major, but relatively short term, market events should prompt changes to the long-term economic assumptions, The Segal Company was recommending that the economic assumptions used for the June 30, 2008 valuation continue to be utilized for purposes of the June 30, 2009 valuation. Mr. Angelo and Mr. Yeung noted that those assumptions included: (a) a 7.875% investment return assumption; (b) a 3.5% inflation assumption; (c) a 0.25% real 'across the board' pay increase assumption; and (d) a 3.75% active member payroll increase assumption.

Discussion followed.

Motion by Mr. Kelly to adopt the recommended economic assumptions; Seconded by Mr. Woods. Motion carried (8-0).

12. Chief Executive Officer Richard Stensrud presented a proposal to make certain modifications to the SCERS office lobby for the purpose of enhancing the safety features of the SCERS offices.

Mr. Stensrud noted the unfortunate reality in the world today of needing to anticipate the possibility of a situation arising in the workplace that could put an organization's staff and customers in jeopardy. Mr. Stensrud explained that while you cannot completely eliminate the chance that such a situation could arise, steps can be taken to reduce significant areas of risk without unduly compromising the look and feel of the work environment in the eyes of both the organization's staff and its customers.

Mr. Stensrud explained that to identify measures that would provide enhanced security without unduly intruding into the ambience of the workplace, staff had consulted with an architectural advisory firm and a security specialist from the County Sheriff's Department. Mr. Stensrud outlined the various considerations that went into the proposed modifications to the lobby area and presented plans and drawings illustrating the proposed modifications and how they would meet the objectives of enhanced security and pleasing aesthetics. Mr. Stensrud noted that bids had been solicited and cost of the proposed modifications would be approximately \$20,000.

Discussion followed and it was agreed that the proposed modifications to the lobby were prudent and well-designed.

ADMINISTRATIVE MATTERS (continued):

Motion by Ms. Jarboe to approve the proposed modifications to the SCERS office lobby and authorize the Chief Executive Officer to select and engage appropriate contractors to perform the necessary work; Seconded by Mr. Johnson. Motion carried (8-0).

INVESTMENT MATTERS:

13. Michael Bowman and Darin Turner of INVESCO Asset Management presented information regarding the INVESCO Mortgage Recovery Fund which had been established to participate in the federal Public-Private Investment Program (PPIP).

Mr. Bowman and Mr. Turner provided information regarding: (a) The purpose of the PPIP program and how it would operate; (b) How the PPIP program differed from the Term Asset Loan Facility (TALF) program; (c) The investments that would be made via the PPIP program and the return potential for those investments; (d) The risks associated with the PPIP investments; and (e) INVESCO's investment strategy, structure, team and process in the PPIP fund.

Substantial discussion followed regarding the various considerations in making a PPIP investment, including the continued uncertainty about the deal terms that would be imposed by the federal government.

Motion by Mr. Woods to receive and file the presentation materials; Seconded by Mr. Kelly. Motion carried (8-0).

14. Chief Investment Officer Jeffrey States presented a report on proposed amendments to the limited partnership agreement for the Hines U.S. Office Value Added Fund II, L.P. and his recommendation that SCERS not support the proposed amendments.

Mr. States outlined the investment in the real estate fund, including the problems the fund has had in investing committed capital due to the condition of the commercial real estate markets. Mr. States noted that expiration of the initial investment period for the fund was upcoming.

Mr. States described the amendments being proposed by the manager, including a proposal to extend the initial investment period and an adjustment to the amount of leverage the manager can use in the fund. Mr. States noted that the proposals had been discussed with Mercer Investment Consulting and in a conference call with other limited partners in the fund. Mr. States noted that Mercer had also conducted an on-site due diligence meeting with the manager.

Mr. States noted that performance to-date in the fund had been very poor. Mr. States further noted that the fund had not had external appraisals of the properties in the portfolio, leaving questions about the true current value of the properties. Mr. States reported that given these concerns, Mercer had recommended that SCERS not support the proposed amendments, and that this was his recommendation as well.

INVESTMENT MATTERS (continued):

Discussion followed.

Motion by Mr. Woods that SCERS not support the proposed amendments; Seconded by Mr. Johnson. Motion carried (8-0).

15. Consideration of providing additional capital to BlackRock Realty Advisors was deferred to a later date.

The meeting was adjourned at 4:23 p.m.

MEMBERS PRESENT: Keith DeVore, John Kelly, Dave Irish, Winston H. Hickox, Alice Jarboe, William D. Johnson, Robert Woods, John Conneally, and William Cox.

MEMBERS ABSENT: James A. Diepenbrock and Nancy Wolford-Landers.

OTHERS PRESENT: Richard Stensrud, Chief Executive Officer; Jeffrey W. States, Chief Investment Officer; James G. Line, General Counsel; Kathryn T. Regalia, Chief Operations Officer; John W. Gobel, Sr., Chief Benefits Officer; Suzanne Likarich, Retirement Services Manager; Julie Rucker, Senior Personnel Specialist; Diana Ruiz, Deputy County Counsel; Tom Lightvoet, Mercer Investment Consulting; Paul Angelo and Andy Young, The Segal Company; Michael Bowman and Darin Turner, INVESCO Asset Management; Kathy Malitz and Theodore Koros, BlackRock Realty; David Kimport, Nossaman LLP; Nakeyshia Kendall, The Townsend Group; Pete Albert, SEIU Local 1021; Robert Lewis, The Sacramento Bee; and Dolores Kattenhorn.

Respectfully submitted,

Richard Stensrud
Chief Executive Officer and
Secretary of the Retirement Board

APPROVED: _____
James A. Diepenbrock, President

DATE: _____

cc: Retirement Board (11); Board of Supervisors (6); County Counsel; County Executive (2); Internal Services Agency (2); County Labor Relations; Employee Organizations (20); Sacramento County Retired Employees' Association; SCERS Member Districts (10); Elected Officials (3); Superior Court of California, County of Sacramento; Amervest Company, Inc.; Mark Merin; John R. Descamp; and The Sacramento Bee.