T H E C A B I N E T

S T A T E O F F L O R I D A

Representing:

STATE BOARD OF ADMINISTRATION

The above agencies came to be heard before THE FLORIDA CABINET, Honorable Governor Crist presiding, in the Cabinet Meeting Room, LL-03, The Capitol, Tallahassee, Florida, on Tuesday, June 8, 2010, commencing at approximately 1:12 p.m.

Reported by:

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I N D E X

STATE BOARD OF ADMINISTRATION
(Presented by ASH WILLIAMS)

P R O C E E D I N G S

GOVERNOR CRIST: My understanding is the General will be here very shortly. So I think that we have a quorum with both the CFO and myself. And, Ash, why don't we go ahead and begin the State Board of Administration. And I know, as I say, the general will be here momentarily.

MR. WILLIAMS: Good afternoon Governor, CFO.

GOVERNOR CRIST: Good afternoon.

MR. WILLIAMS: The first thing we have today is a request for the approval of the minutes from the 13 April meeting.

CFO SINK: Move it.

GOVERNOR CRIST: I second. They are approved.

MR. WILLIAMS: Okay. The second thing is, I would like to give you a little sense of where we're headed today.

CFO SINK: Ash, just speak up.

MR. WILLIAMS: Oh, okay. Is that better?

CFO SINK: You have a quiet voice.

MR. WILLIAMS: Is that better?

GOVERNOR CRIST: Yes.

CFO SINK: Yes.

MR. WILLIAMS: Okay. Good. A little outline of what we're going to cover today. And I'm

mindful we need to wrap up by about 3:00, so we'll keep it moving expeditiously.

You'll recall about a year ago, we had a conversation in this room that, given the tremendous changes we had seen in the financial markets and the haircuts asset pools around the world had suffered during the downturn, that we thought it would be prudent to move ahead proactively, do a review of our assets and liabilities, and from that review of our assets and liabilities, revisit our investment strategy, and to the extent there were any ways in which we could fine-tune our investment strategy to better meet our liability needs over the long term, we would do so.

We are here today primarily to report on that effort, and we are at a point where we have some very tangible recommendations to move forward, and I would like to frame those up for you broadly in terms of context, and then we'll move into the performance reports, the standing reports, and ultimately the review of the asset/liability work.

Basically, we're at a point where we have an investment return assumption of 7 3/4 percent. One cannot possibly earn 7 3/4 percent return without

taking some level of risk, so the question is, how much risk do you take and how do you take it?

Over a period of decades, the investment authority of the State Board of Administration has evolved. When I first worked in the House of Representatives in the late -- mid to late '70s, the sole allowable investments for the State Board were U.S. Treasuries and high-grade corporate bonds.

Over time, over successive years of improved trust, credible performance, and prudent investments, the Board's authority has been broadened to include U.S. equities, expanded to include more U.S. equities, expanded to include foreign equities, expanded to include foreign fixed income, most recently expanded to include alternatives. And also, at some point along the continuum, I left out real estate.

So we have a long history of gradually, incrementally altering investment authority. The cumulative result of these changes over the years and the way they've been implemented is that we now pay 65 cents of every dollar of retirement benefits with investment returns, not taxpayer dollars.

At the current rate we're paying out, which is

roughly $400 a month, that means $270 million every single month, 12 months a year, are being put into the pockets of Florida Retirement System beneficiaries from the proceeds of investment activity, which means those are not dollars that came directly out of the pockets of local government taxpayers and state taxpayers in Florida.

So we feel very comfortable over a lot of years -- and you'll hear the long-term performance information and the short-term performance information in a moment from EnnisKnupp. But we feel very comfortable that the level of risk that we collectively, "we" meaning the Trustees, the Legislature, the staff of the SBA, the Investment Advisory Council, and most recently the Participant Local Government Advisory Council, the level of risk that we have collectively grown comfortable with over the years we feel is about right, and we have no interest in taking any more risk. No interest in taking any more risk; I want to say that again.

And so the purpose of our exercise with the asset/liability study and the revisitation of our investment strategy is very simply to look at how

we take the risk we are taking and answer a couple of questions: Can we take the same or less risk and get a greater return? And if we can do that, what is the mix of investments that would best position us to do that? So that's the real end game here, is that if we can invest more smartly, taking ideally less risk, and make the same or more money, that's a better bet than I think any of us would take as individuals and in the aggregate that makes sense for a pension fund.

The other thing I wanted to touch on is the notion of risk itself. As individuals, people tend to think in terms of risk as being reflected by volatility and perhaps liquidity. Things that go up and down violently in value or things that periodically can't be sold make us nervous, and we perceive them as risky.

With a long-term oriented investment institution, one's view of risk is somewhat different. The real risk that we worry about in managing a pension fund is the risk that when our long-term liabilities come due, we don't have the assets to pay those liabilities.

That has never happened. There has never been a late benefit payment of any kind in the Florida

Retirement System, and there won't be as far as I'm aware.

So the real risk for us, the real issue for us is, how do you compound money at a sufficient rate over a long period of time that you minimize the risk that matters, you minimize the risk that when the benefit payments come due, you don't have the assets to pay them? And the answer is, you take only those risks which you are most appropriately compensated for taking.

And ultimately what that will mean, somewhat counterintuitively, is that by holding some investments in a diversified portfolio that may be a bit more volatile, may be a bit less liquid from time to time, that greatly reduces the risk that really matters, which is the risk that you don't have enough money over the long term.

So I just wanted to sort of re-establish that context of what our fundamental policy mission is here today and how to perhaps think about risk. So that basically is what we're going to be doing.

Just to give you the usual opener on where we are, the Florida Retirement System as of last night's close is about $109 1/2 billion. That's down a bit from where we were. As you know, the

month of May was the worst May in financial markets in decades. That's the bad news.

The good news is, fiscal year-to-date, we're still up 14 percent, and we're still 250 basis points ahead of target. So I would have to say things are working. And if you look at the year-to-date numbers, we're down just about 2 percent year-to-date. But to put that in perspective, the Dow and the S&P 500 are both down just under 6 percent, not 2 percent.

So I think protecting capital in down times is helpful. Obviously, a dollar not lost is as good as a dollar made. So that's where we are.

Why don't we, unless you have any questions on the prefacing marks, move on into the performance, if that suits your pleasure, and why don't we have Mike Sebastian from EnnisKnupp come up and go into our performance reports.

MR. SEBASTIAN: Thank you very much. I would like to give, just in the interest of time, a relatively brief update on the performance of the defined benefit plan, defined contribution plan, the Florida PRIME, and also the Hurricane Catastrophe Fund.

Just to start with a background on major

market returns, over the past one year, this represents the performance of the major asset classes in which the FRS has invested over the period. The lines represent performance over the one year.

And the way that you can interpret it is the growth of a dollar, so investing $1 one year ago would have resulted in $1.64 in wealth invested in foreign equities over the 12-month period. Foreign equities were the strongest performer over that period, followed closely by domestic equities, but fixed income also turned in respectable performance, earning $1.08 for every dollar invested. And since these are the major asset classes in which the FRS is invested, this strong market rebound explains a lot of the good, positive absolute performance of the fund over this period.

The fund's assets, I have numbers just as of March 31st. You heard some more updated ones from Ash, but as of March 31st, the fund, the FRS was $116.7 billion, and that represented a $3.2 billion increase over the calendar quarter period.

Within that 116 billion, there are allocations to various asset classes, U.S. stock, non-U.S. stock, fixed income, and so on. And we closely

track those allocations relative to the long-term investment policy targets, and each one of those asset allocations were within the allowable ranges around the targets. They were very close to the targets, indicating a strong measure of risk control relative to the long-term policy.

This summarizes performance of the FRS relative to a few different measures. The green bars represent the total return of the FRS over the quarter, one-, three-, five-, and ten-year periods.

The orange bars represent the returns of the performance benchmark, which is a representation of the fund's investment policy, essentially the returns of the stocks, bonds, alternative investments, and so on, at their long-term policy allocations. And that's just a measure of success at implementation, the returns relative to that particular benchmark.

The second benchmark shown by the blue bars is inflation plus 5 percent, and that's the long-term absolute target rate of return for the plan, and it's designed to allow for the fund to meet its financial objectives over a long period of time, in other words, to ensure benefit payments and to operate the plan at a reasonable level of cost.

Comparing the green bars and the orange bars, we see that the total fund has outperformed the performance benchmark over all periods. That's a sign of successful implementation, strong results of active management, beating its benchmarks, and also low costs relative to similar plans.

And relative to the blue bars, that is again a long-term rate of return, and we expect the fund to achieve or exceed that target rate of return during normal markets. That's why the asset allocation -- that's what the asset allocation is designed to do.

When markets are especially volatile, we might expect to see shorter term performance that's greater or lower than the long-term target rate of return just because the fund is invested in markets that move up and down, whereas the target rate of return is a flat 5 percent plus inflation.

We've seen very strong outperformance of the fund relative to the target rate of return over the shorter time periods, but over the medium to slightly longer periods, five and ten, we've seen the fund lag the target rate of return.

But again, the proper comparison there is over the very long term. And if you do so, you see over here the blue bars are the fund's total

performance, and the gray bars represent the long-term target rate of return, the inflation plus 5 percent. And as you can see, over the 15- and 20-year periods, the fund has handily outperformed its target rate of return, indicating a well designed asset allocation policy and also successful implementation of that policy.

CFO SINK: Can I just ask a quick question, though?

MR. SEBASTIAN: Sure.

CFO SINK: I mean, obviously, if you just look at this ten-year -- the ten-year number, it's not a very pretty picture. So would that lead you to conclude that we need to have some much better years going forward over the course of the next five- to ten-year horizon? Otherwise, we're going to be in not a good place; right?

MR. SEBASTIAN: You know, better years are always helpful, but the fund has a very long-time horizon measured in the decades, which is why we try to de-emphasize even periods as long as ten years, the comparison with that long-term rate of return. That's really sort of a multi-decade horizon, and we believe that not only that has the fund achieved returns that are good over those

horizons relative to their target rate of return, but we also believe it's well positioned both now and with any possible changes in asset allocation policy. We think it's well positioned to achieve those returns over the long term.

CFO SINK: Okay. Thank you.

MR. SEBASTIAN: This, just briefly, is a measure of the returns relative to the performance benchmark over a period -- essentially a ten-year period starting in March of 2000. And the way to interpret this is that for every dollar that the target rate of return, the benchmark would have returned over this ten-year period, the total FRS, the total pension plan would have earned $1.04. So this is sort of a ratio of wealth over time.

And there's two things to take from this: First, the performance was positive over the period. And $1.04 percent $1 might not sound like much, but when you apply it to 100-plus billion dollars, it adds up to real money in terms of saving plan costs over a long period of time, but also that it's a very steady growth over time. There hasn't been great volatility relative to the policy, but rather a long-term, year-to-year achieving of greater return than what would be

provided by the policy, so, in other words, a successful implementation.

Another thing that's helpful to look at is peer comparisons both in terms of investment policy and investment returns over time. And this is a comparison of -- these pie charts, the one on the left represents the FRS's current investment policy to the various asset classes, and to the right -- I apologize for the abbreviation there, TUCS, Trust Universe Comparison System. What that is is a measure of the top ten, in terms of asset size, defined benefit plans in the United States, both corporate and public, so your largest peers. So we wanted a comparison of asset allocation relative to that over plans of similar size.

