



MINUTES

**Meeting of the Investment Committee
of the Board of Trustees of the
State Universities Retirement System
2:15 p.m. Tuesday, December 1, 2009
The Northern Trust
50 South LaSalle Street
Chicago, Illinois 60603**

The following Trustees were present: Dr. J. Fred Giertz, Chair; Dr. Jeffrey Beaulieu, Mr. Matthew Berns, Ms. Patricia Cassidy, Dr. John Engstrom, Ms. Dorinda Miller, Mr. Steven Rogers (via teleconference), Mr. Antonio Vasquez, Mr. Mitchell Vogel (via teleconference), and Dr. Marva Williams.

Others present were: Ms. Judith A. Parker, Interim Executive Director; Mr. Daniel L. Allen, Chief Investment Officer; Mr. Kelly A. Jenkins, General Counsel; Mr. Douglas C. Wesley, Deputy Chief Investment Officer; Ms. Kimberly Pollitt, Senior Investment Officer; Ms. Lou Ann Fillingham and Mr. Tony Lee, Investment Officers; Ms. Marilyn Branson, Investment Governance and Compliance Officer; Ms. Shelley Porter, Chief Financial Officer; Mr. Steven Hayward, Director of Internal Audit; Mr. Michael Sheppard, Assistant Deputy Director of the Self-Managed Plan; Mr. Doug Steele, Director of Application Development and Research; Mr. Chris Hansen, Director of Operations; Ms. Angela Lieb, Director of Member Services; Ms. Lori Kern and Ms. Stacy Smith, Executive Assistants; Ms. Mary Pat Burns, Burke, Burns & Pinelli; Mr. Russell Ivinjack, Ms. Laurel Nicholson, Ms. Cate Polley, Ms. Heather Christopher, and Ms. Amy Paris, EnnisKnupp + Associates; Ms. Leslie Thompson and Ms. Amy Williams, Gabriel, Roeder, Smith & Company; Mr. Don Pollak, Northern Trust Investments; Ms. Patti Somerville-Koulouris, The Northern Trust Company; Ms. Linda Brookhart, State Universities Annuitants Association; Mr. Jake Baggott, SURSMAC; Mr. Steve Zahn, Governmental Consulting Solutions; Mr. Edgar Hernandez, Service Employees International Union; and Mr. Barry Burr, Pensions & Investments.

Trustee Giertz called the meeting to order at 2:15 p.m.

Trustee Stephen Rogers was unable to physically attend the meeting due to employment commitments. Trustee Berns moved:

- To allow Trustee Rogers to participate via teleconference.

Motion seconded and, with a unanimous vote, was carried.

REPORT FROM THE OCTOBER 20, 2009, INVESTMENT COMMITTEE MEETING

Mr. Daniel Allen distributed the Investment Update as of September 30, 2009, and reported a strong quarter. For comparison purposes, Mr. Allen noted that the calendar year ending December 31, 2008, showed a return of -27.8%; however, for the calendar year-to-date through November 30, 2009, the estimated investment return is 20%. The return for the fiscal year through November 30, 2009, is approximately 15%.

Mr. Russell Ivinjack summarized EnnisKnupp + Associates' (EnnisKnupp) 3rd Quarter Performance Report. SURS showed a healthy return of 13.5% for the 3rd quarter and 18.3% for the calendar year as of September 30, 2009.

Mr. Allen also reviewed the total fund performance as compared to other Illinois public pension funds. A copy of "SURS Funding Status, 2010 Fiscal Year-to-Date Results" is incorporated as a part of these Minutes as [Exhibit 1](#). Mr. Allen further noted that, aside from the Illinois Municipal Retirement Fund, SURS out-performed all other Illinois funds as shown in the "Illinois Public Pension Funds Total Fund Performance" report which is incorporated as a part of these Minutes as [Exhibit 2](#).

APPROVAL OF MINUTES

Trustee Vogel moved that:

- The Minutes from the October 20, 2009, Investment Committee meeting be approved as presented.

Motion seconded and carried with all trustees present voting in favor except Trustee Berns who voted present.

