

**Minutes of the Regular Meeting**

**Held March 24, 2011 at 10:00 A.M. in the State Museum Auditorium  
205 West State Street, Trenton, New Jersey**

**Council Members in Attendance:**

Robert Grady, Chair  
Nicholas Caprio, Vice Chair  
Marty Barrett  
Brendan Thomas Byrne, Jr.  
Andrew Michael Greaney  
Guy Haselmann  
James P. Marketti  
Timothy McGuckin left at 2:05  
Jeffrey Oram  
Richard Klockner  
James C. Kellogg joined by telephone

**Council Members Not in Attendance:**

**None**

**The Regular Meeting was called to order by Chair Grady at 10:04 A.M.**

**Roll Call and Meeting Notice**

Secretary Adams performed roll call and reported that notice of the Regular Meeting scheduled for March 24, 2011 was sent by mail deposited in the post office, by facsimile and email on March 7, 2011. A copy of the notice was posted in the Division on March 7, 2011, mailed to the Council, Times of Trenton, Star-Ledger, Bergen Record, and Courier Post on March 7, 2011 and filed with the Secretary of State on March 7, 2011.

**Approval of Minutes for the Annual and Regular Meetings held January 12, 2011**

Chair Grady welcomed the members of the Council and public and thanked them for attending especially given the inclement weather.

Council Member Haselmann motioned to approve the minutes for the Annual Meeting of January 12, 2011. This motion was seconded by Council Member Brendan Thomas Byrne, Jr. Council Member Marketti had a comment regarding page 3, 2<sup>nd</sup> to last paragraph stating he did not make a motion, but intended to make a motion at regular meeting. Chair Grady proposed to amend the minutes to read that Council Member Marketti stated he intended to make a motion at the regular meeting and strike the second half of the sentence after the semicolon. Chair Grady asked if there were any other comments on the Annual Meeting minutes. The Council unanimously approved the motion approving the minutes, as amended, with Council Member Barrett abstaining.

Chair Grady noted that there was a typo on the cover page, second line of the Regular Meeting Minutes, which should be corrected to say Minutes of the Regular Meeting not Minutes of the Annual Meeting. Council Member Byrne motioned to approve the minutes for the Regular Meeting of January 12, 2011, as so amended. This motion was seconded by Council Member Haselmann. Chair Grady asked if there were any other comments on the Regular Meeting Minutes. Council Member Marketti raised a point of

order regarding when the Council would discuss the motion proposed by him at the prior meeting. Chair Grady replied the motion would be discussed under Action Items. Chair Grady asked if there were any further comments on the Regular Meeting Minutes. Minutes were approved unanimously.

### **Director's Report**

Director Walsh discussed investment results as of December 31, 2010 and February 28, 2011. For the first half of the fiscal year ending December 31, 2010, the Fund was up 11.86% vs. the Council's benchmark of 11.85%, one basis point better. For the fiscal year to date as of February 28, 2011, the Fund was up 15.21% significantly over the Council's benchmark of 14.32%. Director Walsh attributed this outperformance to cutting the duration on bonds and reducing the funds' overexposure to equities, primarily domestic equities but international as well. Director Walsh stated the U.S. Stock Market had a phenomenal return over the past eight months, 32% fiscal year to date and 3% for the past month alone. Chair Grady stated that the fund was up 15.2% since June 30, 2010, a \$10 billion gain. Chair Grady complimented Mr. Walsh and the asset managers for having done a great job. He noted that the Division and Council made a tactical decision months ago to shorten duration and lessen the funds' exposure to fixed income and to overweight on large cap U.S. equities, which yielded the good 15.2% return for the last eight months. The stock market has been up approximately 30% and fixed income has been flat for the fiscal year to date. Chair Grady reminded the Council that past performance is no guarantee for future returns, and that the Division and the Council, in overseeing the Division, needed to keep making good decisions.

Brian Arena stated that the equity market had been strong and the Division had positive returns for eight months. Domestic equities were up 3.5% in February versus the benchmark, which was up 3.6%. The portfolio is up 32.3% fiscal year-to-date, with the benchmark being up 31.2% over the same period. The funds were slightly underweight in energy. The technology sector had produced the strongest relative returns, and Weyerhaeuser, in the materials sector, was the strongest performer. Director Walsh commented that the last five years the funds were significant underweight in financials. He noted that his predecessor, Bill Clark, had made a great call with the former State Investment Council to underweight financials. The funds were now almost at benchmark, gradually accumulating high quality financials.

