MINUTES

INVESTMENT COMMITTEE MEETING
MARIN COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

One McInnis Parkway, 1st Floor
Retirement Board Chambers
San Rafael, CA

January 10, 2013 – 9 A.M.

CALL TO ORDER Chair Richardson called the meeting to order at 9:02 A.M.

ROLL CALL PRESENT: Bolger, Brenk, Given, Gladstern, McFarland, Piombo (alternate safety) (early departure), Richardson (early departure), Shaw (ex officio alternate), Smith, Stevens, Webb (alternate retiree)

ABSENT: Cooper

A. OPEN TIME FOR PUBLIC EXPRESSION

Note: The public may also address the Committee regarding any agenda item when the Committee considers the item.

No public comment.

B. NEW BUSINESS

1. Core Real Estate Investment Manager Selection (**Action**) (TIME CERTAIN: 9:05 A.M.)

Consider and take possible action to select new core real estate investment manager

Jim Callahan, Executive Vice President of Callan Associates, presented three core real estate vehicles as potential replacements for the Cornerstone Patriot Fund: the AEW Core Property Trust, the Invesco Core Real Estate – U.S.A. Fund, and the J.P. Morgan Asset Management Strategic Property Fund. Mr. Callahan explained that core real estate is comprised of the four major property types of office, retail, industrial, and multi-family. In addition, core real estate portfolios focus on high quality, well-leased facilities in favorable geographical regions, and are modestly leveraged.

Avery Robinson, Callan Associates' Real Assets Consultant, provided an overview of the three candidates. As to structure, the AEW vehicle is a private REIT (Real Estate Investment Trust), Invesco's is a limited liability corporation, and J.P. Morgan's is a commingled vehicle. In response to Trustee Bolger's inquiry about differences in fees, Mr. Callahan stated that J.P. Morgan's fees are slightly higher but ultimately fees passed on to investors are fairly comparable. According to Mr.

Callahan another differentiating factor is the notably larger size, and longer entry queue, of the J.P. Morgan vehicle.

a. 9:05 A.M. AEW

Dave McWhorter, AEW Relationship Manager, introduced Dan Bradley, Senior Portfolio Manager of the AEW Core Property Trust (“Trust”). Mr. McWhorter stated that stability of income is the goal of the Trust, which invests in the four major property types listed above. The Trust was initiated in 2007 and has an entry queue extending to the end of the second or third quarter of 2013.

Mr. Bradley stated that the Trust invests in liquid and durable income-producing assets in bi-coastal, top-tier markets. He further stated that the overall occupancy rate is 94% and the fund is currently at 28% leverage, which is relatively high to take advantage of the low interest rate environment. The majority of assets are in the office sector and diversified across high technology, travel and entertainment, federal government, financial services, and health and education industries. Mr. Bradley emphasized the security of cash flow that is based on the strategy of retaining good tenants with long-term leases, the stability of the management team, and the strength of internal research capabilities. In response to Mr. Callahan’s inquiry, Mr. Bradley reviewed a specific tactical acquisition in an off-market transaction and discussed the strategic use of leverage.

b. 9:50 A.M. Invesco

Delia Roges, Invesco Client Advisor, introduced Max Swango, Director of Client Portfolios, who provided an overview of the history of the real estate management team. Mr. Swango introduced Bill Grubbs, Lead Core Fund Portfolio Manager, for the presentation.

Mr. Grubbs stated that the Invesco Core Real Estate – U.S.A. portfolio is the firm’s flagship real estate fund that invests in broadly diversified, high-quality assets located in top-rated metropolitan areas. Mr. Grubbs emphasized the stability of the management team, stating that there were no layoffs throughout the financial crisis and there currently is no entry queue for new investors.

Mr. Grubbs stated that the strategy is to grow income over time, with returns over the long term expected to be comprised of two-thirds income and one-third from appreciation. The investment process, he stated, involves a team-oriented approach that considers sector allocation, market selection, location, return analysis, and execution. A qualitative analysis is performed twice yearly. According to Mr. Grubbs, assets are diversified in institutional, income-oriented properties across the office, multi-family, retail, and industrial sectors. Relative to its index multi-family is overweight as outperformance is expected in this sector. Geographically assets are overweight the benchmark in the East and West regions. As of the end of September 2012, properties are 91.5% leased.