That right-hand pie chart makes up in total $1 trillion in pension assets. And the average of those ten funds' size is about $100 billion, so very comparable in size to the FRS portfolio.

And the takeaways from there are, the FRS has a lower -- I'm sorry, a greater than peers allocation to domestic equities. That's the 38.7 percent versus the 26.8 percent. It has a slightly lower allocation to foreign equities, the 19.9 versus 20.7, and a lower allocation to

alternatives, in general alternative investments relative to peers.

Now, alternatives for the FRS would be the sum of strategic investments, real estate, and private equity. And for the peer comparison on the right, it would be real estate and alternatives, where alternatives consist of private equity, hedge funds, and other investments.

In terms of the performance comparison with peers, here the green bars show the FRS returns and the orange bars show the median return of that top ten group in terms of assets that I just mentioned.

I guess what I would say is that, first of all, these results are shown gross of fees, so were you to show them net of fees, the FRS's results would look even better relative to peers, because you operate at a lower cost than most of your peers. You operate in a very efficient manner. Over shorter time periods, performance has been like that of peers. Over longer periods, it can be above or below similar fund returns, and that's going to be driven by differences in asset allocation. And probably over the long term, a driver of the moderate underperformance of the top ten peers would be driven by a lower than peer

allocation to alternative investments and also to foreign equities.

Those are the comments I have on the DB plan. If there's questions, I would love to take them. Otherwise, I'll move on to the additional funds.

This is a performance summary of the investment plan, the defined contribution plan. You see here you have the investment plan's returns in the top line in bold relative to a number of performance comparisons; directly below it, the return of the average DC plan; and below that, returns relative to the total plan aggregate benchmark.

Now, one thing I'll note, you see the 28.2 percent for the one-year period for your DC plan relative to the 39.3 percent for the average DC plan? That's largely driven by the average DC plan's allocation to company stock. The average DC plan has a 27 percent allocation to company stock. And, of course, the FRS does not issue stock, so that has been a driver of performance, essentially making the average DC plan more riskier, a greater allocation to equities than your DC plan. But over the longer term, the five-year period, we see the FRS investment plan has outperformed the average

plan.

We also see, for example, the 28.2 versus the 27.0. The investment plan has outperformed its individual aggregate benchmark over every period. And that benchmark is simply the weighted average of the investment options in the plan at their benchmark returns, so it's essentially a measure of success of those options in delivering returns over the benchmarks they're measured against.

Costs are very important in any kind of plan, including this DC plan. We see at the top expense ratio of the FRS versus the peer corporate DC plan. We see some footnotes here that the custom peer group shown in the top panel is 20 DC plans with assets between 2.1 and 7.1 billion, so very large plans similar to this plan size. And we see that the FRS operates at a lower cost than peers, 24 basis points versus 30.

It's also helpful to compare that 24 basis points with other types of plans. We have information on defined benefit plan investment management fees for corporate funds and public funds, and that's in the lower table. And those fees are 44 basis points and 39, so again, materially higher than the level of cost at which

you operate. And we believe that's a very sound practice in delivering good returns for the participants over time.

We can look at similar comparisons for each type of investment plan option, so going down the leftmost column, we see the different types of investments that are offered in the DC plan, large cap equities, mid cap equities, and so on, and then the fee for the FRS DC plan for that option, and then the average mutual fund fee. That's a good representation of what an alternative might be to those options. And in each case, the FRS fees are substantially lower than the average mutual fund fee.

Just very briefly, this is growth in the plan assets over time. Starting with fiscal year '02-'03 and ending in the most recent period, we see steady growth in assets over time, with one hiccup in fiscal year '08-'09. That was simply the result of market events. We can see on the next slide that the number of participants in the plan has continued to increase steadily over time, so the plan continues to grow at a good pace.

If I might, I'll speak briefly about Florida PRIME and Fund B. Florida PRIME's overall

investment results are shown on the slide that's up on the screen right now, and results relative to the benchmark, which is an average of similar highly rated local government investment pools. The results have been positive over every time period measured.

And this may be skipping ahead to distributions to participants over time from Fund B, the illiquid assets they're slowly liquidating over time as assets become available. I'll point out that at the bottom line, there's 77.7 percent, almost 80 percent of assets have been returned to participants over time from Fund B.

And then lastly, the CAT Fund, the Florida Hurricane Catastrophe Fund, you see results here relative to the benchmark.

Over the shorter term period, returns have been very strong relative to the benchmark, reflecting a rebound in some of the securities that are held in that fund that suffered some market mark-downs during the recent market crisis. Those have come back very nicely, causing performance to be greater than that of the benchmark over the shorter periods and more benchmark-like over the longer term. And the results are similar, although

there's a shorter time period available for the 2007 A Fund, representing the results of the note that was issued.

And that concludes my remarks. Thank you.

MR. WILLIAMS: Thank you, Mike.

We'll go ahead and get into the standing reports now. And I wanted to also take a minute and thank and recognize, as always, the members of our Audit Committee, our IAC, and the PLGAC. We have, of course, Mr. Sweeney with us, and we also have Dan Wolfson, Patsy Heffner, John Hill, and Rob Gidel with us from the advisory groups.

Bill?

MR. SWEENEY: Our first item is the continuing education we've talked about several past meetings, and the Board has made great strides. We have a new employee who is going to be specifically dedicated to a program to develop a program for continuing education for the employees of the SBA.

I think the Trustees are well aware that we have obligation not only to have competent employees, but to make sure that that competence is maintained over time. So this is the first time we're going to have a formal program of continuing education, and we will have reports quarterly from

Cindy Stiff, who is the new director of continuing education, and we will forward those on to you.

The second item is just a report that we have Ernst & Young under contract to do the first independent audit of both DC plans, and we're expecting that they will be working this month with the Board to discuss the creation of a financial statement. Well, they don't -- they just advise on the financial statement, but the Board employees will be creating the financial statement which they will audit. And so we look forward to having the first independent audit of both plans this fall.

The audit recommendations, this is something that we have been struggling with, and we have a list, and your Audit Committee tries diligently to go through all this every monthly meeting. And we're happy to report that when we started this rather concentrated effort a year ago in January, we had 218 recommendations.

Recommendations are developed by internal and external auditors and the Auditor General. These recommendations are then implemented by the Board and then audited and confirmed that they have been implemented, and they do not go off the sheet until they are implemented, confirmed implemented.

So within a year and now six months, by the end of this current month, we will have -- 86 percent of the recommendations will have been implemented, and I for one will be happy to see this list go to much smaller.

The final thing on the agenda is -- I think it was my mistake in talking to staff about how to -- what we wanted to do is, we have a new statute that creates the Audit Committee, and so what we wanted to do is just make sure that the existing Audit Committee would remain in effect until the new members and the Trustees are briefed about the new law and you appoint the new members. So I guess I would ask for a motion that we would just be continued until the new board is appointed, or new committee is appointed.

CFO SINK: All right. I so move.

ATTORNEY GENERAL McCOLLUM: Second.

GOVERNOR CRIST: Moved and seconded. Show it approved without objection.

MR. SWEENEY: Thank you very much.

CFO SINK: Bill, let me just make a comment that this really is historic. I know you worked hard to choose the independent auditor, and this is going to give the Trustees a lot more -- you know,

even more comfort to have an independent, well-respected, worldwide-known auditing firm looking at the books of the SBA, and it gives protection to all of our employees as well.

But this, Ash, compliments to you. I know what you inherited when you came in here with this extensive 218 different audit recommendations. How in the world it got that point -- it shouldn't have. We all know that. But to have gotten it down by 86 percent is really phenomenal. And it takes a lot of work, and it's very, very tedious.

So please give my kudos to the audit staff, the internal audit staff, but also, Ash, to all the people, the professionals who had to take away from what they were doing to look out for the nitty-gritty. Thanks.

MR. SWEENEY: Thank you very much.

MR. WILLIAMS: Thank you, Bill.

Patsy Heffner, chairman of the PLGAC, chairperson of the PLGAC.

MS. HEFFNER: Good afternoon, Trustees. Since the prior meeting of the Trustees, the Participant Local Government Advisory Council has met twice, once on March the 17th, and then again yesterday. Our next quarterly meeting will be September the

22nd in Osceola County.

We have continued to work on several issues designed to improve the operations, client service, and the investment management of the pool. In addition, council members have maintained a continued dialogue with the SBA staff on matters related to Florida PRIME and Fund B.

Most recently, over the quarter ending March of 2010, participant deposits totaled 2.3 billion. Participant withdrawals totaled 3 billion, for a net decrease of approximately 743 million. Marginal net outflows are normal for this time of year and are in line with the pool's historical cash flow.

We've completed the annual best practice review for 2010 covering the various aspects of Florida PRIME's management and operations. The review included discussions with SBA staff involved in the administration of the pool, an on-site visit to Federated's offices, and discussions with Florida PRIME peers. As part of this report, a full review of Federated's full service model was conducted covering the level and types of service delivered to PRIME participants.

The SBA is currently implementing several new

elements of the SEC's reforms to Rule 2a-7 affecting the investment practices of money market funds. Although not a registered fund with the SEC, the Florida PRIME does operate as a 2a-7-like money market fund. Proposed changes to the PRIME's investment policy include strengthened liquidity requirements and lowered exposure to illiquid securities. Also, BNY Mellon, the pool's custodian, is now calculating a seven-day yield in compliance with the Rule 2a-7 methodology, which will begin to be reported to participants.

A new communications piece, a weekly market commentary, has been added to the Florida PRIME website providing the pool investors with timely coverage of the money market.

For the quarter ended March 2010, Florida PRIME has performed exceptionally well in the current interest rate environment, outperforming its investment benchmark over all time periods. For pool investors, Florida PRIME generated excess returns, performance above the pool's benchmark of 11 basis points over the last 12 months and 15 basis points over the last three years.

In conclusion, I would like to add one final comment. We're seeing the trust and the confidence

steadily returning to the SBA, and I attribute this to two significant actions on your part, the first being the hiring of Ash Williams and the very talented and knowledgeable staff that he has assembled, and the second being the hiring of Federated. Together, we have seen a steady improvement in the confidence of the investors, and we thank you for those actions.

ATTORNEY GENERAL McCOLLUM: If I could, Patsy, first of all, Governor, I would like to thank you for your service. You're putting in a lot of time, so you can thank Ash and the rest of the team, but we thank you.

Also, when you say you're seeing an improvement in the confidence, are we seeing more local governments come back in in the last quarter or so?

MS. HEFFNER: Yes, we are. Yes, we are.

CFO SINK: Good, good. Thank you.

MS. HEFFNER: Thank you.

COMMISSIONER BRONSON: Thank you, Madam Chair. And to your point, General, about thanking again our advisory council members, the advisory councils were in session yesterday from 8:30 in the morning until 5:00 p.m., pretty much nonstop. We had a

lunch break, but people ended up having lunch together, not doing business, of course, but nonetheless spending time together.

Next we have the report from the Investment Advisory Council, Chairman John Hill.

