

**MINNESOTA STATE BOARD
OF INVESTMENT
MEETING**

June 5, 1996

&

**INVESTMENT ADVISORY
COUNCIL MEETING**

June 4, 1996

**AGENDA
STATE BOARD OF INVESTMENT
MEETING**

**Wednesday, June 5, 1996
8:30 A.M. -Room 125
State Capitol - Saint Paul**

TAB

- 1. Approval of Minutes of March 19, 1996**

- 2. Report from the Executive Director (H. Bicker)**
 - A. Quarterly Investment Review (December 31, 1995 - March 31, 1996) **A**
 - B. Portfolio Statistics (March 31, 1996) **B**
 - C. Administrative Report **C**
 1. Reports on budget and travel
 2. Authorization for deferred compensation consultant RFP
 3. Approval of vendor contract for Historical Society retirement plan
 4. Reappointment of IAC members

- 3. Report from the SBI Administrative Committee (M. McGrath)** **D**
 - A. Approval of FY97 workplan
 - B. Approval of FY97 administrative budget
 - C. Approval of Continuing Fiduciary Education Plan
 - D. Approval of process for the Executive Director's FY96 evaluation

- 4. Reports from the Investment Advisory Council (J. Yeomans)**
 - A. Domestic Manager Committee **E**
 1. Review of manager performance
 2. Update on candidates for Manager Monitoring Program
 3. Annual review of active stock manager benchmarks
 4. Renewal of contract for the bond manager for the Assigned Risk Plan (Voyageur)
 5. Authorization to terminate a contract with an active stock manager (Jundt)

 - B. International Manager Committee **F**
 1. Review of manager performance.
 2. Annual review of investment manager guidelines
 3. Update on emerging markets managers funding
 4. Upcoming emerging markets manager "round table"
 5. Approval of contract renewals with existing managers (State Street, Marathon, Rowe Price, Scudder, Templeton)

 - C. Alternative Investment Committee **G**
 1. Review of current strategy.
 2. Results of annual review session with a private equity manager (Coral Group)
 3. Approval of commitment to an existing private equity manager (KKR) for the Basic Funds
 4. Approval of commitment to an existing private equity manager (Golder Thoma) for the Basic Funds
 5. Approval of commitment to a new real estate manager (Starwood) for the Post Fund

- 5. Report from the Proxy Committee (P. Sausen)** **H**

**Minutes
State Board of Investment
March 19, 1996**

The State Board of Investment (SBI) met at 8:30 A.M. on Tuesday, March 19, 1996 in Room 230, Minnesota Judicial Building, 25 Constitution Avenue, St. Paul, Minnesota. Governor Arne H. Carlson, Chair; State Auditor Judith H. Dutcher; State Treasurer Michael A. McGrath; Secretary of State Joan Anderson Growe and Attorney General Hubert H. Humphrey III were present.

Mr. Carlson called the meeting to order and commented that, in the future, he would prefer that Board meetings not be scheduled during the last weeks of Legislative session. The minutes of the December 20, 1995 meeting were approved.

Executive Director's Report

Mr. Bicker, Executive Director, referred members to Tab A of the meeting materials and reported that the Combined Funds had exceeded inflation over the ten year period ending December 31, 1995 (Combined Funds 11.9% vs. Inflation 3.5%) and outperformed the median fund (Combined Funds 13.6% vs. Median 13.5%) and their composite index (Combined Funds 13.6% vs. Composite 13.3%) for the most recent five year period. He stated that the Basic Funds had exceeded their composite index (Basics 13.6% vs. Composite 13.3%) over the last five years while the Post Fund had slightly underperformed its composite index for the 2.5 year period ending December 31, 1995 (Post 11.5% vs. Composite 11.6%).

Mr. Bicker reported that the Basic Funds' assets increased 4.7% for the quarter ending December 31, 1995 and that the Funds' had underperformed its composite index for the quarter (Basics 4.2% vs. Composite 4.4%) and year (Basics 25.0% vs Composite 25.3%).

Mr. Bicker reported that the Post Fund's assets increased 3.3% for the quarter ending December 31, 1995 and that the Fund had underperformed its composite index for the quarter (Post 4.3% vs. Composite 4.5%) while it had matched its composite for the year (at 26.1%).

Mr. Bicker reported that the domestic stock manager group underperformed for the quarter (Domestic Stocks 4.5% vs. Wilshire 5000 4.9%) and that the international stock manager group had underperformed for the quarter (International Stocks 4.0% vs. EAFE-Free 4.1%) but had outperformed for the year (International Stocks 12.4% vs. EAFE-Free 11.3%). He said that bonds also underperformed for the quarter (Bonds 4.2% vs. Lehman Aggregate 4.3%) but had outperformed for the year (Bonds 18.6% vs. Lehman Aggregate 18.5%).

Mr. Bicker reported that the Assigned Risk Plan (ARP) had outperformed its composite index for the quarter (ARP 3.8% vs. Composite 3.7%) and year (ARP 19.9% vs. Composite 18.7%). He concluded his report with the comment that as of December 31, 1995 the SBI was responsible for over \$28 billion in assets.

