NORTH DAKOTA STATE INVESTMENT BOARD
MINUTES OF THE
APRIL 23, 2010 BOARD MEETING

BOARD MEMBERS PRESENT:
Lt. Governor Jack Dalrymple, Chair
Clarence Corneil, Vice Chair
Jeff Engleson, Land Dept.
Levi Erdmann, PERS Board
Mike Gessner, TFFR Board
Adam Hamm, Insurance Commissioner
Howard Sage, PERS Board
Mike Sandal, PERS Board
Kelly Schmidt, State Treasurer
Cindy Ternes, Workforce Safety & Insurance
Bob Toso, TFFR Board

STAFF PRESENT:
Connie Flanagan, Fiscal & Investment Officer
Fay Kopp, Deputy Executive Director
Bonnie Heit, Office Manager
Les Mason, Audit Supervisor
Leslie Moszer, Compliance Officer
Susan Walcker, Accountant

OTHERS PRESENT:
Weldee Baetsch, former SIB trustee
Aaron Birst, NDACo
Greg Burns, NDEA
Becky Dorwart, SIB Audit Committee
Paul Erlendson, Callan Associates, Inc.
Representative Betty Grande
Madeline Heer, former TFFR trustee
Bill Kalanek, AFPE, NDRTA
Becky Keller, Legislative Council
Bryan Klipfel, Workforce Safety & Insurance
Lori Laschkewitsch, Office of Mgmt. & Budget
Lonny Mertz, SIB Audit Committee
Bryan Reinhardt, PERS
Aaron Webb, Attorney General's Office
Dale Wetzel, Associated Press

CALL TO ORDER:

Lt. Governor Dalrymple called the State Investment Board (SIB) meeting to order at 8:30 a.m. on Friday, April 23, 2010, at the State Capitol, Peace Garden Room, Bismarck, ND.

THE FOLLOWING MEMBERS WERE PRESENT REPRESENTING A QUORUM: MR. CORNEIL, LT. GOVERNOR DALRYMPLE, MR. ENGLESON, MR. ERDMANN, MR. GESSNER, MR. SAGE, MR. SANDAL, TREASURER SCHMIDT, MS. TERNES, AND MR. TOSO

Lt. Governor Dalrymple requested the SIB and guests take a few moments of silence in respect to a good friend and great Executive Director/Chief Investment Officer (CIO), Mr. Steve Cochrane, who passed away on April 10, 2010.

AGENDA:

MR. GESSNER MOVED AND TREASURER SCHMIDT SECONDED TO APPROVE THE APRIL 23, 2010 AGENDA.

AYES: COMMISSIONER HAMM, MS. TERNES, MR. ENGLESON, MR. GESSNER, MR. SAGE, LT. GOVERNOR DALRYMPLE, MR. ERDMANN, MR. SANDAL, MR. TOSO, MR. CORNEIL, AND TREASURER SCHMIDT
NAYS: NONE

MOTION CARRIED.

MINUTES:

The Board considered the minutes of the March 26, 2010, meeting.

TREASURER SCHMIDT MOVED AND MR. SANDAL SECONDED TO APPROVE THE MARCH 26, 2010 MINUTES.

AYES: MR. GESSNER, MR. ENGLESON, MR. SAGE, MS. TERNES, TREASURER SCHMIDT, MR. TOSO, COMMISSIONER HAMM, MR. CORNEIL, MR. ERDMANN, LT. GOVERNOR DALRYMPLE, AND MR. SANDAL
NAYS: NONE

MOTION CARRIED

GOVERNANCE:

ADMINISTRATION

Retirement and Investment Office (RIO) Organizational Overview - Ms. Fay Kopp, Deputy Executive Director, provided a historical overview of RIO. RIO was formed in 1989 combining the administrative functions of the Teachers' Fund for Retirement (TFFR) and the SIB. By statute (NDCC 54-52.5), the SIB is the governing board of RIO. The TFFR program is outlined in NDCC 15-39.1 and the SIB investment program is outlined in NDCC 21-10.

Ms. Kopp also reviewed several organizational charts which illustrated the operations of the office in 1991 to its current structure, roles, and the responsibility of staff.

Investment Program Status Report - Ms. Connie Flanagan, Fiscal and Investment Officer, updated the Board on the status of the action that was taken at their February 26, 2010 meeting. Ms. Flanagan indicated at this time there are no managers on review and no outstanding issues that need to be taken care of in terms of a manager on review.

