

New Jersey State Investment Council

July 27, 2017 Regular Meeting

Minutes of the Regular Meeting

Held July 27, 2017 at the Trenton War Memorial, George Washington Ballroom, 1 Memorial Drive, Trenton, New Jersey.

Council Members in Attendance:

Brendan T. Byrne, Jr., Chair
Adam Liebttag, Vice Chair
Michael Cleary
Charles Dolan
Michael Greaney
James Hanson
Guy Haselmann
James Joyner
Timothy McGuckin (via telephone)
Brady Middlesworth
Jeffrey Oram
Eric Richard
Mitchell Shivers
Edward Thomson

Roll Call and Meeting Notice

The Regular Meeting was called to order by Brendan T. Byrne, Jr., Council Chair, at 10:13 a.m. Ernestine Jones-Booker, Council Secretary, reported that notice of the Regular Meeting, scheduled for July 27, 2017, was posted on the website of the Division of Investment (Division); faxed to the Times of Trenton, the Bergen Record, and the Courier Post; and e-mailed to the Secretary of State on June 20, 2017. A copy of the notice was posted at the Division and is on file. Ms. Jones-Booker performed roll call and reported that a quorum of the Council was present.

Mr. Byrne welcomed Brady Middlesworth as a representative of Police and Fire Retirement System (PFRS) and Edward Thomson as representative of Public Employees Retirement System (PERS).

Minutes of the Regular Meeting held May 24, 2017

Mr. Byrne presented for adoption the minutes for the regular meeting held May 24, 2017. Guy Haselmann asked to correct the end of the second sentence of the first full paragraph on page 3 to read: "and further noted that there may be a certain crisis funding level below which taking any risk may be imprudent and the most prudent strategy is to take no risk in order to delay the depletion date as long as possible." Jeffrey Oram made a motion to approve the minutes as amended, with Mitchell Shivers seconding the motion. All Council Members present voted in favor, except for Charles Dolan and Michael Cleary, who abstained because they were absent from the meeting.

Opening Remarks by Chair

Mr. Byrne made some preliminarily opening remarks, reporting positive returns for the fiscal year ending June 30. Mr. Byrne cautioned that the pension plan cannot always count on strong returns to keep the pension funding crisis from getting worse, and emphasized the need for diversification in order to optimize risk adjusted returns. Mr. Byrne noted the benefits of recent legislation requiring quarterly State payments and providing for contribution of the lottery

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enterprise. Mr. Byrne stated that he had directed the Division staff and consultants to consider the appropriateness and mechanics of potentially implementing different asset allocation strategies for different funds. Finally, Mr. Byrne thanked the investment staff for its hard work during difficult circumstances.

Guest Speaker – Sharmin Mossavar-Rahmani

Mr. Byrne introduced Sharmin Mossavar-Rahmani, chief investment officer of the Private Wealth Management Group of Goldman Sachs. Ms. Mossavar-Rahmani discussed the Goldman Sachs Investment Strategy Group's outlook on global financial markets. Mr. Byrne inquired about the potential for equity prices to decline as a consequence of high valuation, to which Ms. Mossavar-Rahmani replied that true bear markets require trigger events, and noted that attempting to time shorter term movements has little probability of success. Mr. Byrne asked Ms. Mossavar-Rahmani if she thought the pension fund should be more conservative in its asset allocation. Ms. Mossavar-Rahmani responded that she would only recommend marginal changes to the fund's portfolio, with an emphasis on U.S. public and private equity and high yield fixed income. In response to Mr. Oram's question about the source of earnings growth, Ms. Mossavar-Rahmani explained that this was based on higher margins due primarily to lower costs, especially energy and labor. Mr. Dolan asked if Ms. Mossavar-Rahmani thought that the next recession would be caused by external forces (e.g., a slowdown in China). Ms. Mossavar-Rahmani answered that markets generally react to internal forces, but could also be affected by external events, depending on their nature and duration. In response to Mr. Dolan's question about her firm's underestimation of 2017 public equity returns to date, Ms. Mossavar-Rahmani noted that the firm bases its general guidance on "base case" ranges and that the firm tended to err on the side of caution. Mr. Haselmann's asked about the reactions of her firm's clients, since most model portfolios recently will have underperformed relative to the S&P index. Ms. Mossavar-Rahmani stated that the firm's clients understand the importance of a diversified portfolio when establishing the risk levels of their individual benchmarks. Further, Mr. Haselmann noted various headwinds to economic growth (e.g., demographics, deficits, debt levels, wealth inequality, etc.), and asked if it was prudent to recommend a continued overweight to public equities. Ms. Mossavar-Rahmani disputed the significance of many of the headwinds and maintained that current investment decisions should not be unduly influenced by speculative future events. In response to Mitchell Shivers' question why the firm recommended investing in Spanish equities, Ms. Mossavar-Rahmani referenced the country's banking and labor reforms and its relative political stability.

