WASHINGTON STATE INVESTMENT BOARD
Board Meeting Minutes
November 17, 2005

The Washington State Investment Board met in open public session at 9:30 a.m. in the boardroom at 2100 Evergreen Park Drive SW, Olympia, Washington.

Present:	Pat McElligott, Chair Debbie Brookman, Vice Chair Senator Lisa Brown Assistant Treasurer Mike Colleran Glenn Gorton Charlie Kaminski John Magnuson George Masten Sandy Matheson Bob Nakahara Dave Scott Jeff Seely Representative Helen Sommers
Absent:	Gary Weeks
Also Present:	Joe Dear, Executive Director Gary Bruebaker, Chief Investment Officer Tom Ruggels, Senior Investment Officer – Private Equity Steve Draper, Senior Investment Officer – Real Estate Kristi Walters, Executive Assistant Paul Silver, Assistant Attorney General Tara Blackburn, Pacific Corporate Group George Roberts, Kohlberg Kravis Roberts and Co. Mike Michelson, Kohlberg Kravis Roberts and Co. Mike Heale, Cost Effectiveness Measurement Inc. Ann Yerger, Council of Institutional Investors

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

Chair McElligott called the meeting to order and roll call was taken.

ADOPTION OF MINUTES – SEPTEMBER 15, 2005

Vice Chair Brookman moved to adopt the September 15, 2005, Board minutes. Mr. Gorton seconded the motion.

Mr. Magnuson noted corrections on page 13 that motions were made by Mr. Gorton, not Mr. Glenn.

The motion to adopt the corrected minutes carried unanimously.

PUBLIC COMMENT

There was no public comment.

QUARTERLY PERFORMANCE REPORTS

Mr. Bruebaker provided the quarterly reports for the commingled trust fund (CTF), defined contribution plans, daily priced investment options, Labor and Industries' funds, and Permanent and Other Trust Funds for the periods ended September 30, 2005.

[Representative Sommers was in attendance at 9:34 a.m.]

WSIB Managed Funds

Commingled Trust Fund

The CTF was at $49.3 billion, up $1.9 billion for the quarter. Performance for the quarter was up 4.9 percent. The fund outperformed its benchmark for the 1-, 3-, 5- and 10-year periods. Mr. Bruebaker pointed out issues with comparing fund performance against the TUCS, which is not a benchmark and does not consider risk. Mr. Colleran acknowledged the issues with TUCS but said that TUCS is a standard comparison and is important from OST's viewpoint.

U.S. equity was at $15.8 billion, up $200 million. It outperformed its benchmark by 2 basis points (bps) for the quarter. It also outperformed the benchmark in all periods. International equity was at $8.7 billion, up $900 million. It underperformed its benchmark by 33 bps for the quarter. It also underperformed for the 3- and 10-year periods, but outperformed for the 1- and 5-year periods.

For the quarter, fixed income was at $12.3 billion, which was unchanged from the previous quarter. It outperformed its benchmark by 41 bps for the quarter due to its short duration, governments, TIPs exposure, and CTF credits. Fixed income outperformed for all periods.

Defined Contribution Plans

For the quarter, the Teachers Retirement System Plan 3 was at $2.7 billion, up $153 million. The School Employees Retirement System Plan 3 was at $758 million, up $37.6 million. The Public Employees Retirement System Plan 3 was at $984 million, up $47 million.

The Deferred Compensation Program was at $2 billion, up $100 million for the quarter. The Judicial Retirement Account was at $15 million, up $900,000 for the quarter.

The Bond Market Fund outperformed for the quarter by 34 bps, due to its shorter duration, TIPS, and credits. The Money Market Fund was down by 4 bps. The TAP Fund outperformed by 89 bps for the quarter. The Short-, Mid-, and Long-Horizon Funds all outperformed for the quarter and 1-year periods. The Socially Balanced Fund was down by 82 bps. It was hurt by being underweight in the energy sector and due to its emphasis on higher quality financial stocks.