Ms. Flanagan reviewed daily program activity job duties that she is responsible for and will continue to perform: reconcile and review performance calculation data from investment consultant; prepare investment performance measurement reports for the SIB and clients; serve as liaison between SIB, investment managers, consultants, and custodian bank; coordinate cash requirements of clients and manage cash contributions; make investment rebalancing decisions

based on client and SIB policies; monitor the activities of money managers, custodian bank, investment consultant, and other agents contracted by the SIB; coordinate cash requirements for capital calls and other funding needs; review, approve, and monitor RIO expenditures.

Ms. Flanagan also reviewed current signature/approval authority for Ms. Kopp and herself for the following: contracts/legal documents (after review by Attorney General's Office); cash transfers (client requests); rebalancing (liquidation/purchase requests); investment fee payments; administrative expense payments; and TFFR checks.

The former Executive Director/CIO had authority, either by the position, through state statute or granted by the SIB to sign/approve all of the above items. Some of the authority was delegated to other staff members to provide efficient work flow and adequate internal controls. The Deputy Executive Director/Retirement Officer has always had contract signature authority in absence of the Executive Director/CIO. This authority was granted in writing by the Chair of the SIB in 2002. The Deputy Executive Director/Retirement Officer was also on the list of authorized check signers at Bank of ND. Checks require two signatures. RIO has been using Executive Director/CIO and Treasurer. The May 1, 2010 checks will use Deputy Executive Director/Retirement Officer and State Treasurer.

Transition Considerations - Lt. Governor Dalrymple has been in discussions with Mr. Paul Erlendson, Callan Associates, Inc., to review transitional recommendations in the absence of a CIO. Mr. Erlendson reviewed with the SIB the following suggestions that he and other senior Callan managers and professionals have discussed and recommend:

1. Inform incumbent service providers - RIO immediately notified SIB clients, and business contacts about the untimely death of the agency's Executive Director/CIO. Interim contact information was provided if there were administrative issues, investment operations, and miscellaneous investment issues.

2. Appoint an Acting CIO - Appoint an interim CIO who is experienced in investments and public fund management.

3. Create an interim Executive Committee - Appoint an interim Executive Committee to oversee and act on issues that may need to be addressed on behalf of the SIB between board meetings.

4. Manage public relations response - Designate a single spokesperson and refer any and all inquiries to that individual.

5. Special audit of the SIB's financial statements - Conduct a special audit of RIO to verify the assets and controls of the program due to a change in senior management.

6. Search for a permanent CIO: Utilize a third-party headhunting firm to help establish search criteria that is relevant to the SIB's investment program needs and other requirements.

The Board discussed the recommendations from Callan and took the following action:

TREASURER SCHMIDT MOVED AND MR. CORNEIL SECONDED TO ESTABLISH A TEMPORARY EXECUTIVE COMMITTEE AND ASK THAT EACH OF THE SUBGROUPS THAT ARE REPRESENTED ON THE SIB (ELECTED/APPOINTED OFFICIALS, PUBLIC EMPLOYEES RETIREMENT SYSTEM (PERS), TEACHERS' FUND FOR RETIREMENT (TFFR), AND WORKFORCE SAFETY & INSURANCE (WSI) MOVE A PERSON FORWARD TO REPRESENT THEM AS A MEMBER OF THE TEMPORARY EXECUTIVE COMMITTEE AND THAT THE TEMPORARY EXECUTIVE COMMITTEE BE DISSOLVED AT THE TIME THE SIB DETERMINES IT IS NO LONGER NEEDED.

AYES: MR. CORNEIL, MR. GESSNER, MR. SANDAL, MR. SAGE, MS. TERNES, TREASURER SCHMIDT, COMMISSIONER HAMM, MR. ENGLESON, MR. TOSO, LT. GOVERNOR DALRYMPLE, AND MR.ERDMANN
NAYS: NONE

MOTION CARRIED.

The Search Committee will be a five member committee representing the subgroups that are represented on the SIB plus a Chair (elected/appointed officials, PERS, TFFR, and WSI). The Search Committee's membership will be based on the Executive Committee with substitutions to be allowed by the members of the Executive Committee. The Search Committee will also have authorization to add a person if they so choose. The Search Committee will narrow the field to approximately three finalists for the permanent Executive Director/CIO. The final selection will be brought back to the full board for their consideration.

MS. TERNES MOVED AND MR. ERDMANN SECONDED TO BASE THE SEARCH COMMITTEE MEMBERSHIP ON THE EXECUTIVE COMMITTEE MAKEUP WITH SUBSTITUTIONS TO BE ALLOWED BY THE MEMBERS OF THE EXECUTIVE COMMITTEE. THE SEARCH COMMITTEE WILL ALSO HAVE AUTHORIZATION TO ADD INDIVIDUALS IF THEY SO CHOOSE.