MR. HILL: Thank you, Ash. Good afternoon. The IAC met yesterday with the executive director and CIO, Mr. Ash Williams, and his leadership team at the SBA for our Q2 update, so this is the first meeting since the last report.

The SBA and their advisors reported to us on several fronts, including the fiscal year and calendar year financial performance of the fund, which we've just overviewed, the fiscal year 2010 and 2011, the upcoming fiscal year budget for the SBA, a private equity market and Florida Growth Fund update with the assistance of outside advisor Hamilton Lane, and revised asset allocation plans with the assistance of EnnisKnupp.

Some of these subjects have been presented today, and I believe that Ash and his team of advisors are going to provide the details in connection with the specific subject matters. However, I would like to just summarize very briefly what was reported to the IAC and the IAC's

perspective where applicable.

So I'm pleased to report on behalf of the IAC that the financial performance of all the funds has been strong and ahead of benchmark targets. In particular, if you look at the last 12 months for the fiscal year ending coming up in June, the fund is more than 200 basis points ahead of benchmark, which on a fund north of $100 billion is more than $2 billion in incremental value add that the SBA through the management of the fund has been able to accomplish. The IAC congratulated Ash and his team for this outstanding financial performance, particularly during the more turbulent and volatile financial markets over the past year.

The SBA team provided the IAC an overview of their intended budget for this next fiscal year. The budget includes new expenses associated with numerous new policies and procedures which have been put in place surrounding investment controls and transparencies and risk management.

Additionally, the CIO expressed to the IAC his long-term concern over the need to invest more in human capital or risk losing key people over time, particularly as the capital markets improve. So I just would note to the Trustees that that's

something for you to take into consideration over time.

The IAC made and approved a motion to show their support of the SBA fiscal year 2010-11 budget as it was outlined to us.

At the meeting yesterday, Hamilton Lane reported to the IAC on the state of the private equity market and their belief that solid returns will be made to this investment category over the foreseeable future. They also presented an update on the $250 million Florida Growth Fund, which has been very active and is off to a good start with three investments in private equity funds focused on Florida and four direct investments into Florida companies, so seven total investments in the last basically year.

Finally, there was a large amount of time and discussion at our IAC meeting in connection with the desire of the CIO and his team at the SBA to implement a change in the asset allocation of the pension fund. Despite the strong financial performance over the last year of the fund, Ash and his team, to their credit, have sought to be proactive in continuing to research ways to improve results relative to risk.

In conjunction with outside advisors EnnisKnupp, the SBA has developed a revised asset allocation model and investment strategy that they believe could earn higher returns with lower risk. The change in asset mix that was proposed to the IAC is estimated to result in more than $2 billion in net present value savings or additional return in addition under a somewhat lower risk-adjusted profile.

The principal changes, which are going to be described to you subsequent to my report, include an increase in strategic investments, to include infrastructure as a category, debt funds, and certain low-risk hedge funds, and a change in equities to a more global perspective, effectively combining the foreign and U.S. investment groups, with an offsetting reduction in fixed income and high yield exposure. The IAC approved a motion in support of this proposed new asset allocation policy.

This concludes the IAC report for the Trustees. Thank you.

CFO SINK: John, let -- I'm just sitting here thinking about your reference to the Florida Growth Fund, and I know we're going to have a presentation

later on from the people who are -- from the Hamilton Lane people.

But sometimes as I go out and about, various business people will comment to me that they wish Florida was doing more, or that we were making our investments different. And I know, Ash, there was a lot of talk around how early in early stage we would be as a pension fund in terms of an investor in this kind of fund.

What's your perspective, or could you share with me the perspective or the conversation with the members of the IAC around the approach that we've chosen to take with the Hamilton Lane relationship and the way we're implementing the growth fund?

MR. HILL: Okay. I'll give you both my perspective as chairman of the IAC and then my perspective being very active in the capital markets in Florida.

I think overall, the IAC is very pleased with Hamilton Lane and their management of the $250 million fund. And they're going to summarize today the activity level, but they've been very active. They've been very well received in the investment community, so I think the perception is very

positive.

You know, myself as a former chairman of the Florida Venture Forum and very active again in the private capital markets in Florida, my perception is that it's off to a very good start. And this is incremental capital that's coming into our market that we wouldn't see otherwise.

We still have a problem that we're fairly undercapitalized in Florida, particularly in connection with early stage capital. So this helps, but doesn't sufficiently solve that problem, but it's at less something better than we had before.

CFO SINK: Well, do you think that it's -- do you think that the Retirement System ought to be looking at a -- you know, a real true early stage component? Because that's the complaint I hear as I go around, that there's just not a lot of early stage capital available here in Florida.

MR. HILL: Right. I mean, I think that's initially addressed through Hamilton Lane, that they are investing in early stage. The question for the fund and the fund managers is, you know, what's the prudent level of exposure to early stage capital for one category, which has historically

been an underperforming category? I mean, if you look at venture overall, it's just not -- the returns have been very poor in venture over the past ten years. You know, when you're getting judged on returns, plus you have fiduciary responsibility, I think people are hesitant to put more money in venture. It's just -- that's not just here in Florida. That's everywhere.

On the other hand, I think Hamilton Lane will say that they think that -- you know, overall, they're very bullish on private equity, including maybe venture is starting to show better returns. So I think what we've done right now is a good start.

And again, from an IAC point of view, people are very supportive. I think you have to be cautious in regards to the pension fund and, you know, how much you do. I think you probably -- you know, I think what they've done is very thoughtful, and it's off to -- it's a good start, and maybe over time you could increase the allocation as you have some successes.

CFO SINK: Can I follow up with that? I think the CFO has made good points. When I first got started in looking at the Florida Growth Fund and

we all saw it develop, I was certainly one who had hoped and anticipated there would be more truly early venture capital investment.

John, do you think that based on the risk factors, the way we're going with this, that from the State's perspective and the demand of growth in our state, that we need perhaps another vehicle outside the pension funds that the State uses to leverage more activity for these small startup companies and for the early stage venture capital? Because it doesn't appear to me that even though Hamilton Lane may tell us later -- I'm sure they will -- that they're going to do a little of this, it doesn't look like we're going to do enough to meet what the CFO and I see out there every day, and the Governor I'm sure has too, as the needs of Florida in this respect, at least it doesn't look like it.

What are your senses? I realize I've asked you to wear a hat a little more broad than simply the advisory chair, but you're in this business, so what do you think?

MR. HILL: I think if you could separate it from the pension fund so it wasn't a situation where you're concerned, as Ash pointed out at the

beginning of the meeting, about overall making sure you have enough money to meet your obligations over the long term for the pensionees, if you could figure out how to fund it, you know, there would be a great need for that, separate from the fund, because if you look at, you know, the major money centers, look at the Boston, the greater Boston market and New York and California and Chicago -- even Washington, D.C., has a lot of venture capital, but there's just not that much down here.

And so for a state relative to our size -- I mean, I've been here for 20 years, and we've always been very much undercapitalized, particularly when it comes to venture. And I think that sometimes -- I mean, the last couple of years, the economy has been slower, so there have been less startup companies.

But as the economy is starting to tick up again and the tide is rising, now is when it really would be great to have capital to put to work to help these emerging businesses get financed so that they can really grow and become big businesses and big employers. Again, I mean, the challenge that you have as a group is, how do you fund it.

ATTORNEY GENERAL McCOLLUM: Of course. I

realize that. And I just wanted to get your perspective, and you gave it, and you were very honest and straightforward about it, and I appreciate it. Thank you for what you do.

MR. HILL: Thank you very much.

CFO SINK: Ash, could I ask you a question about something that John brought up that you all might have -- you obviously discussed, but this triggered something in my mind. I know we're talking about budget later.

We've been in -- in terms of people, our people resources, obviously, we have the fourth largest public pension fund in the country, and we're sitting here in Tallahassee, and when the market was really hot, it was hard for us to attract people at a level of compensation commensurate with what was being paid in Wall Street. And I know we've probably benefited from that because of the downturn in the market for the last three or four years.

But can you just share with us what you're thinking or seeing? Are you beginning to see some beginning pressures again over the next two- to four-year horizon? Are we going to kind of need to rethink our retention strategy and recruitment --

ability to recruit strategy again, and maybe this time we can get ahead of it instead of get way, way, way behind the curve like we were five years ago?

MR. WILLIAMS: Yes. The longer answer to your question is, we did successfully recruit several folks from the private sector during the downturn. We took advantage of the strategic recruitment and reserve dollars that you thoughtfully included in the budget in fiscal '08-'09 at General Milligan's request, and we put half of that amount in the '09-'10 budget last year. We have used some of those dollars to fill some key positions above the comp levels that were already there, but still at very attractive rates that reflected the depressed nature of the hiring market over the past couple of years.

What we're seeing now is that as the capital markets strengthen, people knocking on the doors of our key talent, the frequency of those knocks is going up. And there are several ways we get a sense of those things. Obviously, there are disclosures. For that reason, we don't have any conflicts. And I just think we're going to need to do something about this on a more systematic basis.

We have done an analysis since I've been back using an outside -- two different outside commercial compensation consultants, one specializing in the investment services area, the other just knowledgeable of the immediate physical environs of Tallahassee.

We don't really see Wall Street as the right comparator for us. Even comparing ourselves to other major public pension plans, we're pretty far back in the pack. And I think what we're going to need to do over time is revisit our compensation structure.

And in the meantime, I'm working to identify, and have in fact identified, working with our top management team, a number of individuals that we feel are at very real risk of being picked off who are critical resources. And I can take action on my own authority within the resources you've already provided to harden those targets and will do so.

Again, we'll hit this in the budget, but we see protecting those high-risk people as the most support priority right now, and for that reason, we are not asking in the budget this year to have any sort of across-the-board pay raises or to implement

the incentive comp program, because our thinking is the more important priority is let's focus the resources we've got during an extraordinarily difficult period for governmental economics where they'll do the most good, which is protecting key people that if we lost them tomorrow, replacing them would really be a problem, because we want to maintain an orderly organization.

Unless there are other questions or comments on that subject, which there are not, let's move on to the legal report from the General Counsel, Maureen Hazen.

MS. HAZEN: Good afternoon. For my standing report today, the first topic I was going to provide an update on was securities litigation. Since our last quarterly meeting, the SBA has gone ahead and finalized all of the master agreements with the five firms that were selected by the evaluation team during our securities litigation counsel search. I think at the last meeting, we had finalized two out of the five, so now we have all of them finalized, and we are starting to actively use their services.

Just a couple of sort of high policy, high level policy observations that I've made over the

last couple of months since I've started working with these firms.

The first is, I see a real benefit to the real-time analysis that we've been able to obtain in working with these firms. As cases are filed or potential claims are identified, we've been able to contact the firms, or the firms would contact us and give us real-time information about those cases so that we could evaluate our losses and our exposure and keep on top of that. So that's one observation that I've made thus far that I find has been a real benefit to the SBA.

The second observation I would say is that case evaluation is really important. As we discussed at the last meeting, it's in the best interests of the SBA to be very selective about the cases it chooses to actively litigate, and so case evaluation becomes very important.

And given the challenges, the legal complexities of issues involving loss causation and damages, it's really much more of an art rather than a science, and I think that begs the question about what is the proper way to evaluate a case.

