CITY OF LOS ANGELES
BOARD OF DEFERRED COMPENSATION ADMINISTRATION

ADOPTED MINUTES
REGULAR MEETING OF MAY 15, 2007 – 9:00 A.M.
700 E. TEMPLE STREET, ROOM 350

Board Members:
Present:
Maggie Whelan, Chairperson
Bill Stein, Vice-Chairperson
Eugene K. Canzano
Michael Carter
Richard Kraus

Staff:

Personnel:	Maryanne Keehn, Personnel
	Steven Montagna, Personnel
	Bryan Cowitz, Personnel
	Natasha Zuvich, Personnel
	JoAnn Dominguez, Personnel
	Richard Bobb, City Attorney

1. CALL TO ORDER

Maggie Whelan called the meeting to order at 9:07 a.m.

2. PUBLIC COMMENTS

None.

3. MINUTES

A motion was made by Mike Carter, seconded by Eugene Canzano, to approve the minutes of April 17, 2007; the motion was unanimously adopted.

6. CITY ATTORNEY PRESENTATION: ETHICS

(Note: Item Taken Out of Order on Agenda)

Deputy City Attorney and Board counsel Richard Bobb provided a presentation regarding State and City ethics rules and their relationship to Board decisions to add or delete funds. Mr. Bobb began by reviewing what is required of Board members in terms of annual filing of disclosure statements. He indicated that investments over $2,000 must be reported unless a given investment was specifically excluded by statute.

He then indicated that the Deferred Compensation Plan contains certain institutional investment choices that are not technically mutual funds, and because of that they are all reportable – these choices include the Galliard Stable Value Fund, the Capital Guardian U.S. Equity Fund, the Lotsoff Small Capital Equity Fund and the State Street Russell 2000 Index Fund. He indicated that at least one California plan, the City and County of San Francisco, has eliminated its non-mutual fund investments to avoid potential ethics issues, but that this did not represent the trend of large plans because institutional pricing was generally cheaper.

With respect to conflicts of interest on voting issues, Mr. Bobb indicated that the Board was about to consider deletion of two funds, the Fidelity Magellan Fund and the Lotsoff Small-Capital Equity Fund. He stated that if any Board member owned an interest in these funds on the date a decision was made or the matter deliberated it could present a conflict of interest. As a result, he stated that the Board member should either leave the room at the time the vote was taken or else consult with him prior to a vote to determine if a conflict of interest actually existed. Mr. Bobb then indicated that ethics training would be required of all Board members and provided them information on options for taking it.

5. BOARD REPORT 07-16: FUND CONSOLIDATION/PLAN-BRANDED FUNDS

(Note: Item Taken Out of Order on Agenda)

Mr. Montagna began by indicating that this discussion represented the first of the issues that had been considered by the Investments Committee and for which fuller presentations would be provided to the full Board. He stated that the core concept involved reducing the number of options currently offered in the Plan from 23 down to 8-10 options, and then branding those options with the Plan rather than with the investment manager. He provided an example of how this might work with current City funds included in the Large-Cap asset class. He indicated that ample research existed suggesting that once a Plan offers more than approximately ten options participants tend to make poorer asset allocation decisions, so that a primary argument in favor of reducing the number of options was encouraging participants to diversify.

Mr. Montagna indicated that another argument in favor of reducing investment options was the likelihood it would substantially reduce fees. He compared the City's Plan to the City of New York's Plan, which had substantially lower investment management costs in most asset classes because it had eliminated retail mutual funds and moved to institutional products, and because the composition of the underlying portfolio included a greater weighting of passively managed money. Mr. Canzano asked why the City's costs in the bond category were so competitive with the City of New York, and Mr. Montagna replied this was likely because the City offered only two funds, with the passively managed option being fairly inexpensive and the actively-managed option also low-cost as the result of a recent bid process.

Mr. Montagna indicated that making this change would also provide the Board with greater flexibility for making changes because the underlying managers would not be obvious to Plan participants and participants would associate each investment choice with its branding with the Plan, not the investment provider. He indicated that it was the unanimous recommendation to the Investments Committee from staff, the consultant and the Plan Administrator that the Plan move towards this type of restructuring. He noted that the downside would be that some participants could be expected to react negatively, but that at least in the experience of the City of New York the participant reaction was a short-term event and not enormously disruptive.

Tom Lightvoet of Mercer Investment Consulting was present and indicated that as long as participants were educated about why the change was being made and the benefits it would provide, he did not believe any negative reaction would be severe. Mr. Stein asked if in the case of New York the Plan had experienced any increase in roll-outs from retirees once the change was made. Mr. Montagna replied he had not asked this question but could do so.

Mr. Bobb asked Mr. Lightvoet if a change of this nature could increase the Plan's fiduciary liability. Mr. Lightvoet replied that he was probably not qualified to answer that question, but that he believed the Board would have the same liability exposure as a pension fund. Mr. Montagna added that the Board already selected institutional managers and offered asset allocation funds designed by the Board, so if there were greater fiduciary obligations associated with this kind of approach the Board had likely already taken them on.

