South Carolina Retirement System Investment Commission
Meeting Minutes

June 16-17, 2011

Wampee Training and Conference Center
1274 Wampee Plantation Road
Pinopolis, South Carolina 29469

Commissioners Present:
Mr. Allen Gillespie, Chairman
Mr. Reynolds Williams, Vice Chairman

State Treasurer Curtis Loftis
Mr. Edward Giobbe
Mr. James Powers
Dr. Travis Pritchett

Others present for all or a portion of the meeting on Thursday, June 16, 2011: Mike Addy, Dunkin Allison, Geoff Berg, Bob Borden, Sarah Corbett, Dori Ditty, Robert Feinstein, Hershel Harper, Adam Jordan, Lorrie King, Dave Klauka, Doug Lybrand, Jared O'Connor, David Phillips, Kathy Rast, Nancy Shealy, and Brian Wheeler from the South Carolina Retirement System Investment Commission; Bill Leidinger and Shakun Tahiliani from the State Treasurer's Office; Rhett Humphreys and Tim McCusker from New England Pension Consultants; William Blume, Greg Meetze, Tammy Nichols, John Page, and Faith Wright from the South Carolina Retirement Systems; Samantha Davidson, Mark Evans, Pat Sullivan, and Katie Tipermas from Goldman Sachs Asset Management; Robert Burdick and Marc Rowan from Apollo Capital Management; Bill Michaelcheck and Skip Shaw from Mariner Investment Group; Rob Stuckey from The Carlyle Group; Ware Bush and Paul Morin from Aspen Partners, LLP; Mike Kirchner from Grosvenor Capital Management; Mark Attanasio and Joe Viola from Crescent Capital Management; Blaine Ewing, Cindy Ewing, and Pat Garrigan.

Others present for all or a portion of the meeting on Friday, June 17, 2011: Mike Addy, Dunkin Allison, Geoff Berg, Bob Borden, Harris Chewning, Sarah Corbett, Dori Ditty, Robert Feinstein, Hershel Harper, Adam Jordan, Lorrie King, Dave Klauka, Doug Lybrand, Jared O'Connor, David Phillips, Kathy Rast, Nancy Shealy, and Brian Wheeler from the South Carolina Retirement System Investment Commission; Mike McDermott and Shakun Tahiliani from the State Treasurer's Office; Clarissa Adams from the State Comptroller General's Office; Ashli Aslin, Rhett Humphreys, and Tim McCusker from New England Pension Consultants; William Blume, Greg Meetze, Tammy Nichols, John Page, and Faith Wright from the South Carolina Retirement Systems; Katie Tipermas from Goldman Sachs Asset Management; Skip Shaw from Mariner Investment Group; Joe Deitzer from Deloitte & Touche, LLP; Mike Kirchner from Grosvenor Capital Management; Mark Attanasio and Joe Viola from Crescent Capital Management; and Wayne Pruitt from the State Retirees' Association.

I. CALL TO ORDER, CONSENT AGENDA, AND CHAIRMAN'S REPORT

Chairman Allen Gillespie called the meeting of the South Carolina Retirement System Investment Commission (Commission) to order at 10:00 a.m. and welcomed the Commission and guests to the Strategic Planning Retreat at the Wampee Training and Conference Center.

Chairman Gillespie noted that several items on the agenda would need to be rearranged due to travel issues affecting some of the presenters. He turned the floor over to Bob Borden, Chief Executive Officer/Chief Investment Officer (CEO/CIO). Mr. Borden indicated that the first part of the meeting would focus on updates about the Commission's organization, budget process, and Strategic Planning Goals (Goals) and related Strategic Planning Initiatives (Initiatives). He stated that in addition to progress reports, he wanted to present suggestions for additional Goals and Initiatives.

II. ORGANIZATIONAL AND BUDGET UPDATE

Mr. Borden noted that the Commission's first Strategic Plan was presented and approved at the Commission's retreat on June 18-19, 2008. He said that the Strategic Plan was developed with the assistance of Dr. Travis Pritchett, Commission staff (Staff), and Dr. David Schweiger, the former *Buck Mickel/Flour Daniel Professor of International Business* at the University of South Carolina and Adjunct Professor of Strategic Management at EM Lyon in France.

Mr. Borden referred to materials relating to the Strategic Plan and briefly described the processes by which it had been developed, including review of the Commission's mission, vision, values, SWOT (strengths, weaknesses, opportunities, threats) analysis, goals, initiatives, action plans, budget, and monitoring. He stated that the new proposed Goals had been vetted using a SWOT analysis to determine which of the ideas best addressed the Commission's current strengths and weaknesses and to identify Goals and Initiatives that would help eliminate potential threats to the organization. Mr. Borden opined that the weakest link in the strategic planning process was the budgeting process, and he noted that approximately half of state pension plans set their own budget, unlike the Commission's budget which is subject to legislative approval.

Mr. Borden provided an overview of the components of the Strategic Plan and the role of each in achieving the Commission's Goals. He explained that Staff developed an action plan, which was over 60 pages long and contained a list of tasks to be completed by Staff to achieve the Goals. He said that the document was basically a "to do" list for daily Commission internal operations, which tied daily operations back to the Commission's Goals. He explained that the budget should be an output of the resources necessary to carry out the Commission's Strategic Plan. Mr. Borden stated that if the Goals and underlying Initiatives were approved, Staff would develop and present a budget in the Fall that was designed to execute the adopted Goals and Initiatives. He noted that as of June 16, 2011, the Commission's Fiscal Year (FY) 2012 budget had not been approved by the Legislature. He added that while the Commission waited for approval of the budget, Staff had started developing the proposed budget for FY 2013. He reiterated that this type of budgeting process was the weak link in the strategic planning process. He explained that the budget approved by the Legislature might not contain the necessary funding to complete the Commission's Goals and Initiatives, which would require Staff to eliminate those Goals or Initiatives for which there was inadequate funding to complete. Mr. Borden also indicated that external changes and pressures that were beyond the Commission's control could also derail the strategic planning process and eliminate some of the Goals and Initiatives.

