

**WASHINGTON STATE INVESTMENT BOARD**  
**Board Meeting Minutes**  
**September 18, 2008**

The Washington State Investment Board met in open public session at 9:31 a.m. in the boardroom at 2100 Evergreen Park Drive SW, Olympia, Washington.

Present: Glenn Gorton, Chair  
Sandy Matheson, Vice Chair  
Senator Lisa Brown (via teleconference)  
Charlie Kaminski  
John Magnuson  
George Masten  
Pat McElligott (via teleconference)  
Bob Nakahara  
David Nierenberg  
Mason Petit  
Mike Ragan  
Judy Schurke  
Jeff Seely (via teleconference)  
Representative Helen Sommers (via teleconference)

Absent: Treasurer Mike Murphy

Also Present: Joe Dear, Executive Director  
Gary Bruebaker, Chief Investment Officer  
Theresa Whitmarsh, Chief Operating Officer  
Steve Draper, Senior Investment Officer – Real Assets  
Bill Kennett, Senior Investment Officer – Fixed Income  
Phil Paroian, Senior Investment Officer – Public Equity  
Tom Ruggels, Senior Investment Officer – Private Equity  
Diana Will, Senior Investment Officer – Asset Allocation  
Kristi Haines, Executive Assistant

Steve Dietrich, Assistant Attorney General  
Mike Heale, Cost Effectiveness Measurement Inc.  
Urs Rieder, Capital Dynamics, Inc.  
Michael Humphrey, Courtland Partners, Ltd.

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

Chair Gorton called the meeting to order and took roll call.

## **CHAIR AND VICE CHAIR ELECTIONS**

**Chair Gorton called for nominations for Chair. Vice Chair Matheson nominated Glenn Gorton as Chair. There were no further nominations, and Mr. Gorton was elected Chair by acclamation.**

**Chair Gorton nominated Sandy Matheson as Vice Chair. There were no further nominations, and Ms. Matheson was elected Vice Chair by acclamation.**

## **ADOPTION OF THE JULY 15-17, 2008, MINUTES**

**Mr. Masten moved to adopt the July 15-17, 2008, meeting minutes. Mr. Ragan seconded, and the motion carried unanimously.**

## **PUBLIC COMMENT**

Chair Gorton called for public comment. Mr. John Adler and Mr. Stephen Lerner of the Service Employees International Union (SEIU) introduced themselves to the Board. Chair Gorton noted that the Board is limited as to what it can say due to the filing of an initiative by the SEIU.

Mr. Lerner observed the enormous role that WSIB plays in the economy. He said the economy must be healthy in order for investors to be successful, and a core question is whether investment in private equity contributes to a healthy economy. He said income equality and economic growth are tied together. SEIU became interested in private equity once it found that its largest signatory employers were being bought by private equity firms. They concluded after meeting with the firms that they are disinterested in engaging in a real dialogue about the impact of their ownership on the economy and SEIU membership. He believes private equity firms contribute to the growing inequality in income.

Mr. Adler said that the goal is for SEIU and WSIB to reach a common understanding on how best to address risks in the private equity investments within the WSIB portfolio. He said conditions in the market have brought the private equity boom to an end, and the inability of mega buyout funds to do deals will impact returns and the WSIB's performance. He also raised concerns about the impact on limited partners of private equity funds going public. Mr. Adler referenced the Ludovic Phalippou study on private equity rates of return calculations. He suggested it would be worthwhile for the WSIB to do a cashflow analysis on private equity final rates of returns.

A discussion ensued on the impact of having top quartile managers, the analysis WSIB performs on rates of return, and the availability of public information relating to that.

Mr. Adler said that public funds are increasingly taking environmental, social, and corporate governance issues into consideration in their private equity decision-making. He said the SEIU calls upon private equity buyout firms to adopt seven principles: (1) increased public transparency; (2) responsible employment practices; (3) environmental and public health protection; (4) respect for human rights; (5) fair taxation; (6) zero tolerance for corruption; and, (7) independent monitoring.

Mr. Adler concluded by stating that SEIU's initiative would address the issues. SEIU values its relationship with the WSIB and would like to work together to improve the economy in a socially responsible way.

Mr. Ed Gonion, executive director of the Washington State School Retirees' Association (WSSRA), thanked the WSIB for its superb management of pension funds on behalf of its 16,000 members. He said both employee and employer contributions and pension earnings provide for retirement, and retirees depend on the future management of the funds. He believes the WSIB is doing a wonderful job. He pointed out that 96 percent of stakeholders are members of unions other than the SEIU. The WSSRA is concerned with SEIU's proposal to take away WSIB decision making, and replace it with decisions determined by SEIU's Washington DC headquarters. WSSRA will do its best to educate its members that any effort to take away from WSIB's management is a bad idea.