Mr. Allen's memoranda entitled "Report from the October 20, 2009 Investment Committee Meeting" and "Investment Contracts Approved" are incorporated as a part of these Minutes as [Exhibit 3](#) and [Exhibit 4](#).

**PUBLIC-PRIVATE INVESTMENT PROGRAM (PIIP) INVESTMENT
MANAGER INTERVIEW**

Mr. Ivinjack introduced Oaktree Capital Management’s presentation of their PPIP fund, which is primarily focused on commercial mortgage-backed securities.

Trustee Vasquez moved that:

- The Committee go into closed session pursuant to the Open Meetings Act to consider the sale or purchase of securities or investments or to consider an investment contract pursuant to Section 2(c)(7). Motion was seconded and carried in a roll call vote:

Trustee Beaulieu	aye
Trustee Berns	aye
Trustee Cassidy	aye
Trustee Engstrom	aye
Trustee Giertz	aye
Trustee Hightman	absent
Trustee Miller	aye
Trustee Rogers	absent
Trustee Vasquez	aye
Trustee Vogel	aye
Trustee Williams	aye

Upon the Committee’s return to open session, Trustee Vasquez moved that:

- An allocation of \$40 million, contingent upon successful contract negotiations, be authorized to the Oaktree PPIP Private Fund, L.P., or a parallel vehicle established for tax-exempt investors.

The motion was seconded and carried with all trustees present voting in favor except Trustee Vogel who voted in opposition.

A copy of staff’s memorandum entitled “Public-Private Investment Program Investment Manager Search Recommendation” is incorporated as part of these Minutes as [Exhibit 5](#). A copy of EnnisKnupp’s memorandum dated December 1, 2009, is incorporated as a part of these Minutes as [Exhibit 6](#). A copy of EnnisKnupp’s Investment Profile of Oaktree Capital is incorporated as a part of these Minutes as [Exhibit 7](#). A copy of the letter from the U.S. Department of the Treasury Press Room, dated July 8, 2009, is incorporated as a part of these Minutes as [Exhibit 8](#).

APPROVAL OF THE FISCAL YEAR 2009 ACTUARIAL VALUATION REPORT

Ms. Leslie Thompson and Ms. Amy Williams of Gabriel, Roeder, Smith & Company (GRS) presented the Fiscal Year 2009 Actuarial Valuation Report for the State Universities Retirement System. As of the June 30, 2009, valuation, the total present value of future benefits is approximately \$31 billion, of which approximately \$26 billion is attributable to services already performed (actuarial liability). The normal cost for the current year and future years accounts for the remaining \$5 billion.

Ms. Williams noted that the normal cost has remained relatively level over the last few years. SURS has a net pension obligation (NPO) of approximately \$7 billion dollars, which is attributable to the fact that the State's annual contribution is based on the statutory requirement and not the annual required contribution as determined by GASB standards.

A copy of the memorandum entitled "Fiscal Year 2009 Actuarial Valuation Report" is incorporated as part of these Minutes as [Exhibit 9](#). A copy of the GRS presentation, "SURS Actuarial Valuation as of June 30, 2009," is incorporated as part of these Minutes as [Exhibit 10](#), and a copy of the GRS Actuarial Valuation Report as of June 30, 2009, is incorporated as a part of these Minutes as [Exhibit 11](#).

After discussion of whether to receive and accept or rather to approve the GRS Actuarial Valuation Report, Trustee Berns moved that:

- The Fiscal Year 2009 Actuarial Valuation Report be received and accepted.

The motion was seconded and carried.

APPROVAL OF THE EFFECTIVE RATE OF INTEREST AND NORMAL COST RECOMMENDATIONS FOR FISCAL YEAR 2011

Mr. Allen observed that it is customary practice for GRS to prepare a normal cost calculation, which is based on financials and assumptions as of the end of the fiscal year. The normal cost rate will increase from 9.94% to 10.14% for fiscal year 2011 and a breakdown is presented in the letter from GRS to Mr. Allen, dated November 9, 2009, which is incorporated as a part of these Minutes as [Exhibit 12](#). Ms. Shelley Porter commented that the main practical use of the normal cost rate is to determine employer contributions that come from non-state appropriated sources (i.e. trusts, federal grants, etc.). A memorandum from Mr. Allen entitled "Normal Cost Recommendation" is incorporated as part of these Minutes as [Exhibit 13](#).

