The Board of Retirement met in regular session at 8:30 a.m. on Wednesday, February 25, 2004, in the Conference Room of the Contra Costa County Employees' Retirement Association, 1355 Willow Way, Suite 221, Concord, CA.

Present: Richard Cabral, John Gioia, Brian Hast, Paul Katz, Louis, Kroll, William J. Pollacek, Bob Rey, Helen Shea, Maria Theresa Viramontes, and Clifton Wedington

Staff: Pat Wiegert, Retirement Administrator; Marilyn Leedom, Assistant Retirement Administrator; Rick Koehler, Retirement Accounting Manager; Toni Warren, Retirement Administration Manager.

Outside Professional Support:	Representing:
Bob Helliesen	Milliman, USA
Ashley Dunning	Steefel, Levitt & Weiss
Paul Angelo	Segal Company
John Monroe	Segal Company

Other Attendees:

Joelle Luhn	CCCERA Staff
Luz Casas	CCCERA Staff
Tom Bush	CCCERA Staff
Dave Gaynor	Self
Jerry Telles	Retiree Support Group
Fernando Hernandez	Capital Guardian
Anita Brar	Capital Guardian
Keith Beaudoin	Northern Trust
Bob Nissen	Sonoma County
Arlyn Endman	Local One
Kris Hunt	Contra Costa Taxpayers Assoc.
John Sweeten	County Administrators Office
Richard Soderholm	Self
John Noble	DSA
Joan Woods	San Ramon Valley Fire
Tony Enea	County Administrators Office
Anthony Dehaesus	Self

1. **Public Comments**

No members of the public offered public comment.

Leedom introduced the new Information Technology Project Manager, Tom Bush.

2. **Approval of Minutes**

After discussion, it was M/S/C to approve the minutes of the February 11, 2004 meeting. (Yes: Cabral, Hast, Katz, Pollacek, Rey, Shea, Viramontes, Wedington)

3. **Review of Total Portfolio Performance**

Milliman USA – Bob Helliesen
Helliesen noted that the fourth quarter 2003 domestic equities markets experienced strong returns. The S&P 500 index was up 12.2% for the quarter and the Russell 2000 small capitalization index was up 14.5%.

The median total fund returned 7.6% and the median public fund returned 8.1% in the fourth quarter. CCCERA's return of 8.6% is above the median total fund and the median public fund. Our portfolio has out-performed both medians over longer periods.

CCCERA's domestic equities returned 12.6%, above 12.2% for the S&P 500 and 12.2% for the median equity manager. Helliesen noted that Dreyfus performed best with a return of 18.8%, compared to the Russell 2000 return of 14.5%, while Emerald returned 14.5% versus 12.7% for the Russell 2000 Growth index. Rothschild was up 14.1% for the quarter, below 16.4% for the Russell 2000 Value index. Among larger capitalization managers, Boston returned 14.0%, above 12.2% for the S&P 500, while PIMCO and Intech returned 12.5% and 12.4% respectively, slightly above the S&P 500. ING Aeltus and Wentworth Hauser both trailed the S&P 500 with returns of 11.5% and 10.5%, respectively. Alliance's portfolio was transitioned to a State Street Russell 1000 Growth Index during the fourth quarter.

For the fourth quarter, CCCERA's total international equities returned 15.7%, below 17.1% for the MSCI EAFE Index and slightly above 15.6% for the median international equity manager. Capital Guardian's developed market portfolio return of 15.2% was below MSCI EAFE and the median manager. The GDP-weighted EAFE index product managed by Northern Trust returned 16.6%, trailing 17.6% for the GDP-weighted MSCI EAFE Index. The Capital Guardian emerging market portfolio returned 14.8% versus 17.8% for the MSCI Emerging Market Free Index.

The total domestic fixed income returned 1.3% for the fourth quarter, above 0.3% for the Lehman Aggregate and 0.5% for the median fixed income manager. Western Asset Management's return of 1.2% is above the Lehman Aggregate and median, while PIMCO returned 0.8%, also above the benchmarks. AFL-CIO's return of 0.4% is above the Lehman Aggregate but below the fixed income median. Fountain Capital and Nicholas Applegate returned 4.4% and 4.8%, respectively, trailing 6.4% for the Salomon High Yield Index. Over longer periods, CCCERA's total fixed income has outperformed the median and the Aggregate.

FFTW's international hedged fixed income portfolio returned 0.8% for the fourth quarter, above 0.0% for the Salomon Non US Government Hedged Index.

The median real estate manager returned 2.5% for the quarter. Total real estate returned 6.8%, well above the median. Hearthstone's Fund II returned 19.2% and Hearthstone's Fund I was up 11.0%; Lend Lease Rosen's REIT portfolio returned 9.6%; Prudential SPF-II returned 3.4%; US Realty was up 3.0%; DLJ's RECP II was up 2.4%; FFCA returned 2.1%; WP Carey returned 2.0%; DLJ's RECP I returned 1.7%; and the Willows Office property returned 1.8%.