Director's Report

Director Christopher McDonough presented the Director's Report, providing an update on the performance of the portfolio as a whole and the performance of specific asset classes through May 2017 and describing shifts in asset allocation. Mr. McDonough and Deputy Director Corey Amon provided an overview of capital market returns by asset class and strategy. In response to Mr. Haselmann's request at the Council's prior meeting, Mr. Amon provided a comparison of recent market returns to historical returns during periods of similar economic growth. At the suggestion of Mr. Haselmann, Mr. McDonough agreed to further compare market returns when the Fed is in an easing or a tightening cycle.

Mr. McDonough provided an update on private equity and real estate portfolio cash flows, and announced the receipt of the State's \$1.86 billion contribution on June 30, 2017. Mr. McDonough discussed the implementation of P.L. 2017, c. 98 pursuant to which the Treasurer contributed the Lottery Enterprise for a period of 30 years for the benefit of three pension funds including: Public Employees Retirement System; Teachers Pension and Annuity Fund, and Police and Fire Retirement

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System. In response to a question from Mr. Cleary, Mr. McDonough confirmed that the percentage allocation of the Lottery Enterprise to each of the pension funds is set by statute.

Mr. McDonough notified the Council of the recent retirement of Betty Carr, a senior equity portfolio manager of the Division. Mr. McDonough thanked Ms. Carr for over 40 years of service to the State.

Pursuant to the Council's Alternative Investment Modification Procedures, Mr. McDonough notified the Council of a previously undisclosed affiliated broker-dealer entity engaged by CVC Capital Partners VII, L.P. to market the Fund to investors. Mr. McDonough reported that no fee had been charged to the Fund or its investors for services provided by the entity.

Private Equity Investment

Glendon Opportunities Fund II, L.P.

Michael Pascucci of the Division and Matthew Coyne of Torrey Cove Capital Partners presented an investment of up to \$100 million in Glendon Opportunities Fund II, L.P., a fund focused on investments primarily in credit markets experiencing distress and dislocation. In response to a question from Mr. Byrne, Mr. Coyne described the process by which Torrey Cove identified the fund as a potential investment. At the request of Mr. Byrne and Mr. Dolan, Mr. Coyne and Mr. McDonough described the Fund's key person protections. Mr. Byrne reported that the IPC had reviewed the investment and was satisfied that appropriate and adequate due diligence had been performed.

Investment Objective Survey

Kristen Doyle of Aon Hewitt Investment Consulting presented the results of the investment objective survey that was completed by Council members and the senior investment team at the Division. Ms. Doyle discussed the goals of the survey, data gathered from the survey and feedback from participants.

Adopted Amendments to N.J.A.C. 17:16-69 (Common Pension Funds)

Susan Sarnowski of the Division reported that the recently enacted lottery legislation authorized the Council to adopt regulations relating to the investment account for Common Pension Fund L, the fund created by the statute to receive the lottery proceeds. Ms. Sarnowski described the procedure for adopting the regulation, which would amend Subchapter 69 of the Council regulations, and explained the process by which lottery proceeds would be received and invested by the Division. Adam Liebttag requested that the proposed language in N.J.A.C. 17:16-69.1 stating "[t]he following funds may participate in Common Pension Fund L" be revised by replacing the word "may" with the word "shall" to more accurately reflect the statute. Mr. Liebttag made a motion to approve the resolution (see attached) approving the proposed Special Adopted Amendments as revised, and authorizing the submission to the Office of Administrative Law for publication in the New Jersey Register. Mr. Shivers seconded the motion. All members of the Council present voted in favor.

