

**Minutes of the Regular Meeting – APPROVED 3/18/10 with correction, italicized, page 2
1 pm January 21, 2009**

**Held at Rutgers Student Center, Multi-Purpose Room A
126 College Avenue, New Brunswick, New Jersey 08901**

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Council Members in Attendance:

Orin Kramer, Chair
Jonathan Berg, Vice Chair
Susan Crotty
Mark Kandrak
Karl Kleeberg
Douglas A. Love
James P. Marketti
Timothy McGuckin

Council Members Absent:

James Clemente
James C. Kellogg

The Regular Meeting was called to order by Chair Kramer at 1:05 p.m.

Meeting Notice

Council Secretary Susan Burrows reported that notice of the Regular Meeting scheduled for January 21, 2010 was sent by mail deposited in the post office, by facsimile and email on January 4, 2009. A copy of the notice is on file as posted in the Division and sent to the Council, the **Times of Trenton**, **The Star-Ledger**, the **Bergen Record**, the **Courier Post** and the Secretary of State

Meeting Minutes

Minutes of the regular meeting of the Council held on November 19, 2009, and of the annual meeting held on November 19, 2009 and of the Executive Session held on September 17, 2009 were approved unanimously on a motion by Council Member Crotty, seconded by Council Member Kandrak.

Council Member Kandrak asked that these minutes record his “extreme exception” to remarks made by a public speaker at November’s Annual Meeting equating economic loss with the loss of lives on September 11, 2001.

Audit Committee on FY2009 Audit

Chair Kramer said that Audit Committee Chair Kellogg was out of the country. He asked Council Member Love, who had chaired the Audit Committee meeting held immediately prior to the Council meeting, for the Audit Committee report. Council Member Love reported that the fiscal year 2009 audit of the Pension Fund identified no problems and that the Division had received no management letter. A final version of the audit was expected for release around month’s end.

Opportunities within mortgage-backed securities space

Memorandum “Och-Ziff Structured Credit Separate Account” dated January 14, 2010

The Division’s Hedge Fund Consultant, Daniel Stern of Cliffwater LLC, said the proposed \$300 million commitment to the Och-Ziff Structured Credit Fund would be used by the fund

to invest opportunistically across a variety of structured credit securities, including residential and commercial mortgage-backed securities, cash and synthetic collateralized debt obligations and certain non-mortgage asset-backed securities.

He said due diligence had shown the Och-Ziff Fund well positioned to capitalize on perceived dislocations in the market for these types of securities. The commitment would be the Division's second with the Och-Ziff Management Group. Mr. Stern noted that the management firm had placed a substantial amount of its own capital into the opportunity, and that the investment's favorable terms had been dictated by the Division to ensure that when Och-Ziff felt the opportunities had diminished for its investment, Division funds would be withdrawn at the same time.

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A discussion followed in which Deputy Director Ray A. Joseph said Och-Ziff's commitment to the fund was *in the \$15 million range*. He said the investment terms are consistent with Council regulations governing the percentage of investment the Pension Fund may hold as measured against total firm assets, not the value of individual funds. He said the total funds managed by Och-Ziff were in the \$17 billion range.

Director William G. Clark said he felt the alignment of interests in the investment was unique as Och-Ziff had more invested in this strategy than the Division, though not in the same fund. He said the firm had proven exceptional in determining where value lay in this market, and that the Division would receive the same terms as Och-Ziff, net of fees. Mr. Stern added that terms were structured in such a way that returns must exceed a certain threshold before the firm received any fees.

Council Member Marketti asked if Och-Ziff was undertaking increasing levels of risk, as one publication had reported. Mr. Stern suggested that reference likely applied to the firm's reduction of cash exposure as new investment opportunities appeared. He noted that the firm relies on less leverage than most other management firms.

A brief discussion followed in which Chair Kramer said that representatives of the new Governor were aware of the proposed commitment and had expressed no concerns. He reminded all present that the Council is a body independent of politics, charged with setting investment policy for Division implementation.