Trustee Engstrom moved that:

- The Normal Cost Rate of 10.14% be approved for fiscal year 2011.

The motion was seconded and carried.

Trustee Giertz explained that the effective rate of interest (ERI) was determined by SURS in the past. Public Act 94-4 required that, beginning with fiscal year 2006, the State Comptroller establish the ERI for purposes of the money purchase calculation. Ms. Judith Parker added that the ERI must still be determined by the SURS Board of Trustees for all other purposes, including the calculation of purchases of service credit, refunds for excess contributions, and lump sum retirement benefits. A memorandum from Ms. Parker and Mr. Allen entitled “Effective Rate of Interest” is incorporated as part of these Minutes as [Exhibit 14](#).

Mr. Allen stated that past and expected investment returns suggest a slight decrease in the ERI, and he recommended that it be lowered to 7.5%. Mr. Allen referenced the schedules of Investment Rates of Return & ERI Credited, Tables 2 and 3 of [Exhibit 14](#).

Trustee Vogel moved that:

- The Effective Rate of Interest (ERI) be set at 7.5% to be applied to account balances for fiscal year 2011, beginning July 1, 2010.

The motion was seconded and carried.

DIRECT REAL ESTATE FUNDS ANNUAL MANAGER REVIEWS

Ms. Heather Christopher provided an overview of current real estate market conditions and SURS’ real estate portfolio. A copy of EnnisKnupp’s presentation entitled “Real Estate Overview – SURS December 1, 2009” is incorporated as a part of these Minutes as [Exhibit 15](#). Ms. Christopher noted that, currently, all real estate is producing negative returns, although signs of recovery in the REIT market are evident. Despite the decreased values, Ms. Christopher noted that SURS is ideally situated to take advantage of market recovery through recently approved real estate investments.

Mr. Douglas Wesley discussed performance issues for the direct real estate fund managers as set forth in the memorandums entitled “Executive Summary of the Direct Real Estate” and “RREEF Real Estate Annual Review”, which are incorporated as part of these Minutes as [Exhibit 16](#) and [Exhibit 17](#), respectively. Mr. Wesley advised that SURS currently holds a seat on the Advisory Committees for the UBS Realty Investors Trumbull Property Fund and the Dune Real Estate Parallel Fund II.

Mr. Wesley also reviewed performance issues with respect to RREEF America II, RREEF America III, and the Trumbull Property Fund. For the one-year period ending

June 30, 2009, the total direct real estate portfolio returned -34.2%, lagging the benchmark return of -30.9%. The Dune Real Estate Fund was recently funded, so performance to date is not meaningful.

Consideration followed regarding the potential termination of RREEF America III as a direct real estate manager and the redemption queue process. Discussion was also held regarding Dune's investment strategy. In December of 2008, \$40 million was committed to the fund, and \$3.6 million has been called to date. Mr. Wesley and Ms. Christopher advised that capital can be deployed over the next three years; however, recent market conditions, including changing fundamentals, pricing, and low transaction volume have slowed the process.

Trustee Vogel moved that:

- RREEF America II be retained as a direct real estate manager
- RREEF America III be terminated as a direct real estate manager
- UBS Realty Investors be retained as a direct real estate manager
- An additional \$100 million be allocated to the UBS Trumbull Property Fund
- The limited partnership interest in Dune Real Estate Parallel Fund II be retained.

The motions were seconded and carried.

Copies of the memorandums entitled "UBS Realty Investors Real Estate Annual Review" and "Dune Real Estate Partners Annual Review" are incorporated as a part of these Minutes as [Exhibit 18](#) and [Exhibit 19](#).

REAL ESTATE INVESTMENT TRUST SECURITIES **ANNUAL MANAGER REVIEWS**

Ms. Lou Ann Fillingham presented the Real Estate Investment Trusts (REITs) asset class review. A copy of the memorandum "Executive Summary of the Real Estate Investment Trusts (REITs) Asset Class" is incorporated as a part of these Minutes as [Exhibit 20](#).

