OREGON SHORT-TERM FUND
BOARD MEETING
Minutes
September 23, 2010
Via Conference Call

Board Attendees: Douglas E. Goe, Orrick, Herrington & Sutcliffe LLP
Darren Bond, Oregon State Treasury
Laurie Steele, Marion County Treasurer
Deanne Woodring, Davidson Fixed Income Management
Stewart Taylor, City of Albany
Bob Woodruff, Nike Inc.
Wayne Lowry, Sherwood School District

Attendees (Staff): Perrin Lim, Oregon State Treasury
Tom Lofton, Oregon State Treasury
Ellen Hanby, Oregon State Treasury
Judy Whaley-Fultz, Oregon State Treasury
Heidi Rawe, Oregon State Treasury

i. Opening Remarks
Doug Goe welcomed all to the Oregon-Short Term Fund (OSTF) Board Meeting at 10:00 am and thanked them for being available at short notice.

ii. Revision of Portfolio Rules – Perrin Lim and Tom Lofton
Due to changes that have transpired, mainly since 2008, additional documentation is required by the nationally recognized statistical rating organizations (NRSROs) from the issuers and the underwriters before a rating is assigned to a new issue corporate or agency security; compared to years prior to 2010, this has delayed the process to get an assigned rating at the cusip level. During periods of heavy new issuance, such as August and September 2010, documentation has been delayed, as has formal assigned cusip level ratings, and a given new issue security will have "expected ratings" only, thus creating an OSTF compliance alert.

The recent use of expected ratings, for bonds that have been purchased in the new issue market, are not currently included in the current OSTF investment policy guidelines.

Perrin Lim presented the proposed revisions to the Portfolio Rules to permit the use of expected ratings. Please see attached Description of Proposed Revisions to OSTF Portfolio Rules. The suggested changes were made in an effort to support compliance efforts for the OSTF. Mr. Lim confirmed that expected ratings are not actual ratings but are intended to anticipate a NRSRO forthcoming rating assignment based on reliable information from third party sources such as the issuer or underwriter associated with the given security. Even though expected ratings may often turn out to be the actual rating, the compliance model recognizes expected ratings as no rating and flags such securities as out-of-compliance.

The revisions to the guidelines would allow the use of expected ratings for a period of up to 30 business days after the settlement. Mr. Lim confirmed that actual assigned ratings on the bond would be needed within 30 business days. After 30 business days and still absent an assigned rating, the expected ratings would turn into non-rated in OST's system, impacting the overall credit quality. If ratings are not assigned within the timeframe, they would be put back to the issuer at cost or sold in the secondary markets.

The Board discussed the revisions proposed by Mr. Lim; it was agreed that language in Section VI, Diversification and Limitations of Portfolio would be amended as discussed.

MOTION: Bob Woodruff moved approval of the revisions, with the suggested language as discussed. The motion was seconded by Darren Bond and passed unanimously by the Board.

Mr. Lim confirmed that the changes would formally be put before the Oregon Investment Council (OIC) at their upcoming meeting on September 29, 2010.

i. **Closing Remarks**

Mr. Goe thanked all for their participation and attendance at the meeting.

Meeting adjourned at 9:50 am.

Respectfully submitted by,

Norma Harvey
Investment Analyst

Heidi C. Rawe
Executive Assistant to the Deputy Treasurer

OSTF Board Conference Call
September 23, 2010
Description of Proposed Revisions to OSTF Portfolio Rules (4.02.03)

Purpose:

To implement the same revision to two sections of the Oregon Short-Term Fund Portfolio Rules 4.02.03, Section VI (A)(3) and Section VI (A)(5), Diversification and Limitations of Portfolio, U.S. Government Agency and Corporate Indebtedness. The last revision to the rules occurred at the January 26, 2010 OSTF Board Meeting and was approved by the Oregon Investment Council on April 28, 2010.

Background:

Under ORS Chapter 294.895, the Oregon Short-Term Fund Board shall review the rules promulgated by the investment officer.

Revision/Addition – Allow "outstanding, issuer, senior unsecured or expected ratings" to be used as a proxy for actual ratings for not more than 30 business days from the anticipated settlement date.

Oregon State Treasury has been in the process of fine-tuning the compliance reporting of both internally and externally managed funds across state agencies and pooled assets. This will ensure to governing bodies, state agencies and pool participants that fund assets are being managed with the agreed-upon portfolio rules and investment policies.

The current OSTF Portfolio Rules require the stated minimum credit ratings for securities, at the time of purchase. They do not address the use of "outstanding, issuer, senior unsecured or expected ratings" for newly issued securities. The use of "expected ratings" has been licensed by the nationally recognized statistical rating organizations (NRSROs) to third parties such as Bloomberg to anticipate forthcoming rating assignments and designated by an "e" after the rating code. When new issue securities with an "e" designation are currently purchased for the OSTF, an "out-of-compliance" alert is triggered.

The lag time before an actual rating assignment for a new issue security, as measured from the settlement date, is dependent on various factors, including:

- Submission of documentation by the issuer to the NRSRO
- Submission of documentation by the underwriter to the NRSRO
- Review of documentation by the NRSRO
- Assignment of ratings by NRSRO
- Update of cusip level ratings by Bloomberg staff (replacing expected with actual)

The various parties mentioned above are submitting, processing and reviewing the documentation as diligently as possible but there have been, and may continue to be, instances of delays with the assignment of actual cusip level ratings and the updating of data fields in Bloomberg, which is the source for compliance testing, at least compared to past experience. Through conversations with the involved parties, it is staff understanding that adaptations to operating in a stricter regulatory environment with higher legal scrutiny have simply slowed the process. In the past, data may have been updated based upon oral agreement; now paperwork must be received, reviewed and completed.

Over the past eighteen months, and more so in August and September, the credit markets have witnessed an extraordinary volume of new issue corporate securities ranging in credit quality from AAA to CCC and ranging in maturities from 1-100 years. Year-to-date through September 21, new investment grade fixed rate issuance has totaled $650+ billion for an annualized pace of $975+ billion, eclipsing 2009's record of $918 billion. The 5-year average at the end of 2009 was $571 billion per year.

The new issue market provides OSTF staff the ability to purchase meaningful exposures to favored issuers, should these companies decide to issue new debt securities, often at a concession to same or comparable credits and maturities. Absent the new issue market, the ability to acquire favored issuers in meaningful positions would be extremely challenging in the current environment.

Recommendations:

Staff recommends approval of this revision for U.S. Government Agency and corporate securities.

VI. Diversification and Limitations of Portfolio

A. Eligible Securities:

3. U.S. Government Agency Securities

b. 33% maximum of portfolio per agency issuer.

- For newly issued Agency securities, and absent assigned ratings, "~~outstanding, issuer, senior unsecured or~~ expected ratings" may be used as a proxy for assigned ratings for not more than 30 business days after the anticipated settlement date.

5. Corporate Indebtedness

d. Corporate notes must have minimum long-term ratings of A-, A3, or A-, or better, by Standard & Poor's, Moody's Investors Services, or Fitch Ratings, respectively, at the time of purchase.

- For newly issued corporate securities, and absent assigned ratings, "~~issuer, senior unsecured, outstanding or~~ expected ratings" may be used as a proxy for actual ratings for not more than 30 business days after the anticipated settlement date.