Ms. Bev Hermanson provided public comment as a retired public employee, but noted she is also a lobbyist of the Retired Public Employees Council of Washington (RPEC-WA), former staff member of the Washington Federation of State Employees, and former Board member of the WSIB. As a Board member, she learned quickly to focus on fiduciary responsibilities. The trustees have a common purpose: to maximize investment returns at a prudent level of risk. She believes the Board should oppose any efforts that would affect that responsibility, including Initiative 414. Ms. Hermanson said she is proud of the Board's accomplishments.

Ms. Cassandra de la Rosa said she represents 8,500 dues paying Retired Public Employees Council (RPEC-WA) members that are retirees. The Council's mission is to improve retirement conditions. RPEC-WA supports the Board. Its members depend on good investment returns. She said the Board has met its mission and statutory mandate admirably, by having a diversified portfolio including alternative investments that have been the best performers. She believes the WSIB is a leading pioneer among public pension funds and competent to figure its rate of return. Ms. de la Rosa has confidence the Board prudently invests so benefits are not at risk. RPEC-WA opposes Initiative 414, and any efforts that would change the way WSIB does things. She thanked the Board for all it has done for members.

Mr. Randy Parr said the Washington Education Association (WEA) applauds the WSIB's efforts to maximize investment returns. It opposes any efforts that do not follow the prudent person mandate. He said keeping employer pension costs low allows employers to spend money elsewhere. Retirement income levels of WEA members within the Teachers' Retirement System Plan 3 are dependent on both personal contributions and WSIB returns. The Board's work impacts future livelihoods and WEA resists anything that would inhibit maximization of returns. He encouraged the Board to oppose any efforts that interfere with its fiduciary responsibility to members.

Mr. Rick Jensen, Washington State Patrol Troopers Association, said its small system of about 2,200 active and retired members is very susceptible to trends. He said the Troopers Association is opposed to the SEIU initiative and the change it could bring to the good work of the WSIB.

Mr. Scott Adams of the American Federation of State, County, and Municipal Employees (AFSCME), supported the idea of having federal regulations seek transparency within private

equity, but said going to voters with an initiative is the wrong way to go about it. He said the AFSCME does not support the SEIU initiative, which they believe would take away from the WSIB's ability to meet its fiduciary responsibilities and plan obligations. The state of Washington's private equity investments allow the Board to be engaged and have a voice in issues.

Chair Gorton thanked those who gave public comment.

Mr. Nierenberg spoke to the amount of due diligence and background information considered before the Board makes investments decisions. The WSIB could publicly summarize how it makes decisions without providing proprietary information.

### **EXECUTIVE DIRECTOR'S REPORT**

Mr. Dear provided his monthly report for September on Board governance, staff, investments, operations, public affairs, meetings, and open procurement activities. Mr. Dear said staff received a number of media inquiries this week relating to market conditions.

[Senator Brown joined the meeting via teleconference at 10:00 a.m.]

### **FIDUCIARY EDUCATION**

Mr. Song introduced his education session on fiduciary principles. He said the WSIB statute provides that assets are held in trusteeship by voting members. Prior to 1981, the retirement funds were separate and each overseen by a separate board of trustees, who were advised by separate advisory committees of investment professionals. The Legislature found this to be an ineffective system and consolidated the structure by creating the Investment Board in 1981. The investments professionals who served as advisors became nonvoting members of the Board so that they would be readily available to trustees. The Board is not a board of trustees, it is a fiduciary board comprised of trustees and advisors.

Mr. Song said, as trustees overseeing assets, voting members have common law obligations of prudence and loyalty which are traditional trust guidelines. Further, as a government entity, members also have an obligation to contractual requirements. Mr. Song explained that an employee hired in public capacity has a constitutional right to the retirement formula in effect on their date of hire. The principle evolved over time, and courts began to realize the formula is an empty promise without money to fund the retirement system, and determined, in addition to protecting the formula, the system has a right to funding that is actuarially blessed.

Mr. Song also reported on a recent Employee Retirement Income Security Act (ERISA) development. He noted that the WSIB is not subject to ERISA. However, ERISA is a valuable resource of case law and administrative decisions, and states are adopting principles from those decisions into their pension plan management and governance. In response to a request for an opinion relating to the extent fiduciaries can raise issues in a proxy vote, the Department of Labor said the mere fact a pension plan is impacted by national, economic, and policy issues is not sufficient justification to get involved in proxy votes that are unrelated to increasing investment value.

