

CITY OF LOS ANGELES  
BOARD OF DEFERRED COMPENSATION ADMINISTRATION

APPROVED MINUTES  
REGULAR MEETING OF MAY 18, 2010 – 9:00 A.M.  
700 E. TEMPLE STREET, ROOM 350

BOARD MEMBERS:

**Present:**

Eugene K. Canzano, Chairperson  
Richard Kraus, Vice-Chairperson  
Sally Choi, First Provisional Chair  
Cliff Cannon, Second Provisional Chair  
Maggie Whelan, Third Provisional Chair  
Sangeeta Bhatia  
John R. Mumma  
Michael Perez

**Not Present:**

Staff:

Personnel:           Alejandrina Basquez  
                          Steven Montagna  
                          Natasha Gameroz  
                          Claudia Guevara

City Attorney:       Anita Parys

1. CALL TO ORDER

Eugene Canzano called the meeting to order at 9:06 a.m.

2. PUBLIC COMMENTS

None.

3. MINUTES

Mr. Kraus noted several corrections to the minutes (a name correction and reference to a question he posed). **A motion was then made by Richard Kraus, seconded by John Mumma, to adopt the minutes of the 04/20/10 Board meeting, as amended; the motion was unanimously adopted.** Subsequently, and following discussion of several other items on the agenda, this agenda item was re-opened so that Sangeeta Bhatia, who was not present at the original discussion, could make several corrections

to statements she had made. **A new motion was then made by Maggie Whelan, seconded by John Mumma, to re-approve the minutes of the 04/20/10 Board meeting, as re-amended; the motion was unanimously adopted.**

#### 4. INVESTMENT PROVIDER PRESENTATION: LAZARD

Thomas Franzese, Director, and Martin Flood, Portfolio Manager, both Lazard, were present to review performance for the Lazard U.S. Midcap Equity Portfolio. Mr. Franzese began by indicating that the firm's inception was in 1848 and that it currently had \$120 billion in assets under management, 550 employees, and \$25 billion in public funds. He noted that of all its assets 13% were in U.S. Equity and \$3.5 billion in midcap stocks, with \$240 million in the strategy that the City of Los Angeles participated in.

Mr. Franzese next reviewed some of the top personnel with the firm, indicating that Ken Jacobs had taken over the prior year and was committed to keeping the firm independent. He stated that the firm's balance sheet was strong, that they were receiving strong inflows, and they had not taken any TARP money.

Mr. Flood continued with the presentation, indicating that the mid-cap strategy had a dedicated team. He stated that although the strategy had under-performed recently the fund managers believed they were moving in to a period where the markets would be more favorable to the fund's emphasis on firms with good cash-flow streams and lower levels of debt. He stated that from 2002-2009 highly leveraged firms outperformed firms with lesser debt but that a study of large-cap firms from 1964-2009 suggested this result was unsustainable. He stated that firms with larger amounts of debt typically underperformed and that more recent results were in defiance of that longer trend. He indicated that Lazard believed the market orientation was returning to an emphasis on the kind of stocks emphasized in the fund strategy.

Mr. Kraus asked if the results would also be true for mid-cap. Mr. Flood replied that the answer was yes, and that the firms included in the study captured most of the mid-cap firms. Mr. Kraus asked if mid-cap stocks have the same degree of leverage, and Mr. Flood replied that was likely the case.

Ms. Choi asked for an explanation of the fund's long-term under-performance. Mr. Flood replied that the fund's more conservative approach tended to lag in up markets but outperform in down markets. He indicated that there were three quarters in which the fund had generated most of its underperformance beginning in the second half of 2007, and this was a period of time when there was a belief that world markets had decoupled, which turned out not to be true as the credit crisis emerged. He stated that, in addition, the strategy had been hurt by four poor stock picks. He referred the Board to a review of the fund's performance in up and down markets from the period 7/1/08 through 3/31/10, indicating that the strategy had not fallen as much as its benchmark during the down period even as it lagged during the subsequent up period.

Mr. Cannon asked if Lazard was a potential TARP recipient. Mr. Franzese replied that it was but there was no need to take TARP funding given the strong balance sheet of the firm. Mr. Canzano noted the value of the fund's outperformance during a down period.

The presentation then concluded.

## 5. BOARD REPORT 10-12: INVESTMENT MANAGER PROCUREMENT

Ms. Bhatia entered the meeting during this discussion item. Mr. Montagna indicated that at the last Board meeting the Board had approved draft correspondence to the City Attorney's Office regarding a proposed revised procurement process. He stated that following that action staff met with the City Attorney's Office and, pursuant to that discussion, had developed a compromise approach which staff believed would meet the Board's objectives. He stated that, as a result, staff contacted the Board Chairperson for approval on delaying issuing the letter until the new information could be discussed by the Board.

