

WASHINGTON STATE INVESTMENT BOARD
Board Meeting Minutes
April 16, 2015

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: Marcie Frost, Chair
Kelly Fox, Vice Chair
Arlista Holman
Judy Kuschel
Bill Longbrake
George Masten
Treasurer Jim McIntire
Stephen Miller
Richard Muhlebach
Bob Nakahara
David Nierenberg
Joel Sacks
Jeff Seely

Absent: Senator Mike Hewitt
Representative Timm Ormsby

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
Allyson Tucker, Senior Investment Officer – Risk Management
and Asset Allocation
Diana Will, Senior Investment Officer – Tangible Assets
Kristi Haines, Confidential Secretary

Mary Lobdell, Attorney General’s Office
Tor Jernudd, Attorney General’s Office
Scott Daniels, Conning Asset Management
Neil Rue, Pension Consulting Alliance

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

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

ADOPTION OF THE FEBRUARY 19, 2015, MINUTES

Vice Chair Fox moved to adopt the February 19, 2015, minutes. Ms. Holman seconded, and the motion carried unanimously.

PUBLIC COMMENT

There was no public comment.

EXECUTIVE DIRECTOR'S REPORT

Ms. Whitmarsh reported all of the May Board and Committee meetings were cancelled. She detailed recent meetings she attended including a presentation before the Community Development Round Table (CDRT) in Seattle. Mr. Seely suggested she provide an overview of the WSIB to the CDRT, which is comprised of business and civic leaders. She noted former Governors Spellman and Evans, and former Congressman Slade Gorton attended. Ms. Whitmarsh introduced newly-hired staff, and reported on the strategic workforce strategy project, which gears staff toward taking charge of their careers and has resulted in some recent promotions that she detailed. Ms. Whitmarsh said the WSIB's full budget request was included in the Governor, House, and Senate proposed budgets, so it appears to be in good shape for approval. She said she recently moderated a session on activism with Mr. Bill Ackman, Pershing Square Capital Management, at the Council of Institutional Investors Spring Meeting. Ms. Kate Sandboe also participated in a panel during the Corporate Governance 101 session at the same meeting. Lastly, Ms. Whitmarsh said the WSIB had joined other institutional investors in signing a letter to the Securities and Exchange Commission relating to carbon emissions disclosure.

EDUCATION SESSION

Labor and Industries Annual Review

Mr. Daniels, Conning Asset Management, presented the Labor and Industries (L&I) annual review, including Conning's role in working with the WSIB and L&I in designing strategy, capital structure, and objectives that are appropriate for the insurance operations/workers' compensation program. He gave a brief overview of Conning's operations and the L&I portfolio, which is comprised of four funds: (1) the Accident Fund, which provides benefit for lost wages; (2) the Medical Aid Fund, which pays for medical treatment and carries an inflation risk; (3) the Pension Reserve Fund, which pays pensions to disabled workers and is funded with transfers from the Accident Fund; and (4) the Supplemental Pension Fund, which is the pay-as-you-go cost of living adjustment for pensions.

Mr. Daniels reported the L&I portfolio totaled just under \$15 billion as of year-end 2014. Its allocation is primarily comprised of investment-grade fixed income, with common stocks as the second largest allocation, and a small allocation (less than 5 percent) to high yield bonds. He said Washington State's L&I program is the second largest workers' compensation fund in the U.S. He described the difference between a typical insurance portfolio's holdings and the WSIB's portfolio, with and without the L&I fund investments. He said that L&I does consider industry norms when creating its portfolio, which include limits on higher-risk investments and capital adequacy requirements. L&I had almost \$1 billion in capital at the last fiscal year-end to support risks to the portfolio, loss and benefit reserves, and premiums. Mr. Daniels said that L&I cannot afford too much

volatility from investments, which is why the portfolio allocation is set up the way it is. A discussion ensued on capital adequacy measures.

Mr. Daniels said the current target for capital is \$1.5 billion. Mr. Sacks said that L&I's target goal is to have assets at 114 percent of liabilities, and currently the number is 107 percent. L&I has worked with the business and labor community on a plan to ramp up to 110 to 114 percent to endure fluctuations in the stock market and slowly grow the reserves. He said the challenge is actuarial discounting. L&I is also looking at other asset classes in which the WSIB invests that may help. Mr. Daniels said Conning has done modeling to get a sense of risk, plans to sit down with staff to see what options are administratively possible, and then will also speak with stakeholders to see if they are interested in expanding the asset allocation.

