

# BOARD OF INVESTMENTS AGENDA 3-9-11

## LACERA

300 N. Lake Ave., Suite 810  
Pasadena, CA 91101

9:00 AM

### I. APPROVAL OF THE MINUTES

- A. APPROVAL OF THE MINUTES OF THE MEETING OF THE BOARD OF INVESTMENTS OF FEBRUARY 9, 2011.

### II. PUBLIC COMMENT

### III. REPORT ON CLOSED SESSION ITEMS

### IV. ACTION ITEMS

- A. Recommendation as submitted by Gregg Rademacher, Chief Executive Officer:
1. Accept the June 30, 2010, Actuarial Valuation of LACERA prepared by your actuary, Milliman.
  2. Adopt recommended employer and employee contribution rates.
  3. Direct the Chief Executive Officer to communicate the results of the Actuarial Valuation to the Board of Supervisors by May 15, 2011, with a recommendation that the recommended employer rates be implemented no later than September 30, 2011.
  4. Receive and file the June 30, 2010 Actuarial Audit Reports prepared by your audit actuary, The Segal Company. (Memo dated February 28, 2011.)

#### Milliman

Karen I. Steffen, Fellow, Society of Actuaries Member, American Academy of Actuaries  
Nick J. Collier, Associate, Society of Actuaries Member, American Academy of Actuaries

#### The Segal Company

Paul Angelo, FSA, MAAA, EA Senior Vice President and Actuary

- B. Recommendation as submitted by Robert S. Van Der Volgen, Chief Counsel, that your Board approve the attached ballot insert entitled "POWERS AND DUTIES OF INVESTMENTS BOARD MEMBERS" to be included with the ballot materials for the election of the Second and Eighth Members of the Board of Investments. (Memo dated February 11, 2011.)
- C. Recommendation as submitted by John McClelland, Principal Investment Officer, Real Estate, James Rice, CFA, Investment Officer and Gerald Flintoft, CAIA, Investment Officer, Private Equity: Retain up to two managers and allocate up to \$400 Million for a commercial real estate debt investment mandate. (Memo dated February 28, 2011.)

#### Quadrant

Kurt Wright, Senior Partner and Chief Executive Officer  
Walt Huggins, Senior Partner and Executive  
Vice President  
Jessica Eggins, Partner and Senior Vice President

#### Cornerstone Real Estate Advisers

Dean A. Dulchinos, Vice President  
Robert F. Little, CFA, Chief Investment Officer, Finance  
Pat Kendall, Senior Director, Business Development

#### PCCP

Yon Cho, Partner  
Greg Eberhardt, Partner  
Bill Lindsay, Partner  
Don Kuemmeler, Partner

- D. Recommendation as submitted by Vache Mahseredjian, Principal Investment Officer: Approve attendance of Board members, and staff as designated by the Chief Executive Officer, at the Elkind Emerging Markets Forum hosted by Elkind Economics, Inc. on May 4-5, 2011 at the Four Seasons Hotel at Las Colinas in Dallas, Texas; and approve reimbursement of all costs associated with conference attendance in accordance with LACERA's Education and Travel Policy. (Memo dated February 9, 2011.)
- E. Recommendation as submitted by the Corporate Governance Committee: That your Board adopt LACERA's Revised U.S. Proxy Voting Guidelines. (Memo dated February 18, 2011.)
- F. Recommendation as submitted by Cynthia Lau, Legislative Affairs Officer: That your Board adopt a "Support" position on

Senate Bill 637 which would grant subpoena power to the Board of Investments. (Memo dated February 25, 2011.)

- G. Recommendation as submitted by Cynthia Lau, Legislative Affairs Officer: That your Board adopt an "Oppose" position on HR 567 and S 347, which create the "Public Employee Pension Transparency Act". (Memo dated February 25, 2011.)
- H. Recommendation as submitted by Gregg Rademacher: That the Board of Investments consider joining the Milken Institute as a Corporate Associate member. (Memo dated March 3, 2011.) (Placed on the Agenda at the request of Mr. Barger.)
- I. Recommendation as submitted by Gregg Rademacher, Chief Executive Officer: Approve attendance of Board members, and staff as designated by the Chief Executive Officer to attend NASP's 22nd Annual Pension and Financial Services Conference to be held on June 13-15, 2011 at the Beverly Hilton Hotel in Beverly Hills, California and approve reimbursement of all travel costs incurred in accordance with LACERA's Education and Travel Policy. (Memo dated March 2, 2011.) (Placed on the Agenda at the request of Mr. Santos.)