Mr. Borden referred to information outlining the Commission's budget since inception, including expenditures, surpluses, and the number of full time employees (FTEs) on staff. He noted that the Commission had concluded the fiscal year with total expenditures less than its approved budget every year since its inception, although unfortunately a primary driver of these budget surpluses had been the result of difficulties in recruiting investment staff with the expertise needed by the Commission. He indicated that even if additional FTEs were approved, it would take a long time to fill the positions.

Mr. Borden referred to the Commission's FY 2012 initial budget request and noted that off-budget costs, such as custody fees, had been included in the request. He also explained that former State Treasurer Converse Chellis and other Commissioners had suggested developing a budget request that would allow the Commission to perform aspects of the proposed "NewCo" private market outsourcing strategy internally. Mr. Borden explained to the new Commissioners that a Budget Committee was formed to create the initial FY 2012 budget request, which had included a total of 47 FTEs. Mr. Borden noted that the Commission had surveyed its peers to determine the number of investment professionals needed to properly staff an organization given the Commission's diverse investment strategies, and the results of that survey suggested 50-59 investment professionals would be needed, which did not include any legal or administrative staff.

Mr. Borden reiterated that despite the development of Goals and Initiatives needed for the Strategic Plan, the Commission was not guaranteed the resources to execute its Strategic Plan. He opined that if the final budget approved by the Legislature was inadequate, elements of the Strategic Plan would need to be recast.

(Information relating to these matters has been retained in the Commission's files and is identified as Exhibit A).

III. STRATEGIC PLAN UPDATE

Mr. Borden introduced Adam Jordan, Director of Policy, Planning, and Budgeting, to begin discussions regarding updates to the Strategic Plan. Mr. Jordan explained that the Goals were in three stages currently: completed Goals, modified Goals, and new Goals. He reported that Staff, in conjunction with Dr. Pritchett, had reviewed the previous Goals and the proposed revisions. Mr. Jordan introduced Hershel Harper, Deputy Chief Investment Officer, for a progress report on *Goal I: Execute Major Investment & Portfolio Initiatives* (*Goal I*). Mr. Borden opined that *Goal I* was the most important Goal of the Commission.

Mr. Harper explained that *Goal I* was the largest and most comprehensive Goal because the purpose of the Commission was to invest the assets of the total portfolio (Portfolio) of the South Carolina Retirement Systems (Retirement System). He highlighted salient points briefly and noted that additional information would be provided to Commissioners upon their request. Mr. Harper explained that as the Commission continued to move toward a more sophisticated, diversified investment structure, more focus would be directed to the Hedge Fund Transition, private equity, opportunistic credit/private debt, and real estate investments. He noted that because the Commission was in a net-payable position, current allocations to cash were higher when compared to the Retirement System's peers. Mr. Harper explained that the higher allocation was needed for overlay margin requirements and to fund the private markets allocations. Dr. Pritchett expressed concern with the high allocation to cash, and Mr. Borden replied that the asset allocation and impact of having the current cash allocation would be discussed later in the meeting. Mr. Borden noted, however, that cash had been a drag on performance and opined that the way the unfunded accrued liability was calculated and the liability itself had exacerbated the problem. He estimated that approximately five percent of cash was structural cash with beta exposure and indicated that future commitments in other asset classes required liquidity to fund capital calls. Mr. Harper explained various strategies to mitigate "cash drag" on performance.

Mr. Harper provided a review of the changes that had been made to the Portfolio within each asset class over the past several years. Messrs. Harper and Borden and the Commission discussed the status and allocations within each of the Portfolio's asset classes. They reviewed the fixed income (core, high yield, and emerging market debt) and long-only public equity (domestic, emerging market equity, and Europe, Australasia, and Far East (EAFE)) investments. Mr. Borden noted in particular that risk exposure to public equity had been reduced by approximately 30 percent over the past five years, which was significantly lower than the Retirement System's peers. They reviewed real assets (commodities), global asset allocation (GAA) investments, and the beta overlay program. Mr. Harper noted that the beta overlay program, which was comprised of synthetic exposures to various betas, had aided with the transition of investments from the legacy 50/50 long-only stock/bond mixed portfolio, and that it was used in the portable alpha program.

Mr. Harper highlighted the progress of the Hedge Fund Transition Program. He noted that it was originally designed in 2006 to invest large amounts of capital quickly in a diversified manner through the use of multi-strategy funds and fund of funds structures. He said that because the Commission had increased staff, many of the funds had been "unwound"; over $1.3 billion from initial commitments to hedge fund of funds and over $350 million from multi-strategy hedge funds had been redeemed and redeployed to other funds or strategies. He said that moving forward, the Commission would continue to transition from hedge fund of funds to a platform of separately managed hedge fund accounts using the Commission's key investment partners, rebalancing and resizing the existing hedge fund portfolio based on risk budget analyses, and implementing data and risk platform services. Mr. Borden reiterated that about 18 months ago, the Commission decided to move from a fund of funds structure to more direct strategies to reduce fees, avoid over-diversification, and provide greater transparency. Mr. Borden noted that significant resources for a platform for internal and external data and risk services would be needed to complete the transition, and he expressed concern with moving forward with the transition because the tenure of the current custodian under contract with the State Treasurer's Office was uncertain, which would impact the timing and resources needed for implementation and impact other Commission activities.

Messrs. Harper and Borden and the Commission discussed investments in private markets, including private equity, opportunistic credit/private debt, and real estate. Mr. Harper reported that since 2008, the Commission has invested heavily in opportunistic credit/private debt strategies in order to realize equity-like returns with bond-like risk. He said that performance over the past two years was up approximately 24 percent and added that as performance gains were harvested from opportunistic credit sources, they would be used as a source of funds for private debt investments.

Mr. Harper noted that a Commissioner had not been assigned to work with the real estate asset class since former State Treasurer Converse Chellis' departure from the Commission. He noted further that investments in real estate had slowed after the 2008 economic downturn, but because the current allocation was underweight, Staff recommended resuming searches for real estate investment funds. After further discussion, James Powers made a motion, which was seconded by Reynolds Williams and passed unanimously, to appoint Ed Giobbe as the Commissioner assigned to the real estate asset class.

