



Executive Staff:

Richard Stensrud  
Chief Executive Officer

Jeffrey W. States  
Chief Investment Officer

James G. Line  
General Counsel

Kathryn T. Regalia  
Chief Operations Officer

John W. Gobel, Sr.  
Chief Benefits Officer

Members of the Board of Retirement

James A. Diepenbrock, President  
Appointed by the Board of Supervisors

Keith DeVore, 1<sup>st</sup> Vice President  
Elected by Miscellaneous Members

John B. Kelly, 2<sup>nd</sup> Vice President  
Appointed by the Board of Supervisors

Dave Irish, Director of Finance  
Ex-Officio

Winston H. Hickox  
Appointed by the Board of Supervisors

Alice Jarboe  
Elected by Miscellaneous Members

William D. Johnson  
Elected by Safety Members

Nancy Wolford-Landers  
Elected by Retired Members

Robert Woods  
Appointed by the Board of Supervisors

William Cox  
Elected by Retired Members

John Conneally  
Elected by Safety Members

## MINUTES

### RETIREMENT BOARD MEETING, THURSDAY, OCTOBER 4, 2007

The special meeting of the Retirement Board was held in the Sacramento County Employees' Retirement System Administrative Office, 980 9th Street, 18<sup>th</sup> Floor, Sacramento, California, on Thursday, October 4, 2007, commencing at 1:02 p.m.

#### OPEN SESSION:

##### PUBLIC COMMENT:

1. None heard.

#### CLOSED SESSION:

##### LEGAL MATTERS:

2. CONFERENCE WITH LEGAL COUNSEL – INITIATION OF LITIGATION  
{Government Code Section 64956(c)}  
Support of Petition for Supreme Court Review and Amicus Brief re Cathy Lexin v. The Superior Court of San Diego County (The People, Real Party in Interest) California Court of Appeal, Fourth Appellate District, Case No. D049251

Motion by Ms. Wolford-Landers that SCERS join in the Amicus brief; Seconded by Mr. Kelly. Motion carried (9-0).

**CLOSED SESSION:**

**LEGAL MATTERS (continued):**

3. CONFERENCE WITH LEGAL COUNSEL – INITIATION OF LITIGATION  
{Government Code Section 64956(c)}

Item was withdrawn.

**OPEN SESSION:**

**ADMINISTRATIVE MATTERS:**

4. Chief Executive Officer Richard Stensrud provided opening remarks to the presentation of the Review of Economic Actuarial Assumptions for the June 30, 2007 Actuarial Valuation and the Analysis of Actuarial Experience during the Period July 1, 2004 through June 30, 2007, as prepared by The Segal Company.

Mr. Stensrud discussed the role of actuarial assumptions in establishing the funding for and funded status of the retirement system. Mr. Stensrud noted that in each annual actuarial valuation the actuary compared the previous year's actuarial experience to the actuarial assumptions being used to project the future growth of assets and liabilities, and to the extent there were differences, the contribution rates were adjusted to incorporate the experience. Mr. Stensrud further noted that in a longer period assessment such as the triennial experience study the actuary may find that the actuarial experience or trends call into question the continued reasonableness of an assumption, and in such a case, the actuary will recommend a change in the assumption itself. Mr. Stensrud noted that a change in an assumption can result in an increase or decrease in contribution rates greater than what would be seen in the annual experience adjustment. Mr. Stensrud explained that it was important, however, that the retirement system utilize realistic actuarial assumptions in order to help assure that growth in the retirement system's assets (through the combination of contributions and investment earnings) keeps pace with the growth in its liabilities. Mr. Stensrud explained that collecting the appropriate level of contributions was also important to help assure 'intergenerational cost equity.' Mr. Stensrud explained that this meant both that increased costs should not be pushed onto future generations of participants, but also that current participants should not pay more than they should.