## **V. REPORTS**

- A. Private Equity 2010 3rd Quarter Performance Report  
Christopher Wagner, Senior Investment Officer, Private Equity (Memo dated March 2, 2010.)
- B. Cornerstone Hotel Income and Equity Fund II Report on On-Going Labor Dispute  
John McClelland, CRE, Principal Investment Officer, Real Estate (Memo dated February 22, 2011.)

## **VI. GOOD OF THE ORDER**

(For discussion purposes only.)

## **VII. ADJOURNMENT**

# BOARD OF INVESTMENTS MINUTES 3-9-11

## PRESENT

John M. Barger, Chair  
Simon S. Russin, Vice Chair  
Herman B. Santos, Secretary  
William Pryor  
Mark J. Saladino  
Diane Sandoval  
Michael Schneider  
Leonard Unger  
Estevan Valenzuela

## STAFF, ADVISORS, PARTICIPANTS

Gregg Rademacher, Chief Executive Officer  
Robert Hill, Assistant Executive Officer  
Janice Golden, Assistant Executive Officer  
Lisa Mazzocco, Chief Investment Officer  
Vache Mahseredjian, CFA, Principal Investment Officer  
John McClelland, CRE, Principal Investment Officer, Real Estate  
Christopher J. Wagner, Senior Investment Officer, Private Equity  
June H. Kim, Senior Investment Officer, Equities  
James Rice, Investment Officer  
Robert Z. Santos, Investment Officer, Fixed Income  
Gerald P. Flintoft, CAIA, Investment Officer, Private Equity  
Juan Almaguer, Senior Investment Analyst  
Shelly P. Tilaye, CAIA, Senior Investment Analyst, Private Equity  
Esmeralda Vita del Bosque, Senior Investment Analyst, Equities  
Dale Johnson, Senior Investment Analyst  
Robb Van Der Volgen, Chief Counsel  
Earl W. Buehner, Senior Staff Counsel  
Johanna Fontenot, Senior Staff Counsel  
Michael D. Herrera, Senior Staff Counsel  
Mark Klein, SEIU Local 721

## I. APPROVAL OF THE MINUTES

### A. APPROVAL OF THE MINUTES OF THE MEETING OF THE BOARD OF INVESTMENTS OF FEBRUARY 9, 2011.

A motion was made by Mr. Russin, seconded by Ms. Sandoval to approve the Minutes of the Board of Investments meeting of February 9, 2011. The motion carried with Mr. Unger abstaining.

## II. PUBLIC COMMENT

Caitlin Prendiville, Ivana Krajciovic, David Williamson, Kirill Penteshin, of Unite Here-Local 11 and Joseph Murphy and David Williamson, staff at the Embassy Suites Irvine ("Hotel"), addressed the Board regarding a labor dispute at the Hotel and asked that the Board follow-up and help achieve an amicable resolution. The Hotel is owned by a limited partnership in which LACERA participates as a Limited Partner.

## III. REPORT ON CLOSED SESSION ITEMS

None.

## IV. ACTION ITEMS

- A. A. Recommendation as submitted by Gregg Rademacher, Chief Executive Officer:
1. Accept the June 30, 2010, Actuarial Valuation of LACERA prepared by your actuary, Milliman.
  2. Adopt recommended employer and employee contribution rates.
  3. Direct the Chief Executive Officer to communicate the results of the Actuarial Valuation to the Board of Supervisors by May 15, 2011, with a recommendation that the recommended employer rates be implemented no later than September 30, 2011.
  4. Receive and file the June 30, 2010 Actuarial Audit Reports prepared by your audit actuary, The Segal Company. (Memo dated February 28, 2011.)

### Milliman

Karen I. Steffen, Fellow, Society of Actuaries

Member, American Academy of Actuaries  
Nick J. Collier, Associate, Society of Actuaries  
Member, American Academy of Actuaries

Mr. Rademacher provided an executive summary on the actuarial valuation results for June 30, 2010. He reported that Karen Steffen and Nick Collier of Milliman, LACERA's actuary, would follow-up with a report on the valuation. Mr. Rademacher also indicated that, Paul Angelo, of The Segal Company would report on Segal's audit of Milliman's the June 30, 2010 Actuarial valuation.

Mr. Collier of Milliman provided the results of the valuation and reported that there would be an increased employer contribution rate of 2% and a decreased funded ratio, with small changes in member rates. The strong 11.06% investment return for the current year was more than offset by large deferred asset losses from prior years that were partially recognized in the current valuation under the 5 year actuarial asset smoothing method.