AYES: TREASURER SCHMIDT, LT. GOVERNOR DALRYMPLE, COMMISSIONER HAMM, MS. TERNES, MR. ENGLESON, MR. SAGE, MR. TOSO, MR. SANDAL, MR.ERDMANN, MR. CORNEIL, AND MR. GESSNER
NAYS: NONE

MOTION CARRIED.

The Board recessed at 9:50 a.m. and reconvened at 10:20 a.m.

The SIB discussed membership on the Executive and Search Committees and the following individuals will serve:

Executive Committee - Lt. Governor Dalrymple, Treasurer Schmidt, Mr. Erdmann, Ms. Ternes, and Mr. Gessner.

Search Committee - Designee of Lt. Governor, Mr. Sandal, Mr. Toso, Mr. Bryan Klipfel, and Treasurer Schmidt. Mr. Sage will serve as alternate for any absentees.

Interim Executive Director/CIO - The Board discussed with Ms. Kopp and Ms. Flanagan if they have adequate resources available to them to fulfill the administrative and investment functions of the agency. Ms. Kopp and Ms. Flanagan are to let the Board know if they need assistance.

Special Audit - The Board discussed initiating a special audit of RIO. It is common practice to verify the assets and controls of a program when there is a change in senior management.

Lt. Governor Dalrymple recommended the SIB Audit Committee oversee the audit on behalf of the SIB. Current SIB Audit Committee membership includes Ms. Cindy Ternes, delegated by the Executive Director of Workforce Safety & Insurance, representing elected and appointed officials; Mr. Mike Sandal, representing PERS; Mr. Mike Gessner, representing TFFR; Ms. Rebecca Dorwart and Mr. Lonny Mertz, external representatives.

Mr. Aaron Webb, SIB legal counsel, briefed the Board on procuring services. Under NDCC 54-44.4-05.10 the SIB is exempt from procurement guidelines under certain circumstances. The SIB is exempt from state procurement guidelines when procuring investment management services. The special audit and the search for a third party recruitment firm are not exempt. Based on the current circumstances, it was Mr. Webb's opinion that there could be a reasonable request made to OMB to allow a limited competitive process.

Ms. Dorwart, Chair, SIB Audit Committee, stated Eide Bailly is currently contracted with RIO to provide an annual financial audit for fiscal years ending June 30, 2009, June 30, 2010, and June 30, 2011. Prior to Eide Bailly, Brady Martz & Associates conducted the audit for fiscal years June 30, 2006, June 30, 2007, and June 30, 2008. Since Eide Bailly and Brady Martz performed the annual financial audit of RIO under the supervision of the State Auditor's Office within the last two years and issued clean opinions, both firms would have a stake in the final outcome of the evaluation. Ms. Dorwart stated if the SIB wanted someone objective to come in and evaluate the agency, then the Board may want to look beyond these two firms.

COMMISSIONER HAMM MOVED AND MR. TOSO SECONDED TO GIVE FULL AUTHORIZATION AND DISCRETION TO THE SIB AUDIT COMMITTEE TO CONDUCT A SPECIAL PURPOSE AUDIT OF RIO ON BEHALF OF THE SIB THAT COMPLIES WITH STATE PROCUREMENT REQUIREMENTS WHICH WOULD REQUIRE AT LEAST TWO PROPOSALS. TAKING INTO CONSIDERATION THE CIRCUMSTANCES AND THE SCOPE OF WORK, FINANCIAL AUDITORS INVOLVED IN THE ANNUAL AUDIT OF RIO WITHIN THE LAST TWO YEARS WOULD BE DISQUALIFIED FROM THE PROCUREMENT PROCESS.

AYES: MR. SAGE, MR. SANDAL, MR. CORNEIL, MR. GESSNER, MR. TOSO, MR. ERDMANN, MS. TERNES. COMMISSIONER HAMM, MR. ENGLESON, TREASURER SCHMIDT, AND LT. GOVERNOR DALRYMPLE
NAYS: NONE

MOTION CARRIED.

In order to discuss the directive given them, the SIB Audit Committee scheduled and noticed a meeting for April 23, 2010, at 1:00 pm, in the Peace Garden Room, at the State Capitol.

Selection of New Executive Director/CIO - Mr. Erlendson reviewed Callan's recommendations in the search for a new Executive Director/CIO.

1. Define the job description.
2. Get the Request for Proposal for executive recruitment services out as soon as possible.

