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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, September 28, 2010, commencing at 1:10 p.m.

Reported by:
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STATE BOARD OF ADMINISTRATION
(Presented by ASH WILLIAMS)

P R O C E E D I N G S

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GOVERNOR CRIST: Good afternoon. We are reconvening for the State Board of Administration meeting. Ash Williams. Good morning. Good afternoon.

MR. WILLIAMS: Good afternoon, Governor, Trustees. Item 1 on our agenda, request approval of the minutes from our August 10 meeting.

GOVERNOR CRIST: Is there a motion on the minutes?

ATTORNEY GENERAL McCOLLUM: So moved.

CFO SINK: Second.

GOVERNOR CRIST: Moved and seconded. Show the minutes approved without anyone opposing.

MR. WILLIAMS: Thank you. Item 2 is my little update. I guess there are several thoughts I wanted to share with you just to recap where the SBA is in aggregate as an organization. First of all, people tend to think of us primarily as an investment organization. Rightly so. And toward that end our largest mandate, the Florida Retirement System Trust Fund, as of last evening's close, sits at $117.9 billion. That's up six and a half percent calendar year to date and 119 basis points ahead of target.

But going a little beyond the pension fund, I think it's important to note that our four largest mandates, aggregating to the 128 billion of the roughly 140 billion we manage, continued to operate positively and have received accolades from a range of places based on their strength and achievement and exceeding of benchmarks.

The pension fund itself, the Florida Retirement System, has been consistently recognized for its performance and its low cost and has, in fact, posted very strong results over the last fiscal year. The fund, at the level I just quoted, has increased in size by approximately $8 billion since the 1st of July this year.

The FRS Pension Fund is one of the most well-funded and healthy public funds in the United States, generally characterized as being among the top four by objective publications. If we look at our investment performance for the calendar year ended December 2009, Wilshire's Trust University Comparison Service you will recall ranked us as first among our peers, those being the largest funds in the U.S.

For the fiscal year ended June 2010, our net return of 14.03 percent exceeded our investment benchmark by 251 basis points. That's the largest margin of return relative to benchmark in 25 years.

Our pension fund has also been recognized as one of the four models that entered the 2008 fully funded by the Pew Center on the States when they were writing about the problems of public pension funds generally in their research piece, "The Trillion-Dollar Gap."

So we all know about issues involving public pension funds and funding levels, but it's important to distinguish the healthy from the less so in that universe.

At the same time we've achieved solid investment results, the FRS Pension Fund continues to be ranked among the very most cost-effective by CEM Benchmarking, which is an independent firm that ranks the cost-effectiveness of pension plans in North America.

If we look at the Florida Retirement System Investment Plan, which is the defined contribution side of our plan, as of July 31st, we have over 129,000 members in our defined contribution plan. Our assets in the DC plan exceeded $5 billion during fiscal year '09-'10 for the first time since its inception.

And returns for the plan -- and the way you calculate returns for a defined contribution plan, where the members themselves are making the investment decisions, is we have benchmarks for each financial product that members can choose from. We then look at the aggregate dollars invested and calculate the ratio of the actual employee decisions into each product and then do a pro rata assignment of performance.

Performance for the plan in aggregate was 11.07 percent for the year, which exceeded its benchmark by 75 basis points. That's a direct reflection of the quality of the managers that are in the plan who've delivered outperformance for our members, and the defined contribution plan, like our defined benefit plan, is extremely cost-effective per CEM.

The other thing that's interesting about that number, 11.07 percent, you can't get a number that high if everybody in the plan is investing in money market funds, and you can't accumulate appropriate savings for retirement by staying in money market funds. So what this number tells me is that the one area in which we spend more money than our peers on the DC side, which is employee education, is money well spent, because we've appropriately communicated to people how to make prudent decisions about their own retirement investing so that over the long-term, they can set aside and compound sufficient capital to provide for their retirement years.

If we move on to Florida PRIME, Florida PRIME, as you know, has been completely revamped over the past couple of years. We have made many, many enhancements, many of which came at your direction and came with the guidance of the Florida Legislature. But essentially we dramatically expanded reporting. We've contracted out the asset management role to an SEC-registered adviser, who has done a tremendous job for us. We've dramatically expanded Web functionality, improved service for our clients, and continued to provide prudent investment management.

Over the course of fiscal year '09-'10 we've adopted a number of conservative investment policies that mirror very, very closely the new SEC standards for 2a-7-like funds, which are essentially money market funds. We think we offer a tremendous level of value for governmental investors because we are by far and away the lowest cost option for governments in Florida at a cost of less than three basis points, which is three one-hundredths of one percent. That's just remarkably cheap. So at any rate, we're very pleased with the way Florida PRIME is going. And it should be noted, too, taking the long view, going back to 1998, Florida PRIME has paid participating government investors over $6.8 billion in interest. And we've provided participating organizations cost savings of over $300 million.

Moving on to the Hurricane Catastrophe Fund, the Cat Fund is in the strongest position it's been in since it was created in 1993. If we look at the fund and where it is structurally, since we're right in the middle of a hurricane season, you'll see that, number one, the changes made by the legislature in recent years, I think, have contributed to strengthen the fund. And the reserves that we have on hand, $6 billion in cash, three and a half billion dollars in cash proceeds from pre-event debt issuance, and a very substantial bonding capacity, put us in position to meet the needs of the Cat Fund, the exposure needs of the Cat Fund in their entirety.

So, in summary, I would just say the SBA today is stronger and different than the SBA that existed even two years ago. And we continue to improve in a range of areas, including altering investment policies as needed to make them more clear, more reflective of constraining risk and seeking opportunity and an appropriate balance, furthering our commitment to ethics and disclosure, adjusting asset allocations, as we did in the June meeting, but doing so in a method that's very consistent with what's being done in major financial institutions all over the world and well within the boundaries of reasonableness for fiduciaries.

I think it's worthy of note, too, that we've recently had and will have a report from the Audit Committee in a moment. We've had the Groom Law Firm in recently reviewing ethical standards and other structures that we have to protect assets and provide appropriate disclosures, essentially gave us a very strong report. I'll defer to the chairman of the Audit Committee on that one. And likewise Ernst & Young completed a review of personal investment activity at the Board, which also was a report that was, in general, I think could be summarized as a very favorable one.

So you're going to hear a lot of detail over the next hour and a half or so about performance of different parts of our fund and our organization. But the broad premise I want you to hear is that we're performing well. The organization is sound, and we continue to be committed to heading in the right direction.

Unless there are any questions on those points, I'd like to share another couple of little quick details with you, and then we'll move into our agenda.

ATTORNEY GENERAL McCOLLUM: If I could, I do have one question. In a recent newspaper account, the PRIME fund, I guess, the Local Government Investment Pool, was alleged to have, in terms of assets currently held, still held there, those that are risky, those that are below the value they were purchased at, so forth, saying that if they were liquidated, the liquidation value would show a loss of $300 million plus.

I had the impression that that was not accurate. Can you give me any idea about the accuracy of that, what we're holding today, the value of that, have the assets come back, where we had the division of this in two parts and we held certain assets in one and certain in another. Can you refresh us on that?

MR. WILLIAMS: Yeah. I would say the key takeaway is on Pool B, which is where the assets in the local pool that became illiquid were segregated and have been retained subsequently.

The first headline item there is that as of present, 80 percent of the original purchase value of those investments have been distributed in cash to the original investors. So fully 80 percent has been returned already.

Of the remaining 20 percent, a vast majority of those assets remain current pay, meaning that we are receiving payments every month of interest, et cetera. And under our policies, all cash flows relating to those securities are deemed returns of principal and they are distributed out on a monthly basis, commonly between 5 and 12 or $15 million a month. That's why that percentage that's already been paid out keeps climbing over time, because those payments happen with regularity.

The securities that were put in Pool B were put there because they were illiquid. Some of them are still illiquid, and the original structures that were invested in no longer exist. We have seized the underlying collateral, which continues to pay, and exactly what it would be worth if you were to sell it today I think would be speculation that's not entirely constructive.

That's why the judgment was taken to segregate these securities in the first place, because it makes no sense to sell them and incur losses, if you believe that ultimately most, if not all, of their value can be recouped.

And I would suggest our experience to date, having been able to return 80 percent of their original value in cash, suggests that the decision that was made at the time was prudent. And I think we continue to oversee those securities in a prudent manner. I would hesitate to pick a specific value at any given day at which they could be sold.

ATTORNEY GENERAL McCOLLUM: But you have no idea how they came up with, in the newspaper, $300 million of loss that we'd take if we liquidated them as of this month? You don't know how that --

MR. WILLIAMS: I don't know exactly what the methodology was, no.

ATTORNEY GENERAL McCOLLUM: And the truth is that they are performing in the sense that they are mostly assets that pay, pay back over time, bonds mature, et cetera. So if they can even mature and whoever issued them honors them, as they perform, presumably at some point they will then just end up performing as any other asset. Is that not correct?

MR. WILLIAMS: That is generally correct. I'm not going to tell you that everything is perfect and there's no risk. That's not the case. Some of these assets are subject to certain risks in between now and such time as they mature. And as you know, the economy has been slowly making a bend and recovering gradually. We're not all the way there yet. And until we're completely out of the woods, I can't say without any doubt at all that we won't have any loss experience.

But on the other hand, to the extent we do have any, I think it would be modest at best. We do have a guarantee facility in that fund, a guarantee reserve, so to speak. So there have been no realized losses. And depending on how a few other things we're working on goes --

ATTORNEY GENERAL McCOLLUM: So do you consider $300 million to be modest, if we suffered that loss, if that figure were accurate, if the worst case scenario came to pass?

MR. WILLIAMS: Well, I wouldn't characterize it that way, General, given a choice, simply because I have no reason to believe that is going to happen. I'd be amazed if anything of that scale happened. I just don't think that's realistic.

ATTORNEY GENERAL McCOLLUM: You don't think that $300 million figure is realistic, is what you're saying?

MR. WILLIAMS: Well, I'm saying, I don't see any probability that we would ever suffer losses of that magnitude. It's sort of like if you had said, in March of 2008, if you sold the entire assets of the Florida Retirement System Trust Fund, based on current market as of that date, you would have netted $83 billion.

So you could have wrung your hands at that point and said, this is terrible, we've just lost all this money. Well, that was a mark to market number. And as I said a moment ago, the FRS valuation is more like 118 billion today. So why would you fixate on a particular value at a particular point in time? If you don't have to sell, you don't have to sell. And that's a position of strength.

