

***State of New Jersey
State Investment Council***

**Meeting at
Rutgers Student Center, New Brunswick
126 College Avenue
Multi-Purpose Room B, First Floor
New Brunswick, New Jersey 08901**

**Thursday, February 21, 2008
Noon – Lunch
1 p.m. Council Meeting**

MINUTES

Approved March 20, 2008

Present: Orin Kramer, Chair
Marshall Brown
W. Montgomery “Monty” Cerf
Jose R. Claxton – *via teleconference*
Mark Kandrak
Douglas A. Love

Absent: Jonathan Berg, James Clemente, Sue Crotty, Jim Kellogg, Erika Irish Brown

Also

Present: *From the Division of Investment:*
William G. Clark, Director
Brian Arena, Investment Officer
James Falstrault, Investment Director
Susan Burrows Farber, Chief Administrative Officer
Jason MacDonald, Analyst
Gilles Michel, Assistant Director
O. Ike Michaels, Deputy Director
Christine Pastore, Investment Officer
Ainsley A. Reynolds, Accounting Manager
Tim Rollender, Analyst
Susan Sarnowski, Middle Office Manager and Compliance Officer

From the Governor’s Office, Dept of the Treasury and Attorney General’s Office:
Elizabeth Cervenak, Legislative Liaison, Department of the Treasury
Rubin Weiner, Deputy Attorney General

Other invitees:

Mr. Scott Booth, Townsend
Mr. Harshal Shah, Strategic Investment Solutions
Mr. Daniel Stern, Cliffwater

Members of the Public:

Frederique Adam-Jupillat, LPS
Jamie Barker, Revenue

Also

Present:

(continued)

Karin Bauer, DEP
William Bauer, DOE
Gloria Jean Berry
Ellen Brockmann, SCREA
Dianne Spence Brown, Executive Vice President Local 1033
Shirley Bryant, L&PS
Russell Caffey
Jose Cardona, TESC
Dorothy Carl, Revenue
Sandy Coia
Clifford S. Cooper III, NJ DOBI
Barbara Counts, ELEC
Paul Curcio, P&P
Jeffrey Grossman, DOI
James Jameson, NJEA
Anthony Kozicz, DOBI
Nikk Kriss
Patricia Latimer, DOE
Josh Maeulen, resident of PA
Gary Magzen, BME
P. G. Maurer
Dusty McNichol, *The Star Ledger*
Mitchell Mercer, DSS
Mary Ann Mesics, DOE
Anthony F. Miskowski, Member, CWA Local 1033
Barbara Montgomery
Clayton Mull, SCREA
Marion Mynch, Public Defender
Anne Marie Newman, MVC
Rodney E. Nichols
Kevin P. Norton, Bank of NY Mellon
Shameko K. Palmer, Revenue
Dale Parichuk, LPS
Frank Percoskie, DOBI
Rae C. Roeder, President, Local 1033
Richard A. Rollins, Bank of NY Mellon
John Ruth, Treasury
Saul Smulyan
Rodney Stevens
John Strachan, NJDHTS
Raymond E. Weicker
Marianne Wintens, DOE

I. Call to Order

Chair Kramer called the meeting to order at 1:15 p.m.

II. Notice of Meeting

Interim Council Secretary Susan Burrows Farber reported that in compliance with the Open Public Meetings Act, *NJSA 10:4-1 et seq.*, notice of the meeting scheduled for February 21, 2008 was sent by mail deposited in the post office, by facsimile and email on February 1, 2008. A copy of the notice is on file as posted in the Division and sent to the Council, the **Times of Trenton**, **The Star-Ledger**, the **Bergen Record**, the **Courier Post**, and Secretary of State.

III. Reports of Director Clark

A. Memorandum from Director Clark to the Council, dated February 13, 2008, entitled "Investment Reports."

Chair Kramer asked that the Director's report be presented and that other agenda items requiring a vote be held until a quorum could be reached by teleconference call.

Director Clark reported that January had been a tough month for the market, and that the Fund was down overall as a result. He noted that the market was starting to price as if in recession, regardless of whether a recession was occurring. He noted that the Division's investments in Citigroup and Merrill Lynch as discussed at January's Council meeting had been the largest transactions for the month.