Executive Director's Administrative Report

Mr. Bicker referred members to Tab B for the Portfolio Statistics and Tab C of the meeting materials for the current budget and travel reports and the Legislative update. He asked if anyone had any questions and hearing none, he proceeded by explaining that staff is requesting that consulting contracts with Richards & Tierney and Pension Consulting Alliance be extended for one year while staff conducts a review of the SBI's information needs with respect to accounting and performance data. Mr. Humphrey moved approval of staff's recommendation, as stated in the Committee Report, which reads, "The SBI authorizes the Executive Director, with assistance from SBI legal counsel, to negotiate and execute contract extensions of one year (July 1, 1996-June 30, 1997) for consulting services with: Richards & Tierney, Inc., Chicago, IL and Pension Consulting Alliance, Encino, CA". Ms. Growe seconded the motion. The motion passed.

Semi-Passive Bond Manager Search Committee Report

Ms. Voss referred members to Tab D of the meeting materials and stated that the Committee had interviewed four firms as a possible replacement for Fidelity Management who had resigned the SBI's account in December 1995. She stated that the Search Committee is recommending that the SBI retain BlackRock Financial Management. Ms. Growe moved approval of the Committee's recommendation, as stated in the Committee Reports, which reads, "The Committee recommends that the SBI authorize the Executive Director, with assistance from SBI legal counsel, to negotiate and execute a contract with BlackRock Financial Management, New York, NY, for semi-passive bond management". Mr. Humphrey seconded the motion. The motion passed.

Emerging Markets Manager Search Committee

Mr. Sausen reported that during the quarter, the Search Committee had interviewed six firms as potential emerging markets managers for the SBI. He stated that the Committee is recommending three firms: City of London, Genesis Asset Management and Montgomery Asset Management. Mr. McGrath moved approval of the Committee's recommendation, as stated in the Committee Report, which reads "The Committee recommends that the SBI authorize the Executive Director, with assistance from SBI legal counsel, to negotiate and execute contracts with the following firms for emerging markets stock management: City of London, London, England, UK; Genesis Asset Managers, Ltd., London, England, UK; Montgomery Asset Management L.P., San Francisco, CA. Further, the Committee recommends that the City of London receive a lower allocation than that provided to each of the other firms. The exact amounts should be left to the discretion of the Executive Director". Mr. Humphrey seconded the motion. The motion passed.

Domestic Manager Committee Report

Ms. Yeomans referred members to Tab E of the meeting materials and stated that the Committee is recommending that Investment Advisors be placed on probation due to a change in portfolio management. She added that this action is in accordance with the Manager Continuation Policy. In response to a question from Ms. Growe, Ms. Yeomans confirmed that the action is being taken due to personnel changes and not because of the firm's performance. Ms. Dutcher moved approval of the Committee's recommendation, as stated in the Committee Report, which reads "The Committee recommends that the SBI place IAI on probation due to a change in portfolio managers for the SBI active stock account with the firm. This action is recommended in accordance with the guidelines in the SBI's Manager Continuation Policy". Mr. Humphrey seconded the motion. Mr. Carlson commented that he approves of the review process, however, he suggested that in the future, a term other than "probation" be used to describe this process, especially if a firm's performance has been satisfactory. The motion passed.

Ms. Yeomans stated that the Committee is recommending that the SBI renew the contracts for all the domestic stock and bond managers, as listed in the Committee Report. She added that the recommendation is to execute five year contracts that provide for immediate termination. Mr. Bicker clarified that currently the SBI has a 30 day escape clause and that the new contracts would allow immediate termination. Ms. Growe moved approval of the Committee's recommendation, as stated in the Committee Report, which reads, "The Committee recommends that the SBI authorize the Executive Director, with assistance from SBI's legal counsel, to negotiate and execute five year contract extensions with the following firms, subject to inclusion of a provision which provides for immediate termination."

Domestic Equity Managers

Alliance Capital Management
Brinson Partners, Inc.
Forstmann Leff Associates
Franklin Portfolio Associates Trust
GeoCapital Corporation
IDS Advisory Group
Independence Investment Assoc., Inc.
Investment Advisers, Inc.
Jundt Associates, Inc.
Lincoln Capital Management
Oppenheimer Capital
Waddell & Reed Asset Management
Weiss Peck & Greer

Fixed Income Managers

BEA Associates
Goldman Sachs Asset Management
IDS Advisory Group
Investment Advisers, Inc.
Lincoln Capital Management
Miller Anderson & Sherrerd
Standish Ayer & Woods
Western Asset Management

Ms. Dutcher seconded the motion. The motion passed.

International Manager Committee Report

Ms. Yeomans referred members to Tab F of the meeting materials and stated that approval was needed to renew contracts with Baring and Brinson for five years, including a provision for immediate termination. Mr. McGrath moved approval of the Committee's recommendation, as stated in the Committee Report, which reads "The Committee recommends that the SBI authorize the Executive Director, with assistance from SBI legal counsel, to negotiate and execute five year contract renewals with the following international stock managers subject to inclusion of a provision which provides for immediate termination: Baring Asset Management and Brinson Partners." Ms. Dutcher seconded the motion. The motion passed.