A discussion ensued on the fiduciary obligation to vote proxies, Board member indemnification,

and Attorney General representation. Vice Chair Matheson proposed an education session highlighting the separation of duties within the retirement system to understand who is tasked with what and who bears primary responsibility. Mr. Nierenberg asked for discussion at a subsequent meeting on the impact of securities lending on proxy voting, and the benefit of voting proxies.

[The Board briefly recessed at 11:38 a.m. and reconvened in open session at 11:51 a.m.]

### **COST EFFECTIVENESS MEASUREMENT REPORT**

Mr. Heale introduced the Cost Effectiveness Measurement (CEM) report on the WSIB for the 5-year period ended 2007. WSIB performance results are compared against 156 U.S. funds. Its costs are compared against a custom peer group of 19 funds, with a median size of \$57.2 billion in assets. He said CEM's report measures policy return, value added, implementation risk, costs, cost effectiveness, and asset-liability mismatch risk.

Mr. Heale said WSIB's total return was 16.1 percent above the U.S. median of 13.6 percent. The WSIB's policy return of 15.2 percent was the highest in the fund universe. He said that it was the highest because of the policy overweighting to private equity, the positive impact of the WSIB's high benchmark return for private equity, and a higher weighting to real estate. Mr. Kaminski said it would be interesting to look at the policy return against something other than the S&P 500 + 500 basis points (bps), such as the average return from private equity.

Mr. Heale said that value added measures the contribution from active management. The WSIB 5-year value added was 0.9 percent compared with 0.7 percent for peers and the U.S. universe. He said that active management also carries more risk. The WSIB implementation risk was 2.9 percent compared with the U.S. median of 1.2 percent.

Mr. Heale said that WSIB investment management costs were \$259.6 million or 41.8 bps. WSIB costs have increased between 2005 and 2007 due to the increase in private equity and real estate holdings, which are more expensive asset classes, and the reduction in lower cost passive and internal management. However, the benchmark cost analysis suggests WSIB is low cost by 8.3 bps, primarily due to low cost implementation style and for paying less for similar mandates relative to peers.

Mr. Heale said the WSIB's 5-year performance placed it in the positive value added, low cost quadrant.

Mr. Heale described CEM's neutral asset mix tool used to model WSIB's unsmoothed mark-to-market liabilities, which are volatile. The WSIB's 5-year liability return of 7.5 percent compares to the peer median of 6.0 percent and U.S. median of 6.2 percent. The higher return was due to inflation sensitivity. Assets grew 8.2 percent faster than mark-to-market liabilities.

Mr. Heale concluded his report by stating that WSIB's results are very strong.

[The Board briefly recessed at 12:20 p.m. and reconvened in open session at 12:44 p.m.]

## **ADMINISTRATIVE COMMITTEE REPORT**

Chair Gorton reported on the two-day Administrative Committee meeting, which concluded just prior to the Board meeting.

### **Code of Conduct Policy 2.00.150 Revision**

Chair Gorton said the Committee performed a review of the Code of Conduct Policy.

**Chair Gorton moved that the Board approve the Code of Conduct Policy as is. Mr. Masten seconded, and the motion carried unanimously.**

### **Investment Officer Compensation Consultant Recommendation**

**Chair Gorton moved that the Board approve McLagan to conduct a salary survey and undertake the subsequent design of an incentive compensation plan. Vice Chair Matheson seconded the motion.**

Chair Gorton reported that the Committee heard two presentations from potential vendors. He said the Committee felt McLagan was the front runner due, in part, to the amount of information McLagan has available and their cost.

Mr. Masten said he does not support bonus or incentive pay, which is not a reflection on the quality of staff. He said he would prefer to see salaries adjusted up, as he believes incentive pay is inconsistent.

**The above motion carried, with Mr. Masten voting no.**

### **Executive Director Reappointment**

**Vice Chair Gorton moved that the Board appoint Mr. Dear to a new three-year term from November 12, 2008, until November 11, 2011, and forward its action to the State Finance Committee. Mr. Masten seconded, and the motion carried unanimously.**

### **Assistant Attorney General's Report**

Mr. Dietrich provided an update on the Enron litigation. He said the federal district judge approved the proposed plan of allocation on September 8 for the \$7.2 billion settlement fund; awarded attorney fees of \$688 million, which is 9.52 percent of the settlement fund; and, a supplemental award for expenses to the lead plaintiff, the University of California Regents. Mr. Dietrich did not have an update on what the WSIB can expect to obtain from the settlement. The claims administrator hopes to start payments by year end; there are 1.5 million claims to process.