Mr. Montagna indicated there were three three key agreements reached: (1) mutual funds would not have to demonstrate compliance with any of the City's general contracting requirements or procurement processes as part of an RFP; (2) neither mutual funds nor institutional funds would need to provide information about their products in an RFP response; and (3) an investment management RFP could be issued which would run on two tracks, with mutual funds not having to demonstrate general contracting compliance while institutional funds would need to demonstrate compliance. He stated that the details remaining to be addressed were which documents specifically would need to be provided, or which processes would need to be executed, in advance of an RFP due date, but that staff was hopeful that the list could be narrowed down considerably. He stated that once this was done staff could report back to the Board and, pending a favorable outcome, have the Board adopt the investment manager procurement process.

Mike Perez asked if there were any procurements immediately pending, and Mr. Montagna indicated there were not. Mr. Kraus asked if the Plan would still be in the same position with institutional vendors because of perceived impediments to responding to formal RFPs. Mr. Montagna indicated that this might be the case but since contracts would be required with those vendors in any event they would still need to demonstrate compliance with City general contracting provisions. Mr. Kraus suggested identifying some of the most qualified firms and encouraging their response. Ms. Choi suggested that the Board still consider the possibility of an ordinance change to address Board contracting more comprehensively. Mr. Mumma asked how the agreement with the City Attorney's Office would be codified. Mr. Montagna indicated that the City Attorney's Office might be willing to outline its position in writing, or staff could reflect the City Attorney's position in a Board report.

Following this discussion, **a motion was made by Richard Kraus, seconded by Sally Choi, to place in abeyance the Board's directive of April 20, 2010, directing the**

**Board Chairperson to issue correspondence to the City Attorney's Office regarding a proposed revised procurement process until such time as staff is able to complete further review and report back; the motion was unanimously adopted.**

## 6. BOARD REPORT 10-13: INVESTMENT MENU

Mr. Montagna began by indicating that some of the data from the consultant's report contained errors and needed correction. He indicated that Susan Dalton from Mercer Investment Consulting was in attendance and had the corrected data available and provided the Board with two options: distribute the corrected handouts and then proceed with a Board discussion or delay discussion until the next Board meeting. Ms. Dalton indicated the errors were the result of some incorrect correlations but that the output was not substantively different with the exception of reported tracking error. Mr. Perez suggested allowing Mercer to present and delaying a decision only if the Board determined that was necessary. Mr. Canzano agreed.

Mr. Montagna stated that Board Report 10-13 was a continuance from the April Board discussion of the redesign of the Plan's core investment menu. He referred the Board to the status of decisions regarding the core menu on the Mercer report. He stated that decisions regarding Mid-Cap, Small-Cap, and International funds were still pending.

Ms. Dalton then began her presentation. She indicated that within core fixed income and large cap equity it was difficult for active managers to outperform, but that in the categories to be discussed by the Board Mercer believed its A-rated active managers could add value. She stated Mercer's recommendation was therefore to include an active management component in all three categories.

Mr. Kraus asked whether active manager performance in each category was indicated on a collective basis, or was Mercer just considering one or two funds. Ms. Dalton replied that Mercer was including all of its A-rated funds. She stated that one of the benefits of a fund-to-fund approach was that the Board could replace a fund manager at will. Mr. Kraus indicated that the mid cap value category had apparently not added value and questioned whether this should impact the Board's decision of including a value component in the blended fund. Ms. Dalton replied that this was a concern and Mercer could review the data. Mr. Perez asked whether Mercer had conducted a similar analysis for international markets. Ms. Dalton responded that Mercer had not looked at international performance in this same context but could do so. Mr. Perez asked if there was any data documenting the performance of small or large companies for international funds. Ms. Dalton replied that she did not have this kind of data and since there were fewer international managers it would be more difficult to obtain it.

Mr. Kraus indicated that although the A-managers as a group exhibited outperformance, the Board could still only select one fund. Mr. Montagna indicated that this discussion had arisen during the Investment Committee meetings, and the Board should be mindful of the limitations of the fund selection process, which required that funds be selected

during periods of outperformance, at which point they were more likely to subsequently underperform, and then the limitations of fund elimination policies, which required that eliminations only occur after long periods of underperformance. Mr. Canzano replied that he struggled with this concern as well and that, in light of that, he would be in favor of looking at the implications of moving to a model with 50% active and 50% passive class management.

