

**South Carolina Retirement System Investment Commission
Meeting Minutes**

March 20, 2008

**Second Floor Conference Room
202 Arbor Lake Drive
Columbia, South Carolina 29223**

Commissioners Present:

Mr. Reynolds Williams, Chairman
Mr. James Powers, Vice Chairman
State Treasurer Converse Chellis
Mr. Blaine Ewing
Mr. Allen Gillespie
Dr. Travis Pritchett

Others present for all or a portion of the meeting: Dunkin Allison, Robert Borden, Donald Brock, Brenda Gadson, Douglas Lybrand, Heather Muller, Rick Patsy, Greg Putnam, Kathy Rast, Nancy Shealy, Nicole Waites, Brian Wheeler, and Hilary Wiek from the South Carolina Retirement System Investment Commission; Mike Addy, Delores Dacosta, Rick Harmon, and Shakun Tahiliani from the State Treasurer's Office; Rhett Humphreys from New England Pension Consultants; Peggy Boykin, Sarah Corbett, Tammy Davis, Robyn Leadbitter, John Page, Danielle Quattlebaum, Kelly Rainsford, Joni Redwine, Travis Turner, and Faith Wright from the South Carolina Retirement Systems; Kent Phillips from the State Retirees' Association; and Greg Nordquist from Russell Implementation Services, Inc.

I. CALL TO ORDER, CONSENT AGENDA, AND CHAIRMAN'S REPORT

Chairman Reynolds Williams called the meeting of the South Carolina Retirement System Investment Commission (Commission) to order at 10:00 a.m. and welcomed the Commissioners and guests.

Chairman Williams called for objections or amendments to the meeting's proposed agenda. There being none, the proposed agenda was adopted as presented. Chairman Williams called for objections or amendments to the minutes from the meetings on October 18, 2007, and February 21, 2008, and there being none, the minutes were approved. The minutes from the meeting November 19-20, 2007, were carried over.

Chairman Williams reported on the Institutional Investor and Information Management Network (IMN) Public Pension Fund Awards for Excellence and Public Funds Summit conference, which he and Mr. Robert Borden, Chief Investment Officer (CIO), attended in California. The South Carolina Retirement Systems (Retirement System) had been nominated as one of four finalists for the IMN's Large Public Plan of the Year Award. He reported that the New Jersey Retirement System received the award, but noted that it was a great honor for South Carolina to be recognized for its achievements. Chairman Williams was a speaker on 130/30 Investment Strategies, Mr. Borden was a speaker on Practical Applications of Derivatives, and they reported that it was an informative conference.

Chairman Williams provided an update on pending Sudan Divestment legislation (bill s.241). He reported that pursuant to a request from Senator Joel Lurie, he sent a letter to the Senator outlining some of the concerns discussed by the Commission. Chairman Williams said that his letter addressed the issues at a policy level and suggested that any costs for implementing

divestiture as proposed be paid from the State's general appropriations rather than the Retirement System trust funds. He said he expressed the Commission's general philosophical opposition to legislation that would determine where the Retirement System's assets would be invested because the investment decisions should be made based on fiduciary standards and on what is in the best interest of the members and beneficiaries of the Retirement System. Chairman Williams noted that the bill had since been amended to exempt certain types of investment vehicles and to delete some of the affirmative action requirements for the Commission. He reiterated that the Commission did not endorse the legislation in any form, but that he felt that the Commission should respond to inquiries of this nature.

II. ADMINISTRATIVE MATTERS

Chairman Williams recognized Ms. Nancy Shealy for the Administrative Director/General Counsel's report.

Ms. Shealy noted that meeting materials had been provided in notebooks rather than bound booklets to manage the materials in a more efficient and cost effective manner.

Ms. Shealy referred to hardcopies of the Retirement System's Comprehensive Annual Financial Report for Fiscal Year Ending June 30, 2007, which had been provided to the Commission as information.

Ms. Shealy provided the Commission with a budget status report for Fiscal Year (FY) 2008. She highlighted expenditures and projected expenses for the remainder of the fiscal year. The Commission discussed various aspects of the current budget, the budget process for future years, and future anticipated expenses. Chairman Williams noted that the Commission's expenses would begin leveling within the next few years, so budgeting should become more predictable and allow for "zero-based" budgeting. The Commission discussed resource projections for the Investment Division over the next few years, and Mr. Borden noted that some of the Investment Division's needs might depend on the resources that some of the strategic partnerships would provide in the future, which could decrease costs for the Commission.

(Information relating to these matters has been retained in the Commission's files and is identified as Exhibit A).