In his response to Chair Richardson's inquiry, Mr. Grubbs stated that leverage is expected to increase from the current 20% level. Trustee Brenk inquired about the health of the office market which Mr. Grubbs expects to provide steady returns over time. In responding to Ms. Bolger's comment on the 88.9% office lease rate, Mr. Grubbs addressed specific properties that he expects to be leased soon. Lagging one-year performance was attributed by Mr. Grubbs to one residential property in Seattle that has been sold. In addition, the timing of valuations of assets in New York and Washington, D.C. markets was a drag on performance.

In conclusion, Mr. Grubbs listed the Fund's advantages of no entry queue, the current attractive valuation, and the positive fundamentals of multi-family assets.

c. 10:30 A.M. J. P. Morgan

Christopher Hawkins, Client Advisor in the J.P. Morgan Asset Management Institutional Americas Group, introduced Amy Cummings, Client Investment Specialist in the Real Estate Investment Group based in San Francisco. Ms. Cummings introduced Anne Pfeiffer, Head of U.S. Real Estate Commingled Funds and Portfolio Manager of the J.P. Morgan Strategic Property Fund ("Fund"), and Kimberly Adams, Assistant Portfolio Manager of the Fund. Ms. Cummings stated that J.P. Morgan is one of the largest real estate managers in the United States. Investment decisions are consensus-based through an investment committee. In response to Trustee Bolger's inquiry, Ms. Cummings explained that the firm's asset management group is separate from the investment bank.

According to Ms. Pfeiffer, the Fund is the largest open-end commingled core real estate fund available. An advantage of the large size and scale listed by Ms. Pfeiffer is the ability to acquire high-quality assets and provide sufficient diversification to mitigate risk. The investment process is centered on discipline and patience in order to achieve expected returns. Valuations are performed quarterly by independent appraisers and performance is measured monthly. Established properties provide the bulk of income, with less than 2% devoted to developed assets. Current leverage is 23%. Geographically properties are located in primary markets on the East and West Coast, in addition to energy markets in Dallas and Houston.

Ms. Adams stressed the ability to purchase large assets in high quality markets, such as "fortress" malls, which provide strong performance throughout market cycles. Ms. Adams addressed acquisitions since the 2008 financial downturn, such as recapitalizations as other investors sought to raise capital. Current investment themes include new economies and urban infill resulting from the live-work-play demographic of the younger generation, she said.

In conclusion, Ms. Pfeiffer emphasized active asset management, tenant retention, the 93% lease rate, and favorable long term performance of the Fund. Ms. Pfeiffer responded to trustee inquiries on the investment strategy with regard to office and industrial sectors. Chair Richardson asked about the queue which is nine months out, according to Ms. Pfeiffer. Ms. Pfeiffer responded to Trustee Given's question about the relative risk associated with larger properties, stating that the economic drivers and liquidity of larger properties are favorable. Trustee Bolger inquired about Ms. Pfeiffer's plans for the future, and in response Ms. Pfeiffer addressed the importance of succession planning to provide for smooth transitions.

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Upon the conclusion of the three presentations, Chair Richardson invited discussion. Trustee Given inquired about the importance of the relative size of the properties within each portfolio. Mr. Callahan views the exposure to larger sized properties as a clear differentiator among the three core real estate candidates, and he stressed the importance of location and the long market cycle of larger properties. Trustee Smith felt that the J.P. Morgan Fund could compliment current holdings. Mr. Callahan stated that the J.P. Morgan Fund would be a safe investment that is sufficiently differentiated from the U.B.S. core real estate portfolio.

Upon Ms. Bolger's request, Mr. Robinson reviewed the fees for each portfolio. Total return comparisons were discussed among the three and the effect of timing on the AEW returns was noted. In his response to Trustee Stevens' inquiry about investing in REITs as an alternative, Mr. Callahan explained that REITs are more equity-like and therefore do not provide similar diversification as compared to the real estate asset class.

A motion by Trustee Piombo to select AEW failed for lack of a second.

Trustee Bolger expressed a preference for the J.P. Morgan Fund. Upon Trustee Smith's request, Mr. Callahan reviewed the reasoning that led to the Board's prior decision to diversify the real estate portfolio and the subsequent quest for new core real estate managers.

It was M/S Brenk/Smith to select J.P. Morgan as the new core real estate manager.

