

Patti's Notes: (as she understood the meeting)  
SDCERS INVESTMENT COMMITTEE MAY 17, 2007

#### NEW CITY HALL AS SDCERS INVESTMENT?

Tom Hebrank had heard most recently about SDCERS being asked to invest in a new City Hall and he asked for clarification and an expanded explanation of why such a loan to the City would be prohibited.

Chris Waddell said SDCERS could participate if the terms were the same as other commercial investments, and added that he believed the loan would be limited to 25% of the total project (according to IRS limitations?). It appears that the City Charter limits SDCERS to investing via asset managers and not direct investment as determined by the SDCERS Board. Chris concluded by asking why would SDCERS want an investment manager to buy City of San Diego bonds on the market?

Doug McCalla, SDCERS Chief Investment Officer, argued that SDCERS is already a creditor to the City and this puts us in a bad place to take on a debtor's paper. He also said that it does not make sense to do a tax-exempt loan when SDCERS does not pay taxes. He added that such an investment would drive down returns to SDCERS and result in an increase to the City's annual contribution to SDCERS. (SDCERS has averaged 11% return this year from July to April 2007. Would City bonds pay that much?)

Dawne Clark, Doug's assistant, said the City would rather pay off generally issued bonds, than pay SDCERS.  
SDCERS will research more on this area of investment.

#### DOUG MCCALLA'S INVESTMENT POLICY REVISION

The revised policy gives "corporate memory" to why and how the current investment structure is designed. (page 4 of draft)

Footnote on page 16 of draft: "Beneficiaries are probably better served if governing fiduciaries see themselves as risk managers, not investment managers. Boards manage risk; management adds value."

Appendix A of draft: Risk is controlled by "re-balancing" types of investments, managing risk, and including the risk of insufficient returns to pay retirees. (Need 90% level of probability of meeting projected liabilities over 20 years.)

Doug said that if the funded ratio was 120% then SDCERS could go to less expensive passive management and decrease risk. In the meantime, active managers take on the risk of losing investments.

Fortitude Risk: Patience, judgement and fortitude to support long-term policies and strategies.

Diversification: Combining assets that are not perfectly correlated with each other. Weighed against costs, liquidity, complexity, communication, expertise, knowledge and effort.

A list of investments of money managers was attached to Doug's policy revision, saving

staff time for requests of this information.

#### HOW MUCH DELEGATION TO PRIVATE EQUITY?

Board discussed no longer delegating approval of contracts to SDCERS staff and is considering to have the Board vote on contracts as "Best Practice" like other Boards do.

Callan, the consultant to help select asset managers, was thinking about SDCERS building up Private Equity when he said the more complex the pension plan, the more he recommended delegation of interviewing, policy, etc. Chris Waddell pointed out that the Board is still responsible, whether they delegate or not. Hebrank said the Investment Committee was open to dialogue on the delegating, but the current process of interviewing asset managers, etc. was not unmanageable. Steve Meyer added that authority can be delegated, not responsibility. Murray referred to Peter Q. Davis advice to "challenge, just don't lend stock" owned by SDCERS without asking the borrower the right questions that guard the security of SDCERS' stock. Discussion will continue in the future.

*Notes taken by CSDREA board member Patricia Karnes*