



Final Minutes  
Endowment Fund Investment Regular Board Meeting  
November 18, 2008

A regular meeting of the Endowment Fund Investment Board (Board) was held in the Board Conference Room at 816 W. Bannock Street, Ste. 301, Boise Idaho on November 18, 2008. Chairman M. Dean Buffington called the meeting to order at 9:39 a.m. and recognized that a quorum was present.

**Member's Present:**

M. Dean Buffington  
Gavin Gee  
Representative Max Black  
Vaughn Heinrich  
Tom Kealey  
Senator Brad Little  
Susan Simmons  
Richelle Sugiyama  
John Taylor

**Member's Absent:**

None

**Staff Present:**

Larry Johnson  
Chris Halvorson  
Andy Potter  
Judy Shock

**Legal Counsel:**

Julie Weaver

**Guests:**

Janet Becker-Wold, Callan  
Bill Howard, Callan  
Bob Maynard, PERSI (*absent 10:51am-1:15pm*)  
Bobby Lawrence, Eide Bailly (*departed 9:49 am*)  
James Yee, Eide Bailly (*departed 9:49 am*)  
Darla Rankin, State Controller's Office (*9:47-9:49 am*)  
Bill Reese (*10:04 am-1:45pm*)  
Donna Jones, State Controller (*11:25 am-12:30pm*)  
Scott Phillips, State Controller's Office (*11:25 am-12:30pm*)  
Corrie Keller, JRF (*12:17 pm-1:45pm*)  
Michelle Soderlund (*12:30-1:40pm*)

Hard copies of board materials were mailed and delivered six days prior to the scheduled board meeting and a meeting notice was posted on the door of the EFIB office beginning November 10, 2008.

**Board Meeting Minutes: August 19, 2008 and October 6, 2008**

Mr. Gee made a motion that the minutes of the August 19, 2008 regular meeting be approved as submitted. The motion was seconded by Mr. Heinrich and approved unanimously.

Mr. Gee made a motion that the minutes of the October 6, 2008 special meeting be approved as submitted. The motion was seconded by Ms. Sugiyama and approved unanimously

### **Independent Auditor**

Mr. Gee recused himself from any vote or discussion of this issue because of his wife's previously disclosed employment with Eide Bailly.

*Mr. Gee departed at 9:44 a.m.*

Mr. Taylor stated that 3 firms submitted proposals to be the endowments' Independent Auditor. After reviewing an analysis by staff, assisted by Darla Rankin, Deputy State Controller, the Audit Committee selected Eide Bailly as the firm to be recommended to the Board.

*Ms. Rankin arrived – 9:47 a.m.*

Mr. Kealey asked why the firm with the highest fee was recommended. Mr. Johnson replied that Eide Bailly was the only firm experienced in auditing State of Idaho agencies and therefore has a much better understanding of the strengths and weaknesses of the state's internal controls. They also had a slight edge in some less important areas and they offered to reduce fees based on time savings vs. budget.

Mr. Taylor made a motion to approve hiring Eide Bailly for the next five years of audits (FY 2009 – FY 2013). The motion was seconded by Senator Little and approved unanimously.

*Mr. Gee returned – 9:48 a.m.*

*Ms. Rankin, Mr. Lawrence and Mr. Yee departed – 9:49 a.m.*

### **School Bond Guarantee Legislation**

Mr. Johnson handed out proposed changes to Idaho Code 57-728. He indicated that Ms. Weaver is working with the Treasurer to rewrite all the school bond guarantee statutes to clarify the original intent of the statute and provide clearer guidelines and procedures. The major substantive issues in the EFIB section of the statute include:

- Listing potential administrative rules, including giving the EFIB authority to propose administrative or guarantee fees (subject to legislative review)
- Eliminating the implication that the EFIB has authority to increase the guarantee above the \$200 million approved by the legislature
- Changing the interest rate on funds loaned to the school district to 400 basis points above the 1-year Treasury rate.

The board discussed the guarantee program and the proposed statutory language. Mr. Johnson said the program essentially guarantees timely remittance of semi-annual payments. It is unlikely the fund would be required to pay off the whole debt, but instead would provide a source of funds to keep payments current until the school district is able to restructure its finances to resume payments on the debt.

Ms. Sugiyama and Senator Little pointed out that this legislation is preliminary and may be changed based on input from the Treasurer, the Superintendent of Public Schools and bond counsel. Staff will

inform board members of any material change to the proposed legislation. The board indicated its preference that the sentence specifying the degree of leverage of the endowment's \$200 million lending commitment be moved to the Treasurer's section of code.

Representative Black made a motion to approve, in concept, the proposed legislation. The motion was seconded by Mr. Heinrich and approved unanimously.

