

San Mateo County Employees' Retirement Association
Minutes of the Investment Committee

October 23, 2000 – Investment Committee Agenda

PUBLIC SESSION – The Committee will meet in Public Session at 2:30 p.m.

- 1.0 Call to Order
- 2.0 Roll Call
- 3.0 Approval of the Minutes
- 4.0 Oral Communications from the Committee
- 5.0 Oral Communications from the Public
- 6.1 Acceptance of a Report Updating *SamCERA's* Benchmark Modification Policy with Respect to Investments in the Tobacco Industry
- 6.2 Approval of *SamCERA's Investment Plan*
- 6.3 Approval of Topics for an Investment Manager Review – Bank of Ireland Asset Management
- 6.4 Approval of Topics for a Global Custodian Review – State Street Bank & Trust
- 6.5 Preparation for an Investment Manager Review – Barclays Global Investors
- 6.6 Approval of Revisions to the Monthly Portfolio Performance Report
- 6.7 Approval of Revisions to the Gray & Company Quarterly Performance Report
- 7.0 Other Business
- 8.0 Adjournment

MINUTES OF SAMCERA'S Investment Committee

- 1.0 Call to Order** Ms. Colson called the Public Session of the Investment Committee to order at 2:30 p.m., October 23, 2000, in *SamCERA's* Board Room, Suite 280, 702 Marshall Street, Redwood City.
- 2.0 Roll Call** Mr. Bryan, Mr. Buffington, Ms. Colson, and Mr. Cottle (2:33). *Board Members in Attendance:* Mr. Hoffman, Sgt. Hoffman *Alternate Board Member in Attendance:* None. *Staff:* Mr. Clifton and Mr. McCausland. *Consultant:* Mr. Anderson *Retirees:* None
- 3.0 Approval of the Minutes** Ms. Colson requested a motion approving the minutes of September 25, 2000.

Motion by Bryan, second by Buffington, to approve the Minutes of September 25, 2000 as amended. The motion carried unanimously.

Ms. Colson turned the meeting over to Mr. Cottle who arrived during the approval of the minutes.

- 4.0 Oral Communications from the Committee** None
- 5.0 Oral Communications from the Public** None
- 6.1 Acceptance of a Report Updating *SamCERA's* Benchmark Modification Policy with Respect to Investments in the Tobacco Industry.**

Mr. Clifton asked the Chair to address items 6.6 & 6.7 as the first two items on the agenda. Mr. Alfred Chu of State Street Bank and Trust (SSB) rearranged his schedule on short

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notice to address the Committee's concerns regarding the performance reports. He has a prior commitment later this afternoon. There being no objection the Chair moved to Item 6.6.

6.6 Approval of Revisions to the Monthly Portfolio Performance Report.

Mr. Clifton reviewed the manager reconciliation matrix, which was developed to highlight differences between the custodian and investment manager calculations of portfolio performance. The September 30th report draws attention to the inception to date return for the BGI Russell 2000 Index Fund. The reconciliation points out that BGI calculates the inception to date return 3.78% higher than State Street. The discrepancy results from the use of different inception dates. State Street and Gray & Company use June 1 while BGI uses May 31st. The use of different dates is because on May 31st BGI acquired equal weightings of the Russell 2000 Value and Growth then transitioned those assets into the Russell 2000 on June 1. BGI assures *SamCERA* that the growth and value components are the same as the Russell 2000 and argue that the inception date should be May 31st. Staff reported the consultant and custodian captured all returns. State Street captured the May 31st return of the Russell Value and Growth in the Transition Account. Mr. Cottle questioned if SSB should be instructed to reallocate the return to the BGI Russell 2000 rather than the Transition Account to conform to BGI's Calculation. Mr. Chu responded that a conversation with BGI was scheduled for the following day with the intent to discuss that very issue. • Ms. Colson asked Mr. Chu what is an acceptable difference between the custodian and manager calculations. His response was that a typical client accepts a difference of 15 basis points (bp) on an international portfolio and 10 bp on a domestic portfolio over a twelve-month period. • Mr. Cottle led a discussion regarding the absence of a Domestic Equity Aggregate. Mr. Chu told the Committee that Watson Wyatt had not provided the requisite monthly data to perform an aggregate calculation. Mr. Anderson confirmed that Gray & Company also needed the monthly market values from Watson Wyatt to calculate their returns. Mr. McCausland will contact Watson Wyatt requesting the monthly data. • The Committee endorsed the visual presentation of the Plan's historic asset allocation, which appears on the final page of the monthly report.

Action: The Committee instructed staff to solicit the monthly aggregates from Watson Wyatt and provide them to Gray & Company and State Street Bank & Trust. The Committee accepted the report as presented.

6.7 Approval of Revisions to the Gray & Company Quarterly Performance Report.

Ms. Colson reported that she and Mr. Anderson worked on Gray & Company's Quarterly Performance Report. Mr. Anderson added that half of Ms. Colson's comments have been incorporated and his firm is working on the remaining issues. • Mr. Cottle expressed his pleasure regarding the inclusion of a manager reconciliation page. He reminded the Committee that there might be valid reasons for performance discrepancies. This page simplifies the task of identifying discrepancies and provides a forum for discussion regarding the cause of a discrepancy.