Mr. Borden referred to a flow chart outlining the Commission's general investment process and explained that the investment process was becoming more institutionalized and well documented. He presented an example of the new documentation tools that were being developed to strengthen the Commission's investment selection processes and explained that

Staff had created an internal Investment Committee and a Co-Investment Committee to vet potential investments. Mr. Borden outlined the sourcing, due diligence, recommendation and approval, and execution and closing processes, noting that the infrastructure and processes that had been established during the past few years were significant.

Dr. Pritchett asked whether a Commissioner had been assigned to Strategic Partnerships, and Mr. Borden replied that typically a Commissioner had been assigned during the vetting/due diligence phase; he added that the Commission could also add Commissioners and/or Staff to the Strategic Partnerships' Investment Committees at its discretion. Mr. Powers suggested that a Commissioner participate in the Staff's internal Investment Committee and Co-Investment Committee meetings, and Mr. Borden said that it might be difficult as most of the Staff's internal committees meet for several hours on a weekly basis although he suggested that Commissioners might share the tasks. Chairman Gillespie noted that occasionally the interests of the general partners or investment managers of Strategic Partnerships could diverge from the interests of the Commission, so he suggested the creation of a formalized process to review potential conflicts of interests within Strategic Partnerships. He suggested that when specific asset class conflicts arose, the Commissioner assigned to the specific asset class could be consulted. Nancy Shealy, General Counsel, noted that conflicts disclosures would be a part of the standardized Strategic Partnership investment processes, and the recently formed Strategic Partnerships had conflicts committees that included the Commission Chairman and Mr. Borden or Mr. Harper. She said that the general partners and managers of Strategic Partnerships were required to fully disclose all potential conflicts of interest to the conflicts committees. After further discussion, Mr. Powers suggested that Mr. Borden, the Commission Chairman, and the Vice Chairman explore a more definitive policy for vetting and monitoring investments within Strategic Partnerships.

Mr. Harper reviewed the framework of Strategic Partnerships and outlined the Commission's current involvement, including the dates of formation, investment focus, asset size, and Strategic Partnership Investment Committee structures. He noted that Staff was standardizing and reconstituting the Strategic Partnership legal model and added that Strategic Partnerships were investment vehicles, not an asset class.

Mr. Harper reviewed projects that Mr. Doug Lybrand, Director of Risk Management, had been working on with Goldman Sachs Asset Management to develop risk dashboards and factor-based models to assist with stress testing areas of the Portfolio. He also noted that the Commission was focusing on increased transparency for commingled and partnership investments; developing additional risk modeling, analysis, and reporting capabilities; improving operational processes and controls; and developing data aggregation and reporting tools using components of Strategic Partnerships.

Mr. Harper reported that *Goal II: Develop & Implement Specific Governance Policies* and *Goal VI: Create Efficient and Effective Facilities* had been completed but remained ongoing projects. He introduced Jared O'Connor, Investment Officer, for a presentation regarding *Goal III: Improve & Standardize Due Diligence Processes*. Mr. O'Connor explained that due diligence processes were integrated with every investment activity. He noted that the Commission's new due diligence processes were more detailed and thorough than its peers, who often rely heavily on their consultants for due diligence processes. He outlined the new processes drafted by the Staff's Due Diligence Team, and Mr. Borden noted that the due diligence example material provided to the Commission was in fact an example of best practices. Mr. O'Connor advised that in addition to New England Pension Consultant's (NEPC) due diligence, the Staff performed independent internal due diligence relating to prospective and current managers. In closing, he reiterated that the Commissioners could request to view the due diligence documents for investments.

Mr. O'Connor introduced Sarah Corbett, Director of Administration and Reporting, for a progress report on *Goal IV: Improve Reporting Processes*. Ms. Corbett indicated that Staff was reviewing, evaluating, and striving to improve current internal reports. She also explained the need for document management systems and noted that additional resources to implement new reporting systems would be required to accommodate current and future reporting needs.

Robert Feinstein, Chief Operations Officer, highlighted the major accomplishments of *Goal V: Develop Efficient & Effective Workforce*. With regard to new initiatives, Mr. Feinstein reported that the Staff was focusing on the creation of an organizational culture, noting that while the Commission had grown significantly since its inception, there were difficulties with the recruiting process, particularly in terms of recruiting highly qualified employees with the necessary investment experience. He also outlined the need for independent human resources processes and suggested that the strategic planning process, the budgeting process, and the organizational structure be linked for more efficient operations. Mr. Borden added that the "bottom-up" development of the organization was hampered by the "top-down" state budgeting process. He explained that part of *Goal VII: Perform Feasibility Study & Prepare Recommendations for Long term Organizational Structure* (*Goal VII*) had been to evaluate different organizational structures. He explained the challenges in achieving an appropriate organizational structure and said if, for instance, the Commission planned for 47 FTEs and only received approval from the Legislature for 31 FTEs, then it would have to change its plan to accomplish the same goals with fewer employees. He stated that as the Commission hired additional employees, the employees' knowledge and expertise might require reorganizing the organizational chart to best utilize talent. Mr. Borden explained that each of the Strategic Planning Goals had a cross-functional work team of Staff charged with carrying out tasks to achieve the Goals. Dr. Pritchett stated with regards to *Goal VII*, he originally envisioned a review of the internal organizational structure of the Commission and suggested that *Goal VII* be considered completed as long as the Commission addressed internal organizational development in another Goal. Mr. Borden replied that those elements of *Goal VII* were present in other Goals.

Mr. Feinstein explained the development of a new Goal, *Goal VIII: Improve Legal Processes*. He briefly outlined the following initiatives: legal needs assessment; implementation of solutions; monitoring, reporting, assessment; develop executive action list; governance policy maintenance; update the agency's Freedom of Information Act (FOIA) policy and develop formal procedures to respond to requests; develop e-mail management and retention systems; and develop a formal confidentiality policy for Staff, constituent agencies, and vendors. After further discussion, Mr. Feinstein introduced Ms. Corbett for a review of another new goal, *Goal IX: Improve Internal Controls*.