Director Walsh stated thanked the Investment Policy Committee members for all their time, and noted that a lot of time was spent at the last meeting on the human and economic tragedy in Japan.

Deputy Director McDonough stated the international portfolio was up 2.2% in February vs. 2.4% for the portfolio's custom benchmark. The portfolio was up 26.9% fiscal year to date, with the benchmark being up 29.0%. Deputy Director McDonough stated the international portfolio structure initiated an underweight in emerging markets early in the calendar year and an overweight in developed markets, which was very beneficial to the portfolio as the developed markets significantly outperformed the emerging markets the first few months of the year. The down side to that policy was the portfolio's overweight to Japan. Relative to the benchmark, Japan is 16% and the portfolio's weight is 19%, or \$500 million.

Gilles Michel stated the Division took the option to recover the overweight stance with Japanese futures, while at the same time investing in exporters which have outperformed the market since the event. Chair Grady asked whether the Division altered the mix of the Japanese exposure. Gilles Michel replied that the Division was discussing internally whether to increase exposure to financials which has

been a structured underweight in Japan. Council Member Haselmann commented that Japan is the only stock market in the world that trades at book value, and noted that the actions of the G7 regarding the yen should provide underlying support for the exporters. Council Member Haselmann asked whether the events in Japan have had a spillover effect in countries other than Japan that receive products from Japan. Mr. Michel replied that it is a problem that they were trying to address through stock selection.

Director Walsh reported that the portfolio did well in fixed income versus its benchmark. The Division was looking at changing the fixed income benchmark to properly reflect the Division's reduction in duration. The reported duration exceeded the current duration due to a recent transfer from fixed income into equity.

Tim Patton stated the performance for fixed income (excluding TIPS and High Yield) for February was 1.2% vs. 1.5% for the Barclays Long Government/Credit Index. The underperformance was due to the portfolio's underweight in Financials. For the fiscal year to date, Common Fund B (excluding TIPS and High Yield) returned 1.3% versus the benchmark of 0.0%. The Division sold approximately \$356 million of Build American Bonds (BABS), 84% of which were revenue based, and continued to monitor the market. The Division was reducing its exposure to less liquid issues and putting that money back into more liquid issues.

Phil Pagliaro stated the performance for TIPS for February was 1.8% vs. 0.9% for the Barclays US Inflation-Linked Bond Index. For the fiscal year to date, the TIPS portfolio returned 1.6% vs. the benchmark of 2.9%. The outperformance/underperformance is attributed to the types of TIPS in the portfolio, which were all 20-year TIPS. TIPS continued to outperform nominal Treasuries. For January and February, nominal Treasuries returned -10 basis points and TIPS returned 105 basis points. Mr. Pagliaro noted that inflation was rampant and was starting to be priced in by the market.

Chair Grady noted that, as a matter of context, even with tactical underweighting, one-third of the \$72 billion portfolio, or \$24 billion, is in fixed income, and the Division has outperformed the benchmark by 2.3% fiscal year-to-date, resulting in a gain of \$500 million. He congratulated the team.

Director Walsh reported a change in cash balances from December to February. Cash balances have gone up not for any operational reasons but has been building up as it comes back from private equity, commodities and fixed income.

Christine Pastore reported private equity performance has been better than expected and maturing quite nicely. The portfolio was coming out of the J Curve and profits have increased on the entire private equity portfolio. Over the last few months, the Division has received over \$400 million in distributions. Ms. Pastore reported the real estate portfolio had its best quarter since inception, up 6.3% as of December 31, 2010, with 75% of managers reporting. Ms. Pastore discussed her upcoming trip to California, stating that the Division is looking to invest alpha, or excess gains, in venture capital, which is very underweighted, about 3% of the private equity portfolio. Ms. Pastore stated that it was an opportune time to enter the venture capital market, and that she and Jason MacDonald would be meeting with top-quartile venture capital managers to try to get an idea of the market and to gain access to their funds, which has been difficult historically for public pension funds.