Ms. Yeomans referred members to page 7 of the Committee Report and stated that the Committee is seeking approval of the staff position paper on emerging markets investing. In response to a question from Mr. McGrath, Mr. Bicker said that there were no major changes from what the Board members had seen previous drafts. In response to a question from Ms. Dutcher, Mr. Bicker stated that the SBI will depend on the expertise of its managers to avoid making investments in countries in turmoil. He added that typically, those kinds of countries would not have developed securities markets in which to invest. In response to a question from Ms. Growe, Mr. Bicker reviewed the process managers follow when making investments in the three categories contained in the SBI's guidelines on international investing. Mr. McGrath moved approval of the Committee's recommendation to approve the position paper on emerging markets, as stated in the Committee Report, which reads, "The Committee recommends that the SBI adopt the staff position paper which begins on page 7 as its policy statement on emerging markets investing for the retirement funds." The motion passed.

Alternative Investment Committee Report

Ms. Yeomans referred members to Tab G of the meeting materials and stated that the Committee is recommending two alternative investments to the Board for the Post Retirement Fund. She stated that the first recommendation is to invest up to \$25 million with Merit Energy, a resource manager. In response to a question from Mr. Carlson, Mr. Bicker stated that the SBI has not invested with this manager before, but that Merit has done 11 previous funds that have provided fairly consistent returns. Mr. Humphrey moved approval of the Committee's recommendation, as stated in the Committee Report, which reads, "The Committee recommends that the SBI authorize the Executive Director, with assistance from the SBI's legal counsel, to negotiate and execute a commitment of up to \$25 million or 20%, whichever is less, in Merit Energy Partners - B, L.P. Fund. This commitment will be allocated to the Post Retirement Fund. Approval by the SBI of this potential commitment is not intended to be, and does not constitute in any way, a binding or legal agreement or impose any legal obligations on the State Board of Investment and neither the State of Minnesota, the State Board of Investment or its Executive Director have any liability for reliance by Merit Energy upon this approval. Until a formal agreement is executed by the Executive Director on behalf of the SBI, further due diligence and negotiations may result in the imposition of additional terms and conditions

on Merit Energy or reduction or termination of the commitment.” Ms. Dutcher seconded the motion. The motion passed.

Ms. Yeomans stated that the second recommendation from the Committee is to invest up to \$40 million in TCW/Crescent Mezzanine Partners, L.P., a private equity fund that will make mezzanine investments including subordinated debt with equity participation. In response to a question from Mr. Carlson, Mr. Bicker said that previous returns had been around 17-18%. Mr. McGrath moved approval of the Committee’s recommendation, as stated in the Committee Report, which reads, “The Committee recommends that the SBI authorize the Executive Director, with assistance from the SBI’s legal counsel, to negotiate and execute a commitment of up to \$40 million or 20%, whichever is less, in TCW/Crescent Mezzanine Partners, L.P. This commitment will be allocated to the Post Retirement Fund. Approval by the SBI of this potential commitment is not intended to be, and does not constitute in any way, a binding or legal agreement or impose any legal obligations on the State Board of Investment and neither the State of Minnesota, the State Board of Investment or its Executive Director have any liability for reliance by TCW/Crescent upon this approval. Until a formal agreement is executed by the Executive Director on behalf of the SBI, further due diligence and negotiations may result in the imposition of additional terms and conditions on TCW/Crescent or reduction or termination of the commitment.” The motion passed.

In response to questions from Ms. Growe, Mr. Bicker briefly reviewed the impact of recent litigation involving tobacco companies. He noted that several brokerage firms have put out “buy” recommendations on some tobacco stocks, while other firms have stated that some mutual funds are considering liquidating their tobacco holdings. Ms. Posey stated that she believes there will be some short term volatility, but that over the long-term, the stocks will trade at their fair market value. In response to a question from Ms. Growe, Ms. Yeomans stated that the IAC had not discussed the issues currently associated with the tobacco industry. Mr. Carlson noted that several of the tobacco companies are highly diversified, but he agreed that it is important to monitor the situation and he asked Mr. Bicker to prepare an informational report for the Board to review. Mr. Bicker agreed.

Mr. Carlson adjourned the meeting at 8:46 a.m.

Respectfully submitted,

Howard Bicker
Executive Director

**AGENDA
INVESTMENT ADVISORY COUNCIL
MEETING**

Tuesday, June 4, 1996

2:00 P.M. - SBI Conference Room

Room 105, MEA Building - Saint Paul

TAB

1. **Approval of Minutes of March 19, 1996**

2. **Report from the Executive Director (H. Bicker)**
 - A. **Quarterly Investment Review (December 31, 1995 - March 31, 1996)** **A**
 - B. **Portfolio Statistics (March 31, 1996)** **B**
 - C. **Administrative Report** **C**
 1. **Reports on budget and travel**
 2. **Authorization for deferred compensation consultant RFP**
 3. **Approval of vendor contract for Historical Society retirement plan**
 4. **Reappointment of IAC members**

3. **Report from the SBI Administrative Committee (M. McGrath)** **D**
 - A. **Approval of FY97 workplan**
 - B. **Approval of FY97 administrative budget**
 - C. **Approval of Continuing Fiduciary Education Plan**
 - D. **Approval of process for the Executive Director's FY96 evaluation**

