MINUTES

Marin County Employees' Retirement Association (MCERA)
Retirement Board Strategic Workshop

One McInnis Parkway, First Floor
San Rafael, CA
October 27-28, 2020

This meeting was held via teleconference pursuant to Executive Order N-25-20, issued by Governor Newsom on March 12, 2020, Executive Order N-29-20, issued by Governor Newsom on March 17, 2020, and Executive Order N-35-20, issued by Governor Newsom on March 21, 2020. The public was able to listen to and observe the two-day meeting on YouTube.

Day 1
October 27, 2020

Meeting Chair Steven Block

9:00 a.m.
Call to Order/Roll Call

Chair Block called the meeting to order at 9:07 a.m.

PRESENT: Block, Cooper, Given, Gladstern, Jones (alternate retired), Klein, Murphy, Poirier (alternate safety), Silberstein, Thomas, Werby

ABSENT: Shaw (ex officio alternate)

Open Time for Public Expression

Open time for public expression, from three to five minutes per speaker, on items not on the Board Agenda. While members of the public are welcome to address the Board during this time on matters within the Board's jurisdiction, except as otherwise permitted by the Ralph M. Brown Act (Government Code Sections 54950 et seq.), no deliberation or action may be taken by the Board concerning a non-agenda item. Members of the Board may (1) briefly respond to statements made or questions posed by persons addressing the Board, (2) ask a question for clarification, or (3) provide a reference to staff for factual information.

No members of the public provided comment.

9:00 a.m. – 10:00 a.m.
2020 Experience Study Preview – Economic Assumptions
Graham Schmidt, ASA, FCA, MAAA, EA, Consulting Actuary, Cheiron
Bill Hallmark, ASA, FCA, MAAA, EA, Consulting Actuary, Cheiron

Retirement Administrator Jeff Wickman stated every three years MCERA's Actuary conducts an Experience Study to review the economic and demographic data he used to determine the cost of the Plan. This preview of the actuarial economic assumptions is being presented to the Board prior to formal adoption of economic and demographic assumptions that will be used in the Actuarial Valuation dated June 30, 2020.

Graham Schmidt, Actuary with Cheiron, presented preliminary Experience Study results and actuarial economic assumptions. Mr. Schmidt stated the Experience Study shows how price inflation, wages, and payroll are expected to grow over time. Also, post-retirement Cost of Living Adjustments (COLAs) for retirees and the expected rate of return on assets are projected. Mr. Schmidt explained that economic assumptions are based on a building block approach beginning with price inflation, currently assumed to be 2.75%. Adding the current 4.25% real rate of investment return to price inflation results in the current nominal rate of investment return of 7%. Similarly, wage growth is price inflation plus real wage growth of 0.25%, resulting in 3% wage growth, which is also the payroll growth assumption. COLA growth is set relative to COLA caps of 2%, 3% and 4%. Mr. Schmidt stated economic assumptions have to be reasonable individually and in aggregate. He introduced Bill Hallmark, Consulting Actuary with Cheiron, to discuss price inflation.

Mr. Hallmark presented data showing that average price inflation has come down since 1990. He noted that MCERA's current actuarial price inflation assumption is 2.75% and Callan's 10-year price inflation assumption is 2.25%. To project price inflation going forward, Cheiron looks at the Federal Reserve Survey of Professional Forecasters, the Horizon Survey of Investment Consultants, the U.S. Public Plan Database, and Cheiron's survey of CalAPRS member systems' assumptions. In addition, a "break-even" inflation rate based on 30-year U.S. bonds and the difference between yields on inflation-protected government securities (TIPS) versus regular government bonds are considered.

MCERA wage growth and COLA assumptions are tied to Bay Area-specific inflation, whereas the investment return assumption inflation factor is related to national data. Over the last 10 years there have been significant differences in the two values. The current price inflation assumption is reasonable from a historical perspective but is higher than most forecasters. Therefore, Cheiron will be recommending in the Experience Study that the Board reduce the price inflation assumption from 2.75% to 2.50%.

Arguments for low real wage growth include the budgetary environment and crowding out of wages due to other priorities. Arguments for positive real wage growth include relaxing of some budgetary pressures prior to COVID-19, productivity increases, higher Social Security real wage growth projections, and Bay Area wages. The Experience Study will recommend that the Board consider an increase in the real wage growth assumption from 0.25% to 0.50%, resulting in retaining the 3% wage growth assumption due to lowering the price inflation assumption.

