

IPERS INVESTMENT BOARD MEETING

December 1, 2005
IPERS Board Room

The following people were in attendance at the IPERS Investment Board Meeting that was held in the IPERS Board Room on Thursday, December 1, 2005.

Members of the Board

Bruce Kelley, Chair
Joanne Stockdale, Vice Chair
Treasurer Michael Fitzgerald
Lana Dettbarn
David Creighton
Lorie Bennett

Phyllis Peterson
Senator John Kibbie
Senator Mark Ziemann
Representative Jeff Elgin
Representative Pam Jochum

Administration & Staff

Donna Mueller, CEO
Kathy Comito, CIO
Karl Koch, Investment Officer 4
Jeff Beisner, Investment Officer 3
Keith Scholten, Investment Officer 3
Pat Reinhardt, Investment Officer 3
Muriel Godbersen, Investment Officer 1
Roger Wheatley, Internal Auditor

Julie Economaki, Public Information Officer
Greg Schochenmaier, General Counsel
Kelly Lovell, General Counsel
Bob Sharp, Project Manager
Melinda Prince, Executive Secretary
Robin Hillabolt, Secretary
Leon Schwartz, Chief Operations Officer
David Martin, Chief Benefits Officer

Consultant

Wilshire Associates
Eileen Neill
Jim Rice

Manager/Custodian

Bank of New York
David Blakeley
Mark Schafer

Benefits Advisory Committee

Janie Garr
Brad Hudson
Pat Lynch
Diane Reed
Len Cockman
Gary Walters
Gaylord Tryon
Heather Stubbe
Walt Galvin
Susan Fitzsimmon

Other Guests

Kim Dentlinger, Treasurer's Office
Shane McMahon, Principal Capital Mgmt
Dave Reichart, Principal Global Investors
Ralph Gross, Merrill Lynch
Kelly Ryan, House Republican Caucus Staff

Patrice Beckham, Milliman
Steve Timmins, Iowa Dept. of Management
Ed Cook, Legislative Service Bureau
Jill Purcell, Cost Effectiveness Management (CEM)
Jenifer Parsons, House Democratic Caucus Staff

IPERS INVESTMENT BOARD
MEETING MINUTES
December 1, 2005

Approval of Minutes of Previous Meeting – Tab 2

David Creighton made the motion to approve the minutes of the September 21, 2005 In-Service meeting and the September 22, Board Meeting. Joanne Stockdale seconded. The motion carried by unanimous voice vote.

IPERS CEO's Report – Donna Mueller – Tab 3

Donna announced that \$16.6 million in November dividends have been sent out and \$42.9 million in January dividends are scheduled to be paid. She noted that the payments are made in restricted amounts again for the third year in a row due to IPERS underfunded status. Donna reported on the Public Retirement Systems Committee meeting held at the statehouse last month. She noted that both David Creighton and Lowell Dauenbaugh spoke to the Committee on behalf of IPERS. IPERS presentations covered the system's strong investment returns, our low administrative costs and high member service performance. The presentation also included a report prepared by the Investment staff on loss of investment return based on no increase in contributions. The recommendations to the Committee were to continue to prefund benefit liabilities and to take action on this as soon as possible. There was also information on a technical bill that was filed relating to corrections and clarifications in the IPERS statute.

Actuarial Audit Search Request– Tab 4A

Donna Mueller recommended that board approve an RFP for the hiring of an actuarial auditor. She noted that the minimum qualifications proposed are stated in the board handbook. She noted that a safeguard was added that the firm hired to do the audit would not be eligible to bid on any retainer actuarial consultant RFP that would result if significant errors are found. This audit will include both FY'05 valuation and the experience study to be presented at the September '06 meeting. Motion made by Joanne Stockdale to approve the RFP for an actuarial audit and to approve the minimum qualifications. Lori Bennett seconded. The motion carried by unanimous roll call vote. Board Members Lana Dettbarn and Bruce Kelley volunteered to serve on the committee to engage in the search process.