## **AUDIT COMMITTEE REPORT**

Mr. Petit reported that the Audit Committee met on September 9. The Committee had an education session regarding the basic elements of audit committee oversight, emerging issues, and common and best practices. Mr. Petit recognized the good work done by internal audit staff, Shawna Killman and Rodney Reynolds.

### **State Auditor's Office Public Records Request Performance Audit Report**

Mr. Petit reported that a representative from the State Auditor's Office presented the Public Records Request Performance Audit Report. Overall, the WSIB performed well. Mr. Dear said that management has implemented improvements in response to the audit.

**Mr. Petit moved that the Board approve the State Auditor's Office Performance Audit Report. Mr. Ragan seconded, and the motion carried unanimously.**

### **Internal Audit Report 2008-03, Self-Directed Plan External Managers**

Mr. Petit said that Internal Audit presented Report 2008-03, Self-Directed Plan External Managers. The audit revealed that processes in place at the WSIB for the externally managed self-directed plan investment options are adequate. There were three recommendations to strengthen controls over manager and contract monitoring; management's action plans were discussed.

**Mr. Petit moved that the Board approve Internal Audit Report 2008-03, Self-Directed Plan External Managers. Mr. Ragan seconded, and the motion carried unanimously.**

### **Internal Audit Report 2008-04, Financial Control Systems**

Mr. Petit reported that the Committee discussed the Financial Control Systems Audit in executive session due to information concerning audit recommendations for improving controls, the public discussion of which would result in loss to the funds managed by the WSIB.

**Mr. Petit moved that the Board approve Internal Audit Report 2008-04, Financial Control Systems. Mr. Ragan seconded, and the motion carried unanimously.**

### **Fiscal Year 2008-2009 Internal Audit Plan**

Mr. Petit said a risk assessment was conducted and Internal Audit's plan for the fiscal year was discussed. Six areas will be audited: custodian bank operations; trade processing, confirmation, and settlement; accounting, pricing and unitization of the CTF, Plan 3 (TAP), and commingled bond fund; foreign country market entry application/tax registration; public equity investment contract/manager monitoring; and, limited liability company (LLC) processes. In addition, an independent IT Security Policy and Standards Compliance Audit and a Quality Assessment Peer Review of the WSIB Internal Audit function will also be conducted in 2009.

**Mr. Petit moved that the Board adopt the Fiscal Year 2008 – 2009 Internal Audit Plan. Mr. Ragan seconded, and the motion carried unanimously.**

### **Daily Valued Funds Policy Revision**

Mr. Petit reported that, due to the upcoming transition in investment options for the Deferred Compensation Program and the Defined Contribution participants, the Daily Valued Funds Operation Policy, 2.14.300 requires updating. The changes to the policy are limited to the removal

of the Horizon Funds and the inclusion of the Bond Fund as an investment component of the new Target Date Retirement Strategy Funds.

**Mr. Petit moved that the Board adopt the revisions to the Daily Valued Funds Operation Policy 2.14.300. Mr. Ragan seconded, and the motion carried unanimously.**

#### **Proxy Voting and Securities Lending**

Mr. Petit said the Committee discussed the pros and cons of securities lending in the current collective trust versus the benefits of voting those shares. No action is recommended at this time. Staff will work with Barclay Global Investors (BGI) to obtain additional information requested by the Board, and the Audit Committee will resume discussion of this issue when it receives the 2008 Proxy Voting Report at its December meeting.

Mr. Kaminski requested that staff ask BGI if there is a correlation between meetings that were categorized as “important” or “moderately important” and the number of shares on loan and/or the compensation for loaning such securities, as well as requesting data on any share price movement of loaned securities. He suggested that information could be useful in improving the WSIB’s securities lending process.

#### **Conflict of Interest Compliance Review and Personal Investment Reports**

Mr. Petit reported that Board members and staff continue to demonstrate both an awareness and understanding of the Conflict of Interest Policy and the State Ethics in Public Service law. Full compliance was found with no exceptions.

**Mr. Petit moved that the Board accept the Conflict of Interest Compliance Review and Personal Investment Reports. Mr. Ragan seconded, and the motion carried unanimously.**

#### **Nonvoting Board Member Term Expiration**

Mr. Petit said the Committee discussed the upcoming term expiration of nonvoting Board member David Nierenberg, who indicated interest in continuing to serve on the Board.

**Mr. Petit moved that the Board reappoint Mr. David Nierenberg for another term. Mr. Masten seconded the motion.**

Vice Chair Matheson and Chair Gorton remarked that Mr. Nierenberg adds a lot of value to the Board.