There have been no organizational issues for the past year; however, ING Group announced a restructuring plan that will place ING Clarion under new ownership. Ms. Fillingham further noted that the total REIT portfolio has performed relatively well over the past year. Copies of the annual reviews of ING Clarion Real Estate Securities and RREEF REIT Real Estate Annual Reviews are incorporated as a part of these Minutes as [Exhibit 21](#) and [Exhibit 22](#).

Trustee Beaulieu moved that:

- RREEF be retained as a U.S. and global REIT manager
- ING Clarion Real Estate Securities be retained as a U.S. and global REIT manager

The motions were seconded and carried.

GLOBAL EQUITY ANNUAL MANAGER REVIEWS

Ms. Kimberly Pollitt provided an overview of SURS' global equity asset class. As of September 2009, SURS' global equity portfolio was valued at \$1.2 billion which accounted for approximately 9.4% of the total fund. The portfolio returned -0.1% for the year. A copy of the memorandum entitled "Executive Summary of the Global Equity Asset Class and Manager Reviews" is incorporated as a part of these Minutes as [Exhibit 23](#).

Ms. Pollitt noted performance and organizational concerns with the Capital Guardian global equity account. Since inception, their performance has lagged its benchmark by more than 100 basis points annually. In addition, other organizational concerns include a significant turnover of the portfolio management team and significant losses of accounts and assets in the global equity strategy. SURS and EnnisKnupp jointly recommend termination of the Capital Guardian account due to organizational and long-term performance concerns.

Staff and EnnisKnupp recommended that the approximately \$270 million in assets with Capital Guardian be reallocated with \$200 million to be reallocated as follows:

\$70 million to Aberdeen Asset Management
\$70 million to T. Rowe Price
\$30 million to Calamos Advisors
\$30 million to Payden & Rygel
Remaining balance of \$70 million will be placed in the SURS' cash-flow account (to assist with the paying of benefits)

In response to a process-related question from Trustee Berns, Mr. Allen provided additional background regarding the steps leading to the recommendation to terminate Capital Guardian, including placement of the manager on the watch list. Mr. Ivinjack provided a history of Capital Guardian's poor performance and organizational issues. Mr. Wesley discussed the turnover of the portfolio management team at Capital Guardian, which has drastically changed over time. A copy of the memorandum entitled "Capital Guardian Global Equity Manager Annual Review" is incorporated as a part of these Minutes as [Exhibit 24](#).

Trustee Steven Rogers joined the meeting via teleconference during this discussion.

Trustee Cassidy moved that:

- Capital Guardian be terminated as a global equity manager
- Wellington Management be retained as a global equity manager
- Aberdeen Asset Management be retained as a global equity manager
- Aberdeen Asset Management be allocated an additional \$70 million in the global equity strategy
- T. Rowe Price be retained as a global equity manager
- T. Rowe Price be allocated an additional \$70 million in the global equity strategy
- Payden & Rygel be retained as a global equity manager
- Payden & Rygel be allocated an additional \$30 million in the global equity strategy
- Calamos Advisors be retained as a global equity manager
- Calamos Advisors be allocated an additional \$30 million in the global equity strategy.

The motions were seconded and carried.

A copy of EnnisKnupp's memorandum entitled "Global Equity Overview" is incorporated as a part of these Minutes as [Exhibit 25](#). Copies of the memorandums entitled "Wellington Management Global Equity Manager Annual Review," "Aberdeen Asset Management Annual Review," "T. Rowe Price International Global Equity Annual Review," "Payden & Rygel Global Equity Manager Annual Review," and "Calamos Advisors LLC Annual Review" are incorporated as a part of these Minutes as [Exhibit 26](#), [Exhibit 27](#), [Exhibit 28](#), [Exhibit 29](#), and [Exhibit 30](#), respectively.

INDEX FUND ANNUAL MANAGER REVIEWS

Mr. Tony J. Lee presented a summary of the annual index fund provider reviews. Northern Trust Investments (NTI) and Barclays Global Investors (BGI) manage significant portions of the SURS portfolio. As of December 1, 2009, BGI completed a merger with BlackRock, Inc., and due to the merger, BGI has been placed on SURS' watch list for organizational concerns. Mr. Lee advised that there are no organizational concerns to report regarding RhumbLine Advisers, which currently manages approximately 7.8% of the total portfolio. A copy of the memorandum entitled "Executive Summary of Index Fund Provider Reviews" is incorporated as a part of these Minutes as [Exhibit 31](#).

