

WASHINGTON STATE INVESTMENT BOARD
Board Meeting Minutes
June 21, 2012

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

Present: Treasurer Jim McIntire, Chair
 Mike Ragan, Vice Chair
 Senator Lisa Brown (via teleconference)
 Steve Hill
 Bill Longbrake
 George Masten
 Patrick McElligott
 Bob Nakahara
 David Nierenberg (via teleconference)
 Judi Owens
 Natasha Pranger

Absent: Richard Muhlebach
 Representative Sharon Tomiko Santos
 Judy Schurke
 Jeff Seely

Also Present: Theresa Whitmarsh, Executive Director
 Gary Bruebaker, Chief Investment Officer
 Victor Moore, Chief Operating Officer
 Liz Mendizabal, Institutional Relations Director
 Steve Draper, Senior Investment Officer – Real Estate
 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 – Tangible Assets
 James Mackison, Director of Technology and Innovation
 Kristi Haines, Executive Assistant
 Kristi Bromley, Administrative Assistant

 Steve Dietrich, Attorney General's Office

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

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

ADOPTION OF THE APRIL 19, 2012, BOARD MEETING MINUTES

**Ms. Owens moved to adopt the April 19, 2012, Board meeting minutes.
Vice Chair Ragan seconded and the motion carried unanimously.**

ADOPTION OF THE MAY 17, 2012, BOARD MEETING MINUTES

**Ms. Owens moved to adopt the May 17, 2012, Board meeting minutes.
Vice Chair Ragan seconded and the motion carried unanimously.**

ADOPTION OF THE JUNE 7, 2012, SPECIAL BOARD MEETING MINUTES

**Ms. Owens moved to adopt the June 7, 2012, Special Board meeting minutes.
Vice Chair Ragan seconded and the motion carried unanimously.**

PUBLIC COMMENT

There was no public comment.

EXECUTIVE DIRECTOR'S REPORT

Ms. Whitmarsh reminded the Board that responses to the Board governance and risk survey are due tomorrow. The survey was designed by the Board's governance and risk consultant, Funston Advisory Services LLC, in conjunction with the Board's *ad hoc* Governance Committee and the Executive Director. Chair McIntire noted that he plans to meet in person or by telephone with each Board member individually prior to the July Board meeting.

Ms. Whitmarsh announced that Allyson Tucker, Assistant Senior Investment Officer – Public Equity, has accepted the Senior Investment Officer – Risk Management and Asset Allocation position effective July 1, 2012. The WSIB is now recruiting to fill the Assistant Senior Investment Officer – Public Equity position.

Ms. Whitmarsh stated the custody and security lending contacts with State Street Bank have both been signed and the transition to date has been very successful. She also noted the recent PewCenter on the States report places the Washington pension system in the top four, at a 96 percent funding level. Discussion ensued regarding the report's erroneous finding relative to Washington's funding of retiree health benefits.

Ms. Whitmarsh noted that the WSIB is joining a broad coalition of institutional investors in signing a letter urging the public company executives to increase the gender diversification on their board of directors. The letter targets the S&P 500 companies which currently have no women serving on their boards and footnotes a number of studies which found that companies that embrace gender diversity are better-governed, better-managed, and have better long-term growth prospects. Chair McIntire reported on his meeting with the CEO of a public company with which the WSIB does business and their plans to make progress in this area in the near future.

CAPITAL MARKET ASSUMPTIONS

Mr. Bruebaker introduced himself and stated the Board received a detailed presentation of the proposed capital market assumptions by Pension Consulting Alliance (PCA) at the May Board meeting. Mr. Bruebaker noted that his presentation would focus on a summary of the previous presentation. A comparison of PCA's recommended capital market assumptions, with which the WSIB staff agrees, with the average of all consultants reflects a difference in expected returns greater than 25 basis points in the asset classes of fixed income, tangible assets, and real estate. This difference is due to the construction of the WSIB's specific portfolios. At the same time, the WSIB's projected return in private equity is slightly lower due to our benchmark of 300 basis points over global equity. Mr. Bruebaker noted that the WSIB's fixed income team has consistently delivered solid investment performance and is currently positioned to continue this success. Real estate has also consistently delivered solid investment performance and is positioned to support the expected return assumption. The Board will receive an in-depth report from Ms. Will at its July meeting regarding the goals for the tangible assets portfolio, which staff believes position the portfolio to outperform.

In response to a question from Mr. Hill, Mr. Bruebaker confirmed the next asset allocation study for the Commingled Trust Fund is scheduled for July 2013, with educational sessions leading up to the July 2013 Board meeting.

Chair McIntire noted, while the evaluations are conducted independent of each other, the WSIB's long-term estimated rate of return of 7.8 percent is in line with the Legislature's return assumption for the next two biennium.