Chair Grady noted that venture capital was approximately two-tenths of one percent, about \$150 million, of the private equity portfolio, far less than most public plans. He said that it was important to recognize the venture capital business has underperformed in the last ten years, but significantly

outperformed in the last 20 to 30 years. He stated that investing in venture capital at this point in the cycle, when there is less assets coming in and less competition, should result in better vintage years. Chair Grady offered a motion that, in the areas of venture capital, private equity and hedge funds, the Division should aim to invest with top quartile managers. Council Member Oram asked whether all of the venture capital managers were domestic. Chair Grady responded that the majority are domestic, but it is hard to say given the evolution of global GDP. Council Member Kellogg stated that he intended to vote for the resolution but wanted to mention that when a fund receives a share of profits with no hurdle rate, there is a risk that the fund will turn out to not be a top quartile performer, while the Division would have already paid for top quartile performance. Chair Grady amended his motion to apply only to private equity and venture capital investments.

Director Walsh stated he would try to provide documentation regarding the quartile performance of funds being presented to the Council. Council Member Byrne stated he endorsed the motion completely in concept and agreed that the variance is much wider between the top and the bottom quartile. He stated, as another layer of due diligence, he would like to see more performance data over time. Chair Grady stated that the State should expect a premium from private equity and venture capital managers to compensate for the lack of liquidity, and the key is due diligence to confirm that every single venture capital and private equity manager is in fact top quartile.

Chair Grady restated the motion and Council Member Kellogg seconded. All others voted in favor of the motion, with Council Member Marketti abstaining.

Maneck Kotwal commented on the performance of the Hedge Fund portfolio. The Hedge Fund portfolio returned 2.35% for the month of February versus its benchmark of 0.13% for the HFRI Fund of Funds Composite Index. For the fiscal year to date, the Hedge Fund portfolio returned 10.34% versus the benchmark of 6.16%. The portfolio had approximately \$150 million in redemptions during the month of January and funded approximately \$49.6 million in commitments in February. Chair Grady noted the outperformance of the Hedge Fund portfolio team relative to the benchmark.

Director Walsh commented that all of the Division's alternative investment consultants are in the middle of an RFP process. Chair Grady stated for clarity that the RFP process is not run by the Division or the State Investment Council. Director Walsh said the process is run by the Division of Purchase and Property, but the Division of Investment is quite involved in the process.

Council Member Marketti commented on the lack of ten-year annualized returns of the portfolio from the investment report. He stated that long-run returns were necessary to avoid underfunding the pension plan. Chair Grady directed staff to add three-, five- and ten-year returns to the next report. Director Walsh stated that ten-year returns as of June 30, 2010 were provided at the last annual meeting, but there were still issues with the new bank custodian regarding historical performance and the Division did not want to release numbers until it knew they were correct.

Chair Grady commended the Division on the format and the presentation of the investment report.

### **Annual Report**

Chair Grady stated that the Annual Report for Fiscal and Calendar Year 2010 was sent to the Council by email. Chair Grady made a motion to approve the Annual Report for Fiscal and Calendar Year 2010 as circulated. Council Member Kellogg recommended adding the four union members that left during the

year to the list of departing members of the Council on page 21 of the Annual Report. Chair Grady amended his motion to include this change. Council Member Haselmann seconded the motion. The motion was approved unanimously.

### **Asset Allocation Study**

Chair Grady introduced Pete Keliuotis from Strategic Investment Solution, Inc. ("SIS") to present SIS' "Preliminary Asset Allocation Analysis". Mr. Keliuotis noted the purpose of the presentation was to provide the structure of the asset allocation study, the assumptions for different asset classes, and the initial proposed mixes. At a future meeting, after pulling in the liability projections, the Council could select an asset mix and finalize the FY'12 Annual Investment Plan (effective July 1, 2011). Mr. Keliuotis remarked that the Investment Policy Committee, the Director and Deputy Director, and SIS recommend Mix 3 as a first step towards target allocations.

Mr. Keliuotis discussed SIS' capital market expectations, including expected returns and standard deviations. He also provided definitions and objectives of asset classes that were included in the analysis, and discussed the proposed asset mixes. He recommended that the Council provide flexibility in implementing targets by providing ranges that the Division will operate within.