And my view on this is really to go out and ask all the firms, to the extent they're interested

and not conflicted, to provide an analysis, and then to flesh out ahead of time and have a dialogue with the firms early rather than later to really understand the case ahead of time before choosing whether or not to file a case. And so that's how I plan to handle it over the next year and have started to do that already.

And then the third sort of observation I would make is that after we got these agreements in place, I went back and reviewed cases that have been filed over the last couple of years to determine whether any were possible candidates for an evaluation. I did identify a couple of cases that I thought were potentially good opt-out cases, and I'm currently having those either analyzed or will be having those analyzed. And just as a caveat, I can't say that I would recommend them or not recommend them, but we are looking at them, and it's a little bit too premature for me to make a recommendation one way or the other on those.

With regard to specific active cases, just one update related to AIG. I think I had briefed the Trustees at the last meeting that we had an opt-out case that we filed against AIG back in 2005 that for various reasons had a lot of stops and starts

at the class level, but that the class had been certified and that I anticipated that we would see some movement.

Indeed, we have seen a lot of movement. Depositions are scheduled to close, to end this month. And so I anticipate that as we move into the fall and damages reports by experts are prepared, we will either be moving into settlement mode or preparing for trial in that case.

The next area relates to passive cases. We currently are a passive class member in over 300 class actions. During the months of February, March, April, and May -- the May numbers did come in. The SBA collected just over $6.1 million as a passive member of various class actions.

The next topic that I was going to discuss is contracts, which is the bulk of our work, being an investment transactional sort of office. It has been a busy three months. Since March, the SBA has entered into 30 new contracts across all asset classes and departments, including six new investments for the private equity and strategic investment asset class and 57 amendments and 12 terminations. And looking at the pipeline of investments that we have coming, I anticipate that

for the next several months that we'll be busy as well, to the delight of me and my staff, because we really like the investment work.

And then special projects, I'll just mention one, because you're going to hear about other people's reports, but rules and the PRIME compliance report that was done by Ann Longman's firm for Florida PRIME.

But to echo Mr. Sweeney's earlier remarks about training, during this past quarter, we did have an all-day, nuts-and-bolts hedge funds legal training for all lawyers and for the strategic investment portfolio management staff, and it was very well attended also by other SBA staffers, including notably our compliance and risk enterprise management staff. So just to echo his comments, I just wanted to mention that we did do that during the last quarter.

And I would be happy to take any questions.

CFO SINK: Maureen, I know you can't say too much, I guess, but just a mention of the status of the J.P. Morgan conversations for us.

MS. HAZEN: Sure. We continue to have ongoing settlement discussions with respect to the sale of unregistered securities to the Pool, and we

continue to brief all the senior legal staff.

I am very hopeful that we will have a resolution very soon, hopefully something that I can report to you at the next quarterly meeting. I will say that we've had probably more progress in that regard in the last couple of months than we've had probably in the last year. So I'm very hopeful that I'll have something more definitive to report to you next time.

Thank you.

MR. WILLIAMS: Thank you, Maureen. Why don't we move on to the Inspector General's report, Bruce Meeks.

MR. MEEKS: Good afternoon. I'll begin my remarks with a summary of the results of the SBA's investment protection principles compliance process for 2009.

As I have indicated in the past, that process operates retrospectively, so we received the 2009 certifications just last month. All broker-dealers, with the exception of one firm -- that's 13 out of 14, or 93 percent -- have submitted their certifications indicating compliance with the IPPs. One firm, Investment Technology Group, has not submitted a certification

1 despite multiple requests. And I will discuss
2 sanctions, if any, which may be in order for that
3 noncompliant broker with the SBA senior officer for
4 domestic equity. All investment managers, 41 out
5 of 41, indicated compliance with the IPPs
6 applicable to them.
7 Typically when I speak with you about the
8 investment protection principles, the discourse
9 occurs at a relatively high level, but today I
10 would like to take just a moment and give you just
11 a couple of examples of protection principles that
12 our managers certify to in this process.
13 One, where the investment manager has client
14 relationships where it could invest SBA assets in
15 the securities of those other clients, they must
16 affirm that the SBA assets were managed in the best
17 interests of the SBA and the investment decisions
18 were not made in a manner to advantage other
19 clients to the detriment of the SBA.
20 A second one, the SBA, or the investment
21 manager, excuse me, has adopted safeguards to
22 ensure that the client relationships with any
23 affiliate company do not influence the investment
24 decision the money management firm makes on behalf
25 of the SBA.

And a third, the investment manager is conscious of the investment-related risks and opportunities associated with climate change, and consideration, as appropriate, of an issue or stance and practices related to climate changes is assessed, evaluated, and factored into the investment decision-making process.

The IPP certification submitted must be signed by the investment manager's chief executive officer, senior officer, or partner, that is, someone with the legal authority to bind the firm to the representations made therein.

Next I would like to apprise you of a planned change to be made to the SBA's personal investment activity policy precipitated by a recent question of first impression, that is, whether our policy permits warrants to be traded in the personal portfolios of employees.

Warrants are derivative instruments similar to call options that allow the holder of a warrant to convert it into a share of stock of the issuing company at a prespecified price. At the time that the question was raised, our personal investment activity policy was silent on the issue, but it did specifically prohibit trading of options on

individual securities such as stocks and bonds.

After considerable research and analysis by my office and staff of risk management and compliance, we ultimately recommended making the policy more restrictive by not allowing the personal trading of any derivative instruments, including warrants, on individual securities. It was a consensus opinion of the group that a ban on personal derivatives trading, while protecting the SBA, would not unduly impair the ability of employees to participate in capital markets. The personal investment activity policy will be amended accordingly to reflect this change.

For a while now, I guess about maybe 18 months, I have been searching for an Internet-based fraud training course. And although we have conducted more traditional classroom type fraud training and awareness in the past, in recent years, we've found Web-based, at-your-computer type training to be efficient, economical, and convenient.

With the assistance of the SBA training and development manager, whom Mr. Sweeney referred to, I have found and tested an excellent course offered by a company called SkillSoft. The course covers a

variety of topics, such as definitions of fraud, types of fraud, fraud risk factors, and employee responsibilities for prevention and reporting. I believe strongly that this course will be an important addition to our training program.

Finally, as you may recall, last year we expanded the SBA fraud hotline to be able to receive tips and complaints from external vendors and service providers as well as employees. At a previous meeting, I informed you of a first wave of 191 letters sent to the managers, brokers, and investment consultants for all asset classes soliciting their help in our efforts to prevent and detect fraud, theft, and financial misconduct. Last month we sent a second wave of approximately 200 letters to the other venders of the SBA, including the vendors of Bond Finance and the Florida Prepaid College Program. This.

Process of noticing and soliciting service providers and external vendors in the fight against fraud will be repeated annually.

And I'll take any questions that you might have at this time.

ATTORNEY GENERAL McCOLLUM: I just want to comment that there's no agency of government, I

think, that has more reliance and importance on an inspector general's office than yours, than the SBA, for obvious reasons, huge amounts of money, the confidence of many people whose retirement is affected by it.

And in the times you've presented, and you've presented several times before us, I've been impressed with your thoroughness, your dedication, your obvious on-top-of-it attitude, and I for one want to compliment you on that. I'm sure you get those around from time to time, but oftentimes inspectors general don't get those compliments, but you did fine. You're doing fine. Thank you.

MR. MEEKS: Thank you, General. I appreciate that.

CFO SINK: Ditto, ditto.

GOVERNOR CRIST: Ditto.

MR. WILLIAMS: Okay. With that tough act to follow, Mr. McCauley, corporate governance.

MR. McCAULEY: Good afternoon. I've been instructed to be as brief as I can, so I'll try to go through these, but feel free to stop and ask a question.

Since the last Trustees meeting, we haven't really seen any significant regulatory reform

proposed by the SEC. We do expect them to come out with some final rule or proposal on proxy access sometime later in the summer, most likely after the Congressional financial regulation package is completed. And they also have kind of a -- "proxy plumbing" is what it has been dubbed, where it's a proxy voting mechanics proposal, a concept release that will likely come out either later this month or sometime in July, and we plan on commenting on that.

The SBA's Corporate Governance and Proxy Voting Oversight Group, which meets at least quarterly, has met once in late April, reviewing kind of day-to-day policies and procedures. And then you'll recall from the last Trustees meeting, where I reviewed the single resolution THAT we had proposed at Hospitality Properties Trust, HPT, that proposal, although it didn't legally pass, fortunately it DID garner very, very healthy support levels from a broad range of other institutional investors, notably the largest investors of HPT, like Vanguard and BlackRock, the top 15 institutional investors.

And we look forward to continuing to have a dialogue with the company, plan to do that and

hopefully will move the ball down the field on that one. But it didn't legally pass, unfortunately.

The next slide covers some of the major key voting issues that we've seen so far in the 2010 proxy season. Just a reminder, proxy season is April, May, and June. We do make votes throughout the year, but about 75 percent of the votes occur in April, May, and June.

Probably the most notable on the list is the first disapproval of a management proposal along the lines of "say on pay." Many companies have adopted or received proposals to put a "say on pay" or advisory proposal on their ballots for investors to opine on the broad compensation framework at a company.

Up in the early May, no single U.S. company had ever received a less than 50 percent support level. Motorola has that distinction. It was followed closely by Occidental and Key Corp. All three of those the SBA voted against for various reasons, but broadly speaking, the pay for performance linkage at each of those companies was less than what we thought it should have been.

Massey Energy was -- a "Just Vote No" campaign was at that energy company. That was related to

the mining accident earlier in the year. We withheld support for three directors who did receive at least 50 percent majority support levels, but they were very, very marginal, just over 50 percent, which is highly unusual in board elections, and then a couple of key majority voting items which we both supported as well.

And then the last slide just covers summary statistics. These are all in line with kind of year over year statistics. These cover the key voting items in terms of directors and auditors and votes with management, all in line with prior historical voting patterns.

And we'll disclose more detail in the annual report that will be issued probably late fall, so you'll see more detail and more comprehensive coverage of additional voting items later in the year.

That's all I have unless you have any questions.

CFO SINK: I've got a couple. Was there any one vote that was taken this year that was the big, made the headlines --

MR. McCAULEY: Massey Energy was probably the closest thing to a high profile vote, but there

really hasn't been any truly significant votes. As is the case every year --

CFO SINK: And you say those three directors were re-elected, but by a very small margin?

MR. McCAULEY: Yes. They were all re-elected. They all had 55 to 57 percent of the vote.

CFO SINK: That's really bad.

MR. McCAULEY: Which is really bad. You have to keep in mind, out of the last two years or so, there have only been about 100, 150 directors that have received less than 50 percent out thousands of individual directors serving on boards. It's very, very uncommon for that to happen. So it's a signal from the investor base that there's not a lot of confidence, given the history of that company.

MR. WILLIAMS: Thank you, Mike. Why don't we move on and take a report -- this will be a new report for the routine reports -- from the risk management and compliance officer, Eric Nelson.

MR. NELSON: Good afternoon. I would like to start with, the primary focus of my unit over the last several months has been developing the compliance program in accordance with the framework and recommendations set forth by Deloitte Touche in their compliance program review of the SBA.