The Equity Income Fund outperformed by 20 bps, the Independence Fund outperformed by 390 bps and the Growth Company Fund outperformed its benchmark by 319 bps. The U.S. Stock Market Index was up by 3 bps, the U.S. Stock Fund was up by 5 bps, the U.S. Large Stock Fund was even, and the U.S. Small Stock Fund was up by 13 bps. The Active International Fund was up by 22 bps, while the Passive International Fund was down by 2 bps for the quarter.

Daily Priced Investment Options
Mr. Bruebaker said that the components of the daily priced investment options were included in the defined contribution plans' report.

Labor and Industries' Funds
The Labor and Industries' Funds were at $10.3 billion, same as the previous quarter. Its performance beat every one of the CMIs, with shorter duration and CMOs helping all funds. Mr. Bruebaker reminded the Board that the CMIs are a comparison but not a true benchmark.

Permanent and Other Trust Funds
The Permanent and Other Trust Funds had a great quarter. All of the Permanent Funds outperformed the benchmark for the quarter. Mr. Bruebaker reminded the Board that the funds are not managed on a total return basis.

The Guaranteed Education Tuition portfolio was at $576.6 million, up $28.4 million for the quarter. All asset classes were within their policy ranges. It outperformed by 10 bps for the quarter.

The Developmental Disabilities Endowment Fund state portfolio was at $6.9 million, which was the same as the previous quarter. All assets were within their policy ranges. The private funds portfolio was at $3.8 million, up $592,000 for the quarter. The state funds outperformed by 10 bps and private funds outperformed by 130 bps for the quarter.

Private Equity
Mr. Ruggels introduced Tara Blackburn of Pacific Corporate Group (PCG), the Board's private equity consultant. Ms. Blackburn presented the private equity funds quarterly report for the period ended June 30, 2005.

Ms. Blackburn said that it was a big quarter in terms of commitments authorized, and closing of previously authorized commitments. There were $529.1 million in contributions, which represents a 75 percent increase from the previous quarter. Distributions were also strong at $573.7 million for the quarter. The net portfolio appreciation was almost $630 million, which is the second highest gain since PCG began working with the WSIB. She noted that the portfolio is self-funding at this time.

Mr. Colleran asked Ms. Blackburn to comment on a recent New York Times article about valuations. She said that the focus has clearly been the availability of cash and the amount of cash coming into the market. General partners whom she has spoken with say that valuations are full.

Mr. Ruggels said that the main drivers on the buyout side are: 1) the enormous amount of cash flowing into the market and 2) extremely aggressive financing markets. He noted that 2 or 3 years ago it was difficult to finance a buyout deal; now, financing is very aggressive. If the high yield market goes away or the banks start tightening up, it could be a different story. In response to Mr. Kaminski's question, Mr. Ruggels said that the amount of leverage on deals has been going up in a meaningful way.

Ms. Blackburn said that the KKR portfolio appreciated by 5.2 percent, and the LP portfolio appreciated by 10.5 percent for the quarter. The portfolio internal rate of return (IRR) since inception increased by 30 bps, from 14.0 percent to 14.3 percent. There were six commitments closed during the second quarter. She said that the WSIB's active investments are maturing and the growth in IRR was driven by funds that had strong appreciation, such as First Reserve, Fortress, and the KKR Millennium and European funds.

Ms. Blackburn reported that subsector allocations are within their target ranges. She noted that, at the portfolio company level, international represents one-third of the portfolio, versus 20 percent as shown in the allocation chart. The 20 percent is the percentage of the portfolio invested in funds that invest primarily outside the U.S. She reported that the program continues to be well diversified across industries.

Ms. Blackburn reported that the portfolio outperformed its benchmark on a 1-, 3- and 5-year basis. Within the sub-sectors, small/medium corporate finance, international, distressed and direct secondaries have been the top performers for the 5-year period. Large corporate finance and venture capital have performed best over longer periods.