Considerations for setting the amortization of payroll growth rate lower than the wage growth assumption are:

1. Pensionable pay for PEPRA members may not grow as much as regular members.

2. Budgetary stresses could reduce payroll growth.

3. Increases the likelihood that Unfunded Actuarial Liability (UAL) payments decline as a percentage of pay.

The Experience Study will recommend that the Board consider setting the amortization assumption for wage growth at 2.75%, 0.25% lower than the 3.00% wage growth assumption. Mr. Hallmark said this is a slightly more conservative approach to funding the Plan.

Mr. Schmidt explained how the COLA assumptions are developed. MCERA COLA groups have 2%, 3% or 4% caps depending on tier. COLAs are based on the Bay Area CPI. If the Bay Area CPI is higher than the cap, then the difference is banked for use in another year. Based on stochastic testing, the Experience Study will recommend that the Board consider changing the COLA growth rates to 1.90%, 2.40%, and 2.50% for COLA caps of 2%, 3% and 4%, respectively. Mr. Schmidt said that in a low inflation environment, average COLA growth is expected to be slightly lower than COLA cap levels.

Mr. Schmidt discussed the investment return assumption, which is currently 7.0%. Because the return on the 10-year U.S. Treasury has dropped to less than 1%, a real return of 6% or above has been needed to achieve the expected rate of return on investments. This means pension plans have had to diversify away from traditional bond investments to achieve assumed rates of return. In order to model the assumed rate of return, Cheiron collects assumptions for investment returns, risk, and correlations among asset classes from MCERA's investment consultant and models the return for the current target portfolio. Cheiron then models the return expectation of the current target portfolio using capital market expectations of a broader survey of investment consultants by Horizon Actuarial Services over 10 and 20 years. The result of modeling and averaging these data is there is an over 50% chance of achieving the current 4.25% real rate of return and a 45% chance of achieving the nominal rate of return of 7%. Using a 6.75% assumed rate of return results in a 50% or better chance of achieving the real and nominal rates of return.

Based on these results, Cheiron believes the current real return of 4.25% is reasonable, but the chance of reaching the 7.00% nominal rate of return is less than 50%. As a result, the Experience Study will recommend that the Board consider lowering investment assumption to 6.75 but maintain a real return of 4.25% by reducing the inflation assumption to 2.5%. Mr. Schmidt pointed out that the change to COLA assumptions will have a positive effect on costs for MCERA's employers who have 3% and 4% COLA's because the change assumes that benefits would grow by a lower amount. Conversely, because Marin County has mostly 2% COLA's their costs would not change because the 2% COLA cap was not being revised.

Mr. Schmidt presented a range of reasonable actuarial economic assumptions including the following recommendations:

Nominal Rate of Return:	6.75%
Price inflation:	2.50%
Real rate of return:	4.25%
Wage growth:	3.00%
Payroll growth:	2.75%

Trustee Gladstern asked how local governments' financial stress would affect payroll and wage growth. In response, Mr. Schmidt stated payroll and wage growth would be expected to come down over the short-term, but the assumptions are based on long-term projections. There should be an increase in wage growth over the long term, he said, at least equal to the inflation assumption.

Mr. Schmidt presented a Preliminary Sensitivity Analysis showing what the projected impact to employer and employee contributions rates would be if the Board adopted the changes that will be presented in the Experience Study. The projections are based on the June 30, 2019 Actuarial Valuation and will change with the adoption of the June 30, 2020 valuation. The preliminary projections showed that for Marin County the Normal Cost, which is split between the employer and employee, would increase by 1.3% and the unfunded actuarial liability (UAL) which is paid by employers would increase by 0.6% in the first year (with further increases phased in over the next two years). For Novato Fire Protection District the Normal Cost increases by 1.2% and UAL by 0.3%. For the City of San Rafael the Normal Cost increase is projected as 1.1% and the UAL as 0.3%. Mr. Schmidt reiterated that the impact on the County of Marin looks greater when in reality they are just not getting the benefit of a reduction in the COLA assumptions that employers with a 3% and 4% COLA will receive.

Mr. Schmidt presented projections of employer contribution rates and total contribution rates over time. The Actuary said the impact on the funded ratio of recommended assumptions is very little change, a drop of 1.6%. Mr. Wickman noted these economic assumptions are just projections and do not take into account potential impacts from the demographic variables that will be available in the final Experience Study report.

For Cheiron the next steps are to get feedback from the Board, proceed with demographic assumption analysis, then present the final Experience Study and recommended actuarial economic and demographic assumptions for adoption by the Board.