**The above motion passed unanimously.**

#### **Other**

Mr. Petit also noted that staff continues to work on four prior audit recommendations.

## **PUBLIC MARKETS COMMITTEE REPORT**

Mr. Masten reported that the Public Markets Committee met on September 9 to consider the results of the Consultant Pool Request for Qualifications and Quotations (RFQQ), as well as revisions to four policies.

### **Consultant Pool RFQQ Search Results**

Mr. Masten said that staff reported to the Committee on the 11 firms who submitted 24 responses in the four categories included in the Investment Consultant Pool RFQQ.

**Mr. Masten moved that the Board approve the consulting firms in the stated categories (Pools), subject to successful contract negotiations and any further due diligence, as declared in the following table. Mr. Ragan seconded the motion.**

	<b>Category</b>	<b>Recommended Firm</b>
<b>Pool A</b>	<b>General Investment Consulting Services</b>	<b>Callan Associates, Inc.; Ennis Knupp and Associates; Mercer Investment Consulting, Inc.; Pension Consulting Alliance; and R.V. Kuhns &amp; Associates, Inc.</b>
<b>Pool B4</b>	<b>Risk Management</b>	<b>Cutter Associates Inc.; Holland Park Risk Management Inc.; and Mercer Investment Consulting, Inc.</b>
<b>Pool B10</b>	<b>Marketable Alternative Advisory Services</b>	<b>Albourne America LLC; Aksia LLC; Ennis Knupp and Associates; Mercer Investment Consulting, Inc.; and Pension Consulting Alliance</b>
<b>Pool 11</b>	<b>Specialty Services</b>	<b>Mercer Investment Consulting, Inc.; and Pension Consulting Alliance</b>

Mr. Masten reported that the consultant pool is used by the WSIB to provide services on a project basis. Mr. Bruebaker said that when a project arises in the category areas, a request would be sent to the firms staff believes are qualified to perform the work, and those firms are required to respond with specific information before the project is awarded. He said there is no retainer fee paid to consultants; fees are based on an hourly charge based on the level of employee involved in the project.

**The above motion carried unanimously.**

### **Public Equity Policy Revisions**

**Mr. Masten moved that the Board approve the proposed revisions to the Defined Contribution Plan 3 Retirement Funds Policy 2.11.100 and the Deferred Compensation Program and Judicial Retirement Account Policy 2.13.100 as well as the termination of the Horizon Funds Policy 2.14.100.**

Mr. Masten said the policy changes are needed in order to reflect the addition of the target date strategies and removal of the Horizon Funds.

**Mr. Ragan seconded, and the above motion carried unanimously.**

### **Fixed Income Policy Revisions**

**Mr. Masten moved that the Board approve the proposed revisions to the Bond Market Fund Policy 2.14.200 and Fixed Income – Retirement Funds Policy 2.10.200.**

Mr. Masten said the policy changes place a more restrictive constraint on corporate issues than that required by statute. The fixed income portfolios are already managed to this more strict constraint; hence, the policy revisions do not change the way the funds are managed but merely provide clarification of the limitation.

**Mr. Ragan seconded, and the above motion carried unanimously.**

### **PRIVATE MARKETS COMMITTEE REPORT**

Vice Chair Matheson reported that the Private Markets Committee met on September 4 and 5, and discussed six investment recommendations.

#### **Triton Fund III, L.P.**

**Vice Chair Matheson moved that the Board invest up to €150 million, plus fees and expenses, in Triton Fund III, L.P., subject to continuing due diligence and final negotiation of terms and conditions. Mr. Masten seconded the motion.**

Vice Chair Matheson reported that this is a mid-market European buyout fund that will invest in a portfolio of global and regional companies headquartered within the German-speaking and Nordic regions. Triton focuses on investments in the business services, industrials, and consumer industries and seeks value-oriented opportunities with potential for significant operational enhancements to drive growth. If approved, Triton would be a new general partner relationship for the WSIB. She said the recommendation is based, in part, on Triton's deep, multi-national team; talented leadership and decentralized management structure; strong top quartile performance; focused strategy; and attractive fit in the WSIB portfolio. Staff and Capital Dynamics had originally recommended a commitment of up to €100 million, but both concur with the increased amount, with the understanding that adjustments will be made to other future planned commitments later this year to offset the increase.