Chair Kramer introduced Candace Straight as Governor Christie's liaison to the Council. He said that throughout the transition, Ms. Straight and the transition team had focused on ensuring a quality investment process.

In response to a question from Council Member Marketti, Chair Kramer explained that the Council received presentations on alternative investments but was not required to approve them. Council Member Marketti asked to be put on the record as opposed to this commitment.

Council Changes

Chair Kramer noted that the terms of three Council Members – Erika Irish Brown, W. Montgomery "Monty" Cerf and Jose Claxton – had expired earlier in January, coincident with the end of the legislative session in which their nominations had not been presented for Senate confirmation. Chair Kramer said the three had served the Pension Fund in an excellent manner. He expressed regret that prior employment at varying times with Lehman Brothers had resulted in all three bearing the brunt of criticism for a 2008 Division

investment in Lehman, in which they played no role. The seats will remain vacant pending appointment by the new Governor.

Chair Kramer also announced the resignation of Director Clark, effective February 5. Chair Kramer said Director Clark was leaving for an excellent opportunity not yet announced. (*Secretary's note: On January 29, 2010, the Federal Reserve System's Office of Employee Benefits announced that Director Clark would join the Office as senior vice president and chief investment officer.*)

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Director Clark noted that his decade with the Division, five as its Director, had been a tremendous and challenging experience. He credited Division staff for achieving strong performance numbers, especially during the economic crisis of the past year. He thanked the Council for providing personal and professional support, including members not present whose terms had ended. He said that all interactions with the new Administration had been constructive and cordial, and the same could be expected going forward.

Council Member Crotty said Director Clark left behind a strong legacy, leading the Pension Fund to outperform 95 percent of other public funds. Council Member Love commended him for having dual dimensions as a good manager of people who also is strong on technical details. Ms. Straight relayed the Acting Treasurer's best wishes. Chair Kramer noted that Director Clark was regarded by his peers as one of the strongest chief investment officers among the country's public pension funds, and said he leaves big shoes to fill.

Chair Kramer said that Deputy Director Ray Joseph would assume the post of Acting Director upon Director Clark's departure. He said the Council had responsibility for identifying director candidates to the State Treasurer for his appointment, and he suggested a Council Committee be formed to identify and coordinate the candidate process. Council Member Crotty agreed to chair the Committee, and Council Members Love, Berg, Kandrac and Chair Kramer agreed to serve on it.

Director's Report

Memorandum "Investment Reports" dated January 15, 2010

Director Clark reported that the Pension Fund had an estimated value of \$68.1 billion on December 31, 2009, with out-performance relative to benchmarks in all portfolios. The Pension Fund returned an estimated 19.8 percent for the calendar year, versus 19.1 percent for the Council benchmark. He said the fund's outperformance was largely due to its overweight exposure to public equities relative to the Council benchmark.

He noted outflow for benefits remained a challenge to the Fund, particularly in December when the fund traditionally pays December and January benefits simultaneously to accommodate bank closures on January 1 each year. In December 2009, that payment was about \$800 million, he said.

Director Clark noted that the Division in December had looked across all asset classes for the best risk-adjusted returns: A year ago, it was in corporate bonds but currently the best value was in dividend-paying stocks, particularly utilities. He added that the Division had recently shifted about \$300 million out of corporate bonds and into infrastructure-focused investments, where dividend yields were riding at about 3-4 percent.

Investment Officer Brian Arena said the domestic equities portfolio was up for the month of December relative to the Standard & Poor's 1500 benchmark. He said the portfolio had ended the calendar year at an estimated 32 percent, beating the S&P index at 27.2 percent.

Investment Officer Gilles Michel said the international portfolio had also outperformed its benchmark of 1.3 percent with returns of 1.68 percent for December. He said the portfolio's Japanese exposure was starting to perform strongly.