Trustee Werby asked if the impact on employers is to be considered when determining economic assumptions. Counsel Dunning replied that the Board's primary duty is make sure the Plan has necessary assets to timely pay promised benefits. Also, by statute the Board needs to act within the reasonable set of ranges presented by the actuary to prudently fund the Plan. The Board can consider the impact on employers to some degree, Ms. Dunning said, and here the actuary is proposing a way to prudently fund the Plan that mitigates volatility in employer contribution rates. Contribution rates should not overcharge or undercharge employers. Mr. Schmidt explained the economic assumptions are long-term assumptions and therefore Cheiron does not make big changes from year to year, but rather gradual adjustments based on experience. The impact on employers of rate volatility is also minimized on a year-to-year basis by phasing in and phasing out changes to economic assumptions.

Mr. Schmidt said he will come back in December with the recommendations on demographic assumptions. Then, early in 2021 the Actuary will provide the June 30, 2020 Actuarial Valuation based on the adopted assumptions. Trustee Klein asked if the Bay Area CPI is based on rent or other housing costs. Mr. Schmidt replied the housing factor includes a blend of expenditures. Trustee Klein asked how retiree benefits are affected if CPI comes in negative. In that case, Mr. Schmidt said benefits for retirees can go down, but not below the amount of the original retirement benefit.

Chair Block asked to see a set of actuarial economic assumptions using a 6% nominal rate for the investment return and 2% inflation. He stated he believes we are in a low interest rate and low return environment and a 6.5% investment return assumption may not be low enough. Mr.

Schmidt responded that a 2% inflation assumption is below the investment consultant's expectation and 0.75% lower than the current assumption, which would be a dramatic change. We also know, he said, that market expectations can change significantly over short periods of time. A drastic reduction in the assumed rate of return may not be in the long-term health of the Plan, the Actuary said. Counsel Dunning pointed out that the Board needs to act based on the recommendations of the actuary and to stay within the recommended ranges. The actuary will present reasonable ranges that are based on stochastic modeling.

Trustee Silberstein added that by lowering assumptions that much, contribution rates would go up, and if the assumptions are wrong, the Plan becomes overfunded. He said at that point there may be temptation to increase benefits.

Trustee Cooper asked for the Fund's historical returns – as of June 30, 2020 net fiscal year returns for the Fund are:

1 Year	3.26%
5 Year	6.61%
10 Year	9.52%
15 Year	6.72%
20 Year	5.82%
24 Year	7.18%
25 Year	7.54% (Gross Return)
30 Year	8.46% (Gross Return)

10:00 a.m. – 10:30 a.m.

Agreement with Varde to Manage Private Debt (Action)

Review and discuss agreement with Varde to manage a portion of MCERA private debt portfolio

Mr. Wickman said Varde was hired as one of three private debt managers on September 17, 2020 and the agreements to become a limited partner were completed on October 15, 2020. The Side Letter requires compliance with the Board's Conflict of Interest Code which defines MCERA investment managers as designated filers requiring that they submit a Form 700 to MCERA at the beginning of the relationship, annually, and at the end of the relationship.

Varde correctly noted that the Government Code does not require them to complete a Form 700 but instead it is MCERA's policy that requires a filing. They've indicated a willingness to evaluate the filing requirement to try to find a path forward. The Administrator said the question about filing the Form 700 has been brought to the Board because an impending capital call payment is due, but the manager has expressed reservations about the Side Letter provisions. If the Board is comfortable with our policy filing requirements, staff will continue on its present course of requiring compliance with the Conflict of Interest Code. Counsel Dunning said the decision for the Board now is whether to follow the current policy for investment managers to file Form 700 or to waive the requirement as to Varde. This is a long-standing policy that is in place for good reasons, she said. Staff is requesting direction on whether to withhold the capital call until the Form 700 is filed.

Trustee Silberstein asked what entity is filing and Counsel Dunning said Form 700 is an individual disclosure of economic interests by certain of the entities' representatives. Those individuals who are exercising discretion and judgment in terms of investments made on behalf of MCERA should file the Form 700. Trustee Silberstein asked how many individuals normally file, and Mr. Wickman said it varies according to the manager and who is making investment decisions at a particular manager. In response to Trustee Werby's inquiry, Mr. Wickman said the issue is a potential conflict of interest and to lend transparency into how the public's money is being managed. Trustee Werby asked if the contract prevents self-dealing, and Ms. Dunning replied there are representations made on that topic in the agreement that may not include everything disclosed on the Form 700. She noted that not all peer systems require investment managers to file Form 700, and Fair Political Practices Commission (FPPC) advice letters on this go both ways.

