CITY OF LOS ANGELES
BOARD OF DEFERRED COMPENSATION ADMINISTRATION

MINUTES
MEETING OF AUGUST 16, 2005 – 9:00 A.M.
700 E. TEMPLE, ROOM 350

Board Members:
Present:
Shelley Smith, Chairperson
Joya De Foor, Vice-Chairperson
Don Keith
Richard Kraus
Bill Stein
Maggie Whelan

Staff:

Personnel:	Maryanne Keehn, Personnel
	Steven Montagna, Personnel
	Fernando Campos, Personnel
	JoAnn Dominguez, Personnel
	Richard Bobb, City Attorney

1. CALL TO ORDER

The Chairperson called the meeting to order at 9:04 a.m.

2. PUBLIC COMMENTS

John Hill of the Department of Water and Power (DWP) stated that he first wanted to compliment Shelley Smith on the assistance she had provided to him regarding obtaining information about the Los Angeles City Employees Retirement System's (LACERS) Larger Annuity Program. Mr. Hill indicated that currently City employees can roll Deferred Compensation funds over to this program but that DWP does not have such a program. Mr. Hill indicated he had made contacts with his union and Department management regarding this matter but thus far had not received any definite response. He asked if the Board could take an action in support of instituting a similar DWP program.

Ms. Smith indicated that the Larger Annuity Program had been in existence for some time but that Communications staff within LACERS had recently begun more pro-active outreach to acquaint its membership with the benefits of the program. She asked staff and the City Attorney to examine Mr. Hill's request and explore what, if any, options were available to the Board.

3. MINUTES

Steven Montagna indicated that he had received some corrections of errors from Mr. Kraus and, in the interest of limiting confusion with respect to amendments to the minutes, had made those corrections, noted them and distributed them to Board members. Ms. Smith stated that, given that information, she would ask staff to resubmit the revised minutes for approval at the next meeting.

4. INVESTMENT PROVIDER PRESENTATION: VANGUARD INVESTMENTS

Ed McGettigan, Relationship Manager, and Michael Fleming, Investment Analyst, both with the Vanguard Group, were present to review performance data for the Vanguard Institutional Index Fund and Vanguard Total Bond Market Index Fund offerings within the City's Deferred Compensation Plan. Mr. McGettigan began by asking if the Board preferred that he go through the company overview or move directly to performance review. Mr. Keith indicated that he would like the company overview, so Ms. Smith asked him to proceed with that.

Mr. McGettigan began by reviewing the mission statement for the firm, indicating that Vanguard's objective is to provide top quality investment management consistent with reasonable costs. He indicated that Vanguard has a unique ownership structure in that fund shareholders are also corporate owners. He indicated that the firm traced its ownership back to the Wellington Fund established in 1929 and established itself as the Vanguard Group in 1975. The firm's focus was on providing services on an at-cost basis, noting that in 2004 the average expense ratio for Vanguard was 23 basis points vs. 135 basis points for all other funds.

He noted that most of Vanguard's funds are managed in-house with approximately one-third of assets under outside management. He briefly referred the Board to the breakout of assets under management included in the presentation booklet as well as a list of investment managers affiliated with the company.

Mr. McGettigan then indicated that the City Plan's holdings with Vanguard had grown to $226 million, with the balance in the Vanguard Institutional Index having risen to $176 million. He stated that once the holdings in that fund reached $200 million the expense ratio would drop from the current five basis points to two and a half basis points.

Mr. Fleming spoke next, beginning by stating that both Vanguard Funds offered by the City had been able to meet their objective by tightly tracking their benchmarks during the various time periods indicated in the report. He said that Vanguard was able to achieve this tight tracking as a result of its low-cost fee structure.

Turning specifically to the Vanguard Institutional Index Fund, he stated that the Fund through the S&P 500 Index represented approximately 75% of the U.S. stock market, including a combination of both growth and value stocks, with the remaining 25% concentrated in small-capitalization stocks. He indicated that the Fund was currently run by Don Butler, replacing Gus Sauter who had since promoted within the company. He stated that the Fund currently holds 506 stocks and referred the Board to the breakout of holdings indicated on page 12 of the report.

Discussing next the performance of the Fund relative to its peer group, he indicated that over various time periods the Fund had out-performed 98% or higher of its peers, and in fact over a 10-year time period had outperformed 100% of its peers. Ms. Smith commented that if one believed in the concept of efficient markets and low cost competitiveness, then this would be an appropriate Fund to hold.