PruTimber reported a return of 1.3%, Adams Street Partners' private equity portfolio reported a return of 2.4%; and Pathway reported a return of 0.2% for the quarter.

There was discussion of placing Fountain Capital on the watch list. Helliesen noted that their Morgan Stanley High Yield benchmark may not be appropriate given the manager's investment style. He intends to study the matter further and will return with a recommendation on the appropriate benchmark. It was the consensus of the Board to consider the consultant's recommended benchmark before considering placing Fountain Capital Management under review for performance.

Discussion continued on the difficulty in establishing performance measures for alternative investments and whether exposure to international fixed income could be achieved by allowing our domestic fixed income managers this flexibility.

4. <u>Manager Presentations</u>

a. <u>Capital Guardian Trust</u> – Fernando Hernandez, Anita Brar
Hernandez began by noting that Capital Guardian has been one of CCCERA's managers for over fifteen years.

Brar reviewed last year's performance, noting that equity markets were very strong for the year with double-digit returns. The non-U.S. market out performed the U.S. market by 29%. The U.S. dollar weakened against most other currencies and lower quality did better than higher quality companies.

She noted that stock selection and overweighting in materials and health care helped performance in the fourth quarter, while stock selection in information technology, financials and consumer discretionary securities hurt their results.

<u>Emerging Markets Growth Fund</u>
Brar then reviewed the Emerging Markets Growth Fund for the fourth quarter 2003. Declining interest rates, solid corporate earnings, a recovering global economy and market-friendly outcomes in several elections helped emerging markets stock rise nearly 18% in the quarter to bring the annual gain to more than 55%. Energy, materials, industrials and consumer discretionary stocks outperformed, while those in technology and health care lagged.

She noted the portfolio benefited from the strong bull market in emerging market stocks. Overweight positions in Brazil and India, two of the best-performing major markets, helped relative returns. Strong stock selection in Russia also helped. The portfolio was underexposed to China and South Africa, hurting the relative returns. The overweight in Mexico was also a negative factor.

Cabral and Hast were not present for subsequent discussion and voting.

b. **Northern Trust** – Keith Beaudoin
Beaudoin began by reviewing portfolio performance as opposed to the EAFE Regional GDP Index, and the differences between a capitalization weighted index and a GDP-weighted index. GDP weighting addresses the issue of economic importance by weighting countries by their gross domestic product. GDP is a relatively uniform measure across all developed countries.

Hast was present for subsequent discussion and voting.

After a review of the portfolio's characteristics and top ten holdings, Beaudoin explained how Northern Trust's regional funds are constructed and the flexibility that investors have in using this strategy to construct their own regional allocations.

Kroll was not present for subsequent discussion and voting.

5. Consultant's Update

a. Paladin Capital Management
Helliesen reviewed the biographies for the management team in the Paladin Home Security Fund. He noted he received three names of competitor firms from Adams Street. Of those three, it appears that only one firm, Dunrath, is similar to Paladin.

When questioned why Adams or Pathway didn't include this type of fund in their portfolio, Helliesen noted that neither one saw this type of fund as a fit within their overall investment strategy.

It was the consensus of the Board that the consultant proceed with collecting more information on Dunrath and return with results in May or June.

Kroll and Cabral were present for subsequent discussion and voting.

This was followed by general discussion on the Board's past policy of using fund-of-funds managers such as Pathway and Adams Street to invest in private equity or other alternative investments. Helliesen suggested that the Board revisit this policy in light of its recent manager hires. In response to a suggestion that the Board retain a second consultant who specializes in alternative investments, Helliesen offered to check within the Milliman organization to see if there is someone who might have more expertise in this area. This issue will be discussed further at a future meeting.

b. Asset Allocation Study

Helliesen reported that the process will begin after the actuarial valuation is completed and information from that study can be used in conducting the asset allocation study.

6. New Asset Allocation Targets

Helliesen reviewed his proposed target revisions noting that they adjust for the additions of Relational and Clarion Mortgage. It was M/S/C to adopt the asset targets as recommended by the consultant. (Yes: Cabral, Hast, Katz, Pollacek, Rey, Shea, Viramontes, Wedington)

7. Portfolio Rebalancing

Leedom reviewed her report on rebalancing of the portfolio based on December 31, 2003 asset values. It was M/S/C to accept the recommendations of staff to rebalance the portfolio as proposed and according to policy.

8. Retirement Administrator Search

Bob Nissen, Retirement Administrator for Sonoma County discussed what a Board should consider when searching for an administrator. He shared the recent steps his Board had taken to replace their retiring Administrator.