Staffing efforts are now complete. Staff are being trained. We've created several databases. We've got a database of policy requirements that will allow us to monitor frequency, due dates, assigned persons, assigned tasks, that sort of thing.

We've also created a database to record all our compliance exceptions that are detected. That will provide a centralized repository of compliance violations across all asset classes.

We are on track to finalize an independent real estate asset class compliance program effective the June 30 quarter end, which will also close out an open audit issue, and then we will turn our focus to the private equity and strategic investments asset class compliance programs.

Deloitte, as part of their third and final phase of the compliance program review, evaluated the FRS defined contribution program and presented their final report to management in mid April. I would characterize the report as a very clean bill of health, as there were no significant deficiencies detected. The report and associated recommendations were presented to the Audit Committee in mid April.

A large part of the compliance program we've been working on recently was the external investment manager oversight program. Given that we have over 150 external manager relationships in place, this was an important part in Deloitte's overall recommendations.

We've organized a dedicated, centralized manager oversight group that is going to provide a unified risk-based approach to manager oversight across all asset classes. Formerly, manager oversight might be characterized as somewhat siloed up to this point.

Now, this centralized group will monitor manager codes of ethics, ADVs, SAS 70s, financial statements, disaster recovery plans, compliance manuals, et cetera. And using those evaluations and other criteria, we've constructed a risk-based scoring methodology to determine the appropriate level of surveillance on these managers, ranging from due diligence visits through certifications, additional documentation requests, et cetera.

On the Local Government Investment Pool compliance program, in response to recommendations we had received during the last two financial statement audits performed by the Auditor General,

we've finalized a risk-based compliance monitoring program for the Local Government Investment Pool that is effective May 31 month end. Unofficially, it will be used for April 30.

The risk-based approach we developed was approved by the Investment Oversight Group in March. We obtained some additional enhanced security rating services from BNY Mellon in April and tested those enhanced rating services and implemented and documented the procedures in mid May. We forwarded that documented program to the chief internal auditor, who I believe subsequently forwarded it to the Auditor General.

On the risk management front, we continue to develop a comprehensive enterprise-wide risk management plan. We're still collecting and scrubbing risk assessment and risk response data received from business units and mapping those responses against generally accepted risk principles that have been set forth by various industry working groups to ensure that our risk management practices conform to best practices.

We continue to work on a business case for implementation with the total fund, a holdings-based risk management system. We've

gathered some benchmarking data from public fund peers. We are evaluating the individual risk systems utilized by our internal asset classes, and we're finding the cost-benefit analysis on that.

Training and development you've heard a little bit about. I don't belabor that too much, other than the training and development manager that works with me is developing a curriculum using a bottom-up employee interview approach, and then we will have an overlay with what the organization sees as its needs on the three- to five-year horizon as far as employee development.

We've identified some very cost-effective online training programs that have very robust course offerings covering specialized investment products and skills, and I've assigned a variety of staff to evaluate those training programs.

We've also recently upgraded our learning management system, which serves as both a training delivery tool and a learning management tool. And I know Maureen had mentioned a full day course we had on hedge funds, on the legal aspects, but we also had -- our consultant, Cambridge Associates, presented a half-day training program on their operational due diligence processes, which was also

very well attended. We had 40-plus individuals.

I would like to conclude in saying that Ash and our deputy executive director have been incredibly supportive in the implementation of this compliance program, not just in their words, but in their actions and decisions. They have proactively fostered a culture of compliance throughout the board and involved risk and compliance staff early on and very frequently as issues arise. And I would report to you today that there has been complete, unqualified senior management support and a positive tone at the top, and that is the foundation for an effective compliance program and internal control environment.

And that concludes my remarks.

CFO SINK: Well, similar to the General's comments about the Inspector General, I'll make similar comments about risk management and compliance. We are so glad to have you here. Thank you.

MR. NELSON: Thank you.

MR. WILLIAMS: Thank you, Eric.

Jack Nicholson is off attending to the wedding of his son today, so I will cover the CAT Fund update, and Ann Bert is here if you have any

questions beyond my depth.

Short takeaways on the CAT Fund. We come into this hurricane season with the strongest liquidity position we've ever had, $9 1/2 billion.

Additionally, we have recently reconfirmed the borrowing capacity of the CAT Fund at 16 billion. It would thus take a hurricane loss of something on the order of $17.2 billion to exhaust our cash reserves. And if we compare the combination of those reserves and borrowing capacity to what our potential liabilities are, the maximum statutory capacity for the '10-11 hurricane season is 25.461 billion. We have cash and borrowing capacity of 25.5 billion, meaning that we can handle a single event of up to a 1-in-45-year event, which is a 2.2 percent probability actuarially that we get hit that hard or worse in a single event.

So unless there are questions, that will conclude the standing reports, and we can move on to major projects.

CFO SINK: I have one. You may not know the answer to it, for legitimate purposes, obviously.

But the optional coverage layer, it's a maximum of 8 billion, but I'm recalling that last

year it wasn't all taken down. So do we know yet -- is it still early to know whether or not --

MR. WILLIAMS: I don't think we know yet, but we will shortly. Is that right, Ann?

CFO SINK: Will we know -- what do they have? Until the end of June to --

MS. BERT: They have until the first of June, so we are working on that now. We should have it hopefully next week.

CFO SINK: Okay. Would you just get word -- I mean, we're not meeting for another six weeks, so would you just get word? I'm just curious to know what was actually taken down out of the 8 billion possible. Thank you.

MR. WILLIAMS: Okay. Why don't we then move on to major projects and welcome the CEO of Hamilton Lane, Mario Giannini, to tell us about the Florida Growth Fund.

MR. GIANNINI: Thank you. I have a short presentation that I think you have seen large parts of it already from the prior quarter. Not that much has changed. So as I go through this, what I would like to do, if it is okay, is really deal with this early stage venture question, because it is, frankly, the question that we get the most, and

it is -- I think the program has done very well, but we get the same criticism -- I never like using "criticism." We get the same comment regarding, "Boy, I wish there was more early stage."

And so if I can turn -- sorry. There are two parts to this program, and it is the second part that I think really relates to early stage. The first part is putting out 250 million and making sure you get a good return in technology and in Florida-focused businesses.

The early stage part of this program -- and we knew from the very beginning that that was a big focus in Florida. The difficulty with early stage, you heard some it from the beginning. Early stage, generally in the market, there has been an enormous amount of capital leaving early stage from venture capitalists because the returns have been so bad.

And they've been bad for a number of reasons, one being that the loss ratio in early stage is very high, and everyone expects that. You have 50, 60 percent loss ratios.

The second reason is because the public markets have not been as easy to access, and so the holding periods have been very long.

And so when you look at areas that do early

stage very well, Silicon Valley, Boston, parts of Washington, what you see is that there are a lot of pools of capital for early stage investing. It's not just one. And the reason for that is because the early stage venture capitalists can then diversify their risk out. It's why you see early stage companies with, you know, a firm that can easily put in 5 million, they'll break it up and only do a million and a half so they can diversify their risk.

In Florida, unfortunately, today, there are not enough pools of capital for early stage investors to diversify their risk, so you don't have a lot of general partnerships the way you do in Silicon Valley. You can go get 10 people who will look at your particular company. You simply don't have that in Florida.

And so part of our effort -- and I'll talk a little bit about it -- is that, unfortunately, the early stage part of this almost has to come a little more slowly as we develop partnerships that invest in early stage, diversify risk, and then allow the Florida Growth Fund to come in as one of those investors. It's very difficult from a fiduciary and a return standpoint to put together

50 companies early stage in the Florida Growth Fund today, because you will literally be the only investor in all of those companies. That's an enormous risk profile.

I wish it were different, because the other part of early stage, the characteristic -- and you're getting it, because we get it. The entrepreneurs that have the idea or the company are the most passionate and convinced that it is the greatest thing in the world, and so when they're turned down, it's just unbelievable to them.

And so we know very well that this is something that has to succeed. It has to succeed for this fund to succeed, because we can sit here and do later stage venture, but if there's not a good pool of early stage, there's nothing to feed into this.

So from our perspective, part of our mission is to build this ecosystem around the whole venture capital and private equity community in Florida. It's simply not all there today.

The other factor that is huge in Florida is the exceptional university system. And we've spent a lot of time with the universities. They have an enormous volume of very early stage deals that

literally require 10, 50, $100,000. And so when we've tried to work them, that's not appropriate for this program. It is appropriate to try to use this program to create pockets of capital that will invest in those and then create this ecosystem.

I'm happy to answer your questions in terms of early stage, because I do think it underlies so much of what we're trying to achieve here. But it is not -- as you look at the numbers here, I think to date only about 10 percent, maybe a little bit more, is in early stage. I think that's a reasonable number, but I know out there, that number should be 99 percent as far as some of the people that we talk to.

So I'm happy to go through the rest of presentation, but --

ATTORNEY GENERAL McCOLLUM: Let me ask you a question. It's very interesting what you say. Do we have other states that have any comparable models to the problems we've got?

I know, for example, I was in Nevada not too long ago, and they're a growth state like Florida is, and they've had troubles with the economy. And a couple of the people who are major leaders in the community said, "You know, Florida has one big

advantage over the State of Nevada. You have research universities, and you have the opportunity to spin off companies and grow."

And if we're not able to take advantage of that, then we're no better off, if you will, than Nevada in that sense. I shouldn't say that, because obviously it's great to have the research. But if we've got this research here, we really need to find a way to do this.

So now that you're digging in and you've come and we've set this up, I think I for one would hope that as each quarter you report to us, you work on anything you can recommend that we can do to further that. We wear our hats today as the State Board of Administration, but we also wear other hats in governing in this state. And if there's something else we need to be doing, it would be great if Hamilton Lane could tell us, you know, in your own way what could we do to further develop this capital pool that you say, and obviously we all see needs to be developed.

It just needs to be done. All of us hear ideas, but because you're dealing with it so closely, we respect you a lot, and we would really appreciate it. At least I would, and I'm sure all

the rest of them would.

MR. GIANNINI: I'm happy to do that. So you know, three or four of us were at a couple of meetings with two of your major universities. Part of the goal of the meeting -- and I think one of them will do that -- was to set up a pool of capital that would do nothing but invest in that university's ideas and products, again at a very small level.

But part of our job as part of this was to get capital in and find places for it. So I think part of it -- and the good news on this program is the amount of enthusiasm around this program, the idea of, okay, there is a pool of capital that is here -- it may not be everything that we want it to be for all of our ideas, but it's here, and you begin to build a group of people around it.

The universities, there are a couple here in Florida that are very active in this. And I wouldn't be surprised in the next six months that at least one of them will have a program to invest in the commercialization of the products --

ATTORNEY GENERAL McCOLLUM: And you would anticipate the methodology that they probably would use for that would be to get some of their major

investors that might otherwise be gifting to a chair or something to instead gift to a fund? Is that kind of how you see it?

MR. GIANNINI: That's what I think they will set up. And that way you can invest in a hundred of these ideas. Part of where the Florida Growth Fund comes in, importantly, is, once they then go into a middle or later stage, then it's a much less risky proposition for the Florida Growth Fund to be investing in. You don't have to make as many bets, and you don't have the 60 percent writeoff. So it really is a process of building each of the components. I think we want to act, where we can't provide the capital, as catalysts for bringing the people together, and as I said, maybe providing the later stage investment.