**The above motion carried unanimously.**

## **Charterhouse Capital Partners IX, L.P.**

**Vice Chair Matheson moved that the Board invest up to €200 million, plus fees and expenses, in Charterhouse Capital Partners IX, L.P., subject to continuing due diligence and final negotiation of terms and conditions.**

Vice Chair Matheson reported that the fund will focus on management buyouts, corporate restructurings, and similar transactions in a small number of high quality investments targeting large, established companies primarily headquartered in Western Europe, with a focus on the United Kingdom and France. The WSIB has invested in three prior Charterhouse funds, and this recommendation is consistent with the private equity annual plan approved by the Board in January 2008. She said the recommendation is based, in part, on Charterhouse's deep, experienced, and stable investment team; strong long-term track record; focused, consistent investment strategy; and strong deal flow.

**Chair Gorton seconded, and the above motion carried unanimously.**

## **FountainVest China Growth Capital Fund, L.P.**

**Vice Chair Matheson moved that the Board invest up to \$50 million, plus fees and expenses, in FountainVest China Growth Capital Fund, L.P., subject to continuing due diligence and final negotiation of terms and conditions.**

**Mr. Masten seconded the motion.**

Vice Chair Matheson reported that FountainVest will target growth equity investments in China, in partnership with local entrepreneurs. The fund will pursue companies that are direct beneficiaries of three long-term macro themes in China: (i) growing middle class and domestic consumption, (ii) rapid urbanization, and (iii) sustainable production and development of resources. While FountainVest is a first-time fund, the four co-founders worked together previously as senior members of the China-based investment team of Temasek Holdings, the investment arm of the Singapore government. If approved, this investment would create a new general partner relationship for the WSIB. This proposed emerging market investment is consistent with the private equity annual plan approved by the Board in January 2008. She said the recommendation is based, in part, on the firm's experienced and cohesive investment team, attractive investment strategy, successful prior track record of the principals, compelling macro environment in China, and the attractive fit in the WSIB portfolio.

**The above motion carried unanimously.**

## **Hometown America Holdings, LLC**

**Vice Chair Matheson move that the Board invest an additional \$400 million, plus fees and expenses, in Hometown America Holdings, LLC, subject to continuing due diligence and final negotiation of terms and conditions. Mr. Petit seconded the motion.**

Vice Chair Matheson reported that Hometown is a real estate operating company focused on owning and operating manufactured housing communities and other residential property. The WSIB has invested in Hometown since 1998 and consistently receives good returns from the Company. A further investment in Hometown constitutes a commitment to this relatively lower-risk sector and to growing one of the WSIB's best partners' businesses in an attractive investment climate. The recommendation is consistent with the update to the real estate annual plan presented at the July 2008 Board meeting. She said the recommendation is based, in part, on Hometown's excellent management team, their ability to take advantage of current demographics, the attractive, low-volatility strategy, and the diversification provided to the WSIB's real estate portfolio through this investment.

**The above motion carried unanimously.**

#### **Evergreen Real Estate Partners, LLC**

**Vice Chair Matheson moved that the Board invest an additional \$500 million, plus fees and expenses, in Evergreen Real Estate Partners, LLC, and approve the changes to the Partnership's financial terms consistent with the discussion in the confidential memo provided to the Board, subject to continuing due diligence and final negotiation of terms and conditions. Mr. Masten seconded the motion.**

Vice Chair Matheson reported that Evergreen's strategy is to invest in or with real estate operating companies on a global basis. The recommendation is consistent with the real estate annual plan approved by the Board in January 2008. She said the recommendation is based, in part, on the firm's investment strategy, which is the primary driver of the WSIB's real estate program, their excellent management team, and the diversification benefits of the partnership owning multiple operating companies, each with different geographic and property types mandates.

**The above motion carried unanimously.**

#### **Tangible Assets Co-Investment, LLC**

**Vice Chair Matheson moved that the Board invest \$250 million, plus fees and expenses, in Tangible Assets Co-Investment, LLC, subject to continuing due diligence and completion of terms and conditions. Chair Gorton seconded the motion.**

Vice Chair Matheson reported that Tangible Assets Co-Investment, LLC, will be the legal vehicle through which the WSIB will undertake co-investments with existing WSIB Tangible Asset Investment partners and on tangible asset transactions with existing WSIB Real Estate investment partners. The LLC will be managed by WSIB staff with the assistance of external consultant(s) and external legal counsel. Individual investment decisions will be at staff discretion, upon an affirmative recommendation by the consultant. The Executive Director and Chief Investment Officer will have final review and approval of all transactions. The recommendation is consistent with the tangible assets annual plan approved by the Board in February 2008. She said the

recommendation is based, in part, on the opportunity to expand existing relationships, and on the ability to better manage portfolio diversification and risk.

Mr. Petit asked if the fund had specific investments in mind. Mr. Dear said there are co-investments being considered. All co-investments are limited to existing relationships already approved by the Board.

