

**Oregon Investment Council  
MINUTES  
November 19, 2003**

The Oregon Investment Council was called to order at 9:05 a.m. by Gerard Drummond.

**OIC Members Present:** Jerry Bidwell, Gerard Drummond, Randall Edwards, Mark Gardiner, Diana Goldschmidt and Laurie Warner.

**Staff Present:** Jay Fewel, Steve Gruber, Norma Harvey, Todd Jones, Perrin Lim, Michael Mueller, Kevin Nordhill, Cesar Porte and Ron Schmitz.

**Consultants Present:** John Ilkiw, Russell Investment Group  
Tara Blackburn, Pacific Corporate Group  
Allan Emkin, Pension Consulting Alliance  
Randall Doser, Compass Advisors

**Legal Counsel:** Dee Carlson, Oregon Department of Justice

**I. Review and Approval of Minutes - 9/24/2003 & 10/29/2003**

**MOTION:** Mark Gardiner moved approval of the 9/24/2003 and 10/29/2003 minutes. The motion was seconded by Randall Edwards and passed unanimously by the Council.

Mr. Drummond introduced Laurie Warner, serving as PERS Interim Director since the resignation of James Voytko.

Mr. Drummond announced that Diana Goldschmidt would arrive later in the meeting and that several action items would be moved to the end of the meeting.

**II. Consultant Contract Extensions**

Mike Mueller updated the OIC regarding consulting contracts under review and noted that over the past couple of years, for various reasons, the OIC has modified otherwise expiring consulting contracts, through short-term extensions. OIC policy did not contemplate several short-term extensions, but rather, up to two extensions of two years each. When coupled with the initial contract term of three years, it appears that the main goal of OIC policy was to ensure the RFI's would be solicited at least every seven years (Policy 4.01.13).

Since the roles of PCA-Nori and PCG will most likely change when PrivateEdge is fully implemented in the first half of 2003, staff recommended delaying the RFI process until staff is comfortable with the role being served by PrivateEdge.

**MOTION:** Jerry Bidwell moved to accept staff recommendation to extend the PCA-Nori and PCG OIC Consulting contracts to December 31, 2004. The motion was seconded by Randall Edwards and passed unanimously by the Council.

### **III. 3Q 2003 Performance Report**

Allan Emkin and Mike Mueller presented the 3rd Quarter OPERF performance review for discussion. The third quarter market environment was outlined and it was noted that OPERF ended the quarter with all asset classes at or near policy targets. Jay Fewel commented on the improvement in public markets and private equity realizations in October. Mr. Mueller and Mr. Emkin answered questions from the Council.

### **IV. Asset Allocations & NAV Updates**

Ron Schmitz reported that asset allocation was close to targets and within policy ranges.

### **V. Calendar - Future Agenda Items**

Ron Schmitz discussed the 2004 agenda items and the proposed 2004 meeting schedule.

### **VI. CSFB Customized Fund Investment Group**

Ron Schmitz reported that Jay Fewel has been in contact with several organizations that manage in-state investment programs throughout the U.S with similar mandates as House Bill 3613. Mr. Schmitz noted that the CSFB approach had many interesting qualities and since staff will be in the process of working with the Department of Justice regarding definitions and procedures regarding compliance with HB3613, a presentation at this time would provide timely information.

Mr. Schmitz updated the Council on the progress of DOJ regarding definitions and procedures and noted that a preliminary draft document was in the process of being crafted.

Randall Edwards spoke on behalf of the Oregon Growth Account Board and summarized some parallel thoughts and concerns between the two boards. He suggested a joint meeting between the OIC and OGA regarding the approach to the market place with respect to the implementation of HB3613.

Jay Fewel outlined some of the difficulties staff would encounter regarding implementation of HB 3613, if it attempted to manage the \$100 million in-state investment program internally. He noted that it would be most appropriate to

outsource the implementation of this program. Mr. Fewel described the meeting processes over the past two months, with prospective groups experienced in managing in-state investment programs for other states. He expressed the opinion that CSFB was the most impressive group.

Mr. Fewel introduced Michael Arpey and Kelly Williams of the CSFB Customized Fund Investment Group. CSFB's Customized Fund Investment Group (CFIG) is uniquely qualified to develop an in-state investment program for OPERF. CFIG's in-state approach is centered around the primary objective of generating returns for investors, which leads the way to improved economic activity. CFIG has extensive experience managing in-state investment private equity programs. CFIG will work to create deal flow and reasons for investors, entrepreneurs and established businesses to work in-state. Mr. Arpey and Ms. Kelly outlined some of Oregon's best opportunities as high technology, healthcare, advanced textiles and micro-technology. Technology transfer within the university system was also discussed.

