SANTA BARBARA COUNTY
EMPLOYEES' RETIREMENT SYSTEM

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Vincent P. Brown
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Received
JUL 0 8 2009
Santa Barbara
Grand Jury

July 1, 2009

Honorable Judge J. William McLafferty
Santa Barbara Superior Court
1100 Anacapa Street, 2nd Floor
P.O. Box 21107
Santa Barbara, CA 93121-1107

RE: Board of Retirement's Response to 2008-09 Grand Jury Report

Dear Judge McLafferty:

This letter is in response to the Grand Jury's letter to the Santa Barbara County Employees Retirement System (SBCERS) dated April 13, 2009, requesting a response to its 2008-2009 report entitled "Santa Barbara County Employees' Retirement System." The response is provided pursuant to the requirements of California Penal Code Section 933(c).

We have enclosed with this letter the detailed response to the findings and recommendations contained in that report as approved by the Board of Retirement at its regular meeting of June 24, 2009.

Please feel free to contact us should you have any questions concerning SBCERS' response or if you need any further information.

Sincerely,

Shawn Terris

Shawn Terris, Chair
Board of Retirement
Santa Barbara County Employees' Retirement System

cc: ✓Grand Jury Foreperson
Members, Board of Supervisors
Michael F. Brown, County Executive Officer
Alan Blakeboro, Esq., Reicker, Pfau, Pyle, & McRoy

Response to Finding 3:
We disagree wholly with the finding. The Board of Retirement spends limited time to consider its prior actions to ensure the minutes of its meetings are entirely accurate.

Recommendation 3:
That the Board meet more than once a month or establish specialized sub-committees.

Response to Recommendation 3:
This recommendation has been implemented. While the Board of Retirement holds one regular meeting per month, it holds special meetings as needed. The Board met on eighteen days in 2008, and as of June 24 has held eleven meetings to date in 2009. The Board also established a standing Investment Risk Advisory Committee in March 2009, in addition to the existing Operations Committee and Disability Process Review Committee.

Finding 4:
The use of an actuarial interest rate of 8.16% is overly optimistic, has understated the estimated payments required to fund retirement benefits, and has therefore contributed to the growth in the unfunded liability.

Response to Finding 4:
We disagree wholly with the finding. As reported in the 2006 actuarial experience study, as of June 30, 2005, the fund's 18-year compound average net return on assets was 9.7%. Since that time, the fund earned 10.8% in 2006 and 17.2% in 2007, and lost 7.1% in 2008. This record indicates that the assumed rate of 8.16% is well within the range of reasonableness for the fund's long-term investment horizon. However it should be noted that actuarial assumptions are reviewed and set by the Board of Retirement every three years following an investigation of experience and with expert advice from the System's actuary. The actuarial interest rate was set most recently in 2007 and will again be reviewed in 2010.

Recommendation 4:
That the Retirement Board adopt an actuarial interest rate between seven and seven and three-quarters percent.

Response to Recommendation 4:
This recommendation will not be implemented because it is not warranted. As indicated above, the long-term investment performance of the fund supports an actuarial interest rate above seven and three-quarters percent. As previously indicated, actuarial assumptions are reviewed and set by the Board of Retirement every three years following an investigation of experience and with expert advice from the System's actuary. The next review will be in 2010.

Finding 5:
Increased pension obligations will be a significant County budget problem in the near future. Accounting changes are required to provide temporary relief from the near term impacts of recent market events.

Response to Finding 5:
We agree partially with the response. Policy changes that involve accounting changes are possible and are under current consideration by the Board of Retirement. The decision to implement of any such changes must be made only after full consideration of the relevant facts and must be consistent with the Board's fiduciary responsibility to the membership of the system.

SANTA BARBARA COUNTY EMPLOYEES' RETIREMENT SYSTEM RESPONSE
SANTA BARBARA COUNTY 2008-09 GRAND JURY

FINDINGS AND RECOMMENDATIONS REGARDING SANTA BARBARA COUNTY EMPLOYEES' RETIREMENT SYSTEM

Finding 1:
While in the recent past, according to accepted actuarial practices, the Santa Barbara County Employees' Retirement System was adequately funded, recent market losses will have a significant negative impact on the funding level of the Retirement System.

Response to Finding 1:
We agree with the finding. This is the situation faced by virtually all pension plans nationwide, public and private.

Finding 2:
The investment performance of the Santa Barbara County Employees' Retirement System in general has ranked in or near the bottom quartile of the Bank of New York Mellon Corporation universe of public pension funds during the one – three – five year periods ending December 31, 2008.

Response to Finding 2:
We agree with the finding. We would, however, note that SBCERS' somewhat conservative asset allocation has weathered the recent repricing in the market better than more aggressive funds. As of the first quarter of 2009, our ranking has risen to just below the second quartile for the one-, three-, and five-year periods ending March 31, 2009.

Recommendation 2a:
That the Retirement Board improve its in-house investment analysis capability, and consider establishing the position of Chief Investment Officer.

Response to Recommendation 2a:
The recommendation has not yet been implemented, but will be implemented in the future.

Recommendation 2b:
That the Retirement Board adopt stated criteria for the termination of underperforming investment managers.

Response to Recommendation 2b:
The recommendation requires further analysis. SBCERS has a written policy and process by which we hire, monitor and terminate investment managers. We generally believe that the decision to terminate an underperforming manager is appropriately a judgment requiring active consideration of various market and organizational factors, and input from the Board's investment consultant. In December 2008, SBCERS employed the services of investment counsel to review and make recommendations regarding our investment policies, and the manager termination process will be included in that review.

Finding 3:
During Board meetings, considerable time is spent recalling what happened at the previous meeting.

It should be noted that policy changes that provide temporary employer relief will increase long term costs.

Recommendation 5:
That the Retirement Board institute a temporary increase in the unfunded liability amortization period to 30 years, returning to a 15-year amortization after a period of between 10 to 15 years.

Response to Recommendation 5:
The recommendation requires further analysis. In accordance with Article 16, Section 17 of the California Constitution, the System's funding policies are delegated to the Board of Retirement. The Board is in the process of reviewing and considering alternatives to its current funding policies. The Board will take the action that it deems prudent and most appropriate with regard to the amortization period and other factors in consultation with its expert actuaries and legal advisors.