Mr. Daniels responded to Board members' comments and questions about whether the L&I numbers include self-insured workers, risks faced by L&I, and the level of legislative involvement.

ADMINISTRATIVE COMMITTEE REPORT

Charter of the Board Chair 1.00.160 and Board Education 2.00.200 3-Year Policy Review

Chair Frost reported the Administrative Committee met earlier this morning.

3-Year Policy Review

Chair Frost said Mr. Moore presented the Charter of the Board Chair 1.00.160 and Board Education Policy 2.00.200 with no recommended changes.

Chair Frost moved that the Board reaffirm approval of the Charter of the Board Chair 1.00.160 and the Board Education Policy 2.00.200 with no recommended changes. Vice Chair Fox seconded, and the motion carried unanimously.

Directors and Officers Insurance Analysis

Chair Frost reported the Committee received information on Directors and Officers Insurance (D&O), a summary of existing coverage and protections, and a comparison of the Self-Insurance Liability Program to D&O. She also provided an Attorney General opinion, dated January 17, 2008, on liability of Board members.

Based on staff assessment, the Committee agreed the WSIB Board member current liability protections are sufficient, and no additional D&O liability insurance is recommended.

Executive Director Evaluation Process

Chair Frost announced the executive director's evaluation is due in June. The process will be conducted as it was last year, via Survey Monkey. Input from members will be due June 5, and results will be discussed at the June 18 Administrative Committee and Board meetings. She said Ms. Whitmarsh's three-year contract expires in September so she would like to back-up the timeframe of her evaluation to allow sufficient time for it to go before the State Finance Committee for confirmation prior to the end of Ms. Whitmarsh's term. Chair Frost said she felt the evaluation questions from the previous year are

sound, and Board members and direct reports of the Executive Director will provide comment. Ms. Haines will distribute the survey in mid-May.

Assistant Attorney General's Report

Ms. Lobdell introduced Mr. Tor Jernudd, who is replacing Ms. Dawn Cortez.

Ms. Lobdell provided an update on the Seaport Village litigation, which began in San Diego and involves Terramar, one of the real estate investment companies the WSIB invests in. Ms. Lobdell reported the WSIB was dismissed from the San Diego litigation, but Seaport Village refiled the litigation in Delaware and included the WSIB and Calzada Capital Partners LLC as defendants. The WSIB and Calzada were dismissed without prejudice from the Delaware litigation.

EXECUTIVE SESSION

Assistant Attorney General's Report - Continued

Chair Frost announced the Board would go into executive session to discuss litigation or potential litigation with legal counsel since public knowledge regarding the discussion is likely to result in an adverse legal or financial consequence to the WSIB. She said the executive session was expected to last until about 5 minutes, at which time the Board would take a brief recess and then reconvene in open public session.

[The Board went into executive session at 10:20 a.m., and then took a brief recess at 10:34 a.m. The Board reconvened in open session at 10:47 a.m.]

CAPITAL MARKET ASSUMPTIONS

Ms. Tucker introduced Mr. Rue of Pension Consulting Alliance (PCA). PCA has worked with the WSIB for 10 years on its asset allocation studies. This year, PCA was asked to develop and recommend the capital market assumptions (CMAs). Ms. Tucker referred to the white paper distributed to Board members, which contains educational components to accompany the Board's decision on adopting staff's proposal.

Mr. Rue noted a correction on slide 15 of the presentation, the graphed line representing Wilshire should be adjusted up and that he would send a corrected slide.

Mr. Rue began by defining correlation as how the asset classes move in relationship to each other over a given time period. He said expected investment risk is another dimension to understand. He said in developing CMAs, consultants' expectations are used, which are achieved by applying proprietary approaches to develop estimates. These expectations are arrived at independently of staff initially, then presented, vetted, and adjusted before the proposal comes to the Board for consideration. He said that consultants' expectations and risk variances can widely range one from another, and there are differing views on what falls into assets classes, such as Tangible Assets. He noted the WSIB's tangible assets class is custom in nature. He provided the history and comparison of geometric return assumptions over the past 15 years. He said, going forward, assumptions have dampened a bit, due to the nature of the global economy.

