

**BWC Board of Directors  
Investment Committee  
Thursday, August 28, 2008, 12:00 p.m.  
William Green Building  
Neil Schultz Conference Center  
30 W Spring St, 2nd Floor (Mezzanine)  
Columbus, Ohio 43215**

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Members Present:            Robert Smith, Chairman  
                                 Alison Falls  
                                 Larry Price  
                                 David Caldwell  
                                 James Harris  
                                 William Lhota, ex officio

Other Members Present:    James Hummel  
                                 Jim Matesich  
                                 Kenneth Haffey  
                                 Thomas Pitts  
                                 Chuck Bryan

Members Absent:            None

**CALL TO ORDER**

Mr. Smith called the meeting to order at 12:15 pm.

**ROLL CALL**

Roll call was taken. All committee members were present.

Introductory comments were made by Mr. Smith regarding the development of the Investment Policy Statement. There may be a revision of the Investment Policy Statement in the third quarter of 2008. Mr. Smith indicated that the first stage in the four-step review process of the Investment Policy Statement has been completed. The Deloitte Touche and Oliver Wyman reports have been addressed.

**APPROVE MINUTES OF THE JULY 24, 2008 MEETING**

Motion was made by Mr. Price, seconded by Ms. Falls as follows: that the minutes of the July 24, 2008 be approved as written. Roll call was taken and the motion passed 6-0.

There was discussion of the revised agenda provided for this meeting.

## **NEW BUSINESS / ACTION ITEMS:**

### **ALTERNATIVE INVESTMENT OPTIONS UPDATE FOR PUBLIC WORK-RELIEF EMPLOYEES' FUND AND MARINE INDUSTRY FUND**

Bruce Dunn, Chief Investment Officer, led a discussion regarding State Street Global Advisors and the status of the applicable Request for Quote for an Intermediate Duration U.S. Fixed Income Commingled Passive Index Manager for these two trust funds. A handout provided by Mr. Dunn updating the RFQ process is incorporated into the minutes. Mr. Dunn indicated that three pages numbered six through eight have been added to this RFQ process summary report since it was initially presented at the April 2008 meeting. Page six of this RFQ report summarizes the additional information obtained and discussed with the Investment Committee in each of the May, June and July 2008 meetings. Mr. Dunn reemphasized that it was learned by the Investment staff subsequent to the April, 2008 RFQ approval of Barclays Global Investors as recommended manager that Barclays utilizes derivatives in the management of the securities lending cash collateral pool for this mandate that would be in violation of the Investment Policy Statement. Furthermore, Barclays use of derivatives in the management of its securities lending collateral pool includes derivative types such as swaps, including synthetic swaps, that the Board has previously indicated it would not be comfortable with. Mr. Dunn indicated that although State Street is authorized to use derivatives in its commingled fund management charter, State Street has never used derivatives in the management of commingled assets to this intermediate duration fixed income mandate and has not used derivatives for securities lending activities for the past eleven years.

### **APPLICABLE DERIVATIVES EDUCATION**

Mercer Consulting provided an educational session on derivatives. Guy Cooper and Kristin Finney-Cooke provided detailed analysis of derivatives. The education included discussing what derivatives are and how they are used.

Mr. Matesich arrived at 12:30 pm.

The value of a derivative is derived from something else. The derivative has a fixed life, and is bought on margin (not paying full price). There was discussion of derivatives markets. There was discussion of types of derivatives. There was further discussion with regard to the authorization for limited use of derivatives. Mr. Price inquired as to the details of futures contracts, as did Mr. Hummel and Mr. Harris. There was much discussion in detail with regard to futures contracts. Lengthy discussion was made of various uses of derivatives. There was a general warning made by Mr. Cooper with respect to an investor that is appearing to hedge, but is actually speculating in the market. Mr. Smith inquired as to "controls" that are utilized to detect speculating. Mr. Cooper indicated that there are controls that can be used such as limits, internal audit procedures, and having several different individuals monitor activity. There was discussion of effective hedging. There was discussion of vigilance with regard to the number of contracts an institution owns. Mr. Dunn provided further discussion on this matter, as the management of derivatives contracts must be closely monitored on a daily basis. There was robust discussion on the risks associated with derivatives, as well potential rewards.

Discussion was made of the types of derivatives used by other plans. Discussion was made by Ms. Finney-Cooke of a research survey performed by Mercer with regards to the types of derivatives allowed by eighteen other public pension funds, including four Ohio state pension funds. This handout is incorporated into the minutes. All public plans provided in this survey make use of securities lending and derivatives. Most all plans utilized futures contracts. Mr. Smith inquired as to how widespread and prevalent derivative use was. Mr. Cooper and Ms. Finney-Cooke indicated such derivatives use is very prevalent and widely accepted. There was also a general acceptance that a controlled use of derivatives is a best practice among public pension funds.

Mr. Haffey and Mr. Dunn thoroughly discussed the layers of risk management required to protect against speculation. Mr. Dunn indicated that internal control “Check points” are typically in place by large investment management firms such as State Street and Barclays to prevent rogue trading in excess of prescribed imposed internal limits for derivatives contracts. Ms. Falls discussed when dealing with institutions, controls are very important. The Bureau must deal with an organization of size and substance that will stand behind internal controls.