**The above motion carried unanimously.**

### **CTF CURRENCY EXPOSURE**

Ms. Will summarized the currency exposure discussion from the June Board meeting. She said staff does not recommend pursuing a currency overlay program at this time, but will continue to monitor currency exposure and report periodically to the Board. The Board agreed with staff's recommendation, and took no action.

[The Board briefly recessed at 1:26 p.m. and reconvened in open session at 1:36 p.m.]

[Mr. McElligott joined the meeting via teleconference at 1:37 p.m.]

### **QUARTERLY DISCUSSION OF MARKETS**

#### **Discussion**

##### Market Environment

Mr. Bruebaker introduced the discussion. He said there is a crisis of confidence in the financial markets. Lehman Brothers is gone, the debt supercycle could be over. Consumers are faced with weak labor, high gas and food prices, and instability in housing. Further, the required deleveraging that will now take place will act as a headwind to growth for quite some time. Mr. Bruebaker reported that Alan Greenspan said the sub-prime crisis, which led to the collapse of mortgage, will lead to failure of more firms. The sub-prime meltdown has been compared to other significant events such as Black Monday, the savings and loan crisis, the Russian debt crisis, and September 11. Mr. Bruebaker said that while he is unsure when the crisis will end, he is confident it will end. The WSIB has a high quality, globally diversified portfolio that is positioned well for long-term performance.

##### Fixed Income

Mr. Kennett discussed the credit crisis, the real economy, and housing. He reported the chief concern for the WSIB's fixed income unit regarding the credit crisis was exposure to financial institutions. Although the WSIB portfolio is overweight credit, it is underweight financials. He reported that fixed income performance is still excellent for the calendar year. He discussed the weakening economy. He said that recession would cause defaults to spike, but the WSIB is in good shape as it is underweight in high yield securities. Mr. Kennett said housing prices have fallen more than 18 percent, and should fall further. He reported that the WSIB has very little non-agency mortgage-backed security exposure. The Board discussed financial institution failures.

[Mr. Seely joined the meeting via teleconference at 1:50 p.m.]

Mr. Nierenberg suggested that the Private Markets Committee discuss the potential to increase its commitment in the distressed asset category.

### Public Equity

Mr. Paroian discussed three topics: (1) the Lehman Brothers and AIG holdings and what effect recent events have had on the WSIB portfolio; (2) markets and performance for the fiscal year ended June 30, 2008; and, (3) markets since June 30.

Mr. Paroian noted that the majority of the U.S. equity portfolio is indexed and thus held a market weight in Lehman and AIG. However, where WSIB employed active managers (U.S. enhanced index and global managers) they were underweight Lehman and generally underweight AIG, somewhat mitigating the effects on the portfolio. Staff has also talked extensively with both of WSIB's money market managers and was reassured that they had limited exposure.

He said the global index was down almost 10 percent for the fiscal year ended June 2008, with the commodity based sectors of oil and gas and material delivering strong returns and the financials sector falling sharply. WSIB's overall portfolio was overweight oil and gas and underweight financials, but was hampered somewhat by an underweight to emerging markets which outperformed and due to U.S. enhanced index managers struggling.

Since June 30, financials have continued to fall and the commodity-based sectors turned and have also fallen sharply. Mr. Paroian said that, while value managers typically help during a down period, this is an unusual period where they have done worse. Irrational markets are very difficult for investment managers. Mr. Paroian believes that the key is maintaining a long-term focus on managers in whom the WSIB has conviction in, even if it is difficult over the short-term. He added that staff is currently reviewing its managers, while maintaining that long-term focus. Mr. Nierenberg commented the WSIB has advantage with its long-term view and liquid portfolio.

### Real Estate

Mr. Draper said that times like these are part of the reason for having real estate in the Commingled Trust Fund (CTF) portfolio. He noted that the real estate portfolio is doing reasonably well under the circumstances. He highlighted that, while real estate is not immune to the current market conditions, it tends to be less volatile because of its long-term investment horizon. The real estate portfolio will be subject to the impact of contagion of the general economy and the ongoing meltdown of the financial sector, but it is not expected to be as severe as the impact to public markets. He expects the demand for industrial and office space to soften, which will likely decrease rents and cause valuations to ease off. He said it is also possible that some retailers may fail, which would impact occupancy rates in some retail properties. The lack of liquidity in the market has led to less leverage being available for real estate investing, and that which is available is more expensive. He said the picture of how the current turmoil will affect real estate would not be entirely clear for some time. The WSIB's broadly diversified global portfolio is helpful in this environment, and he expects some interesting opportunities will come out of this situation for WSIB's partners.