Mr. Stensrud noted that the Board would be acting as fiduciaries when considering the assumptions that would be utilized by the retirement system. Mr. Stensrud requested that General Counsel James Line provide the Board with a summary of the fiduciary duties associated with the Board's decisions in such matters. Mr. Line outlined the various elements of the fiduciary duties that the Board must be cognizant of in making its decisions regarding actuarial assumptions. Mr. Line also noted that under the California Constitution, the Board had plenary authority for the management of the retirement system, and that the Constitution vested sole authority in actuarial matters to the Board.

**OPEN SESSION:**

**ADMINISTRATIVE MATTERS (continued):**

Mr. Stensrud noted that it was important that the Board understand the financial impact of the assumptions it was considering. Mr. Stensrud further noted, however, that in carrying out its fiduciary responsibilities in establishing actuarial assumptions, the Board should be careful not to base its decisions on a particular outcome, as opposed to whether a given assumption was reasonable and prudent.

Mr. Stensrud noted that the Board would be receiving two reports from The Segal Company, which would present various recommended changes to the current actuarial assumptions. Mr. Stensrud noted that in addition, the Board was being presented with information regarding an alternative investment return assumption (i.e., 7.875%) that he had asked the actuary to evaluate. Mr. Stensrud explained that he had asked the actuary to prepare such an evaluation so that the Board could assess whether an adjustment to the current investment return assumption might be warranted given recent changes to SCERS' asset allocation model. Mr. Stensrud noted that the actuary's assessment of the alternative investment return assumption was addressed in a supplemental memorandum.

Mr. Stensrud also noted that he had worked with both Sacramento County and The Segal Company to assess whether there was a reasonable basis for concluding that the actuarial experience regarding the merit and promotional salary increases might be anomalous, rather than reflective of a permanent trend that warranted a change to that assumption. Mr. Stensrud noted that the arguments submitted by the County on the issue were contained in a memorandum from the County and were addressed in the previously referenced supplemental memorandum from The Segal Company.

Finally, Mr. Stensrud noted that in a letter from the County Executive submitted at the start of the Board Meeting, the County was asking that the Board consider changing the investment return assumption to 8% and delay implementing the proposed change to the merit and promotional salary increase assumption to allow for further time to study whether an assumption change was warranted.

In concluding his remarks, Mr. Stensrud noted that due to the need to complete the fiscal year-end financial analysis and the evaluation of actuarial data, combined with deadlines related to the upcoming audit, Comprehensive Annual Financial Report (CAFR), and actuarial valuation, the consideration of the proposed actuarial assumptions was on a tight timeline. Mr. Stensrud commended both The Segal Company and the County for their efforts in analyzing and responding to the proposed actuarial assumptions within the necessary timeframe.

Paul Angelo and Andy Yeung of The Segal Company presented the Review of Economic Actuarial Assumptions for the June 30, 2007 Actuarial Valuation and the Analysis of Actuarial Experience during the Period July 1, 2004 through June 30, 2007, and discussed the actuarial assumptions recommended in the two reports.

**OPEN SESSION:**

**ADMINISTRATIVE MATTERS (continued):**

With respect to the Actuarial Experience During the Period July 1, 2004 through June 30, 2007, Mr. Angelo and Mr. Yeung explained that The Segal Company was recommending that: (a) the retirement rate assumptions be modified by increasing the current assumed rate for Tier 1 Miscellaneous members, but reducing the current assumed rate for Tier 2 and Tier 3 Miscellaneous members and for both Safety Tiers; (b) modifying certain of the mortality rate assumptions; (c) increasing the termination rate assumption to reflect that a higher proportion of terminating members are electing to withdraw their contributions rather than go to deferred status and ultimately draw a benefit; (d) increasing the sick leave conversion assumption to reflect the higher level of sick leave conversion at retirement; and (e) increasing the merit and promotional salary increase to reflect the fact that actual experience with this salary component has been running consistently and substantially higher than the current set of assumptions.

With respect to the Review of Economic Actuarial Assumptions for the June 30, 2007 Actuarial Valuation, Mr. Angelo and Mr. Yeung explained that The Segal Company was recommending that: (1) the investment return assumption be maintained at 7.75%; (2) the inflation assumption be maintained at 3.50%; (3) the inflation and 'real across the board' components of the salary increase assumption be maintained at current levels; but (4) the promotional and merit salary increase component for the reasons noted in subparagraph (e) above.