Ms. Shealy referred to the draft Continuing Education Policy, which had been provided to the Commission prior to the meeting for review. She noted that the draft addressed reimbursement for college tuition and costs associated with continuing education to acquire and maintain professional certifications that would enhance employees' job performance. The Commission reiterated the importance of continuing education and obtaining and maintaining professional certifications, and they discussed various provisions of the proposed policy.

Ms. Shealy advised that the FY08 Appropriations Act provided that upon approval, agencies could reimburse their employed attorneys for expenses for mandatory license fees/dues for membership in the South Carolina Bar Association (SCBA). She noted that while dues for other organizations had been authorized by law previously, this was the first year the expense was reimbursable for membership in the SCBA. Chairman Williams noted that membership in the SCBA was mandatory for attorneys to be licensed to practice law in South Carolina.

Mr. Blaine Ewing made a motion to adopt the proposed Continuing Education Policy, which was seconded by Dr. Travis Pritchett and passed unanimously. Chairman Williams noted that the Commission had concurred with the policy in principle in November, although the document had not been finalized. Mr. James Powers made a motion to make the Continuing Education Policy

effective retroactively to July 1, 2007. Mr. Ewing seconded the motion, which passed unanimously. The Commission reiterated the benefits of continuing education in terms of staff performance and incentives for retention and recruitment.

(Information relating to these matters has been retained in the Commission's files and is identified as Exhibit B).

Mr. Ewing made a motion to reimburse attorneys employed by the Commission for license fees/dues for membership in the South Carolina Bar Association in accordance with State law. Mr. Allen Gillespie seconded the motion, which passed unanimously.

Ms. Shealy referred to the Investment Division Organizational Chart and staffing plan. She explained that the Commission had previously approved organizational charts and internal position titles for the agency. After the meeting in November, Mr. Borden discussed changing the internal titles relating to "Equity" staff to include "Public Private Equities". The Chairman approved the changes in late January as an administrative matter to avoid delay in recruiting investment staff. Ms. Shealy recommended that the resulting changes to the organizational chart be ratified by the Commission to update the organizational chart approved previously. The Commission discussed the Administrative Division's organizational chart and the role of the Compliance Officer. They discussed whether the Compliance Officer should report directly to the Commission or through the Administrative Division with direct communications to the Commission. Ms. Shealy explained that the Compliance Officer would have the same reporting responsibility to the Commission as the CIO and the Administrative Director/General Counsel, but would be under the Administrative Division for administrative purposes.

Mr. Ewing asked about the time frames for filling vacant positions, and Chairman Williams asked Ms. Shealy to discuss the staffing plan for the Administrative Division. Ms. Shealy stated that the Commission had approved the position of Resource Coordinator at its November meeting. She reviewed the general responsibilities for the position and requested that the Commission authorize her to begin recruiting and hire a Resource Coordinator. With regard to the Compliance Officer, Ms. Shealy asked for guidance as to the specific job functions and minimum qualifications the Commission wanted for the position. Mr. Ewing asked for information about other states, and Ms. Shealy replied that based on a survey of other states, there were various responsibilities and reporting lines. She noted that some performed more accounting-type duties, while others monitored compliance with legal and investment policy matters. After further discussion, Ms. Shealy said she would provide additional information at the next meeting.

After further discussion, State Treasurer Converse Chellis made a motion to amend the organizational chart to ratify the changes to the internal titles in the Investment Division relating to Equity staff, to provide that the Compliance Officer would report directly to the Commission, and to make other technical changes to the organizational chart to conform to the discussions. Mr. Ewing seconded the motion. The Commission discussed the role of the Compliance Officer and job responsibilities further.

Chairman Williams asked about the status of current recruiting efforts. Mr. Borden said that he anticipated hiring the Director of Alternatives by the end of April and that Ms. Hilary Wiek was in the mid-point in recruiting for the Public and Private Equities Officer. Mr. Borden requested that the Commission authorize him to begin recruiting and hire the Alternatives Officer to avoid further delay in staffing the Investment Division.

After further discussion about staffing and matters to consider in its corporate governance policy, the pending motion relating to the organizational chart passed unanimously.

Mr. Gillespie made a motion to authorize the recruitment and hiring of an Alternatives Officer and Resource Coordinator. The motion was seconded by Mr. Ewing and passed unanimously.

(Information relating to these matters has been retained in the Commission's files and is identified as Exhibit C).

III. INVESTMENT MATTERS

Chairman Williams recognized Mr. Borden for the Chief Investment Officer's report.