These are the specific steps that CFIG recommends for a successful in-state program:

- Finalize investment guidelines and policies.
- Establish an in-state presence.
- Build relationships with key in-state parties.
- Initial due diligence and deal sourcing initiatives.
- Build a network to link entrepreneurs, corporate partners and private equity firms.
- Educate local and regional private equity firms by organizing ongoing entrepreneurial tech-ins, private equity and venture capital seminars and industry conferences.
- Facilitation of capital investment.
- Comprehensive due diligence.
- Ongoing transparent reporting.

Mr. Arpey and Ms. Williams answered questions from the Council. Discussion followed regarding the current lack of a CSFB in-state presence and Mr. Drummond requested sample guidelines and fiduciary standards from some of the other in-state investment programs managed by CSFB.

Discussion followed regarding Oregon's capacity to absorb \$100 million in venture capital funds and the not-fully-exploited technology transfer arena.

Diana Goldschmidt arrived at 10:33am

## **VII. State Accident Insurance Fund (SAIF) - Annual Review**

Jerry Dykes and Brian Steffel of the SAIF Corporation presented the SAIF annual report for review. Mr. Steffel addressed the Council and noted that the mission of SAIF is to be the leading competitive force in the workers' compensation marketplace, providing economic advantage to Oregon through innovations in risk management services, which contain costs while paying fair and consistent benefits. He outlined SAIF's investment strategy and policy decisions, discussed the frequency of loss, service representation and prices. The claims process and duration was outlined and the changing nature of the workplace was addressed. Medical inflation and its affect on worker's compensation was discussed as well as forecasting and estimating future costs.

Jerry Dykes discussed risk based capital (RCB) requirements as well as asset allocation. Questions from the Council were answered by Mr. Steffel and Mr. Dykes.

There were no SAIF recommendations at this time.

### **VIII. Small/Midcap Domestic Equity Manager - Mazama Capital**

Jay Fewel addressed the Council and reminded them of the August 2003 termination of the Nicholas Applegate Midcap Growth product and subsequent staff authorization to search for a replacement manager in the Small/Midcap (SMID) growth space. He noted that the collective benchmark for domestic equity is Russell 3000, which does have some Midcap representation, and that it seemed best to search in the SMID growth space. He further noted that staff feels that Mazama Capital Management is a good complement to the other managers in small and large cap growth. He outlined the search process and criteria used for ultimately choosing Mazama.

Mr. Fewel introduced Ron Sauer and Jill Collins of Mazama Capital Management. Ms. Collins noted that Mazama has been working for OPERF for over five years through the Northern Trust Emerging Manager Program. During that time, Mazama outperformed the Russell 2000 Growth benchmark by 870 bps annually, for the OPERF program. Ms. Collins gave an overview of the firm and management team, addressing the division of functional and sector responsibilities within the investment team. Mazama's investment universe was outlined and the market capitalization analysis as of 10/31/2003 was presented for discussion. Mr. Sauer further addressed the investment strategy including the bottom-up, fundamental stock selection process and the focus on market cap represented by Russell 2500 Growth Index. The investment philosophy and process was discussed and Mr. Sauer spoke about Mazama's proprietary price performance model and their buy/sell discipline.

Ms. Collins presented performance statistics outlining Mazama's consistent outperformance track record. Mutual fund trading policies were addressed as well as Mazama's code of ethics and personal trading policy.

Ms. Collins and Mr. Sauer answered questions from the Council

**MOTION:** Mark Gardiner moved that the OIC fund Mazama Capital Management, SMID Cap Growth, with \$200 million (1.5% target +/- 1.5%), subject to successful contract negotiations, working in concert with the Department of Justice. The motion was seconded by Diana Goldschmidt and passed by the Council.

Jerry Bidwell abstained from voting.

#### **IX. Putnam Investments & Alliance Capital – Manager Updates**

Jay Fewel addressed the Council regarding the ongoing scandal with respect to mutual funds, market timing and after hours trading. He noted that two of OPERF's managers, Putnam and Alliance, have been implicated so far. He outlined the ongoing staff and consultant research and offered the opinion that, from an investment perspective, staff feels it is appropriate to remain with the two organizations. However, there are issues relating to the nature of the fall-out and the ethical behavior of individuals in some of these organizations and possible fiduciary concerns for the OIC. He further noted that staff plans on conducting an onsite visit to Putnam the first week of December. Mr. Fewel pointed out that OPERF's investment process has not been compromised with regards to these market timing practices and that the losses that have occurred have been attributed to mutual funds and have not adversely impacted the OPERF portfolios run by these organizations. He directed the Council to the letters included in the agenda book from both Putnam and Alliance outlining the issues and the steps taken, to date, to address the issues.