Mr. Arena, investment officer-Domestic Equities, reported that portfolio had followed the market down, with technologies down significantly. He said the Division's underweight position in financials continues to help Fund's overall performance. Director Clark said the Division evaluates this underweight position on a continual basis.

Director Clark said the bond portfolio was strongly out-performing its index, and that the Division had moved \$500 million into long-term European bonds

Mr. Michel, assistant director-International, said this portfolio was holding its defensive position of the past few months, particularly with regard to utilities. Mr. Cerf commended the early decision to underweight European financials.

(Mr. Claxton joined the meeting by teleconference call at 1:30 pm, completing the quorum).

Director Clark noted recent attention to auction-rate securities in the press and said the Division had never owned any, largely because the size of the issues typically didn't warrant the work expended for credit analysis. He said the Division would be open to such investments if they made sense in the future.

Director Clark also reported on his attendance, and that of Chair Kramer, Council Member Erika Irish Brown, and Chief Administrative Officer Sue Farber, at a United Nation's

Investor Summit on Climate change held Feb. 14 in New York City. He said the strong presence of organized labor at the Summit helped create a united effort for investment action, and said the Division would continue to look at its investments and managers critically for their contributions to reducing climate change. Chair Kramer said New Jersey was in a catch-up mode in activism on this issue compared to other states.

IV. *Approval of Minutes*

Chair Kramer offered one correction to the minutes of the regular meeting of the Council held on January 17, 2008; specifically, the deletion of the words “needing improvement” from the first sentence in the last paragraph on page 4. The sentence as corrected reads, “Ms. Sarnowski noted that KPMG had issued no management letter to the Division, a positive indication that the auditors saw no significant weaknesses in internal controls.”

The minutes as corrected were approved unanimously on a motion by Mr. Kandrac, seconded by Mr. Cerf.

V. *Committee Reports*

There were no committee reports.

VI. *Pending Matters*

There were no pending matters.

VII. *New Business*

A. *Proposed Alternative Investments*

- 1. Memorandum from Director Clark to the Council, dated February 13, 2008, entitled, “Proposed Real Estate Investments in Westbrook Real Estate Fund VII, Lehman Brothers Real Estate Partners Fund III, Apollo Domestic Emerging Market Fund, PLA Residential Fund III, Walton Street Mexico Fund I and Walton Street Real Estate Fund VI, L.P.”*

Director Clark noted that because Mr. Cerf had recused himself from all discussions of investments with Lehman, and because Mr. Cerf’s presence was needed for a quorum, the discussion of a proposed investment in Lehman Brothers Real Estate Partners Fund III would be held at the next Council meeting.

Mr. Booth of Townsend said a proposed commitment of \$100 million in the Westbrook Real Estate Fund VIII marks the Division’s second investment in a Westbrook fund. He said Westbrook VIII is a \$2.5 billion global high-return fund, pursuing opportunistic real estate investments resulting from undervalued assets and portfolios, corporate and government divestitures, urgent recapitalizations and ineffective ownerships.

Mr. Booth said a proposed commitment of \$50 million in the Apollo Domestic Emerging Markets Fund would be part of a \$500-\$525 million fund investing in “domestic emerging markets” in US major metropolitan areas, including in New York and New Jersey.

He said the proposed commitment of \$50 million in the PLA Residential Fund III LP would be part of a \$1.5 billion closed-end commingled fund focused on making high-return investments in residential real estate in Mexico and other select countries of Latin America. The fund is sponsored by Prudential Real Estate Investors.

He said the demographic and economic trends favoring a strong demand for housing in the Mexico and Latin American region was also behind the proposed commitments of \$25 million in the Walton Street Mexico Fund I and \$25 million in the Walton Street Real Estate Fund VI.

2. *Memorandum from Director Clark to the Council, dated February 13, 2008, entitled, “Proposed Private Equity Investment in Tenaska Power Fund II, L.P.”*

Mr. Shah of Strategic Investment Solutions said a proposed commitment of \$100 million to the Tenaska Power Fund II LP would be used toward primarily controlling acquisitions in a diverse group of power and energy-related companies and assets in the United States. Dr. Love noted such investments in transportation and distribution assets are typically not insured against natural or manmade disaster, an issue for the industry to resolve.