Chair Grady commented the asset allocation analysis is a work in process, with testing over the next few months, prior to adoption of the annual investment plan in the May - June timeframe. He stated that it was helpful to have a discussion regarding the objective of the different sub asset classes, and endorsed the establishment of ranges, instead of single data points, in implementing an investment plan to give the Division some flexibility.

Chair Grady noted that the biggest moves made over the last couple of months were a decrease in exposure to U.S. Treasuries due to the current situation with respect to interest rates and inflation risk, an increase in exposure to high quality corporate fixed income instruments, and an increase in exposure to Real Estate, which given the underperformance of that category, is worth discussion.

Council Member Byrne noted that other managers were viewing Treasury securities as a very risky asset, and asked whether the terms Capital Preservation and Risk Mitigation were being used as synonymous terms. Mr. Keliuotis responded that capital preservation and risk mitigation were different strategies. Chair Grady commented that both were important; it was just a matter of classification.

Council Member Caprio commented on the liability side of the equation, asking the consultant whether it would be considering pension fund benefits and consulting with the funds' actuaries. Mr. Keliuotis responded that in April and May the final liability projection will be complete, and that they are working closely with the actuary of the State to get the most recent data available.

Council Member Marketti questioned how the consultant was dealing with the obviously flawed calculation of the assumed rate of return, as opposed to the actual historical return. Mr. Keliuotis responded that they did not focus on the actuary's expected return or discount rate as part of its analysis. Instead, they try to come up with a mix that is the best risk adjusted mix appropriate with the Council's overall risk tolerance. Chair Grady noted for the record that in the governor's package of reforms regarding the pension system one of the recommendations was to lower the expected rate of return to 7.5%. Council Member Caprio stated if the rate of return drops to 7.5%, it will put more pressure on the asset side because these liabilities will grow considerably.

Chair Grady stated that this debate should continue but noted for the record that the objective of the Council is to maximize the risk adjusted returns in the system.

Council Member Haselmann commented that this asset allocation study encompasses thousands of different scenarios. Under Mix 3, current exposure goes up, risk goes down and Sharpe Ratio increases. The upside and downside risk returns captured in a bad scenario will be improved because the mix allocations diversify the portfolio a little bit better. Also, he supported moving to a range rather than a specific target, which allows the portfolio manager to have flexibility, and the ability to find ways of gaining more yield enhancement through tactical shifts.

### **Secondary Sale Procedures**

Chair Grady introduced a memorandum entitled "Secondary Sale Procedures for Alternative Investment Program". He stated the memorandum set forth the process the Division would undertake to sell any of its alternative investment assets in a private market transaction.

Director Walsh commented that, in FY2010, the Division bought and sold tens of billions of dollars of securities in the public market, but never looked at the possibility of selling alternative investments in the private market. Jason MacDonald gave an overview of the proposed procedures, and stated the goal was to maximize net sale proceeds while minimizing counterparty risk. Division staff, the general consultant and asset class consultant will review each alternative investment asset class on a periodic basis, no less than semi-annually. Chair Grady said it was a well thought out proposal. Chair Grady made a motion to adopt the process as outlined in the memo. Council Member McGuckin seconded. The motion carried unanimously.

Chair Grady stated the Investment Policy Committee has reviewed a number of Private Equity and Hedge Fund Investments.

### **Hedge Fund Investments**

Maneck Kotwal stated the Division was proposing a \$100 million investment in Third Point Partners, L.P.; an add-on \$100 million investment to Pershing Square, L.P.; a \$200 million investment in Reservoir Strategic Partners Fund, L.P.; and an add-on \$200 million investment in Och-Ziff Structured Credit. Chair Grady wanted to clarify for the record that Daniel Stern, the Hedge Fund Consultant from Cliffwater LLC, is not related to Mr. Daniel Stern of Reservoir Strategic Partners Fund, L.P.

*Memorandum "Proposed Investments in Third Point Partners, L.P. and Add on Investment to Pershing Square, L.P. Fund" dated March 18, 2011*

Mr. Stern commented on Third Point Partners, L.P. Fund. The firm currently managed \$4.4 billion in its flagship event-driven fund. Performance was very good 22 percent since inception, putting it in the top quartile over long time periods. Chair Grady asked for the performance for 2008, 2009 and 2010. Performance in 2008 was down 32.8%, in 2009 up 38% and in 2010 up 42%. Mr. Stern also noted the fund charges a 2% management fee and a 20% performance fee. The incentive allocation is subject to a modified high water mark provision; however, it requires that the fund recoup 250% of prior losses. Chair Grady stated that the conclusion of the Investment Policy Committee was that staff had conducted appropriate due diligence. Council Member Marketti went on record as opposing the investment.

