

VERMONT STATE EMPLOYEES' RETIREMENT SYSTEM

Meeting of the Board of Trustees

June 29, 2005

Members present:

WARREN WHITNEY, Chairperson, VSEA member (term expiring September, 2006)
JEB SPAULDING, Vice-Chairperson, VT State Treasurer
WILLIAM HARKNESS, VSEA member (term expiring September 2005)
ROBERT HOOPER, VSEA member (term expiring September 2006)
DICK JOHANNESSEN, Governor's Delegate
STEVE GOLD, Representing LINDA McINTIRE, Commissioner of Human Resources
JAMES REARDON, Commissioner of Finance & Management

Members absent:

LINDA McINTIRE, Commissioner of Human Resources
JANICE ABAIR, Retired Vermont State Employees' Association

Also attending:

Catherine Simpson, VSEA member Alternate (term expiring September 2005)
Donna Holden, Board Coordinator
Cynthia Webster, Director of Retirement Operations
David Minot, Director of Finance and Investments
Bill Rice, Director of Law and Policy
Elizabeth Pearce, Deputy State Treasurer
VEDA/VOF Representatives

The Chairperson, Warren Whitney, called the meeting to order at 8:09 a.m. on Thursday, June 29, 2005, in the Treasurer's Office, 133 State Street, Montpelier, VT.

ITEM 1: Approval of minutes for June 9, 2005

On a motion by Mr. Harkness seconded by Mr. Hooper, the Board voted to approve the minutes of June 9, 2005, as submitted. Mr. Harkness, Mr. Hooper, Mr. Whitney, Mr. Spaulding, and Mr. Gold, voted yes. Mr. Reardon and Mr. Johannesen abstained.

ITEM 2: Discuss/Act on VEDA/VOF Alternative Investment

Jo Bradley and Peter Cline joined the meeting. Mr. Minot reviewed the Vermont Opportunity Fund (VOF) investment and partnership program proposal and June 20, 2005, NEPC recommendation memo. Mr. Minot explained the question before the Board was whether to approve a "soft circle" or investment "letter of intent" in an amount between \$500K to \$1M. Mr. Minot cautioned the Board depending on SBIC licensing requirements; a letter of intent could result in an actual deposit of funds to prove funding and secure licensing. The Board was further advised the 10-year partnership, projected a 12-15% return target based on \$18-\$24 million invested in 20-25 companies over five years, and had VEDA backing, however, investments would not be limited to Vermont, with the goal of the fund to produce returns for the investors.

Mr. Spaulding disclosed that he is also a statutory member of the VEDA Board and that he didn't believe this presented an inappropriate conflict, but he would refrain from further participation if any Board members were concerned about a potential conflict.

The Board discussed their experience and lack of reward from participation in other venture capital funds. Mr. Minot advised of the system's 3% asset allocation the balance in remaining venture investments was minimal even with an allocation to the VOF fund.

Mr. Johannesen asked whether anyone knew the Governor's position regarding investments in this fund. Mr. Spaulding advised that both the Legislature and Governor originally supported the VOF concept, which promoted business and employment in Vermont. Mr. Reardon and Mr. Gold agreed and concurred with Mr. Spaulding that they were not aware of what the Governor's current position is with respect to investment in this particular Fund by the State's pension Board.

Mr. Whitney advised the Board there appeared to be three paths of action; vote to approve a tentative commitment, vote not to invest in the fund, or table action to a later date. Discussion ensued. The Board acknowledged, as fiduciaries, participation should not be limited to VT, and questioned whether the expanded targeted investment vehicle would require Attorney General and Secretary of Administration approval.

Mr. Reardon asked whether a stipulation to the investment strategy could be applied giving extra emphasis to marketing for companies in Vermont?

Mr. Hooper made a motion to table action on the item until the next meeting. The motion failed due to a lack of a second.

The Board further discussed the proposed investment type and associated risks, poor track record of the Fund's principals, below median historical performance of previous and existing venture capital investments, and VEDA's involvement in the current proposal. Mr. Cline advised the Board that VEDA would be a limited partner only, and would have no investment committee decision-making power.

Mr. Gold made a motion seconded by Mr. Reardon, to move forward with a \$500K investment letter of intent, which would include appropriate contingencies approved by the Board and a condition that best efforts to support businesses in Vermont would be applied.

Mr. Whitney asked for a friendly amendment to add "and upon approval by the Attorney General's and Secretary of Administration Offices.

