

**STATE COMPENSATION INSURANCE FUND
INVESTMENT COMMITTEE**

MINUTES OF OPEN SESSION MEETING

July 14, 2011

The Investment Committee met on July 14, 2011 at the Omni San Francisco Hotel, Russian Hill Room, 500 California Street, San Francisco, California.

AGENDA ITEM 1: CALL TO ORDER AND ROLL CALL

The meeting came to order at 12:10 p.m. and the following members were present: Chair Senator Michael J. Machado (Ret.); Donald E. Garcia; and Scott K. Reid. Francis E. Quinlan (Alternate) joined the meeting at agenda item 2.

There was a quorum.

Also present: President Tom Rowe; Chief Financial Officer Dan Sevilla; Chief Investment Officer Peter Guastamachio; General Counsel and Corporate Secretary Carol Newman; Treasury & Investments Program Manager and Assistant Corporate Secretary Stephanie Chan; Treasury & Investments Manager Maria Quintanilla; Staff Counsel David Freitas; Wellington Management Company, LLP, Director of Financial Reserves Management Eric Tanaka and Tactical Asset Allocation Analyst Eric Rice, PhD.

AGENDA ITEM 2: APPROVAL OF MAY 12, 2011 OPEN MEETING MINUTES

Sen. Machado requested a motion to approve the minutes of the May 12, 2011 Open meeting of the Investment Committee as presented.

Sen. Machado requested public comment of which there was none.

MOTION: Mr. Reid SECOND: Mr. Garcia

To approve the minutes of the May 12, 2011 Open meeting of the Investment Committee as presented.

YES: 3 NO: 0 Motion carried.

AGENDA ITEM 3: APPROVAL OF INVESTMENT TRANSACTIONS

Stephanie Chan, Treasury & Investments Program Manager, recommended that the Investment Committee approve investment transactions from April 1, 2011 to May 31, 2011. All investment transactions for this period were made in accordance with the Investment Policy at the time of purchase. During the months of April and May 2011, State Fund purchased 57 securities totaling approximately \$805M. During this same time period, State Fund sold 8 bonds for

a total of \$173.6M. Year-to-date through May 31, 2011, State Fund recognized a net capital gain of approximately \$10.6M. The book value of State Fund's portfolio as of May 31, 2011 was approximately \$19.2B.

Sen. Machado requested public comment of which there was none.

After presentation of the Bond Transactions report, the following actions were taken:

MOTION: Mr. Reid

SECOND: Mr. Garcia

To approve the Bond Transactions for the period of April 1, 2011 through May 31, 2011.

YES: 3

NO: 0

Motion carried.

Ms. Chan presented the Compliance Report indicating that all of State Fund's investments were in compliance with the Investment Policy and met certain minimum credit rating standards at the time of purchase. There are two items on the report. The two out-of-compliance bonds are Rancho Cucamonga and the State of Oregon bonds. At the end May 2011, the total amount of the bonds listed on the report is \$39M, which represents approximately 0.2% of State Fund's investment portfolio.

Sen. Machado requested public comment of which there was none.

After presentation of the Compliance Report, the following actions were taken:

MOTION: Mr. Reid

SECOND: Mr. Garcia

To approve the Compliance Report for the period of April 1, 2011 through May 31, 2011.

YES: 3

NO: 0

Motion carried.

AGENDA ITEM 4: PEER ANALYSIS ON 2010 INVESTMENT RESULTS

Peter Guastamachio, State Fund's Chief Investment Officer, presented the Peer Analysis as of Year End 2010. This Peer Analysis includes results of 43 peer companies, of which 17 are other state funds, 15 are competitors in California and 11 comparable companies of similar size to State Fund. Mr. Guastamachio reported that State Fund has a strong portfolio compared to our competitors and has the highest NAIC Bond rating distribution when compared to both competitors and other State Funds. State Fund's portfolio is also highly liquid and due to the short duration, 48% of the bonds will mature within the next five years. He also reported that State Fund is in the top quartile in regards to investment yield and State Fund's high investment income placed us near the top of the 43

peers. Mr. Guastamachio stated that some of State Fund's competitors are ahead in total return, which is most likely due to the fact that they can invest in Equities and State Fund cannot. Of the 43 peer companies included in this study, 32 invest in equities as part of their portfolio, including 16 other state funds that are authorized to invest in equities.