Ms. Corbett reported that Deloitte & Touche LLP (Deloitte) had been engaged to provide an investment risk assessment of the Commission and would provide a more detailed presentation about the focus of their engagement later in the meeting. Ms. Corbett highlighted the following new initiatives under *Goal IX*: complete investment Risk Assessment; create a risk-based internal audit function; implement additional internal controls for reporting and due diligence processes; fully determine the scope of the Retirement System's external audit functions as they relate to the Commission; and review termination procedures. In closing, she stated that completion of the formation of the Commission's Audit Committee would be necessary before Deloitte's suggestions could be implemented. Chairman Gillespie stated that since the former

Vice Chairman, Mr. Blaine Ewing, had been a member of the Audit Committee, a new member would need to be selected to fill his position. Mr. Williams made a motion, which was seconded by Mr. Powers and passed unanimously, to select Chairman Gillespie as the chairman of the Audit Committee,

After further discussion, Mr. Powers made a motion, which was seconded by Mr. Williams and passed unanimously, to select Dr. Pritchett as a member of the Audit Committee. Chairman Gillespie stated that the Audit Committee would be comprised of himself serving as chairman, Mr. Williams, and Dr. Pritchett.

Mr. Jordan discussed *Goal X: Strengthen Information Technology Resources*, noting that the lack of sufficient information technology resources was an inherent weakness of the Commission. Mr. Jordan thanked the Retirement System for supporting the Commission with information technology resources and stated that the Commission was at a point where information technology should be controlled internally. He reported that if the Commission's budget was approved, a job posting for Director of Information Technology would be opened on the first of July. Mr. Edward Giobbe questioned whether information technology security was a concern, and Mr. Borden responded that security was always a concern of any enterprise and noted that disaster recovery for the Commission would also be improved.

Mr. Jordan referred to *Goal XI: Enhance External Communications*. He stated that the Commission had a broad range of stakeholders and that it needed to develop and maintain relationships continually to better educate and keep stakeholders informed about Commission activities. He also stated that the Commission planned to update the website and refine external reports.

After further discussion about the Strategic Plan, Dr. Pritchett made a motion, which was seconded by Mr. Giobbe and passed unanimously, to approve the Strategic Planning Goals and Strategic Planning Initiatives as presented and discussed.

(Information relating to this matter has been retained in the Commission's files and is identified as Exhibit B).

IV. CREDIT AND FIXED INCOME MARKETS

During lunch, Mr. Borden introduced Marc Rowan, Co-Founder of Apollo Capital Management, for a presentation regarding *Investing in Uncertain Times*, which related to credit and fixed income markets. Mr. Rowan highlighted market risks relating to inflation and deflation; global events; European monetary issues; the US deficit; and Chinese demand. Mr. Rowan opined that it was currently the best time to be an institutional investor, although the media focused on the negative aspects such as overreaction to the 2008 crisis and benefits supposedly spinning out of control. He noted that institutional investors were among the last long-term investors remaining in the world. He said that he was impressed by the dialog during the Commission's strategic planning review and explained that in his experience, most trustees of funds did not have the same high level of quality communication that the Commission seemed to enjoy. Mr. Rowan highlighted the challenging traditional asset "bucket" definitions including: fixed income to credit; liquidation of European bank assets; commodities super cycle; longevity based investment opportunities; emerging markets; and real estate deleveraging. The Commission and Mr. Borden asked questions throughout the presentation and discussed the impact of various factors on investment strategies for the Retirement System's Portfolio.

(Information relating to this matter has been retained in the Commission's files and is identified as Exhibit C).

V. CTAs AND PORTFOLIO CONSTRUCTION

Chairman Gillespie introduced Messrs. William Bush, Partner, and Paul Morin, Co-Chief Investment Officer, from Aspen Partners, Ltd. (Aspen) for a presentation regarding Multi-Dimensional Diversification. Mr. Bush provided the Commission with a brief history of Aspen and noted that Aspen had a unique understanding of alpha generation and beta replication in futures. He said that managed futures operated independently of stocks, bonds, and physical commodities, and he highlighted aspects of Commodity Trading Advisors (CTAs) and multi-dimensional diversification processes including: identifying the primary dimensions of diversification; understanding the sources of return and risk; quantifying and aggregating the sources of return; the impact of manager hiring and firing decisions and portfolio rebalancing; and the applicability of multi-dimensional diversification on other strategies and asset classes. The Commission and Mr. Borden asked questions throughout the presentation and discussed the impact of various factors on investment strategies for the Retirement System's Portfolio.

(Information relating to this matter has been retained in the Commission's files and is identified as Exhibit D).

VI. REAL ESTATE MARKETS

David Klauka, Senior Alternatives Officer, introduced Rob Stuckey, Managing Director, from The Carlyle Group for a presentation on a value-based investment approach to real estate. Mr. Stuckey opined that markets would need more equity to refinance their positions, which would create opportunities in distressed assets. He also suggested that markets were slowly improving, thus creating increased demand due to household formation and job growth, which would raise real estate prices. He discussed various aspects of real estate markets and indicated that there was potential for housing shortages in the future, despite current oversupply. He also explained that there might be future investment opportunities in multifamily apartments because of a chronic shortage of dwelling units. The Commission and Mr. Borden asked questions throughout the presentation and discussed the impact of various factors on investment strategies for the Retirement System's Portfolio.

(Information relating to this matter has been retained in the Commission's files and is identified as Exhibit E).

