MINUTES

MARIN COUNTY EMPLOYEES' RETIREMENT ASSOCIATION
RETIREMENT BOARD STRATEGIC WORKSHOP
Acqua Hotel, Mill Valley
September 15, 2010

---

8 – 9 A.M.
Continental Breakfast

CALL TO ORDER Committee Chair Gladstern called the meeting to order at 9:07 A.M.

ROLL CALL PRESENT: Bolger, Brenk (late arrival), Given, Gladstern, Haim (late arrival), Phillips, Richardson, Smith (late arrival), Webb (late arrival), Wofford

ABSENT: Hufford

BOARD OF RETIREMENT MATTERS

AGENDA

9 – 10:30 A.M.
Presentation Regarding System Risk Software
SF Sentry Risk Advisors

David Hansen from SF Sentry Advisors introduced Tim Holtz to review the firm's system risk evaluation software. Mr. Holtz stated that market extremes are becoming more frequent and software can provide insight to the board on managing risk. Mr. Holtz discussed risks including market-related interest rates, correlation, inflation, capitalization, geographic, industry/sector, currency, liquidity and political.

Mr. Holtz stressed the importance of awareness of portfolio exposure in a multi-manager portfolio, because diversifying across multi-managers may not provide the desired non-correlation. Holdings-based risk analysis allows for a determination of the total portfolio holdings in similar or the same assets in order to assess risk, he said.

Board Chair Jim Phillips sought and received confirmation that every holding in the portfolio would be included in the analysis. Mr. Hansen explained that the historical rate of return over time and the change in risk can be assessed. He explained that correlation analysis may allow for portfolio efficiencies.

Trustee Haim joined the meeting at 9:30 A.M., and Trustee Webb joined the meeting at 9:45 A.M.

Board Chair Phillips requested a review of the need for an analysis outside of the current investment consultant. Mr. Hansen said that an additional analysis provides an objective approach to counteract the inherent biases of investment managers and investment consultants in favor of their own recommendations and strategies. Trustee Phillips said that if the Board is interested, then the concept of third-party risk assessment can be pursued.

Chair Gladstern recessed the meeting at 10:30 A.M., reconvening at 10:45 A.M.

10:30 A.M. – 12 P.M.
Overview and New Developments in Form 700 Reporting
MCERA Conflict of Interest Code Review (<u>Action</u>)
Ashley Dunning – Manatt Phelps Phillips

Counsel Dunning presented an overview of, and discussed new developments in, Form 700 reporting requirements. Ms. Dunning focused specifically on Form 700 requirements regarding disclosure of gifts to public officials and, in some cases, their spouses. Ms. Dunning also discussed some exceptions to the gift disclosure rules. Subsequent Board discussion focused on the exception to the gift disclosure rules for educational activities, while noting that meals, accommodations and travel not paid for by the trustee, MCERA or an attendee's employer would need to be reported on the attendee's Form 700 if the items met the statutory reporting requirements of gifts. The Board also discussed the invitation-only-event rules relating to gift disclosures.

Trustee Smith joined the meeting at 11:10 A.M.

Ms. Dunning reviewed the Form 700 reporting process, such as when and where to file, and pointed out that disclosure obligations under the Conflict of Interest Code may be more narrow for certain designated employees from those stated on the Form 700, which applies to Board trustees and other statutory filers. She said that reporting requirements under the Conflict of Interest Code include employees who make or participate in making governmental decisions, as defined in regulations promulgated by the Fair Political Practices Commission. Ms. Dunning noted that pending legislation would require that those staff positions required to file a Form 700 be listed on an attachment to the Conflict of Interest Code, and that the legislation would require the Code to be posted on the public agency's website. The Trustees and Administrator Wickman discussed staff positions that may be included in the Code as "designated employees" and determined that updates to the Conflict of Interest Code should be recommended by the Administrator and counsel to the Governance Committee, who should then recommend updates to the full Board.

Chair Gladstern recessed the meeting for lunch at noon, reconvening at 1:30 P.M.

Trustee Brenk joined the meeting at 1:30 P.M.

12– 1:30 P.M.
<u>Lunch – Piatti</u>

1:30 – 2 P.M.
GASB Preliminary Views
Graham Schmidt – EFI Actuaries

Actuary Graham Schmidt of EFI Actuaries provided the Trustees with an update to proposed changes in Government Accounting Standards Board (GASB) pension accounting standards. He stated that proposed modifications to accounting standards include:

- Moving the unfunded liability to the balance sheet, instead of in notes to financial statements
- Determining the unfunded liability by using market value of assets
- Changing the calculation for determining the annual pension expense
- No major changes to discount rate, unless assets and future contributions are not expected to cover benefit payments
- Recognizing and funding ad hoc COLAs that look like permanent COLAs

Mr. Schmidt noted that the change to how annual pension expense is calculated has drawn the most attention. While current rules allow for expensing the funding contribution amount, with changes to the unfunded actuarial accrued liability amortized up to 30 years, new expense rules would shorten amortization periods to the working lifetime of active employees. Other changes to expense rules may include immediate recognition of gains/losses, or assumption and benefit changes, he said. Another proposed rule would require immediate recognition of asset gains/losses outside of a 15% corridor, he stated. Mr. Schmidt said that it is likely that funding contributions required of plan sponsors will be different from accounting expense, if the new expense calculation is considerably more volatile than under current rules.