Mr. Stein asked if the Plan Administrator wished to comment. Usha Archer of Great-West Retirement Services indicated that Great-West supported this move from the perspective of how decision-making would be simplified for Plan participants, and added that she believed the Plan should also add a more robust brokerage window for its active participants. She also indicated that the County of Los Angeles had also recently adopted the same approach as the City of New York. Ms. Whelan asked about the County's experience, and Ms. Archer indicated that implementation had not yet occurred and was scheduled for 2008. Kent Morris of Great-West Retirement Services indicated that the County did not have as many funds as the City to eliminate.

Ms. De Foor suggested that the Board ask an individual from the County's Deferred Compensation Plan Board to come to one of its meetings to discuss the changes. Mr. Montagna indicated that this could be requested. Mr. Kraus asked about the potential expansion of conflict-of-interest issues if a number of funds were going to be eliminated. Mr. Lightvoet noted that in a recent legal case involving the City/County of San Diego the court had thrown out a charge that the County's retirement board was disqualified from acting because members participated in the investments. Mr. Kraus questioned whether the Board should be moving the issue ahead until it had considered all of the questions related to investment menu design. Mr. Montagna indicated that staff was not making a specific recommendation to approve the concept, only to investigate further.

A motion was then made by Bill Stein, seconded by Eugene Canzano, referring the matter back to the Investments Committee to develop a proposal for phased implementation once other investment design issues have been resolved; the motion was adopted by a vote of 4-2 (Canzano, Carter, Stein and Whelan in favor; De Foor and Kraus opposed).

7. BOARD REPORT 07-17: FIDELITY MAGELLAN & LOTSOFF SMALL CAPITAL EQUITY FUNDS

(Note: Item Taken Out of Order on Agenda)

Mr. Bobb asked whether there were Board members who wished to review with the City Attorney the question of whether they were eligible to vote on these issues. Ms. De Foor and Mr. Kraus indicated that the would need to consult with the City Attorney. In order to allow the potential for the full Board to consider the issue, **a motion was made by Eugene Canzano, seconded by Bill Stein, to defer consideration of this item until the next Board meeting; the motion was unanimously adopted.**

4. INVESTMENT PROVIDER PRESENATION: VANGUARD

(Note: Item Taken Out of Order on Agenda)

Bryan Scott and Ed McGettigan of Vanguard Investments were present to review the performance of the Vanguard Institutional Index Fund and the Vanguard Total Bond Market Index Fund. Mr. McGettigan began by providing a brief overview of the firm, its assets under management and ownership structure. He noted how Vanguard's investment management costs compared with average costs for the broad mutual fund industry. He stated that the City's holdings in the Vanguard Institutional Index Fund were now sufficient to justify a reduction in investment management fees from 0.05% to 0.025%.

Mr. Scott briefly presented the performance returns for the two funds. He noted that the information presented was fairly straightforward, in that the intent of the funds was to replicate the return of their respective indices. With respect to the Vanguard Institutional Index Fund, he indicated that the fund owned all the stocks in the index and in identical proportion to its weighting in the index. Mr. Canzano asked about adjusting to changes to the index, and Mr. Scott indicated that Standard and Poors did make changes but did not pre-announce them, so one of the challenges in running the Fund was to anticipate those changes and then to be able to react quickly once they were instituted.

With respect to the Total Bond Market Fund, Mr. Scott indicated that the Bond Fund used a sampling methodology to replicate the return of the index. Mr. Kraus asked for an explanation of the significant tracking error in 2002. Mr. Scott replied that in 2002 the volatility in the market was extreme and the Fund had experienced difficulty in adjusting to the rapid swings in gradings of the underlying bonds. However, he noted that since then the sampling process had been tightened up considerably so that the tracking error was much smaller. The presentation concluded.

8. BOARD REPORT 07-18: PLAN GOVERNANCE ORDINANCE

Bill Stein left the room during consideration of this item since his position on the Board was potentially affected. Mr. Montagna indicated that the recommendations included within its report attempted to reflect the direction given by the Board at the prior month's meeting. He indicated that the implementation dates for the ordinance were proposed to be pushed back, such that the elected positions for the LACERS and Pensions representatives would be effective July 1, 2008, and the elected positions for the DWP and Retired Participant representatives would be effective July 1, 2009. He stated that the retirement plan manager positions would begin serving on the Board July 1, 2008, but that in all other respects the ordinance would largely remain as previously written.