VII. ASSET ALLOCATION AND TAA POLICY PORTFOLIO

Mr. Borden introduced Mark Evans, Managing Director for Global Portfolio Solutions and IMD Strategies, and Ms. Samantha Davidson, Vice President and Managing Director, from Goldman Sachs Asset Management (GSAM) for a presentation on the Palmetto State Policy Plus Fund (Policy Plus Fund). Mr. Evans explained that the Policy Plus Fund was structured to address a non-standard set of questions and designed to partner with Staff to assist them in implementing and managing the investments to achieve the long-term actuarial assumed rate of return of 8 percent as set by the Retirement System's trustees, at an appropriate level of risk. Mr. Evans noted that the Portfolio was subject to a series of constraints or requirements, including the policy portfolio and working within the degrees of constraint on Staff. He stated that the Policy Plus Fund was a test platform to develop the best ways to outperform the policy portfolio, and to ask "are there better or different ways to achieve higher performance?" Ms. Davidson reported that in conjunction with Staff, GSAM had created risk reports for the Policy Plus Fund to test and invoke dialog and conversation regarding asset allocations. She also noted that GSAM had created a “mini- portfolio” to invest with the same goals as the Portfolio in an effort to outperform the benchmark within the same constraints. Mr. Evans also opined that the Policy Plus Fund could be used as a tool to hold managers accountable for their actions because most managers were focused on limited benchmarks involving their portfolio only, not on how their portfolio fits into the Retirement System’s Portfolio. He also suggested that the Policy Plus Fund could test whether certain allocations could be overweighted to increase performance. The Commission and Mr. Borden asked questions throughout the presentation and discussed the impact of various factors on investment strategies for the Retirement System’s Portfolio.

(Information relating to this matter has been retained in the Commission’s files and is identified as Exhibit F).

VIII. UPDATE ON ASSET ALLOCATION FORECAST

Mr. Borden introduced Messrs. Rhett Humphreys, Partner, and Tim McCusker, Partner, from NEPC for an update on asset allocation. Mr. Humphreys provided the Commission with an overview regarding internal changes within NEPC recently. Mr. McCusker highlighted changes since NEPC’s 2011 Asset Allocation Analysis for the Portfolio and indicated that market returns were lower than expected. He also noted that most markets had been driven by macro or top-down factors; quantitative easing by the Federal Reserve; and stress on the global currency regime. Moving forward, Mr. McCusker suggested that the Commission maintain discipline with regard to asset allocation decisions; examine the Portfolio structure; continue to build illiquid strategies; and consider hedging developed market currency to reduce uncompensated risk. He explained how NEPC used scenario analyses to determine and test the viability of alternative asset mixes through various economic scenarios. The Commission and Mr. Borden asked questions throughout the presentation and discussed the impact of various factors on investment strategies for the Retirement System’s Portfolio.

(Information relating to this matter has been retained in the Commission’s files and is identified as Exhibit G).

After conclusion of the investment-related presentations, Chairman Gillespie requested that former Commissioner Blaine Ewing stand. He said that the Commission wanted to recognize Mr. Ewing for his many years of service to both the State Retirement Systems Investment Panel and the South Carolina Retirement System Investment Commission, and he presented Mr. Ewing with a framed copy of a resolution that had been adopted by the Commission unanimously. Dr. Pritchett read the following resolution:

> “**Whereas,** Mr. Blaine Ewing, III, Senior Vice President of Investments at the Charleston offices of Morgan Stanley Smith Barney, LLC, was appointed by the Governor to serve on the Retirement System Investment Commission of the South Carolina Retirement Systems and has rendered loyal and faithful service in that position from June 30, 2005 to April 1, 2011, and
>
> **Whereas,** Mr. Blaine Ewing, III, served on the original 1998 Investment Panel, which was created to provide advice to plan trustees on diversification of the investment portfolio by investing up to 50 percent of assets in domestic equities, and he was the only Panel member to transition to the South Carolina Retirement System Investment Commission (“Commission”) in 2005, and
>
> **Whereas,** Mr. Blaine Ewing, III, was a valuable participant, including almost a year as Vice Chairman, in all major Commission business decisions from the Commission’s

inception until April 2011, and was particularly tireless in efforts regarding public equity and enterprise risk management, and

Whereas, Mr. Blaine Ewing, III, over a span of approximately 13 years, witnessed the maturation of the portfolio from one with fixed income assets alone to the Large Public Pension Plan of the Year with 16 asset classes using Modern Portfolio Theory.

NOW, THEREFORE, BE IT RESOLVED, by the South Carolina Retirement System Investment Commission that deep appreciation and gratitude is hereby expressed to Mr. Blaine Ewing, III for sharing his investment expertise and for his long and devoted service as a fiduciary responsible solely to the participants and beneficiaries of the South Carolina Retirement Systems; and

BE IT FURTHER RESOLVED that the Commission formally recognizes and gratefully acknowledges Mr. Blaine Ewing, III's valued service and dedication by the presentation of this certificate this sixteenth day of June, 2011."

Mr. Ewing thanked the Commission and stated that his tenure had been an incredible journey, and he was proud to have served. Mr. Ewing said that during his tenure the Portfolio went from last in 1999 to 2009 Large Pension Plan of the Year at incredible speed. He recognized the Honorable Richard Eckstrom for his foresight and efforts to change laws to allow the Portfolio to be invested in equities and for the creation of the Investment Panel and the Commission. He also said that Mr. Williams had been the best choice for the first Commission Chairman, and he thanked Messrs. Gillespie, Powers and Williams and Dr. Pritchett for all of their hard work, noting that he did not think that anyone realized the amount of time and diligent work that these gentlemen had dedicated to the Commission's success. He said that Mr. Borden had been a great addition and helped to earn the 2009 Large Pension Plan of the Year designation for the Portfolio. Mr. Ewing said that he had learned much during his tenure and was very appreciative of the Commission's accomplishments, particularly given the small staff size. Mr. Ewing also thanked Ms. Shakun Tahiliani, Senior Assistant State Treasurer, for her work behind the scenes and other members of the State Treasurer's Office, and in closing, he said that Ms. Shealy's legal knowledge was extensive, and he thanked her for her hard work throughout the years.

Chairman Gillespie thanked the guests in attendance and recessed the meeting at 6:00 p.m. on Thursday, June 16, 2011, to resume at 8:30 a.m. on Friday, June 17, 2011.

I. CALL TO ORDER, REGULAR COMMISSION BUSINESS MEETING

Chairman Gillespie reconvened the meeting at 8:30 a.m. on Friday, June 17, 2011, and asked if there were any changes to the agenda. There being none, the Commission proceeded with the agenda as adopted the previous day.