Mr. Rue presented simulated return expectations for the Commingled Trust Fund (CTF) over 1-and 15-year time horizons using the 2105 proposed CMAs as shown below:

	Arithmetic Return (%)	Standard Deviation (%)	Geo. Comp. Return (%)
Fixed Income	3.90	5.25	3.77
Tangible Assets	6.60	8.60	6.25
Real Estate	8.00	15.70	6.85
Global Equity	8.80	18.85	7.15
U.S. Equity	8.25	18.00	6.74
Non-U.S. Equity	9.25	20.70	7.27
Private Equity	11.80	25.00	8.97
Cash	2.30	2.00	2.28
Inflation	2.20	1.45	2.19

(Geo. Comp. Return Change Since 2013:)

Comments:

- Higher consensus plus unique WSIB structure (higher yield, more credit)
-
- Higher risk assumptions of WSIB components increased volatility's impact
- 20 basis points (bps) increase in risk assumption of WSIB structure/leverage
- Lower consensus return and risk assumptions translate to a slight decline
- Lower risk assumption decreased volatility's impact on the compound return
-
- Higher consensus expectations due to valuations and long-term currency trend
- Lower risk assumption versus 2013, increasing compound return by 23 bps
- Lower consensus levels plus WSIB structure slightly above consensus
- Adjusted in line with lower consensus levels

A discussion ensued on approaches and premiums used in developing estimated returns by asset classes, the differences between the proposed 2015 and 2013 CMAs, and any trends that have occurred in classes consistently going up or down in terms of perceptions. Mr. Rue and Ms. Tucker said the white paper contains some of these details. Mr. Rue said one trend is a modest decline in volatility since the 1920s. Mr. Bruebaker said the minor changes in these CMAs essentially do not hold major implications for the current asset allocation for the CTF. He noted that CMAs used to be reviewed every year, now the CMAs are reviewed every other year.

Vice Chair Fox moved that the Board adopt the proposed 2015 capital market return, risk, and correlation assumptions. Treasurer McIntire seconded, and the motion carried unanimously.

Mr. Bruebaker noted the Office of the State Actuary (OSA) uses the WSIB's CMAs (which are a 15-year view), in its 50-year statistical analysis. The WSIB's CMAs serve as a consideration for OSA, rather than a definitive input. He said the numbers are affected by whatever time horizon is being looked evaluated.

PRIVATE MARKETS COMMITTEE REPORT

Mr. Masten reported the Private Markets Committee met on April 2 to consider six investment recommendations.

[Mr. Miller left at 11:27 a.m.]

TA XII, L.P.

Mr. Masten moved that the Board invest up to \$250 million, plus fees and expenses, in TA XII, L.P., subject to continuing due diligence and final negotiation of terms and conditions. Vice Chair Fox seconded the motion.

Mr. Masten said, consistent with the strategy of the prior funds, TA XII will make both minority and control investments in rapidly-growing middle-market companies, primarily in North America and Western Europe. The fund will invest across several industry sectors, including technology, healthcare, financial services, consumer, and business services. The WSIB has invested in 4 prior TA funds since 1997. The proposed investment is consistent with the Board-approved 2015 private equity annual plan and the private equity model portfolio. He said the recommendation is based on TA's deep and experienced investment and deal origination teams, strong long-term track record, focused and consistent investment strategy, complementary fit in the WSIB's private equity portfolio, and other factors relevant to the recommendation.

The above motion carried unanimously.

Rhône Partners V, L.P.

Mr. Masten moved that the Board invest up to €150 million, plus fees and expenses, in Rhône Partners V L.P., subject to continuing due diligence and final negotiation of terms and conditions. Vice Chair Fox seconded the motion.

Mr. Masten said the fund will invest in middle-market companies with a focus on achieving value creation through operational improvements and international expansion initiatives. Investments will be made in both Europe and North America with no dedicated percentage allocation to either region. If approved, Rhône would be a new general partner relationship for the WSIB. The investment would fall into the unidentified allocation in the Board-approved 2015 private equity annual plan and is consistent with the model portfolio. He said the recommendation is based on the firm's experienced team, strong track record, value-added investment approach, excellent fit with the WSIB's private equity portfolio, and other factors relevant to the recommendation.

[Mr. Miller returned at 11:30 a.m.]

The above motion carried unanimously.

Blackstone Capital Partners VII, L.P.

Mr. Masten moved that the Board invest up to \$500 million, plus fees and expenses, in Blackstone Capital Partners VII, L.P., subject to continuing due diligence and final negotiation of terms and conditions. Vice Chair Fox seconded the motion.

Mr. Masten reported the fund will invest in classic buyouts, growth equity, buy and build platforms, and strategic minority investments on a global basis across multiple industry sectors. The WSIB has invested in two prior Blackstone funds since 2006. This proposed investment is consistent with the Board-approved 2015 private equity annual plan and model portfolio. He said the recommendation is based on the firm's strong franchise, deep and experienced investment team, extensive operational value-creation capabilities, long-term track record, fit within the WSIB's private equity portfolio, and other factors relevant to the recommendation.