Chair Block summarized we have a covenant to make a capital call which is due prior to Varde's requirement to file Form 700. He said we should communicate to Varde that we expect them to live by the agreement and we need clarity on how Varde wants to proceed before we make any decision about the capital call. Trustees Klein, Silberstein, Gladstern, Given, Thomas and Werby were unified in supporting not making the capital call prior to confirming compliance with MCERA's policy. Trustee Klein asked about the other two private debt managers, and Mr. Wickman said we have not received communication from them on this topic as of the meeting date.

Mr. Wickman stated based on discussions staff will continue on its current course with Varde. Chair Block affirmed that direction to staff is to communicate to Varde that the Board does not intend to waive the Form 700 filing requirement with respect to this investment and the capital call will be withheld until the situation is resolved.

Chair Block recessed the meeting for a break at 10:48 a.m. and reconvened at 10:57 a.m.

10:30 a.m. – 11:30 a.m.
Derivatives and Their Use in MCERA's Portfolio
Jim Callahan, President, Callan LLC
David Zee, CFA, Senior Vice President, Global Manager Research, Callan LLC

Jim Callahan, President of Callan LLC, stated derivatives play an important role in MCERA's portfolio to manage risk and provide liquidity and are not being used in a speculative fashion. He introduced David Zee, Senior Vice President, Global Manager Research at Callan LLC, to review the use of derivatives in the Fund.

Mr. Zee defined a derivative as a synthetic financial contract deriving value from underlying instruments. Examples are futures, swaps, and options used as efficient risk management tools with very little frictional costs associated with cash securities. Derivatives are primarily used for hedging, risk management, and beta replication.

Equity index futures are exchange-traded, standardized agreements used to achieve a market beta of 1. Futures can also be sold to reduce the amount of beta in a portfolio. Equity index futures are used in the MCERA S&P 500 portfolio, BlackRock REIT portfolio, Invesco Commodities portfolio, and the Parametric Overlay Program. Interest rate futures based on U.S. Treasurys are an efficient way for fixed income managers Wellington and Western Asset to lay on duration exposures. Interest rate swaps are also used in these portfolios. Chair Block asked about Colchester's use of Over-the-Counter foreign exchange transactions which Mr. Zee said are currency forwards to gain exposure to foreign currencies. He explained a currency forward is customizable and a futures currency contract is not.

U.S. Treasury Futures Contracts are based on 2, 5, 10 or 30-year maturities and have a basket of securities that are closest to the profile of each of the key maturities. Mr. Zee stated U.S. Treasury futures trading volume makes it one of the most liquid markets in the world.

Mr. Zee explained that a futures buyer puts up initial margin through a central clearing house that pairs the trade with a seller. At the end of the day there is a zero balance between each of the parties. Chair Block pointed out the contract remains in place until the end of the quarter or it is closed out. Mr. Zee added the counterparty risk for exchange-traded futures is one day's margin.

MCERA's Commodities and Parametric Overlay portfolios are 100% derivative-based holdings. Other MCERA portfolios range from negative 5.3% to plus 4.2% exposure to derivatives. Chair Block pointed out that when cash in the Fund is overlayed, that cash is at risk. Mr. Callahan noted cash is securitized to achieve market exposure through the Parametric Overlay Program because over the long-term cash is a drag to Fund returns. Parametric adjusts exposure depending on MCERA's cash needs and does not use leverage. Chair Block asked what the most likely concern is with derivative exposure. Mr. Zee replied in his experience trading derivatives they are liquid even in extreme circumstances such as during the financial crisis. He said during the initial COVID-19 pandemic Treasury futures traded very well, which is a testament to the depth of the derivatives market. There were no failures of contracts for clearing houses and no counterparty failures. Chair Block asked if there is concern with the stability of the smaller international derivatives markets. Mr. Zee said no because the clearing members are responsible for assuring clearing house liquidity. Chair Block asked about leverage and Mr. Callahan said no MCERA managers use leverage to employ derivatives.

11:30 a.m. – 12 p.m.
Abbott Capital Management – Private Equity Review
Jonathan Roth
Ryan Green

Ryan Green, Director with Abbott Capital Management overseeing business development activities, stated Abbott focuses exclusively on private equity investments through performance-driven portfolios. Mr. Green presented historical returns showing Abbott has generated Internal Rates of Return exceeding the public equity markets over time.