4. **Reports from the Investment Advisory Council**
 - A. **Domestic Manager Committee (D. Bergstrom)** **E**
 1. **Review of manager performance**
 2. **Update on candidates for Manager Monitoring Program**
 3. **Annual review of active stock manager benchmarks**
 4. **Renewal of contract for the bond manager for the Assigned Risk Plan (Voyageur)**
 5. **Authorization to terminate a contract with an active stock manager (Jundt)**

 - B. **International Manager Committee** **F**
 1. **Review of manager performance.**
 2. **Annual review of investment manager guidelines**
 3. **Update on emerging markets managers funding**
 4. **Upcoming emerging markets manager "round table"**
 5. **Approval of contract renewals with existing managers (State Street, Marathon, Rowe Price, Scudder, Templeton)**

 - C. **Alternative Investment Committee** **G**
 1. **Review of current strategy.**
 2. **Results of annual review session with a private equity manager (Coral Group)**
 3. **Approval of commitment to an existing private equity manager (KKR) for the Basic Funds**
 4. **Approval of commitment to an existing private equity manager (Golder Thoma) for the Basic Funds**
 5. **Approval of commitment to a new real estate manager (Starwood) for the Post Fund**

5. **Report from the Proxy Committee (P. Sausen)** **H**

**Minutes
Investment Advisory Council
March 18, 1996**

The Investment Advisory Council met on Monday, March 18, 1996 at 2:00 P.M. in the State Board of Investment (SBI) Conference Room, 55 Sherburne Avenue, St. Paul.

MEMBERS PRESENT: Gary Austin; Dave Bergstrom; Roger Durbahn; Ken Gudorf; Laurie Fiori Hacking; Peter Kiedrowski; Judy Mares; Malcolm McDonald; Daralyn Peifer; Patrick Sexton; Michael Stutzer; Debbie Veverka and Jan Yeomans.

MEMBERS ABSENT: John Bohan; Laura King; Han Chin Liu and Gary Norstrem.

SBI STAFF: Howard Bicker; Beth Lehman; Jim Heidelberg; Lois Buermann; Mark Regal; Karen Vnuk; Debbie Griebenow; Charlene Olson and Lin Nadeau.

OTHERS ATTENDING: Ann Posey, Tom Richards, Richards & Tierney; Carey Moe; Peter Sausen; Elaine Voss; John Wicklund, Teachers Retirement Association; Ed Stuart and John Hagman, Susan Mills and John Moriarity, REAM

Ms. Yeomans called the meeting to order and the minutes of the December 12, 1995 meeting were approved.

Executive Director's Report

Mr. Bicker, Executive Director, referred members to Tab A of the meeting materials and reported that the Combined Funds had exceeded inflation over the ten year period ending December 31, 1995 (Combined Funds 11.9% vs. Inflation 3.5%) and outperformed the median fund (Combined Funds 13.6% vs. Median 13.5%) and their composite index (Combined Funds 13.6% vs. Composite 13.3%) for the most recent five year period. He stated that the Basic Funds had exceeded their composite index (Basics 13.6% vs. Composite 13.3%) over the last five years while the Post Fund had slightly underperformed its composite index for the 2.5 year period ending December 31, 1996 (Post 11.5% vs. Composite 11.6%).

Mr. Bicker reported that the Basic Funds' assets increased 4.7% for the quarter ending December 31, 1995 due to positive investment returns and that the Funds' had underperformed its composite index for the quarter (Basics 4.2% vs. Composite 4.4%).

Mr. Bicker reported that the Post Fund's assets increased 3.3% for the quarter ending December 31, 1995 due to positive investment returns. He said that the Post Fund is also moving towards its new international targets. He stated that the Fund had underperformed its composite index for the quarter (Post 4.3% vs. Composite 4.5%).

Mr. Bicker reported that the domestic stock manager group underperformed for the quarter (Domestic Stocks 4.5% vs. Wilshire 5000 4.9%) and that the international stock manager group had underperformed for the quarter (International Stocks 4.0% vs. EAFE-Free 4.1%) but had outperformed for the year (International Stocks 12.4% vs. EAFE-Free 11.3%). He said that bonds also underperformed for the quarter (Bonds 4.2% vs. Lehman Aggregate 4.3%) but had outperformed for the year (Bonds 18.6% vs. Lehman Aggregate 18.5%).

Mr. Bicker reported that the Assigned Risk Plan (ARP) had outperformed its composite index for the quarter (ARP 3.8% vs. Composite 3.7%) and year (ARP 19.9% vs. Composite 18.7%). He concluded his report with the comment that as of December 31, 1995, the SBI was responsible for over \$28 billion in assets.

Executive Director's Administrative Report

Mr. Bicker referred members to Tab B for the Portfolio Statistics and Tab C of the meeting materials for the current budget and travel reports and the Legislative update. He reported that staff is monitoring several bills that impact the SBI to various degrees. He said that one provision contained in the Omnibus Pension bill would include the SBI's Executive Director on a task force which would review local fire relief association investment reporting requirements. Mr. Bicker said a bill to abolish the State Treasurers' Office is still pending and that a bill related to local government investment restrictions is in Conference Committee. He added that the latter bill was a hold over from last session and came about as a result of the problems in Orange County, California. Mr. Bicker stated that a bill to change the retirement formula for the Post Retirement Fund did not pass the bill deadline and may be introduced again next year. He said that a bill to establish an Education Investment Fund also did not pass the bill deadline, however, he noted the possibility that it could still be attached to another piece of legislation.