And it's one of the great assets we have in the pension fund, because the fact that we are not liquidity constrained, as a number of other funds are, gives us the flexibility to take advantage and make longer term investments that ultimately will reward our beneficiaries and indirectly our taxpayers as a consequence.

ATTORNEY GENERAL McCOLLUM: Thank you.

MR. WILLIAMS: Thank you. A couple of other quick points I just wanted to touch on. One is on the inspector general. You know that Bruce Meeks retired in June. We have -- where is Melinda? Is she here? We have been through an exhaustive selection process and identified Melinda Miguel, Chief Inspector General of the State from Governor Crist's staff, who will be joining us on 8 November.

We look forward to that. We had a wonderful group of applicants, had several who are very, very highly qualified. This was not an easy decision. But Melinda is just outstanding in every way. Our understanding is she's the interim president of the National Association of Inspectors General. So I guess one could argue, given her credentials and that honor, that we've netted the best inspector general in the United States. We are --

GOVERNOR CRIST: She is indeed that.

(Applause)

GOVERNOR CRIST: Melinda is in a class by herself.

MS. MIGUEL: Thank you, Governor.

MR. WILLIAMS: Thank you. We are also in the market for a new COO/CFO. Gwenn Thomas, who is here, is retiring, as you know. We've advertised that position nationally. We have not made a determination we will go outside, but we thought it was important enough to look both inside the organization and outside.

We had roughly 140 responses to our ad. We have basically segmented the qualified applicants into three groups, those who could potentially be both CFO and COO, in which case a single individual could assume the responsibilities, as Gwenn did, those who are qualified to be COO and those who are qualified to be CFO.

So we are in process of combing through those presently and will report back to you on our progress. But we do have some very strong folks there.

CFO SINK: Governor, if you don't mind, I'll just make a comment about that.

GOVERNOR CRIST: Sure, of course.

CFO SINK: Aside from you, Ash, this is one of the key roles and responsibilities in the fund, and we appreciate all of our investment people back there, Kevin and Michael and everybody else. But unless we have the right controls in place and the right administration and the right operations, you-all deal with 15,000 different investments and maybe more.

That's a big, huge job. And I just would encourage you to be sure we look nationwide to get the very best person, and if that very best person happens to be sitting right under your nose, that's all for the good. But we owe it to ourselves to offer this up pretty broadly.

MR. WILLIAMS: Agreed.

CFO SINK: The fourth largest pension fund in the country, we ought to attract some good candidates.

MR. WILLIAMS: I couldn't agree more. I couldn't agree more. The last thing I wanted to touch on and then go into a couple of slides, if I may, about the portfolio is I shared with you recently a letter we received from the Financial Crisis Inquiry Commission.

This is a federal body that was created, I guess in '09, for the purpose of looking into the causes and effects of the economic downturn and financial upheaval that affected not only the U.S. but the entire industrialized world and is trying to draw some inferences from that experience.

It's absolutely a worthwhile effort. And to the extent we can help them in trying to shed some light on various factors related to that set of events and the consequence thereof, we think that's a very constructive use of our time and we'll do so.

Nothing really to report there, other than we are working on collecting the information requested and will provide it timely.

CFO SINK: And would you just clarify that this is not a letter to say that we are being investigated. It is a letter that asked us for information, because my presumption from what I've read is that they're looking at a number of these potential sales abuses that occurred in many different funds across the country to determine what happened, what went wrong, where were the regulators, et cetera.

MR. WILLIAMS: That's correct. And I think guidance can be taken from the name of the group. It's the Financial Crisis Inquiry Commission. The operative term there seems to be "inquiry." And I have no reason to believe it's anything other than that.

And, again, I think, if you think about it, their mission is to look at causes and effects. And it's perhaps speculation on my part, I'll admit, but it's perhaps as likely that the local government pool experience was as much an effect as it was a cause, probably more so an effect than a cause. So that's where that sits.

Why don't we move into the materials, if we could, under Tab 2 and just look at a couple of things very quickly. On page two you will see mandate numbers, and this was put together as of 17 September. And as I said earlier, the actual FRS balance as of last night's close was 117.9 billion, so up a bit there. The investment plan likewise up slightly.

But what you'll see overall is I think a good, strong picture in terms of assets. Let's move on to page three and look at a high level picture of performance. I would encourage you here to look at the longer term numbers because those obviously are the most relevant.

And I think on the pension plan, what you'll see, if you look at the one-, three-, five- and ten-year columns, is that all of the performance for those periods of time relative to benchmark is positive. I think that tells you something about the direction we're headed.

Moving on to page four, if you look at the various components of the pension plan, the different asset classes, and if you look at the -- basically from that first blue bar down through the last white bar, where you'll get the six asset classes, again, you'll see a strong contribution coming from a range of different areas. And that's what gets you the aggregate outperformance for the fund.

Moving on to page five, touching on a couple of areas of investment focus. First, private equity. You'll remember we discussed, golly, a year and a half or longer ago the potential for some of the private equity investments that had been made during the balloon period of the market, if you will, that had been brought into the portfolio at somewhat higher prices, that the GPs were working hard to get those back in bounds, de-lever them, make management changes, otherwise add value and position as to realized value over time.

Happy to report today that that effort has been very, very successful in those few funds that had some sort of challenges related to them. And if you add those results to the many other funds that didn't have any such challenges, the collective benefit of that is about 20 percent performance gain over the last 12 months. That's obviously a pretty meaningful add to a portfolio.

We also are positioned well to take advantage of opportunities that present themselves as we continue our path through the current recovery. We have about four and a half billion dollars currently in uncalled capital commitments, which means that we've selected managers whose strategies we believe are very, very well suited to the environment we're now in.

We've made the capital commitment. The documents are all in place, and we're now simply waiting for them to say, okay, I've found an opportunity, I need X dollars, please wire me the money. That's capital call. We respond to those. The money gets put to work, and on you go. That's how investments in private equity are made.

In the real estate area, it is no secret that the recovery is slow. There are a range of factors that are continuing to hold down real estate values in different parts of our economy. We are not immune to that. The important part of where we're positioned -- and this is in contrast to a number of other very large public funds -- is that the vast majority of our real estate exposure is in directly-owned properties that are leased up and have very, very low leverage.

So rather than being in properties or in investments that are in fund structures where you have leverage, you have no control over the properties other than your selection of the GP, et cetera, we're fairly conservatively positioned in that regard.

We likewise have got significant committed but uncalled capital out there looking for opportunistic investments that could become available as a consequence of the distress in the real estate markets.

So, again, I think our core positions are good. And that's not to say some of them won't be challenged. They absolutely will. But the analogy we sometimes use is that you can be a farmer and have a very productive farm, even if the occasional plant suffers from drought and withers and dies or gets a disease or whatever. You will always have a handful of investments out of that 15,000 the CFO referred to a moment ago that are challenged. You'll have some that suffer the ultimate consequence, as Peter Cooper Village did that we talked about a year or so ago.

But as these numbers illustrate and the performance numbers you'll hear later will illustrate even more strongly, that in no way means that we're not getting the job done in the asset class broadly or in the fund overall.

Moving on, on page six, strategic investments up 18 percent over the last 12 months, largely because of opportunistic debt funds. Again, we all know we're in an environment where capital is hard to come by for a lot of players in the market. And if you can be a provider of capital for restructurings or other opportunistic investments, do your underwriting carefully and be prudent in your entries and exits, you can do very well. And that's why you pay fees to debt fund managers, and they've done a good job for us.

Again, like private equity and real estate, we have very significant commitments out there, with funds that we think are well chosen for the environment we're in and will be coming out of in the next few years hopefully, so that we are positioned to take advantage of things as they come down the pike in the way of investment opportunities.

Likewise, we continue and are in various stages of research or negotiation in other strategic investment areas, including credit funds, residential and commercial real estate funds, corporate governance activist funds, timberland, infrastructure and hedge funds.

ATTORNEY GENERAL McCOLLUM: Could I ask you a question there?

MR. WILLIAMS: Yes.

ATTORNEY GENERAL McCOLLUM: Your critics, our critics say that hedge funds are too risky. What do you say in answer to that?

MR. WILLIAMS: I'll be honest with you. I think that's a very frustrating bit of misinformation. Hedge funds really, in my mind, are nothing other than investment structure. Hedge fund commonly means that the manager of the fund is paid a management fee, which is some levy on assets, commonly one to two percent.

And in addition to that, they're paid a fee on gains. So, that is, they get a portion of the gains on the fund, commonly 20 percent. So if you had a

$1,000 investment in one of these funds, it was up by 10 percent, that would be $100, you would get 80, the manager would get 20.

What that means is there's a very strong alignment of interest between the underlying investor and the manager, because the only way the manager makes serious money is if the investor first makes serious money.

That said, there's absolutely nothing about the management structure that prescribes what the underlying investment strategy is. And that's the primary place the risk comes from. So you could think of the risk of the strategy itself based on things like what the underlying security focus is, is it U.S. investment-grade bonds or is it equities in frontier markets, about as two different extremes of a security volatility nature as you could have.

How much leverage is present? What's the nature of the investment strategy? Is it fundamental, where you can sit down and understand why a given position makes sense on a fundamental economic analysis, or is it some secret black box? Is there leverage? Is there no leverage? Is there a lot of leverage, or is there something in between?

We look at all of those factors. And my own view is that perhaps the best statistic I can offer you about the relative risk of hedge funds to other types of investments is if we think of the most horrendous recent year in U.S. securities markets and global securities markets, it would be 2008. And in that year the S&P 500 was down roughly 40 percent.

If you look at the Hedge Fund Research Index, HFRI, which is the most broadly accepted, broad hedge fund industry performance measure, it was down about 19 percent. So you have to say, well, gee, if I started the year with $100 and I had the choice of being in the U.S. equity market and ending the year with 60 or having a portfolio of hedge funds and ending the year with 81, would you rather have 60 or 81? You tell me. Where's the risk?

That is why the primary investors in hedge funds are endowments, foundations, very wealthy families who have family offices, et cetera, corporate pension funds, and a number of public pension funds as well. So I think hedge funds have unfairly gotten a bad wrap.

And the idea that most of them are unregulated is not going to be true for very long. Under the Financial Reform Act that was recently adopted in

Congress, the SEC now has authority to regulate hedge funds. No reason to believe they won't over time, and a number of them are already registered by their own choice.