Jonathan Roth, President of Abbott Capital Management, reviewed the history of MCERA's private equity program beginning in 2008. As of June 30, 2020 the ACE VI fund has a net Internal Rate of Return (IRR) of 12.2% and is expected to continue to increase in value. ACE VII has a net IRR of 16.3% enhanced by opportunistic investments early in the life of the Fund and over-allocation by Abbott. Annual Program (AP) 2016 has similar portfolio construction to ACE VII and a net IRR of 11.7%, and AP 2017 has an IRR 12.0%. In summary for the total program so far through June 30, 2020, MCERA has contributed 87% of commitments, which is currently valued at $270 million including distributions, has a Total Value to Paid-In Capital (TVPI) of 1.6 times, and a net IRR of 12.7%.

Mr. Roth discussed strategic details for the Funds. ACE VI and ACE VII strategies show the contribution of venture capital and growth equity, buyouts, special situations, and secondaries to returns. The team increased the return of ACE VII from ACE VI by investing in secondaries earlier in the life of the Fund, resulting in an IRR of 16.7% for ACE VII. Trustee Gladstern asked if the energy investments made in ACE VI were traditional or alternative energy. Mr. Roth said they included upstream, midstream, and downstream investments in traditional energy resources, including exploration, production, and distribution.

In ACE VII more exposure to information technology and health care has led to strong performance. Also, early diversified secondaries are contributing to returns. Mr. Roth discussed the particulars of successful investments that include GoodRx and CloudFlare. He noted AP 2016 is a young portfolio, with the exception of early secondaries that shortened the J-curve. He emphasized the variety of multiple investments contributing to returns that are on track for expectations. In AP 2017, the last investment made by MCERA, secondaries are generating early returns leading to an IRR of 23.7% as of June 30, 2020.

In summary, Mr. Roth said private equity has provided exposure to private companies and generated returns above the public equity market. MCERA's portfolio is now cash-flow positive as distributions continue to flow back to MCERA. Mr. Roth emphasized the importance of investing consistently over time.

Chair Block asked if each annual plan is coinvesting with the subsequent annual plan and how these are allocated. Mr. Roth replied the Portfolio Construction Committee employs a formula-driven process to determine the most appropriate account for each investment. Gary Robertson of Callan asked if the allocation is pro rata and Mr. Roth replied no, the analysis is first according to full bite and then reverts to pro rata.

Mr. Green concluded by announcing that AP 2021 was launched in July 2020 and the final close will be by March of 2021. This investment vehicle can be customized according to strategy, he said. Abbott's Select Co-investment Fund and Secondary Opportunities II, L.P are also available.

12:00 p.m. – 12:30 p.m.
Pathway Capital Management – Private Equity Review
Jim Reinhardt
Valerie Ruddick

Jim Reinhardt, Senior Managing Director with Pathway Capital Management, stated MCERA's private equity portfolio is performing well. Initiated in 2008, the Pathway Private Equity Funds are PPEF 2008, PPEF I-7, PPEF I-8 and PPEF I-9. Mr. Reinhardt said co-investments are available to MCERA. These are direct investments so that no general partner carried interest or management fees are charged. The purpose is to make progress in reducing fees.

Mr. Reinhardt said as of June 30, 2020 the private equity market has bounced back from weakness early in 2020. He noted the software sector outperformed and MCERA's weighting was 33.7% in that sector. Since inception net Internal Rates of Return (IRRs) for the Funds range from 11.1% to 17.6%. Strategies include Buyouts, Venture Capital, Special Situations, and Distressed Debt. Performance by strategy and region was presented.

Trustee Cooper was excused from the meeting at 12:30 p.m.

Valerie Ruddick, Managing Director at Pathway, stated after contributions increased in early years, since 2017 distributions are now outpacing contributions. As of June 30, 2020 MCERA has paid in 90% of committed capital and has received 72% of that capital in distributions. She highlighted the notable projected drop-off in fund market value in 2021 and subsequent years due to distributions depleting current funds and the recent lack of new commitments by MCERA.

Ms. Ruddick said most investments are in the United States or Western Europe and are diversified across industries and strategies. Recently over the past few months there have been multiple Initial Public Offerings (IPOs) representing diversified industries, and transaction activity has returned to a healthy level. Net IRRs and distributions to paid-in capital compared with public equity benchmarks show outperformance over all but one vintage year.

Chair Block recessed Open Session for a lunch break at 12:47 p.m., reconvening at 1:47 p.m.

12:45 p.m. – 1:45 p.m.
Lunch Break

1:45 p.m. – 2:30 p.m.
Private Equity Annual Review and Pacing Plan
Gary Robertson, Callan LLC

Gary Robertson, Private Equity Consultant with Callan LLC, presented the private equity annual review and pacing plan. Mr. Robertson said MCERA began the private equity program in the depth of the financial crisis which delayed the early development of the program. Since then, private equity returns have been lending stability to the Fund. Mr. Robertson stated it has been about four years since the last commitment was made, advising it is likely time to continue commitments to the program.