*Bill Reese arrived 10:04 a.m.*

### **International Equities - Implementation**

Mr. Johnson presented staff's recommendation for implementing the previously approved increase in international equity: move in 3 stages over the next three years:

- 1) Increase international by 3% with a stand-alone emerging markets mandate in the next six months;
- 2) Add 3.5% international as part of a global equity mandate in 2 increments one year apart.

Ms. Becker-Wold and Mr. Johnson discussed the timing of finding an emerging markets manager and performing the due diligence. Ms. Becker-Wold indicated that a hurdle to rapid implementation of either the Mid-cap Growth mandate or the Emerging Markets mandate would be the current trading limitations on the Northern index funds as a result of stress in the securities lending pools.

Ms. Sugiyama asked if the emerging markets search should be delayed to include global managers, particularly given that at the last meeting, Staff did not feel comfortable with 'how a dedicated emerging markets manager would fit with global equity managers'. Mr. Johnson noted that since then, he has been able to review the issue and is comfortable with proceeding. Ms. Sugiyama asked that Callan and staff address the issues identified at previous Board meetings, including information regarding the impact of additional currency risk. Ms. Becker-Wold indicated that Callan will be prepared to do that at the next meeting and that the first step in the recommendation, increasing emerging markets equity, would, for the most part add new currencies to the portfolio which would improve diversification and reduce volatility.

Mr. Kealey made a motion to commence a search for an emerging markets manager to be identified by next board meeting in February 2009 and to address any staff or board issues preceding the February meeting regarding the selection of emerging markets investments. The motion was seconded by Senator Little. and approved unanimously.

### **Securities Lending**

Mr. Johnson and Ms. Becker-Wold discussed the present status of securities lending. Mr. Johnson provided graphs of floating rate note spreads that showed continued deterioration of the market value of 1-2 year floating rate notes, which make up a large share of the discounted securities in the collateral pool. As a result, the unrealized loss in the pool for the three EFIB clients has grown to an estimated \$4.6 million. While Northern still expects all of these securities to mature at par, an evaluation by Clearwater implies that some securities may be at risk. In response to a question from Ms. Simmons, staff agreed to obtain an updated evaluation from Clearwater that better quantifies that risk.

Staff and Ms. Becker-Wold described restrictions on trading in the accounts tied to securities lending. Staff has asked Northern to provide an option which would allow the EFIB to move index funds to an active Mid-cap Growth manager when that search is completed.

Staff and Callan continue to closely monitor Northern Trust's securities lending programs and Ms. Weaver indicated that she is monitoring current and potential litigation against Northern related to securities lending. Ms. Becker-Wold indicated that she supports staff's recommendation to remain in the securities lending arrangements until the unrealized loss is recovered, either thru maturity of the securities or reductions in market risk premiums.

*Senator Little departed 10:50 a.m.*

*Mr. Maynard departed at 10:51 a.m.*

### **Trail of the Coeur d'Alenes Endowment**

Mr. Johnson presented a proposed management agreement for the \$2.6 million Trail of the Coeur d'Alenes Endowment, which is essentially the same as the management agreement for the Ritter Island Endowment Fund. The investment policy statement is still being drafted pending a better understanding of the income needs and risk tolerance of the beneficiary. Based on input from EFIB staff, Idaho Parks and Recreation will determine the overall asset mix as well as the timing and amount of distributions. The EFIB will produce monthly performance reports and act as investment manager for IDPR, with authority to hire and fire managers and the custodian.

The board expressed concern about investing in index funds that engage in securities lending. Staff agreed to examine non-lending options and asked the board to defer approval of hiring a custodian or investment manager until after the Investment Policy is finalized.

Mr. Kealey made a motion to approve the Investment Management Agreement for the Trail of the Coeur d'Alenes Endowment. The motion was seconded by Mr. Heinrich and approved unanimously.

*Chairman Buffington departed at 11:09 a.m.*

### **Callan Fees**

Mr. Johnson indicated that the contract with Callan provides that they may increase their annual fee by 3% after the initial 12 months upon prior written notice. When the contract was signed, staff expected that Callan would increase their fee by 3% beginning July 2008, but Callan overlooked the prior notice requirement and only notified the EFIB of the increase in early November. EFIB staff believes that in the interest of fairness, the 3% increase for July thru October (approximately \$1,700) be paid. Staff and Callan also noticed that the wording of the contract did not fit the original intent that Callan be afforded an opportunity to raise fees every year. Staff noted that even though Callan could unilaterally ask for an increase, the board has authority to terminate the contract at any time.

Representative Black made a motion to pay Callan an additional 3% retroactive to July 1, 2008 and approve a modification to the contract to clarify that annual inflationary increases of up to 3% are permitted upon written notice. The motion was seconded by Mr. Heinrich and approved unanimously.

*The board recessed for a break at 11:20 a.m.*

*Controller Donna Jones and Scott Phillips arrived at 11:25 a.m.  
Representative Max Black departed at 11:25 a.m.*

*The board resumed at 11:37 a.m.*

### **Fund Performance and Evaluation**

Ms. Becker-Wold and Mr. Howard reviewed the third quarter performance for EFIB clients.