That said, being registered with the SEC in and of itself is no guarantee of safety, as we know from WorldCom, Enron, Madoff, et cetera. Incidentally, none of those entities -- and those were all very serious problems -- were hedge funds, none of them.

So I think it's all in how you go at it. The advisory firm we're using to help us build our hedge fund portfolio is Cambridge Associates. They're the best, the largest and most highly regarded in the world. We're taking a go slow, be careful, be prudent approach. We will continue to do that, and the funds we're focusing on are of institutional grade.

We're not only using Cambridge to do the due diligence on them, but we're visiting them ourselves on multiple occasions, checking out references, checking who their other investors are, et cetera, making sure we have appropriate transparency, and there's nothing hasty here.

ATTORNEY GENERAL McCOLLUM: So as I understand it, from what you're saying, hedge funds are not inherently risky. It's a structure.

MR. WILLIAMS: That's right.

ATTORNEY GENERAL McCOLLUM: And there are some hedge funds that probably are risky, but you look at them, this group that we've hired looks at them, and we're looking at being in things that aren't any riskier than other types of investments, and you believe the structure allows for a more likely good return because of the incentives and the way the appropriate hedge funds are structured. Is that the bottom line?

MR. WILLIAMS: That is the bottom line. I would go even further and say that a representation has falsely been made in some of the media that the foray into hedge funds and alternatives generally is an effort to take more risk in hopes of getting a higher return. That is just 180 degrees off the truth.

The fact of the matter is, if you look at the return assumptions we're using on hedge funds, it's actually slightly below U.S. equities. That's counterintuitive, but that's what we're seeing. And the reason we're putting them in the portfolio is that they're dramatically less volatile, number one, and number two, they tend not be as correlative.

Go back to my example of 2008. If you had a portfolio in 2008 that had some component of hedge funds in it that did not go down as much as the broad equity market and maybe moved at different times, then your overall fund performance would actually do better.

And that's why in our June meeting the analysis came back from EnnisKnupp, after doing literally thousands of simulations ranging from extremely severely unmentionably bad markets to blow-offs to the upside type markets, the general consensus of all those simulations was we actually lowered the risk in the portfolio by adding a small increment of hedge funds, slightly increasing our exposure in real estate, slightly increasing our exposure in private equity, et cetera, and at the same time increase the net present value of the fund, looking forward 15 years, by $2 billion.

Yes, that's somewhat counterintuitive, but that's the math. And if you go to any major institution in the world, it holds up, and we'll stand behind it.

ATTORNEY GENERAL McCOLLUM: Thank you.

MR. WILLIAMS: So with that introduction, why don't we move on and go into the investment performance report. And we have with us Mr. Steve Cummings from Hewitt EnnisKnupp.

MR. CUMMINGS: Thanks, Ash. Thank you, Governor Crist, Trustees. Good afternoon. As Ash mentioned, I am here before you for the first time as a representative of Hewitt EnnisKnupp. On September 1st EnnisKnupp & Associates became part of Hewitt Associates.

And I will just briefly let you know three things. I have been named as CEO of the combined organization. So I am in charge of the slightly larger investment consulting group called Hewitt EnnisKnupp. We remain an independent firm. We maintain independence from the investment managers that we evaluate on behalf of our clients.

And most importantly, I hope, your consulting team remains unchanged. Kristen Doyle and Mike Sebastian are with me today, and the three of us will continue to serve as long as we are welcome. So with that, I'd be happy to answer any questions, but I was going to get right into the presentation.

I'm going to reiterate a few of the things that Ash has already shared with you. It's mostly good news today. I'm going to spend a little bit of time talking about the numbers, the absolute returns that were earned by the various portfolios that Ash summarized, compare it to benchmarks, give you a little bit of peer comparisons and then revisit this notion of fees, both on the DB plan and the participant-directed plan. And I think you'll agree with me that the news is very good.

We'll turn to the next slide, slide three in this deck. We always start these presentations with a brief recap of what the capital markets have done to us. So we can't control the capital markets, but we can try to ensure that your portfolios are structured to participate on the up side and hopefully insulate us on the down side.

As you see for the last 12 months, although the numbers in this report are as of June 30th, 2010, we had some very strong performance in the equity markets, both domestically and abroad up until really the end of the first quarter of this year. And I think, as we all know, the second calendar quarter of this year was disappointing, with a downdraft in both of those markets. If we roll that picture forward, it reversed again somewhat, and we've seen a rebound in the equity markets.

We go forward two slides to the asset allocation. This is an important risk control mechanism. Each of the major asset classes in the FRS has a target allocation and a permissible range around that target. The bars on the left-hand side represent those targets and ranges, and then the orange bars represent the actual allocations as of June 30th of the, at that point, $109 billion portfolio.

And you'll see that in no case are the actual allocations outside the permissible bounds, which is what we want to see in a portfolio of this nature. And these target allocations do not reflect the new target allocations that Ash referred to. As you know, those are being phased in starting July 1st of this year.

We flip forward two slides to the next bar chart. This is a graphical representation of the investment results of the FRS after fees compared to the two benchmarks that we look at every quarter. One is designed to be a relatively short-term benchmark; how would this portfolio have performed had it been invested entirely in index funds or passively tracking the policy portfolio. And for that comparison I ask you to compare the green bars for the actual FRS results to the orange bars, representing the performance benchmark.

And you'll note here graphically what Ash mentioned to you earlier. In all periods shown those bars represent an outperformance of the FRS versus the benchmark, or in the cases of the two downward pointing bars, where the markets were negative, less downward than the benchmarks, which is exactly what we hope to see in a portfolio of this nature.

The second benchmark is a much longer term benchmark, the absolute nominal target rate of return, which as you may recall is the Consumer Price Index plus five percent per annum. Over long periods of time, this benchmark is very important. Over short periods of time, it's going to either be wildly beaten or wildly underperformed based on what is a happening in the markets. And you will see that is indeed the case for these shorter term periods.

But if you turn your attention to the next slide, you'll see that on the long-term, 15 to 30 years, in all cases that long-term absolute benchmark has been not only met but handily beaten.

We like to look at trends as well, and the next slide gives you a graphical representation of the relative performance of the FRS versus that benchmark over time. The reason we like to look at this chart is to make sure that we're not seeing a portfolio that earned all of its excess return over a very short period of time. We like to see some consistency in the way that value-added has been produced over long periods of time, in this case a full 10 years.

And although you'll have to squint a little bit, this is a chart that we -- it looks very attractive to us, a fairly smooth value added. The turbulence of the greatest recession since the Great Depression in 2008, 2009 produced a little bit of rockiness but less so than we would have expected in non-risk-controlled portfolios. And then as the markets have rebounded, you see very nice participation for last three quarters of this chart.

ATTORNEY GENERAL McCOLLUM: Could I ask you one question?

MR. CUMMINGS: Certainly.

ATTORNEY GENERAL McCOLLUM: Before we get all the way away from the long-term rate of return and expectations, there has been criticism, not of our fund, but nationally in the press recently about all pension funds, government pension funds, not taking into account the recent changes in fundamentals like the real estate market in Florida, et cetera, and that any comparisons to 15 or 20 years in the past are not the way to project the future.

That's the shorthand of what I read into those. They've been in the Wall Street Journal, New York Times, publications like that. You obviously read those things. What take do you give to that and what should we?

MR. CUMMINGS: Well, that's a very good question. We, as you may recall from our asset-liability work with the FRS, use an economic model that is a forward-looking model, and we look forward 15 years, which we think is the right way to think about expected returns for investment programs of this nature. Unfortunately, it's an abstract concept. When you're looking at an economic model and a projection, it doesn't exhibit characteristics that you can get your hands around and examine. Whereas the historical track record presents you with those factual results.

What we try to do with our clients is never fail to observe what happened in the past, make sure we understand what happened and how our portfolios reacted or failed to react to it, but not to let the rearview mirror drive the way we're driving a car, to rely more on the economic forecast of the future, while being informed by the past, but not extrapolate past returns into future expectations.

So the work that we did with you-all did not rely on our past laurels for future projections, but it certainly was informed by them. So I guess I would say, if I had to pick one, I would pick the forward-looking economic oriented forecasting, but it's nice to be able to have both in hand, just don't rely too heavily on one versus the other.

ATTORNEY GENERAL McCOLLUM: I got the impression that these critics were thinking that those who do the modeling like you are looking out through too rosy of glasses for the next few years in whatever you do. But obviously that's subjective, and there are many different ways of looking at what the future holds, since none of us really do know.

But I will leave it at that. I don't expect you to fully respond to that. But that's an observation. Nonetheless, there is a lot of literature recently about public pension funds and a -- that we're too comfortable in our skin, that we trustees here would be listening to you project out into the future, and yet we shouldn't be feeling that that's likely to occur in 15 or 20 years.

But I don't, again, expect you have much you can comment on about that. I just know that that's the literature that's out there right now in the past two or three months.

MR. CUMMINGS: And one comment, General McCollum, and that is that I recognize those criticisms. And our 15-year forecast will undoubtedly be wrong one way or the other. It's very rarely exactly right. But I can tell you we've been using this methodology to do that 15-year forecast for about 15 years, and we have never been more pessimistic about the expected returns for stocks and even fixed income, I believe, than we are currently.

So we still may have slightly rose-colored glasses in the eyes of some, but they're the weakest shade of rose they've ever been.

ATTORNEY GENERAL McCOLLUM: So you're suggesting we might get a pleasant surprise because you're predicting pessimism.

MR. CUMMINGS: I certainly hope so, certainly hope so. Shall I move on? Thank you. The next slide is one that can be a little bit confusing, but I always like to stop on it, because what we've done here is deconstruct the relative performance of the FRS over the last one-year and five-year periods, which has been positive relative to its benchmark, into the various asset classes.

The size of those bars for the different asset classes, domestic equity, strategic investments, foreign equity, et cetera, are a function of how well that portfolio performed versus its particular benchmark and how large a component of the portfolio it is. So larger components have a larger contribution, and larger outperformance or underperformance will have a larger impact.

What you see here is some very large bars to the right contributing to that bottom line significant outperformance of 267 basis points, or 2.67 percent, the largest two coming from strategic investments and fixed income.