3. *Memorandum from Director Clark to the Council, dated February 13, 2008, entitled, “Proposed Hedge Fund Investment in Pershing Square II, L.P.”*

Mr. Stern of Cliffwater noted the proposed commitment of \$100 million to Pershing Square II, LP represented the first of several activist hedge funds to be brought to the Council. He noted the fund is a concentrated, deep-value fund focused on both long and short opportunities, with a bottom-up and highly intensive internal research process focused on themes and sectors. Director Clark noted the fund’s management would help the Division be more active on the corporate governance front by identifying where within the fund’s operations its corporate management could better perform, and that these lessons could be applied elsewhere in the portfolio.

4. *Memorandum from Director Clark to the Council, dated February 13, 2008, entitled, “Proposed Investments In Commodity-Linked Notes.”*

Director Clark said the proposed investment of up to \$500 million in one or more Commodity-Linked Notes (CLNs) is identical to the commodities proposal made to the Council a year ago. He said the Division was seeking authority now to buy CLNs whenever entry points seemed most advantageous to the portfolio.

B. For Action by the Council

- 1. Memorandum from Susan Sarnowski to the Council, dated February 14, 2008, entitled "Approval of Revisions to the State Investment Council Alternative Investments Policy and Procedures."*

Ms. Sarnowski reported that the proposed revisions represented the first update to the Council's alternative investments policy and procedures since the inception of the program in 2005, and were needed to ensure consistency with regulation changes, investment plans and the Division's current organization.

Dr. Love requested that a chart with allocation percentages be treated in separate detail as an appendix. Mr. Kandrac asked if the increase in proposed allocation of alternative investments within the policy from 13 to 18 percent was consistent with the Council regulations, and was told it was.

Director Clark said the updated document detailed the Division's due diligence process, and would be posted to the Division's website for public review immediately following the Council's adoption.

The Council approved the revisions unanimously on a motion by Dr. Love, seconded by Mr. Cerf. *(The revised Policies and Procedures were posted to the Division's website on February 22, 2008. The appendix is being drafted and will be posted at a future date)*

- 2. Memorandum from Director Clark to the Council, dated February 14, 2008, entitled "Approval of Proposed Changes to the State Investment Council Regulations for Filing with Office of Administrative Law."*

Ms. Sarnowski said the proposed amendments to Council regulations were necessitated by the investment plan approved by the Council at its January meeting. She said the primary amendments would: increase the maximum limitation on alternative investments to 28 percent, to allow some flexibility above the current plan for the future, and to bring the aggregate in line with the summation of the subcategories; expand the Division's ability to invest in additional alternative investment vehicles; and revise the categories within the absolute return strategy assets.

Mr. Kandrac questioned raising the maximum limit on alternative investments to 28 percent when the Council had just adopted policy revisions that raised the limit to 18 percent. Director Clark responded that the 28 percent in the proposed regulations set a ceiling and was sought for flexibility. He said the Council policy of 18 percent as just amended would continue to govern alternative investments until and if amended in the future by the Council. Mr. Kandrac asked and received confirmation that the proposed regulations would be subject to a public approval and comment process.

Chair Kramer recognized a member of the public who objected to a vote on the regulations without the quorum present reviewing the same material. He was told that the entire Council had received the entire package of regulations in advance; Mr. Claxton added by teleconference that he had his package in front of him.

Chair Kramer read the following resolution approving proposed amendments to N.J.A.C. 17:16-12, 43, 45, 46, 69, 71, 90 and 100:

“Be it resolved that the State Investment Council (the ‘Council’) hereby approves proposed amendments to N.J.A.C. 17:16-12, 43, 45, 46, 69, 71, 90 and 100. The Council hereby authorizes the Director of the Division of Investment to submit the attached proposals to the Office of Administrative Law for publication and public comments, and hereby delegates to staff of the Council and the Division of Investment the authority to make revisions to the proposal as required and as shall be made upon the advice of the Attorney General. This resolution shall take effect immediately.”

The resolution was approved by roll call vote, with ayes from Major Brown, Mr. Cerf, and Mr. Claxton, Mr. Kandrak, Chair Kramer and Dr. Love. There were no nays or abstentions.