ATTORNEY GENERAL McCOLLUM: Thank you. I think you were about to -- I interrupted you.

MR. GIANNINI: No, no. I ramble, wander. It doesn't -- that's fine.

I won't go through this, because again, you've seen it. You know the Growth Fund is designed to be both direct investing and fund partnership opportunities.

We've been very happy with the deal flow to

date. You can see here on the next page -- I've got different numbers, 66 -- four direct investments, three partnership investments. But importantly, from our perspective, on the left side of the screen, the number of deals that have come in is just remarkable. We've been very surprised at the number that have come in, and the pipeline is very strong.

You see here on the next page, 67, the deals themselves. Where I note, because I think, as I said, it is very difficult for us to do a lot of early stage deals this early in the program. We're looking at a couple that may end up. But on the partnership side, our goal is really to try to get more early stage partnerships, because that will be the separate pools of capital that will provide the diversification element. And if you build it, they will come. If you have the money, they will come. You want these general partners coming here knowing that there's a strong, stable source of capital. And so that is a very fundamental part of the program's objectives.

On page 68, the diversification, not surprising across the state. The partnership side is the one I would focus more on in terms of the

different areas economically. What I'm glad to see here is that there's not an industrial component. It really is more on the venture, on the earlier stage relative to, you know, the mature companies. That's what the program is designed to do, and I think it has done a good job of that to date.

And then this page is really the most important in terms of this discussion, the kind of outreach and things that are not purely investment related. I mean, again, from our perspective, we understand that having meetings where you're trying to get people into the state, having meetings where you're trying to get the universities to work together is as important to the future success of this program's returns as any investment that we're doing, and so that is a huge part of the effort. We have people located in the state, and that's what they spend a huge majority of their time doing.

That's all I have. I'm happy to answer any questions beyond that.

ATTORNEY GENERAL McCOLLUM: Thank you very much.

MR. WILLIAMS: Thank you, Mario. Why don't we then move on into the Florida Retirement System

asset/liability and asset allocation review and bring on Rowland Davis with EnnisKnupp.

MR. DAVIS: Good afternoon. My part today will be pretty simple. It is to first kind of recap where we left off in early March, where we presented to the board the results of what we would refer to as phase 1 of the asset allocation study. Phase 1 is where the focus is on overall portfolio risk, not the details of specific asset class allocations, but overall risk.

So to summarize where we were then, and then hand off the discussion to Mike Sebastian, who will take you through a bit more about phase 2, where we deal with diversification, the potential benefits of diversification, and try and then move into specific policy targets for each individual asset class and a recommended policy.

This chart is one that we presented in March, early March to the board. It is sort of the punch line of all of our analysis on risk and reward for the pension plan. We use a long-term cost metric, so we're looking at 15-year-plus time periods and trying to find the right balance between risk and reward.

Ash opened the comments today indicating that

it's important that the plan has to take some risk to achieve the level of return that keeps costs at reasonable and expected levels, and yet there's risk that comes along, and so you need to constantly keep a close eye on how much risk is appropriate.

Without going into all the details of this, this picture that we presented in March shows a plan where, if you look at incremental changes in risk-reward from your current policy, we found none that improved the results relative to where you were.

So this curve, which is positioned the way it is, what we look at in this graph is, if there are points that plat above the diagonal line, those would be interesting points for us. They would indicate that maybe there's a direction in taking more or less risk.

But in this particular graph, no points platted above the line as we dialed fixed income down or up. Basically that's all we're doing with this chart, is saying if we take more fixed income and take some risk off the table or take less fixed income and move the risk up, how do these results change? And again, we look for points that will

move us to the upper left corner, so above the diagonal. Nothing was there.

At that point, we paused in March and promised to come back to you following the legislative session to confirm that nothing happened to change that perspective. So the next chart just makes that point. There were no major legislative changes in the plan. The only thing that was slightly different from our forecasting involved the next fiscal year, where the funding of the plan will be normal cost only, no amortization payment, and then resuming back to the full funding after that.

We reran the model with that. The curve that we just looked at was the same, basically, negligible changes in the relative risk-reward. So the story on risk and reward remains the same, that you are currently in a good spot.

Now, those curves are not always shaped like that. If you recall, three years ago when we presented a similar curve, there were signals that said we should take some risk off the table, and that was done. The board did approve and move from 22 percent fixed income up to 29 percent fixed income. It turned out to be a good choice, but it

was a very long-term proposition. So now we're comfortable with the overall level of risk measured against the liabilities.

The next phase, phase 2 of the study, is where we try and drill down and look at a little more detail. So the best way I think maybe I can describe this is, that red line that we see here on this chart is basically saying we've got a recipe now for different asset class components that we've got, and as we move up and down the red line, all we're changing is fixed income. You could think in terms of a cooking metaphor, that we've got a recipe, and all we're doing here is seeing how much water we want to add to the stew to have it turn out right.

Now, the next phase, phase 2 is to say, "Okay. We've established that very important parameter. Now let's play with the recipe itself. Let's change maybe the relative proportion of some of these ingredients. Let's maybe add some new spices that we didn't have in before and just see if we can" -- basically, what happens is, if you change the recipe, you can move that red line up or down. We're looking to find ones that might move it up, and in particular, see if we can find points in

that yellow shaded area where we're moving in the proper direction towards the upper left corner of the graph.

So this is sort of a trial and error process. Like a chef, you play with some things and see how it turns out.

In this kind of zoomed in, same kind of sharp zooming in on the center portion here, that yellow shaded area we wanted to explore, all the dots that are shown there are specific portfolio ideas that were explored and measured. And you can see that all of them are above the diagonal. Some we looked at weren't above, but the ones of interest are above the diagonal line, indicating more efficient.

Some of them, however, are to the right-hand side of that up-and-down vertical axis there, which indicates taking more risk, not less risk. So those were not considered too strongly after that, because we did want to stay either at or somewhat below current risk levels.

So the ones that you'll hear about today primarily will be the recommended policy allocations shown by a red dot. The red dot on this graph is slightly to the left of the axis, which means it's got less risk. When you put all

the pieces together and measure it over the long haul, it has less risk.

And specifically what we mean by that is, we you know what the future will be. We make some projections. And what we're saying with that particular recommended portfolio is that in normal times, we would expect somewhat higher returns and better results, meaning lower costs to the taxpayers, but even in the bad times, even if our estimates come in at the low end of the spectrum, that we would have results that are better than what we would be getting under the current policy now, so less risk from an overall financial standpoint.

CFO SINK: Could I just ask you, when you say long-term cost savings of 2.1 billion, does that mean a reduction in employer contributions? Is that what you meant?

MR. DAVIS: This is employer contributions measured over 15 years, but also including any change in the funded status at the end of the fifteenth year.

CFO SINK: Right.

MR. DAVIS: So it really even extends beyond 15 years when you put all that together. But

basically 2.1 billion of cost savings ultimately long-term --

CFO SINK: For the employers.

MR. DAVIS: Fifteen years plus to the taxpayers.

CFO SINK: Okay.

MR. DAVIS: And at a slightly lower level of risk.

The other red dot, I don't think we're going to talk much about it, but what we put together for the IAC presentation yesterday was a somewhat lower risk alternative in case, you know, that became of interest. But the IAC was unanimous in their support of the recommended policy, so that will be our focus for today's presentation.

And I'm going to turn it over to Mike Sebastian, who will cover some of the details of that.

MR. SEBASTIAN: Thank you very much. As Rowland had indicated, our analysis of the asset/liability nature of the plan suggests that the current risk level is about right, suggesting over the long term maintaining that level of risk or even reducing it. We sought to identify ways through broader diversification to improve on the

results that are available from what we see here.

Our goals in this analysis were the following: One, to maintain or to reduce the level of risk in the plan; to increase the level of returns over time; and to reduce the long-term plan costs, again through broader diversification.

The ways that we would achieve that would be through greater diversification in a number of ways, more global diversification, and also into additional alternative asset classes -- as we saw in the earlier performance presentation, relative to your largest peers, the areas in which you are somewhat underweight in terms of allocation are foreign equities and alternative asset classes -- and also to increase the flexibility for the fund to be opportunistic, essentially to get paid efficiently for taking on the appropriate level of risk that's needed to achieve the fund's long-term objectives, which would be essentially the 7.75 percent actuarial assumed rate of return.

And what we came out with were primarily a recommended portfolio. But in between the current policy shown here and the recommended portfolio is what we call the near-term policy. The recommended portfolio contains allocations to alternative asset

1 classes that are above the 10 percent aggregate
2 allocation to private equity, venture capital,
3 distressed debt, and hedge funds that are currently
4 within the legislative authority. So while our
5 best thinking is the recommended portfolio, and
6 that is what was welcomed by the IAC yesterday, the
7 near-term serves as a stopping point in between
8 while the SBA seeks to get expanded legislative
9 authority to increased investments in those areas.
10 And what we see here, you can see the sort of
11 general themes of transition from the current to
12 the recommended policy.
13 One is a reduction in the overall level of
14 equity -- we consider that to be a form of risk
15 reduction; a combination of foreign and domestic
16 equity into one asset class, global equity, because
17 we believe that the distinction between U.S. and
18 non-U.S. companies is becoming eroded as the world
19 becomes more globalized; a greater diversification
20 into foreign equity within the global equity asset
21 class; and an increase in the strategic investments
22 asset class from the current actual allocation of
23 1.8 percent to 11 percent over time. And the
24 purpose of that is to allow for greater
25 flexibility, to give opportunities to your skilled

professional staff and external investment advisors to add value, and also to reduce risk by diversifying more away from traditional asset classes.

CFO SINK: So which ones of these -- you may not know this, but Ash will. Which ones of those on that chart would require specific legislative changes?

MR. SEBASTIAN: The recommended policy.

CFO SINK: Well, we don't have this current -- this is not in legislation now, is it?

MR. WILLIAMS: Let me clarify. The place where you would need an expansion of legislative policy would be to take the alternatives north of the current statutory 10 percent. And the way alternatives are defined, you include, I believe, not only what we currently have in strategic, but also private equity and real estate. So if you --

MR. SIGRIST: No.

MR. WILLIAMS: No? No real estate. Sorry.

CFO SINK: Not real estate, just the private equity and the strategic investments.

MR. WILLIAMS: Right.

CFO SINK: Does that add -- 4 plus 6 is 10. I guess that's -- is that right, Kevin?

MR. SIGRIST: That's correct. The exception is, within strategic currently we have some global equity portfolios. Those wouldn't count against the 10 percent. Private equity, venture capital, distressed debt fund, and hedge funds.

CFO SINK: So we're saying from 10 to 16, and that would have to be a legislative change, just like we did the foreign equity change.

MR. WILLIAMS: Correct. But changes of this nature obviously take long time to implement, and our recommendation would be that we have at least a year to do so.

CFO SINK: Right.