Trustee Vasquez moved that:

- Barclays Global Investors be retained as an index fund manager
- Northern Trust Investments be retained as an index fund manager
- RhumbLine Advisers be retained as an index fund manager

The motions were seconded and carried.

Copies of the memorandums entitled “Barclays Global Investors Annual Review,” “Northern Trust Investments’ Quantitative Management Group Annual Review,” and “RhumbLine Advisers Annual Review” are incorporated as a part of these Minutes as [Exhibit 32](#), [Exhibit 33](#) and [Exhibit 34](#), respectively.

PROPOSED MODIFICATIONS TO SURS INVESTMENT POLICY

Ms. Kimberly Pollitt provided a brief overview of the proposed modifications to SURS’ Investment Policy for the defined benefit plan. Staff recommended a change to Section V – Asset Allocation and Rebalancing Strategy to reflect the recent 1.0% allocation to the PPIP. Staff also recommended a change to Section XV – Emerging Investment Managers and Broker/Dealers to encourage direct trade execution with minority- and women-owned broker/dealers. A copy of the memorandum entitled “Investment Policy Review” with an attached redlined version of the SURS’ Investment Policy is incorporated as a part of these Minutes as [Exhibit 35](#).

Trustee Vasquez moved that:

- The revised Investment Policy document for the defined benefit plan be approved, as presented.

The motion was seconded and carried.

RECOMMENDATIONS REGARDING THE SURS MANAGER DEVELOPMENT PROGRAM

Mr. Allen requested authorization to conduct a search for minority- and women-owned firms to manage the Treasury Inflation-Protected Securities (TIPS) portfolio in the Manager Development Program (MDP). Currently, the approved strategic TIPS allocation is 5%, while the actual allocation is approximately 2.5% due to the liquidation of assets from TIPS during the recent financial crisis. Completion of the TIPS search will assist in the process of achieving desired utilization levels of minority- and women-owned investment management firms. The search allocation is estimated to be \$175 million, \$25 million more from what was initially considered in the plan. A copy of the memorandum entitled “Recommendation to Approve Search for Treasury Inflation-Protected Securities (TIPS) Mandate” is incorporated as a part of these Minutes as [Exhibit 36](#).

Trustee Beaulieu moved that:

- A search be conducted to identify qualified domestic Treasury Inflation-Protected Securities (TIPS) investment managers in the Manager Development Program.

The motion seconded and carried.

Mr. Lee reported that concerns with Cypress Asset Management (Cypress) have emerged as a result of organizational changes and current investment strategies. Cypress is not a funded manager, and due to the issues outlined by Mr. Lee, SURS staff recommended that Cypress be terminated as a fixed income manager in the MDP. A copy of the memorandum entitled “Concerns Regarding Cypress Asset Management” is incorporated as a part of these Minutes as [Exhibit 37](#).

Trustee Beaulieu moved that:

- Cypress Asset Management be terminated as a fixed income manager in the Manager Development Program.

The motion seconded and carried.

A copy of the memorandum entitled “Manager Development Program – Fixed Income Manager Recommendation” is incorporated as a part of these Minutes as [Exhibit 38](#).

FIDELITY INVESTMENTS SELF-MANAGED PLAN (SMP) **ANNUAL REVIEW**

Ms. Fillingham presented the Fidelity Investments (Fidelity) annual review. Fidelity recently began to offer Class K mutual funds, a lower-cost share class of existing funds, to certain retirement plans. SURS plans to implement Class K share funds in February of 2010 for the SMP. In order to expand the socially responsible investing (SRI) options in the SMP, Fidelity, EnnisKnupp and SURS staff continue to research potential funds that could be offered on the Fidelity platform. A copy of the memorandum entitled “Fidelity Annual Review” is incorporated as a part of these Minutes as [Exhibit 39](#).