In response to questions from Mr. Kaminski and Ms. Matheson, Ms. Blackburn said that Canada and emerging private equity markets without enough capital supplied to them, such as South Africa, Central Europe, and mid-market Europe, may present some interesting investment opportunities. Finding inefficiencies in the marketplace is the key. Ms. Blackburn commented on valuations, the enormous supply of capital across the market, and the number of companies within the market to absorb the capital. Mr. Ruggels said a large portion of the additional capital flowing into private equity is from outside the U.S.

Mr. Colleran noted the negative 12.5 return for venture capital over the 5-year period. Ms. Blackburn explained some of the reasons for poor returns in this area, but said she would need to look at the specific factors driving these numbers in the WSIB portfolio.

In response to Mr. Masten's question about the number of high net worth individuals invested in private equity compared to institutional investors, Ms. Blackburn said that the industry is seeing more participation by wealthy individuals, but the percentage is very small.

Real Estate

Mr. Draper reported on the real estate portfolio performance through June 30, 2005. The portfolio market value was at $4.4 billion, representing 9.3 percent of the CTF. The net returns were 24.1, 15.1, 13.6 and 16.3 percent for the 1-, 3-, 5- and 10-year periods respectively, which beat the gross returns of NCREIF over the same periods by 610, 300, 300, and 490 basis points. He said that the WSIB is benefiting from the excellent returns of its large investments and investments made years ago are paying off.

Mr. Draper said that Hometown America experienced exceptional returns with a relatively lower risk strategy; Principal Enterprise Capital had outstanding returns driven primarily by investments in California; and Lone Star continued its outstanding performance. He said that PacTrust, the longest standing real estate relationship of the WSIB, has been very steady with a high income component to returns. Other solid performers included Washington Holdings and Corporate Properties.

Mr. Draper reviewed property type diversification. He said that the portfolio was underweight in retail and overweight in residential due to its manufactured housing investment. He reviewed the geographic diversification, which is underweight in the East, and overweight in the South and West as well as internationally, consistent with the WSIB's strategy.

Overall, real estate continues to be subject to remarkable capital inflows, resulting in highly competitive asset pricing; the WSIB's partners continue to exhibit excellent underwriting discipline; and performance is good, with long-term partners exceeding expectations.

[The Board recessed at 10:38 a.m. and reconvened in open public session at 10:48 a.m.]

KKR ANNUAL PRESENTATION

Mr. Roberts and Mr. Michelson presented Kohlberg Kravis Roberts and Company's (KKR's) annual report to the Board. Mr. Roberts said that KKR has been in business for 30 years and began with $120,000. Since that time, KKR has completed over 130 transactions with a total value of over $165 billion within 25 different industries. The firm creates value by improving businesses and helping to manage businesses as a partner. He said that KKR has a simple operating philosophy: organizations that let the best people do their best work are organizations that will thrive.

Mr. Michelson said that the WSIB has been a leading investor with KKR since 1982, having invested $3.3 billion in its funds. KKR has returned $5.3 billion in realized proceeds, created $3.9 billion in profits, and generated a 20 percent IRR and a 2.2x multiple on invested capital for the WSIB.

Mr. Michelson provided an overview of KKR operations and reviewed their experience in completing large transactions. He reviewed KKR's strategy, competitive advantages, experience, team, internal processes, and industry expertise. Mr. Michelson provided examples of KKR's theme-based investing and reviewed its 2004 and 2005 investments.

Mr. Michelson reviewed the WSIB's overall returns within KKR funds since inception to September 30, 2005. KKR has consistently outperformed the market indices by 700 bps. He reviewed the amount in each KKR fund that the WSIB has invested, totaling $3.3 billion, of which KKR has returned $5.3 billion. He provided details on the fund returns and market indices of the KKR 1996, European, and Millennium funds.