Proposed Amendments to N.J.A.C. 17:16-12 (Global Debt Obligations), 19 (Collateralized Notes and Mortgages), 23 (Global Diversified Credit Investments), 40 (Non-Convertible Preferred Stocks), and 58 (Mortgage Backed Senior Debt Securities; Mortgage Backed Pass-Through Securities)

Mr. McDonough presented proposed amendments to Subchapters 12, 19, 23, 40 and 58 of the Council regulations, describing the amendments and the purpose of the amendments. Mr. McDonough confirmed that the amendments would not affect the existing asset allocation plan. Mr. Byrne noted that the amendments were consistent with realities of the marketplace, and Mr. Haselmann added his support for giving the Division more flexibility to adapt to market

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conditions. Mr. Haselmann made a motion to approve the resolution (see attached) directing submission of the proposals to the Office of Administrative Law for publication in the New Jersey Register and public comment, with Mr. Oram seconding the motion. All members of the Council present voted in favor.

Election of Nominating Committee

Mr. Shivers made a motion, seconded by Mr. Liebtag, to elect Mr. Oram, Timothy McGuckin, and Mr. Haselmann to the Council's Nominating Committee. All members of the Council present voted in favor, except for Mr. Oram, Mr. McGuckin and Mr. Haselmann, who abstained.

Report on Qualified Independent Representative (QIR) Policy

Ms. Sarnowski reported to the Council regarding the Division's Qualified Independent Representative (QIR) Policy relating to certain derivative transactions, stating that the Division received all of the relevant representations and was in compliance with the Policy.

Report on Soft Dollar Expenditures/Brokerage Commission

Mr. Amon reported on the Division's soft dollar arrangements, under which brokers allocate a percentage of commissions paid by the Division to pay for research and trading services on behalf of the Division. In response to a question from Mr. Shivers, Michael Wszolek, Head Trader for the Division discussed the incremental cost of commissions incurred as a result of paying for research through the use of soft dollars.

Treasurer's Report

There was no report from the State Treasurer.

Public Comment

There was no public comment.

Adjournment

Chair Byrne announced that the next State Investment Council meeting would be held on October 4, 2017 instead of the proposed date in September. Mr. Cleary made a motion to adjourn the meeting, with Michael Greaney seconding the motion. All Council Members present voted in favor. The meeting was adjourned at 1:08 p.m.

**Resolution Approving Special Adopted Amendments
to N.J.A.C. 17:16-69 (Common Pension Funds)**

BE IT RESOLVED THAT:

The State Investment Council (the "Council") hereby approves the proposed Special Adopted Amendments to N.J.A.C. 17:16-69 (Common Pension Funds) as attached hereto.

The Council hereby authorizes the Director of the Division of Investment to submit the attached Special Adopted Amendments to the Office of Administrative Law for publication, and hereby delegates to staff of the Council and the Division of Investment the authority to make revisions to the Special Adopted Amendments as required and as shall be made upon the advice of the Attorney General.

This resolution shall take effect immediately.

DATED: July 27, 2017

TREASURY - GENERAL

STATE INVESTMENT COUNCIL

Common Pension Funds

Special Adopted Amendments: N.J.A.C. 17:16-69.1

Special Amendments Adopted: July 27, 2017 by the State Investment Council,

And Christopher McDonough, Director, Division of Investment

Filed: _____, 2017 as R. 2017 d. ____.

Authority: N.J.S.A. 52:18A-91.

Effective Date:

Expiration Date:

Take notice that the State Investment Council has adopted amendments at N.J.A.C. 17:16-69.1 to codify new statutory requirements enacted through P.L. 2017, c. 98. The rules are designed to make clear that Common Pension Fund L, established by P.L. 2017, c.98, shall be a "Common Pension Fund" for purposes of N.J.A.C. 17:16-69. These specially adopted amendments will remain in effect until _____, or until the rules are proposed for public comment and readopted through standard rulemaking procedures.

Full text of the special adoption follows (additions indicated in boldface **thus**; deletions indicated in brackets [thus]):

SUBCHAPTER 69. COMMON PENSION FUNDS

17:16-69.1 General Provisions

(a) (No change.)