Mr. McElligott moved to adopt the proposed 2012 WSIB capital market return, risk, and correlation assumptions. Vice Chair Ragan seconded and the motion carried unanimously.

AUDIT COMMITTEE REPORT

Mr. Hill noted that the Audit Committee met on May 24, 2012. The Committee reviewed the Financial Statement Auditor Independence Review, the Audit Recommendations Status Report, and the Investment Referrals Quarterly Report at the May meeting. Mr. Hill reported that one outstanding audit recommendation, which relates to travel expenses paid by outside sources, is expected to be completed by July 1. Four new investment referrals by Board members were reported at the May meeting; two of which were of no interest and two continue to be reviewed by staff.

IT Security Review and Compliance Audit

Mr. Hill reported that Intrinium Networks completed their audit in May and that a follow-up review in August will confirm the resolutions of issues noted. Intrinium's confidential report is available to Board members upon request.

Mr. Hill moved that the Board approve the IT Security Review and Compliance Audit. Mr. Masten seconded the motion.

Mr. Longbrake referenced a session at the University of Maryland's Director's Institute which he recently attended and the experts' recommendations that best practice involves conducting some components of this type of audit annually. Mr. Mackison noted the WSIB currently conducts this review every three years but agreed that more frequent reviews would be beneficial. Mr. Hill agreed to discuss the frequency of IT security reviews at the next Audit Committee meeting.

In response to a question from Mr. McElligott, Mr. Mackison confirmed that the vast majority of the audit's recommendations have already been implemented and the remaining items will be resolved by the end of July. The vendor will review the WSIB's progress in August.

Ms. Owens stressed how important it is to stay on top of IT security and noted that the recommendations in the audit all seemed to be easily implemented.

The motion carried unanimously.

2011 Conflict of Interest Policy Compliance Review Auditor Appointment

Mr. Hill reported that the Audit Committee recommends the 2011 Conflict of Interest Policy Compliance Review be conducted by an external audit service provider.

Mr. Hill moved that the Board appoint Peterson Sullivan LLP to perform the calendar year 2011 Conflict of Interest Compliance Review. Mr. Masten seconded and the motion carried unanimously.

Fiscal Year 2013 Internal Audit Plan

Mr. Hill noted the rigorous risk assessment process that was used to identify the eight audit areas incorporated into the fiscal year 2013 internal audit plan.

Mr. Hill moved that the Board adopt the Fiscal Year 2013 Internal Audit Plan. Ms. Owens seconded and the motion carried unanimously.

PRIVATE MARKETS COMMITTEE REPORT

Mr. Masten noted that the Private Markets Committee met on June 7 to consider two private equity investment recommendations, additions to the tangible assets consulting pool, and policy revisions for private equity and real estate.

In addition to the detailed investment-specific discussions with staff, Hamilton Lane and the WSIB's general partners regarding the proposed private equity investments, lengthy discussions took place at the Private Markets Committee meeting regarding the current market conditions in Europe, the WSIB's overall exposure to the euro, and potential impact to the WSIB's investments if the situation were to worsen.

Advent International GPE VII, L.P.

Mr. Masten moved that the Board invest up to \$400 million, plus fees and expenses, in Advent International GPE VII L.P., subject to continuing due diligence and final negotiation of terms and conditions. Mr. McElligott seconded the motion.

Mr. Nierenberg noted the full discussion at the Private Markets Committee meeting regarding the market conditions in Europe and the effect on the two private equity investments before the Board. He stated that the in-depth information on the investments provided by staff and the Board's consultant addressed the questions he had prior to the Private Markets Committee meeting.

Mr. Masten stated that GPE VII will pursue control positions in buyout, recapitalization, and growth equity opportunities in upper middle-market companies with enterprise values of €200 million to €2 billion in the developed private equity markets of Continental Europe, the United Kingdom, and North America. Advent is an existing relationship for the WSIB, as the Board has invested in three prior Advent funds. The proposed investment is consistent with the Board-approved 2012 private equity annual plan and model portfolio. The recommendation is based, in part, on the firm's experience, team, global presence, proven investment strategy, 23-year performance history, strong sector focus, in-depth industry knowledge, and fit in the WSIB's private equity portfolio.

The motion carried unanimously.

Nordic Capital Fund VIII, L.P.

Mr. Masten moved that the Board invest up to €320 million, plus fees and expenses, in Nordic Capital Fund VIII, L.P., subject to continuing due diligence and final negotiation of terms and conditions. Vice Chair Ragan seconded the motion.

Nordic VIII is a buyout fund focused on the Nordic region with a target size of €4 billion. The fund will invest in sector-diversified, large- and middle-market companies primarily in Sweden, Norway, Finland, Denmark, and Germany. The WSIB has invested in five previous Nordic Capital funds. The proposed investment is consistent with the Board-approved 2012 private equity annual plan and model portfolio. The recommendation is based, in part, on Nordic's experienced and stable investment team, consistent and successful investment strategy, strong realized track record for over 20 years, and fit in the WSIB private equity portfolio.