Now, as you may recall from a couple of years ago, we saw the opposite picture for the fixed income component of the portfolio, where it was a significant detractor from the relative performance. What we're seeing here is the flip side of the recovery in the fixed income markets. The fixed income portfolio was adversely affected during the recession, and those same holdings are now rebounding quite nicely. So it's good to see what we predicted two years ago has actually come to pass.

Similarly, in the strategic investments, it is the debt-oriented strategies in that area that have been particularly successful in beating the benchmark. So the fixed income markets have contributed in several ways to this relative performance.

On the right-hand side, the standout bar for me is the real estate Ash mentioned, that the directly-held properties in the real estate portfolio are performing quite nicely, and that's borne out in this nearly complete explanation of the total fund return, 29 out of the 32 basis points coming from the real estate portfolio. So a very positive picture.

Moving now into peer comparisons, the first one is the TUCS, the Trust Universe Comparison Service. In a real sense, there is no true peer for the FRS, but what we have done is look at the largest ten defined benefit plans in this universe, represents about $878 billion in total assets, with a median fund size of $66 billion.

The pie chart on the following page gives you kind of a rough graphical representation of the differences between the FRS and the TUCS. And these differences in asset allocation are the primary drivers of the differences in the returns. The big differences here is the TUCS average large plan has a larger allocation to private equity and hedge funds and a smaller or a lower allocation to domestic equity. Is there a question?

CFO SINK: Steve, I have a question.

MR. CUMMINGS: Yes, ma'am.

CFO SINK: The TUCS, you say the top ten, are these all public pension funds, or are they -- are some of them private pension funds?

MR. CUMMINGS: I believe they're all public. No?

MS. DOYLE: There are a couple of corporate.

MR. CUMMINGS: A couple of corporates that are in there are that large? Do you happen to know the combination?

CFO SINK: But the majority are the publics, but there are some corporates in there. Okay, thank you.

MR. CUMMINGS: Yeah. There may be -- there couldn't be more than a few corporates that are that large.

CFO SINK: Could you just get that to my staff? Not today. But I'd just be curious as to what they are.

MR. CUMMINGS: Certainly, we will.

CFO SINK: And the sizes also.

MR. CUMMINGS: And the sizes?

CFO SINK: Yeah.

MR. CUMMINGS: I think we have that information as well. We will get it to you.

CFO SINK: Thank you.

MR. CUMMINGS: Certainly. So the primary drivers here again are the differences in the allocations between TUCS large funds to private equity and hedge funds and domestic equity. If you look at --

CFO SINK: Another comment to make along the lines that General McCollum what talking about, too, is that clearly these other ten largest funds have been ahead of Florida, if you will, in terms of getting out there in some of these alternative and strategic investments. So we're not engaging in funds, any kind of path that is not already accepted practices at the other large funds.

MR. CUMMINGS: That's correct. One of the weaknesses of the TUCS system is that there's a little bit of opacity to the actual composition of their alternatives buckets. We can't see through to the actual holdings, but I'm very confident that that is indeed the case.

CFO SINK: Thank you.

MR. CUMMINGS: If we look at the performance differences on the next slide, you'll see that for the most recent quarter the FRS underperformed the TUCS universe top ten and then for the longest time period. The reasons for that underperformance are different. In the most recent quarter, with the FRS having more in stock and stocks having that negative downdraft, that's the primary driver, we believe, of that difference.

Over the very long period, the ten years, that underperformance we think is mostly a function of a lower allocation to the alternative investment market with the FRS program historically versus this peer group. But the central periods, one, three and five years, you'll see that the FRS performed handily versus the TUCS universe.

I should note here, it's mentioned in the exhibit, but to make an apples-to-apples comparison, these numbers are reported before investment fees so that they would be appropriately compared.

The next slide shows the same information graphically. There's been such volatility in the markets it's hard to make head or tails out of these charts these days. The gray bars represent percentile distributions of those top ten funds. The top of the gray bar is the top five percent. The bottom of the gray bar is the bottom five percent.

And it's difficult to tease out how FRS ranks, but if you look at the numbers at the bottom, a low ranking is good. So a 25th percentile ranking means top quartile. So one-, three- and five-year, top quartile to top third and then bottom quartile -- the boundary between the bottom and the third quartile for the ten-year period. A very, very tight distribution.

We're a little hesitant to rely too heavily on these types of analyses when the sample size is so very, very small. With only ten funds, it's hard to draw too many conclusions from this type of analysis, but that's what the data says.

Ash mentioned Cost Effectiveness Measurement. We were very gratified, when we started working with the Florida SBA, that they are a member of this survey. We think it's the best in the industry, and many of our clients use it. If you look to the next slide, you get an idea of the peer group that has been constructed for FRS, with 17 public and corporate pension funds, a little over a trillion dollars in total assets, $68 billion average size, and then ranging from 32 to 203 billion.

And then the chart on the next page gives us a little more information. It's the same sort of gray bar chart, with a fifth percentile median, 25th, 75th and 95th percentile. What you'll see here graphically is what Ash referred to earlier. The total cost of the FRS is very, very competitive, ranking in the 13th percentile. And in this particular chart, obviously low is better than high, unlike other -- as opposed to returns.

And we were asked yesterday to what do we attribute this very, very favorable cost structure. And there's a couple of things that we think are driving this. The first is a healthy allocation to passive management in the FRS, which is a low cost way of getting access to the capital markets. There's a heavy use of internal investment management, which generally is lower cost than externally hired managers, and the internal management is very competitively priced at the SBA.

And then lastly but not leastly, there's a very aggressive fee negotiation that goes on on the part of staff whenever external management is used, to make sure that those fees are as competitive as they can be, and obviously it's fair and prudent. Any questions on the FRS before I move on?

The next several slides -- thank you. So here we have a comparison of the investment returns, and the 11.07 is rounded here to 11.1 on my slide for the one-year period for the investment plan. Every time we're before you we give you two comparisons. We compare the plan to its aggregate benchmarks, but we also compare to this thing called an average defined contribution plan.

Well, unfortunately, I know I've given you this disclaimer before. There is no amalgamation of defined contribution plans. So what we use here is a construct. What we look at is the average allocations of defined contribution plans that we get from a Council of America Survey. And then we load into that average allocation the median return from Morningstar's database of mutual funds.

The reason I give you that caveat is you'll notice that relative to the FRS, it looks like the FRS underperformed the average defined contribution plan for the year by 2.8 percent, which is true. The primary driver there is the so-called average defined contribution plan has over 20 percent allocated to company stock. Obviously, there is not a company stock proxy for this plan.

So when we model the company stock component of the average defined contribution plan, we load into that component the return of the U.S. stock market. Over the last year that's been a very strong market. So we completely attribute that performance to that quirk, if you will, of this comparison.

We always say that the most relevant comparison in our minds is the one at the lower part of this table that compares the FRS to an aggregation of its benchmarks, what those individual portfolios are set out to be. And here you see a very favorable picture. Over all three time periods, outperformance on the part of the FRS.

The next slide goes back to fees. I love showing you fees because they look good. At the top of the page we have the average plan expense ratio versus corporate defined contribution plan expense ratios. And for that we're using large corporate plans. We have a universe of 20 plans with assets between 2 and 11 billion. That may not seem large to you, but it is large in the corporate defined contribution space. And you can see the FRS expense ratios are four basis points lower than those in that peer.

We've also included a comparison for you of the typical defined benefit plan investment management fees, because it's often said that defined contribution plans are fundamentally more expensive than defined benefit counterparts. And I find it interesting to see that in the case of Florida, your participant-directed plan is less expensive than defined benefit plans of both corporate and public fund peers. So, again, hopefully you'll agree a very favorable picture.

On that continued theme, the next slide shows the fees by option. And I won't belabor it other than to say there is no area of the investment program where the fees in this plan are not cheaper than the average mutual fund fees. So, again, very competitive.

The next slide shows the change in assets in this plan. You'll see the dip is a result of the recession and subsequent recovery. And more interesting to me is always the next slide, which shows the investment plan membership continuing to increase with nearly 128,000 participants at fiscal yearend. Any questions on the investment plan?

ATTORNEY GENERAL McCOLLUM: Actually, I have one overall question in that regard. Have you examined the methodology by which our pension fund, our State Board of Administration determines its benchmark or its benchmarks?

MR. CUMMINGS: Yes. In fact, we did a study last year?

MR. SABASTIAN: This year.

MR. CUMMINGS: It was earlier this year. Yes, we do routinely evaluate benchmarks on all aspects of the investment program, across all the portfolios, and routinely come with recommendations for changes when there's a new benchmark that exists in the marketplace or a change in the portfolio that suggests that a benchmark might be worth revisiting.

We try not to encourage frequent benchmark shifts because it can make score-keeping challenging and complicated. But we do regularly examine the benchmarks.

ATTORNEY GENERAL McCOLLUM: The reason I ask that is simply because, as you referred to several times today and you have in the past in reporting to us, that the benchmark is the most important thing for us to compare to. So obviously the validity of the benchmark becomes ever more significant. I just wanted to know the degree that you got involved with it and continue to do that. Do you do this annually, looking at benchmarks, with us?

MR. CUMMINGS: It's at least every other year that we look at benchmarks. I'm looking at my colleagues, if they may have a recollection, or Ash, if you recall.

MR. WILLIAMS: They certainly get looked at every time there's any change in what we're doing. So, for example, the shift from separate domestic and non-U.S. equities to a global benchmark would represent a fine-tuning, or if you add hedge funds or you add this or that or the other, there's always a fine-tuning.

MR. CUMMINGS: We also have a tendency to revisit benchmarks across all our portfolios whenever there's a change in benchmark providers. There's been a lot of mergers and acquisitions in the industry of calculating benchmarks. And when they buy a benchmarking firm, they feel like they have to tweak the methodology a little bit. And every time that happens, we have to go back and revisit the benchmarks to make sure they continue to be the appropriate ones.

So it's not a routine and regulated part of our service, but it is kind of a continuous -- an ongoing effort to make sure that we're always using the right benchmarks.

ATTORNEY GENERAL McCOLLUM: Thank you.

MR. CUMMINGS: Turning now to the PRIME fund, we have the performance here of the PRIME fund relative to its benchmark over all periods ending June 30th. A couple of things driving the favorable results here. As you see, the results are ahead of benchmark in all periods. An important one Ash alluded to during his comments. This is a very, very cost-effective program, which is a theme for my comments today, I think. Three basis points was the exact figure.