A review of the historical 10-year cash flow shows contributions of $2.5 billion, distributions of $4.8 billion, and a net cash flow of $2.3 billion since 1995. Details on 2004 distributions were provided. Mr. Michelson provided an update on recently announced pending exits and gave status of unfunded commitments. He reported that the KKR European Fund II closed at €4.5 billion and provided a breakdown of the types of limited partners represented in the fund.

Mr. Roberts said that KKR is constantly thinking of ways it can improve. It distinguishes itself by the people in its organization. He said that KKR recently hired two new principals. KKR believes that people make a difference and that is what they invest in. Mr. Roberts responded to questions from the Board regarding two recent departures from the firm, KKR's interest in investing in Asia, and the environment that created larger initial returns than anticipated in recent investments.

ASSET ALLOCATION POLICY REVISION AND IMPLEMENTATION PLAN

Mr. Bruebaker introduced the revised Retirement CTF Asset Allocation Policy 2.10.050. The major change in allocation moves the target midpoint of U.S. equity from 31 to 23 percent, and increases the international equity allocation by a like percentage. The portion deployed for international developed markets will go to existing managers. The portion allocated for emerging markets will be tied in with the Request for Proposal (RFP) process for additional international equity emerging managers. This transition should be completed by March 31, 2006. Mr. Bruebaker said that interim allocation targets have been established through 2009 for real estate and private markets when they are expected to be fully funded.

Mr. Bruebaker explained the changes to the blue-lined policy, which include housekeeping changes and removal of redundancies. He said that the changes made within the Background section regarding the introduction of defined contribution features do not change the fact that the fund is still long-term in nature. A review of liabilities is added to the policy as this has been a part of the allocation process since 2001. The frequency of a formal asset allocation review is restated to occur every four years instead of using a range of every three to four years to be more specific. He noted that the Board can review the allocation as often as they deem necessary. The major policy change is the allocation targets on pages 2 and 3, which reflects action taken by the Board at its September meeting. Mr. Bruebaker said that section 3, on page 3, contains the interim year-end targets for the asset classes through 2009, and the changes on page 4 make it clear that staff has the ability to hire overlay managers to assist with transitions and rebalancing. Mr. Bruebaker said that a discussion of overlay manager(s) is planned in early 2006 with the Public Markets Committee. The policy reflects the Board's decision made two years ago to take asset allocation decisions directly to the Board, instead of the Administrative Committee. An implementation value added section is included, which provides for a custom benchmark that is a better measurement of WSIB performance identifying the return due to manager over or underperformance and staff's allocation decisions. He said that staff's goal is to provide the Board with a quarterly investment report the month following the quarter end. TUCS would not be available at that point, but TUCS information would be provided to the Board when it becomes available.

Mr. Nakahara said that he is pleased with the change in language concerning the formal review, but asked what best practices dictate concerning how often the asset allocation should be reviewed. Mr. Bruebaker responded that the Board reviews its asset allocation every month and discusses it annually at the Board retreat. A formal analysis will occur every four years, but it can be done more frequently. He said he feels this is a best practice.

Vice Chair Brookman moved that the Board approve the asset allocation implementation plan and the changes to the Retirement CTF Asset Allocation Policy 2.10.050. Mr. Gorton seconded the motion.

Mr. Masten asked if policy changes always come direct to the Board for approval. Mr. Bruebaker replied that the Board had decided during its 2003 governance review to have all asset allocation decisions come directly to the Board.

The above motion carried unanimously.

ADMINISTRATIVE COMMITTEE REPORT – EXECUTIVE DIRECTOR COMPENSATION

Chair McElligott reported that the Administrative Committee met just prior to the Board meeting to discuss the executive director's compensation. The Committee reviewed salary survey data for executive director compensation and is recommending a median salary level.

Chair McElligott moved that the Board accept the Administrative Committee's recommendation to increase the executive director's annual salary to $191,180 effective December 1, 2005. Vice Chair Brookman seconded and the motion carried unanimously.