Discussion followed regarding various aspects of the two reports and the recommendations contained therein.

Extensive discussion took place regarding The Segal Company's methodology for establishing the investment return assumption, including: (a) how The Segal Company establishes the set of projected asset class returns; (b) whether the assessment is based on index returns ('beta') and/or whether it contains additional investment return from investment manager out-performance ('alpha'); (c) how The Segal Company establishes the 'risk adjustment'; and (d) how The Segal Company determines the 'confidence level' that a given investment return assumption will be achieved over a ten to fifteen year period.

Mr. Angelo noted that there is not one 'right' investment return assumption, but rather a range of assumptions that would be considered reasonable and prudent in light of the circumstances, including projected market returns and the investment model of the retirement system. Mr. Angelo noted that for the purposes of performing the actuarial valuation, the actuary recommends a single point within the range, but that the appropriate point is a subject on which the Board's expertise and knowledge regarding the system's investment model could yield an equally reasonable alternative to that recommended by the actuary.

**OPEN SESSION:**

**ADMINISTRATIVE MATTERS (continued):**

With respect to the last observation, Mr. Stensrud explained that there was no special 'magic' to his request that The Segal Company assess the reasonableness of considering an investment return assumption of 7.875% as opposed to some other alternative. Mr. Stensrud explained that he had suggested that the actuary analyze that number because it was mid-way between the current assumption of 7.75% and SCERS' previous assumption of 8%, and as such, would provide a basis for assessing the impact of making a cautious, measured change in the assumption.

Mr. Angelo stated that based on the circumstances, a 7.875% investment return assumption would be a reasonable investment return assumption for SCERS. Mr. Angelo noted that SCERS had recently modified its asset allocation model, which now projected a higher investment return than the previous model. Mr. Yeung noted that the new asset allocation also carried a lower level of risk than the previous model. Mr. Yeung further noted that the combination of the higher projected return and lower level of risk resulted in only a modest reduction in the confidence level (i.e., from 62% to 60%) if the investment return assumption was increased to 7.875%. Mr. Angelo and Mr. Yeung explained, however, that because the new asset allocation model had not yet been fully implemented, The Segal Company had elected to recommend that the investment return assumption of 7.75% be maintained for the present.

Discussion followed regarding whether the goal of the Board in adopting the new asset allocation model had been to generate higher absolute returns or to achieve a higher level of confidence that the actuarial investment assumption would be achieved. It was agreed that both goals had been a factor in adoption of the asset allocation model. It was further recognized and agreed that the changes being considered to the investment manager structure for implementing the new asset allocation model would add additional projected investment returns.

Extensive discussion followed regarding the basis for The Segal Company's recommended change to the actuarial assumption related to merit and promotional salary increases.

Mr. Angelo and Mr. Yeung noted that the biggest cost impact from The Segal Company's proposed changes to the demographic assumptions came from the proposed change in the merit and promotion salary increase assumption, and that it would affect both employer and employee contribution rates.

Mr. Angelo and Mr. Yeung noted that the County had submitted information for their review in support of their argument that the merit and promotional increase experience may be distorted due to: (1) large, retroactive one-time pay differentials that resulted from the implementation of new labor agreements; (2) higher rates of retirement due to recent benefit enhancements, which in turn, meant more promotions and replacement hires; and (3) pay equity adjustments over the last few years.

**OPEN SESSION:**

**ADMINISTRATIVE MATTERS (continued):**

Mr. Angelo and Mr. Yeung noted that the recommended changes to the assumption regarding merit and promotional salary increases was based on not just three years of experience, but rather, was based on nine years of experience, over which time the experience had run well above the assumptions. Mr. Angelo and Mr. Yeung further noted that the recommended changes to the assumption would not fully adjust the assumption to the experience, and as such, they believed it did not represent an over-weighting of the recent experience. Mr. Angelo did note, however, that The Segal Company would be happy to further analyze the arguments of the County, and if the findings supported it, they would recommend that the assumption be modified next year, rather than in three years as would normally occur with such an assumption.