The benchmark has an amalgamation of other government investment pools, but I'm certain that the average fee is higher than three basis points. I don't have the statistic handy, but I know three basis points is among the cheapest if not the cheapest. So obviously very strong and consistent results for that portfolio.

The next slide shows the cash flows, the opening balance compared to the ending balance. As is usual, participant deposits and participant withdrawals are large. That's not unusual for this portfolio. You also will notice the transfers from Fund B of a little over $26 million.

The next slide gives you an idea --

CFO SINK: Excuse me. The transfers from Fund B, I thought that when we got liquidity out of Fund B, they were going straight to the investors. Is that not right?

MR. CUMMINGS: I believe the way this is -- and I'll turn to my colleagues if I get this wrong -- is we wanted to record that the money came back, but it doesn't stay. It also then factors into the participant withdrawals. We wanted to be able to record here that this is the amount from Fund B.

CFO SINK: So there hasn't been a change in policy.

MR. WILLIAMS: No.

CFO SINK: It's incorporated into those withdrawals.

MR. CUMMINGS: Right. We just didn't want it to get completely swamped by the regular contributions and withdrawals, so you can see the magnitude of that particular cash flow.

The next slide just gives you an idea of the quality and liquidity. About 90 percent of this portfolio is liquid within 90 days, so a very liquid portfolio and a very high quality, with nothing but A1 paper in there, and 70 percent of it being A1-plus paper. Again, no real change in this characteristic since the last time.

This is a lot of numbers on the page. The one that is most important, I believe, is the one that Ash referred to earlier, the bottom right-hand number, which shows the proportion of original principal returned to the participants out of Fund B. And there's the 80 percent we referred to during his comments, and the 422 million to the left there of the remaining principal. Any questions on the PRIME fund?

All right. I just have a few more slides. On the Cat Fund, two portfolios here, about a little over $8 billion in total. If you flip to the next slide, jump straight to the results. This is a tale of credit spreads, really. This investment portfolio has slightly more credit risk than the benchmark. So you see during the three- and five-year period, when we've got the recessionary period, a slight underperformance relative to the benchmark and a very strong bounce-back in the one-year period, with results handily trouncing the benchmark.

So the long year, ten-year period is the one that kind of incorporates both the near term and the mid term and shows a very positive result for the Cat Fund. Again, we didn't like the downdraft that we saw when the credit markets fell apart, but it's nice to see that the portfolio performed on the other side the way that we expected it to.

And then the last slide is for the Cat 2007A fund, which again shows for a shorter time period, but very strong favorable performance of the portfolio versus its benchmark.

That concludes my prepared comments, other than to finish how I started. The portfolio has weathered the storm quite well, on a relative and most recently on an absolute basis, and continues to be, as Ash pointed out, a model for low cost institutional investing.

GOVERNOR CRIST: Thank you, Steve.

MR. CUMMINGS: Thank you very much.

MR. WILLIAMS: Thank you, Steve. Why don't we move into the standing reports, led by Mr. Bill Sweeney, chairman of the Audit Committee.

MR. SWEENEY: Good afternoon. First I'd like to introduced my colleagues on the committee, Kim Mills and Judy Goodman. These are the people that get to spend four or five hours monthly. The only remuneration that I can tell that we get is a cup of coffee, although management has served this in the smallest cups. Lilliputian would be proud of them. I think they were hoping that we would have a cup of coffee and leave. And our defecting member, Melinda -- I don't know if she's still here.

CFO SINK: She's back there.

GOVERNOR CRIST: She's here to defend herself.

MR. SWEENEY: She also, we're really looking forward to cross-examining her in her new role. There's lots of retribution to be had.

The first topic is the annual report or the annual audit. About a year ago you directed us to look into an independent audit of the funds of the defined benefit and defined contribution. We solicited proposals from national accounting firms, selected a firm, and we are well on our way.

This is a major, major achievement in my mind, that we are finally going to have an independent audited statement of the two pension funds. I think that not only the trustees deserve to have this, but our beneficiaries.

Now, that's not to say that the funds were not audited, because the auditor general did it, but it was in a context of a statewide CAPRA. And to our beneficiaries, that's very hard to then try to parse out what belongs to them and what belongs to the entire state.

We have -- the management has worked very diligently to produce it, and we think they will have that within a month, a financial statement, and then we will have the audited report as scheduled for December 15th.

I will say that having this firm aboard does, at least in my mind, provide a lot of advantages to your Audit Committee, and that is that while they have auditors, we have skilled auditors as well with the auditor general, but these auditors also have access to specialists, and these specialists are all over the country, and sometimes all they do is work on hedge funds. They work on REITs. They work on evaluations.

And I will have to tell you that that's been a very impressive part of this process, is having access to individuals who have worked with major insurance companies, major banks, major investment banks and financial investment funds.

CFO SINK: Bill, have they raised any flags at this point in time over the way we've been looking at or evaluating certain assets versus what they see as being more standard practice?

MR. SWEENEY: As of this point they have not raised any major -- one of the other interesting specialties that they bring to the table is they are auditing -- doing an IT audit, which is probably only something that you're going to get from a major firm. The other advantage of having a major firm like this is, since this is their full-time business, they have the luxury of being able to have people go to the FASB meetings. They follow Congress, and they're there when they're writing the rules and regulations. And so this is something that we will be able to take advantage of in the future.

One of the other specialties, of course, they have is an evaluation specialist, and this is important in various aspects of the Board's business. I think some people were apprehensive about how the auditor general might feel about this. And to my understanding, they've had several meetings, and it's been very cooperative, and they're working together.

With respect to some of the other audits that we have delivered, these are now being -- we are now hiring auditors who are directly reporting to the Audit Committee. The direct-owned real estate, we received the audits. And that is a major change in the way business was done, since the asset manager often employed the auditors, and this offers the board and our participants at least some more degree of independence.

Current audits that are being conducted, the auditor general is doing the local government fund, and the Cat Fund is being audited by Ernst & Young.

We would like to suggest and ask your approval of a proposal that we think would be helpful, and that is we want to preapprove three or four auditing firms, go out and solicit, put them on an approved list and have them ready to go for three years.

It's so difficult, the way our procurement policies are, that it takes us six weeks, two months to get somebody on board. And if you would approve that, we will undertake to do that before the end of the year.

CFO SINK: I see a lot of heads shaking.

GOVERNOR CRIST: Nodding.

CFO SINK: Nodding.

ATTORNEY GENERAL McCOLLUM: We don't need to formally do anything to approve that?

MR. SWEENEY: The nods are good enough for me.

GOVERNOR CRIST: Unanimous nod.

CFO SINK: Maybe for the record, Bill, we ought to put it in the record there are nods.

MR. SWEENEY: Of approval.

CFO SINK: Right. So the idea would be that you would put an RFI or something out and say, we'd like to have two or three accounting firms that we've identified that do go through a competitive process, that they become for a three-year period in the stable of firms that we can call on when we have something quick that we need to get done.

MR. SWEENEY: Exactly. Sort of like a shelf registration.

CFO SINK: Right. I got that.

MR. SWEENEY: One of the other --

CFO SINK: But, Bill, excuse me. I think it's also important to -- I don't know how you think through this, but they ought to disclose how they would charge in terms of their fees and that sort of thing. What we don't want is an open-ended, well, I'm on the list and I can charge whatever I want to.

MR. SWEENEY: We have thought about that, and it's possible that we would show an assignment to more than one and see what the price would be.

CFO SINK: Yeah, okay, that there would be competition within the stable of firms that you preapproved.

MR. SWEENEY: Right.

CFO SINK: Perfect, okay.

MR. SWEENEY: We now have a risk and compliance officer making monthly reports to us. Eric Nelson has done a good job with a lot of extra duties that have been in response to prior audit criticisms.

My personal interest and one that we have brought up before this board is the matter of training our own people and continuing education. To this end, the board has hired Cindy Stiff, and she has been working -- she works for Eric, I guess, but she's been working, and it's been an amazing thing to me, what is out there, and she's surveyed what other major financial institutions do.

And she has a whole -- she's hired a firm that provides computer-generated courses. And I think there are over 300 titles. Eric has warned me not to get into the details because he has a report on this later in the meeting. But I think we have already had 100 people go through.

We also are, as I understand it, going to have seminars on hedge funds, mortgage-backed securities, third-party repos, Rule 144, things that are directly related. And I think it's incumbent upon us to give our employees the tools and the education.

And the most expensive way is to send them all over the country to seminars, and this seems to be the modern trend and it's tele-education. And many of the firms, in fact, I think the initial contact was with Mellon, and they use this extensively. And I think the first reports from employees who have been through this are very favorable.

These are vigorous courses, and they are in step so that you can take the first branch and keep moving up. And since we do have some turnover, this would be good to keep everyone working in the same direction.

Now, with respect to our favorite -- my favorite other subject is the audit recommendations. As you know, when we started looking at this in January of '09, we had 219 outstanding audit recommendations. Today, from those 219, we have 27 that we haven't completed yet but anticipate that those will be completed by the fiscal year.

Since January 1 of '09 we have 71. I think it's slightly optimistic, but I've been told by the internal auditing staff that we think that there are now 55 of the 75 outstanding, and we're hoping to have those complete by the end of the fiscal year.

So that would mean that what we would have is whatever audits are being conducted this year. And I think this is a major achievement by management, who have worked very hard to reduce this backlog.

I think that our next sort of points of emphasis might be a couple of things. Going back, getting a more thorough report on liquidity and how we're going to address that problem. It's going to be a continuing problem. And another factor is a catastrophic risk, how we are going to operate given those, and the Audit Committee and all the standard procedures, that's something that we have to think about. And it's not only if the catastrophic event occurs here, but what happens when it occurs somewhere with like major dealers that we deal with.

And so we haven't yet taken the steps to go to a remote site. I think other major financial institutions have gone through this process. It's really hard to bite that bullet the first time, to see if you can go somewhere else and do your business. But it's something we'll probably have to do. And that concludes our report.

GOVERNOR CRIST: Thank you, sir.

MR. SWEENEY: Thank you.

GOVERNOR CRIST: Well done.

MR. WILLIAMS: Thank you, Bill. Moving on with the standing reports, we have Patsy Heffner with us, the chairperson of the Participant Local Government Advisory Council.

MS. HEFFNER: Governor, Trustees. Since the prior meeting in June of the trustees, the Participant Local Government Advisory Council has met once, September the 22nd, and our next quarterly meeting is scheduled for December the 8th, 2010, in Osceola County.

