



Approved
8/12/04

**Finance Committee
Special Teleconference Meeting
Summary Minutes**

**July 19, 2004
ABAG Conference Room A
101 Eighth Street, Oakland, CA**

Presiding

Jim Steele, Chairman

Jurisdiction

So. San
Francisco

Committee Members Present

Emma Karlen, Vice Chair
Jim O'Leary
Jesus Nava

Milpitas
San Bruno
Burlingame

Committee Members Not Present

Debra Ryan

Half Moon Bay

Staff Present – ABAG PLAN Corporation

Marcus Beverly, Risk Manager
Henry Gardner, Deputy Executive Director
Joseph Chan, Chief Financial Officer
Carol Johnson, Recording Secretary

Consultants Present – PFM Group

Richard Babbe

1. CALL TO ORDER:

Meeting was called to order at 1:00 p.m. and quorum was established by roll call.

2. PUBLIC COMMENTS: There were no public comments.

3. APPROVAL OF MINUTES OF FEBRUARY 18, 2004 FINANCE COMMITTEE MEETING:

Motion was made by Karlen/S/O'Leary/C to approve the February 18, 2004 revised Finance Committee meeting minutes as presented.

4. INVESTMENT POLICY AND STRATEGY REVIEW:

As directed by the Committee at its July 19th meeting, an investment consultant was hired through a competitive bidding process to perform a one-time review of investment policy and strategies. Consultant Richard Babbe of PFM Asset Management presented a power point presentation outlining his firm's review of PLAN's investment policy, portfolio, and investment strategy.

He reported that, generally, PFM found the investment portfolio to be in compliance with both the California Government Code and PLAN's Investment Policy. However, there are some minor inconsistencies in the Investment Policy that need to be improved or clarified. He provided a sample policy as part of his firm's report.

He also reviewed PLAN's investment strategies in the context of current market conditions. He made suggestions for improving performance without significantly affecting credit quality or liquidity. Highlights of his review and suggestions included:

- Portfolio diversified across issuers but diversification among sectors can be improved
- Moderate exposure to liquidity risk
- Moderate level of call risk
- Policy limit of 30% on callable securities is above the level PFM usually recommends (20-25%) but reasonable if PLAN continues to select those securities with good call protection and good spread over comparable bullet securities. We can limit call risk by purchasing one-time calls and spreading out call dates over several years.
- Managing portfolio duration within a 10-15% band of average liability duration
- Competitively purchase securities whenever possible
- Consider adding U.S. Treasuries to enhance diversification
- Explore use of AA rated corporate securities. The Government Code allows A rated corporate notes and our policy allows only AAA rated. Lowering rating requirement to AA for corporate notes may improve our opportunity to enhance overall portfolio performance. It is important to understand that corporate notes need ongoing monitoring and therefore PFM recommends purchasing these notes only when yield spread v. government securities are high and monitoring these investments closely.

Joseph Chan presented a report containing his analysis of the PFM report and recommendations. He pointed out that staff is in agreement with all the changes to PLAN's Investment Policy as reflected in the sample investment policy presented by PFM. Accordingly, he recommended adopting the sample policy as presented. In addition, he reported staff is in agreement with all

investment strategies recommended by PFM, with the exception of using total return, and liquidity rating.

Total rate of return is a measure of evaluating investment performance that includes changes in market value. Because PLAN intends to hold its investments to maturity, including changes in market value in investment performance evaluation is not in conformity with PLAN's investment objective. PLAN has been using the effective yield in evaluating portfolio performance.

Liquidity rating, as PFM defines it, is a measure of how easily a security can be sold—the difference between its bid and ask prices. Again, because PLAN intends to hold securities to maturity, this measure has little significance to our investment portfolio.

The committee members and staff discussed these and other points in detail as they were presented. The committee was in general agreement with the investment strategy and policy revision recommendations but agreed that more time was needed for discussion and decision making. Key issues to resolve included:

- Corporate Notes - whether to reduce rating to AA or eliminate from the policy
- Callables – whether or not to reduce limit from 30% to 20-25% and if not, whether to articulate in the policy or strategy limiting purchases to one-time calls or limiting the number of call dates within each year of maturity.

A follow-up teleconference meeting to discuss these issues and take action will be arranged between the dates of August 11th and 13th

5. OTHER BUSINESS: none.

6. ADJOURNMENT: meeting was adjourned at 2:35 p.m.

Respectfully Submitted,



Marcus Beverly
Risk Manager & Secretary
ABAG PLAN Corporation