(Teleconference participation by Mr. Claxton ended at this point)

C. *For the Information of the Council*

1. *Memorandum from Chief Administrative Officer Burrows Farber to the Council, dated February 13, 2008, entitled “Corporate Governance and Legislative Update.”*

Ms. Burrows Farber briefly reviewed highlights of the memorandum. Ms. Sarnowski said a consulting research provider to the Division had provided a list of companies qualifying for divestiture under the Iran legislation, and that the Division had written to each company and was now reviewing responses in preparation of a report due to the Legislature on March 4.

2. *Memorandum from Chief Administrative Officer Burrows Farber to the Council, dated February 13, 2008, entitled “Investment News Clips for February 2008 Council Meeting.”*

Memorandum noted with no discussion.

3. *Memorandum from Chief Administrative Officer Burrows Farber to the Council, dated February 13, 2008, entitled “Schedule of 2008 Meetings of the State Investment Council.”*

Ms. Burrows Farber noted that an annual meeting of the Council had been scheduled to follow the Council’s regular meeting on Thursday, October 16, in conformance with legislation passed in June 2007. The Chair recognized Ms. Roeder in the audience, who questioned whether the meeting was to be held in the spring, prior to the anniversary date of union contracts. Director Clark said the Division would check the law’s language, and added that the October date was chosen to permit more analysis of the previous fiscal year ending in June.

VIII. *Public Comment*

Two audience members who had submitted speaker request forms prior to the meeting were invited to address the Council.

John Strachan said he had 24 years of state service, and was part of a group attending Council meetings to ensure revenue for the pension was not used for non-pension related matters. He noted the state's failure to fully fund its obligation to the pension fund for several years and concern the state had overstated other contributions as reason for heightened concern about use of pension monies. Mr. Strachan questioned the Fund's sale of other equities in order to make major investments in Citigroup and Merrill Lynch, and the use of pension funds to provide start-up money for small businesses in New Jersey. He concluded that pension funds are not revenue, but represent an obligation.

Mr. Cerf said the Council shared employee concerns about contribution under funding by the legislature. Chair Kramer said the current Governor had reversed years of under funding with a \$1 billion contribution last year, and that the Council had also changed its strategy after years of lagging other public and private funds to increase investment diversification and reduce investment risk.

Rae C. Roeder, president of CWA Local 1033, commended the Council's concern for state shortfalls and the commitment of Division workers. She asked the Council for a statement to the legislature in support of full state funding, and asked the Council to assume a more proactive role in ensuring that a proposed early retirement incentive offered by the state not adversely deplete either the existing fund or the Investment staff. She offered her Local's commitment of support to the Council in both efforts.

Mr. Cerf said he did not see an advisory role for the Council on early retirement offers or other labor-related issues, and that such issues were beyond the Council's charter. A brief discussion followed in which several Council members agreed. Director Clark said early estimates showed the Division could lose 10-11 staff if an early retirement offer were made; he said in response to a question from the audience that the Division had not been approached about impacts of such an offer on the pension fund.

Mr. Cerf said in lieu of an appropriate position for the Council, he would write as an individual to his Senator requesting full funding for the pension fund, and urged others in the audience to do the same.

IX. *Presentation by Dr. Doug Love offering an analysis of actuarial accounting impacts on investment.*

Dr. Love summarized his participation in a recent meeting at New York University between the professional organizations that represent actuaries on pension disclosures, and the significance of the issue for pension fund investors and recipients. He noted that the opaque standards used for financial disclosures opened the door to morale hazard, and that while there was much defense of existing positions by both the research and practicing sides of the profession at the conference, the exchange had been helpful in building

consensus around the need for better standards. Dr. Love shared briefly his arguments of the past several decades in pushing for more transparency and said the audience could have faith in the generation of actuaries represented at the meeting. His was given a round of applause for his presentation and work on behalf of higher accounting standards.

X. *Communications*

There were no matters presented on behalf of the Acting Treasurer.

XI. *Next Meeting*

Thursday, 3/20/08

Noon: Lunch/1 p.m. Meeting

Rutgers Student Center
126 College Avenue, Room MPR-B
New Brunswick, NJ 08901

XII. *Adjournment*

All regular business of the Council being concluded, the meeting was adjourned by unanimous vote at 3:05 p.m.

Susan Burrows Farber
Interim Secretary to the Council