

BOARD OF DEFERRED
COMPENSATION
ADMINISTRATION

MARGARET WHELAN
CHAIRPERSON

BILL STEIN
VICE-CHAIRPERSON

--
EUGENE CANZANO
JOYA C. DE FOOR
MIKE CARTER
RICHARD KRAUS
RICK ROGERS

DEFERRED COMPENSATION PLAN BOARD REPORT 07-35



Date: September 12, 2007

To: Board of Deferred Compensation Administration

From: Staff

Subject: Capital Guardian Contract & Core Large-Cap Fund Offering

Recommendation:

That the Board of Deferred Compensation Administration (a) authorize staff to request, and the Board Chairperson to execute, a one-year contract extension for the Capital Guardian U.S. Equity Fund; or (b) eliminate the Capital Guardian U.S. Equity Fund from the City's Plan based on recent fund under-performance or in the interest of reducing redundancy in the Plan's large-cap investment offerings.

Discussion:

The Capital Guardian U.S. Equity Fund is the Deferred Compensation Plan's "Core" large-cap fund. The reference to "Core" means that the investment manager was selected by a prior Board as a result of a formal Request for Proposal (RFP) process and was intended to represent the City's "Core," or primary, Actively-Run Large-Cap investment option.

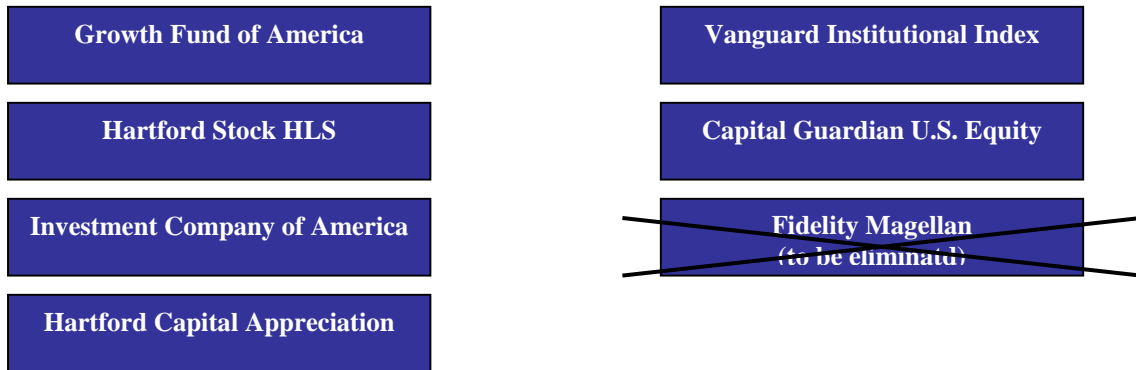
The Capital Guardian fund is offered as a separate account and thus the City has a direct contractual relationship with the provider. The contract with the provider expires on April 29th, 2008.

As Board members are aware from prior consultant performance reviews, this Fund has been on Performance Watch for the first and second quarters of 2007. Pursuant to the Board's investment policy, if the Fund were to continue to be on Watch for two additional quarters the Board would need to eliminate it from the Plan; the Board also has the discretion to act before the full four quarters have elapsed, as it did with the Fidelity Magellan and Lotsoff Capital Management Funds.

The Board has previously endorsed, in general terms, several of the investment menu redesign concepts developed by staff and the Investments Committee, including consolidation of Plan investment options and reducing redundancy in the investment menu. However, the Investments Committee has not yet developed a formal proposal

for instituting all of the elements of the proposed redesign, including fund consolidation, fund re-branding, etc.

Currently there are seven large-cap funds offered in the City's Plan. The Board has already made a decision to eliminate the Fidelity Magellan Fund. The current Large-Cap funds are listed as follows:



Because the current contract with Capital Guardian will expire next year, some action must be taken by the Board regarding this Fund. The Board has several options:

- (1) Issue a Request for Proposal (RFP) for a large-cap fund manager, allowing Capital Guardian to compete to retain its position in the Plan;
- (2) Terminate the Capital Guardian Fund at the end of the current contract;
- (3) Temporarily extend the Capital Guardian contract (by securing City Council authorization to do so) to provide additional time to determine whether the Fund should be eliminated based on the terms of the Board's investment policy.

With respect to Option 1, staff does not recommend that the Board issue a new RFP. Although Capital Guardian theoretically represents the Plan's "core" large-cap offering, given the redundancy in the Plan's large-cap offerings it makes little sense to initiate a selection process to add yet another fund in this category. Based on the fact that the Fund is presently on Performance Watch, it is also unlikely that it would be competitive in a new selection process and would thus need to be eliminated on that basis anyway.

Staff would support Option 2. The Board's decision to eliminate one of the Plan's investment options should certainly not be based on the timing of a terminating contract. However, it is within the Board's discretion to make a decision to eliminate based either on fund under-performance or in the interest of investment menu consolidation. It should be noted that if the Board were to act immediately, there would be insufficient time to afford the customary six months of advance notice of fund closure following issuance of the next quarterly statements - the notice period would rather be approximately three months.

Staff would also support Option 3 if the Board is not prepared at this point to make a long-term decision regarding this Fund. If the Board took Option 3, staff would recommend a one-year contract extension. This would provide additional time to

determine if the Fund should be eliminated pursuant either to extended under-performance or in the interest of consolidating the Plan's investment options.

Submitted by: _____
Steven Montagna

Approved by: _____
Maryanne Keehn