Nav Gill, Chief Operations Officer for Sacramento County and Mark Norris, Administrator of the Internal Services Agency of Sacramento County addressed the Board. Mr. Gill and Mr. Norris presented the Board with information in support of the County's request that the investment return assumption be changed to 8% and that the proposed change to the merit and promotional salary increase assumption be deferred to allow more time to evaluate the data. Mr. Gill and Mr. Norris noted that if any shortfall resulted from its requests, the County would be responsible for paying the unfunded liability. Finally, Mr. Gill and Mr. Norris expressed their appreciation for Mr. Stensrud's efforts to facilitate consideration by the actuary of alternatives to the actuarial assumptions The Segal Company had proposed.

Mr. Stensrud provided the Board with additional information that he believed would be helpful for the Board in its consideration of the actuarial assumptions.

First, Mr. Stensrud provided information from two studies regarding the investment return assumption utilized by public retirement systems. One was a national study reporting on investment return assumptions as of June 2005. Mr. Stensrud noted that as of that date, the median assumption was 8%, but the study further noted that the number of retirement systems using 8% was declining and the number of systems using an assumption below 8% was increasing. The second study reported on the investment return assumptions utilized by the 1937 Act retirement systems as of December 2006. Mr. Stensrud noted that this study reported 8% as the median assumption as of that date, but as with the national data, there was a clear trend among the systems to move to a lower assumption.

Next, Mr. Stensrud provided information about the projected impact of SCERS' five year smoothing process on employer contribution rates. Mr. Stensrud noted that the information was premised on certain assumptions, the key one being that SCERS would neither exceed nor fall short of its investment return assumption for the next four years. Mr. Stensrud explained that while it was not likely that SCERS would directly hit its investment return assumption each year, using such an assumption would allow the Board to see how the substantial net deferred gains currently contained in the smoothing

**OPEN SESSION:**

**ADMINISTRATIVE MATTERS (continued):**

process would reduce employer contribution rates and employer costs each year for the next five years. Mr. Stensrud noted that the data showed that the current level of net deferred gains would result in a substantial reduction in employer costs over the period, or alternatively, would serve as a substantial buffer against increased costs if investment returns should fall short of expectations.

Mr. Stensrud also provided information showing the projected impact on the employer contribution rate and annual costs for the next fiscal year if the smoothed investment gains were combined with a decision by the Board to adjust the investment return assumption upward to 7.875% and adopt the merit and promotion salary increase assumption proposed by The Segal Company. Mr. Stensrud noted that under such a scenario, the increased costs associated with the change in the merit and promotion salary increase assumption would be more than offset by the decrease in costs associated with the change in the investment return assumption and the realization of smoothed deferred gains, and overall, there would be a reduction in current employer costs and contribution rates. Mr. Stensrud again cautioned, however, that such information was offered to illustrate the impact of possible decisions, and that the Board's selection of actuarial assumptions should be based on whether the Board determined they were reasonable and prudent and not because of their impact on costs.

Before returning to discussion of the actuarial assumptions under consideration, the Board acted to receive and file the reports by The Segal Company and the other information presented to the Board on a Motion by Ms. Wolford-Landers, Seconded by Mr. Kelly. Motion carried (9-0).

Discussion followed regarding the actuarial assumptions recommended by The Segal Company, exclusive of the investment return assumption and the merit and promotion salary increase assumption. It was agreed that the latter two assumptions should be considered separately. Motion by Mr. Kelly to adopt the actuarial assumptions recommended by The Segal Company, except for the investment return assumption and the merit and promotion salary increase assumption; Seconded by Ms. Wolford-Landers. Motion carried (9-0).

Discussion followed regarding the alternative investment return assumptions that had been presented for consideration. Motion by Mr. Kelly to adopt 7.875% as the investment return assumption; Seconded by Mr. DeVore. Motion carried (9-0).