Since the last trustees meeting in June, the council has continued to work on several issues designed to improve the operations, client service and investment management of the pool. Most recently, over the quarter ending June 10th, participant deposits totaled 2.69 billion. Participant withdrawals totaled 3.03 billion, for a net decrease of approximately 313 million.

Marginal net outflows were normal for this time of year and are in line with the pool's historic cash flow cycle. The SBA and Federated Investors continue to implement elements that affect reforms to Rule 2a-7, affecting the investment practices of money market funds.

One of the significant changes, which were approved by the Board of Trustees after review and recommendation from the PLGAC and the IAC, impacted minimum levels of liquidity for PRIME holdings. Florida PRIME is now required to hold at least 10 percent in securities accessible within one day and at least 30 percent in securities accessible within seven days. These liquidity thresholds were 5 percent and 20 percent respectively prior to July 1st investment policy changes.

These new investment policy obligations represent even higher levels of liquidity for pool investors and are a clear example of PRIME's commitment to be a Rule 2a-7-like money market investment vehicle. During the first week of July we began to report the seven-day SEC yield to all pool participants, in compliance with the Rule 2a-7 methodology.

For the period ending June 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 12 basis points over the last three months, seven basis months over the last 12 months, and one basis point over to last three years. Thank you.

CFO SINK: Thank you.

GOVERNOR CRIST: Thank you.

MR. WILLIAMS: Thank you, Patsy. Why don't we move on to Mr. John Hill, chairman of the Investment Advisory Council.

MR. HILL: Governor, Trustees, good afternoon. I'm going to make the report as chairman of the IAC. The IAC met yesterday with the executive director and CIO, Mr. Ash Williams, and his leadership team at the SBA for our Q3 update. The SBA and their advisers reported to us on several fronts, including performance, major initiatives or mandates update, which was led by Kevin SigRist, the pension plan performance review by EnnisKnupp, which we just got a review of, and then the real estate performance review by The Townsend Group.

So some of this has been reported, but in summary, the fund has been performing well, as reported to the IAC. As Ash mentioned, as of 9/23, we are up to $116 billion in the fund, up from 109 billion in June at our last meeting. Through August of 2010, the pension plan was up almost one percent for the third quarter and over eight percent for year to date.

Relative to the benchmarks, the plan is ahead of benchmark for the year by more than two percent. And for the year the plan has generally been performing well across all the sectors, with fixed income and global equity performing the best relative to targets. So I guess also the fund is in balance relative to the respective allocation categories and asset weights across all the categories.

In regards to the major mandates that were discussed with the IAC, the SBA has made some initial investments in select debt securities and hedge funds, and it is exploring investments in real assets, including timberland, all in accordance with the investment policy mandates. We also had an update on risk management compliance and new hiring efforts.

EnnisKnupp, as they did today, reviewed for us in some more detail the recent and long-term performance of the fund and the asset allocation of the fund and its comparison relative to our peer group. And as we heard from Steve Cummings, you know, we're really generally favorably compared in all regards. I'd say typically you're in the top quartile or the top half of our peer group. So that was good news.

And then the last part of our meeting had to do with specifically looking at the real estate performance, and The Townsend Group made a presentation about that. And the real estate asset category has been one of the best performing categories and asset classes for the pension fund over the long-term. They've exceeded the benchmarks for one-year, three-year, five-year and ten-year. The ten-year return is 7.1 percent.

So the real estate investments have included kind of all the traditional core real estate categories and also farmland and REITs, and they've been about three-quarters percent direct and 25 percent through other funds. There's currently about $7 billion invested in the real estate asset category, which is around seven percent of the fund. And the real estate investment results have also generally outperformed their peer group. So real estate is a good story.

So, in summary, the pension fund is performing well relative to benchmarks across all the sectors and as measured against peer groups. So this was a favorable meeting yesterday and a very positive report. You know, one of the points that was made was that -- and even where we have fallen short somewhat, it's almost by conscious effort to take less risk, to maybe take a little less return, so that might not rank us quite as high but still achieve a good result. Any questions of the IAC?

CFO SINK: I like these good reports.

GOVERNOR CRIST: Thank you, John.

MR. HILL: Okay. Thank you very much.

MR. WILLIAMS: Thank you, John. I just want to say, as I always do, how much we appreciate the time of our Audit, Investment Advisory and Participant Local Government Advisory committee members. They give generously of their time. Only Sweeney would complain about the size of the coffee cups.

General Counsel. Maureen Hazen.

MS. HAZEN: Good afternoon. I'd like to start my standing report today by discussing two major developments in the law that have occurred during the previous quarter. The first is the passage of the Dodd-Frank Reform and Consumer Protection Act, which was signed into law by the president on July 21st. The act is very complex and will have far-reaching effects on the financial markets in general.

And other than the corporate governance provisions that Michael McCauley will talk about later, there are really three parts of the act that have more direct impact on the SBA as an institutional investor. The first two I'll discuss now, and the third I'll mention during my discussion of the Morrison case.

First, Title IV of the act, entitled the Private Fund Investment Advisers Registration Act of 2010, generally eliminates the private fund exemption from the registration requirements of the Investment Advisers Act. So this will, going forward, cover private funds generally with assets under management in excess of $150 million.

The act directs the SEC to promulgate rules regarding record-keeping and reporting requirements for these funds. I believe they have until next July to enact those rules, but we anticipate the SEC will start publishing proposed rules sometime between October and December of this year.

The second portion of the act is Title VII, entitled the Wall Street Transparency and Accountability Act, which generally imposes additional regulation on over-the-counter derivatives markets, including mandatory clearing of swaps. The act requires the SEC and the Commodities Futures Trading Commission either individually or in some cases jointly to promulgate final rules no later, again, than July 11, 2011. We've already started seeing the SEC and the CFTC propose advances or publish advances to the proposed rules.

And as the SEC and CFTC do propose rules, SBA staff will review them, analyze them and decide on a case-by-case basis whether or not it's appropriate for the SBA to comment as an institutional investor.

The second major legal development that I'd like to discuss today is the Morrison case. On June 24th, the United States Supreme Court issued an opinion in the case styled *Morrison v. National Australia Bank*. This case will have a profound impact on securities fraud litigation and the revenues that are available to U.S. institutional investors like the SBA.

The facts of the Morrison case were limited to a foreign plaintiff suing a foreign issuer, that is, the National Australia Bank, for securities fraud under Section 10(b) of the Securities Exchange Act in connection with losses of stock which was purchased on a foreign stock exchange, the Australia Stock Exchange.

The Court, in an opinion authored by Justice Scalia, held that Section 10(b) is limited to deceptive conduct, quote, only in connection with the purchase or sale of a security listed on an American stock exchange and the purchase or sale of any other security in the United States.

The court drew this conclusion based upon the application of a longstanding principle of American law that unless Congress clearly expresses the intent for a law to have extraterritorial application, the law applies only within the territorial jurisdiction of the United States.

This Supreme Court case is important for two reasons. First, the jurisprudential value. The court overturned 40 years of judicial precedent, primarily in the Second Circuit. Under the body of case law at that point, the courts had concluded that because the securities laws were silent as to extraterritorial application, courts should discern whether Congress wanted the law to apply extraterritorially.

And in order to make this judgment, the courts had developed what's called the effects and conduct test, which is a test in which courts examine whether the wrongful conduct had a substantial effect in the United States or upon U.S. citizens and whether the wrongful conduct occurred in the United States, compared to the transactional test that Justice Scalia had adopted.

The second reason why the case is so important, the practical reason, is that notwithstanding that the facts of the case were limited to non-U.S. plaintiffs, the bright-line transactional test adopted by the court, most experts agree, probably will have the effect of barring U.S. investors from recovering damages in securities fraud cases for foreign securities issued by foreign companies if they're purchased on a foreign stock exchange.

And indeed it's been four months since the court has issued its opinion, but federal district courts are already interpreting Morrison in that fashion. There have been a couple of cases that have been dismissed outright on this basis.

The case has effectively produced an incongruous result in the sense that a private cause of action exists against U.S. investors but not against foreign issuers, even if a foreign company received a significant portion of its capital from U.S. investors and is actively soliciting capital from U.S. investors on our soil.

In my view, the case requires action by the U.S. institutional investor community, and because the case is one of statutory construction, the court's holding can be addressed through congressional action modifying the Securities Act and the Securities Exchange Act to clearly express an intent for extraterritorial application.

A moment ago I mentioned the Dodd-Frank, that there was a third aspect. This is actually also addressed in the Dodd-Frank Act, apparently in response to the Morrison decision. Two things. The Dodd-Frank Act expressly provides, one, that the SEC may enforce from a regulatory perspective the anti-fraud provisions of the securities laws in these kind of cases; and, two, specifically directs the SEC to study whether extraterritorial application should be extended to private causes of action.

A moment ago I mentioned that in my view this requires action. I want to just mention briefly some of the steps the SBA has taken. First, on

August 4th, the general counsel for New York State Common trust fund and I presented on the topic in a Council of Institutional Investor teleconference in order to inform other institutional investors about the issue and possibly organize other public pension funds.

Then we held a call with the general counsels of 15 of the largest public pension funds to assess others' interests in investigating and acting on this issue.

And from that call, we formed a working group consisting of the general counsels of New York State Common, New York State Teachers, Connecticut, Colorado, North Carolina, New York City and myself -- I hope I'm not leaving anybody out -- to implement a plan of action which will consist of approaching both Congress for legislative change and the SEC to consider the public pension fund position in its study. And that work is very active right now and ongoing. The next --

CFO SINK: Governor.

GOVERNOR CRIST: Yes.

CFO SINK: I like seeing Florida take a leadership role in issues like this. We're the fourth largest fund in the country. This is exactly what I think we ought to be doing. Thank you, Maureen.

MS. HAZEN: Thank you.

GOVERNOR CRIST: Thank you.

MS. HAZEN: The next topic in my standing report is SBA agreements. In the last quarter the SBA general counsel's office negotiated and finalized 39 new contracts, which include notably seven new alternative investments, one new real estate investment and contracts with three new global equity managers. We also finalized 72 contract amendments and 15 contract terminations.

Next I'll move on to SBA litigation matters. The SBA is currently a passive member of the class. There were 440 securities class action cases. During the last quarter the SBA collected $2.3 million in recoveries as a passive member of the class.