3. Once the headhunting firm is under contract, work with the firm to refine the job description, compensation, and establish search criteria that is relevant to the SIB's investment program needs and other requirements.

The Board discussed the job description of the Executive Director/CIO, senior management structure of the office and the roles, and compensation.

After discussion,

MR. GESSNER MOVED AND COMMISSIONER HAMM SECONDED TO REAFFIRM MS. KOPP AS THE ACTING EXECUTIVE DIRECTOR UNTIL FURTHER NOTICE AND THAT THE EXECUTIVE COMMITTEE BEGIN THE SEARCH FOR AN INTERIM CIO.

AYES: MR. CORNEIL, MR. TOSO, LT. GOVERNOR DALRYMPLE, COMMISSIONER HAMM, MR. GESSNER, MS. TERNES
NAYS: MR. ERDMANN, TREASURER SCHMIDT, MR. ENGLESON, MR. SANDAL, MR. SAGE

MOTION CARRIED.

INVESTMENTS

Report on Estimated Fiscal Year-To-Date Investment Returns - Ms. Flanagan provided estimated fiscal year-to-date returns: TFFR 23.5%, PERS 22.4%, Pension 22.8%, WSI 14.7%, and Insurance Trust 13.8%.

Broker Commission Recapture Revisited - The Board had tabled this issue to allow staff time to provide them a historical overview of the program. Ms. Flanagan stated in the SIB's commission recapture program, the SIB has an arrangement with one or more brokers who agree to rebate a portion of the commissions paid by the investment managers who transact with that broker. The broker therefore is guaranteed a certain amount of business and the client receives a rebate on commission expenses. In FY2000, the average gross commission cost of the total SIB program was $0.035 per share. The recapture program brought that down to $0.032 per share. In FY2009, the average gross commission cost was $0.008 per share with no measureable savings from the recapture program ($5,059 recaptures in FY09 and $2,646 in FY08). Ms. Flanagan recommended the program be discontinued because the amount of revenue that is being brought in is insignificant in comparison to the amount of time it takes to monitor and track the transactions.

TREASURER SCHMIDT MOVED AND MR. ENGLESON SECONDED TO ACCEPT STAFF RECOMMENDATION AND DISCONTINUE THE COMMISSION RECAPTURE PROGRAM.

AYES: MS. TERNES, LT. GOVERNOR DALRYMPLE, COMMISSIONER HAMM, TREASURER SCHMIDT, MR. ENGLESON, MR. ERDMANN, MR. TOSO, MR. SANDAL, MR. SAGE, MR. CORNEIL, AND MR. GESSNER
NAYS: NONE

MOTION CARRIED.

Status Report on Overlay Program - Ms. Flanagan updated the Board on the Clifton overlay program. Ms. Flanagan stated the intent is to decrease the amount of funds that are being allocated to the overlay program. The goal is to get out of the program and into physicals in all of the asset classes.

MONITORING:

Budget and Financial Conditions - The Board was provided a budget/financial report for the period ending March 31, 2010.

MR. GESSNER MOVED AND MR. ENGLESON SECONDED TO APPROVE THE BUDGET/FINANCIAL REPORT.

AYES: COMMISSIONER HAMM, MR. SANDAL, MR. CORNEIL, MR. GESSNER, MR. TOSO, MR. ERDMANN, MS. TERNES, MR. ENGLESON, MR. SAGE, TREASURER SCHMIDT, AND LT. GOVERNOR DALRYMPLE
NAYS: NONE

MOTION CARRIED.

Lt. Governor Dalrymple stated the Executive Committee is going to be actively looking for an interim Executive Director/CIO and the Committee will be advising the Board on any decisions that need to be made.

Lt. Governor Dalrymple will appoint an individual to serve as Chair of the Search Committee to begin that process as well.

Lt. Governor Dalrymple also stated that he has been briefed on the financial condition of the PERS and TFFR funds and steps that need to be taken to fortify the funds. The administration is in the process of analyzing and studying the issue through OMB.

OTHER:

The next SIB meeting is scheduled for May 21, 2010, at 8:30 a.m. at the State Capitol, Peace Garden Room, Bismarck, ND.

The next SIB Audit Committee meeting is scheduled for May 21, 2010, at 2:00 p.m. at the State Capitol, Peace Garden Room, Bismarck, ND.

ADJOURNMENT:

Lt. Governor Dalrymple adjourned the meeting at 11:55 a.m.

Respectfully Submitted:

J.S. Dalrymple
Lt. Governor Dalrymple, Chair
State Investment Board

Bonnie Heit
Bonnie Heit
Reporting Secretary