

WASHINGTON STATE INVESTMENT BOARD

Board Meeting Minutes

March 20, 2003

The State Investment Board met in open public session at 9:34 a.m. in the boardroom at 2100 Evergreen Park Drive SW, Olympia, Washington.

Present: John Charles
Glenn Gorton
Charlie Kaminski
John Magnuson
George Masten
Patrick McElligott
Mike Colleran (for Treasurer Murphy)
Bob Nakahara
Lee Ann Prielipp
Paul Trause
Debbie Brookman
Jeff Seely

Absent: Senator James West
Representative Helen Sommers
Jeffrey Hanna

Also Present: Joe Dear, Executive Director
Gary Bruebaker, Chief Investment Officer
Sue Hedrick, Executive Assistant
Nancy Calkins, Senior Investment Officer, Public Equity
Beth Vandehey, Internal Auditor
Steve Draper, Senior Investment Officer, Real Estate
Tom Ruggels, Senior Investment Officer, Private Equity
Bill Kennett, Senior Investment Officer, Fixed Income
Diana Will, Investment Officer
Alicia Markoff, Portfolio Administrator
Linda Lester, Investment Officer
Dino Patiag, Client Relationship Officer for State Street Bank

Evelyn Lopez, Senior Assistant Attorney General
Jeff Lane, Senior Assistant Attorney General
Paul Silver, Assistant Attorney General

[Names of other individuals attending the meeting are not included in the minutes, but are listed in the permanent record.]

Chair Charles called the meeting to order and identified the members in attendance.

ADOPTION OF MINUTES – FEBRUARY 20, 2003

Ms. Prielipp moved to adopt the Board minutes of February 20, 2003. Mr. McElligott seconded.

Mr. Kaminski suggested one change to the minutes. On page 12, he asked that the sentence at the top of the page read, "Mr. Murphy asked if these were 2a-7 type funds. Mr. Kaminski said yes, some were. Some are not and can invest in instruments with maturities of up to 18 months."

The minutes, as corrected, were approved.

Evelyn Lopez, Senior Assistant Attorney General, introduced Paul Silver who will be transitioning into the position of counsel to the WSIB. Mr. Silver is currently the Division Chief of the Consumer Protection Division at the Attorney General's Office. Ms. Lopez indicated that Jeff Lane, the Board's current counsel, has more than 36 years with the state and could retire at any time, if he so chose. Mr. Lane will remain involved with the WSIB, but will also take on other duties as well.

PUBLIC COMMENT

Marguerite Young, senior pension fund organizer with the Service Employees International Union (SEIU) Western Region, addressed the Board on the Economically Targeted Investments (ETI) policy. She said the SEIU represents 15,000 public sector members in Washington State who are participants in the Washington State retirement system, and the union is concerned about the security of its members' retirement. The union also represents 35,000 workers in the health care and building services sectors whose livelihoods depend on a healthy economy in the state of Washington.

Ms. Young said they appreciate the Board's long history of support for and investment in Washington-based businesses. They believe a pro-active, explicit policy on how to approach ETI is a good way to promote the long-term health of the state's economy and well-being, and also ensures the security of the retirement savings invested in the state employee retirement system.

She reiterated the recommendations she suggested in comments submitted to the WSIB on March 7. Ms. Young said it is important to dedicate staff to the review of appropriate investment opportunities, and encouraged the staff to look at all sectors of the Washington economy, not just technology. Secondly, she encouraged staff to identify and analyze potential investment opportunities on an ongoing basis, and present that work to the Board annually. The staff should prepare a report for the Board that reviews the ETI practices and policies developed by other states. She referenced a California Investment Focus report produced by CalPERS, and indicated she would send copies of the report to the Board members to review. Lastly, she encouraged the Board

She referenced a California Investment Focus report produced by CalPERS, and indicated she would send copies of the report to the Board members to review. Lastly, she encouraged the Board in the future to develop a proactive ETI policy for each asset class, including strategic objectives, collateral benefits, target program sizes, and standards of evaluation.