I'd like to say a few words about the case, noting sensitivity of some matters that relate to active litigation, and that is the Countrywide case. Countrywide is one of those cases that I've been evaluating and monitoring over the last several months. It's kind of taken a life of its own in the last few weeks.

But the Countrywide class action case was filed back in 2007 after investors learned that Countrywide had concealed the quality of the home loans that were on its books. Investors in that case have alleged that the concealment artificially inflated the company's earnings from '04 to '07 and caused the company's financial statements to be materially false and misleading. The fraud in that case was so egregious that the SEC filed a securities fraud action against three of its officers.

The SEC's action recently survived a motion for summary judgment and is set to go to trial on October 19th. In the class case, the lead plaintiff has reached a proposed settlement with the defendants, which the court will hear for approval on November 15th.

Under that proposed plan of allocation -- I say it with the caveat that the Court has not approved it yet. But under that proposed plan of allocation, the SBA will recover very little if any of its losses, which is why it's been on my screen for monitoring right now.

And as a result of that, we've engaged one of our securities litigation counsel to assist in negotiating a settlement outside of that class action, because we believe that will provide an enhanced recovery for the Florida Retirement System Trust Fund with respect to that case.

ATTORNEY GENERAL McCOLLUM: May I ask you a question? Why will we get so little out of the class action in proportion to what we should be getting?

MS. HAZEN: Under the plan of allocation, the way that the experts' testimony that the courts are accepting, assuming they accept the plan of allocation, the portion of the sales in which the court -- or the damages expert is assessing the inflation to the price per shares does not correspond to a period in which the SBA had the majority of its losses.

So the class period in that case is three years, and there's a portion that the plan is allocating a heightened amount of the price of inflation, and we will not be in that group. And working with this particular firm, we have our own damages experts that suggest that that's not a proper allocation, which is why we think that we can benefit from negotiating a settlement outside of the class action.

ATTORNEY GENERAL McCOLLUM: With Bank of America now as Countrywide or with whom? Who are we negotiating with?

MS. HAZEN: It would be with Countrywide, Bank of America now.

ATTORNEY GENERAL McCOLLUM: Thank you.

MS. HAZEN: The last thing that I'll mention in my report to the litigation-related is really just some portfolio monitoring. SBA staff is in the process of implementing a portfolio monitoring tool offered by one of its securities litigation counsel firms.

The SBA currently uses a service to monitor litigation and performs its own loss calculations for independence reasons, and we will continue to do so. However, the software that this firm is providing provides supplemental real-time information about particular cases and will notably provide an independent check to ensure that the SBA's custodian bank timely and accurately files all the SBA's claim. It's a good check to make sure we don't leave money at the table.

That concludes my prepared remarks. I'm happy to take any questions.

GOVERNOR CRIST: Thank you.

MS. HAZEN: Thank you for your time.

MR. WILLIAMS: Thank you, Maureen. Why don't we move on to Mike McCauley with the corporate governance report.

MR. McCAULEY: Good afternoon. I'm just going to provide a brief update on the SBA's corporate governance program and activities since the last trustees' meeting.

We have not submitted any formal regulatory comment letter since the last meeting, but we are currently drafting a response -- I believe we touched on this at the last meeting -- to respond to the SEC's concept release that they released a few months ago related to proxy mechanics or proxy appointment.

And that will cover quite a few different issues but primarily how the proxy voting research firms may or may not be regulated, their performance, their potential conflicts of interest, that sort of thing, and then kind of a range of different voting mechanics and logistics, how votes are counted, how shareowners are registered, what role the SEC plays in that. So we're kind of actively working on that right now.

The proxy voting, the corporate governance and proxy voting oversight group met in mid-July as part of its quarterly meeting and discussed a number of issues, but the three listed here are probably the most notable.

The first one is a fairly comprehensive voting review that was conducted, and we do this periodically. This was probably the most comprehensive one that we've done historically, covered all the votes for our foreign equity portfolio managers, covering the entire fiscal year, and essentially was aimed at benchmarking their votes, reconciling them back to their own policies, comparing and contrasting those voting decisions based on our own. The SBA maintains quite a few portfolios internally that we vote foreign equity shares or non-U.S. company proxies.

And as a result of that review, we will in the next probably six to nine months, through the end of the fiscal year, kind of re-examine what portfolios we may or may not add to the voting coverage alongside of our internal accounts.

The second one is investor initiative, and this I believe was touched on in some of the monthly trustee reports. But we are a member in Ceres, which is an investor organization that is focused on environmental advocacy and policy disclosure. We've been a member of Ceres for several years now. And they coordinated, spearheaded an initiative shortly after the BP spill aimed at oil and gas companies and even insurance companies as a follow-up inquiry into how -- these, again, are global oil and gas companies -- how they are implementing various risk management procedures, what kind of safety protocols they have for -- focused on deepwater drilling. So offshore deepwater drilling.

ExxonMobil, several of the large U.S. companies received a letter, Petrobras, many of the large global oil and gas companies. So we're eagerly awaiting those responses. Letters were sent out to about 26 companies on the oil and gas side and about 27 insurance companies. So the deadline for that is November. It will take a few months probably to collate and summarize the response. We'll get that back from Ceres.

CFO SINK: Michael, is the focus on the insurance companies more how they -- how they evaluate insuring the oil companies? Is that the nexus there?

MR. McCAULEY: Yes, essentially. It's how they are going to potentially change their business process to encompass the new exposures that they may not have covered previously or, given the market dynamics in that industry, what role that that will play in some of their policy coverage and exposures that they have.

And the last item is the majority voting initiative, which is something that we had planned on doing a little earlier in the year, but it was delayed actually because we thought it may be included in the Dodd-Frank Act. Actually, it fell out at the 11th hour.

But this is essentially a lobbying effort on our behalf. We have worked with a couple of other large institutional investors, but it's essentially our own campaign where we've reached out to U.S. companies that are in our target benchmark -- we started with the Russell 1000, or the large cap firms -- who have not adopted some type of majority voting procedure in terms of their board elections, so they have a plurality standard, which is not considered a best practice.

We fairly strongly believe that an accountable board and kind of a legitimate election process with respect to a board of directors should constitute a majority. So a majority of the shares voted and/or outstanding, depending on how the company implements it, should be the baseline requirement to allow a director to serve and represent investors on their behalf.

So we started to send out the letters in mid-August, have just completed that the last week. And we've gotten quite a bit of response actually, especially from the large cap firms, many of which have already adopted or just recently adopted majority voting. So it's so far so good.

And as the letters penetrate the smaller companies that have historically not adopted governance practices as quickly as the larger firms, we hope to have more of a dialogue and increase that outreach effort with the smaller firms.

And then the next two slides I'll cover the Dodd-Frank. Maureen mentioned that a little bit. This was passed, as you know I'm sure, it was passed in late July. Very extensive. This slide just covers some of the major generic governance items.

The next slide will cover some of the executive compensation items. And I won't go into each one of these in any detail. Proxy access will be covered in a couple of slides. But the Dodd-Frank Act has essentially allowed the SEC to have the federal authority to go forward, which they did about a month later.

Chairman/CEO disclosures, this is really just kind of an enhancement or a codification of existing SEC rules that they passed late last year. There may be some further modification to that, but that remains unknown. This is essentially requiring companies to explain why they do or do not have an independent chair position on their board. They have a CEO in that role, playing the role of the chief executive officer as well as the chairman of the board. The companies will be required to explain why, provide a rationale.

Broker discretionary voting is something we've talked about in the past. And this is really, again, an advancement of an existing reform that the SEC has worked on over the last several years. The Dodd-Frank Act essentially makes it more encompassing on executive compensation issues. So essentially, for all intents and purposes, there really are no broker votes that really cover any significant items now.

Board elections were excluded last year, and the Dodd-Frank Act now will encompass such things as say-on-pay and any significant executive compensation item before investors.

Risk committees, it's kind of yet to be determined how the Federal Reserve will deal with that and its related Sarbanes-Oxley modifications. Again, that's kind of a big unknown, how that will hit the smaller -- or the smaller companies will be excluded. How that will cover the mid cap companies is kind of up in the air.

And then finally the act essentially codified and expanded the scope of an existing investor advisory committee that the SEC had implemented about a year, year and a half ago.

The next slide covers all of the significant executive compensation items. The most notable item was say-on-pay. That probably received the most attention from investors and companies alike. And going forward sometime next year, the final rules will be put in place by the SEC. But essentially all companies will be required to put a say-on-pay item on their ballot or an advisory nonbinding shareowner ratification of a company's compensation framework.

You'll recall many companies had received proposals on this in the past if they had received TARP moneys before they were required to put a say-on-pay item. Now it essentially is market-wide. And coupled with the say-on-pay vote is what they've called the say-when-on-pay, or the frequency of which the say-on-pay vote will be conducted, and that will be put before share owners, and it remains to be seen how that will be implemented.

And there are several related disclosure items that will ultimately require some SEC work and expansion and strengthening of listing standards at the NYC or other exchanges. Probably the most notable or most significant is the clawbacks.

Compensation clawbacks are something that many of the large companies have begun to adopt recently. But the Dodd-Frank Act went much further and goes much beyond the existing practices. And essentially what will happen is if a company has a financial restatement, the most common scenario is a financial restatement and then a clawback or recoupment of any incentive payouts that may have been made to the CEO or other named executives.

What the Dodd-Frank Act does is it really strengthens the circumstances or the scenario under which the clawback must occur. It's no longer really an option. Companies will have to have a clawback policy. It will have to be meaningful, and it won't be excludable under fraud circumstances. So this will be any financial restatement, any kind of material restatement that occurs, the CEO or other senior executives will be required to pay back that compensation.

Many companies are starting to kind of move in response to this. I think we'll see more companies deferring or delaying the actual payout of long-term incentive plans to avoid the possibility that they will have to be clawed backed or recouped if there's a future restatement. And then hedging is another one. But a lot of these things are really uncertain, and we'll have to see how this SEC reacts.

Next slide. The next slide covers another very significant item. This is something the SEC has been working on for several years, proxy access or the ability of investors to actually nominate and put their own candidates for board directorship on the company's proxy. So this avoids the burden, if you will, of running a proxy contest, which is very expensive, legally very cumbersome.

There's now a federally mandated mechanism for which investors can nominate. And it's fairly narrow. It's prescribed circumstances, a three percent ownership, three percent holding requirement.