Mr. Harper referred to the proposed Commission meeting schedule for 2011-2012. He explained that starting in Calendar Year 2012, Staff proposed moving to a quarterly meeting schedule. Mr. Powers made a motion, which was seconded by Mr. Giobbe and passed unanimously, to adopt the Meeting Schedule for 2011-2012.

(Information relating to the matter has been retained in the Commission's files and is identified as Exhibit H).

Chairman Gillespie called for amendments to the draft minutes from the meeting on November 18-19, 2010. He also noted that the minutes from the April 21, 2011 meeting had not been distributed to the Commission. Upon motion of Dr. Pritchett and second by Mr. Powers, the minutes from the meeting November 18-19, 2010 were approved.

Chairman Gillespie said that the Commission Evaluation forms had been distributed and needed to be submitted to Dori Ditty, Legal and Policy Counsel, as soon as possible

II. INVESTMENT ITEMS

Mr. Borden stated that he proposed no additional changes to the Portfolio's target asset allocations. He asked Messrs. McCusker and Humphreys from NEPC if they had omitted any salient points from the presentation they made the previous day. Mr. Humphreys reiterated that there had been many structural changes to the Portfolio during the past 4 years. Mr. McCusker noted that changes to the target asset allocations that were recommended in November 2010 were being implemented and opined that the Commission was taking the right steps.

Mr. Humphreys began discussions regarding investment performance of the Portfolio. He referred to the Market Environment Overview that had been distributed to the Commission prior to the meeting. Mr. Humphreys explained that some performance metrics and final pricing figures required additional time to study, so the Market Environment Overview covered performance as of March 31, 2011. He said that the Portfolio met the world equity benchmark with minimal risk during the past year. He referred to an asset allocation chart that provided details of the target asset allocation, the actual asset allocation, and the notional asset allocation and explained the asset allocation percentages across the Portfolio. Dr. Pritchett questioned whether the allocation to Strategic Partnerships included investments that could be categorized in different asset classes, and Mr. Humphreys indicated that because of the nature and structure of Strategic Partnerships, the allocation contained a mix of different asset classes that were presented in the notional asset allocation graph.

Mr. Humphreys stated that the composite performance was 3.5 percent for the quarter, 13.4 percent for the last year, and 22.1 percent for the two-year annualized return. He emphasized the significant changes that the Commission had made to the Portfolio since inception and noted that since the Commission was still in its early stages, historical rankings clouded current performance rankings. He said that the Portfolio ranked in the 91st percentile among public pension funds for five-year annualized returns. Mr. Borden explained the impact of various market trends on the Portfolio and its peer rankings. Mr. Humphreys highlighted performance of several different asset classes within the Portfolio.

Mr. Borden referred to Portfolio performance reports prepared by Staff, which included the report for periods ended March 31, 2011, a draft report for periods ended April 30, 2011, a memorandum relating to preliminary performance estimates for periods ended May 31, 2011, and the RSIC Weekly Portfolio-Level Dashboard as of June 15, 2011. He provided highlights of the reports and estimated that as of June 14, 2011, the fiscal year-to-date return was 16.71 percent with a policy benchmark return of 15.46 percent. He projected that returns for the current fiscal year would be even more solid than the excellent returns from the last fiscal year.

(Information relating to the matter has been retained in the Commission's files and is identified as Exhibits I-1 through I-7).

Mr. Borden introduced Mark Attanasio, Managing Partner, and Joe Viola, Vice President, from Crescent Capital Group (Crescent) to provide a review of the TCW Palmetto Strategic Partnership (TCW-SP) and to discuss potential opportunities. Mr. Borden provided background information about the Commission's history with the Trust Company of the West (TCW) and

TCW-SP and explained several structural changes that had occurred since inception of the TCW-SP. He noted that the TCW-SP had been comprised of primarily two groups: TCW mortgage investments and TCW/Crescent for other credit-type investments.

Mr. Attanasio explained that Crescent had been spun out of TCW effective January 1, 2011, but Crescent continued to manage $10-11 billion for various TCW clients on a sub-advisory basis, and he provided additional background information. He noted that the exit from TCW was amicable and that he continued to serve on the TCW-SP Investment Committee as a TCW representative.

Mr. Attanasio said that the TCW-SP's structure allowed flexibility to address changes in capital markets. Mr. Viola provided additional detail regarding the various strategies and funds within the TCW-SP. He explained that $685 million of total commitments had been made in a variety of strategies, $555 million had been funded since inception, and approximately $166 million in cash distributions had been returned to the TCW-SP. Mr. Attanasio explained several new investment opportunities that could provide favorable economics and equity to the partnerships. Mr. Viola provided details regarding individual strategy and fund performance and estimated that the TCW-SP's total net internal rate of return was approximately 20 percent. Moving forward, Mr. Attanasio explained several additional opportunities that would be available to the Commission through the TCW-SP or an alternate investment vehicle. Mr. Borden provided additional information about potential opportunities for a strategic partnership with Crescent and said that Staff did not have a formal recommendation prepared for this meeting. Chairman Gillespie noted that the Commission would consider the opportunities in the future.

(Information relating to the matter has been retained in the Commission's files and is identified as Exhibit J).

Chairman Gillespie stated that the Commission began discussions relating to the creation of the South Carolina Co-Investment Program for private equity investments approximately two years ago. He explained that there had been several iterations of the plan, including hiring a gatekeeper and/or merging it into the NewCo proposal. Chairman Gillespie said that $100 million was approved for South Carolina private equity co-investment opportunities but since progress had been side-tracked, he felt the Commission should reexamine the program and decide to either eliminate or recast it. Mr. Borden explained that at one extreme the Commission could decide not to continue with the concept of a program, and at the other extreme, they could take a more targeted approach to investing in South Carolina.

Mr. Borden reiterated that South Carolina was an underserved market. He noted that the Commission had focused on some regional firms, which by virtue of their companies, had stated goals of investing in the southeast of the United States. He said that the Commission could focus on the underserved market in South Carolina, although the risk return considerations would need to be the same as other potential investments and enough deal flow would be needed to create a properly diversified South Carolina portfolio. He highlighted some of the shortcomings with the proposed gatekeeper model and other approaches.