Discussion followed regarding the merit and promotion salary increase assumption, including whether the experience in the most recent three year period was skewed by anomalous events, and whether the same could be said for the longer nine year period.

**OPEN SESSION:**

**ADMINISTRATIVE MATTERS (continued):**

Mr. Stensrud reminded the Board that if it chose to adopt the merit and promotion salary increase assumption proposed by The Segal Company, the Board could also direct the actuary to study the data further, and if the actuary concluded that a re-adjustment was appropriate, such a change could be made for the next actuarial valuation.

Mr. Stensrud also noted that the merit and promotion salary increase assumption would be utilized in determining the cost for Additional Retirement Credit (ARC) service purchases, which would be made available in the near future. Mr. Stensrud noted that offering the ARC purchase option had been delayed so that the cost calculations could be based on the most current actuarial assumptions. Mr. Stensrud further noted that subsequent changes in the actuarial assumptions would have an impact on the cost for ARC purchases, with the result that the cost could vary depending on when a purchase was initiated. Mr. Stensrud noted that based on the experience in other retirement systems that had made ARC purchases available, he expected there would be a high level of interest in ARC purchases when they were introduced. Mr. Stensrud also noted that if the price for an ARC purchase was subsequently increased due to a change in actuarial assumptions, unfunded liability could accrue from the earlier purchases which would have to be paid by the County.

Discussion continued regarding whether the change in the merit and promotion salary increase assumption proposed by The Segal Company should be: (1) adopted; (2) delayed for further analysis; or (3) adopted in part, with additional analysis to follow. In response to the question of whether The Segal Company would consider the third option (specifically, adopting an assumption based on one-half of the change proposed by The Segal Company) as yielding a reasonable assumption for the upcoming valuation, Mr. Angelo stated that The Segal Company would consider such an assumption as reasonable. Mr. Stensrud noted that if the experience fell short of the assumption, it would be factored into the actuarial valuation as an 'actuarial loss' during the annual experience adjustment.

Further discussion followed. Motion by Mr. Irish to adopt a merit and promotion salary increase based on one-half of the change proposed by The Segal Company; Seconded by Mr. Woods. Motion carried (8-0, with Ms. Wolford-Landers abstaining).

Mr. Stensrud noted that pursuant to the Board's discussion he would direct The Segal Company to further analyze the data with respect to the experience regarding merit and promotion salary increases and to report next year on whether a further adjustment in the assumption was warranted.

The meeting was adjourned at 4:11 p.m.



**MEMBERS PRESENT:** James A. Diepenbrock; Keith DeVore; John B. Kelly; Dave Irish; Winston Hickox (arrived at 1:03 p.m.); William D. Johnson; Robert Woods; Nancy Wolford-Landers; Alice Jarboe; and John Conneally.

**MEMBERS ABSENT:** William Cox

**OTHERS PRESENT:** Richard Stensrud, Chief Executive Officer; Jeffrey States, Chief Investment Officer; James G. Line, General Counsel; Kathryn Regalia, Chief Operations Officer; John Gobel, Chief Benefits Officer; Suzanne Likarich, Retirement Services Manager; Nav Gill, County Chief Operations Officer; Mark Norris, County Internal Services Agency Administrator; David Devine, County Director of Personnel Services; Paul Angelo and Andy Yeung of the Segal Company; Thuyet Ziyalan, Senior Accountant; and Jennifer Foster, Executive Assistant.

Respectfully submitted,

SACRAMENTO COUNTY EMPLOYEES'  
RETIREMENT SYSTEM

Richard Stensrud  
Chief Executive Officer

APPROVED: \_\_\_\_\_  
James A. Diepenbrock, President

DATE: \_\_\_\_\_

cc: Retirement Board (11); Board of Supervisors (6); County Counsel; County Executive (2); Internal Services Agency (2); County Labor Relations; Employee Organizations (20); Sacramento County Retired Employees' Association; SCERS Member Districts (10); Elected Officials (3); Superior Court of California, County of Sacramento; Amervest Company, Inc.; Mark Merin; John R. Descamp; and The Sacramento Bee.