The Board reviewed, discussed, and agreed to all of the recommended stipulations listed in a June 27, 2005, e-mail from Mr. Minot:

1. - Investor's review and acceptance of the Limited Partnership Agreement and related legal documents; and
2. - receipt of similar commitments which together with the VSERS commitment would total a minimum amount, currently slated at \$5 million for both the \$2 million of Series B

interest and other limited partners' series A (the VSERS investment would be Series A) interest.

3. - Key Man Risk: Investors would have the ability to stop funding if the participation of either manager of the General Partner (Michael Sweatman or Peter Cline) were to terminate.
4. - A free flow of information between the SBA and Limited Partners would be allowed.
5. - VOF will present a business management plan to VSERS (similar to what is given to the SBA) demonstrating that the General Partner can operate effectively given the proposed level of funding, organization costs and fee structure.
6. - The Limited Partners would have the ability in response to poor future performance to terminate additional Partnership draw downs and investing with a two-thirds vote. There would also be a test of the ratio of LP current value to funded capital -- if this were to get low enough, Partnership draw downs and investing could also be terminated.
7. - While obvious, obtaining an SBIC license is a condition of investment.
8. - The Partnership must achieve its first closing of limited partnership funding no later than a certain date, certainly in this calendar year.
9. - Organizational expenses must not exceed a defined amount, certainly no more than the \$400,000 shown in the Private Placement Memorandum.
10. - There shall be no material adverse disclosures regarding the performance of Green Mountain Capital LP or MerchantBanc LLC (investment partnerships with current or prior involvement of the management) prior to closing.

On a vote of 5 to 2, the Board voted to approve the original motion made by Mr. Gold seconded by Mr. Reardon, with the friendly amendment to move forward with a \$500K investment letter of intent, which would include appropriate contingencies approved by the Board (as listed above) plus additional conditions that best efforts to support businesses in Vermont would be applied, and upon approval by the Attorney General's and Secretary of Administration Offices. Mr. Gold, Mr. Reardon. Mr. Johannesen. Mr. Spaulding, and Mr. Harkness voted yes. Mr. Hooper and Mr. Whitney voted no.

Staff of the Treasurer's Office was directed to follow-up with the letter of intent, which was to include the 12 contingency points discussed.

Mr. Harkness left during the next item.

ITEM 3: Discuss/Act on RMK Timberland Options

Mr. Rice provided the Board with a historical review of the issues regarding RMK. He said the original 10-year contract between the VSERS and the Contractor would expire in July 2005. In May 2005 representatives of RMK presented the Board with two amendment proposals, #1 to extend the relationship for 6 years affording the Contractor ability to participate in a wetland mitigation opportunity, and #2 allow RMK to resolve a stockholder violation issue.

As follow-up to Board action in May, Mr. Rice briefed the Board on numerous communications with Mr. Williams of RMK, and the lack of any response from the other Fund investors regarding the contract amendment proposals. The Board also reviewed an NEPC memo dated June 23, 2005, opposing approval of either of the amendment proposals.

The Board reviewed their options to: Vote to approve one or both amendments, Vote to reject one or both proposals, ask the Attorney General to contact shareholders, or do nothing and the prudence of that lack of action.

On a motion by Mr. Spaulding seconded by Mr. Hooper, the Board unanimously voted not to support either of the proposed amendments, advise the Contractor to proceed with the orderly liquidation of investments, and to notify other investment shareholders of the State of Vermont decision.

Mr. Harkness returned during the next item.

ITEM 4: Any other business to come before the Board

Ms. Pearce reported that three RFP responses were received and upon review Great-West Retirement Services was judged to be the most responsive to the needs of the system. Ms. Pearce explained the current SDIA administration involved a three-way partnership between the current record keeper, fund custodian, and Treasurer's Office staff. She said the goal of the third party administration was to consolidate services, and provide "one-stop-shopping" for SDIA Plan participants. The Board referred to a June 15, 2005 cost analysis prepared and previously distributed by Mr. Minot.

On a motion by Mr. Reardon seconded by Mr. Johannesen, the Board unanimously voted to direct the Treasurer's Office to enter into contract negotiations with Great-West Retirement Services for the purpose of providing full-service, third party administration for the SDIA Plan.

Next Meeting Dates:

The VPIC meeting is scheduled for July 12, 2005.

The next scheduled disability conference call meeting is July 14, 2005

Adjournment:

On a motion by Mr. Spaulding seconded by Mr. Reardon, the Board unanimously voted to adjourn at 10:25 p.m.

Respectfully submitted,

Donna Holden, Board Coordinator for
Cynthia Webster, Secretary to the Board