Mr. Bicker reported that, as part of his FY 1997 workplan, staff will be conducting a comprehensive review of the SBI's information needs with respect to accounting and performance data. He said that he believes that it is in the SBI's best interest to conduct this review prior to initiating a new request for proposal (RFP) for consulting services. He said that staff is recommending that the SBI authorize a one year contract extension of the current contracts with Richards & Tierney and Pension Consulting Alliance. He added that this would allow the SBI to initiate RFP's for consulting services and for portfolio accounting services at the same time.

Semi-Passive Bond Manger Search Committee

Ms. Voss referred members to Tab D of the meeting materials and stated that the Committee had conducted a semi-passive bond manager search to replace Fidelity

Management Trust Company, who resigned the SBI's account in December 1995. She reported that four firms were interviewed and that the Committee is recommending that BlackRock Financial Management be retained as a semi-passive manager. In response to questions from Mr. Bergstrom, Mr. Bicker stated that the management fees for the portfolio had been lowered substantially during the negotiation process. Ms. Yeomans stated that no action was needed by the IAC on this recommendation and she asked Mr. Sausen to present the Emerging Markets search report.

Emerging Markets Manager Search Committee

Mr. Sausen thanked the five IAC members who served on the Search Committee. He stated that the Committee had interviewed six firms that specialize in emerging markets and that the Committee is recommending that three firms be retained by the Board: City of London, Genesis Asset Managers and Montgomery Asset Management. Mr. Sausen requested that the IAC affirm the Committee's selections. Mr. McDonald moved approval of the Emerging Market Search Committee's recommendation, as stated in the Committee report. Mr. Bergstrom also moved approval of the semi-passive Bond Manager Search Committee's recommendation to retain BlackRock Financial Management, as stated in the Committee Report. Mr. Gudorf seconded both motions. In response to questions from Ms. Mares regarding City of London's capacity, Mr. Bicker confirmed that if approved, the SBI would comprise approximately one-quarter of the firm's business. He stated that the SBI had determined that it should not be more than one-third of the business of any firm. Mr. Gudorf stated that it was easier for him to feel comfortable with the City of London's size due to the fact that they are primarily a manager of closed-end funds. Ms. Lehman clarified that the City of London will manage a separate account for the SBI. Both motions passed.

Domestic Manager Committee Report

Mr. Bergstrom referred members to Tab E of the meeting materials and briefly reviewed the equity managers' performance. He noted that staff is continuing to closely monitor three firms due to concerns regarding underperformance: GeoCapital, Jundt Associates and Weiss Peck & Greer. He also reviewed the bond manager performance and stated that the Committee is very comfortable with the existing bond managers.

Mr. Bicker stated that during the quarter, staff had hosted a joint meeting of the SBI's active, semi-passive and passive domestic stock managers. He explained that the purpose of the meeting was to review the goals and objectives of the SBI's domestic equity program, to discuss performance expectations and concerns and to review benchmark quality issues. He added that he believes the meeting was well worth the effort and that everyone gained some valuable insights into the domestic equity program.

Mr. Bergstrom stated that the Committee is recommending that IAI be placed on probation due to a change in portfolio managers for the SBI's account. Mr. McDonald moved approval of the Committee's recommendation, as stated in the Committee Report. Ms. Hacking seconded the motion. In response to a question from Ms. Yeomans, Mr.

Bicker stated that IAI will be reviewed again at the end of six months. The motion passed.

Mr. Bergstrom stated that the Committee is recommending that five year contract extensions be approved for the domestic stock and bond managers whose contracts expire June 30, 1996. He added that the new contracts will include an immediate termination provision. Mr. Gudorf moved approval of the Committee's recommendation to renew contracts, as stated in the Committee Report. Mr. McDonald seconded the motion. The motion passed. In response to a question from Ms. Hacking, Mr. Bicker said that IAI's VAM graph has been affected by the implementation of a new benchmark and that Weiss Peck & Greer's was affected by poor performance for approximately 12 month period during 1994 and part of 1995.

International Manager Committee Report

Ms. Veverka referred members to Tab F of the meeting materials and briefly reviewed the performance of the international segment. She updated members on the status of the asset allocation transition taking place which is to move from a 10% to a 15% allocation in international stocks. She said that once the emerging markets managers are funded, the funds should be close to the 15% target. She added that as of January 31, 1996, the new currency overlay program had generated a small profit.

Ms. Veverka reported that the Committee is recommending that the Board approve 5 year contract renewals with Baring Asset Management and Brinson Partners. Mr. McDonald moved approval of the Committee's recommendation, as stated in the Committee Report. Mr. Durbahn seconded the motion. The motion passed.

Ms. Veverka stated that the Committee is requesting approval of the position paper on emerging markets investing. She noted that the Committee had now reviewed the paper twice and had fairly extensive discussions about the benchmark. Mr. Gudorf moved approval of the position paper as included in the meeting materials. Mr. McDonald seconded the motion. The motion passed.