The motion carried unanimously.

Tangible Assets Consultant Pool

Mr. Masten moved that the Board approve the addition of Altius Associates, Callan Associates Inc., Meketa Investment Group, Inc., Mercer Investment Consulting, Inc., and TorreyCove Capital Partners LLC to the Tangible Assets consulting pool, subject to continued due diligence and final negotiation of terms and conditions. Mr. McElligott seconded the motion.

To address gaps in the current lineup of consultants in the Tangible Assets consulting pool, staff issued a Request for Qualifications and Quotations (RFQQ) on February 10 seeking proposals from firms to be placed in a pool to provide consulting services for Tangible Assets. Nine firms submitted proposals to provide consulting services for tangible assets investments, which staff evaluated based on the depth, stability, and capacity of the organization; experience and expertise of the staff; quality and innovativeness of the consulting services and advice provided; and the quality of the research and due diligence process. The review culminated in a recommendation to add the identified firms to the pool. Courtland Partners responded to the RFQQ, but it was unnecessary for them to do so as they are already in the consulting pool.

The motion carried unanimously.

Board Policy Review – Substantive Policy Revisions

Mr. Masten moved that the Board adopt the proposed substantive revisions to policy 2.10.600. Vice Chair Ragan seconded the motion.

The intent of the proposed real estate investment policy revisions is to redefine geographic and property type diversification guidelines.

Mr. McElligott noted the discussions of the policy revisions that took place at the Private Markets Committee and expressed his appreciation of the information provided by staff at that meeting. Ms. Owens stated that, while she is not a member of the Private Markets Committee, she attends the meetings and appreciates the depth of discussion that takes place.

The motion carried unanimously.

Mr. Masten moved that the Board adopt the proposed substantive revisions to policy 2.10.700. Vice Chair Ragan seconded.

The proposed private equity investment policy revisions reflect the evolution of the investment categories used to segment the portfolio; discontinuation of the Board's discretionary venture capital manager program, while maintaining the flexibility to add discretionary manager programs in the future; and lowering of the guideline limiting the percentage of a fund that the WSIB should generally be, consistent with existing practice and the Board's continued focus on risk management.

Chair McIntire noted that the policy revisions reflect the diversification of the private equity investments.

The motion carried unanimously.

[The Board recessed at 10:17 a.m., and reconvened at 10:31 a.m.]

ADMINISTRATIVE COMMITTEE REPORT

Chair McIntire reported the WSIB has a projected appropriated budget balance of \$610,000, a 4.3 percent savings, and a projected non-appropriated budget balance of \$27.2 million, which represents a savings of 8 percent.

Four-Year Resource Plan and 2013-2015 Biennial Budget

Mr. Moore introduced himself and presented the four-year resource plan and 2013-2015 biennial appropriated budget. The WSIB's budget is funded from assets under management and sorted into two categories: operations expenses (appropriated budget) and investment expenses (non-appropriated budget). The Office of Financial Management monitors both appropriated and non-appropriated expenditures. Mr. Moore reviewed the budget cycle timeline, budget process, and budget categories.

Mr. Moore reviewed a summary of the four-year resource plan which addresses staffing needs, supports investment strategies, provides competitive salaries, and prepares for the accounting book-of-record conversion. The first two years of the plan are incorporated into the 2013-2015 biennial budget proposal. The proposed appropriated budget is estimated at \$34,533,000, which represents 0.041 percent of total assets under management. The proposed non-appropriated budget for 2013-2015 biennium is estimated at \$694,998,780.

Mr. Moore reviewed the Board-approved compensation plan for investment staff which will make progress in closing the 42 percent compensation gap between WSIB investment officers and the average investment officer compensation of WSIB's peers. The first move in closing the gap will be reinstatement of the 3 percent salary reduction on June 30, 2013, per current law. The proposal then assumes a two-step move of raising Investment Officer salaries in 2014 and 2015. The proposal, with a cost of \$1.4 million, would bring WSIB Investment Officer compensation in 2015 to within 10 percent of the 2010 average compensation of WSIB's peers.

Mr. Moore noted that over 94 percent of the non-appropriated budget is spent on investment management fees. He reviewed a chart which compared the size of the appropriated and non-appropriated budgets, with appropriated expenses representing 4.74 percent of the WSIB's total 2013-2015 biennial budget. Mr. Moore also reviewed a chart depicting the relationship between the WSIB's costs and growth in assets under management. The costs, shown as basis points, reflect a downward trend as assets under management increase. Another chart reflected the WSIB's position as less expensive and higher performing compared to peers.