Endowment Fund: The endowment portfolio posted a -9.3% return for the quarter ended September, 110 basis points behind its benchmark, and -14.5% for the last 12 months, 140 basis points ahead of its benchmark. Relative to peers, the fund ranked in the 68<sup>th</sup> percentile for the quarter and 44<sup>th</sup> percentile for the year relative to public funds (51<sup>st</sup> percentile for the quarter and 48<sup>th</sup> percentile for the year relative to endowments and foundations).

Judges' Retirement Fund: The JRF portfolio posted a -7.9% return for the quarter ended September, 10 basis points above its benchmark, and -14.3% for the last 12 months, 150 basis points ahead of its benchmark. Relative to public fund peers, the fund ranked in the 35<sup>th</sup> percentile for the quarter and 41<sup>st</sup> percentile for the year.

State Insurance Fund: The SIF portfolio posted a -2.0% return for the quarter ended September, even with the benchmark, and 0.8% for the last 12 months, 40 basis points above of its benchmark.

*Senator Little arrived 11:45 a.m.*

*Corrie Keller arrived 12:17 p.m.*

Ms. Becker-Wold described the reasons for underperformance by Chicago Equity and Barrow, Hanley. Staff and Ms. Becker-Wold indicated that they will continue to monitor Chicago Equity's performance very closely to ensure that there remains a reasonable likelihood of reversion to the mean in their returns.

### **EFIB Staff Reports**

Ritter Island Endowment Fund - Mr. Halvorson reported that the fund lost 15.2% fiscal year-to-date thru October and has lost 14.5% for since inception.

Market Value, Summary Expense and Coverage Ratio reports – Mr. Potter reported on the market value, expenses and the coverage ratio for the 3<sup>rd</sup> quarter. The EFIB expects to finish the year 3.8% under budget vs. a proposed holdback, from which the EFIB is exempt, of 2.5% for General Fund agencies. Thru October, the reserve funds of all endowments contained at least 3 years coverage of their distribution.

*Michelle Soderlund arrived 12:26 p.m.*

*Donna Jones and Scott Phillips departed at 12:30 p.m.*

Six Month Average Stumpage, Gift Log and Upcoming Issues – Mr. Johnson reported on the auction price of stumpage and the gift log. On December 4<sup>th</sup>, Dave Iben, CIO of Tradewinds will host a breakfast presentation meeting at EFIB at 8:30 a.m.

### **Board Compensation Legislation**

Mr. Johnson reviewed draft legislation, approved by the Governor's office, which will allow board members to be paid for official duties in addition to attending board meetings. This will make the EFIB's compensation consistent with all other boards and commissions in the state. Staff will present the proposed legislation to the Land Board in December for their information and solicit legislators, outside the EFIB, to carry the legislation in the next session.

### **Executive Session**

At 12:49 p.m., Mr. Heinrich made a motion that the board enter Executive Session pursuant to *Idaho Code §67-2345* for the purpose of personnel/agent matters *§67-2345 (1)(b)*. The motion was seconded by Ms. Simmons and approved unanimously.

*Chairman Buffington arrived at 12:48 p.m.*

The board went into Executive Session at 12:49 p.m.

The roll call vote was as follows:

Gavin Gee – Aye

Vaughn Heinrich – Aye

Tom Kealey – Aye

Senator Little – Aye

Susan Simmons - Aye

Richelle Sugiyama – Aye

John Taylor - Aye

Guests present during Executive Session:

Julie Weaver

Larry Johnson

*Representative Max Black arrived at 1:12 p.m.*

At 1:16 p.m., a motion to return to regular session was made by Mr. Gee, seconded by Ms. Simmons and approved unanimously.

### **Judges' Retirement Fund – Annual Actuarial Valuation**

Ms. Soderlund presented the annual valuation. At June 30, 2008, the plan was 82.9% funded. With the recent downturn, EFIB staff estimates the plan is now 58-60% funded. The board discussed the lack of sufficient contributions to the fund, both to cover normal costs and to retire the deficit.

*Mr. Maynard arrived at 1:40 p.m.*

The board discussed the reasonableness of the 7.5% return assumption in the valuation, options to change the asset mix, and a proposed letter to the Chief Justice.

### **Employee Recognition**

Mr. Taylor made a motion to acknowledge Andy Potter and Judy Shock with a letter of commendation for a job well done with the FY 2008 financial statements and with saving the EFIB \$3,600 annually. The motion was seconded by Ms. Simmons and approved unanimously.

### **Adjournment**

There being no further business to come before the Board, Representative Black made a motion to adjourn, seconded by Mr. Gee, and passed unanimously. The meeting adjourned at 1:50 p.m.