Mr. Fleming next discussed the Vanguard Total Bond Market Index Fund. He stated the Fund is based on the Lehman Aggregate Bond Index and had an average duration of 4.2 years. He indicated the fund holds approximately 1,700 issues. With respect to performance, the Fund over most time period outperformed approximately two-thirds of its peers.

He drew the Board's attention to the three-year time period comparison which showed that the Fund had outperformed only 46% of its peers, noting that some distortions in tracking had occurred during 2002 as a result of some of the financial upheavals created by stocks like Enron and Worldcom. Ms. Smith asked if in connection with this Vanguard was participating in any litigation related to recovery of funds, and Mr. Fleming replied that although the firm was not a litigant it had an internal group that was working to recover any funds possible.

Ms. De Foor asked if the Fund had any limitation on its exposure to foreign markets. Mr. Fleming responded that the Fund had minimal exposure and only to the extent that the Lehman Brothers index upon which it was based did so. Ms. Smith commented that given the growing popularity of asset allocation funds within the City's Plan it was likely that over the next five years the Plan would see increases in total bond assets.

5. BOARD REPORT 05-26: REQUEST FOR PROPOSAL-PLAN INVESTMENTS

Mr. Montagna indicated that he had made some corrections to errors on the RFP and outlined them for the Board's review. Ms. Smith asked staff to review the changes with the Board members. Mr. Montagna indicated that on Page 5 a repeated paragraph had been deleted and one of the text boxes moved forward a page with two funds added. Mr. Kraus indicated that there still appeared to be funds missing from the other text box, and staff indicated this would be corrected.

Next, Mr. Montagna indicated that page 9 had been modified to replace the reference to "Committee" with the reference to "City," and that on page 14 new questions 45 and 46 were added regarding expense caps and front-end sales loads to be consistent with the questions asked for the other investment category. Mr. Montagna stated that page 18 the Standard Deviation and Sharpe ratio had been added. Mr.Kraus indicated that it appeared Information Ratio had also been added. Staff acknowledged that this appeared to be the case, indicating that Mercer had revised this section. Finally, staff indicated that on page 20 a new section header entitled “Additional Questions” had been added to make clear that those questions applied to all respondents, not only to those proposing Mid-Cap Funds.

Mr. Kraus asked if the questionnaire could also ask proposers about fee rebates, and Mr. Montagna indicated this question had been expanded on page 14 to ask about that. Ms. Smith noticed that the question numbering appeared to be off on this page and Mr. Montagna indicated this would be corrected as well. Mr. Stein indicated he had a change on page 34, changing the word “evolutions” to “evaluations.”

Ms. De Foor indicated her concern regarding a particular minimum qualification, specifically the one stipulating that a vendor’s proposed fund should contain no more than 20% of foreign holdings. Ms. Whelan asked if an issue like this should really be addressed as a policy issue concerning all the Plan’s funds. Ms. Smith indicated that it might be difficult to do that across the Board with all the fund offerings in the Plan. Ms. De Foor stated that her point was that this was simply a policy issue the Board might wish to consider.

Ms. De Foor indicated she had a further concern about the Mid-Cap Fund minimum asset threshold being set at only $250 million. Ms. Smith responded that her feeling was that this was a minimum and that it would be better to define a broader playing field within reason, and the Board could then decide once all the proposals were received what specific product it would offer. Ms. De Foor indicated she would then just like to note for the record her objection that the $250 million threshold was too low.

Mr. Stein asked whether staff was comfortable with the number of rating sub-factors, and Mr. Montagna indicated that most of these weightings had come from Mercer based on their development of the technical segment of the RFP questionnaire. Ms. De Foor then asked about the fee weighting and indicated her preference that the RFP be structured so as to evaluate the responses based on the other factors first, without regard to fees, and then conduct a fee review. Mr. Montagna indicated that in the scoring of proposals all of the response data would be fully transparent, so that it would be possible to identify proposals which might have scored marginally on services but excelled with respect to fees, or the reverse. Ms. Smith indicated that she felt it was appropriate to look at both fees and services together. Mr. Keith indicated his thought that performance returns are the most important factor and fees impact performance returns. Ms. De Foor then stated that she wished to go on record with her preference for conducting a services analysis before a fee analysis.

Following this discussion, **a motion was made by Richard Kraus, seconded by Bill Stein, approving the revised draft Request for Proposal for a Core Bond and a**

Core Mid-Cap investment fund for the City's Deferred Compensation Plan; the motion was unanimously adopted.