Mr. Borden said that some potential deal flow providers had been identified in South Carolina that could provide relevant opportunities. He also explained that if a potential investment was identified, the Commission could seek co-investment and due diligence assistance from a national or international firm with expertise in the same field as the potential investment. He said the Commission was at a crossroad of either putting a structure in place to continue with the program or rely on the regional firms to provide some access. Mr. Borden noted that if the

Commission decided to continue with the program, a significant amount of internal resources would need to be devoted to ensure the program's success. He estimated that South Carolina was approximately 0.2 percent of GDP for all of the investment opportunities for the Portfolio, but it would require two or three FTEs to administer such a program. Mr. Borden opined that with appropriate resources, a South Carolina program could be developed over time, but the Commission also had other opportunities that would require fewer resources with much greater potential return. Mr. Giobbe questioned the amount of the initial allocation, and Mr. Borden replied that $100 million was envisioned, but $200 million would most likely be necessary to get the program off the ground and to create adequate diversity. The Commission discussed various aspects and issues relating to the program, including budget and resource constraints, fiduciary considerations, focused investments within South Carolina versus regional exposure, and alternative ways to capture investment opportunities in South Carolina. Mr. Williams noted that South Carolina firms had always been evaluated and considered the same as other domestic and international managers in accordance with the Commission's fiduciary responsibilities, the Portfolio had gained exposure to South Carolina investments through natural, prudent selection, and he did not feel that it would be in the best interest of the Portfolio to create a program that would focus solely on opportunities in South Carolina unless the Legislature approved the additional funding to properly run the program. After further discussion, Mr. Borden said that this issue would be added to the agenda for the Commission's meeting in September 2011.

(Information relating to the matter has been retained in the Commission's files and is identified as Exhibit K).

Mr. Borden introduced David Klauka, Senior Alternatives Officer, for a presentation regarding the Avenue-SC Global Opportunities Fund, L.P. (Avenue). Mr. Klauka stated that Staff recommended increasing the Avenue allocation from $250 million to $500 million. He noted that current fund performance was very favorable, and he highlighted various reasons to increase the allocation, including market opportunities, preferred economics, and return potential. After further discussion, Mr. Powers made a motion, which was seconded by Mr. Williams and passed unanimously, to approve the recommendations of Staff as presented, to commit an additional $250 million for investments in the Avenue-SC Global Opportunities Fund, L.P. for a total allocation to Avenue not to exceed $500 million, and to authorize the Chairman or his designee to negotiate and execute any necessary documents to implement the investments upon approval for legal sufficiency by General Counsel.

(Information relating to the matter has been retained in the Commission's files and is identified as Exhibit L).

Mr. Harper referred to a memo regarding proposed investments with the D.E. Shaw Group (DESCO) that had been provided to the Commissioners prior to the meeting. He stated that the Commission currently had $350 million committed to the D.E. Shaw Composite Fund and $100 million committed to the D.E. Shaw Direct Capital Fund. Mr. Harper proposed combining both funds into one master account with a limited partnership structure and increasing the allocation to the master account to $750 million, which would provide the Commission with the ability to efficiently access and rebalance within DESCO's investment strategies. He noted that the Commission approved $750 million for investment in a Strategic Partnership with DESCO several years ago, which was later rescinded due to market conditions and liquidity issues. After further discussion, Mr. Williams made a motion, which was seconded by Mr. Loftis and passed unanimously, to approve the recommendations of Staff as presented, to create a master account structure or a limited partnership with the D.E. Shaw Group, to allocate an amount not to exceed $750 million to be invested in DESCO investment strategies which would include the transfer of the investments from the D.E. Shaw Composite Fund (approximately $350 million) and investments from the D.E. Shaw Direct Capital Fund (approximately $100 million), and to authorize the Chairman or his designee to negotiate and to execute any necessary documents to implement the investments upon approval for legal sufficiency by General Counsel.

(Information relating to the matter has been retained in the Commission's files and is identified as Exhibit M).

Mr. Borden referred to the item on the agenda relating to the Aquiline II Co-Investment Fund. Mr. Borden explained that while a limit on co-investments had been discussed, it was not established when the Commission approved co-investments with Aquiline in May 2010. He explained that the Commission had approved a $100 million commitment to Aquiline Financial Services Fund (Aquiline I) in 2007, a $50 million commitment to Aquiline Financial Services Fund II (Aquiline II) in October 2009, and a $50 million commitment to a co-investment sidecar relating to Aquiline II in October 2009. Additional opportunities arose prior to closing Aquiline II and the co-investment sidecar, including a co-investment opportunity relating to Aquiline I, and the Commission approved an increase to a $100 million commitment to Aquiline II and authorized co-investments with Aquiline without tying the co-investments to a specific fund. Mr. Borden said that he had originally suggested no limit on the co-investments, but after discussion with the Commission, he had suggested a $500 million cap on all Aquiline co-investments, but the motion passed by the Commission without a specified limit on co-investment allocations. He added that the Commission had invested in $100 million in a co-investment with Aquiline I relating to Credit Research and Trading (CRT). Chairman Gillespie and Dr. Pritchett suggested a lower limit than $500 million and if necessary, an increase could be brought to the Commission as needed in the future. After further discussion Mr. Williams made a motion, which was seconded by Mr. Powers and passed unanimously, to authorize an allocation in an amount not to exceed $400 million in investments with Aquiline Capital Partners, LLC and its affiliates, and to authorize the Chairman or his designee to negotiate and execute any necessary documents to implement the investments upon approval for legal sufficiency by General Counsel.