Public hearings on these matters will occur in October.

2 – 3:30 P.M.
Interest Crediting, Excess Earnings, Reserves and Funding Policy Discussion
Graham Schmidt – EFI Actuaries
Ashley Dunning – Manatt Phelps Phillips

Administrator Jeff Wickman provided a brief introduction to the interest crediting, excess earnings, reserves and funding policy discussion.

Counsel Ashley Dunning then explained the inter-relationship of interest crediting and excess earnings under the 1937 Act, and noted that once interest crediting is accomplished and a statutory contingency reserve is funded at a minimum of 1% of the total assets of the retirement system, the balance may be deemed “excess earnings” under the 1937 Act.

Ms. Dunning said the first item in an Interest Crediting Policy should be to define "available earnings" so as to identify those funds that would be included when assessing funds available to credit interest to reserves. She noted that earnings are currently tracked by MCERA for interest crediting purposes in the three employer valuation groups that MCERA maintains: the County; the City of San Rafael; and Novato Fire Protection District.

Ms. Dunning then noted that two topics for a policy discussion on interest crediting are whether: 1) to credit all reserves with interest at the actuarially assumed rate of return, which is the current practice; or 2) to credit *up to* the assumed rate, in which case some reserves are credited with different amounts. Ms. Dunning observed that historical deficiencies in interest crediting may be tracked in a "contra" account, as was established administratively during 2009 with respect to the City of San Rafael.

Actuary Graham Schmidt stated that the purpose of such a "contra" account is to track deficiencies in funds available to credit interest. He also noted his preference that MCERA continue crediting all reserves with interest at the assumed rate of return and maintain a "contra" account to track deficiencies, as he described. The Board noted general policy agreement with this possible approach.

Ms. Dunning then discussed the 1937 Act requirement that a "contingency reserve" be maintained with a minimum of 1% of total retirement system assets prior to using excess earnings for supplemental benefits. Ms. Dunning and the Actuary recommended that MCERA's contingency reserve be treated as a non-valuation reserve in the Board's policies on this topic. There was Board discussion about the range of acceptable alternative percentages of assets to include in a non-valuation contingency reserve and the Board directed staff to include a range of 1%-5% for the Board's further discussion purposes.

Trustee Phillips was excused from the meeting at 3:13 P.M.

Ms. Dunning stated that once an interest crediting policy, including a contingency reserve approach, is developed, then the next topic is to develop an Unrestricted Earnings Policy, commonly referred to as an "excess earnings" policy. Ms. Dunning noted that one potential matter to consider in such a Policy may be to increase funding in the retiree reserves that MCERA maintains. Ms. Dunning also noted that an Unrestricted Earnings Policy could identify funding priorities, if the Board so chooses. The Board policy could also establish set funding ratios to be reached before using unrestricted earnings for supplemental benefits. Finally, Ms. Dunning observed that even if one employer valuation group maintained a statutory contingency reserve of 1%, the Board is permitted to provide supplemental benefits to retirees under the 1937 Act only if the system maintains at least 1% of *total retirement system assets*, as calculated to include all three employer valuation groups within MCERA. Thus, the Unrestricted Earnings Policy would need to address the topics it covers as to both employer valuation group, and total fund, considerations.

There was a general discussion regarding the interplay between funding policies and fiduciary responsibilities. The Board then asked counsel, the Retirement Administrator and actuary to prepare draft Interest Crediting and Unrestricted Earnings policies for its further consideration.

3:30 – 4 P.M.
Adoption of Retirement Administrator Business Objectives for FY 2010/11 (Action)

Committee Chair Gladstern reviewed the proposed business objectives for the Retirement Administrator. The Trustees discussed a minor amendment suggested by Trustee Smith.

It was M/S Smith/Gladstern to adopt the Retirement Administrator Business Objectives for FY 2010/11, as amended. The motion was approved by unanimous vote.

4 – 4:30 P.M.
Open Session

Trustee Wofford requested a review of the decision to convene the Investment Committee meetings on a different day from the regular Board meetings. She also asked whether strategic workshops should be held on site at MCERA.

In response to Trustee Wofford's second comment, Chair Gladstern explained the rationale for holding off-site workshops as providing a forum for executive staff to meet with the Board in a focused, uninterrupted, manner, to discuss important topics for the retirement system. She also noted that off-site workshops are the norm for boards that engage in strategic planning.

Trustees Smith and Given recommended consideration of alternative investments for the purpose of generating alpha. Investment Committee Chair Richardson said that it may be reasonable to research alternative investment managers. He also stated that it is important to follow spending trends in emerging markets. The Trustees agreed to discuss alternative investments at another time and with MCERA's investment consultant. Trustees also noted that the key service provider evaluation process may provide a means to obtain comments from, and provide input to, MCERA's investment consultant regarding these and other topics.

There being no further business, Chair Gladstern adjourned the meeting at 4:25 P.M.

______________________________ ______________________________

Maya Gladstern, Chair Michael Smith, Secretary