ADMINISTRATIVE COMMITTEE REPORT

Economically Targeted Investments (ETI)

Chair Charles said that the Administrative Committee met just before the Board meeting and discussed the ETI draft. The Committee recommends adoption of the policy with one addition at the very end of the policy with regard to staff responsibilities. Mr. Dear read the addition. On Page 3, under “Responsibilities”, Number 2, after “responsible for” the following was inserted, “facilitating exchange of information between its private equity general partners, and appropriate parties with knowledge of quality in-state investment opportunities,” and then the rest of the sentence follows.

Chair Charles moved the motion, Mr. Masten seconded it.

Chair Charles said that the draft they were considering is very similar to the draft that was considered by the Board at the last meeting. There were only some minor housekeeping changes made by staff.

The motion to approve the policy, as amended, carried unanimously.

Chair Charles said that the second item that came before the Committee was Engrossed Substitute Second Bill 5192. Mr. Dear gave a summary of the bill as passed by the Senate. He said the bill contains several flaws that conflict with the trustees’ fiduciary duties, and it also makes changes to the make-up of the Board. Bill Song, the WSIB’s fiduciary counsel, reviewed the bill and determined that Section 2, which involves the prudent person and prudent investor standard, is flawed and would need to be rewritten.

Mr. Dear said the bill would add two new members to the Board – the Governor or his designee, and a local government representative, and create a statutory Audit Committee. The bill would also change the terms of the non-voting members from three years to two, and make their removal not subject to cause. He also said the description of the representation would create ambiguity about the fiduciary duties of some members. He noted that proponents of the bill have been responsive to requests for changes.

Mr. Charles said he also met with the Chair of the House Financial Institutions and told her there are a number of changes that need to be made to the bill. Otherwise, the Board would not support it. Mr. Charles said the Chair indicated she does not have any intention of pushing through a bill that is not supported by the Board.

Chair Charles moved that the Board accept the recommendation of the Administrative Committee and take a position in opposition to ESSB 5192. Ms. Prielipp seconded.

The motion passed unanimously.

Chair Charles also reported that the Administrative Committee approved a work request through the Department of General Administration to find a contractor to do an administrative review of certain WSIB operations.

**AUDIT COMMITTEE REPORT
INTERNAL AUDIT 2003-03, CUSTODIAN BANK**

Mr. Masten moved that the Audit Committee recommend that the Board accept Internal Audit 2003-03, Custodian Bank. Mr. Collieran seconded.

Beth Vandehay, the internal auditor, briefly spoke to the audit.

The motion passed unanimously.

DAILY VALUED FUNDS OPERATIONS POLICY DRAFT 2.14.300

Mr. Masten moved that the Audit Committee recommend that the Board adopt Daily Valued Funds Operations Policy 2.14.300. Ms. Prielipp seconded.

Alicia Markoff, WSIB portfolio administrator, described the changes that were made to the policy.

The motion passed unanimously.

PROXY VOTING POLICY REVISION 2.05.200

Mr. Masten moved that the Board approve the revisions to Proxy Voting Policy 2.05.200. Ms. Prielipp seconded.

Gary Bruebaker spoke to the changes that were made to the policy. He said that the policy incorporates adoption of the Council of Institutional Investors (CII) proxy voting principles and core policies by reference. He said this would eliminate the necessity of the Audit Committee taking action every year when the CII updates its proxy voting principles and core policies.

The motion passed unanimously.

PUBLIC MARKETS COMMITTEE REPORT

Mr. Kaminski said the Public Markets Committee met on March 3 and received a portfolio review report from the Fixed Income Unit. The Committee also began a series of educational sessions over the next few months that will result in a review of the structure and management of the international equity program. He urged the other board members to attend future Public Markets Committee meetings, if possible.