Nissen reviewed Sonoma's history, noting that they became independent from the Treasurer's office in 1998 and he was Sonoma's first Retirement Administrator. Sonoma's Board had a succession plan in place for five-years which fell apart two years ago when the Assistant Administrator was offered another job.

Shortly after the second Assistant Retirement Administrator was hired, Nissen had a family emergency giving his Assistant a chance to work in the capacity of the Administrator for a period of time.

Nissen felt it is important for the Board to see how the individual will work with the Board and to observe critical thinking. He felt the skill sets needed include managerial tools, relations with others, and a sense of humor.

The Board thanked Nissen for his comments and the opportunity to ask questions.

LUNCH BREAK

Shea was not present for subsequent discussion and voting.

AFTERNOON SESSION

Gioia was present for subsequent discussion and voting.

9. Valuation, December 31, 2003

John Sweeten, County Administrator, noted that the decision made over the assumptions would have significant ramifications on the County budget. In a letter which he distributed, he asked that the Board delay taking action to allow the County and other employers more time to review the implications.

Angelo began by reviewing the four economic actuarial assumptions and how their recommendations are determined. He summarized their recommendations:

- Inflation – decrease from 4.25% to 4.00%.
- Investment Return – decrease from 8.00% to 7.75%.
- Salary increases – decrease from 4.25% to 4.00% (inflation); continue no "across the board" increases; merit and promotion: will be included in the non-economic assumption report.
- Terminal Pay - will be included in the non-economic assumption report.

In response to questions, Angelo noted that the investment return assumptions of many systems have been lowered recently but it would not be imprudent if the Board chose to leave its existing economic assumptions unchanged.

There was discussion on reviewing the non-economic assumption before making decisions on economic assumptions and on keeping the current assumptions for another year. It was M/S to maintain the current economic assumptions in light of the dramatic drop in the investment return assumption in recent years and in anticipation of the impact on rates once the Board is asked to adopt changes in non-economic assumptions after the Experience Analysis is completed.

After further discussion, **the second was withdrawn from the motion.** It was M/S/C to adopt the assumptions as recommended but with a 7.9% Investment Return assumption. (Yes: Gioia, Hast, Katz, Kroll, Pollacek, Rey, Viramontes, Wedington; No: Cabral)

Kroll and Wedington were not present for subsequent discussion and voting.

10. Triennial Experience Analysis Process

Angelo reviewed the process used for the Triennial Experience Analysis noting that he will be proceeding differently for this analysis and will use a simpler model. He reviewed the significant changes that have occurred in the last three years and noted certain procedures that he will eliminate. He will, however, focus on special items: the percentage of members who remarry, sick leave conversion rates and terminal pay.

11. Policy for Accessibility of Investment Records

It was M/S/C to approve the letter to be sent to CCCERA's investment managers seeking their input on the proposed Policy for Accessibility of Investment Records. (Yes: Cabral, Gioia, Hast, Katz, Pollacek, Rey, Viramontes)

Kroll and Wedington were present for subsequent discussion and voting.

12. Miscellaneous

(a) There were no requests for counsel opinions.

(b) Wiegert reported the DVDs of the Spring and Fall SACRS Conferences were now available in the library. Karen Krieger, our medical advisor, has accepted a position with Merrill Lynch and will be leaving as of April 1, 2004. Staff will be returning to the Health Services Department to seek a replacement.

(c) Trustee Comments – Viramontes and Wedington reported on their on-site visit with Fidelity. They noted no deficiencies and felt very confident with the firm. A report will be completed early next week on the visit.

Pollacek commented that the on-site visit with Relational Investors will be on March 16th.

(d) Consultants Comments – None.

CLOSED SESSION

13. The Board went into closed session under Gov. Code Section 54957 to evaluate the performance of the Assistant Retirement Administrator and to consider her possible appointment as Retirement Administrator.

OPEN SESSION

14. Replacing the Retirement Administrator

It was M/S to offer Leedom the appointment to replace the Retirement Administrator upon her retirement.

A substitute motion was offered: it was M/S to initiate a national search to replace the Retirement Administrator and to invite Leedom to participate as a candidate in the search. (Yes: Cabral, Gioia, Rey, Viramontes; No: Katz, Kroll, Hast, Wedington, Pollacek) **The motion failed.**

The original motion carried. (Yes: Hast, Katz, Kroll, Pollacek, Rey, Wedington; Abs: Gioia, Cabral, Viramontes)

Katz announced that the Board will need to discuss the terms of Leedom's compensation package as Administrator after which he, Pollacek and Hast will meet with Leedom.

The board members who abstained from the previous vote noted they did so only because of the process involved. They expressed their full support and confidence in Leedom.

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Paul Katz, Chairman Clifton Wedington, Secretary