In response to Trustee Brenk's inquiry about risk to clients, Mr. Callahan compared leverage levels of each candidate portfolio and noted that if a parent firm were stressed, it could choose to divest from asset management assets. Hearing no further discussion, Chair Richardson called for the vote. The motion failed as follows:

AYES: Bolger, Brenk, Gladstern, Smith

NOES: Given, McFarland, Piombo, Richardson, Stevens

ABSTAIN: None

ABSENT: Cooper

Subsequent discussions focused on a comparison of the relative merits of the AEW and Invesco core real estate vehicles. Trustee Piombo reiterated his preference for

AEW in that it would provide balance to the relatively larger U.B.S. core real estate portfolio. AEW was characterized by Mr. Callahan as the more conservative option and preferred by Chair Richardson for the purpose of size diversification.

It was M/S Piombo/Given to select AEW as the new core real estate manager. The motion was approved as follows:

AYES:	Brenk, Given, Gladstern, McFarland, Piombo, Richardson, Stevens
NOES:	Bolger, Smith
ABSTAIN:	None
ABSENT:	Cooper

Chair Richardson recessed the meeting for lunch at 12:47 P.M.

Trustee Piombo was excused from the meeting at 12:48 P.M.

Trustee (Chair) Richardson and Trustee Shaw were excused from the meeting at 1 P.M.

The meeting was reconvened by Acting Chair Bolger at 1:18 P.M., who directed deliberations to **Agenda Item B.3**.

3. <u>RREEF America REIT III Redemption Request (**Action**)</u>
   Consider and take possible action to request redemption of RREEF America REIT III investment

   Mr. Callahan presented an analysis of recent developments at RREEF America REIT III ("RA3") which have resulted in Callan Associates' recommending that MCERA submit a redemption request to RREEF. Mr. Callahan stated that the request was appropriate given the significant modifications approved by the RREEF Independent Board to RA3 that change expectations for the portfolio. These modifications include a new fee structure with additional incentive compensation and seeking to invest in new developments which is inconsistent with the approach to have an orderly liquidation of the fund. According to Mr. Callahan the exit queue is currently less than the 40% threshold required to trigger a shareholder vote on whether to liquidate the fund.

It was M/S Given/McFarland to make a redemption request from the RREEF America REIT III. The motion was approved as follows:

AYES:	Bolger, Brenk, Given, Gladstern, McFarland, Smith, Stevens
NOES:	None

ABSTAIN: None

ABSENT: Cooper, Piombo, Richardson

Acting Chair Bolger directed deliberations to **Agenda Item B.2**.

2. Private Equity Program (**Action**) – Callan Associates
Consider and take possible action on new commitments to private equity program

Mr. Callahan presented a pacing analysis for MCERA's private equity program in order to consider further commitments that would help achieve the target allocation. Based on the analysis, Mr. Callahan recommends total new commitments of $70 million divided equally between the two private equity managers, Abbott and Pathway. As Mr. Callahan explained, the pacing analysis is based on the funding cycle commencing with initial capital commitments called by investment partners. As time goes by, distributions lower the amount of capital committed, making new commitments necessary in order to achieve the private equity target allocation of 8%.

The pacing analysis assumes five years of paying in commitments, with distributions completed over a period of seven years. In response to Trustee Stevens' inquiry, Mr. Callahan explained vintage year diversification.

It was M/S Smith/Gladstern to make new commitments to the private equity program of $70 million, divided equally between Abbott Capital Management and Pathway Capital Management.

Discussions included a review of the pacing analysis by Trustee Brenk and Trustee Smith's remarks on the value of due diligence visits to the two private equity managers. The motion was approved as follows:

AYES: Bolger, Brenk, Given, Gladstern, McFarland, Smith, Stevens

NOES: None

ABSTAIN: None

ABSENT: Cooper, Piombo, Richardson

4. Investment Manager Reporting for 2013 (**Action**)
Consider and take possible action to schedule annual portfolio reviews by investment managers at Strategic Workshops

Mr. Wickman presented a proposal to change the current practice of scheduling investment manager reports at each Investment Committee meeting. Instead, public equity and fixed income managers would report at the Spring Strategic Workshop, and alternative and real estate managers would report at the Fall Strategic Workshop.

