

**WASHINGTON STATE INVESTMENT BOARD**  
**Administrative Committee Meeting Minutes**  
**February 17, 2011**

The Administrative Committee met in open session at 8:30 a.m. in the boardroom at 2100 Evergreen Park Drive SW, Olympia, Washington.

Committee Members Present: Pat McElligott, Chair  
Treasurer Jim McIntire, Vice Chair  
Steve Hill  
George Masten  
Mike Ragan

Other Members Present: Bill Longbrake  
Richard Muhlebach  
David Nierenberg  
Judi Owens

Also Present: Theresa Whitmarsh, Executive Director  
Gary Bruebaker, Chief Investment Officer  
Victor Moore, Chief Operating Officer  
Liz Mendizabal, Public Affairs Director  
Steve Lerch, Research Director  
Celina Verme, Finance and Administrative Services Director  
Kristi Haines, Executive Assistant  
  
Chad Standifer, Assistant Attorney General

[Names of other individuals attending the meeting are listed in the permanent record.]

Chair McElligott called the meeting to order.

**ADOPTION OF THE DECEMBER 16, 2010, MINUTES**

**Mr. Ragan moved to adopt the December 16, 2010, Administrative Committee meeting minutes. Mr. Masten seconded, and the motion carried unanimously.**

## **NON-VOTING BOARD MEMBER CANDIDATE REVIEW**

Chair McElligott said the non-voting Board member vacancy has been open for the past month. Voting Board members discussed the performance of Messrs. Nakahara and Seely in executive session at its December meeting.

**Chair McElligott moved the Administrative Committee recommend the Board reappoint both Robert Nakahara and Jeffrey Seely as non-voting Board members for three-year terms beginning January 1, 2011, and ending December 31, 2013. Mr. Ragan seconded the motion.**

In response to Mr. Masten's question about whether other nominations were solicited, Chair McElligott said the information has been on the website and no new candidates were received. Chair McElligott said the incumbents have done a great job serving on the Board.

**The above motion carried unanimously.**

## **QUARTERLY BUDGET UPDATE**

Ms. Verme said the appropriated budget has a projected balance of \$1.3 million which represents an 8 percent savings. There was an adjustment of \$1.4 million to zero out the risk system proviso. The balance decreased \$285,000 from last quarter's projections. Staff believes the estimate is conservative and expects it to grow. The non-appropriated budget has a projected balance of \$42.4 million, which represents a 12.5 percent savings. This is an \$8.5 million increase from last quarter. The balance is expected to vary due to market volatility, asset values, investment contributions, distribution pace, and consulting needs. In response to Mr. Hill's question, Ms. Verme said the remaining balance goes back into the managed funds. Mr. Moore reported staff plans to do a one-time office reconfiguration to optimize space and reduce noise.

## **STRATEGIC PLAN**

Ms. Whitmarsh introduced the proposed 2011 strategic plan. She said staff developed a six-year plan in 2008 based on its vision at that time. The Board noted in its six-year plan that the investment environment has gotten more complex and traditional asset classes may not provide sufficient return going forward. The Board agreed to address the need to increase organizational capacity, focus on risk, maintain and attract highly skilled staff, and maintain conviction in its investment strategy through periods of underperformance. Ms. Whitmarsh announced staff will kick off a series of discussions with the Board today around the 8 percent return mandate in anticipation of the upcoming capital market assumptions decision in April.

Ms. Whitmarsh reviewed the budget requests developed in support of the long-range plan. In 2009-2011 budget, the WSIB gained an additional Investment Officer and funding for the risk system and real estate data integration services. In 2009, the economy changed and the state put a halt to spending; salaries were frozen, agency services were consolidated which resulted in a 0.5 FTE loss, and savings were used to reduce the budget in lieu of staff furloughs.

[Treasurer McIntire arrived at 8:40 a.m.]

In recognition of the state economy, the six-year budget plan was scaled back and the 2011-2013 budget was adjusted downward from the previously Board-approved amount. The upcoming biennial budget request includes a request for a Tangible Assets Senior Investment Officer, risks system analyst, and phone system upgrade. No salary increases were requested.

Ms. Whitmarsh said the goals to improve risk management and maintain the Board's commitment to its investment strategy are on track, though the challenge will be to maintain focus during periods of Board member turnover. Two goals face headwinds: increasing capacity under spending restrictions and attracting and retaining staff. Ms. Whitmarsh said markets are recovering faster than state revenue and the recruiting advantage the WSIB had during the market downturn has closed. She has had a number of Board member discussions around how to maintain the WSIB franchise and its outperformance.

Ms. Whitmarsh said strategies for 2011 were developed to address the challenges.

Staff will continue strategies to invest with the best managers, deepen relationships with those managers in which there is strong conviction, eliminate relationship with managers in which staff does not have the same level of conviction, and seek out new partners. But the state on which the strategies will be implemented is larger and more complex. There have been significant changes to the Commingled Trust Fund (CTF) geographic concentration over the past five years, with increased allocations to emerging markets and decreased investments in North America. Ms. Whitmarsh also compared travel to emerging markets countries from 2005 to 2010 which shows growth in trips to South and Central Americas, Asia, Australia, and the Pacific Islands. Staff expects that to continue.