Mr. Kaminski noted that the Plexus Group presented "Transition 101", followed by Barclays Global Investors (BGI) and State Street Global Advisors (SSgA) who presented a specific case study based on a transition from the Wilshire 5000 to the Russell 3000. Staff from the Frank Russell Company provided a wrap-up. A standard periodic report was also presented by Plexus.

PRIVATE MARKETS COMMITTEE REPORT

Mr. Masten said there was nothing to report.

EXECUTIVE STAFFS' REPORT

Executive Director's Report

Mr. Dear distributed his monthly report. He said the Investment Seminar will be held on May 15 and 16. There will be a make-up session in the future for those members who cannot attend in May.

Mr. Dear listed eight policy areas that will be reviewed by Cortex Applied Research, and will be worked on at the July 31-Aug 1 Board workshop.

In terms of legislation, he mentioned there are three four bills he has been following: Engrossed Substitute Senate Bill 5192, which has been amended and sent to the House for consideration; House Bill 1766, which died; Substitute House Bill 2197, which implements the provisions of I-790 and also appears to be dead, and House Joint Memorial 4011, which passed the House. Mr. Dear said he continues to meet with legislators on an ongoing basis.

Monthly Investment Reports

Mr. Bruebaker provided the February monthly performance report. Domestic Public Equity is down 1.7 percent while International Equity is down 2.2 percent. The only positive side is that this month is less negative than last month. Fixed Income is the only bright spot, up 2.2 percent for the month, 78 basis points above the benchmark. We outperformed in all major sectors; government, credit as well as securitized.

Real Estate is down 0.8 percent. We still have positive returns for all of the longer time periods, the one-, three- and five-year period. Private Equity is down 0.3 percent. For the month, we closed on Evercore. The draws are up, at \$156 million for the month of February. That's compared to \$67 million last month and an average over the last year of about \$102 million. Distributions are at \$43 million for the month. That's compared to \$22 million last month, but that's still below the average that we had for the year. For the assets under management, we're down \$422,000. The most significant changes this month are that the CTF is down \$235 million, but the Labor and Industries

(L&I) funds are up \$214 million. The L&I funds are up for two reasons, new cash coming into the organization as well as an outstanding performance in fixed income. In fact, the Accident Fund is up almost 300 basis points for the month.

Looking at the long-term asset allocations, Fixed Income and Real Estate combined, the range is 31 to 43 percent, and they're at 39.6 percent, solidly in the middle of the range, and all other asset classes are also within range for their targets. In the capital market environment, the Wilshire 5000 is down 1.3 percent. For the capital markets, everything is down except the Lehman Universal. Month-to-date, the Wilshire is actually up 3.69 through yesterday, and the ACWI Free Ex U.S. is down .16 percent. The Lehman Universal, the only thing positive for the month of February, the fiscal year and the one-year, is down .75 percent so far this month.

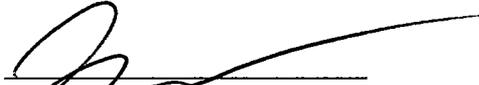
Mr. Seely raised a concern about the Board's holdings in HealthSouth. Mr. Bruebaker responded that staff will look into this matter and report back on it.

ASSISTANT ATTORNEY GENERAL'S REPORT

Mr. Lane indicated that he did not have a report for this meeting.

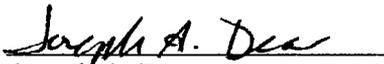
Chair Charles distributed the Department of Retirement Systems' Summary Annual Financial Report. The report provides an overview of the department's services, funding and investment information, highlights of the retirement plans and a summary of the past year's achievements. Mr. Charles said he wanted the Board members to have an opportunity to see it before it was distributed to the general public.

There being no further business to come before the Board, the meeting adjourned at 10:34 a.m.



John Charles
Chair

ATTEST



Joseph A. Dear
Executive Director