The Bureau staff recommendation is to change from Barclays Global Investors to State Street Global Advisors as the recommended RFQ Finalist to serve as the investment manager for this investment mandate for the two referenced trust funds. State Street has an outstanding record in the management of its securities lending activities since 1974. Mr. Smith inquired as to how the Bureau would discover derivative usage. Mr. Dunn indicated that there is a longstanding relationship with State Street and that State Street is expected to inform the Bureau of any such derivatives usage. Nevertheless, such derivatives usage would be detected by the Bureau investment staff through due diligence and regular monitoring, including the review of detailed monthly portfolio reports provided by the manager. .

**PROPOSED INVESTMENT POLICY STATEMENT MODIFICATION  
(SECTION IV.C.vii ON DERIVATIVES and Section IV.C.ix.b ON GENERAL  
PROHIBITIONS) FOR DISCUSSION**

A multitude of resources and discussion was utilized in today’s committee meeting, including an educational package prepared by Mercer Consulting entitled Overview of Derivatives, a research survey prepared by Mercer Consulting entitled Strategies Utilized by Other Plans, and the Intermediate Duration U.S. Fixed Income Commingled Passive Index manager Request for Quote process summary report presented by Mr. Dunn as Bureau chief investment officer. These materials are incorporated into the minutes by reference.

Revisions of language to the Investment Policy Statement have been drafted by Mercer Consulting in consultation with Mr. Dunn. Such recommended revisions parameters for using derivatives as a risk control measure for futures contracts. Ms. Falls indicated that

the educational session had been very informative. The reputation of the peer groups is outstanding. At this point, Ms. Falls expressed that she is comfortable with regard to making this major investment policy revision, She suggested one additional change to the revised language proposed for Section IV.C.vii that would insert the words “passive indexed” preceding “investment managers” in the first sentence of the paragraph numbered one. Ms. Falls emphasized that these modifications are not a major policy change due to the limited scope defined for the use of derivatives. Mr. Price emphasized that the Bureau needs to be able to get out of derivatives when necessary.

Motion was made by Mr. Smith, seconded by Mr. Harris, as follows: that the Investment Committee of the Workers’ Compensation Board of Directors recommend to the Board that it amend current section IV.C.vii. and current section IV.C.ix.b. of the statement of Investment Policy and Guidelines, as amended to permit the conservative and controlled use of derivatives by the funds or their investment managers. The exact changes adopted as a result of this motion will be incorporated in the minutes of this meeting of the committee. Roll call was taken and the motion passed 6-0.

Motion was made by Mr. Smith, seconded by Ms. Falls, as follows: that the Investment Committee of the Workers’ Compensation Board of Directors recommend to the Board that it rescind its April 2008 approval of Barclays Global Investors as the Bureau’s Intermediate Duration U.S. Fixed Income Commingled Passive Index Manager for both the Public Work Relief Employees’ Fund and Marine Industry Fund, for the reasons set forth in the Memorandum dated August 28, 2008. Roll call was taken and the motion passed 6-0.

Motion was made by Mr. Smith, seconded by Mr. Harris, as follows: that the Investment Committee of the Workers’ Compensation Board of Directors recommend to the Board that it approve State Street Global Advisors as the Bureau’s Intermediate Duration U.S. Fixed Income Commingled Passive Index Manager for both the Public-Work Relief Employees’ Fund and Marine Industry Fund, for the reasons set forth in the Memorandum dated August 28, 2008, and upon such terms as are outlined in State Street’s response to the request for quote issued March 11, 2008 and such other terms as are favorable to the Bureau. Roll call was taken and the motion passed 6-0.

## **DISCUSSION:**

### **MONTHLY TO DATE PORTFOLIO VALUE COMPARISONS**

Portfolio comparisons were discussed by Mr. Dunn. Ms. Falls raised the issue of exposure to Fannie Mae and Freddie Mac. Mr. Dunn indicated there is a current three million dollar market value exposure regarding common stock ownership of these two companies. There is significant fixed income ownership exposure to these two companies totaling approximately \$625 million in current market value.

## **SECOND QUARTER 2008 PORTFOLIO PERFORMANCE**

Mercer Consulting provided a discussion of portfolio performance with emphasis on second quarter 2008 . A handout is incorporated into the minutes. Discussion was made of performance benchmarks. Discussion was made within the context of the economic environment.

## **CIO REPORT**

The report was provided by Mr. Dunn. Discussion was made of Investment Division goals. Request for proposals, selection of managers, staffing, and training matters were discussed. Mr. Dunn indicated that the Investment Division now has six chartered financial analysts, as Assistant Investment Manager Roy Charles passed the level 3 exam. Internal investment procedures were discussed, as was the Mellon system, and the sales of remaining miscellaneous assets the Investment Department intends to liquidate. These miscellaneous assets had a twelve million dollar carrying market value represented at the end of July 2008.

Motion was made by Ms. Falls, seconded by Mr. Harris, to adjourn the meeting at 2:00 pm. Roll call was taken and the motion passed 4-0. Mr. Lhota and Mr. Caldwell had left the meeting just prior to the motion.

Prepared by: Thomas Woodruff, Staff Counsel  
August 28, 2008