Alternative Investment Committee Report

Mr. Gudorf referred members to Tab G of the meeting materials and stated that during the quarter staff had conducted an annual review of one of its real estate manager, Aetna. He said that one item of interest is that Aetna had agreed to be sold to TA Associates, and he said that staff and the Committee are both comfortable with that change.

Mr. Gudorf stated that the Committee is recommending an investment for the Post Fund with a new resource manager, Merit Energy, an oil and gas limited partnership. He noted that it has been difficult to find resource investments of adequate size for the SBI to invest in, and he said the Committee feels this fund presents a good opportunity to invest in the energy area. Mr. Gudorf said that the Committee is also recommending a private equity investment for the Post Fund in TCW/Crescent Mezzanine Partners, L.P. and he gave a brief summary of the organization and its management history.

In response to a question from Ms. Veverka, Mr. Gudorf and Mr. Bicker explained that Merit's strategy is to buy small oil and gas properties and package them together. Mr. Gudorf added that the fund can be more efficiently managed by using this approach. In response to a question from Ms. Mares, Mr. Gudorf replied that Merit does anticipate doing additional funds, but he noted that they may be 2-3 years apart. In response to a question from Ms. Veverka, Mr. Gudorf said the Committee is satisfied with the return expectations for Merit. Mr. Austin moved approval of the Committee's recommendations to invest with both Merit Energy and TCW/Crescent, as stated in the Committee Report. Mr. McDonald seconded the motion. The motion passed.

The meeting adjourned at 2:45 p.m.

Respectfully submitted,

A handwritten signature in cursive script that reads "Howard Bicker".

Howard Bicker
Executive Director

Tab A

RETURN OBJECTIVES

Period Ending 3/31/96

COMBINED FUNDS: \$24.3 Billion	Return	Compared to Objective
Provide Real Return (10 yr.)	11.1% (1)	7.5 percentage points above target
Provide returns that are 3-5 percentage points greater than inflation over moving 10 year periods.		
Exceed Median Fund (5 yr.)	12.1% (1)	0.1 percentage point above target Rank: 47th percentile (2)
Outperform the median fund from a universe of public and corporate funds with a balanced asset mix over moving 5 year periods.		
Exceed Composite Index (5 yr.)	12.1% (1)	0.4 percentage point above target
Outperform a composite market index weighted in a manner that reflects the actual asset mix of the Combined Funds over moving 5 year periods.		

BASIC RETIREMENT FUNDS: \$12.8 Billion	Return	Compared to Objective
Exceed Composite Index (5 Yr.)	12.2%	0.4 percentage point above target
Outperform a composite index weighted in a manner that reflects the long-term asset allocation of the Basic Funds over moving 5 year periods.		

POST RETIREMENT FUND: \$11.5 Billion	Return	Compared to Objective
Exceed Composite Index	11.6% (3)	0.0 percentage point above target (3)
Outperform a composite index weighted in a manner that reflects the long-term asset allocation of the Post Fund over moving 5 year periods.		

(1) Reflects performance of Basic Funds only through 6/30/93, Combined Funds thereafter.

(2) The SBI's stated performance objective is to rank in the top half (above 50th percentile) of the comparative universe. The SBI will strive to achieve performance which ranks in the top third (above 33rd percentile).

(3) Since asset allocation transition to 50% domestic stocks was completed, 7/1/93, annualized.

ACTUARIAL VALUATIONS

MSRS, TRA, PERA General Plans June 30, 1995

	Active (Basics)	Retired (Post)	Total (Basics & Post)
Liability Measures			
1. Current and Future Benefit Obligation	\$16.9 billion	\$8.0 billion	\$24.9 billion
2. Accrued Liabilities	12.1	8.0	20.1
Asset Measures			
3. Current and Future Actuarial Value	\$16.7 billion	\$8.0 billion	\$24.7 billion
4. Current Actuarial Value	8.9	8.0	16.9
Funding Ratios			
Future Obligations vs. Future Assets (3 ÷ 1)	99%	100%	99%
Accrued Liabilities vs. Current Actuarial Value (4 ÷ 2)	74%	100%	84%*

* Ratio most frequently used by the Legislature and Retirement Systems.

The funding ratio required by **Governmental Standard Accounting Board Statement No. 5** compares Cost Value of assets to the Current Benefit Obligation. This calculation provides funded ratios of **83%** for the Basics, **100%** for the Post and **91%** for the Total, respectively.

Notes:

1. Present value of projected benefits that will be due to all current participants.
2. Liabilities attributed to past service calculated using entry age normal cost method.
3. Present value of future statutory contributions plus current actuarial value.
4. Same as required reserves for Post; Cost plus one-third of the difference between cost and market value for Basics.