(b) The following funds may participate in [the] Common Pension Funds **A, B, D and E**:

1.- 4. (No change.)

(c) Common Pension Fund L was established pursuant to P.L. 2017, c. 98, effective July 4, 2017. The following funds shall participate in Common Pension Fund L in accordance with the allocable percentages established by P.L. 2017, c. 98 as it may be amended from time to time:

- 1. Police and Firemen's Retirement System;**
- 2. Public Employees' Retirement System; and**
- 3. Teachers' Pension and Annuity Fund.**

**Resolution Approving Proposed Amendments
to N.J.A.C. 17:16-12 (Global Debt Obligations), 19(Collateralized Notes and
Mortgages), 23 (Global Diversified Credit Investments), 40 (Non-convertible
Preferred Stocks), and 58 (Mortgage Backed Senior Debt Securities;
Mortgage Backed Passthrough Securities)**

BE IT RESOLVED THAT:

The State Investment Council (the "Council") hereby approves the proposed amendments to N.J.A.C. 17:16-12 (Global Debt Obligations), 19(Collateralized Notes and Mortgages), 23 (Global Diversified Credit Investments), 40 (Non-convertible Preferred Stocks), and 58 (Mortgage Backed Senior Debt Securities; Mortgage Backed Passthrough Securities) as attached hereto.

The Council hereby authorizes the Director of the Division of Investment to submit the attached proposals to the Office of Administrative Law for publication and public comment, and hereby delegates to staff of the Council and the Division of Investment the authority to make revisions to the proposals as required and as shall be made upon the advice of the Attorney General.

This resolution shall take effect immediately.

DATED: July 27, 2017

TREASURY - GENERAL

STATE INVESTMENT COUNCIL

**Global Debt Obligations, Collateralized Notes and Mortgages, Non-Convertible Preferred Stock, Mortgage-Backed Senior Debt Securities; Mortgage-Backed Passthrough Securities
Permissible Investments**

Proposed Amendments: N.J.A.C. 17:16-12.2, 19.2, 40.2 and 58.2

Global Diversified Credit

Definitions, Permissible Investments, Limitations

Proposed Amendments: N.J.A.C. 17:16-23.1, 23.2 and 23.4

Authorized By: State Investment Council, Christopher McDonough, Director,

Division of Investment

Authority: N.J.S.A. 52:18A-91

Calendar Reference: See Summary below for explanation of exception to calendar requirement.

Proposal Number: PRN 2017-XX

Submit comments by XXX XX, 2017 to:

Christopher McDonough

Administrative Practice Officer

Division of Investment

PO Box 290

Trenton, New Jersey 08625-0290

The agency proposal follows:

Summary

N.J.A.C. 17:16-23 permits the Director to invest the monies of any eligible fund in global diversified credit investments.

The proposed amendments to N.J.A.C. 17:16-23.1 include proposed definitions for bridge financing, common stock, convertible debt issue, convertible preferred stock, debtor-in-possession financings, exchange-traded funds, global collateralized notes, high yield debt, opportunistic credit, post-reorganization equity, preferred stock, private placement and senior loan which are proposed to be added as permissible investments in N.J.A.C. 17:16-23.2. The definition of global diversified credit investments is proposed to be amended to clarify that these types of investments may include equity participation.

The definition for credit structured products in N.J.A.C. 17:16-23.1 is proposed to be amended to (a) clarify that permissible investments is not limited to securities and includes investment in any instrument for the purpose of generating future income, (b) broaden permissible investments to include investments whose cash flow characteristics depend upon a pool of collateral, securities or similar strategies designed to replicate the return of a basket of securities to reflect a more comprehensive investment opportunity set, (c) delete the requirement that the issuer's payment obligations be contingent on changes in the value of underlying assets, indices, interest rates or cash flows as that may not be the case for all investments, and (d) eliminate the potential subjectivity in application by requiring that the investment return be sensitive to, rather than highly sensitive to changes in the value of underlying assets, indices, interest rates or cash flows.