The Employer Normal Cost rate decreased from 10.10% to 9.84%, due mainly to the adoption of new demographic assumptions with the 2010 Investigation of Experience. The Employer's required contribution rate to finance the Unfunded Actuarial Accrued Liability (UAAL) over 30 years increased from 4.12% to 6.47%. Milliman is also recommending new member contribution rates based on the new demographic assumptions adopted with the 2010 Investigation of Experience.

The combined result is an increase in the total required Employer contribution rate from the prior valuation of 2.09% (from 14.22% to 16.31% of payroll). The most significant factor causing this increase was the recognition of investment losses, which resulted in a 2.29% increase. All other factors had a relatively minor impact, causing a 0.20% decrease in total. A brief discussion followed.

### **The Segal Company**

Paul Angelo, FSA, MAAA, EA Senior Vice President and Actuary

Mr. Angelo of The Segal Company ("Segal") followed with his report on Segal's audit of the valuation report and Milliman's 2010 experience study. Segal concluded that Milliman has employed generally accepted actuarial practices and principles in studying plan experience, selecting assumptions, computing employer contribution rates, and presenting the results of their work. Mr. Angelo also reported that the actuarial assumptions as recommended by Milliman, as well as those approved by the Board of Investments are reasonable for use in LACERA'S actuarial valuation. He also stated that the audit of Milliman's valuation report confirms that the actuarial calculations as of June 30, 2010 are reasonable and based on generally accepted actuarial principles and practices. A brief discussion followed.

A motion was made by Mr. Unger, seconded by Mr. Saladino to:

1. Accept the June 30, 2010, Actuarial Valuation of LACERA prepared by your actuary, Milliman;
2. Adopt recommended employer and employee contribution rates;
3. Direct the Chief Executive Officer to communicate the results of the Actuarial Valuation to the Board of Supervisors by May 15, 2011, with a recommendation that the recommended employer rates be implemented no later than September 30, 2011; and
4. Receive and file the June 30, 2010 Actuarial Audit Reports prepared by your audit actuary, The Segal Company.

The motion carried with Mr. Schneider, Ms. Sandoval, and Chair Barger voting no.

- B.** Recommendation as submitted by Robert S. Van Der Volgen, Chief Counsel, that your Board approve the attached ballot insert entitled "POWERS AND DUTIES OF INVESTMENTS BOARD MEMBERS" to be included with the ballot materials for the election of the Second and Eighth Members of the Board of Investments. (Memo dated February 11, 2011.)

A motion to approve the recommendation was made by Mr. Russin, seconded by Ms. Sandoval. The motion carried by unanimous vote. (Mr. Pryor was not present for the vote.)

- C.** Recommendation as submitted by John McClelland, Principal Investment Officer, Real Estate; James Rice, CFA, Investment Officer, and Gerald Flintoft, CAIA, Investment Officer, Private Equity: That your Board retain up to two managers and allocate up to \$400 million for a commercial real estate debt investment Mandate.

Mr. McClelland provided an executive summary on the proposed allocation for the commercial real estate debt investment mandate and reported that three commercial real estate debt manager finalists would give presentations.

Mr. McClelland also reported that the proposed managers were proposing two different loan strategies: Strategy A involves making long-term 5-10 year, fixed-rate loans secured by stabilized core assets. Quadrant proposes to pursue Strategy A with 70%-100% of LACERA's allocation and may invest 0%-30% in a traditional subordinated debt. Staff finds this strategy attractive for the reasons outlines below. Strategy B involves making short-term 3-5 year, floating-rate loans secured by transitional assets. Cornerstone and PCCP propose to pursue Strategy B with a LACERA allocation.

Both strategies involve originating new whole loans that would be in a senior or a first debt position. These loans

would then be aggregated and leveraged at the portfolio level to create subordinated-loan-like positions for LACERA. He introduced the principals of Quadrant who followed with their presentation.

### **Quadrant**

Kurt Wright, Senior Partner and Chief Executive Officer  
Walt Huggins, Senior Partner and Executive Vice President  
Jessica Eggins, Partner and Senior Vice President

The principals of Quadrant provided an overview on the firm's historical background, investment strategy and philosophy. Quadrant is headquartered in Alpharetta, Georgia and is registered with the SEC as an investment advisor.