Staff Reports – Tab 5A

Kathy Comito noted the estimated market value as of November 18 was approximately \$19.3 billion. All asset classes are within their target ranges with only one exception, private equity. This asset class market value, although below the minimum of its target range, has increased recently due to large valuation increases. Unfortunately, such valuation increases are usually a precursor to a flood of distributions.

Consultant and Manager Watch List – Tab 5B

Wilshire continues on the list until a re-evaluation in February of next year. RCM is being removed from the list. Jeff Beisner and Eileen Neill both noted they were impressed by the amount

of analysis this firm has done over the last couple of years to retool their staffing and investment process.

Wilshire Associates Consulting Service to IPERS – Tab 6

Kathy Comito outlined the history of Wilshire's placement on the Watch List, noting in particular the 2004 departure of head of the consulting division. There was also structural reorganization at Wilshire in 2004. They continue to be on the watch list in order to evaluate a new structure and process for consulting team service to individual clients like IPERS. Also discussed were service shortfalls that staff reported to Wilshire management during the recent annual Wilshire client satisfaction survey. Staff reported that Wilshire has been very responsive to date to IPERS' identification of service shortfalls

Bank of New York Settlement with U.S. Attorney's Office – Tab 7

Treasurer Fitzgerald reported on the recent settlement by Bank of New York with the U.S. Attorney's Office. The Bank has agreed to pay \$38 million to settle criminal investigations involving fraudulent activities between 1996-1999. Treasurer Fitzgerald stated that the case was against the retail banking side of the bank's operations and there were no pension funds involved. Mark Schafer from Bank of New York assured the board the bank has taken measures to put in place a new compliance group and investigative group. The Treasurer stated that there was full disclosure and this case was discussed before the initial contract (2002) contract was awarded to Bank of New York.

Risk Budgeting – Tab 8

Eileen Neill outlined a process for risk budgeting. In IPERS public equity markets asset class returns have not met the system's stated expectations for the last five year period. Five issues were proposed for approval; adoption today of the proposed active risk targets for each of the public asset classes, seek approval of the domestic equity restructuring analysis, approval for evaluation of the feasibility of implementing a customized unbundled approach of portable alpha which would add six to nine months on the time line as stipulated, and suggest putting off the index funds provider rebid until after the international and domestic restructuring analysis. David Creighton made a motion to approve the recommendations. Joanne Stockdale seconded. The motion carried by unanimous roll call vote.

Defined Benefit Investment Cost Effectiveness Analysis – Tab 9B

Jill Purcell gave a report based on the calendar year 2004. The five year policy return was 3.8%, which is above the US median of 3.2% and above the peer median of 3.0%. IPERS five year Implementation Value Added was 0.4%, which compares to the US median of 0.8% and peer median of 0.8%. IPERS had a five year Implementation Risk of 2.0% which compares to the US median of 1.5% and the peer median of 0.8%. The total cost of 28.4 bps was below the benchmark cost of 38.5 bps. This is due to the avoidance of fund-of-fund for venture capital/LBO and because the Fund paid less for most services. For 2004, IPERS was in the negative value added, low cost quadrant of the Cost Effectiveness Chart and the five year performance placed the Fund in the positive value added, low cost quadrant.

IPERS Investment Management Cost Review – Tab 9A

Karl Koch gave an annual investment management cost review focusing on the fiscal year that ended in June. He noted the purposes of this review including the fiduciary responsibility to conserve the assets of the Trust Fund. This examination will also determine if costs are reasonable for IPERS' asset allocation and portfolio structure. It will also check the compliance with Iowa Code section 97B7 which places a 0.40% limit on investment management expenses in any fiscal year. These objectives have been met. IPERS' investment management costs were 27 basis points for FY'05