One of the key items in this that was hotly debated was whether or not investor or investors, plural, can group and aggregate their shares. Ultimately that was passed in the final rule. And that will, I think, you know, significantly change the landscape in terms of some of the activist funds, what they can do and how they work with kind of traditional long-term institutional investors, such as public pension funds and others that are not considered to be kind of short-term money.

CFO SINK: Theoretically, you and CalPERS and CalSTRS and New York and New Jersey could get together and nominate somebody to be on a board.

MR. McCAULEY: Yes, yes. Some of the members --

CFO SINK: Well, that's going to be very interesting.

MR. McCAULEY: Yes, it will, it will. Some of the members of the Council of Institutional Investors have already begun to plan work on identifying directors.

CFO SINK: Very good.

MR. McCAULEY: Kind of a database for

directors. The three percent ownership level, some view that as being kind of an onerous, very difficult threshold. I don't personally believe that will be all that difficult to hit. Not easy, but at the same time I think it will be doable, and we'll just have to see how the group dynamic plays out.

And that will be effective for most meetings next year. There's essentially a 30-day window before proxy materials have been filed that an investor or investor group can approach the company. And, of course, the SEC will weigh in and determine how this works and who can do what and when under what circumstances.

And then the last slide is just the normal voting statistics. This is essentially the same table that you saw at the last meeting. I believe the data at the last meeting was through mid or late May. This goes through the end of the fiscal year.

And we issued a press release in late July that covers some of the statistics and momentum on some of these issues a little bit more -- in more detail, but essentially the same, very much in line with year-over-year numbers. We actually did have a little bit of an uptick in the votes in favor of management and support of individual directors.

That's all I have. Any questions I'd be happy to --

GOVERNOR CRIST: Thank you.

MR. WILLIAMS: Thank you, Mike. Mindful of our time, we'll go on to Eric Nelson and a risk management and compliance report.

MR. NELSON: Good afternoon, Trustees. A couple of high level remarks. First, the SBA's compliance program is, I would say, maturing nicely at this point. We're settling in on processes across all asset classes. And the emphasis over the near term now is going to be the very unglamorous work of documenting in detail written procedures and other facets of that.

Also at a high level we've implemented a number of policy changes and enhancements recently, with the deputy executive director policies as well as executive director policies. Some of these have incorporated the Groom Law Group's ethics recommendations. Other changes pertain to the transfer of certain duties from the inspector general's role to the area of compliance, most notably personal investment activity, compliance activities. There are also other policy changes we'll touch on in a few moments.

The first issue I want to touch on is a legacy issue from our previous inspector general, and that's regarding the SEC adoption of pay-to-play rules. The SEC commissioners voted unanimously on June 30th, 2010, to adopt new rules designed to curb pay-to-play practices. New rules are set forth effective September 13th of 2010, and compliance with these rules is required by March 14th of 2011, to give advisers time to identify covered associates and implement compliance procedures around these new rules.

I'm happy to report an internal placement agency disclosure policy that we implemented last year, correctly anticipated the direction of the SEC's new rules. That is, the SEC did not ban the use of third party placement agents. Rather, the SEC required that placement agents must be registered in order to ensure that they are governed by the new pay-to-play rules, which was consistent with our adopted policy.

Additionally, our policy requires disclosure by investment advisers of compensation paid to third party placement agents. It sets forth SBA contractual requirements that require investment managers to be solely responsible for the payment of placement agent fees. The placement agent disclosure form has since been incorporated into our investment management compliance program.

The next item I have is a new conflict of interest certification that we've implemented. Among our recent policy changes was an amendment to our investment management acquisition policy that incorporates a new certification regarding conflicts of interest. The affected persons by this will be the portfolio manager from the asset class, the applicable asset class senior investment officer, the deputy executive director and the executive director, who have to certify they have no conflicts with respect to an adviser or fund that is under consideration.

Specifically, these individuals have to certify that they have no material financial interest in the adviser, material being defined as $20,000 or more, they have no relation to employees of the firm, they haven't been employed by the adviser or fund within the last five years, they have not been offered employment by that firm, nor have they discussed future employment with that firm.

This conflict certification is similar to a requirement that we've had for a number of years in our procurement policy, which requires SBA staff that serve on evaluation teams for invitations to negotiate fill out a certification that they had no conflict with ITN respondents. This conflict of interest certification is now part of the investment management compliance program for both public market and private market asset classes.

Next is an assessment that was performed, an external assessment of our disaster recovery capabilities. We retained a small D.C.-based consulting firm called BDA Global to review and determine if the SBA COOP plan, that's Continuity of Operations Program plan, provides reasonable assurance that the SBA has the ability to timely recover from a major business interruption and continue critical business functions.

The assessment included an examination of our written COOP plan, an evaluation of our alternate work group site located in Marianna, an evaluation of our alternate data center site at the shared resource center in Southwood, and an assessment of our business interruption testing procedures.

We received what I consider to be a favorable evaluation of our COOP plan. BDA stated that our plan is well constructed and effectively identifies an overall strategy for an emergency and that our alternate data center site has sufficient redundancies built in.

The consultant's report contained 31 recommendations, otherwise known as suggestions for improvement. Many of them very narrow in scope. The primary "to dos" that emanated from the report are suggestions regarding updating our business impact analysis, our critical path analysis and enhancing our disaster recovery testing, their tabletop exercises, simulations, telework tests, et cetera. The consultants report and findings was reported at the Audit Committee meeting on 9/23.

Next, the Audit Committee directed us at their meeting of August 9th to perform a review of our information security policies and practices in the context of our personal investment activity policy. The first step in that was we evaluated our confidentiality policy and incorporated numerous enhancements and additions, many related to post-transaction information handling of information that's both confidential and exempt from disclosure. This information primarily is related to alternative investment asset class.

We are currently incorporating these policy additions and enhancements into our information security awareness training program, which is a component of our annual mandatory training. We also reviewed user access to trade order management systems and subsequently determined that only appropriate asset class staff do have access to these systems and that have a legitimate need to know what is in these order management systems.

Next, we reviewed asset allocation distribution lists on our e-mail system, and we're in the process of deleting a number of folks from those e-mail distribution lists that did not have a legitimate need to know on a pre-transfer basis.

Finally, we also did some preliminary research on electronic record data vault products and will likely more formally evaluate these products in the context of a broader electronic records initiative in the near future.

I presented my review of the information security policies and presented the confidentiality policy to the Audit Committee at their meeting on 9/23.

An initiative that we're kicking off very shortly is a total fund risk system procurement.

We're intending to issue an invitation to negotiate hopefully Friday or next week. This ITN has been structured so that firms may respond with either a total fund risk system that does or does not include a hedge fund risk component or firms may respond if they only have a standalone hedge fund risk product.

Our strategy at this point in time is that this will be a complementary risk system and will not replace risk systems that currently reside in the public market asset classes, this system being Wilshire and Barra. It is contemplated right now that we will make a selection decision or possibly a decision not to procure the system in February 2011.

And finally training, I know Mr. Sweeney tried to hijack what little glory can be eked out of reporting on training, but I'll touch on a couple of things. It cannot be stressed enough how important it is, serving as a fiduciary, to ensure that the staff is adequately trained and possesses the appropriate level of expertise.

Our dedicated training development manager is working on a variety of training fronts. I'll touch on a couple of the higher level ones. We recently issued an RFQ, request for quotes, for a fiduciary training program designed to be administered to internal SBA staff, our advisory and oversight committees, as well as you, our trustees.

We selected Groom Law Group to develop and administer this fiduciary training program. We intend to offer this training program to staff this fall, whereby we will tweak the program based on feedback, and then we'll work on further scheduling with committees and trustees.

And Bill had briefly mentioned this curriculum we're building with the Intuition product. And what we have is an advisory group of seven investment professionals, are using this Intuition product, which has a very robust catalog of 250 or so classes, covering virtually the entire spectrum of investment products.

This advisory group has designed a six-level mandatory curriculum for investment staff as well as investment support staff. And right now they're on the finishing stages of taking the classes and evaluating the class applicability and relevance to SBA business and then bucketing the class in the approximate six-level curriculum.

And as Mr. Sweeney mentioned, we've had several seminars actually that have taken place, that he said were going to take place. We had Black Rock in a week or so ago. We did about a five-hour seminar on mortgage-backed securities. BNY Mellon came in and did an on-site seminar of global network documentation tax seminar issues. And we've got BNY Mellon coming in October 12th to address a -- or conduct a tri-party repo seminar.

ATTORNEY GENERAL McCOLLUM: Can I ask a question? Three or four years ago we weren't doing this type of training?

MR. McCAULEY: It was very bottom-up driven. Budget entities had training budgets, and it was somewhat in their discretion on how they utilized their resources to obtain training for their staff. What we are working on right now is putting a top-down overlay and trying to determine what skills does the organization need going forward to adequately address turnover, succession, that sort of thing.

So while we recognize that there's a need for personal, professional development plans, we also recognize the organization should set training direction and core skills that the organization deems as being important. So we're doing sort of at the moment a top-down bottom-up approach that's training curriculum building.

ATTORNEY GENERAL McCOLLUM: Thank you.

GOVERNOR CRIST: Thank you.

MR. McCAULEY: Thank you.

MR. WILLIAMS: Thank you very much. I just wanted to close it up by saying you've patiently gone through a lot of detail. You've asked a lot of good questions, and I think the facts speak for themselves. The funds are in great shape. You have a tremendously gifted and dedicated team. I want to recognize and thank all of them and thank you for your leadership.

CFO SINK: Pretty impressive. As somebody said, we've come a long way in two years. I know we have more progress.

GOVERNOR CRIST: Very well done. Thank you very much.

(Whereupon, the meeting was concluded at 3:10 p.m.)

CERTIFICATE OF REPORTER

STATE OF FLORIDA)
COUNTY OF LEON)

I, Jo Langston, Registered Professional Reporter, do hereby certify that the foregoing pages 4 through 99, both inclusive, comprise a true and correct transcript of the proceeding; that said proceeding was taken by me stenographically and transcribed by me as it now appears; that I am not a relative or employee or attorney or counsel of the parties, or a relative or employee of such attorney or counsel, nor am I interested in this proceeding or its outcome.

IN WITNESS WHEREOF, I have hereunto set my hand this 19th day of October 2010.

____

JO LANGSTON
Registered Professional Reporter