PRIVATE MARKETS COMMITTEE REPORT – INVESTMENT CONSIDERATIONS

Private Equity

Nordic Capital VI, L.P.

Vice Chair Brookman reported that the Private Markets Committee met on November 3 and discussed four investment recommendations.

The Private Markets Committee recommends an investment of up to €150 million in Nordic Capital Fund VI, L.P. The recommendation is based, in part, on the following: the investment team is strong and experienced, with substantial industry operating experience to complement their financial expertise; Nordic Capital will continue its successful investment approach, focusing on investments in the Scandinavian countries of Sweden, Norway, Finland, and

Denmark; the firm has the ability to execute complex transactions, including industrial combinations, "leveraged partial dispositions" where the seller retains an equity stake, and leveraged buildup; the team has an excellent long-term track record, with a cumulative 50.6 percent net IRR on €2.26 billion invested since 1990 in five prior funds; the fund's middle-market focus in the Nordic region is complementary to other European partnerships in the WSIB portfolio that focus on different countries and larger transactions; and the investment is an opportunity to expand a successful, long-term relationship with a high-quality general partner. Vice Chair Brookman said that staff and Pacific Corporate Group each originally recommended a commitment to the fund in the amount of €125 million. However, based on the high quality of the opportunity, the unique fit in the portfolio, and the successful long-term relationship with Nordic Capital, members of the Private Markets Committee indicated a desire to increase the recommended commitment to €150 million. Both staff and PCG indicated that they are comfortable with the recommendation of the higher amount.

> **Vice Chair Brookman moved that the Board approve the Private Markets Committee's recommendation to approve an investment of up to €150 million, plus fees and expenses, in Nordic Capital Fund VI, L.P., subject to continued due diligence and final negotiation of terms and conditions. Mr. Masten seconded and the motion carried unanimously.**

Avenue Special Situations Fund IV, L.P.

Vice Chair Brookman reported that the Private Markets Committee recommends an investment of up to $100 million in Avenue Special Situations Fund IV, L.P. The recommendation is based, in part, on the following: the investment team is deep and experienced; the 25 investment professionals collectively have over 270 years of relevant distressed investing experience, with complementary backgrounds and expertise. The two partners and the senior portfolio manager each have 19 or more years of relevant experience. The team has a strong track record; since 1998, the firm has invested $7.3 billion with aggregate commitments of $1.55 billion across three prior funds, producing an aggregate net IRR of 19.9 percent, including $7.3 billion in realizations. The loss ratio has been a very low 1.1 percent. The proven investment strategy has allowed Avenue Capital Group (ACG) to produce attractive returns with a lower risk profile. The firm's focus on senior debt and its expertise in trade claims lending are differentiating. This opportunity is an excellent portfolio fit as the distressed sub-class is currently at the low end of the established range in the portfolio. In addition, ACG's investment strategy is complementary to the strategies of the WSIB's other distressed managers.

> **Vice Chair Brookman moved that the Board accept the Private Markets Committee's recommendation approve an investment of up to $100 million, plus fees and expenses, in Avenue Special Situations Fund IV, L.P., subject to continued due diligence and final negotiation of terms and conditions. Mr. Masten seconded and the motion carried unanimously.**

Real Estate

Fillmore East Fund, L.P.

Vice Chair Brookman reported that the Private Markets Committee recommends an investment of up to $50 million in Fillmore East Fund, L.P. The recommendation is based, in part, on the following: Fillmore Capital Partners (FCP) investment team has become a major player in structured finance. The team maintains excellent market connections, receiving the opportunity to pursue most meaningful transactions in hospitality and health care property structured finance that reach the market. This investment is an opportunity for attractive risk-adjusted returns; income yields on structured finance investments, in general, are currently higher than those on pure equity investments. Therefore, on a risk-adjusted basis, structured finance investments are very attractive, given the high-income component. The WSIB staff has had a positive relationship with Ron Silva for over 8 years. Mr. Silva and the FCP team have always been responsive and reporting has been thorough, particularly involving transaction underwriting. FCP focuses on sectors of the real estate market that receive less attention and capital than the primary property types and generally have a significant operating component to them (hospitality, health care, etc. rather than office, industrial, retail, multifamily). These sectors generally require a high level of specific expertise and, therefore, competition is less severe. The track record of FCP's team shows a consistent ability to source, underwrite, and manage quality structured finance investments. The net IRR of the FCP team's investments on behalf of the WSIB is an unleveraged 13.5 percent. FCP's track record on behalf of other investors is an aggregate net IRR of 13.7 percent.