Ms. Choi indicated that no fund is ever in the top quartile all the time and as a result the Board needs to rely upon the process recommended by the consultant. Mr. Perez replied that managers have a tendency to revert to the mean and the Board must have a good process for not just hiring but also terminating fund managers. He asked for staff's recommendation. Mr. Montagna indicated that as previously discussed in the Investment Committee meeting staff would place a greater weight on the passively managed components. Mr. Canzano asked the other Board members if there was any compelling reason to not go completely passive. Mr. Kraus indicated he would like to obtain charts comparing performance of growth, value and passive managements to determine if actively managed mid-cap value could outperform the market in a way that may not have been seen in the total mid cap space. He added that a bar graph might also help to better visualize the options available. Ms. Dalton indicated that the case for active managers outperforming in the mid-cap space was not as compelling as it was for small-cap and international markets, but Mercer believed there were still opportunities to achieve out-performance.

Board members next discussed the small-cap asset class. Mr. Perez indicated he was comfortable with Mercer's recommendation for this asset class. Mr. Canzano indicated he would be willing to entertain a motion. **A motion was then made by Mike Perez, seconded by Sally Choi, approving replacement of the Plan's current Small-Cap investment fund with a new "DCP Small-Cap Stock Fund" which would be 34% comprised of a passively managed small-cap index fund, 33% comprised of active growth management, and 33% composed of active value management; the motion was unanimously adopted.**

The Board next discussed international stocks. Ms. Dalton indicated that the United States represented approximately 50% of world equity markets. She indicated that Mercer was recommending that the Board benchmark this option to the MSCI ACWI index, which excluded the United States but included emerging markets. She added that Mercer had considered a separate emerging market fund stand-alone option, but that doing so might lead to participants chasing returns. She indicated that Mercer's recommendation was to have a blended option with one third index, one third value, and one third growth blend. Mr. Mumma asked where he might find the growth and value charts for international stocks, and Ms. Dalton replied that this information was not included in the booklet. Mr. Kraus asked if it was more likely that emerging markets would be considered in the growth or value asset class. Ms. Dalton responded that the emerging markets would more likely represent a growth asset class. Mr. Montagna suggested that staff and Mercer develop an alternative model for the international option which would set specific targets for sector weightings rather than being tied to growth

and value management, and return at the next Board meeting with information on this fund category as well as additional data on the mid-cap fund.

#### 7. BOARD REPORT 10-14: DEFERRED COMPENSATION PLAN ANNUAL REPORT

Natasha Gameroz presented the proposed 2009 Deferred Compensation Plan Annual Report. She briefly reviewed each page of the report, indicating highlights from the text and charts presented. Mr. Kraus asked if the report could be posted online, and Ms. Gameroz indicated it could be posted on the Plan-level website. Mr. Kraus asked if the Board member page should include the current members or those members from 2009. Mr. Montagna replied that the report was a communication from the Board to elected officials so it was appropriate to have it transmitted from the current Board.

Mr. Kraus asked if the change from OptionsPlus to Charles Schwab should be noted, and Ms. Gameroz replied the change had occurred in 2008. He asked if reference should be made to the fact that the Plan was operating with fewer staff. Ms. Whelan indicated she didn't feel it was advisable to reference a point like that in this type of report. Mr. Kraus questioned whether the participation rate reflected the fact that employees could be Plan members but not currently contributing, and Mr. Montagna indicated identifying a more reliable participation rate was on staff's project list. Ms. Bhatia requested a change to the report in reference to the appropriate name of the DWP Retirement Plan. She also asked if the asset allocation funds referred to the Profile Funds, and staff indicated they did.

Following this discussion, **a motion was made by Richard Kraus, seconded by Cliff Cannon, approving the 2009 Annual Report as amended; the motion was unanimously adopted.**

#### 8. BOARD REPORT 10-15: NAGDCA CONFERENCE AND PLAN ADMINISTRATOR ON-SITE

Mr. Montagna indicated staff was recommending approval for funding for the 2010 NAGDCA Conference. He stated that staff was further recommending funding approval for sending a number of individuals to conduct a Plan Administrator on-site review at Great-West headquarters, and that this be approached as a long-term rotating educational opportunity. Mr. Perez indicated there might be problems regarding the Great-West on-site visit as a result of only allowing three Board Members to attend and having contact with an existing contractor that the other Board members did not have. Mr. Perez then exited the meeting.