MR. WILLIAMS: Clearly, the way markets move around, you don't want to be hasty one way or the other on these things. And also, a lot of this is opportunistically driven. So our thinking would be, if we approve in principle the direction that is being recommended by EnnisKnupp and the staff and confirmed by the IAC, start down that road, with the understanding that to go all the way to our destination, we'll have to have a legislative embrace, that then positions us to go to work in the interim in preparation for the next legislative session to take this initiative forward.

CFO SINK: Okay.

MR. WILLIAMS: With the clear understanding that there are boundaries in life and we will respect them at all times.

CFO SINK: Because right now -- we're at 5.3 now between private equity and strategic? That's what I'm --

MR. WILLIAMS: Yes.

CFO SINK: 5.3. So within the current legislative framework, we have a lot of maneuvering room. Actually, if it's 10 --

MR. WILLIAMS: Well, we have some head room.

CFO SINK: More or less.

MR. WILLIAMS: Right. And that's why we were comfortable saying why don't we go ahead if we agree on this master plan. It's a long-term plan. Keep in mind, these sorts of adjustments are commonly only done every three to five years.

CFO SINK: Right.

MR. WILLIAMS: The reason we moved out with this one within two hour three years after doing the last one was because the environment we were in, we thought it was the right thing to do.

So the notion with an exercise like the one we've been through over the past several months,

which is expensive and time-consuming, is to take a fairly durable long-term strategy from the exercise, implement it over time, and commit to it, and then move forward.

CFO SINK: Okay. Thanks. That's helpful.

ATTORNEY GENERAL McCOLLUM: Ash, while you're still standing up there, just to put some historical perspective of the last four or five years into this, weren't we somewhat higher than 57.4 percent in equities four or five years ago?

MR. WILLIAMS: Yes. And again, I was not here, so this is all after the fact.

ATTORNEY GENERAL McCOLLUM: I understand.

MR. WILLIAMS: But as I understand it, there was a significant review done in '07, I believe, and risk was taken off the table in the form of reallocating money away from equities.

ATTORNEY GENERAL McCOLLUM: But we were up to 70 percent or more at one point in equities, I think, at one point.

MR. WILLIAMS: It was substantially higher, and a wise action was taken by the Trustees and the IAC.

ATTORNEY GENERAL McCOLLUM: Thank you.

MR. SEBASTIAN: If I might move ahead a bit

just to the results that we hope to achieve from these changes in asset allocation policy, focusing on the middle panel here, which is funded ratio projections over a 15-year period for the current policy, the near-term, and the recommended, the goal here and what we believe can be achieved is to achieve full funding in a prudent manner over this 15-year time period.

You see the rightmost column. The 99 percent in the middle is the expected funded ratio over that period, with no added downside in terms of worst outcomes, the 40 and 71 percent, for example, but with a greater amount of upside in terms of the 131, 186 percent. That's perhaps unlikely, but those are the highest percentile outcomes.

The second goal and what we hope to achieve is to reduce costs over the long term. You see in the top panel, the $2.1 billion in cost savings mentioned by Rowland Davis earlier in the expected scenario for the recommended portfolio, but at the same time a reduction of risk.

The line directly below that is the expected cost savings during bad conditions. That would be the worst 20 percent economic and market outcomes. Even in those bad scenarios, we expect to still

achieve a meaningful $700 million reduction in cost over that time period.

So we believe that this recommended portfolio really adds to the efficiency of an already successful investment policy. And I would like to take any questions.

CFO SINK: Yes. Would you mind going back two slides? I'm sorry. I wanted to ask a few more questions about the strategic -- yeah, you got it.

Tell me what infrastructure means.

MR. SEBASTIAN: Infrastructure is --

CFO SINK: I can make up something that I think it means, but I would rather you tell me what it means.

MR. SEBASTIAN: Sure. Long-term investments in physical, income-producing properties, like airports, toll roads, courthouses, and so on.

CFO SINK: Like if we wanted to buy Alligator Alley, for example, that would be an example of an --

MR. SEBASTIAN: Yes.

CFO SINK: -- infrastructure investment.

Okay. And debt oriented funds, to me, that means taking advantage of the market we're in now and being able to buy some -- you know, some debt

that could really achieve big returns for us, like distressed debt and new sort of thing. Is that --

MR. SEBASTIAN: Yes. That's the sort of investment strategy that's in place in the fund right now. You see they have the current allocation of 1.8 percent, and that's an area in which SBA has been very successful in generating returns and adding value.

CFO SINK: Okay. And are we --

ATTORNEY GENERAL McCOLLUM: Could we --

CFO SINK: Excuse me, General.

ATTORNEY GENERAL McCOLLUM: No, you go ahead.

CFO SINK: And are we assuming we're not interested in timberland at all?

MR. WILLIAMS: No.

CFO SINK: It just didn't meet the --

MR. SEBASTIAN: Just to briefly comment on that, these are -- for lack of a better term, we call them indicative allocations that we used for modeling purposes for this asset class to come out with expected returns and risks. This is meant to be very fluid in the sense it allows the flexibility for staff and advisors to select investment opportunities that can add value.

So while this we believe is a good, efficient

portfolio, the allocations you see here, it may change over time as additional opportunities are identified. Commodities and timberland are two areas that staff has considered in the past and may initiate allocations --

CFO SINK: They would be permitted? They would be permitted if staff decided that's what they wanted to do?

MR. SEBASTIAN: That's right.

CFO SINK: Okay. Thank you. I'm sorry.

ATTORNEY GENERAL McCOLLUM: What I was going to ask is the obvious, what's left here, and those are the hedge funds. Can you differentiate and explain them a bit, what type of structure and risks are involved in those types of hedge funds?

MR. SEBASTIAN: Sure. For each of those hedge fund types, we would expect a return somewhere between that of stocks and of bonds. There would be a very strict due diligence process to make sure that funds are being identified that don't have undue amounts of leverage and that are very transparent in terms of the amount of risk that they take and what's in the portfolios.

Long/short equity hedge funds would be ones that focus on equity securities, but can have not

just a long position, but short positions to add value when they believe that stocks are overvalued.

Absolute return hedge funds can follow a much broader strategy and aren't expected to have a market exposure over time. And part of the attraction of strategic investments that this is a diversifier, and so to the extent that these are skilled, active strategies that don't have exposures to the sort of market forces that drive the stocks and bonds that make up most of the portfolio, this is the way you can allocate to these areas and reduce overall portfolio risk.

And open mandate hedge funds are also very broadly defined. They're value oriented funds that can invest a wide number or types of securities, including debt and equity.

ATTORNEY GENERAL McCOLLUM: Thank you.

MR. SEBASTIAN: Thank you.

MR. WILLIAMS: Thank you, Mike. Why don't we then move forward into the business plan review, which is a continuation of tab 5, a couple of key points here that move us toward the directions we've talked about strategically in the plans that have been outlined by EnnisKnupp and are also very consistent with conversations we've been having

over the past year, year and a half.

We would suggest going a little bit further in some of the directions we are already pretty heavily committed to. For example, looking at both our equity and credit portfolios in-house, we would move more in the direction of passive management. One of the things we've suggested, and Mike alluded to it, is combining domestic and foreign equities into a single team, keep the same two senior investment officers we have, put them together -- they've work together previously. It makes a lot of sense.

One of the immediate gains we would see coming out of that is, it would position us to potentially run a global equity portfolio passively on our own trading desk. We're currently doing that with domestic equities at a fraction of the cost of what it would take to do that externally. Admittedly, doing that in multiple markets and different currencies, et cetera, is more complicated. That's why we would evaluate it use an independent advisor, make sure we're comfortable we could do it in an appropriately buttoned-down manner, and if so, would proceed on that basis and potentially save significant dollars and also have a

significant passive exposure and therefore take little or no risk to the market benchmark.

Secondly, we would, as we have discussed, look further at how to approach opportunistic investment classes. And we would -- for the existing active managers we have, particularly in the large cap equity area, we would, as managers need to be replaced over time, take a very, very hard look at that, and absent a really compelling case, would be inclined to take moneys currently in active large cap equity mandates into either passive, or, if we're going to stay active, do it in the small cap area, where there's a much higher probability of getting paid for that risk.

Looking at some of the other things we would be doing in investment grade fixed income, we would increase the passive allocation there, do less active, more passive. That has two benefits -- well, three benefits, really. First, it reduces risk. Second, by managing things in keeping with the Barclays Aggregate Index, there would be an element of Treasury exposure in there, which means when markets are really horrible and liquidity is very hard to come by, having that Treasury exposure gives you some liquidity that you don't otherwise

have in the portfolio.

We would bring the current passive mortgage-backed portfolios in the house, potentially saving about a million dollars in fees there. We would reduce the internal active management to a level not to exceed 15 percent of the portfolio. It's currently 25. And we think this restructuring overall would save us about 5 to $7 million in fees, increase our liquidity, and reduce our risk. So I think that's a pretty attractive mix.

The hedge funds, we've touched on it. I just wanted to add to the comments there. That's an area I have a pretty significant amount of experience in, and it's an area that a lot of people express some anxiety about. I would just say that all hedge funds are not created equal. We're not talking about black boxes. We're talking about fundamentally oriented funds with modest leverage to the extent they have leverage at all, an appropriate institutional level of transparency, and institutional quality investment teams and institutional quality investor bases.

Obviously, I've had the pleasure in my prior life of working with some of the leading investment

institutions in the world who have very significant hedge fund holdings, and it's not something that should cause you to lie awake at night.

The last thought I would offer on the subject of the risk of hedge funds is, if you look at the misery of 2008, which was probably the worst year in market history a long, long time, the broad equity averages in the U.S. were down north of 40 percent. If you looked at what went on in the hedge fund industry, the average across the industry was down about half of that or less. So counterintuitively, the asset area or subclass that a lot of people think of as sort of exotic and potentially risky actually in reality preserved capital more effectively than what are perceived to be less risky areas.

So that really is the summary of where we are on the business model issues.

ATTORNEY GENERAL McCOLLUM: Can I ask you a question on that, Ash? I'm a little confused, because you tell us about wanting to save more money by bringing some of the management into the house, so to speak.

MR. WILLIAMS: Yes.

ATTORNEY GENERAL McCOLLUM: And yet I thought

I just heard you before you got over to hedge funds saying you were going to reduce the active management of equities internal management from 25 percent to 15.

MR. WILLIAMS: No. That was active --

ATTORNEY GENERAL McCOLLUM: What does that mean?

COMMISSIONER BRONSON: -- management of fixed income in-house.

ATTORNEY GENERAL McCOLLUM: Oh, fixed income. Okay. I'm sorry. I was confused.

MR. WILLIAMS: So we would keep it in-house, but it would be passive, not active.

ATTORNEY GENERAL McCOLLUM: Okay. All right.

MR. WILLIAMS: Thank you. Any questions on business plan issues?

Okay. So you've heard then from the consultants who have worked with us on the asset/liability review and its implications for recommendations for changes in investment policy. You have heard Chairman Hill's affirmation of those from the IAC. We also have Mr. Gidel with us today from the IAC. And unless there are further questions there, why don't we move on to Item 6, which is a request for approval of changes in the

investment policy.

Now, it's important to note, we marked in the agenda items that this was a draft. We said it was a draft because it was pending action by the IAC. The IAC has now voted these exactly as drafted, so there's nothing that would change here. These would in fact be the policy changes.