> **Vice Chair Brookman moved that the Board accept the Private Markets Committee's recommendation to approve an investment of up to $50 million, plus fees and expenses, in Fillmore East Fund, L.P., subject to continued due diligence and final negotiation of terms and conditions. Ms. Matheson seconded and the motion carried unanimously.**

Fillmore Strategic Investors, LLC

Vice Chair Brookman reported that the Private Markets Committee recommends an investment of up to $350 million in Fillmore Strategic Investors, LLC. The recommendation is based, on part, on the same factors noted for Fillmore East Fund in addition to the following: the WSIB will have excellent governance rights, including the ability to remove the managing member with or without cause; Fillmore Strategic Partners will be created between the WSIB and Fillmore's management team to capture transactions that fall outside the mandate of the Fillmore East Fund. The Fillmore East Fund has limitations regarding deal size, property type diversification, and leveragability. It is also limited to certain parts of the capital structure, perhaps leaving either less risky or riskier transactions available for investment. Fillmore Strategic Investors will invest in these opportunities, thus encapsulating all of the investment ideas of the Fillmore management team.

> **Vice Chair Brookman moved that the Board accept the Private Markets Committee's recommendation to approve an additional investment of up to $350 million, plus fees and expenses, in Fillmore Strategic Investors, LLC,**

subject to continued due diligence and final negotiation of terms and conditions. Mr. Scott seconded and the motion carried unanimously.

[Senator Brown was no longer in attendance at 11:59 a.m.]

AUDIT COMMITTEE REPORT

Internal Audit Report 2005-04, Public Equity International Managers

Mr. Masten reported that the Audit Committee met on November 1. It heard an audit report on the public equity international managers. Three active managers, Capital Guardian, William Blair, and LSV Asset Management were selected for audit, representing each of the portfolio styles: core, growth & value, respectively.

There were no audit findings. However, observations were made during the audit relating to best industry practices. The executive director and chief investment officer will follow-through with top management of the firms to communicate audit suggestions.

Mr. Masten moved that the Board approve the Audit Committee's recommendation to accept Internal Audit 2005-04, Public Equity International Managers. Mr. Scott seconded and the motion carried unanimously.

Conflict of Interest Compliance Review

Mr. Masten reported that the Assistant Attorney General provided the annual report on conflict of interest compliance. Reporting of gifts, investments made, travel paid for by external sources, and statements of financial affairs from 2004 were reviewed. Mr. Silver found that Board members and staff are in compliance with the Board's Conflict of Interest Policy and with the Ethics in Public Service Law.

Mr. Masten moved that the Board approve the Audit Committee's recommendation to accept the 2004 Conflict of Interest Compliance Review report. Vice Chair Brookman seconded and the motion carried unanimously.

Nonvoting Board Member Candidate Recommendation

Mr. Masten reported that the Committee interviewed candidates for the vacant nonvoting Board member position created by Jeff Hanna's recent departure. One candidate initially selected for an interview withdrew, and staff brought forward an alternate candidate. The Committee interviewed David Nierenberg, Joseph Sasenick, and Al Symington. Following the interviews, the Committee went into executive session to discuss the candidates' qualifications. The Committee selected David Nierenberg as its recommendation to the Board.