Fixed Income Portfolio Review and Recommendations – Tab 10

Jim Rice from Wilshire presented a review of the fixed income capital market. Keith Scholten provided an overview of IPERS' fixed income structure and strategy. He noted that overall the fixed income portfolio is performing well, with a one-year return of 4.05%, beating its benchmark by 67 bps. During the year ending September 30, 2005, one core plus manager (J.P. Morgan) was terminated and another (Principal) hired. A high yield manager has been added for capacity reasons. Long term performance has been good with a ten-year return of 7.15% exceeding the benchmark by 45 bps and no changes are being recommended at this time. Motion made by Lana Dettbarn that no changes be made in the fixed income portfolio at this time. Treasurer Mike Fitzgerald seconded. The motion carried by unanimous roll call vote. Peterson absent.

CY '05 Commitment Approval – Private Equity – Tab 11A

Karl Koch reviewed the policy for the maximum commitment amount that can be made by Pathway for the private equity portfolio for the upcoming calendar year. IPERS staff recommends the Investment Board approve \$562 million as the maximum dollar amount that can be committed by IPERS to private equity investments in the calendar year 2006. Motion made by Joanne Stockdale to approve IPERS staff recommendations for private equity investment. Lori Bennett seconded. The motion carried by unanimous roll call vote. Peterson absent.

CY '05 Commitment Approval Real Estate – Tab 11B

Pat Reinhardt covered the reasoning behind the staff recommendation for real estate investment commitments. IPERS staff recommends the Investment Board approve \$359.2 million as the maximum dollar amount that can be committed by IPERS to real estate investment in calendar year 2006. Motion made by David Creighton to approve IPERS staff recommendations for 2006 real estate investment. Lana Dettbarn seconded. The motion carried by unanimous roll call vote. Peterson absent.

Bridgestone Securities Litigation

David Creighton moved to go into closed session to discuss matters in litigation under Iowa Code Section 21.5(1)(i)(c). Joanne Stockdale seconded. The motion carried by unanimous roll call vote. Peterson absent.

Upon a return to open session Joanne Stockdale moved that IPERS file to become lead plaintiff in the case against Bridgestone/Firestone in the event that the current lead plaintiff is removed. Treasurer Mike Fitzgerald seconded. Motion carried on a five to one vote with affirmative votes

cast by Kelley, Stockdale, Treasurer Fitzgerald, Dettbarn and Bennett, and a negative vote cast by Creighton..

FY'05 IPERS Actuarial Valuation Report – Tab 12

Pat Beckham discussed the reasons for an Actuarial Valuation: there is a lower cost by funding the benefit structure on an actuarial basis, it provides benefit security and it provides for equitable treatment for members, employers and taxpayers. IPERS' funded ratio at June 30, 2005 was 88.6%, up slightly from the prior year's ratio of 88.62%. IPERS' unfunded actuarial liability at June 30, 2005 was \$2.289 billion, up from the prior year's \$2.176 billion. Her observations of the long term funding is that the system is not fully funded per IPERS Funding Policy and the system is not in actuarial balance. Despite favorable investment experience, funding challenges still exist. Her projection is that even if all actuarial assumptions are met, funded status will decline. Changes in the contribution rate and/or benefit structure are needed to return to actuarial balance. The shortfall between actuarial required and statutory contributions will continue to increase the unfunded actuarial liability. Her recommendation is to continue to monitor closely and encourage action.

Staff Reports – Tab 13

Board Educational Update – Tab 10A – Keith Scholten

Keith reviewed several upcoming seminars that would be appropriate for Board members as outlined in Tab 10A.

Benefits Update – Tab 10C – David Martin

David Martin gave a report on the situation at the Laverne Community School District where there were questions regarding the retirement status and re-employment earnings of two individuals.. The results of the State Auditor's report on this situation were forwarded to the County Attorney in Kossouth County, the Department of Revenue and Finance, Social Security Administration and Iowa Attorney General's office for further action.

Confirm Next Meeting Date and Adjournment

The next meeting date of the IPERS Investment Board will be March 31, 2006. The meeting adjourned at 2:47 p.m.