AGENDA ITEM 5: PORTFOLIO DIVERSIFICATION – THE CASE FOR EQUITIES

Eric Tanaka, Director of Financial Reserves Management at Wellington Management Company, LLP, reported that Wellington has \$660B assets under management (AUM). He discussed that bonds and equities serve different investment objectives. Equities provide higher investment returns but have more risk. Wellington's Tactical Asset Allocation Analyst, Eric Rice, PhD, discussed that U.S. equities outperform U.S. bonds over longer periods (10 years plus) but are more volatile from year to year. Mr. Rice stated that an incremental reallocation of up to 10% of a bond portfolio to U.S. equities would provide greater diversification for the portfolio, less overall volatility and better returns. Although State Fund is not currently authorized to invest in equities, Mr. Rice stated that we should consider our investment duration benchmark to determine whether we can accept the short-term volatility of equities. Additionally, a limited U.S. equity portfolio could act as a hedge against inflation.

AGENDA ITEM 6: REVISED INVESTMENT COMMITTEE CHARTER

Staff Counsel David Freitas presented the revised Investment Committee Charter. He explained that the purpose of the Investment Charter is to provide guidance to the Investment Committee concerning the oversight responsibilities of the Investment Committee in assisting the Board of Directors to fulfill its supervisory and approval responsibilities for the investment of State Fund money and periodic review of State Fund's investment portfolio and bank relationships.

Mr. Freitas stated that effective as of this meeting, the Investment Committee shall as authorized by the Board of Directors and as provided for in the Investment Committee Charter, approve and ratify on behalf of the Board, all the investment transactions entered into by State Fund from and after April 1, 2011 and onward, per the procedures set forth in the California Insurance Code Sections 1200 and 1201.

Mr. Freitas also explained that the revised Investment Committee Charter includes references to certain statutes in the California Insurance Code pertaining to the investment and banking activities of State Fund.

Mr. Freitas advised that the Investment Committee should consider providing a calendar of specific oversight activities at the next Investment Committee meeting in September 2011.

After presentation of the Investment Committee Charter, the following actions were taken:

MOTION: Mr. Reid

SECOND: Mr. Garcia

To approve and recommend the Board of Directors approve the Investment Committee Charter.

YES: 3

NO: 0

Motion carried.

AGENDA ITEM 7: PUBLIC COMMENT ON APPROPRIATENESS OF CLOSED SESSION FOR ITEMS 10 THROUGH 11

Senator Machado requested public comment of which there was none.

The Investment Committee immediately convened into Closed Session.

AGENDA ITEM 12: CALL TO ORDER AND ROLL CALL

The meeting was called to order at 1:55.m. following the conclusion of the Closed Session and the following Members were present: Sen. Michael Machado (Ret.) Chair; Donald E. Garcia; Scott K. Reid; and Francis E. Quinlan.

There was a quorum.

Also present: President Tom Rowe; Chief Financial Officer Dan Sevilla; Chief Investment Officer Peter Guastamachio; General Counsel and Corporate Secretary Carol Newman; Treasury & Investments Program Manager and Assistant Corporate Secretary Stephanie Chan; Treasury & Investments Manager Maria Quintanilla; and Staff Counsel David Freitas.

AGENDA ITEM 13: COMMITTEE MEMBER PRESENTATIONS

Senator Machado asked if there were any presentations from the Committee members of which there were none.

AGENDA ITEM 14: PROPOSALS AND SUGGESTIONS FOR SEPTEMBER 14, 2011 AGENDA

Senator Machado asked if there were any additional recommendations from the committee for the September 14, 2011 agenda. No additional recommendations were made.

ADJOURNMENT

There being no further business before the Investment Committee, the meeting adjourned at 1:56 pm.

Respectfully submitted,

Stephanie Chan
Assistant Corporate Secretary