At mid-year the MCERA Fund value was $2.6 billion and the private equity program was about 10% of the Fund, slightly over the 8% target. Trustee Klein said with final private equity values the program was about 11.5% of the portfolio. Mr. Robertson agreed with updated private equity values, which lag by one quarter, and given custodial values are smoothed across quarters, the allocation could be about 11%. However, he noted, the amount of uncalled capital is only about $70 million, which will not sustain the 8% target allocation for private equity without additional commitments.

Callan recommends additional private equity commitments to maintain the target allocation. Based on the annual pacing plan, Mr. Robertson recommended committing $25 million to each private equity manager this year and then $30 million to each manager over the next 6 years.

Mr. Robertson presented return comparisons based on the Cambridge Private Equity Database (benchmark). Abbott and Pathway returns over the long term are similar and rank in the second quartile overall. In the year ending March 31, 2020 for the total program MCERA received $44 million in distributions and paid in $28.6 million, netting $15.4 million. The Total Value to Paid-In (TVPI) for the private equity program is 1.49 times as compared with the 1.29 median TVPI for the benchmark.

Trustee Gladstern asked about Pathway's co-investments. In response, Mr. Robertson stated when Pathway started co-investments in 2014 Callan considered it nascent until a proof of principle of their processes could be determined. Now with six years of experience it is evident that co-investments are more volatile than partnership holdings but have an attractive IRR of approximately 13%. Mr. Robertson recommended considering the co-investments.

Mr. Robertson reviewed aspects of Abbott and Pathway's new offerings. Abbott's first close for the AP 2021 Fund will be in December and will include a fee discount (a waiver of 2021 fees). Pathway has started investing in its PPEF 2021 Fund and anticipates a final close in the 4th quarter of 2020. Fees for both managers scale up and scale down. On average fees including carry interest are about 50 basis points for Abbott based on a $25 million commitment. The Pathway management fee is a bit higher resulting in a total fee including carry interest of 52 basis points.

Other options the Board could consider for the private equity program include combining the two portfolios to one manager or adding secondaries which would drive up fees. These would preclude the advantage of getting a larger allocation to good managers and Mr. Robertson does not consider these avenues to be optimal. In conclusion, he emphasized the importance of maintaining the 8% exposure to the private equity markets by making modest additional commitments to current managers based on the pacing plan.

It was M/S Gladstern/Silberstein to commit $25 million to Abbott Capital Management's AP 2021 Fund and $25 million to the Pathway Capital Management PPEF I-10 Fund to include Pathway's co-investment product.

Trustee Klein asked why we are not receiving more distributions from the older investment vehicles whose values have risen from March to June 2020 in a healthy Initial Public Offering (IPO) market. Mr. Robertson explained that IPOs are more of a financing event than a liquidity event. There is also a lockup period. Abbott and Pathway have to wait for the general partners who have discretion on when to sell and tend to time taking profits and making distributions. Trustee Klein said since the private equity program is above the target allocation now any further commitments should be delayed one year. Chair Block said co-investments would not be a good strategy because available deals may not be the best deals.

The motion was approved by a vote of 6-3 as follows:

AYES:	Given, Gladstern, Murphy, Poirier, Silberstein, Thomas
NOES:	Block, Klein, Werby
ABSTAIN:	None
ABSENT:	Cooper

2:30 p.m. – 3:00 p.m.
Private Equity Annual Fee Disclosure Review
Gary Robertson, Callan LLC

Mr. Robertson reviewed the Private Equity Annual Fee Disclosure presented in accordance with California Government Code Section 7514.7. The report is based on a template developed by the Institutional Limited Partners Association (ILPA). It provides details for fund-of-fund manager fees and expenses and for underlying partnership fees and expenses. Abbott's management fees including carried interest and expenses for 2019 were under $1.5 million. Including underlying partnership fees and expenses of under $10.2 million, the total for Abbott is $11.6 million for the year. Pathway management fees including carried interest and expenses were $1.6 million and underlying partnership fees were $11.4 million, resulting in a total of $13 million for the year. Total private equity program fees and expenses were $24.6 million for 2019. Pathway was not able to provide details for underlying partnership fees and expenses.

Trustee Gladstern asked if Mr. Robertson thinks the fee reporting has any gaps. He replied how to interpret accrued versus paid carry allocations is a consideration and the managers do not always know what the paid carry is. She asked if other states require the fee disclosure and he replied it is only California.