Actuarial Assumptions:

Salary Growth: 6.5%

Interest/Discount Rate: 8.5% Basics, 5.0% Post

Full Funding Target Date: 2020

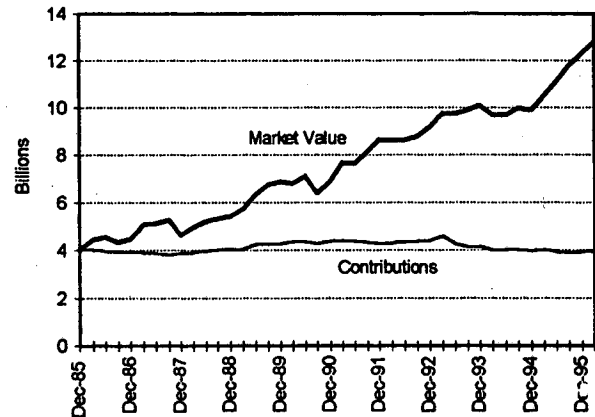
EXECUTIVE SUMMARY
Basic Retirement Funds

Asset Growth

The market value of the Basic Funds increased 3.7% during the first quarter of 1996. Positive investment returns accounted for the majority of the increase during the period.

Asset Growth
During First Quarter 1996
(Millions)

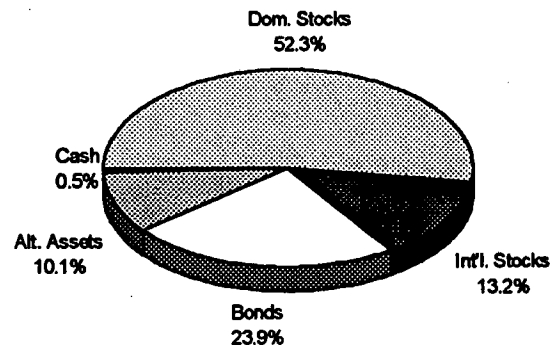
Beginning Value	\$ 12,338
Net Contributions	35
Investment Return	424
Ending Value	\$ 12,797



Asset Mix

Assets are moving from domestic stocks to international stocks to reflect the Board's new asset allocation targets to accommodate normal fund rebalancing.

	Policy Targets	Actual Mix 3/31/96	Actual Market Value (Millions)
Domestic Stocks	45.0%	52.3%	\$6,693
Int'l. Stocks	15.0	13.2	1,688
Bonds	24.0	23.9	3,059
Alternative Assets*	15.0	10.1	1,295
Unallocated Cash	1.0	0.5	62
	100.0%	100.0%	\$12,797

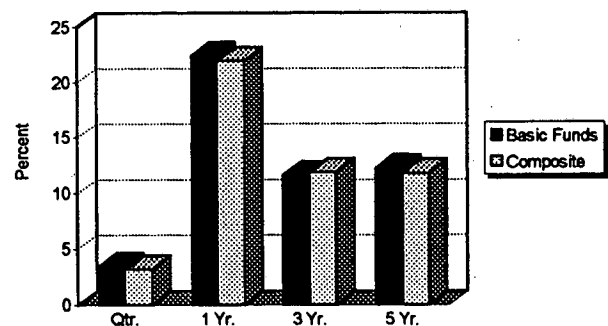


* Any uninvested allocation is held in domestic stocks

Fund Performance

The Basic Funds outperformed its composite market index for the quarter and for the year.

	Qtr.	1 Yr.	3 Yr.	5 Yr.
Basics	3.4%	22.4%	11.6%	12.2%
Composite	3.2	21.9	11.9	11.8



EXECUTIVE SUMMARY

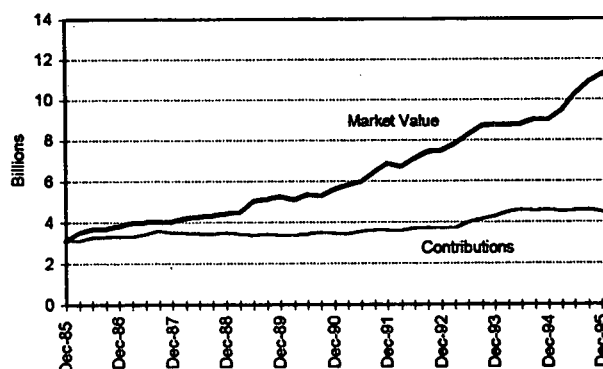
Post Retirement Fund

Asset Growth

The market value of the Post Fund increased 2.5% during the first quarter of 1996. The increase resulted from positive investment returns.

Asset Growth During First Quarter 1996 (Millions)

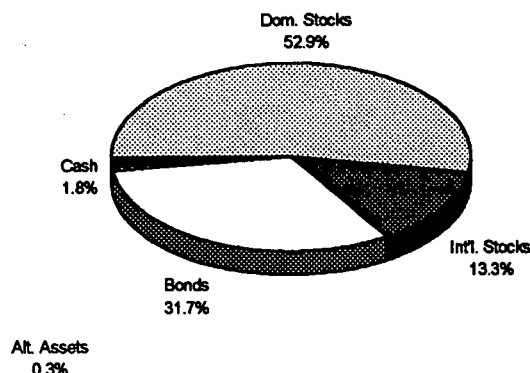
Beginning Value	\$ 11,216
Net Contributions	-55
Investment Return	335
Ending Value	\$ 11,496



Asset Mix

Assets are moving from bonds and domestic stocks to international stocks to reflect the Board's new asset allocation targets and to accommodate normal fund rebalancing.