Mr. Borden discussed the recent events involving Bear Sterns and the J.P. Morgan/Federal Reserve buyout of the firm. He noted that the Retirement System had no equity exposure in Bear Sterns, and two bond exposures totaling approximately \$55 million. He said that the Retirement System did not have any material negative impact by the events, and some of the Retirement System's hedge fund exposures may have gained from the events. The Commission discussed risk controls for these types of events, and Mr. Borden advised that he was working on the risk control plan and anticipated completion by the end of the year. Mr. Borden noted that he might recommend additional changes to the organizational structure of the Investment Division to provide dedicated staff for risk controls.

Mr. Borden introduced Ms. Wiek for a review of the long-only equity portfolio and explained that the purpose of the review was to provide a background for transitioning the total portfolio to the target allocation. Ms. Wiek reviewed the changes that had been made to the equity portfolio since January 2007, including the changes in managers and allocations. She compared the current allocations of each strategy to the target allocations and discussed aspects of each manager's performance and investment strategies. Ms. Wiek discussed the total portfolio needs and the role of the long-only equity portfolio and provided recommendations for strategic plans for the long-only portfolio. The Commission discussed the target asset allocations within the total portfolio compared to the current allocations and discussed the value added by the long-only equity portfolio relative to other asset classes.

(Information relating to these matters has been retained in the Commission's files and is identified as Exhibit D).

Mr. Borden discussed the recommendations relating to investment in the CVC European Equity V L.P. (CVC), which had been carried over from the previous meeting. CVC had been approved by the Commission in January, subject to satisfactory due diligence review by New England Pension Consultants, Inc. (NEPC). Mr. Borden asked Mr. Rhett Humphreys with NEPC to discuss their recommendations. Mr. Humphreys said that NEPC met with CVC in London and that while they liked the team and past performance was not an issue, CVC would not disclose information about future investments or complete NEPC's Request for Proposal information. He said that due to the lack of transparency and disclosure, NEPC did not recommend the investment. Dr. Pritchett, who had served on the search team, noted that while he and Ms. Wiek were comfortable with CVC based on their on-site due diligence meetings, they understood NEPC's concerns and would recommend that the Commission not move forward with the investment. Mr. Borden added that while unanimity of the search team was not required, there should be strong conviction to move forward absent unanimity. He said that there may be future opportunities with CVC and sufficient time to complete further due diligence. Dr. Pritchett said that the search team recommended that the Commission reconsider its prior approval of the investment. After further discussion, Mr. Powers made a motion to discontinue

negotiations to invest in CVC and rescind the Commission's prior approval of the investment, which was seconded by Mr. Ewing and passed unanimously.

Mr. Borden referred to information about the High Yield recommendations that had been provided to the Commission prior to the meeting. He said that the search team, which was comprised of Messrs. Ewing, Gillespie, and Borden and Mr. Rick Patsy, recommended that the Commission invest in the Loomis Sayles High Yield Full Discretion Trust (Loomis). Mr. Borden provided information about the diversification that this investment would provide for the portfolio and reviewed information about the recommended fund, including a description of investment strategy and the investment manager, the recommended allocations, and track record. Mr. Borden noted that due to a current allocation to another Loomis Sayles fund, Loomis Sayles would negotiate fees to aggregate the assets in both funds so as to provide a net fee not to exceed 50 basis points (bps), which would provide a reduction in the fees for the current investment and the recommended investment. He said that due to the nature of the fund, the recommendation was to invest an amount not to exceed \$500 million, with \$100 million to be funded initially and up to an additional \$400 million to be invested opportunistically over a period of time as recommended by the manager. The Commission discussed the high yield asset allocation in general, the differences in various investment strategies, the competitive advantages, the transition to the total portfolio target allocation, and the resulting diversification of the portfolio. Mr. Patsy echoed Mr. Borden's confidence in the investment manager, the investment strategy, and the firm. Mr. Humphreys said that NEPC concurred with the recommendations and the investment strategy. Chairman Williams asked if there was a sense of how long it would take to invest the full \$500 million allocation, and Mr. Borden replied that it would depend on opportunities identified by the manager. He explained that this particular manager was extremely disciplined and would not invest until the appropriate opportunities arose. After further discussion, Mr. Gillespie made a motion to invest up to \$500 million in the Loomis Sayles High Yield Full Discretion Trust with an initial allocation of \$100 million and the remainder to be invested as recommended, to authorize the Chairman or his designee to negotiate fees not to exceed 50 bps and to execute any necessary documents to implement the investment upon approval for legal sufficiency by General Counsel. Mr. Ewing seconded the motion, which passed unanimously.

(Information relating to these matters has been retained in the Commission's files and is identified as Exhibit E).