The above motion carried unanimously.

Teays River Investments, LLC

Mr. Masten moved that the Board invest up to \$300 million, plus fees and expenses, in Teays River Investments, LLC, or a related special purpose vehicle, subject to continuing due diligence and final negotiation of terms and conditions. Vice Chair Fox seconded the motion.

Mr. Masten reported that Teays River is a diversified, U.S.-focused, privately-owned agricultural holding company with vertically integrated upstream and midstream assets in four operating segments: organic dairy, seed production, table grapes, and row crops. Teays is seeking to raise new equity to finance its plan to expand its existing operating segments, invest in new opportunities, and provide liquidity to current shareholders on a negotiated basis. This proposed investment is consistent with the Board-approved 2015 tangible assets annual plan. He said the recommendation is based on Teays' strong record of building and operating platform companies, experienced team, high visibility of current and future assets, the firm's vertically integrated operations, exposure to protein, potential to hold assets long term, the low-cost strategy with an alignment of interest, fit within the tangible assets portfolio, and other factors relative to the recommendation.

The above motion carried unanimously.

EnerVest Energy Institutional Fund XIV, L.P.

Mr. Masten moved that the Board invest up to \$200 million, plus fees and expenses, in EnerVest Energy Institutional Fund XIV, L.P., subject to continuing due diligence and final negotiation of terms and conditions. Vice Chair Fox seconded the motion.

Mr. Masten said EnerVest Energy Institutional Fund XIV, L.P. (Fund XIV), is a \$2.5 billion (target) fund that will pursue investments in natural gas and oil properties throughout the United States. This proposed investment is consistent with the Board-approved 2015 tangible assets annual plan. EnerVest currently manages \$11 billion on behalf of 177 institutional limited partners, focusing on value-related and contrarian strategies in oil and gas. Fund XIV will focus on out-of-favor assets and will likely include both oil and natural gas assets, given the distress in both markets. The Enervest team has particular expertise in natural gas assets, which have been deeply out of favor given the low price/supply glut dynamic in play since 2008. EnerVest pursues a strategy of establishing large footholds in specific basins and seeks to establish "basin dominance," which it defines as being a top five producer in a given basin. Since its founding in 1992, EnerVest has managed 13 closed-end funds and 4 dedicated co-investment vehicles. He said the recommendation is based on EnerVest's experienced team, demonstrated performance, large existing footprint, balance of income with capital growth, exposure to strong fundamentals of natural gas, attractive entry point due to current market dislocation, portfolio fit, and other factors relative to the recommendation.

The above motion carried unanimously.

Principal Enterprise Capital Holdings LLC

Mr. Masten moved that the Board invest an additional \$500 million, plus fees and expenses, in Principal Enterprise Capital Holdings LLC and authorize the transfer to PECH of the WSIB's direct \$200 million commitment to Alere Property Group, subject to continuing due diligence and final negotiation of terms and conditions. Vice Chair Fox seconded the motion.

Mr. Masten reported the WSIB has previously committed \$2.3 billion to Principal Enterprise Capital Holdings LLC (PECH) in five increments, beginning in 1999, and \$200 million directly to Alere in 2011. If this recommendation is approved, the WSIB's total commitment to PECH will be \$3 billion. PECH is sponsored by Principal Enterprise Capital, a Chicago-based Registered Investment Advisor that is a wholly-owned affiliate of Principal Real Estate Investors. Alere is a real estate operating company majority-owned by PECH. PECH's strategy is to invest in or with real estate operating companies, consistent with the WSIB's primary strategy for real estate investment. At present, the Partnership is invested in seven companies and has committed \$2.045 billion of the WSIB's current \$2.3 billion commitment to PECH. This new commitment is necessary for the further growth of existing portfolio companies or for commitments to new companies. He said the recommendation is based on the WSIB's successful long-term relationship with PEC management, excellent returns, the diversification created by the investment, concentration in relatively conservative strategies, attractive governance rights, and other factors related to the recommendation.

The above motion carried unanimously.

AUDIT COMMITTEE REPORT

Treasurer McIntire reported the Audit Committee met on March 3 to review the scope of work and auditor appointment recommendations for the 2015 External Audit Services.

For the upcoming Fiscal Year 2015 audit of the Board-prepared financial statements, staff would like to engage Eide Bailly LLP to perform the independent audits based on the firm's audit experience, qualifications and experience of the proposed auditors, and proposed fees.