N.J.A.C. 17:16-23.2(a)1(ii) and 2(a)2(i) provide that global diversified credit investments meet certain minimum rating criteria. N.J.A.C. 23.2(b) provides that to the extent the rating criteria is not met, such investments, aggregated with other high yield investments, are subject to a cap. More specifically, N.J.A.C. 17:16-12.2(c), 19.2(b), 23.2(b), 40.2(b) and 58.2(c) provide that up to eight percent of the combined assets of all of the Pension and Annuity Funds may be

invested in global debt obligations, collateralized notes and mortgages, global diversified credit investments, non-convertible preferred stock and mortgage backed passthrough securities that do not meet the minimum credit ratings set forth in N.J.A.C. 17:16-12.2, 19.2, 23.2, 40.2 and 58.2, respectively. The proposed amendments will delete global diversified credit investments from the high yield investment category, and the corresponding eight percent limitation on such investments by (a) eliminating the rating criteria for global diversified credit investments through the proposed deletion of N.J.A.C. 17:16-23.2(a)1(ii) and 2(a)2(i), and (b) deleting global diversified credit investments from the eight percent limitation on high yield investments through the proposed amendments to N.J.A.C. 17:16-12.2(c), 19.2(b), 23.2(b), 40.2(b) and 58.2(c). The proposed amendment to N.J.A.C. 17:16-23.4(a)(1) will increase the limitation for global diversified credit investments from seven to ten percent of the market value of the combined assets of all of the Pension and Annuity Funds. These amendments will provide the opportunity for increased risk-adjusted returns.

As a result of the proposed deletions of N.J.A.C. 17:16-23.2(a)1(ii) and 2(a)2(i), corresponding changes to the language in N.J.A.C. 17:16-23.2(a), N.J.A.C. 17:16-23.2(a)1 and 2 have been proposed. N.J.A.C. 23.2(a)(1)(i)(1) is proposed to be recodified as N.J.A.C. 23.2(a)(1)(i). N.J.A.C. 23.2(a)(2) is proposed to be recodified as N.J.A.C. 23.2(a)(ii).

Proposed N.J.A.C. 17:16-23.2(a)3 provides that the Director may purchase the common stock of an entity that primarily invests in global diversified credit investments, and whose stock is traded on a securities exchange or over-the-counter market or offered and sold through a private placement. Proposed N.J.A.C. 17:16-23.2(a)4 provides that the Director may purchase exchange-traded funds traded on a securities exchange or the over-the-counter market that primarily invest in global diversified credit investments. For the purposes of this subchapter,

exchange-traded funds shall be considered as common stock in determining all applicable limitations contained in this subchapter. These amendments will provide the opportunity for increased risk-adjusted returns.

N.J.A.C. 17:16-23.2(c) will be recodified as N.J.A.C. 17:16-23.2(b). N.J.A.C. 17:16-23.2(b) 2 will be amended to provide that the Director may retain any distribution by a global diversified credit investment, even if such distribution does not meet the requirements of the subchapter. Proposed N.J.A.C. 17:16-23.2(b)3 will provide that the Director may purchase the preferred stock, whether convertible or not, or rights of an entity the common stock of which qualifies for investment under this subchapter. Proposed N.J.A.C. 17:16-23.2(b)4 will provide that the Director may purchase the convertible debt issue of an entity, the common stock of which qualifies for investment under this subchapter. Proposed N.J.A.C. 17:16-23.2(b)5 will provide that the Director may purchase stock in new public offerings of entities that primarily invest in global diversified credit investments. These amendments will provide for consistency among subchapters and provide the opportunity for increased risk-adjusted returns.

Proposed N.J.A.C. 17:16-23.4(a)4 will provide that the total amount of a particular class of stock purchased or acquired of any one issuer shall not exceed 10 percent of that class of stock outstanding. Proposed N.J.A.C. 17:16-23.4(a)5 will provide that the total amount of shares directly purchased or acquired of any one exchange-traded fund shall not exceed 10 percent of the total shares outstanding of such fund. These amendments will provide for consistency among subchapters.

Because the Division is providing a 60-day comment period on this notice of proposal, this notice is exempted from the rulemaking calendar requirement pursuant to N.J.A.C. 1:30-3.3(a)5.

Social Impact

The proposed amendments shall have a positive social impact because the opportunity for increased overall risk-adjusted returns for the State-administered funds will benefit the funds' beneficiaries and will lessen the long-term burden on the State's taxpayers.