Mr. Cottle asked Mr. Anderson and Mr. Chu to address the reason(s) for a 55 bp discrepancy between their total plan return calculations. Mr. Anderson stated that at this juncture he wishes to speak for his firm's calculation methodology. That methodology involves a calculation, which rolls-up each manager return. The individual returns are asset weighted to

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capture each manager's proportionate share of the total fund. Gray & Company then rolls-up the individual returns to arrive at a total fund return. The described methodology is compliant with the Association for Investment Management and Research (AIMR) Performance Presentation Standards. • Mr. Chu reported that SSB takes all underlying assets and treats that as one single portfolio, which also is AIMR compliant. • Mr. Cottle noted that when you transition 60% to 65% of your assets such as *SamCERA* experienced, there is no doubt the return calculations are affected. The different methodologies may account for some of the variance, but not the entire 55 bp difference. The parties should reconcile all differences in performance and report back to the Committee.

Action: Staff will facilitate a meeting between *SamCERA*, State Street and Gray & Company. The meeting's objective is to reconcile and/ or explain the 55 basis point difference between the Gray & Company and State Street calculation of total plan return for the period ending 6/30/2000.

The Committee returned to the scheduled agenda.

6.1 Acceptance of a Report Updating *SamCERA*'s Benchmark Modification Policy with Respect to Investments in the Tobacco Industry.

Mr. Cottle reviewed the materials provided with the agenda item, which include the Benchmark and Benchmark Modification Policies, a letter from BGI and a memorandum from staff. The BGI letter indicates the impact to *SamCERA*'s portfolio would be predominately in the Russell 1000 Index Fund. The Russell 2000 contains only two tobacco equities totaling ~\$115,000. *SamCERA* can not justify the increased transaction costs created by the divestiture of this portfolio. The US Debt Index Fund contains 24 tobacco-related bonds in the corporate module of the Lehman Aggregate. A separate *SamCERA* portfolio in this strategy would not have sufficient assets to allow BGI to adequately replicate the corporate index. It is estimated that this lack of replication would create a tracking error of 15 to 25 basis points, which is an unacceptable tracking error. The principles that apply to the US Debt index also apply to the Deutsche Asset Management Core Fixed Income Portfolio. The Committee unanimously agreed that it would not recommend divestiture for the fixed income portfolios. The Committee also reiterated the Board's position that the commingled structure of the Bank of Ireland Asset Management Portfolio would not allow it to be measured against a tobacco free benchmark. After reviewing all materials the Committee determined that only the Russell 1000 Index Fund meets the criteria in *SamCERA*'s Benchmark Modification Policy. The Committee will recommend that the Board adopt a Russell 1000 Ex-Tobacco benchmark for the Russell 1000 portfolio and that all other portfolios continue to be measured against their current benchmarks.

Motion by Colson, second by Buffington, to solicit a proposal from Barclays Global Investors to provide a Russell 1000 Ex-Tobacco Index Fund including an estimate of the transition cost. The Committee determined that the Russell 2000 Index Fund, US Debt Index Fund, Deutsche Asset Management Portfolio and Bank of Ireland Asset Management Portfolio do not meet the Benchmark Modification Policy. The motion carried unanimously.

6.2 Approval of *SamCERA*'s Investment Plan.

The Investment Committee reviewed the final draft of the Investment Plan. • Mr. Buffington

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expressed concern that the *Investment Plan* still allows acquisition of 144A Securities. His main concern is that the only requirement a 144A Security has is to provide publicly available financial statements within sixteen to eighteen months of coming to market. *SamCERA* should not be in the practice of acquiring securities that do not provide appropriate financial information, Ms. Colson reminded Mr. Buffington that 144A Securities are in the US Debt Index Fund. The Investment Committee determined excluding the securities would be inappropriate. However, the Committee will review the issue in six months. • Mr. Cottle proposed several editorial amendments to the Plan.

Motion by Colson, second by Buffington to recommend that the Board adopt the amended Investment Plan.

6.3 Approval of Topics for an Investment Manager Review – Bank of Ireland Asset Management.

The Committee approved the questions, which will be submitted to BIAM for written response. Mr. Cottle proposed that staff request Bank of Ireland Asset Management prepared to address the MSCI modifications to EAFE regarding Free Float. He believes it would be educational.

Action: It is the consensus of the Committee to recommended that the Board instruct staff to forward the list of questions and the Compliance Certification Checklist to Bank of Ireland Asset Management.

6.4 Approval of Topics for a Global Custodian Review – State Street Bank & Trust.

Mr. Clifton questioned whether the Board wished to review an Investment Manager and Custodian at the same meeting. Mr. Cottle and Mr. Hoffman express a desire to have State Street in to explain the methodology of their performance calculations. Mr. Buffington recommended that BIAM be put over, but concurred that State Street should be invited for an annual review. Mr. Cottle noted that BIAM has a large portion of our active portfolio. He recommends not postponing the BIAM review. By consensus the Committee will recommend that the Board review both firms at the November Board Meeting.

Action: It is the consensus of the Committee to recommended that the Board instruct staff to forward the list of questions and the Compliance Certification Checklist to State Street Bank and Trust.

6.5 Preparation for an Investment Manager Review – Barclays Global Investors.

Mr. Cottle and Ms. Colson expressed their appreciation that the Committee receives written responses to the prepared questions.

Action: No action was required.

7.0 Other Business: There was no other business.

8.0 Adjournment: There being no further business Mr. Cottle adjourned the Committee at 4:00.