Mr. Moore concluded by reviewing the expected results of investments in new staff, compensation, and additional resources, which are to meet the targeted rate of return, remain

disciplined in our investment approach, and sustain our operational excellence, all in the best interests of the WSIB's beneficiaries.

Chair McIntire moved to approve the proposed 2013-2015 operating biennial budget. Vice Chair Ragan seconded and the motion carried unanimously.

Board Self-Evaluation Process

Chair McIntire reported the Administrative Committee discussed how to conduct the Board's annual self-evaluation at the July Board meeting. The Committee recommends the Board forego using the evaluation tool used in recent years and, instead, complete the risk and governance survey tool prepared by Rick Funston and participate in discussions Mr. Funston will facilitate on July 18 and 19. Chair McIntire requested that all members respond to the survey.

Chair McIntire moved to approve the governance survey designed by Mr. Funston in place of the previous tool for its 2012 self-evaluation. Vice Chair Ragan seconded and the motion carried unanimously.

Board Policy Review

Mr. Moore summarized the process used for the 3-year review of Board policies. The reviewed policies fall into four categories. Rescinded, substantive, or technical changes to policies require appropriate Committee and Board action, while policies with no recommended changes are brought to the Board for reaffirmation.

Mr. Moore reviewed the reasons for the recommendation that four policies be rescinded: (1) The addendum to Policy 2.05.200 Proxy Voting is no longer pertinent to the way proxies are voted; (2) Policy 2.05.700 Directed Brokerage is no longer needed as the directed brokerage program has been discontinued; and (3) Policies 2.15.600 Pension Funding Stabilization Account and 2.35.300 Budget Stabilization Account are no longer needed as the assets were moved to the Office of the State Treasurer pursuant to RCW 41.45.230.

Chair McIntire moved that the Board approve the rescinding of policies 2.05.200 Addendum, 2.05.700, 2.15.600, and 2.35.300. Mr. Masten seconded and the motion carried unanimously.

Mr. Moore reviewed the recommended substantive policy revisions. The revisions to Policy 1.10.100 Role of Consultants add risk and compliance and research consultants to the list of consultant contracts approved by the Executive Director and delete references to deal log reporting, which occurs at the staff level, and investment referrals, which are covered under 2.05.800 (Investment Referral Process). The revisions to Policy 2.01.100 Investment Officer Compensation Levels limit automatic cost of living adjustments of investment officer pay ranges to statutory upper limits.

Chair McIntire moved that the Board approve the proposed substantive changes to policies 1.10.100 and 2.01.100. Vice Chair Ragan seconded and the motion carried unanimously.

Mr. Moore noted that a table detailing the proposed technical policy revisions was available in the Board materials. He clarified that the proposed technical revisions to Policy 2.00.210 Board Operations do not contain staff's original recommendation to the Administrative Committee that a quorum of the Board be present in order to discuss current or future Board actions. The Administrative Committee originally approved that change, but the language was subsequently determined to be too restrictive and was removed.

Chair McIntire moved that the Board adopt the proposed technical revisions to 1.00.170, 1.00.180, 1.05.100, 1.10.200, 2.00.175, 2.00.210, 2.00.240, 2.00.250, 2.00.260, 2.01.000, 2.01.050, and 2.01.150. Vice Chair Ragan seconded and the motion carried unanimously.

Mr. Moore noted that there were no changes recommended to nine policies, which require reaffirmation by the Board as part of the 3-year policy review.

Chair McIntire moved that the Board reaffirm approval of policies 1.00.140, 1.00.150, 2.00.150, 2.00.230, 2.00.900, 2.05.500, 2.05.600, 2.10.800, and 2.14.200 with no recommended changes. Vice Chair Ragan seconded and the motion carried unanimously.

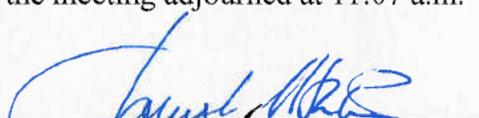
Chair McIntire and Theresa Whitmarsh noted that the WSIB's process for establishment and management of Board policies is looked at as a best practice by other public pension funds.

Assistant Attorney General's Report

Mr. Dietrich updated the Board on the status of a lawsuit in California regarding Terramar Retail Centers, one of the Board's real estate investments. Terramar's counsel, which also represents the WSIB in this matter, has filed a motion to dismiss WSIB from the suit.

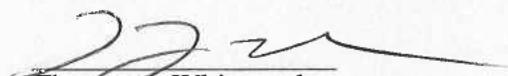
OTHER ITEMS

There were no further items to come before the Board, and the meeting adjourned at 11:07 a.m.



James L. McIntire
Chair

ATTEST



Theresa J. Whitmarsh
Executive Director