Economic Impact

The proposed amendments shall have a positive economic impact by providing an opportunity for increased risk-adjusted returns of the State-administered funds.

Federal Standards Statement

A Federal standards analysis is not required because the investment policy rules of the State Investment Council are not subject to any Federal requirements or standards.

Jobs Impact

The proposed amendments will allow for an increased allocation to global diversified credit investments. A portion of the allocation to global diversified credit is focused on investment strategies which provide loans to small and mid-size businesses in the United States. Since the global financial crisis, this segment of the market has been under served by traditional lenders, limiting their ability to grow. Access to capital can help these businesses grow which in turn can increase available jobs.

Agriculture Industry Impact

The proposed amendments will have no impact on the agriculture industry.

Regulatory Flexibility Statement

A regulatory flexibility analysis is not required since the proposed amendments regulate only the Director of the Division of Investment and will have no effect on small businesses as the term is defined in the Regulatory Flexibility Act, N.J.S.A. 52:14B-16 et seq.

Housing Affordability Impact Analysis

The proposed amendments will have no impact on the affordability of housing in the State of New Jersey. The proposed amendments will modify investment in global debt obligations, collateralized notes and mortgages, global diversified credit investments, non-convertible preferred stocks and mortgage backed passthrough securities thereby providing an opportunity for increased risk-adjusted returns of the State-administered funds.

Smart Growth Development Impact Analysis

The proposed amendments are not anticipated to have an impact on the availability of affordable housing or housing production within Planning Areas 1 or 2, or within designated centers under the State Development and Redevelopment Plan in New Jersey. The proposed amendments will modify investment in global debt obligations, collateralized notes and mortgages, global diversified credit investments, non-convertible preferred stocks and mortgage backed passthrough securities thereby providing an opportunity for increased risk-adjusted returns of the State-administered funds.

Full text of the proposal follows (additions indicated in boldface **thus**; deletions indicated in brackets [thus]):

SUBCHAPTER 12. GLOBAL DEBT OBLIGATIONS

17:16-12.2 Permissible investments

(a) - (b) (No change.)

(c) Notwithstanding the restrictions in (a) above, the Director may invest and reinvest the moneys of any eligible Common Pension Fund in global debt obligations, collateralized notes and mortgages, [global diversified credit investments,] non-convertible preferred stock, and mortgage-backed passthrough securities that do not meet the minimum credit ratings set forth in

this section and N.J.A.C. 17:16-19.2, [23.2,] 40.2, and 58.2, respectively; provided, however, the aggregate market value of such investments shall not exceed eight percent of the combined assets of all of the Pension and Annuity Funds.

(d) – (f) (No change.)

SUBCHAPTER 19. COLLATERALIZED NOTES AND MORTGAGES

17:16-19.2 Permissible investments

(a) (No change.)

(b) Notwithstanding the restrictions in (a) above, the Director may invest and reinvest the moneys of any eligible Common Pension Fund in global debt obligations, collateralized notes and mortgages, [global diversified credit investments,] non-convertible preferred stock, and mortgage-backed passthrough securities that do not meet the minimum credit ratings set forth in N.J.A.C. 17:16-12.2, this section, and N.J.A.C. 17:16-[23.2,]40.2, and 58.2, respectively; provided, however, the aggregate market value of such investments shall not exceed eight percent of the combined assets of all of the Pension and Annuity Funds.

(c) (No change.)

SUBCHAPTER 23. GLOBAL DIVERSIFIED CREDIT INVESTMENTS

17:16-23.1 Definitions

...

“Bridge financing” means interim financing used by entities until a long-term financing option can be arranged. Bridge financing typically comes in the form of a debt obligation or equity investment.

...

"Common stock" means shares of stock, other than preferred stock, representing ownership in a corporation or other form of legal entity.

"Convertible debt issue" means a debt obligation of any corporation or other form of legal entity that is convertible into the common stock of the entity.

"Convertible preferred stock" means preferred stock of any corporation or other form of legal entity that is convertible into the common stock of the entity.

"Credit structured products" means [securities] investments whose cash flow characteristics depend upon a pool of collateral, one or more securities, indices or similar strategies designed to replicate the return of a basket of securities, or that have embedded forwards or options or securities where the investment return [and the issuer's payment obligations are] is contingent on, or [highly] sensitive to, changes in the value of underlying assets, indices, interest rates or cash flows.