Trustee Vogel questioned the attraction of the Puritan Fund. Ms. Fillingham stated that said fund is an actively managed, balanced fund. Discussion followed.

An additional concern was the manner in which information is distributed to members participating in the SMP. Ms. Judy Parker advised that Mr. Mike Sheppard, Assistant Deputy Director of the Self-Managed Plan, is responsible for the outreach, a joint effort between SURS and the providers to provide the outreach.

Trustee Vogel moved that:

- Fidelity Investments be retained as an investment service provider for the SURS Self-Managed Plan.

The motion was seconded and carried.

**CONSIDERATION OF ORGANIZATIONAL CHANGES AT HOLLAND
CAPITAL MANAGEMENT**

Mr. Allen provided a brief overview of organizational changes at Holland Capital Management, which is a manager in the MDP. Mr. Allen advised that, following Mr. Louis Holland's recent retirement, Holland Capital is in the process of redistributing ownership throughout the organization. Ms. Monica Walker is the current President and CIO. As Board consent is required whenever a change in ownership structure occurs, staff and EnnisKnupp jointly recommended that consent to the assignment of the investment management agreement with Holland Capital Management be approved. A copy of the memorandum entitled "Holland Capital Management Consent" is incorporated as a part of these Minutes as [Exhibit 40](#).

Trustee Engstrom moved that:

- Consent to the assignment of the investment management agreement with Holland Capital Management be approved pending legal reviews, which will result from the expected acquisition of the 90% interest of Louis Holland.

The motion seconded and carried.

A copy of EnnisKnupp's memorandum entitled "Holland Organizational Update" is incorporated as a part of these Minutes as [Exhibit 41](#). A copy of the letter from Holland Capital Management dated October 20, 2009, is incorporated as a part of these Minutes as [Exhibit 42](#).

**CONSIDERATION OF LEGAL COUNSEL
FOR INVESTMENT RELATED ISSUES**

Mr. Kelly A. Jenkins informed the Committee that outside legal counsel, Mayer Brown, has a conflict of interest with respect to Macquarie Infrastructure Partners II Fund. Mr. Jenkins advised that staff compiled a list of experienced attorneys and, after sending inquiries to all of the firms identified, Bryan Cave, LLP, was selected to be recommended as external legal counsel for negotiations with the Macquarie Infrastructure Partners II Fund.

Trustee Cassidy moved that:

- Bryan Cave LLP, be selected as external legal counsel contingent upon successful contract negotiations, for document review and negotiations of the transaction with the Macquarie Infrastructure Partners II Fund.

The motion was seconded and carried.

A copy of the memorandum entitled "Outside Counsel for Macquarie Infrastructure Partners II Fund" is incorporated as a part of these Minutes as [Exhibit 43](#).

INFORMATIONAL ITEMS NOT REQUIRING COMMITTEE ACTION

The following items were provided for reference and are incorporated as a part of these Minutes:

1. [Exhibit 44](#) - Letter to Senator Iris Y. Martinez dated November 6, 2009
2. [Exhibit 45](#) - Memorandum entitled "December 2009 Investment Manager Watch List"
3. [Exhibit 46](#) - Memorandum entitled "Annual Review of Minority-Owned and Women-Owned Broker/Dealer Usage by SURS Investment Managers"
4. [Exhibit 47](#) - Memorandum entitled "Compliance Update"
5. [Exhibit 48](#) - Possible Topics for SURS Trustee Educational Forum
6. [Exhibit 49](#) - Standard Investment Reports as of September 30, 2009
7. [Exhibit 50](#) - Investment Compliance Activities 2009-2010
8. [Exhibit 51](#) - SURS and EnnisKnupp Fiscal Year 2010-11 Work Plan
9. [Exhibit 52](#) - Schedule of Formal Reviews for SURS Investment Managers, Defined Benefit Plan & SMP
10. [Exhibit 53](#) - Memorandum entitled "Schedule of Investment Committee Meetings"

There being no further business to come before the Committee, Trustee Berns moved that the meeting be adjourned. The motion was seconded and carried.

Respectfully submitted,



Ms. Judith A. Parker
Interim Executive Director

JAP:ssr