Treasurer McIntire moved that the Board appoint Eide Bailly LLP to perform the Fiscal Year 2015 independent financial audits. Ms. Holman seconded, and the motion carried unanimously.

The Committee also reviewed the scope of services proposed to conduct a comprehensive Information Technology (IT) security review, perform penetration testing, and conduct an application controls review of the WSIB's Data Warehouse and Performance System. Staff would like to engage Intrinium to perform this work based on the qualifications and experience of the proposed staff, quality of previous performance, and proposed fees.

Treasurer McIntire moved that the Board appoint Intrinium to conduct a comprehensive IT security review, perform penetration testing, and conduct an application controls review of the WSIB's Data Warehouse and Performance System. Ms. Holman seconded, and the motion carried unanimously.

The Committee received an internal audit report on the Board's custody bank, State Street Bank. The overall results were positive, and the report contained one audit recommendation regarding outgoing wire payments. State Street Bank and the WSIB staff agreed with the recommendation, and the Committee will receive a status update on the resolution at its June meeting.

The Committee received updates on the status of prior audit recommendations; the annual audit plan status, proxy voting results for 2014; the quarterly investment referrals log; and the 2014 Personal Investment Report.

Treasurer McIntire reported the Committee heard a panel discussion on high frequency trading and dark pools, and how WSIB and its managers monitor trading to ensure trade execution is in the best interests of beneficiaries. It received an overview of the 2014 Enterprise Risk Management and Investment Compliance Program work. WSIB staff described the investment compliance testing processes and presented the 2014 results.

WSIB staff presented the Daily Valued Funds Annual Report, which noted two errors in the new U.S. Treasury Inflation Protected Securities Fund. The only participant in the TIPS fund is the Retirement Strategy Funds 2000-2025. The errors had no impact on the overall unit prices of this fund. The Committee is proposing revisions to the Board's Daily Valued Funds (DVF) Operations Policy 2.14.300, which has been updated to allow the DVF's book of record to be either the custodian bank or the investment accounting system. A change was also made regarding the daily cash factor. If the current day's factor is not received timely, the prior day's factor may be used.

Treasurer McIntire moved that the Board approve the revisions to the Daily Valued Funds Operations Policy 2.14.300. Ms. Holman seconded, and the motion carried unanimously.

Lastly, the Committee met in executive session to discuss the Audit Director's performance evaluation.

EDUCATION REPORT

Council of Institutional Investors (CII) Spring Meeting

Treasurer McIntire complimented Theresa's moderated panel presentation on activism investing. Although this is not an area the WSIB invests in, the discussion raised some interesting questions. A panel he found particularly interesting and engaging was a discussion with the Chief Justice of the Delaware Supreme Court. This also raised a number of interesting questions including whether CII should have a policy with regard to annual votes on say on pay and membership, which was referred to as "annual froth," and whether or not it is productive for a board, as well as compensation strategy, and whether or not significant changes should be made relating to that year-to-year. Treasurer McIntire said he found it particularly refreshing the Chief Justice did not seem

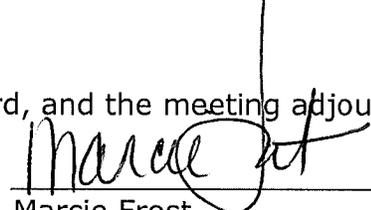
to mind raising questions that are not necessarily popular or the conventional wisdom of the CII audience.

Mr. Masten reported he found the Spring Meeting better this year than last year and noted the changes within the CII Board over the 22 years he has been involved. He agreed the Justice's presentation was very good. He commented that trustees need to pay particular attention to losses being filed, where the only gains seem to be made by the attorneys. While that has not happened here, he said he feels a lot of unnecessary work goes into groups trying to be lead plaintiff in a lawsuit that does not necessarily have a lot of stock. He found the activism discussion interesting, but he said he cannot figure out why anyone would want to invest in it. Mr. Masten commented on women who were at the conference representing corporate boards, and he wished there were more women participants, rather than a few who participate on many boards. He commented on an AFL-CIO side meeting he attended.

Treasurer McIntire congratulated Ms. Whitmarsh on her appointment as co-Chair of CII. A discussion ensued regarding the financial state of the CII and sponsorship of the events.

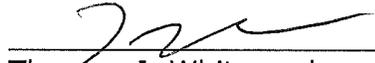
OTHER ITEMS

There was no further business to come before the Board, and the meeting adjourned at 11:56 a.m.



Marcie Frost
Board Chair

ATTEST



Theresa J. Whitmarsh
Executive Director