"Debtor-in-possession financings" means financing arranged by an entity while under a bankruptcy reorganization process.

"Exchange-traded funds" means funds that invest in underlying securities that track a pre-determined index or strategy, a commodity, or a basket of assets, and whose shares can be traded like shares of common stock.

...

"Global collateralized notes" means securities collateralized by loans, receivables, claims or any other assets.

"Global diversified credit investments" means investments in opportunistic credit,

global collateralized notes, bank loans, mezzanine debt, credit structured products, commercial and residential mortgage-backed securities, commercial and residential whole loans, and other similar strategies, including equity participation.

“High yield debt” means a debt obligation with a lower credit rating than investment-grade debt.

...

“Global collateralized notes” means securities collateralized by loans, receivables, claims or any other assets.

“Global diversified credit investments” means investments in opportunistic credit, global collateralized notes, bank loans, mezzanine debt, credit structured products, commercial and residential mortgage-backed securities, commercial and residential whole loans, and other similar strategies, including through equity participation.

“High yield debt” means a debt obligation with a lower credit rating than investment-grade debt.

...

“Opportunistic credit” means primary and secondary opportunities in performing, stressed, and distressed public and private securities. This includes senior loans, high yield debt, debtor-in-possession financings, and bridge financings, as well as post-reorganization equity.

“Post-reorganization equity” means equity issued by an entity as part of a bankruptcy, reorganization or other, similar restructuring.

“Preferred stock” means shares of stock which provide a dividend that is paid before any dividends are paid to holders of common stock and additional rights above and

beyond those conferred by common stock.

“Private placement” means a negotiated sale in which the securities are sold directly to institutional or private investors, rather than through a public offering registered with the U.S. Securities and Exchange Commission or applicable foreign regulatory body.

Private placement includes the sale of securities pursuant to Section 4(2), Regulation D, Regulation S, or Rule 144A under the Securities Act of 1933, as amended.

“Senior loan” means a debt financing obligation that holds legal claim above other, junior debt obligations. Senior loans may include embedded equity instruments.

17:16-23.2 Permissible investments

(a) Subject to the limitations contained in this subchapter, the Director may invest and reinvest the moneys of any eligible fund in **global diversified credit investments in any of the following ways:**

1. [Direct] **Invest in direct bank loans provided that[:]** the borrower:

i. [The borrower:

(1)] Is not in default as to the payment of principal or interest upon any of its outstanding obligations. Subsequent to purchase, if the borrower defaults, the loans do not have to be sold; and

[(2)] ii. Has shareholder’s equity of at least \$200 million. Subsequent to purchase, if shareholder’s equity falls below \$200 million, the investment does not have to be sold; [and

[ii. The issue has a credit rating of Baa3 or higher by Moody's Investors Service, Inc., BBB- or higher by Standard & Poor's Corporation, and BBB- or higher by Fitch Ratings, except that two of the three ratings is sufficient and one of the three ratings is sufficient if only

one rating is available. If a rating for the issue has not been obtained from the above services, the issue may be purchased if the issuer rating meets the minimum rating criteria. Subsequent to purchase, if ratings fall below the minimum rating for such issues, they do not have to be sold, and they may be exchanged with issues with a credit rating lower than the minimum rating if the issues received in exchange are, on balance, similarly rated; and]

2. [Separate] **Invest in separate** accounts, funds-of-funds, commingled funds, co-investments, and joint ventures that primarily invest in global diversified credit investments provided that[:

i. At the time of purchase or commitment by an eligible fund, the securities included or intended to be included in the investment vehicle shall consist primarily of those with a credit rating of Baa3 or higher by Moody's Investors Service, Inc., BBB- or higher by Standard & Poor's Corporation, and BBB- or higher by Fitch Ratings, except that two of the three ratings is sufficient and one of the three ratings is sufficient if only one rating is available. If a rating for the security has not been obtained from the above services, the issue may be purchased if the issuer rating meets the minimum rating criteria; and

ii. The] **the** further provisos contained in N.J.A.C. 17:16-69.9 have been met[.];

3. Purchase the common stock of an entity that primarily invests in global diversified credit investments, and whose stock is traded on a securities exchange or over-the-counter market or offered and sold through a private placement; and

4. Purchase exchange-traded funds traded on a securities exchange or the over-the-counter market that primarily invest in global diversified credit investments. For the purposes of this subchapter, exchange-traded funds shall be considered as common stock in determining all applicable limitations contained in this subchapter.