6. BOARD REPORT 05-27: TASK FORCE RECOMMENDATIONS/UPDATE

Mr. Montagna indicated the Administrative Issues Task Force has met over the last couple of months to discuss the development of a participant survey. Mr. Montagna indicated the main focus of the task force was to develop the best survey possible, keeping in mind the timeline in respect to reporting back to City Council. Mr. Montagna provided a project calendar to illustrate possible survey release dates. The project calendar was used for discussion purposes only and was not intended to commit to an exact release date.

Mr. Montagna continued by discussing three task force concerns. First, identifying the best method for pre-survey notifications to plan participants. Second, requesting a news bulletin from the Board of Deferred Compensation Administration informing plan participants of the survey and the purpose of the survey. Mr. Montagna indicated the need to clearly state that the Board of Deferred Compensation Administration is conducting the survey and not Great-West Retirement Services. Third, timing to complete the survey and issuance of future RFP. Mr. Montagna further indicated that staff would like to complete the survey by the end of calendar year 2005 and issue the RFP by mid-year in 2006.

Mr. Montagna indicated that the survey dates are meant to provide an optimistic estimate of when the survey may be released. Mr. Montagna informed the Board of other obstacles that may add additional time to the survey process, such as the Board may not want to act based on the task force recommendations, internal and/or external mail time processing, and future modifications to the survey process. Mr. Montagna requested approval from the Board to start drafting the survey and the use of Mercer Consulting.

Mr. Kraus asked if the City Council reported on Mercer Consulting contract extension. Mr. Montagna replied that staff did not have to report to City Council because the contract term, with the extension, does not exceed three years. Ms. Whelan acknowledged that the project calendar dates were optimistic and she would like to get the process started.

Ms. Smith asked if pre-survey notifications were cost-effective. Mr. Montagna replied that it all depends on the type of communication method elected. Mr. Kraus asked if staff could post the pre-survey notification on the plan's web-site and if participants will be given the option to download a printable version of the survey. Mr. Montagna replied that staff could post survey information on the web-site. Mr. Montagna introduced Mr. Jason Jaross from Mercer Consulting to reply to the question regarding printable version of the survey.

Mr. Jaross assisted in answering questions from the Board. Mr. Jaross indicated that mailing is more of a cost-benefit and a scanable survey would provide an easier method to tally the results. Ms. Whelan asked if there is a way to number each survey. Mr. Jaross replied there was not. Mr. Jaross concluded by indicating that pre-survey notifications are the driver to response rates.

Mr. Stein asked about the existing contract term with Mercer and could a prolonged survey process cause a gap in services provided by the firm. Mr. Montagna indicated that the goal is to have a selected vendor before the expiration of the current vendor. Mr. Stein asked if the survey process is slowed-down and the consultant is needed for additional time, do we need to increase their contract authority. Mr. Montagna indicated that he would ask City Attorney's for other options if the Plan was faced with that situation.

Mr. Kraus asked about the progress of the Plan Governance Task Force and if the Task Force would conduct a similar survey as the Administrative Issues Task Force. Mr. Montagna indicated that the Plan Governance Task Force would not conduct a survey and that the task force has met once in the last couple of months. Mr. Kraus suggested that staff could provide additional training sessions for the Board with respect to some of the information acquired by the Task Forces, and staff indicated this could be done.

Ms. Smith indicated that she wished to state for the record that her husband's prior employer's 401(k) plan at one time owned equities in the parent holding company of Mercer, although those holdings had all been liquidated in 2004. Ms. Smith inquired of the City Attorney as to whether a recusal on the matter would be appropriate. Richard Bobb of the City's Attorney advised that that he did not believe a recusal was legally necessary. However, Ms. Smith then indicated that out of an abundance of caution she would be recusing herself from voting on this matter. Ms. Smith left the Board meeting room. Following this discussion, **a motion was made by Richard Kraus, seconded by Bill Stein, approving the recommendation of the Administrative Issues Task Force that the Board authorize the Plan consultant to begin initial work on development of a survey for review/refinement by the Task Force and eventual submission to the Board; the motion was unanimously adopted**.

7. NEXT MEETING DATE: OCTOBER 18, 2005

8. ADJOURNMENT

A motion was made by Maggie Whelan, seconded by Don Keith, to adjourn the meeting; the motion was unanimously adopted and the meeting adjourned at 10:45 a.m.

* Minutes prepared by Staff member Steven Montagna & Fernando Campos