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Senior Portfolio Manager Tim Patton said the Division was monitoring rising rates in fixed income, and said the duration of Division holdings had declined from 10.8 to about 10.2 years at year's end. He said the Division's holdings in corporate bonds, Treasuries and US agency bonds returned 7.0 percent, strongly outperforming the Council benchmark of 3.9 percent for the calendar year. Also contributing strongly were high-yield investments, which returned about 66.3 percent for the calendar year against a benchmark of 58.2 percent, he said. Treasury Inflation-Protected Securities (TIPS) earned 6.3 percent, versus a calendar year benchmark of 11.4 percent, he said, adding the underperformance is attributable to the portfolio's overweight position in longer-maturity securities.

Director Clark noted that the direction of long-term interest rates ranked among the Division's biggest internal debates.

Report on Compliance with Treasury Ethics Code

Director Clark reported that the Division's historic, personal trading policy had been codified in November 2009 as a part of the Department of the Treasury Supplemental Ethics Code. With a goal of ensuring that employees cannot trade ahead of the Division, the policy requires pre-approval of all personal trades by Division personnel, copies of investment statements sent to the Division Compliance Officer, blackouts on personal trades seven days before and after Division trades, and an annual certification by each employee acknowledging they are familiar with the policy.

Director Clark said there were no violations requiring significant remedial action in the previous year, and only one minor violation corrected with the cooperation of the employee. He said the Division is preparing a broader policy governing insider trading that will encompass practices now in place.

Director Clark commended a training session led by Compliance Officer Susan Sarnowski as contributing to strong Division compliance.

Investments in Northern Ireland

Memorandum "Report on Northern Ireland" dated January 8, 2010

Compliance Officer Sarnowski reported that the Division remains in compliance with state law governing pension fund investment in Northern Ireland, and that a full copy of the compliance report would be provided to the Legislature as required by state law passed in 1987. In response to a question from Council Member Crotty, Ms. Sarnowski said it would require a change in state law to halt production of the annual report.

Audit of the Division by Office of the State Auditor

Memorandum "Report by State Auditor and Division Response" dated January 15, 2010

Director Clark said the report recently released by the State Auditor was historically more an operational than a financial audit. He said the latest audit carried only one recommendation,

namely to end Division reliance on external advisors for investment in international emerging market equities. Director Clark said moving this direction would raise many staffing and operational impediments.

Chair Kramer said that the audit underestimated the costs of the change, noting the Division lacked the necessary resources to perform the work in house. He added that large, national trusts capable of paying more for such expertise than the Division could pay still choose to rely on external advisors for the simple reason that they would not want to pick stocks for investment in India or China without benefit of experts in those countries. Chair Kramer said he'd be extremely uncomfortable seeing the Division move in this direction, an opinion echoed by Council Member Crotty.

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Council Member Marketti noted that he continued to wait for a list of fees paid to external managers and advisors. Director Clark said the information would be summarized in the forthcoming annual report.

Committee Reports

There were no committee reports beyond the Audit Committee report previously noted.

Pending Matters

Compliance Officer Sarnowski reported that a public comment period on the proposed repeal of N.J.A.C. 17:16-2 regarding engagement of external managers was scheduled to end February 5, 2009.

She reported that amendments to N.J.A.C. 17:16-12, 16 and 40 regarding investments in corporate obligations, international corporate obligations and non-convertible preferred stocks of U.S. corporations as adopted by the Council on November 19, 2009, went into effect on December 21, 2009. The amendments will allow one percent of the combined assets of all the Pension and Annuity Funds to be invested in obligations of companies that do not meet the minimum market capitalization of \$100 million.

Communications

There was no report from the State Treasurer.

Public Comment Period

Mr. Anthony Miskowski protested the difficulty in hearing Council proceedings, and suggested increased use of the microphones.

Ms. Rae Roeder expressed gratitude for the service of Director Clark on behalf of the members of CWA Local 1033. She acknowledged staff and resource shortages in the Division, and in particular funds for travel, but said she disagreed with not transferring the work of external emerging market advisors to inside staff.

Adjournment of Meeting

The meeting was adjourned at 2:09 pm by unanimous vote on a motion by Mr. Kleeberg, seconded by Mr. Berg.

Respectfully submitted,



Susan M. Burrows
Secretary to the Council