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Michael Norman
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Re: Deferred Compensation Plan Stable Value Fund

On behalf of the Board, allow me to first thank you for the continued service of Galliard Capital Management in administering the City of Los Angeles' Deferred Compensation Plan Stable Value Fund. This investment option plays an important role in the retirement savings objectives for many of our participants, and we appreciate your ongoing capable management of the Fund.

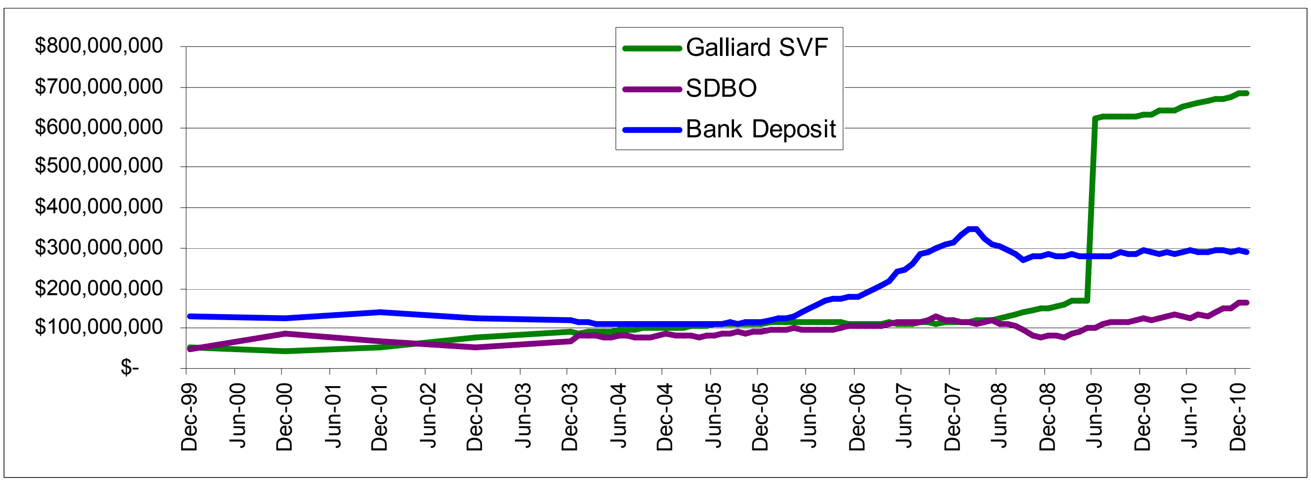
The purpose of this correspondence is to make you aware of the Board's position as it relates to what we understand is growing interest on the part of wrap providers in instituting equity wash restrictions which prohibit direct transfers to self-directed-brokerage-options (SDBOs or brokerage window) from stable value products. We understand that in your management of the fund you must secure relationships with wrap providers and believe that you are in the best position to share our concerns with the providers supporting the City's account.

In the Board's view, we do not believe there is a sound basis for extending an equity wash limitation to the City's SDBO. The theoretical objective for extending an equity wash to the brokerage window is that participants might, under certain conditions, move <u>significant amounts of assets</u> back and forth between a stable value fund and short-term, interest-bearing products offered in the SDBO in order to exploit interest rate arbitrage opportunities that may exist in a given market environment.

In our view, the salient question is not whether any given participant might attempt such a transaction, but whether this type of transaction is likely to occur on a scale significant enough to be of any consequence to wrap providers. Wrap providers bear the theoretical risk of making payments to shareholders in the event of a mass liquidation of assets from a stable value fund at a time when the fund's market value is less than book value. This, of course, represents an extreme scenario for wrap providers, when the volume of redemptions would be so great that there would not be sufficient assets in the fund to support book value payments. In practice, it appears to us that the more likely scenario is that a large participant exodus negatively impacts rates of return for remaining shareholders in the fund as assets are sold to provide book value treatment for those leaving.

Moreover, our experience with the Plan's brokerage window suggests there is little evidence to support the notion that our participants have on the aggregate shifted assets out of the stable value fund in search of better yielding short-term investment vehicles (i.e, the type of activity that an equity-wash restriction is designed to limit). In fact, there is ample evidence indicating the converse: that participant inertia is the dominating force in determining participant asset flows (or the absence thereof).

A review of our Plan's data demonstrates this very clearly. The chart below tracks participant holdings in our SDBO and the Galliard Stable Value Fund from 1999 to the present. During this period, we experienced a broad range of interest rate environments and extreme market events, including the bursting of a stock market bubble in 2000, the bursting of a real estate bubble in 2008, two bear markets, an inverted yield curve, a global financial crisis, and a historically unprecedented reduction of short-term interest rates to near zero. Nevertheless, the asset pools held within our stable value and SDBO accounts remained entirely stable. In fact, a closer review of our data indicates that over this period, stable value assets have been remarkably stable year-to-year, never registering a decline in total assets (see attachment). Asset growth in both appears to have been driven overwhelmingly by new fund flows, and what asset fluctuation did occur appears to have been due to participants' shifting assessment of risk (reducing or increasing equity exposure) rather than interest rate arbitrage. The one anomaly on this chart, the sharp increase in stable value assets which occurred in 2009, was due to the mapping of funds from a closed account.



While the Board certainly recognizes the value of maintaining stability in these assets, we do not support restrictions on our Plan participants that are not grounded in credible theory or data. We urge you to share our concerns with our existing and prospective wrap providers and ask you to work diligently to protect the current treatment of our SDBO when negotiating provider relationships.

We respectfully thank you for your consideration of our position, and thank you once again for your long partnership with the City's Plan.

Eugene K. Canzano, Chairperson
Board of Deferred Compensation Administration