Mr. Stern commented on the add-on investment to Pershing Square, L.P. Fund. The fund is a concentrated, deep-value, activist hedge fund, which seeks to identify stocks that exhibit significant valuation discrepancies between their current trading price and intrinsic business value. The fund charges a 2% management fee and a 20% performance fee. Pershing Square Fund is the best performing hedge fund so far with a cumulative return of 24.5% since inception in 2004. Looking at the rankings against all hedge funds, against all event-driven, the fund is in the top 2%. The performance for 2008 was down 12%, for 2009 up 40% and for 2010 up 29.5%.

Council Member Haselmann stated with these managers you don't just get the best managers, you get exposure from the portfolio that is more idiosyncratic in nature with no correlation to the majority of the risk group.

Chair Grady stated that the conclusion of the Investment Policy Committee was that staff had conducted appropriate due diligence. Council Member Marketti went on record as opposing the investments.

*Memorandum "Proposed Investment in Reservoir Strategic Partners Fund, L.P." dated March 18, 2011*

Mr. Stern commented on Reservoir Strategic Partners Fund, L.P. The firm currently manages \$4.5 billion in a series of opportunistic hedge funds that make investments in both public and private markets, with a focus on out-of-favor sectors and asset classes, including seed investments in external hedge fund managers. The fund will charge a 1.5% management fee on capital commitments and a 20% incentive fee on distributions which will be held in escrow during the lock-up period. Chair Grady asked, since the Division has direct access to so many hedge fund managers, why is it investing in a fund of funds. Chair Grady also expressed concern that the Division's \$200 million investment constituted more than 20% of the initial close. Mr. Stern responded that Reservoir will launch with \$200-\$300 billion in assets. He also responded that it is very difficult to spend time and do due diligence on the types of funds invested in by Reservoir. Instead, like in private equity, it is better to invest in people who have demonstrated that they are top tier in terms of identifying and nurturing successful new firms.

Council Member Haselmann stated that it was probably an ideal time to invest in such a fund, because a lot of the money flowing into the hedge fund industry is going into the larger more institutional quality funds. He stated that if the State were going to invest in a fund-of-funds, it was important to identify seasoned veterans such as these, with 17 years of experience in seeking out managers.

Council Member Marketti went on the record as opposing the investment.

*Memorandum "Proposed Add-on to Och Ziff Structured Credit" dated March 18, 2011*

Mr. Stern commented on the add-on Investment to Och-Ziff Structured Credit. Och Ziff is a separate account with New Jersey and the principals of Och Ziff as investors. Terms are very attractive, with a 75 bps management fee, a 20% carry, and 8% preferred return. Performance from April of 2010 annualized at 22.87% with 3% volatility, which significantly outperformed the broad universe of hedge funds. Och Ziff was structured with a timed investment period (rather than an open end), with a lock up investment period of 2½ years and a life of fund 5 years to liquidate.

Chair Grady stated that the conclusion of the Investment Policy Committee was that the staff had conducted appropriate due diligence. Council Member Marketti went on the record as opposing the investment.

### **Private Equity Investments**

*Memorandum "Proposed Investments in Centerbridge Capital Partners II and Newstone Capital Partners II" dated March 24, 2011*

Pete Keliuotis, the consultant from Strategic Investment Solution, Inc., commented on Centerbridge Capital Partners II. Centerbridge II is an opportunistic private equity manager that merges buyout and distressed investing across control and non-control situations. NJDOI is currently invested in Centerbridge Capital Partners I, whose performance is in the top quartile and who is one of the top performing partnerships in the NJDOI private equity portfolio. The proposed investment of \$100 million in Centerbridge Capital II will be part of a \$4 billion fund.