Mr. Montagna indicated that because of the new dates the Board would need to fill its retired representative position under the existing Administrative Code rules. Ms. Whelan noted that a selection Committee would need to be established. Ms. Whelan, Mr. Canzano and Mr. Carter all volunteered to serve on this Committee. **A motion was then made by Richard Kraus, seconded by Joya De Foor, (a) approving the change in implementation dates for pending Plan Governance changes as indicated in Board Report 07-18; (b) authorizing staff to initiate a new selection procedure for the retired representative on the Board; and (c) approving creation of an ad hoc Retired Representative Selection Committee to review candidates for the Retired Representative on the Board and provide a recommendation for selection; the motion was unanimously adopted**.

9. BOARD REPORT 07-19: NAGDCA CONFERENCE

A motion was made by Bill Stein, seconded by Eugene Canzano, approving the necessary funding for available Board members and staff to attend the 2007 NAGDCA Conference in Palm Springs, California; the motion was unanimously adopted.

10. BOARD REPORT 07-20: FEE REDUCTION &
EXPENSE REIMBURSEMENT PROPOSAL

Mr. Montagna indicated that this report provided the revised fee reduction proposal requested as a result of discussion at the prior month's Board meeting, in which the Plan Governance Committee was asked to review the City's internal costs of administration and whether the Plan was reimbursing the City for all of those costs. Mr. Montagna indicated that staff had developed data for the Committee which included all of the positions within the City servicing the Plan along with "indirect costs" calculations used by the City and DWP. He indicated that when all those costs were tallied, salary costs averaged slightly over $600,000 annually over the five-year period reviewed by the Committee. He noted that this additional expense was partially negated by the fact that the earliest implementation date of the fee reduction would afford the City's Plan two additional quarters of revenue under the current fee structure. He indicated that the net impact to the fee proposal was an increase in the fee cap to $125, with other aspects of the proposal remaining as previously presented to the Board.

Mr. Kraus asked about the assumptions used for growth in participation, and Mr. Montagna noted that the fee modeling included the impact of auto enrollment and that the Plan could still maintain a modest surplus if this were to occur. Mr. Kraus asked about revisiting the projections on a regular basis, and Mr. Montagna indicated this could be done annually. Mr. Montagna indicated that should the Board approve the new reimbursements, the changes would still need to be adopted by the City Council since the existing reimbursement structure was originally set by Council.

Following this discussion, **a motion was made by Eugene Canzano, seconded by Mike Carter, approving the expense reimbursement methodology and fee reduction proposal outlined in Report No. 07-20, and authorizing the Board Chairperson to forward a report to City Council requesting approval for changing the expense reimbursement methodology; the motion was unanimously adopted.**

11. BOARD REPORT 07-21: STAFF REPORT

Mr. Montagna presented the updates in the monthly staff report. He indicated that staff had received the mailing information and termination dates for DROP participants and was now in the process of issuing correspondence to those individuals regarding their ability to roll their funds into the City's Plan. Following some brief discussion, the report was noted as having been received and filed.

12. HARDSHIP APPLICATIONS

The Board first considered those hardship applications recommended for approval. **A motion was made by Mike Carter, seconded by Eugene Canzano, to approve a full withdrawal in Case No. 07-18 pending City Attorney verification of resolution of community property issues, and a full hardship withdrawal in Case No. 07-19; the motion was unanimously adopted.**

The Board next considered Case No. 07-15. Staff indicated that the applicant was not present and had requested that his case be deferred until a subsequent meeting. **A motion was made by Mike Carter, seconded by Eugene Canzano, to defer consideration of the case; the motion was unanimously adopted.**

The Board next considered Case No 07-17. The applicant was present. Staff indicated that the Board had previously reviewed this application but had not found a majority to either approve or deny the application. The applicant reviewed his reasons for applying with the Board, describing the investment property purchases he had entered into and how he was now in danger of losing those properties. Following discussion by Board members**, a motion was made by Mike Carter, seconded by Eugene Canzano, to approve a full withdrawal in Case No. 07-17; the motion was adopted by a vote of 5-1 (Canzano, Carter, De Foor, Kraus and Whelan in favor; Stein opposed).**

The Board next considered Case No. 07-20. The applicant was present. The applicant indicated that she had been evicted from her residence for being a few days late on her payments, but that in the past she had been allowed to be late and that the change in policy had not been previously communicated to her. Following some discussion, **a motion was made by Bill Stein, seconded by Eugene Canzano, to approve a partial withdrawal of $3,500 (net); the motion was adopted by a vote of 5-1 (Canzano, Carter, Kraus, Stein and Whelan in favor; De Foor opposed)**.

There were no appearances on Case Nos. 07-21 and 07-22. **A motion was made by Joya De Foor, seconded by Mike Carter, to deny the applications in Case Nos. 07-21 and 07-22; the motion was unanimously adopted.**

13. REQUESTS FOR FUTURE AGENDA ITEMS

None.

14. NEXT MEETING DATE – JUNE 19, 2007

15. ADJOURNMENT

The meeting adjourned at 11:33 a.m.

Minutes prepared by staff member Steven Montagna