John Ilkiw commented on different perspectives regarding the issue and noted that Lew Sanders, CEO of Alliance, has set up reserves for any company that has been financially harmed by Alliance. He noted that the Russell rankings on the Putnam products are currently suspended. He further outlined the vast organizational uncertainty.

The Council discussed transition costs and procedures in the case of termination of Putnam. Randall Edwards expressed a collective feeling of the uncertainty with Putnam due to the fact that the very person presenting to the Council, one year prior, was directly involved in the scandal. He expressed the desire for the Council to send a message to Putnam and the investment community that such behavior would not be tolerated.

Discussion followed regarding risk exposure due to the organizational changes at Putnam.

Diana Goldschmidt requested that legal counsel, Dee Carlson, look into the possibility of recovering transition costs from a manager, when the Council feels an ethical responsibility to terminate.

Mark Gardiner asked about transitioning the funds, in the case of the termination of Putnam, between Arrowstreet and Lazard. Mr. Fewel commented that it may put them over the top of their ranges. Spreading the funds out among market-oriented managers was also discussed. Mr. Fewel mentioned the possibility of allowing Arrowstreet and Lazard to choose from Putnam's existing holdings. Mr. Fewel further discussed transitioning assets through State Street Bank. Mr. Gardiner directed staff to explore the ideas discussed.

**MOTION:** Randall Edwards moved termination of Putnam Advisors. The motion was seconded by Mark Gardiner and passed unanimously by the Council.

Jay Fewel announced that the allegations regarding Alliance are more indirect regarding our portfolio.

Discussion followed regarding policies regulating mutual fund companies in the future and disclosure.

Mr. Fewel informed the Council that Alliance manages a Large Cap Growth product, a Large Cap Value product, an International product and also a Fixed Income portfolio constituting approximately 10% of OPERF, in total. The Alliance high exposure and concentration was discussed and it was the consensus of the Council to revisit the exposure issue at a future meeting.

Ms. Goldschmit recommended hearing the initial response from legal counsel at the next meeting and revisiting the Alliance issue at that time. Mr. Fewel noted that he would invite Lew Sanders, CEO of Alliance Capital Management, to address the Council at the next meeting.

It was the consensus of the council to advise staff to put all Alliance products on the watchlist and to revisit the question of high concentration of the portfolio to any one firm, within the next few months.

**X. Alternative Equity Sub-Committee – TPG Partners Fund IV, L.P.**

Jay Fewel advised the OIC that during the November 10, 2003 Alternative Equity Investment Sub-committee meeting, a commitment was made to TPG Partners Fund IV, L.P. in the amount of \$300 million, subject to satisfactory negotiation of the requisite legal documents by legal counsel working in concert with OST Staff.

Diana Goldschmidt made a statement, for the record: "Because of the business involvement of my husband, Neil Goldschmidt, with Texas Pacific Group, I wish to state, for the record, that I will no longer participate in any discussions or actions, direct or indirect, that involve Texas Pacific Group in the future." She

offered to discuss the issue further with any interested parties. Steve Gruber advised her of some Real Estate deals involving TPG and she stated further that she would have “no future involvement in anything relating to TPG or PGE in any respect.”

Mr. Drummond directed staff to alert Ms. Goldschmidt where there are may be conflicts of interest of which she may be unaware.

## **XI. Public Comment**

Dennak Murphy of the Service Employees International Union spoke regarding the systemic problem of conflicts of interest within the industry. He offered suggestions for annual certifications of policy compliance.

Allan Emkin noted that most every public fund is facing the same issue and offered to gather information and forward it to staff and the Council regarding this issue.

Mr. Murphy urged staff and Council to develop a clear policy regarding economically targeted investments to insure that the HB3613 program is successful for the participants of the pension fund.

Harvey Mathews of the Associated Oregon Industries expressed concerns regarding the implementation of HB3613 and the possible hiring of CSFB for the in-state program.

Ron Schmitz read a public comment by Bill Parish urging the College Savings Plan to replace the recently terminated Strong Capital, with Vanguard. Mr. Drummond noted that the Oregon Investment Council has no decision-making authority with regards to the Oregon College Savings Plan.

The meeting adjourned at 12:25pm.

Respectfully submitted,

Norma Harvey  
Investment Coordinator