Quadrant is owned 50% by its management team and 50% by its financial partner, Mirvac Limited, a publicly traded Australian Listed Property Trust. The investment team is led by Kurt Wright. Walt Huggins, one of the firm's senior partners, is the portfolio manager that would be assigned and dedicated to the LACERA account. Quadrant investment philosophy revolves around the proposition that offering customized terms attracts higher quality borrowers and investments and those borrowers tend to perform better over time.

Quadrant proposes a primary strategy of originating a portfolio of traditional, high quality, 75% loan to value, whole loans and utilizing prudent (50%) portfolio leverage. Portfolio leverage will be provided by a Top 5 life insurance lender utilizing pre-negotiated documentation. It is anticipated that 70-to-100% of LACERA capital would be deployed into this strategy. To supplement the primary strategy, Quadrant proposes a secondary strategy of origination and acquisition of traditional mezzanine, B-Note and preferred equity opportunities with no additional leverage. Quadrant anticipates that this secondary strategy would account for no more than 30% of LACERA capital. A brief discussion followed.

### **Cornerstone Real Estate Advisers**

Dean A. Dulchinos, Vice President  
Robert F. Little, CFA, Chief Investment Officer, Finance  
Pat Kendall, Senior Director, Business Development

The principals of Cornerstone summarized the firm's historical background, investment strategy and philosophy. Cornerstone is headquartered in Hartford, Connecticut and has been registered with the SEC as an investment adviser since 1996. As of June 30, 2010, Cornerstone's assets under management ("AUM") totaled \$30 billion; of this amount, about \$20 billion is in real estate debt with the remainder in real estate equity and REITs.

Cornerstone is an active lender in low, medium, and high-risk real estate loans. They have capabilities to originate, manage, and service mortgage loans in-house. Loans are originated from direct relationships at Cornerstone as well as through third party brokers. As a seasoned lender, Cornerstone's underwriting process takes into account the property condition, the feasibility of the borrower's business plan, the rent roll, tenant leases, and macro and local market conditions.

The organization, with significant AUM, is deeply resourced and the team can tap into its expertise during the underwriting process in such areas as engineering, legal, local market conditions, and appraisal. Cornerstone also has an experienced internal loan servicing team including special servicing capabilities that would service loans in the proposed program. All loans are approved by a nine person Investment Committee, comprised of senior professionals across functions. They also propose using up to 50% leverage on certain loans to increase returns. The leverage would be in a revolving credit facility provided by a portfolio lender such as a commercial bank or an insurance company. A brief discussion followed.

### **PCCP**

Yon Cho, Partner  
Greg Eberhardt, Partner  
Bill Lindsay, Partner  
Don Kuemmel, Partner

The principals of PCCP spoke of the firm's background, investment strategy and philosophy. PCCP was founded in 1998 by four partners, Nicholas Colonna, Aaron Giovara, Donald Kuemmel and William Lindsay. They are an integrated real estate investment and asset management firm focused on both commercial real estate ("CRE") debt and equity investments. The firm is an established fiduciary having raised, invested and managed 16 real estate investment vehicles representing \$6.5 billion on behalf of institutional investors and have originated over \$3.5 billion of debt in 228 senior and mezzanine floating rate real estate loans since 1999. PCCP is headquartered in El Segundo, California and have regional offices in San Francisco, Sacramento and New York City.

PCCP reported that in order to generate unique opportunities, they prioritize markets and assign investment professionals to each market with the responsibility for maintaining relationships with local lenders developers, operators, brokers and institutions. Their investment philosophy is based on traditional lending principles: originate a well underwritten loan, earn a strong spread and fees, and be repaid at maturity. PCCP's underwriting process focuses

on three key areas: (1) cash flows of the collateral real estate and the profitability of the underlying investment, (2) borrower's experience, financial position, and the viability of the proposed business plan, and (3) asset's underlying market fundamentals. PCCP seeks a high degree of alignment with borrowers and further mitigates risk through a sound deal and legal structure. The firm advocates using leverage up to 50% to improve returns. Underlying leverage will be secured on a deal-by-deal basis by a commercial bank or insurer rather than aggregated on a collection of loans prior to funding. The floating rate financing would match the term of the underlying collateral loan. At the portfolio level, all loans would be cross-collateralized. If one loan loses value, the portfolio lender can recover the loss from other loans in the portfolio. Borrowing under the facility would be non-recourse to LACERA. PCCP has negotiated provisions that seek to minimize mark-to-market/margin call risk since leverage is less than 50% LTV.