Ms. Whitmarsh reviewed highlights from each of the asset class annual plans. Plans for Tangible Assets are somewhat on hold pending hiring of the Senior Investment Officer, although the single staff person assigned to Tangible Assets has done a good job monitoring the portfolio and seeking new opportunities. Staff discussed plans to create completion portfolios to gain exposure in resource equities. The strategy is propriety and different from what the WSIB has done in the past. Mr. Nierenberg spoke in support of staff's plan. He said it is a very cost effective way to make up for a deficit in composition of the overall portfolio, largely because of benchmark construction. Mr. Bruebaker described it as a temporary overlay. Staff plans to discuss the strategy further with the Public Markets Committee and its size would be limited to half a percent of the CTF. Ms. Whitmarsh said this is a good example of how staff operates creatively within its operational constraints.

Ms. Whitmarsh said the emphasis on risk over the past few years and implementation of the data warehouse and risks system will start producing more reports this year. There is also asset allocation work to do in the permanent funds, Guaranteed Education Tuition (GET) program, and Labor and Industries' (L&I) investment beliefs. Staff will also explore implications to the CTF of pension reform options, and conduct further policy analysis and research.

There are a number a pension stakeholder issues within the support area, including in-state investing, capital markets assumptions, and the WSIB value proposition—what the WSIB investing program brings in terms of economic benefit to the state. Ms. Whitmarsh relayed that

75 to 80 percent of the pension benefit comes from investment earnings, and most of the pension benefits are spent within Washington State. Mr. Hill said the Department of Retirement Systems' website includes data on pension benefits paid by county. Ms. Whitmarsh said staff will be monitoring GET discussions in the legislature, dealing with the permanent funds corpus issue, L&I premium increases, and financial regulatory reform and international proxy voting issues. Mr. Ragan said he would like education on Dodd-Frank—the Wall Street reform act. Mr. Hill suggested the session cover implications of the initiative rather than the details of it.

Ms. Whitmarsh said within the capacity area there are two approaches: to optimize within constraints or seek more flexibility and autonomy in budget and operations. Treasurer McIntire said it would be useful for the WSIB to think about how to characterize WSIB needs with policy makers. The WSIB needs to meet its investment return obligations and grow capacity in an environment of budget cutbacks and shrink-backs. Chair McElligott cautioned that the WSIB try not to look separate from the rest of state government. Mr. Moore said staff would be examining best organizational practices through participation in a new Cost Effectiveness Measurement study that will include U.S. and international participants. Staff plans to come to the July Board meeting with various approaches. The goal is to consider whether any approach should be brought forward during the 2012 legislative session. Mr. Masten encouraged staff to look outside of the U.S. for best practices. Mr. Hill suggested benchmarking against another entity that is not in the same industry is often useful at a macro level and to break down processes for best practice review. He encouraged staff to be innovative.

Ms. Whitmarsh said staff examined agency expenses in 2010 and plans to do deeper dives in 2011. It will also look at streamlining operations and making process improvements.

[Ms. Schurke arrived at 9:29 a.m.]

Other issues for 2011 include the accounting system approach, preparing for the custodial procurement in 2012, and dealing with tax issues in foreign markets. Staff is looking for a foreign tax consultant to assist in that area.

For Board initiatives, Ms. Whitmarsh said the *ad hoc* Governance Committee has met once and came up with a number of things to examine in Board operations, conduct, Board and Chair development, and selection. The goal is to bring preliminary work to the June Administrative Committee and full Board at its July meeting. Ms. Whitmarsh described proposed Board educational sessions include examining the 8 percent expected return and strategies that make a difference in the return. A Dodd-Frank educational session will be added.

Mr. Hill complimented staff's work. He wondered if there is current capacity to get all the tasks done. Chair McElligott and Treasurer McIntire agreed with the observation.

**Treasurer McIntire moved the Administrative Committee recommend the Board approve the 2011 Strategic Plan. Mr. Ragan seconded, and the motion carried unanimously.**

### **ASSISTANT ATTORNEY GENERAL'S REPORT**

Mr. Standifer reported on two items. The WSIB signed onto the Council of Institutional Investors' amicus brief supporting the Securities and Exchange Commission's rule on proxy voting access which the U.S. Chamber of Commerce and Business Roundtable seeks to overturn. Also, there was a recent development in the Lehman Brothers ongoing litigation filed in May 2009 to recover \$100 million in losses on Lehman notes. The WSIB was invited by a group of insurers to participate in settlement negotiations on one portion of the litigation involving former Lehman executives and directors. The Attorney General's Office has authorized the outside attorney to participate in that discussion. The amount of the recovery may be limited.

### **OTHER ITEMS**

There was no further business to come before the Committee, and the meeting adjourned at 9:37 a.m.