(b) [Notwithstanding the restrictions in (a) above, the Director may invest and reinvest the moneys of any eligible Common Pension Fund in global debt obligations, collateralized notes and mortgages, global diversified credit investments, non-convertible preferred stock, and mortgage-backed passthrough securities that do not meet the minimum credit ratings set forth in N.J.A.C. 17:16-12.2, 19.2, this section, and N.J.A.C. 17:16-40.2 and 58.2, respectively; provided, however, the aggregate market value of such investments shall not exceed eight percent of the combined assets of all of the Pension and Annuity Funds.

(c) [In addition to (a) above, the Director may:

1. Exercise the rights or conversion privileges of any security acquired under this subchapter; [and]
2. Retain any distribution received as a result of a corporate action **or distribution by a global diversified credit investment**, even if such distribution does not meet the requirements of this subchapter[.];
3. **Purchase the preferred stock, whether convertible or not, or rights of an entity the common stock of which qualifies for investment under this subchapter;**
4. **Purchase the convertible debt issue of an entity, the common stock of which qualifies for investment under this subchapter; and**
5. **Purchase stock in new public offerings of entities that primarily invest in global diversified credit investments.**

(d) - (e) (No change.)

17:16-23.4 Limitations

(a) (No change.)

1. Not more than [seven] **ten** percent of the market value of the combined assets of

all of the Pension and Annuity Funds shall be invested in global diversified credit investments, whether directly or through separate accounts, funds-of-funds, commingled funds, co-investments, and joint ventures that primarily invest in global diversified credit investments;

2. The total amount of direct bank loans purchased or acquired under this subchapter shall not exceed 10 percent of the outstanding long-term debt of the borrower except that these requirements may be waived by the Council; [and]

3. The total amount directly invested in the equity and fixed income obligations of any one issuer and affiliated entities by the Pension and Annuity Funds and the Common Pension Funds, in the aggregate, shall not exceed five percent of the combined assets of all the Pension and Annuity Funds[.];

4. The total amount of a particular class of stock purchased or acquired of any one issuer shall not exceed 10 percent of that class of stock outstanding; and

5. The total amount of shares directly purchased or acquired of any one exchange-traded fund shall not exceed 10 percent of the total shares outstanding of such fund.

(b) (No change.)

SUBCHAPTER 40. NON-CONVERTIBLE PREFERRED STOCKS

17:16-40.2 Permissible investments

(a) (No change.)

(b) Notwithstanding the restrictions in (a) above, the Director may invest and reinvest the moneys of any eligible Common Pension Fund in global debt obligations, collateralized notes

and mortgages, [global diversified credit investments,] non-convertible preferred stock, and mortgage-backed passthrough securities that do not meet the minimum credit ratings set forth in N.J.A.C. 17:16-12.2, 19.2, [23.2,] this section, and N.J.A.C. 17:16-58.2, respectively; provided, however, the aggregate market value of such investments shall not exceed eight percent of the combined assets of all of the Pension and Annuity Funds.

(c) – (d) (No change.)

SUBCHAPTER 58. MORTGAGE-BACKED SENIOR DEBT SECURITIES; MORTGAGE-BACKED PASSTHROUGH SECURITIES

17:16-58.2 Permissible investments

(a) - (b) (No change.)

(c) Notwithstanding the restrictions in (a) above, the Director may invest and reinvest the moneys of any eligible Common Pension Fund in global debt obligations, collateralized notes and mortgages, [global diversified credit opportunity investments,] non-convertible preferred stock, and mortgage-backed passthrough securities that do not meet the minimum credit ratings set forth in N.J.A.C. 17:16-12.2, 19.2, [23.2,] 40.2, and this section, respectively; provided, however, the aggregate market value of such investments shall not exceed eight percent of the combined assets of all of the Pension and Annuity Funds.

(d) (No change.)