Mr. Keliuotis commented on Newstone Capital Partners II. Newstone is a middle market focused provider of mezzanine capital to private equity sponsors; the firm will structure investments to provide substantial current income, adequate principal protection and upside in the form of warrants, common stock or other-equity-type investments. NJDOI is currently invested in the firm's first mezzanine fund which is currently performing in the top quartile per Venture Economics. The proposed investment of \$100 million in Newstone Capital II will be part of a \$750 million fund.

Chair Grady stated that the conclusion of the Investment Policy Committee was that the staff had conducted appropriate due diligence. Council Member Marketti went on the record as opposing the investments.

*Memorandum "Proposed Consolidation & Amendment of Blackrock Mandates (SONJ II & Sidecar)" dated March 18, 2011*

Mr. Keliuotis commented on the proposed consolidation and amendment of SONJ Private Opportunities II and SONJ Private Opportunities Side car into one vehicle (SONJ II). Chair Grady commented that these funds, called co-invest funds, are looking at opportunities to make direct investments into companies, but typically alongside private equity managers who might be leading those investments but are raising additional capital. Blackrock has a mandate in a separate vehicle to look at buying secondary interests in private equity funds. Christine Pastore explained that the Division had negotiated the ability to merge the two separate programs into one separate account vehicle with more attractive terms.

Council Member Marketti inquired if the Investment Policy Committee had reviewed the investment. Chair Grady stated that they had, and did not have any issues with the proposed investment. Council Member Marketti went on the record as opposed to this investment. Chair Grady stated that this was not a new investment, but granted more flexibility to the manager to be more opportunistic in investment selections.

### **Commodity linked notes program**

Director Walsh provided an update on the commodities program. The Division does not have the ability to use swaps due to the lack of ISDA agreements, and so it would likely pursue additional investments in



commodity linked notes. The Division recently unwound one note, taking profits since there was no further upside to the investment. There are still two notes outstanding in the portfolio. To date, a \$100 million profit has been recognized on a \$400 million investment. Mr. Walsh stated that the Division was seeking a modification of the current policy to allow two year notes to provide further optionality of providing downside protection in what can be a very volatile market.

Several questions were posed by Council members. Mr. Walsh stated the three current notes were executed with Barclays, Cargill and JP Morgan, but that the Division did not have specific issuers in mind for future notes. The Division would work in conjunction with SIS to identify issuers that meet the requirements set forth in the policy. The Division would also need to identify the benchmark that will be used. The notes will be part of the real asset allocation.

**Proposed Adoption of Amendments to NJAC 17:16-69, 71, 90 and 100 regarding Common Pension Fund E, Real Assets, Private Equity and Absolute Return Strategy Investments**

Susan Sarnowski presented an overview of the proposed adoption of amendments to Subchapters 69, 71, 90 and 100 of the State Investment Council regulations. Council Member Byrne recommended one change in the response to Comment No. 2 from CWA Local 1033 with respect to the proposed changes, recommending that the term "downside protection" be changed to "greater stability". Council Member Kellogg stated that he intended to vote against the proposed amendments; while generally in favor of alternatives, he felt that the proposals increased the limits above what he felt is appropriate. A discussion amongst several Council members, Mr. Stern and Mr. Nesbitt of Cliffwater ensued regarding fees and hurdle rates.

Chair Grady made a motion to approve the resolution. Council Member Haselmann seconded the motion. The resolution carried 8 to 3, with Council Members Barrett, Kellogg and Marketti voting against the resolution.

**Proposed Amendments to NJAC 17:16-22 (Fixed Income Exchange Traded Funds) and NJAC 17:16-45 (Put Options)**

Mr. Walsh summarized the proposed amendments to Subchapter 45 which would allow the Division to purchase puts in all of the funds as well as provide the ability to sell puts against them. Chair Grady emphasized that the funds would not be able to write naked puts. Chair Grady made a motion to approve the resolution. Council Member Haselmann seconded the motion. The motion carried unanimously.

Mr. Walsh summarized the proposed amendments to Subchapter 22 which would allow the flexibility to purchase international fixed income ETFs which are US dollar denominated. Chair Grady made a motion to approve the resolution. Council Member Haselmann seconded the motion. The motion carried unanimously.

