

WORKERS' COMPENSATION BOARD OF DIRECTORS

INVESTMENT COMMITTEE

**WEDNESDAY, SEPTEMBER 26, 2007, 12:00 PM
WILLIAM GREEN BUILDING
THE NEIL SCHULTZ CONFERENCE CENTER
30 WEST SPRING ST., 2ND FLOOR (MEZZANINE)
COLUMBUS, OHIO 43215**

Members Present: Robert Smith, Chairman
Alison Falls, Vice Chair
David Caldwell
James Harris
Larry Price

Scribe: Tom Sico

CALL TO ORDER

Mr. Smith called the meeting to order at 12:20 PM and the roll call was taken.

MINUTES OF AUGUST 24, 2007

The minutes were approved with paragraph 5 on page 5 modified to reflect that the drafting process of the Investment Policy be left to the Chief Investment Officer and the investment consultants.

NEW BUSINESS / ACTION ITEMS

Investment Committee Charter

Ms. Falls led a discussion regarding the draft contained in the Investment Committee meeting materials for September 26, 2007. A recommendation was made that the Investment Committee be limited to five people. A recommendation was made that paragraph three of "Responsibilities and Authority" section of the Charter to change the word "counsel" to "consultant." Paragraph nine of "Responsibilities and Authority" was recommended to be change the word "approve" to "recommend to Board for approval." A recommendation was made to add a paragraph indicating that the Investment Committee would coordinate with the other two committees on items of common interest. The recommendations were approved by a unanimous roll call vote.

Investment Consultant

Mark Brubaker from the current investment consultant, Wilshire Associates, introduced himself to the members of the Investment Committee. Following this introduction, he excused himself from the room so that the Committee could discuss the contract for the investment consultant. Bruce Dunn, Chief Investment Officer, provided background information concerning the investment consultant to the Committee. Mr. Dunn discussed

the terms of the current contract with Wilshire. He explained that the current contract had been signed by the Administrator, but that the investment consultant acts on behalf of the Board of Directors. The contract is a one year contract with two one year renewal terms. Currently BWC is in the first one year renewal. Within the terms of the contract, there is a clause permitting the Board to terminate the contract for convenience. In order to exercise this clause, the Board would need to provide thirty days advance notice to the consultant to terminate services. Mr. Dunn indicated that it would also take three to four months to obtain the services of a new investment consultant through the request for proposal (RFP) process. Mr. Dunn recommended continuing the consulting services with Wilshire Associates, at least until such time as a new consultant would be retained. The issue of whether or not Wilshire should continue as investment consultant was discussed. It was suggested that Wilshire's contract be extended for an additional one year, but also issue an RFP for a new consultant in the near future. It was determined that this issue should be revisited at the next meeting of the Investment Committee in October.

Custodial Structure

Mr. Dunn discussed the difference between holding investment accounts in commingled and separate accounts. Commingled accounts pool the assets of various clients with similar investments. A separate account structure keeps the investments of a client separate from any other client. Currently, BWC investments are held in separate accounts for investment management and custodial purposes. However, the investment management fees are higher for separate accounts than for managed accounts under a commingled structure. **Mr. Dunn presented an investment analysis prepared by the Investment Division that estimated combined investment management fee savings, offset by slightly higher custodial fees, could be approximately \$1.7 million on an annualized basis. These estimated savings could result if all existing passively managed investment assets (currently 100%) were converted to a commingled management structure.**

Mr. Brubaker from Wilshire Associates also provided input. He stated that voting by proxy cannot be done through the commingled fund structure. Wilshire provided two memorandums comparing the commingled fund structure and the separate account structure.

It was noted that the Treasurer of the State of Ohio has previously recommended that the invested assets of the BWC trust funds be held in separate accounts. However, no one from the Treasurer's Office was present to provide any additional explanation. Mr. Smith indicated that he is in favor of commingled funds investment, as is Ms. Falls. It was determined that this issue may be revisited at the next meeting of the Investment Committee in October. If this issue becomes an Agenda item at the October Investment Committee meeting, an invitation to attend this meeting will be made to the Treasurer of the State of Ohio.

Investment Policy Recommendation regarding Long Duration Fixed Income Benchmark

Mr. Dunn explained that BWC's investment strategy has previously been set to target a 54% allocation to Long Duration Fixed Income (LDFI) assets. As part of this strategy, the widely recognized Lehman Long Government/Credit (LLGC) Index recommended by

the BWC Investment Consultant (Wilshire) was approved for use as the benchmark index for the LDFI assets of BWC in July 2006 by the former BWC Investment Committee and Workers' Compensation Oversight Commission. Ms. Falls noted that for popular and widely used fixed income benchmarks, Lehman Brothers is the leading provider in the fixed income area. Mr. Dunn then explained that parts of the LLGC index did conflict with the BWC investment policy statement (IPS). Specifically, the LLGC index had a portion of its representation in non-US government debt issues. Because the IPS prohibited foreign government debt, this index conflicted with BWC's investment policies. In response, a customized LDFI benchmark was developed with Lehman Brothers by Mr. Dunn to reflect the specific restrictions of the IPS. Mr. Dunn indicated this customized benchmark was adopted as the LDFI benchmark of BWC in March 2007, just prior to BWC assets being transferred to its two approved LDFI asset managers effective April 1, 2007. Mr. Dunn mentioned that over a 1,3,5 and 10 year comparative period ending July 31, the widely accepted LLGC index provided consistently higher returns than the customized LDFI benchmark index. Mr. Dunn made the recommendation that the conventional LLGC index serve as the new LDFI benchmark index for BWC, with the intent that the IPS be modified to permit investments consistent with the LLGC index.

The Board members then discussed whether or not BWC investment funds should be invested in foreign governments and/or foreign corporations which are both part of the conventional LLGC index. The discussion included the subject of fiduciary responsibility to invest funds in a manner that yields the greatest return, as well as issues of social responsibility.

Motion was made BUT NOT seconded to recommend to the Board to adopt the LLGC index as the long duration fixed income benchmark index, and to amend section V.A. of the IPS. As a result of the motion not being seconded, there was no further discussion or vote.

Temporary Waiver of Appendix XV of the IPS

Mr. Dunn requested a temporary waiver of Appendix XV regarding the schedule of required reports to be made by the Chief Investment Officer. Mr. Dunn requested a list of reports that would be appropriate for him to make at the October meeting. A motion was made, and seconded to recommend to the board to remove the requirements of Appendix XV of the IPS regarding the schedule of reporting by the CIO. The motion was passed unanimously.

DISCUSSION ITEMS

Wilshire presented its recommendation that BWC maintain a long term orientation and utilize an asset mix with a minimum equity allocation target of twenty percent. An asset mix with a minimum of twenty percent equities for balance between long term growth of the surplus and surplus preservation over intermediate time horizons was discussed. Mr. Smith raised the issue as to what is the Committee's risk tolerance, in addition to the issue of reducing premiums required to keep Ohio competitive. Wilshire explained that it

takes a forward looking view of market expectations. Wilshire also looks at efficient frontiers for recommended investment strategy. Mr. Smith emphasized that everything was foundational to what would eventually be presented to the Board.

Mr. Dunn presented on portfolio performance. In particular, Mr. Dunn pointed out that July and August were good performance months with fixed income asset performance being strong. The major asset transitions occurring in 2007 were mentioned. Mr. Dunn also mentioned that proposed House Bill 79 provides specification of permitted investments for BWC. If this legislation is passed by the respective bodies of the Ohio Legislature, its investment standards would be implemented.

A motion to adjourn was made, and seconded, unanimously approved at 2:45 pm.