Oregon Investment Council
MINUTES
April 28, 2004

The Oregon Investment Council was called to order at 9:03 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, Linda Haglund, Norma Harvey, Andy Hayes, Michael Mueller, Kevin Nordhill, Perrin Lim and Ron Schmitz.

Consultants Present: Michael Beasley, Strategic Investment Solutions (SIS)
John Meier, Strategic Investment Solutions
Paul Harte, Strategic Investment Solutions
Tara Blackburn, Pacific Corporate Group (PCG)
Eric Becker, Pacific Corporate Group
Allan Emkin, Pension Consulting Alliance (PCA)
Nori Lietz, Pension Consulting Alliance

Legal Counsel: Dee Carlson, Oregon Department of Justice

I. Review and Approval of Minutes – March 31, 2004

MOTION: Randall Edwards moved approval of the 3/31/2004 minutes. The motion was seconded by Mark Gardiner and passed unanimously by the Council.

II. Relational Investors – Presentation and Recommendation

Jay Fewel addressed the council and discussed a possible commitment to a corporate governance investment vehicle based on return merit. He noted the "hybrid" nature of Relational Investors as having characteristics of both public and private equity. He further noted that there was no formal recommendation at this time, and Council direction is requested after the presentation. Mr. Fewel introduced Ralph Whitworth of Relational Investors LLC.

Mr. Whitworth outlined his involvement in shareholder reforms and public policy discussions since 1992. Relational makes significant equity investments in publicly traded companies in the United States and Canada with equity market capitalizations over $1 billion or the equivalent thereof in Canadian dollars. Their investment thesis is to make investments in publicly traded companies they believe are undervalued but fundamentally sound, and then work with management, boards of directors, and shareholders on issues of governance, strategy, capital structure, management and performance.

Relational seeks to be the catalyst for each of its portfolio companies, effectuating changes that will result in increased market valuation. Through a shareholder activist program focused on performance related issues at the Board of Directors level, Relational seeks to achieve an annual rate of return equal to the total return of the S&P 500 Index plus eight percentage points. They use a value based selection process designed to identify poorly performing, under managed companies that lack fatal flaws while possessing most of the essential ingredients for improved performance.

Mr. Whitworth outlined the firm's performance, proactive involvement, shareholder activist positions and answered questions from the Council.

Jay Fewel, Tara Blackburn and Mike Beasley answered Council questions and commented on the deal structure as well as the "special situation" nature of the product.

Allan Emkin commented on Relational Investor's relationship with CaLPERS and their fee structure.

It was the consensus of the Council to negotiate a fee structure matching that of CalPERS, and return with the results of that discussion, at a subsequent meeting, if successful.

Diana Goldschmidt requested that SIS examine OPERF's overall fee expense as a future agenda item. Mr. Beasley noted that SIS was in the process compiling such a report and it would be presented at a future meeting.

III. Real Estate – Retail Allocation

Steve Gruber and Nori Lietz addressed the Council and noted that due to the increase in the overall size of the OPERF Portfolio from $32 billion at year-end 2002 to $42 billion at year-end 2003, additional allocation capacity within the real estate portfolio had been created. OPERF and Regency Centers formed Columbia Regency Retail Properties (CRP) in 2000 with commitments of $200 million from OPERF and $50 million from Regency Centers. Columbia Regency Retail Properties II is being proposed to capitalize on the success and momentum of CRP I. The proposed venture will execute the same investment strategy as CRP I by investing in non-mall retail properties, primarily consisting of infill, suburban grocery anchored neighborhood and community shopping centers. It was noted that Brian Smith, John Delatour and Craig Ramey of Regency Centers were present and willing to address the OIC and answer questions.

MOTION: Diana Goldschmidt moved to adopt staff recommendations 1) to allocate $50 million to Columbia Regency Retail Properties II (CRP2), and 2) return of capital and profits (if any) from Columbia Regency Retail Property dispositions be transitioned to CRP2 as additional capital allocations, as

realized. This recommendation is subject to satisfactory negotiation of the requisite company documents by staff and the Department of Justice. The motion was seconded by Mark Gardiner and passed unanimously by the Council.

IV. Short Term Fund Guideline Revisions – 4.02.03

Perrin Lim discussed proposed revisions to Investment Policy 4.02.03, the Oregon Short Term Fund Portfolio Rules, in order to provide more clarity and explicit guidelines versus the current rules in addition to allowing additional flexibility with the investment of the fund. The last revision to the rules occurred on September 27, 2000. Under ORS 294.895, the Oregon Short Term Fund Board shall review the rules promulgated by the investment officer. At the OSTF Board Meeting held on March 9, 2004, staff had proposed the revisions to the Portfolio Rules. The Board supported all the proposed changes with minor revisions.

MOTION: Randall Edwards moved approval of the revised Oregon Short Term Fund Portfolio Rules, Investment Policy 4.02.03, as approved by the Oregon Short Term Fund Board on March 9, 2004. The motion was seconded by Jerry Bidwell and passed unanimously by the Council.

V. Fund Governance – Annual Review

Ron Schmitz addressed the Council and noted that in accordance with Section 1.5 of the OIC's Statement of Fund Governance for OPERF and Section 1.5 of the OIC's Statement of Investment Objectives and Policy Framework for OPERF, staff is recommending updates to these documents. He further noted that SIS had reviewed documents defining technical changes only and had no substantive recommendations for changes.

Mike Beasley commented on the reasonableness test of the current asset allocation structure. He noted that OPERF's mix of assets, as they are currently structured, is reasonable and efficient in the sense that a higher expected return cannot be achieved with the current level of risk.