**Motion regarding funding of the pension system**

Council Member Marketti read his proposed motion contained in the January 12, 2011 minutes which would encourage the Governor and the NJ State Legislature to fully fund the actuarially-computed contribution to the pension systems for fiscal year 2011. Chair Grady stated he intended to oppose the motion as the fiduciary obligation of the State Investment Council is to provide investment and policy

oversight and assist the Division in its mandate of maximizing investment returns while mitigating risk. Council Member Marketti stated that he believed it was the mission of the Council to protect the interests of the beneficiaries and that, during his tenure on the Council, the Council had historically adopted policy statements. Past legislators and Governors had failed to adequately contribute to the systems. Chair Grady commented that it was bipartisan failure. Council Member Marketti stated that he would consider the current system to be not much more than a Ponzi scheme, with retirees being funded by current employees. The assets currently cover 94% of what is owed to current retirees and 10% owed to current employees. Chair Grady stated that he considered Ponzi scheme to be a pejorative term since the pension system has real assets prudently invested by the Division. Council Member Marketti encouraged the employee representatives on the Council to support the motion. Council Member Klockner seconded the motion. Council Member Barrett suggested that a letter be sent to the Governor. Council Member Marketti amended his motion to include that a letter be sent to the Governor and each member of the Legislature. Council Member Kellogg indicated he was opposed to the motion since it only specified the current fiscal year and that was not possible. Council Member Marketti amended his motion to refer to the fiscal 2012 contribution. Council Member Haselmann expressed his concern that the motion would serve to politicize the Council without accomplishing any benefits over time. Council Member Oram stated that as fiduciaries he did not believe the Council should take political positions. Council Member Caprio stated he opposed the motion since there was no legal requirement to fund the systems and the Governor was not mandated to make the contributions; it should be left to the Governor and Legislature to work it out. Council Member Byrne stated that the body should be maintained as an investment body and not a political body although he was sympathetic to the funding issue. The motion was defeated by a 6-5 vote, with Council Members Kellogg, Barrett, Klockner, Marketti and McGuckin voting in favor of the motion and the remaining members opposed.

#### **Trading Desk Overview**

Chief Trading Officer Michael Wszolek provided a brief overview of the trading operations of the Division, focusing on the lack of adequate technology, and addressed various questions of the Council Members.

#### **Supplemental Ethics Code**

Ms. Sarnowski gave a verbal annual report as required by the Treasury Supplemental Ethics Code regarding personal trading by Division employees. For the calendar year 2010, all employees, with the exception of one on medical leave, filed the required report. There were two violations during the year. One employee sold securities without obtaining prior approval. A second employee failed to report a new account and provide statements. The violations were referred to Labor Relations for appropriate action.

Ms. Sarnowski also reported that in February 2010 the Division finalized and issued a written policy regarding Insider Trading. Ms. Sarnowski noted that this was a codification of procedures previously followed by Division employees. All employees received training on the new Policy.

#### **Proxy voting guidelines related to Executive Compensation**

Ms. Sarnowski presented two proposed proxy voting guidelines on executive compensation as required by Dodd-Frank. The Division will support annual frequency votes on executive compensation since it provides the highest level of accountability and corresponds to annual proxy voting. With respect to the

non-binding "say-on-pay" proposals, the Division will review the proposals on a case-by-case basis, utilizing information from its proxy research provider. The portfolio analyst and Director (or Deputy Director in his absence) will review all instances where we intend to vote against management. Similarly, the Division will continue to review Golden Parachute proposals on a case-by-case basis in accordance with its current guidelines. The Division will have to report its votes on compensation matters to the SEC this year in accordance with the requirements of Dodd-Frank. Chair Grady made a motion that the Council go on record supporting the annual vote proposal. Council Member Oram seconded the motion. The motion passed unanimously.

#### **Iran Divestment**

Ms. Sarnowski presented a status of compliance with the statute governing investments in Iran. The pension fund had divested of all holdings as of January 4, 2011 in accordance with the statute and has issued its annual status report to the Legislature, a copy of which was furnished to the Council.

#### **Report from the State Treasurer**

There was no report from the State Treasurer.

#### **Public Comment**

The two registered speakers, Ms. Raeder and Mr. Miskowski departed the meeting prior to the public comment period. Chair Grady indicated that Ms. Raeder spoke with him before departing, and indicated they would speak at a future meeting.

#### **Motion to Adjourn**

Chair Grady made a motion to adjourn. Council Member Haselmann seconded the motion. The motion carried unanimously.