Trustee Silberstein observed that the total annual fees and expenses are about 10% per year of the Net Asset Value of the private equity program, meaning the investments on average yield about 25%.

It was M/S Silberstein/Thomas to adopt the Private Equity Annual Fee Disclosure. The motion was approved by a vote of 9-0 as follows:

AYES:	Block, Given, Gladstern, Klein, Murphy, Poirier, Silberstein, Thomas, Werby
NOES:	None
ABSTAIN:	None
ABSENT:	Cooper

3:00 p.m. – 3:30 p.m.
Closing and Follow-up Items from Today's Agenda

No discussion.

There being no further business, Chair Block adjourned the session at 2:47 p.m.

Day 2
October 28, 2020

9:00 a.m.
Call to Order/Roll Call

Chair Block called the meeting to order at 9:01 a.m.

PRESENT:	Block, Cooper, Given, Gladstern, Jones (alternate retired), Klein, Murphy, Poirier (alternate safety), Shaw (ex officio alternate), Silberstein, Thomas, Werby
ABSENT:	None

Open Time for Public Expression

No members of the public provided comment.

9:00 a.m. – 11:00 a.m.
Fund Governance – Developing a Process to Manage Priorities
Tom Iannucci, President, Cortex Applied Research

Tom Iannucci, President of Cortex Applied Research, presented a discussion on Policy-Focused Boards: Moving from Theory to Implementation. In his previous presentation to the Board Mr. Iannucci discussed how the most effective boards are policy-focused. He said Board members set the direction and agenda for the organization, ensure the organization is positioned to carry out its mission, set policy, manage risk, and provide oversight.

Mr. Iannucci stated the question is how a board identifies issues, deliberates, and acts in an efficient manner. He gave an example of a new board member who was enthusiastic about a new investment vehicle that many members were unfamiliar with. Eventually the matter was tabled for consideration at an undetermined future date. The question is how effective the board was in considering this recommendation, whether it had been productive, and how trustees felt about it. He said this is a common phenomenon that boards fall into when considering new issues.

According to Mr. Iannucci, successful organizations are those that can adapt to change. There is a need for constant assessment of risks and assessing which require attention. Change is essential but boards need to be cautious of making changes for the sake of change. A useful tool is to group topics into important but not urgent, important and urgent, not important and urgent, and not important and not urgent. The logic is the more time spent in the first category of important but not urgent, the less need for time spent in the others.

Mr. Iannucci outlined the following approach to managing issues as they arise:

1. Issue Identification – A periodic idea-generation session for Board and management. Consider all ideas and sort in terms of importance and urgency. Focus on important but not urgent – be prepared in advance – no decisions are made at this stage.

2. Frame the Issue and Approach – Avoid the tendency to define and solve problems at the same meeting. This allows some time for management to frame issues properly.

3. Rank the Issues – Develop consensus on the number of priorities to focus on over subsequent months. Other issues are held for future consideration.

4. Education and Analysis – The responsibility of management with support from advisors. Define terminology, confirm current practice and legal parameters, understand peer practice and major schools of thought. Then identify options, including status quo, and evaluate.

5. Decision-making.

6. Repeat process on a periodic basis.

Mr. Iannucci engaged the trustees in a discussion of the scenario he outlined about a new board member introducing a new asset class as to what went well or what went wrong. Trustee Gladstern noted the issue was not framed, nor analyzed and Chair Block agreed framing is a key step. Trustee Silberstein noted there was no education, and some board members had no knowledge of the investment instrument. Trustee Klein observed that education by an expert who was not in the industry would be advisable. Chair Block added if there is not sufficient understanding to rank an issue, education would be needed prior to ranking. Trustee Given said the real question is, when Board members have different perspectives and experience, how not to stifle ideas. Mr. Iannucci replied that by slowing the process down and making it non-threatening and routine, then more ideas can be generated.

Chair Block asked how to narrow down a list of issues. Mr. Iannucci suggested each member could submit preferred issues to management which would be divided into important but not urgent, and important and urgent. Then let management consider how to frame the issues or categorize them, and whether education on any issue is appropriate. Issues would then be ranked by priority and management will consider how best to analyze the issues.

Mr. Iannucci went into detail on the kinds of questions to be asked about an issue to further its understanding. Options, costs, and benefits are some considerations. The idea is to get a full analysis and good understanding, including presentations from advisors. Trustee Gladstern asked what happens if a motion to invest is made and there is no second due to diverse opinions. Mr. Iannucci replied it should be run through the process outlined above. Trustee Silberstein noted it could be referred to investment consultants. Chair Block asked about the initial idea generation phase, and Mr. Iannucci said there is no ranking of initial issues before management can frame the issues.