According to Mr. Wickman, strategic work sessions are common practice among similar-sized '37 Act systems, with some also having regular reporting by each manager on a rotational schedule. Discussions included suggested structures for the presentations and Trustee Stevens' recommendation to exclude the S&P 500 Index portfolio and the securities lending program.

It was M/S Brenk/Gladstern to approve investment manager reporting at Strategic Workshops as proposed by staff.

AYES: Bolger, Brenk, Given, Gladstern, McFarland, Smith, Stevens

NOES: None

ABSTAIN: None

ABSENT: Cooper, Piombo, Richardson

5. Due Diligence (**Action**)
Consider and take possible action on investment manager due diligence site visit schedule for 2013

Mr. Wickman presented the proposed due diligence site visit schedule for 2013 that includes visits to Clifton, Dimensional Fund Advisors, and Woodmont.

It was M/S Given/Brenk to approve the 2013 due diligence visit schedule as presented.

AYES: Bolger, Brenk, Given, Gladstern, McFarland, Smith, Stevens

NOES: None

ABSTAIN: None

ABSENT: Cooper, Piombo, Richardson

6. Consider and take possible action on Amendment to Investment Policy Statement re Statements of Objectives: remove terminated managers Clarion Partners, Dodge and Cox, and RCM; add Cornerstone. (**Action**)

Uvan Tseng, Vice President for Callan Associates Fund Sponsor Consulting, presented and reviewed updates to the Investment Policy Statement as defined in Agenda Items B.6, B.7, and B.8. The Committee took action to approve the three items as shown below in Agenda Item B.8.

7. Consider and take possible action on Amendment to Investment Policy Statement re: Appendix A, Long-term Strategic Asset allocation Targets and Ranges, for adjustments to domestic equity class. (**Action**)

See action under Agenda Item B.8.

8. Consider and take possible action on Amendment to Investment Policy Statement re: add policy review period of one year. (**Action**)

It was M/S Gladstern/McFarland to approve updates to the Investment Policy Statement as submitted and documented in Agenda Items 6, 7, and 8 above.

AYES: Bolger, Brenk, Given, Gladstern, McFarland, Smith, Stevens

NOES: None

ABSTAIN: None

ABSENT: Cooper, Piombo, Richardson

C. INVESTMENT CONSULTANT QUARTERLY REPORT AND PERFORMANCE UPDATE

For quarter ending September 30, 2012

Anne Heaphy, Vice President, Callan Associates, presented the quarterly review as of September 30, 2012. For the quarter MCERA's Total Fund, valued at $1,564.0 million, returned 5.5% net of fees, ahead of the Fund's benchmark return of 4.9%, and ranking in the top decile of the Callan Public Fund Universe. Ms. Heaphy stated that the quarter was marked by positive macroeconomic factors leading to a rally in the equity markets. Contributors to performance during the quarter included domestic equity, fixed income, and real estate managers. The asset allocation effect was slightly positive during the quarter. Supporting metrics presented by Ms. Heaphy included asset class weightings, actual versus target returns, and relative attributions by asset class for the quarter and for the previous twelve months.

Ms. Heaphy presented new data in the quarterly report comparing the returns of the Eaton Vance portfolio to the CIT commingled fund. In addition, the Wellington fixed income portfolio data differentiates returns of the new core plus portfolio from the historical core fund. Finally, cash levels for each manager have been added to the quarterly report. Ms. Heaphy offered to add additional metrics to the quarterly report upon request.

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

In conclusion, Ms. Heaphy addressed the acquisition by Eaton Vance Corporation of the Clifton Group Asset Management Company ("Clifton"). As manager of the futures overlay program for MCERA, Chief Investment Officer Jack Hansen of Clifton will continue to have autonomy, she stated. The CEO of Clifton will report to Brian Langstraadt, Chief Executive Officer of Parametric (a subsidiary of Eaton Vance). However, Mr. Hansen will not have to report to David Stein, Chief Investment Officer of Parametric. The move is viewed as positive in view of the firms' similar risk control and cost management strategies. A further benefit is enhanced succession planning for

Clifton. Due to five-year contracts for key Clifton personnel, Mr. Callahan expects the transition to be stable.

D. OLD BUSINESS

None.

There being no further business, Acting Chair Bolger adjourned the meeting at 3:37 P.M.

Bernadette Bolger, Acting Chair	Attest: Jeff Wickman Retirement Administrator