Mr. Masten moved that the Board approve the Audit Committee's recommendation to appoint David Nierenberg to fill the remaining term of the vacant nonvoting Board member position until December 31, 2005, and

for a three-year term ending December 31, 2008. Mr. Scott seconded and the motion carried unanimously.

Chair McElligott said that Mr. Nierenberg would take the oath of office at the December meeting.

[The Board recessed at 12:12 p.m. and reconvened in open public session at 12:35 p.m.]
[Ms. Matheson and Mr. Nakahara were no longer in attendance at 12:35 p.m.]

COMMITTEE ASSIGNMENTS

Chair McElligott said that he contacted each member regarding Committee assignments. After these discussions, he decided to ask that the Board move him from the Private Markets Committee to the Public Markets Committee. He said that he is also recommending that Mr. Masten serve as the Private Markets Committee Chair, replacing Vice Chair Brookman.

Chair McElligott moved that the Board approve his recommendation to move him from the Private Markets Committee to the Public Markets Committee, move Mr. Masten from the Public Markets Committee to the Private Markets Committee and appoint Mr. Masten as the Private Markets Committee Chair, and appoint Mr. Nierenberg to the Private Markets and Public Markets Committees. Mr. Scott seconded and the motion carried unanimously.

PUBLIC MARKETS COMMITTEE REPORT

Mr. Gorton reported that the Public Markets Committee met on November 1 to participate in an interactive dialogue with most of the Board's international equity managers on topics of interest related to international investing. Ten firms participated including Arrowstreet, Barclays Global Investors, Capital Guardian Trust, Fidelity, Goldman Sachs, Julius Baer, LSV Asset Management, Mondrian, State Street Global Advisors, and William Blair. The discussion focused on the following topics: macroeconomics and the challenge of investing in an era of low returns, international investing, long only constraints, value versus growth, possible shocks, and behavioral finance. The WSIB received many favorable comments on the timeliness and quality of the discussion and staff is looking at ways to build on the success of this meeting for future manager symposiums.

COST EFFECTIVENESS MEASUREMENT INC. REPORT

Mr. Dear introduced Mike Heale of Cost Effectiveness Measurement (CEM) to report on the cost effectiveness of the WSIB's investment activities compared to its peer group.

Mr. Heale said that data for the 5-year period ended December 31, 2004, was analyzed. The WSIB was compared to CEM's performance database, which is comprised of data from 20 U.S. sponsors that manage $20 to $110 billion in size. The average size of the participating sponsors was $49 billion, compared to the WSIB's $46 billion.

CEM's analysis focused on the following key performance measurements: policy return, implementation value added, implementation risk, costs, cost effectiveness, and asset-liability mismatch risk.

Mr. Heale reported that the WSIB's policy return of 3.3 percent was slightly above the U.S. median of 3.2 percent and the peer group's median of 3.0 percent. The WSIB's policy return was close to the median despite large differences between its policy asset mix and the U.S. average. The differences were mostly offset over the 5-year period with a positive impact of overweighting to real estate and a negative impact of underweighting in fixed income.

[Mr. Scott was no longer in attendance at 12:46 p.m.]

The WSIB's implementation value added of 0.7 percent was very close to the U.S. median of 0.8 percent and matches the peer median. Mr. Heale said that the WSIB's implementation risk of 3.0 percent is slightly above the U.S. median of 1.5 percent and peer median of 1.2 percent.

The WSIB's total cost of 38.5 bps was below its benchmark cost of 49.0 bps, which suggests a low cost fund. The WSIB was low cost because it had a lower cost implementation style and paid less for services.

Mr. Heale said that the WSIB's 5-year performance in 2004 placed it within the high value added/low cost quadrant for cost effectiveness. The asset-liability risk was 14.5 percent, which is below the U.S. median of 17.6 percent and peer median of 17.4 percent

CORPORATE GOVERNANCE EDUCATION SESSION
Mr. Dear introduced Ann Yerger of the Council of Institutional Investors (CII). The WSIB has been a CII member since 1991.