Laurie Warner commented on the long-term rate of return and future PERS Board topics of interest. Allan Emkin discussed liability structures versus returns and actuarial assumptions. Randall Edwards suggested that this discussion could be a possible joint topic with OIC/PERS Board.

Ron Schmitz outlined specific, proposed policy changes and discussion followed regarding changes in the policy documents to the Alternative Equity and Real Estate Committees. Mr. Schmitz led a discussion regarding the recommendation to raise the threshold for flexibility in the Real Estate sub-committee, as well as proposed changes in the committee policy defining the language and committee membership. It was the consensus of the Council

that one of the OIC members sit on the committees. Mr. Drummond agreed to volunteer to serve on the Alternative Equity and Real Estate Committees for a period of one year in rotation with other OIC members.

Diana Goldschmidt expressed discomfort with increasing the limits on the Real Estate Committee.

Steve Gruber and Nori Lietz addressed questions from the Council regarding proposed changes.

MOTION: Mark Gardiner moved to adoption of staff recommendations as follows subject to revisiting after the asset allocation study:

- Statement of Investment Objectives and Policy Framework for OPERF
  - a. Section 2.3: Clarify that no new funds are flowing into the Variable Account, due to action taken by the State Legislature during the enactment of PERS reform legislation.
  - b. Section 3.5 & 3.6: Revise expected rates of return based on SIS return assumptions and change the horizon to coincide with SIS methodology.
  - c. Section 6.1: Reflects OIC approved change in international equity benchmark.
  - d. Section 6.2: Reflects OIC approved change to reduce international equity passive allocation to 20%, to implement a 10% enhanced international equity strategy.
  - e. Section 10.4: Verbiage changed to eliminate sample performance Exhibit that would need to be regularly revised with current data.
  - f. Glossary: Various deletions and additions based on changes reflected above.

The motion was seconded by Diana Goldschmidt and passed unanimously by the Council.

Further discussion occurred regarding the proposed increased limits for Real Estate Sub-Committee.

MOTION: Diana Goldschmidt moved to raise the threshold for first time Real Estate investments to $100 million and to leave the allowance for follow-on investments at $100 million. The motion was seconded by Mark Gardiner.

After discussion, the motion was tabled until the next meeting. Ms. Lietz agreed to re-work and simplify the policy language and return with a recommendation for further discussion.

VI. Asset Allocation Study Overview

Ron Schmitz addressed the topic to review the consultant's asset allocation return assumptions and the potential impact on the expected total fund return.

The Council regularly assesses the continued suitability of the approved investment objectives and policies and makes changes as necessary.

Mike Beasley and John Meier discussed asset/liability modeling and OPERF's pension funding objectives. The asset allocation goal is to achieve the systematic construction of a total fund portfolio, consistent with the investment objective of maximizing the expected return for the chosen level of risk. Long-term targets were discussed. Mr. Beasley outlined their asset allocation approach, strategy, process and asset mix optimization. Discussion followed regarding the capital markets expectations process, assumptions and methodology.

Mr. Beasley noted that the current policy mix is on the efficient frontier. Once the Oregon Supreme Court rules on last year's reforms, an integrated asset and liability study will assist the Council in determining where on the efficient frontier, in terms of risk and return, is the best place to achieve its investment/liability objectives.

Mr. Beasley answered Council questions and noted that SIS and the Treasury Staff are open to new ideas and suggestions from the OIC.

VII. Manager Concentration

Mike Beasley and John Meier reported on the concentration of managers in the OPERF portfolio. Discussion followed regarding the market and business risk that the OIC has with its managers. A SIS analysis of manager concentration was presented including the pros and cons of large assignments. Lists of OPERF's largest concentrations total dollar allocation as of 12/31/03 were presented for review and discussion.

OPERF Summary:

- Need enough diversified manager strategies to meet alpha target.
  - Number of managers looks OK
  - Asset class manager structure studies may change perspective
- Firms where Oregon is large owner of total assets require additional business risk monitoring.
  - Thompson Rubinstein, Winslow, Froley Revy, Becker, ArrowStreet, Acadian.
- Firms where Oregon is large owner of product assets require additional product development monitoring.
  - Wanger, Thompson Rubinstein, BGI, Fidelity, Froley Revy, Becker.
- Oregon Public Markets total managers similar to industry norms.

Mr. Beasley outlined the manger structure approach and implementation of asset allocation policy target, risk factors and risk measurement. He noted that SIS would continue to monitor managers and products on an on-going basis.

VIII. Asset Allocations and NAV Updates

Ron Schmitz reported Ron Schmitz reported that asset allocation and NAV updates are all within policy parameters.

IX. Calendar – Future Agenda Items

The OIC forward agenda topics were discussed.

X. Other Items

The minutes of the Real Estate Investments Sub-Committee meeting of April 15, 2004 were submitted where the following was approved: (i) an additional commitment of $11 million to Columbia Regency Retail Partners (CRP), (ii) modification of the property specific CRP leverage limitations solely for the Chicago transaction, and (iii) modification of the leverage guidelines as CRP liquidates, as described in Staff's memo dated 3/16/2004. Subject to satisfactory negotiation of the requisite amendments to the CRP agreements by the Department of Justice and Treasury staff.

Diana Goldschmidt requested staff's opinion on the subject of the SEC's current rule-making on the "trade-through" provisions, including the contemplation of an opt-out provision. She requested information on whether or not the Council should file a separate letter in support of changes, which will increase the brokerage fees charged by the NYSE to investors.

XI. Public Comment

There were no comments from the public.

The meeting adjourned at 12:52pm

Respectfully submitted,

Norma Harvey
Investment Coordinator