### Private Equity

Mr. Ruggels noted that the investment business is cyclical, and that private equity cycles tend to be exaggerated by the use of leverage. During good times, leverage magnifies gains. However in a period of declining valuations, losses are also magnified by leverage. Currently, we are in a period

of declining valuations, as the credit markets are in disarray, economic growth has slowed, and global public equity markets have declined significantly. Staff is seeing multiple compression across the board, and even companies that continue to perform relatively well have declined in value. We are also starting to see evidence of the softening economy as some portfolio companies have experience operating challenges and declining profitability. We are starting to see some writedowns in the portfolio, and things are expected to get worse before they get better.

[Mr. Seely left the teleconference due to technical problems at 2:40 p.m.]

Mr. Ruggels said that there are also reasons to be optimistic. The WSIB has been through down cycles before, and while declining valuations negatively impact current returns, they create attractive buying opportunities that can result in strong future returns. WSIB saw similar valuation declines in 2001 to 2003, and some of the private equity investments made during that time period turned out to be among the best ever. Staff expects that the current environment will create many excellent buying opportunities for our general partners.

It is important to remember that private equity is a long-term game and cyclical by nature. Difficult periods are inevitable. Staff has said many times that the keys to success in private equity are good manager selection, a well diversified portfolio, and a patient, long-term perspective. The Board has built a well diversified portfolio managed by high quality general partners. We must now focus on our patience and long-term perspective.

A discussion ensued regarding the negative affects the cycle could have on private equity firms and within companies.

Mr. Dear said that smart people find a way to take advantage of difficult conditions, and great things can come out of tragic events. The WSIB has every reason to legitimately express confidence about its portfolio and should stay with its plan.

Mr. Bruebaker reported that the fund outperformed the implementation value added benchmark by 104 bps for the quarter ended June 30, 2008. Performance was hurt by the allocation decision, but helped by the manager decision. The implementation value added is positive for the quarter, the 3- and 5-year, while we slightly underperformed for the one-year by 26 bps. Mr. Bruebaker said that while 10-year performance was below 8%, looking back since inception of the CTF, performance is 9.88%, which means the CTF is more than meeting its benchmark over the longer term. Our investment portfolios are positioned well for the long-term. Mr. Bruebaker stated that our job now is to be careful not to diverge from our long-term mission during the time of market turmoil and to continue to seek ways to take advantage of investment opportunities during these troubled times. Mr. Nierenberg pointed out the WSIB had far outperformed the S&P 500 which for the ten years ended June 30, 2008 only returned 2.88 percent.

### **Private Equity**

Mr. Rieder addressed how the credit crisis has impacted private equity. Bad debt affects the amount financial institutions can lend. The availability of debt has decreased, and financing terms have become more onerous. Credits spreads have widened as a result of the credit crunch and there has been a repricing of risk. Distributions are expected to come down.

Mr. Kaminski asked what happens when a contractual investment period ends on a fund and it is not fully invested. Mr. Rieder said that funds are unable to invest in new companies but can do follow-on investments in current companies, or can seek to amend agreements. He said it depends on the market opportunity.

### **Real Estate**

Mr. Humphrey discussed various economic issues, focusing on home foreclosures and their impact. He highlighted that in addition to sub-prime loans, the market still had to work through issues with "Alt-A" mortgages, and he noted the number of borrowers facing payment resets in the near term. Mr. Humphrey reviewed historical market conditions and the relationship of appreciation and income levels during cycles. While market conditions are stressful, in his opinion, the WSIB is well positioned to take advantage of the downturn.

### **2009 MEETING SCHEDULE**

**Vice Chair Matheson moved that the Board accept the proposed meeting schedule for 2009. Mr. Ragan seconded, and the motion carried unanimously.**

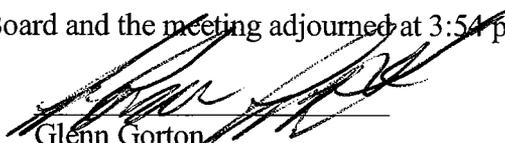
### **BOARD DISCUSSION**

Chair Gorton announced that the Board would go into executive session to review and discuss the performance of Board members and of the Board. He said the executive session was expected to last ten minutes, at which time the Board would reconvene in open session.

[The Board went into executive session at 3:40 p.m. and reconvened in open session at 3:54 p.m.]

### **OTHER ITEMS**

There was no further business to come before the Board and the meeting adjourned at 3:54 p.m.

  
Glenn Gorton  
Chair

ATTEST

  
Joseph A. Dear  
Executive Director