Ms. Yerger said that CII was founded in 1985 and represents corporate, public and union pension funds addressing investment and corporate governance issues and shareholder rights. Corporate governance closes the gap between ownership and managerial control. She said that CII looks at general issues affecting market transparency, integrity and accountability, and specific checks and balances between board management and investors. Corporate governance covers accounting standards and principles, federal and state legislation, regulations, best practices, and company-specific issues. Ms. Yerger said that corporate governance is important because empirical studies are mixed and there are extraordinary costs involved with governance failures. Scandals within the past four years have been extensive.

Ms. Yerger reported that current hot issues within corporate governance involve executive compensation and majority votes for directors. She explained the concerns with each of these issues and urged Washington State to get involved and ensure its proxy voting guidelines are set to deal with proposals.

Ms. Yerger said that CII assists staff with specific questions on various issues. It educates members through its publications, conference calls, and meetings. It advocates reform and best practices for corporate governance and serves as a voice for investors.

[Ms. Brookman was no longer in attendance at 1:31 p.m.]

Ms. Yerger recommended that the WSIB continue to stay informed on governance issues, talk and collaborate with other investors, continue leadership on voting proxies of passive U.S. equities, and stay involved with public policy debate by following CII's lead on comment letters and asking money managers where they stand on governance issues.

STAFF'S REPORT

Executive Director's Report

Mr. Dear noted that the 2006 schedule of Board and Committee dates was distributed. He provided his monthly report for November on Board governance, investments, operations, and communications. Mr. Dear introduced the new Finance and Budget Manager, Celina Hernandez Verme.

Monthly Investment Report

Mr. Bruebaker provided the CTF monthly investment report for October. For the month, U.S. equity lost 185 bps, underperforming its benchmark by 1 bp while outperforming for the year ended October 31 by 6 bps. International equity lost 372 bps, underperforming its benchmark by 8 bps for the month and 6 bps for the year. Fixed income lost 63 bps percent, but outperformed the Lehman Universal by 17 bps. The CTF governments underperformed the index governments by 10 bps, while CTF credits outperformed index credits by 12 bps. Securities outperformed the index by 3 bps. Private equity draws were $297 million, which is almost double the 2004 average. There were $68 million in draws from KKR and $229 million from the LP portion of the portfolio. Private equity distributions were $138 million. KKR distributions were $23 million, with the balance coming from the rest of the portfolio. There were no investments closed in October. For real estate, draws were $122 million, which was a very active month. Real estate distributions were $79 million.

ASSISTANT ATTORNEY GENERAL'S REPORT

Mr. Silver reported on the WorldCom settlement. The WSIB's claim settled at approximately $18 million, with $1.6 million paid toward attorney fees and litigation costs. A total of $16.4 million was wired to the WSIB and put back into investments.

Mr. Silver noted that the court set a January 17 hearing date to make a final decision on what will be included the Enron class action. The WSIB is a co-lead on the sub-class action suit. Seven billion in settlements has already been received: $2 billion from CitiGroup, $2.2 billion from J.P. Morgan, and $2.4 billion from CIBC. Mr. Silver anticipates that criminal trials will begin early next year and civil proceedings should conclude by the end of 2006. In response to Mr. Colleran's question, Mr. Silver said that the WSIB received approximately 15 cents on the dollar in the WorldCom settlement, with roughly $100 million in losses. He noted that, had the WSIB stayed within the class action instead of deciding to bring a separate action, it would have hardly recovered any money.

OTHER ITEMS

Chair McElligott reported that Mr. Hanna, who resigned from the Board in early November, was presented with a letter and plaque at the December 3 Private Markets Committee meeting. He noted that Mr. Hanna served the Board well over his five-year tenure. The Chair asked that the letter to Mr. Hanna be entered as part of the record.

There was no further business to come before the Board. The meeting adjourned at 1:48 p.m.

Pat McElligott
Chair

ATTEST

Joseph A. Dear
Executive Director