The Board followed with a discussion on strategy and portfolio fee concerns.

A motion was made by Mr. Santos to hire Quadrant and PCCP. The motion died for lack of a second.

A motion was made by Mr. Schneider, seconded by Ms. Sandoval to hire Cornerstone and Quadrant, as the portfolio managers for the commercial real estate debt investment Mandate with an allocation of up to \$400 million. The motion carried with Messrs. Russin and Santos voting no.

- D.** Recommendation as submitted by Vache Mahseredjian, Principal Investment Officer: Approve attendance of Board members, and staff as designated by the Chief Executive Officer, at the Elkind Emerging Markets Forum hosted by Elkind Economics, Inc. on May 4-5, 2011 at the Four Seasons Hotel at Las Colinas in Dallas, Texas; and approve reimbursement of all costs associated with conference attendance in accordance with LACERA's Education and Travel Policy. (Memo dated February 9, 2011.)

A motion to approve the recommendation was made by Mr. Valenzuela, seconded by Mr. Saladino. The motion carried by unanimous vote.

- E.** Recommendation as submitted by the Corporate Governance Committee: That your Board adopt LACERA's Revised U.S. Proxy Voting Guidelines. (Memo dated February 18, 2011.)

A motion to approve the recommendation was made by Mr. Santos, seconded by Mr. Valenzuela. The motion carried, with Chair Barger abstaining.

- F.** Recommendation as submitted by Cynthia Lau, Legislative Affairs Officer: That your Board adopt a "Support" position on Senate Bill 637 which would grant subpoena power to the Board of Investments. (Memo dated February 25, 2011.)

A motion was made by Mr. Unger, seconded by Mr. Russin to adopt a Support position on Senate Bill 637. The motion carried by unanimous vote.

- G.** Recommendation as submitted by Cynthia Lau, Legislative Affairs Officer: That your Board adopt an "Oppose" position on HR 567 and S 347, which create the "Public Employee Pension Transparency Act". (Memo dated February 25, 2011.)

Mr. Mark Klein of Local SEIU 721 spoke in opposition to HR 567 and S 347.

A motion was made by Mr. Schneider, seconded by Ms. Sandoval to adopt a "Watch" opposition on HR 567 and S 347. The motion failed with Messrs. Valenzuela, Russin, Pryor, Saladino, Santos, and Unger voting no, and with Mr. Schneider, Ms. Sandoval and Chair Barger voting yes.

A motion was made by Mr. Santos, seconded by Mr. Pryor to adopt an "Oppose" position on HR 567 and S 347.

The motion carried with Mr. Schneider, Ms. Sandoval and Chair Barger voting no.

- H.** Recommendation as submitted by Gregg Rademacher, Chief Executive Officer: Approve attendance of Board members, and staff as designated by the Chief Executive Officer to attend NASP's 22nd Annual Pension and Financial Services Conference to be held on June 13-15, 2011 at the Beverly Hilton Hotel in Beverly Hills, California and approve reimbursement of all travel costs incurred in accordance with LACERA's Education and Travel Policy. (Memo dated March 2, 2011.) (Placed on the Agenda at the request of Mr. Santos.)

A motion to approve the recommendation was made by Mr. Valenzuela, seconded by Mr. Santos. The motion carried by unanimous vote.

- I.** Recommendation as submitted by Gregg Rademacher: That the Board of Investments consider joining the Milken Institute as a Corporate Associate member. (Memo dated March 3, 2011.) (Placed on the Agenda at the request of Mr. Barger.)

A motion to approve the recommendation was made by Mr. Saladino, seconded by Mr. Russin. The motion carried by unanimous vote.

## **V. REPORTS**

- A.** Private Equity 2010 3rd Quarter Performance Report Christopher Wagner, Senior Investment Officer, Private Equity (Memo dated March 2, 2010.) (For information only.)

The Private Equity 2010 3rd Quarter Performance Report is for information only and was received and filed.

- B.** Cornerstone Hotel Income and Equity Fund II Report on On-Going Labor Dispute John McClelland, CRE, Principal

Investment Officer, Real Estate (Memo dated February 22, 2011.)

The Cornerstone Hotel Income and Equity Fund II Report is for information only and was received and filed.

**VI. GOOD OF THE ORDER**

(For discussion purposes only.)

**VII.** Ms. Mazzocco reported that the SACRS Conference conflicts with the May Investment Board meeting. The Board of Investments meeting was rescheduled to be held on Monday May 9, 2011.

**VIII. ADJOURNMENT**