Ms. Choi indicated her agreement with Mr. Perez and believed the on-site visit would be appropriate for staff as part of a due diligence exercise but not for Board members. Mr. Canzano asked for a response from the City Attorney. Ms. Parys indicated she could review the matter. Mr. Cannon indicated he was leaning towards the concerns expressed by Mr. Perez and Ms. Choi. Ms. Bhatia asked when the current contract with Great-West would expire. Mr. Montagna replied that it expired at the end of 2011 but

that the process of developing the RFP would be initiated the following month. Mr. Kraus suggested having staff attend the on-site visit and then have Great-West produce highlights of the information at the following Board meeting. Mr. Montagna indicated that if there were concerns regarding the appropriateness of an on-site visit to the Plan administrator so close to the point of initiating RFP development, that perhaps approval on this even for staff only should wait pending a response from the Board's legal counsel.

Mr. Mumma asked whether the on-site visit with Great-West was considered an educational opportunity. Mr. Montagna replied affirmatively. Mr. Mumma indicated additional training beyond the NAGDCA Conference would be valuable for the Board members. Mr. Cannon agreed. Mr. Canzano asked if a proposal for more training could be developed. Mr. Montagna replied that a training policy was one of the pieces of draft bylaws developed by staff for which additional consideration by the Plan Governance & Administrative Committee was still pending. Mr. Kraus asked if it was possible to have guest speakers attend the Board meeting. Mr. Montagna indicated that staff had been thinking along these lines and had made arrangements for Marilyn Collister of Great-West to attend the August Board meeting to provide a primer on fiduciary issues. Ms. Choi indicated she could send invitations to other Board members regarding attending LACERS trainings. Ms. Archer of Great-West indicated that Marilyn Collister would also be providing a further training session following the August Board meeting. Mr. Kraus asked whether Mr. Montagna could inquire about training opportunities when he attended the Sacramento meeting of other large California plans. Mr. Montagna responded affirmatively.

Following this discussion, **a motion was made by Ms. Choi, seconded by Mr. Kraus, to approve the necessary funding for available Board members and professional staff to attend the 2010 NAGDCA conference in Philadelphia, Pennsylvania; the motion was unanimously adopted.**

## 9. GREAT-WEST QUARTERLY REPORT

Ms. Archer presented the Deferred Compensation Plan report for the first quarter of 2010. Ms. Archer noted that Plan assets were at \$2.9 billion. She stated that Stable Value Fund assets were at \$650 Million and FDIC insured assets at \$300 Million, with additional large sums in the Vanguard Institutional Index and Hartford Capital Appreciation Funds. She indicated that the number of contributing employees had fallen 3% in the first quarter of 2010 with bi-weekly contributions decreasing 10%. She stated that overall participation was at 61% which continued to be an exceptional number given that the County of Los Angeles had a participation rate only 6% higher, at 67%, but with an employer match.

Ms. Archer indicated that in terms of cash flows the largest increase was to the pre-mixed asset allocation funds, and that the average account balance for the first quarter 2010 was slightly over \$72,000. She then indicated Mr. Robison would cover local account activity.

Mr. Robison indicated that Great-West had seen an increase of 26% in participant contact in comparison to the first quarter of 2009. He indicated the vast majority of questions have involved the topic of distributions. He added that Great-West still provides Early Retirement Incentive Program informational seminars and continues to provide table service to City employees, and continues to hold many meetings at the Department of Water and Power. Following this discussion, **a motion was made by Mr. Cannon, seconded by Mr. Kraus, to receive and file the report; the motion was unanimously adopted.**

#### 10. BOARD REPORT 10-16: STAFF REPORT

Mr. Montagna indicated that staff had changed the format of the report to include more ongoing data regarding participant services activity as well as a more comprehensive outline of staff projects. He indicated that the type of project tracking format utilized in the report was identical to an internal tracking system that had been used by staff for some time, and that this information was being provided in order to provide more transparency and accountability.

#### 10. REQUESTS FOR FUTURE AGENDA ITEMS

Mr. Canzano indicated that he was aware that a fee war was occurring amongst several brokerage firms with respect to exchange-traded-funds, and he asked if staff could verify whether a reduction on these types of trades applied to participants with Charles Schwab. He further thanked staff for the work done in assembling the meeting packages each month.

#### 11. NEXT MEETING DATE – JUNE 15, 2010

#### 12. ADJOURNMENT

**A motion was made by Sangeeta Bhatia, seconded by Maggie Whelan, to adjourn the meeting; the motion was unanimously adopted.** The meeting adjourned at 11:59 a.m.