Mr. Borden referred to reports for the Retirement System's portfolio for periods ending January 31 and February 29, 2008, which were included in the meeting materials. He discussed the reports and said that staff had devoted time to developing processes to ensure proper reconciliation between managers and the custodian. Based on the Commission's meeting schedule, reconciliations and various methodologies used for analysis, he noted that there would be differences between the preliminary reports and final reports. Mr. Borden and the Commission discussed the performance of the managers, asset classes, and total portfolio.

Mr. Borden introduced Mr. Greg Nordquist with Russell Implementation Services, Inc., to review performance of the Beta Overlay Program. Mr. Nordquist discussed asset allocations and exposures, performance, index performance, and the Beta Overlay Program's value added to total portfolio in February 2008. Mr. Borden reviewed the mechanics of the Beta Overlay Program relative to the fixed income portfolio and overall transaction costs. He reiterated that parts of the gains would be realized by minimizing transition costs, which the Beta Overlay Program was designed to manage. Mr. Nordquist reviewed counterparty exposure and the costs and performance of synthetic replication of domestic and international exposures.

Mr. Borden referred to the Morgan Stanley risk reports, which were included in the meeting materials and compiled based upon the meetings the previous month with Messrs. Ewing, Gillespie, and Borden and Morgan Stanley to develop methods to monitor risks within the portfolio. The Commission discussed valuation assessment and liquidity and leverage analyses for the portfolio and the formats and contents of the reports.

(Information relating to these matters has been retained in the Commission's files and is identified as Exhibit F).

Mr. Borden referred to a list of Private Equity Advisory Board/Committee Seats, which was included in the meeting materials. He explained that the Commission had the right to seats on advisory committees for a number of the Retirement System's limited partnerships. He said that participating in the annual meetings could be beneficial, although there were logistical issues to consider such as time commitments and costs. Chairman Williams said that while he had not researched the issues or made a decision, he had some concerns about exposure to potential liability and ethical considerations relating to service on an advisory committee and wanted the Commission to be clear about any benefits or consequences before taking any action. Mr. Gillespie concurred and said that the Commission should develop a policy relating to service in limited partnerships in an advisory capacity. After discussing the benefits of participating on advisory committees, logistics of managing participation, and various ways to address the concerns, Chairman Williams said that he and Ms. Shealy would begin working on ways to address concerns about such participation so that the Commission could then address other issues and policies.

(Information relating to these matters has been retained in the Commission's files and is identified as Exhibit G).

Mr. Borden advised that he would provide the Commissioners with a draft of the Annual Investment Plan for FY 2008-2009 prior to April 1, 2008.

IV. OTHER BUSINESS

Ms. Shealy reminded the Commission that the deadline to file Statement of Economic Interest Forms with the State Ethics Commission was April 15, 2008, and she said that she would provide each member with a list of travel and per diem reimbursements to reconcile with their records and with instructions for online filing prior to the deadline.

V. EXECUTIVE SESSION

Mr. Powers made a motion that the Commission meet in executive session to discuss the 2008 Transition Funding Schedule pursuant to S.C. Code Ann. §§9-16-80 and 9-16-320, to receive legal advice, and to discuss a personnel matter. Mr. Ewing seconded the motion, which passed unanimously. Chairman Williams announced that the Commission would meet in executive session for those purposes.

The Commission reconvened in open session and Chairman Williams reported that the Commission did not take any reportable action while in executive session. Chairman Williams noted that any action that did occur while in executive session pursuant to S.C. Code Ann. §§9-16-80 and 9-16-320 would be publicized when doing so would not jeopardize the Commission's ability to achieve its investment objectives or implement a portion of the annual investment plan.

Mr. Powers made a motion to invest additional amounts not to exceed \$350 million in the Putnam Total Return Trust, \$350 million in the Bridgewater All Weather Fund, \$100 million in Mariner Partners, L.P., \$100 million in the D.E. Shaw Composite Fund, LLC, \$100 million in the

FrontPoint Multi-Strategy Fund Series A, L.P., and \$100 million in the Bridgewater Pure Alpha Fund for the purpose of implementing a portion of the Transition Plan and to authorize the Chairman to negotiate and execute any necessary documents to implement the investments upon approval for legal sufficiency by General Counsel. Upon second by Mr. Ewing, the motion passed unanimously.

VI. ADJOURNMENT

There being no further business, Chairman Williams thanked everyone for attending, and the meeting adjourned at 2:00 p.m.

[Staff Note: In compliance with S.C. Code Ann. §30-4-80, public notice of and the agenda for this meeting were delivered to the press and to parties who requested notice and were posted at the entrance, in the lobbies, and near the 2nd Floor Conference Room at 202 Arbor Lake Drive, Columbia, SC, on March 18, 2008.]