Ms. Shealy began discussions regarding a proposed policy relating to Strategic Partnerships. She explained that Strategic Partnerships were structured based on the Commission's needs and noted that throughout the process of creating Strategic Partnerships over the past few years, provisions had been included in the legal documents that allowed the Commission additional input into certain investment and operational matters. She proposed a uniform policy for Strategic Partnerships whereby the Commission appointed the Chairman as its designee and delegated the authority to make decisions relating to certain matters within Strategic Partnerships and to authorize the Chairman to delegate that authority as he deemed appropriate. She explained that this process, as had been implemented in the Morgan Stanley Strategic Partnership, would provide the Chairman with the option to bring certain Strategic Partnership matters to the full Commission, to make a determination on behalf of the Commission, or to delegate the authority to implement the action to appropriate Staff. She gave several examples of the types of decisions that were routinely made within Strategic Partnerships, such as ministerial tasks that would not require full Commission input or the admission of additional partners, which should be approved by the full Commission. Mr. Powers, speaking as a former Commission Chairman, noted that this proposal would only codify the current practice and added further that if full Commission input was required for every minor or non-substantive decision, the Commission would spend all of its meetings discussing ministerial or technical changes. Mr. Borden, noting that Mr. Loftis had requested an executive action report at the previous meeting, reported that Ms. Shealy had maintained a master log that tracked changes to any contract or constituent documents, that she had compiled a summary for the Commission, and these types of actions were included in the master log. Ms. Shealy noted that when issues arose in contracts or legal documents that were either not contemplated, not inherent in that particular type of investment, or deviated from what the Commission had approved, the issues would be brought before the full Commission for action. After further discussion, Mr. Williams made a motion to appoint the Chairman as the Commission's designee for purposes of implementing pertinent provisions of the contracts and constituent documents relating to Strategic Partnerships and to authorize the Chairman to delegate the authority, address the issues himself, or bring the matters before the Commission for discussion relating to those provisions as the Chairman deemed appropriate. Mr. Loftis seconded the motion, which passed unanimously.

Mr. Borden referred to materials regarding extending the Commission's contract with NEPC for Fiscal Year 2011-2012. Mr. Borden said that the selection of a general investment consultant was exempt from the South Carolina Procurement Code by action of the South Carolina Budget and Control Board on February 14, 2002 pursuant to South Carolina Code §11-35-710 and was governed by the "Named Service Provider" provisions of the Commission's Service Provider Selection Policy. Chairman Gillespie noted that NEPC's fee was 30 to 40 percent lower than the other proposals submitted by consultants during the 2006 Request for Proposals process. Mr. Williams said that although he was pleased with NEPC's performance, he did not feel that the Commission should rush into a contract extension longer than one year. After further discussion, Mr. Powers made a motion, which was seconded by Mr. Williams and passed unanimously, to extend the contract with NEPC until the end of Fiscal Year 2012.

(Information relating to the matter has been retained in the Commission's files and is identified as Exhibit N).

Mr. Harper referred to the draft revisions to the Statement of Investment Objectives and Policies (SIOP), which merged the Statement of Investment Objectives and the Statement of Investment Policies previously adopted by the Commission into one document. He highlighted several changes made at the request of the Commission, including also merging certain sections of the Annual Investment Plan with the SIOP and consolidating some provisions. He noted that the SIOP must be reviewed and reaffirmed or amended at least on an annual basis per statute and that the Commission could amend the document anytime as it deemed appropriate. After further discussion, Dr. Pritchett made a motion, which was seconded by Mr. Powers and passed unanimously, to approve the Statement of Investment Objectives and Policies as presented.

(Information relating to the matter has been retained in the Commission's files and is identified as Exhibit O).

III. ADMINISTRATIVE ITEMS

Mr. Borden stated that Deloitte-Touche LLP (Deloitte) had been selected to conduct an investment risk assessment for the Commission. Ms. Corbett introduced Joe Deitzer, Senior Manager, and Michael Chung, Director (via telephone conference call), from Deloitte for a project overview. Mr. Deitzer explained the project scope, key activities and deliverables, and he provided an estimated timeline for completion. He also noted that the engagement would be divided into an investment risk assessment and assistance in developing an internal investment audit program. Mr. Powers asked whether the deliverables would result in a signed audit letter, and Mr. Deitzer replied that a signed audit letter was not typically provided for consulting engagements. He said the deliverables would be a Risk Methodologies Report, a Risk/Gap Report, an Audit Committee Structure recommendation, a draft Audit Committee Policy and Procedures Manual, and a suggested Year-One Audit Plan. Mr. Chung stated that Deloitte would also assist the Commission with the identification and recruiting of a Director of Internal Audit and possibly assist with the execution of the Year-One Audit Plan. The Commission and Mr. Borden asked questions throughout the presentation and discussed the impact of various factors on investment strategies for the Retirement System's Portfolio.

(Information relating to the matter has been retained in the Commission's files and is identified as Exhibit P).

Mr. Borden began discussions regarding fiduciary liability insurance. He reported that the policy for fiduciary liability insurance was maintained by the Retirement System currently, it was due for renewal, and it would be worthwhile to review the coverage and scope. Mr. Borden said that the current policy was broad and covered the Commission, Staff, the Retirement System, and key staff of the South Carolina Budget and Control Board. He also noted that as the Commission hired more staff, additional coverage might be needed. Mr. Borden stated that the State was supposed to indemnify the Commission and Staff for liability, but noted that he understood that legislative action might be required to set aside funds for indemnification if the need arose. He opined that the Commission should evaluate the fiduciary liability insurance issue more thoroughly and perhaps increase the scope and amount of coverage. Mr. Powers suggested that the Audit Committee and Deloitte discuss fiduciary liability insurance issues.

IV. OTHER BUSINESS

Chairman Gillespie asked if there was any other business for the Commission in open session, and there was none.

V. EXECUTIVE SESSION

Mr. Loftis made a motion that the Commission recede to executive session to receive a legal briefing and to discuss a personnel matter. Mr. Williams seconded the motion, which passed unanimously, and Chairman Gillespie announced that the Commission would meet in executive session for those purposes.

The Commission reconvened in open session and Chairman Gillespie reported that the Commission took no action while meeting in executive session.

VI. AJOURNMENT

There being no further business, the meeting adjourned at 1:15 p.m.

[Staff Note: In compliance with S.C. Code Ann. §30-4-80, public notice of and the agenda for this meeting were delivered to the press and to parties who requested notice and were posted at the entrance and in the lobby at 1201 Main Street, Columbia, SC, and at the Wampee Training and Conference Center at 1274 Wampee Plantation Road, Pinopolis, South Carolina prior to 9:00 a.m. on June 15, 2011.]