Roles and duties of board members include identifying potential policy issues or risks, making sure all issues are considered and properly analyzed, and being objective when voting on which issues are priorities. Chair Block said the framing is the most important step and asked for Mr. Wickman's view of the process outlined. Mr. Wickman replied that staff uses this process today, framing, analyzing, and providing education on issues for the Board. The Administrator said the approach we take is to try to understand the breadth and scope of any issue, if there is an education component, and who best would speak to that. Staff tries to remain neutral so that issues are addressed from a policy viewpoint. He said the idea generation process is what would be new for the Board.

In response to Chair Block's inquiry, Mr. Iannucci said once the issues have been prioritized and analyzed, the Board would be in a position to determine whether to make a change or maintain the status quo. Chair Block indicated it is the first steps that are not being done. Trustee Silberstein noted any trustee can bring up an issue at each Board meeting under trustee comments.

Mr. Iannucci suggested reviewing issues on the idea list on a regular basis. Trustee Gladstern noted the Administrator has business objectives each year. Chair Block asked how the Board Chair and staff organize ongoing agendas to respond to issues that are priorities. Mr. Wickman said those issues would be addressed during the Administrator's report. Trustee Silberstein noted some topics are properly addressed at the committee level. Trustee Thomas suggested that expectations for how new trustees can bring issues to the Board should be addressed during orientation. Mr. Wickman agreed it would be valuable to have an issue/item generation process that could be shared with trustees during orientation.

In summary, Mr. Iannucci said when everyone knows there is a process for prudent consideration of issues, there is less of a tendency to bring up the same issues continually over time. The Board will accomplish more over the long run with a disciplined process.

Trustee Silberstein was excused briefly from the meeting at 10:32 a.m.

Responding to Chair Block's inquiry on what next steps would be, Mr. Iannucci advised letting some time pass and then considering if this process makes sense. The Administrator could come back to suggest a tailored approach for this Board, he said, and there could be a Board Planning Policy that would be a guide for idea generation. Mr. Wickman said that he would like to consult with Mr. Iannucci on such a policy.

Trustee Given said he prefers Mr. Wickman to think about whether this is an efficient process to pursue before money is spent. Trustee Given noted the Board is already doing some of these processes but they are not formalized. He asked why we need help on this or whether to look at our processes as opposed to getting consultants involved.

Trustee Silberstein returned to the meeting at 10:39 a.m.

Trustee Gladstern suggested having the Governance Committee consider the matter. Trustee Silberstein recommended letting trustees know Trustee Comments is for idea generation. Counsel Dunning noted the Governance Committee would be an appropriate place to start regarding policy development. Trustee Cooper, who chairs the Governance Committee, agreed that Committee can consider the matter. Mr. Wickman agreed the Governance Committee would be a good place to tackle the question.

Chair Block said based on discussions the matter can be moved forward through the Governance Committee. He expressed appreciation to Mr. Iannucci for the presentation.

11:00 a.m. – 11:30 a.m.
Closing and Follow-up Items from Today's Agenda

Chair Block invited comments by trustees on the Workshop topics and asked for a recap on going forward with private equity. Mr. Wickman stated the Board voted yesterday to make new commitments to Abbott and Pathway of $25 million each and he has put the process in motion. Trustee Silberstein said the private equity total fees and expenses of 10% per year measured against total assets seem high. He requested a better understanding of why "2 and 20" results in 10% per year in fees, and Trustees Klein and Werby agreed. Trustee Klein also asked that Callan provide the most current data for private equity analysis. Mr. Wickman said he will share the concern on current reporting and the IRR that is being generated on current fees. Trustee Silberstein suggested having education on the CalPERS approach to in-house private equity.

Chair Block said he found Mr. Iannucci's presentation to be valuable. He indicated managing priorities could be rolled into an agenda-setting process and encouraged the Governance Committee to embrace this undertaking. Having everyone brainstorm agenda topics would be valuable, he said. Trustee Silberstein indicated workshops are a good place to rank issues.

There being no further business, Chair Block adjourned the meeting at 11:01 a.m.

Jeff Wickman, Retirement Administrator
On behalf of:

Steve Block
Ad Hoc Education Committee Chair

Michelle Hardesty, Assistant Retirement Administrator

On behalf of:
Laurie Murphy, Board Secretary