So if you're comfortable moving ahead, I would ask your approval on this investment policy statement.

ATTORNEY GENERAL McCOLLUM: I have a couple of quick questions, just basic stuff. I listened to the presentations that we've had today, and I know we're moving into a -- in one sense, a more conservative posture. That is obviously a little lower risk overall. That's clear from the graphs and the different types of investment mix that we're making here.

Does that mean that we're going to have a lower rate of return over a period of 15 years?

MR. WILLIAMS: Counterintuitively, it actually means the opposite. We would probably have a slightly higher rate of return with a slightly lower level of risk. And that's exactly what this kind of exercise is about. It's about --

ATTORNEY GENERAL McCOLLUM: I hear you. I just remember when your predecessor was here before us when I first came on this board, the emphasis was on the fact that we did really well compared to other funds in the country because we put all this money into domestic equities, and we took a higher level of risk, and look at how we succeeded at it because we knew how to manage it. That was really what he said to us. I think I'm parroting that right.

Now we're moving in an opposite direction. I know the economy is down. I know things don't look real rosy out there, so I'm not necessarily opposed to doing that. But I just wanted to think in those terms. And I assume that's part of your calculus. There's some fundamental underlying assumption here that because of the way the world's economy looks at the present time and the way that everything is shaping up for the next few years, one would not have as rosy a scenario for the domestic equity markets in predictability as you would have maybe had ten years ago, or even seven or eight years ago, and therefore we need to make these changes, and if we make them, you'll have a higher rate of return, but maybe not -- comparatively speaking,

but maybe not as high a rate of return in the actual real time as we had back when things were going really well in the domestic equity and the boom of -- that ten-year boom we had.

MR. WILLIAMS: I think that's right, General. And I would go further and say it's not an issue relating just to domestic equities. It's an issue relating to all equities. Notice our recommendation is to lower the overall equity exposure, which reduces risk, not just U.S.

ATTORNEY GENERAL McCOLLUM: And a lot of that has to do with things like what we're seeing happening in Greece and other places. But we've not talked about any of that. We've just talked about this is the preferred way compared to other ways that other funds are managed, and the need, of course, to do hedge funds and the sensibility relationship to what happened when we had that down period.

But again, we didn't ask this question of John on the Investment Advisory Council, but I'm assuming you and they, as people who are professionally involved in this every day, made some assessment and said, hey, the risk out there today in the world marketplace is greater and

likely to be greater in the next few years, so we would be better off moving into these other kind of asset categories and taking less equity risk, because equity risk is more exposed to the potential for something blowing up, if you will, which there may be a higher rate of probability of that happening in the next few years than it was two years ago.

Am I stretching my broad economic analysis too much here?

MR. WILLIAMS: No, I don't think you are.

ATTORNEY GENERAL McCOLLUM: Okay. Fair enough. Thank you.

CFO SINK: Governor, I did have one proposed change on the investment policy statement. I'm looking at page 3 of something. It's under the Executive Director's Roman numeral 4.

MR. WILLIAMS: The bullets -- yes, Roman numeral 4, the bullets about the executive director responsibilities.

CFO SINK: It has the four bullets, and then at the top of the next page, it says "Pursuant to written SBA policy."

MR. WILLIAMS: Right.

CFO SINK: The executive director is going to

organize an investment oversight group. You're going to review compliance exceptions. And then it says, "The executive director is delegated the authority and responsibility to prudently address any such compliance exceptions with input from the Investment Advisory Council as necessary."

MR. WILLIAMS: Right.

CFO SINK: I would like to propose that we add "with input from the Investment Advisory Council and the Audit Committee."

MR. WILLIAMS: Sure.

CFO SINK: I just think that's a good check and balance to have in there.

MR. WILLIAMS: Agreed. Okay.

CFO SINK: So I guess we need a motion with that amendment. I'll move Item 6 with the amendment of the "and Audit Committee."

ATTORNEY GENERAL McCOLLUM: I'll second it.

GOVERNOR CRIST: Show it approved without objection.

ATTORNEY GENERAL McCOLLUM: That wasn't such a big deal, was it?

MR. WILLIAMS: Thank you. We're not there yet, are we?

ATTORNEY GENERAL McCOLLUM: Was that motion

intended to approve Item 6? Right?

CFO SINK: Yes, Item 6.

ATTORNEY GENERAL McCOLLUM: So we are there.

MR. WILLIAMS: I'm sorry. I thought we were just on the change.

ATTORNEY GENERAL McCOLLUM: No, no. We made the change, and we approved it. That's what I meant by how quick that was, you know.

MR. WILLIAMS: Great. I didn't mean to seem that ungrateful there.

CFO SINK: In fact, as soon as my partners here are ready, if appropriate, if we think that -- we've got items 7 through 16 to go through, correct?

MR. WILLIAMS: Correct. I think we can --

CFO SINK: I'm comfortable myself with making a motion that we approve items 7 through 16. But if we think we need to go through --

MR. WILLIAMS: Works for me --

CFO SINK: -- them one by one, it's okay with me.

ATTORNEY GENERAL McCOLLUM: Well, I would at least like to hear about them, what they are.

CFO SINK: Okay. Well, let's go ahead --

MR. WILLIAMS: Sure. We can move crisply

here.

CFO SINK: -- through them, then.

MR. WILLIAMS: Item 7 is certification to the Joint Legislative Auditing Committee that the recent audit issues relating to the annual financial audit of the Local Government Surplus Funds Trust Fund have been addressed. They have in fact -- we delivered a letter to your offices I believe last week or the week before confirming that. It's done. We're required to by law to do this letter and have that certification.

CFO SINK: I move it.

ATTORNEY GENERAL McCOLLUM: Second.

GOVERNOR CRIST: Show it approved without objection.

MR. WILLIAMS: Thank you. Item 8 is a draft letter to the Joint Legislative Audit Committee for annual certification of legal compliance and best investment practices for the Local Government Investment Pool. This, of course, is the Ann Longman letter from Lewis, Longman & Walker and relates to the certification that Chairman Heffner with the PLGAC referred to a moment ago that was taken up yesterday.

CFO SINK: Move it.

ATTORNEY GENERAL McCOLLUM: Second.

GOVERNOR CRIST: Show it approved without objection.

MR. WILLIAMS: Thank you. Item 9, we request permission to file for notice for the following amended rules for the Local Government Surplus Funds Trust Fund. These are simply fine-tuning to existing rules reflecting the evolution of the SEC's regulations on 2a-7 and 2a-7-like funds.

ATTORNEY GENERAL McCOLLUM: I move it.

CFO SINK: Second.

GOVERNOR CRIST: Show it approved without objection.

MR. WILLIAMS: Thank you. Item 10 is request approval for changes to the investment policy statements for the Local Government Surplus Funds Trust Fund, a.k.a. Florida PRIME. Again, what we have here is minor adjustments to keep us in keeping with best practice. EnnisKnupp presented a review of Florida PRIME investment policies yesterday.

We're under a statutory mandate on an annual basis to have an external certification of compliance with best investment practices and also legal compliance. So Ann Longman did the legal

side, and EnnisKnupp did the investment best practices side. This is the fine-tuning keep us in the band of compliance with best investment practices.

CFO SINK: Move it.

ATTORNEY GENERAL McCOLLUM: Second.

GOVERNOR CRIST: Show it approved without objection.

MR. WILLIAMS: Thank you. Next we have a string of fiscal sufficiencies. Item 11 requests approval for a fiscal sufficiency for State of Florida full faith and credit Board of Education PECO bonds.

ATTORNEY GENERAL McCOLLUM: I move it.

CFO SINK: Second.

GOVERNOR CRIST: Show it approved without objection.

MR. WILLIAMS: Thank you. Item 12, fiscal sufficiency for Florida Board of Governors, Florida State University dormitory revenue bonds.

ATTORNEY GENERAL McCOLLUM: I move it.

CFO SINK: Second.

GOVERNOR CRIST: Show it approved without objection.

MR. WILLIAMS: Thank you. Item 13, fiscal

sufficiency for State of Florida Board of Governors, Florida Agricultural and Mechanical University dormitory revenue bonds.

CFO SINK: Move it.

ATTORNEY GENERAL McCOLLUM: Second.

GOVERNOR CRIST: Show it approved without objection.

MR. WILLIAMS: Thank you. And Item 14, request approval of a fiscal sufficiency for State of Florida Board of Governors Florida A&M University dormitory revenue bonds.

ATTORNEY GENERAL McCOLLUM: Move it.

CFO SINK: Second.

GOVERNOR CRIST: Show it approved without objection.

MR. WILLIAMS: Thank you. Item 15 is a request approval of and authority to file a notice of proposed rule for the five rules listed below. These all relate to the CAT Fund and simply address technical changes. You remember before we had had rules come up, and pending the outcome of certain legislation, we might need to come back and redo it. This is the final on that.

ATTORNEY GENERAL McCOLLUM: I move it.

CFO SINK: Second.

GOVERNOR CRIST: Show it approved without objection.

MR. WILLIAMS: Thank you. Item 16 is the budget for the State Board of Administration, also the Public Employee Optional Retirement Program, the Florida Hurricane Catastrophe Fund, Division of Bond Finance, and the Florida Prepaid College Board. I'm happy to take these in any order you would like them in.

CFO SINK: I'll move all of them.

ATTORNEY GENERAL McCOLLUM: I'll second all of them.

GOVERNOR CRIST: They all are approved without objection.

MR. WILLIAMS: I like it. Thank you very much.

ATTORNEY GENERAL McCOLLUM: Before you leave, Ash. I do think that we've got a couple of guests here. I know Judy Goodman is here, who is on our Audit Committee. We're glad to have you here. I know Rob Gidel is here. I don't know who else -- he may have been introduced earlier. I'm not sure. There may be a couple other members of these committees I'm overlooking. If there's anyone else here we ought to recognize, please do it.

MR. WILLIAMS: Daniel Wolfson is with us.

ATTORNEY GENERAL McCOLLUM: Yes, I see him hiding back there. Hi. Welcome. We really appreciate you being here. I know I speak on behalf of all of us. Thank you for the hard work you're doing.

MR. WOLFSON: Thank you all very much.

ATTORNEY GENERAL McCOLLUM: Thank you.

MR. WILLIAMS: Thank you.

GOVERNOR CRIST: Appreciate it. We stand adjourned.

(Proceedings concluded at 3:16 p.m.)

1 CERTIFICATE OF REPORTER

2

3 STATE OF FLORIDA:

4 COUNTY OF LEON:

5 I, MARY ALLEN NEEL, Registered Professional
6 Reporter, do hereby certify that the foregoing
7 proceedings were taken before me at the time and place
8 therein designated; that my shorthand notes were
9 thereafter translated under my supervision; and the
10 foregoing pages numbered 1 through 106 are a true and
11 correct record of the aforesaid proceedings.

12 I FURTHER CERTIFY that I am not a relative,
13 employee, attorney or counsel of any of the parties, nor
14 relative or employee of such attorney or counsel, or
15 financially interested in the foregoing action.

16 DATED THIS 30th day of June, 2010.

17

18

19 MARY ALLEN NEEL, RPR, FPR
2894-A Remington Green Lane
20 Tallahassee, Florida 32308
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