	Policy Targets	Actual Mix 3/31/96	Actual Market Value (Millions)
Domestic Stocks	50.0%	52.9	\$6,082
Int'l. Stocks	15.0%	13.3	1,526
Bonds	27.0%	31.7	3,646
Alternative Assets*	5.0	0.3	35
Unallocated Cash	3.0	1.8	207
	100.0	100.0	\$11,496
	%	%	



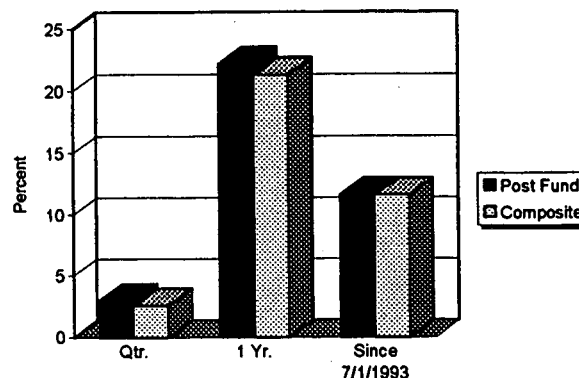
* Any uninvested allocation is held in bonds

Fund Performance

The Post Fund outperformed its composite market index for the quarter and for the year.

	Qtr.	1 Yr.	Since 7/1/93*
Post	3.0%	22.2%	11.6%
Composite	2.6	21.3	11.6

* Date asset allocation transition to 50% domestic common stocks was completed.



EXECUTIVE SUMMARY

Stock and Bond Manager Performance

Domestic Stocks

The domestic stock manager group (active, semi-passive and passive combined) outperformed its target for the quarter and trailed its target for the year.

	Qtr.	1 Yr.	3 Yr.	5 Yr.
Dom. Stocks	5.9%	31.7%	14.6%	14.5%
Wilshire 5000*	5.6	32.2	15.3	14.9

* Buy/hold index adjusted for liquor and tobacco restrictions through 3/31/93 and AHP restriction through 10/31/93.

International Stocks

The international stock manager group (active and passive combined) outperformed its target for the quarter and for the year.

	Qtr.	1 Yr.	3 Yr.	Since Incept.*
Int'l. Stocks	3.6%	16.5%	14.0%	14.2%
EAFE-Free	2.9	12.5	13.5	13.8

* since 10/1/92.

Bonds

The bond manager group (active and semi-passive combined) outperformed its target for the quarter and for the year.

	Qtr.	1 Yr.	3 Yr.	5 Yr.
Bonds	-1.7%	11.1%	6.3%	9.0%
Lehman Agg.*	-1.8	10.8	6.1	8.6

* Prior to July 1, 1994, the Salomon Broad Investment Grade Bond Index was used.

Note: The above returns reflect the performance of the Basic Funds' managers through 6/30/93 and of the Combined Funds (Basic and Post) since 7/1/93.

Wilshire 5000: The Wilshire 5000 stock index reflects the performance of all publicly traded stocks of companies domiciled in the U.S.

EAFE: The Morgan Stanley Capital International index of 20 stock markets in Europe, Australia and the Far East. EAFE-Free includes only those securities foreign investors are allowed to hold.

Lehman Aggregate: The Lehman Brothers Aggregate Bond Index reflects the performance of all investment grade (BAA or higher) bonds, U.S. treasury and agency securities and mortgage obligations with maturities greater than one year.

EXECUTIVE SUMMARY
Assigned Risk Plan

Investment Objectives

The Assigned Risk Plan has two investment objectives: to minimize the mismatch between assets and liabilities and to provide sufficient liquidity for the payment of on-going claims and operating expenses.

Asset Mix

The Assigned Risk Plan is invested in a balanced portfolio of common stocks and bonds. The actual asset mix will fluctuate in response to changes in the Plan's liability stream.

	3/31/96 Target	3/31/96 Actual
Stocks	20.0%	25.3%
Bonds	80.0	74.1
Unallocated Cash	0.0	0.6
Total	100.0%	100.0%

Investment Management

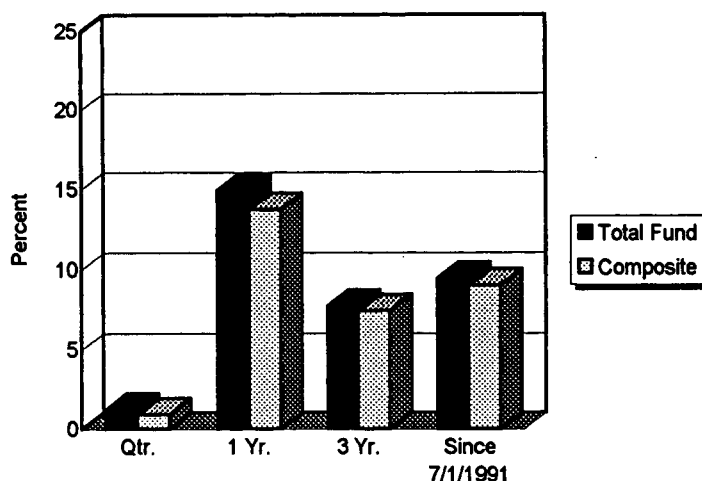
The entire portfolio was transferred from the Department of Commerce to the SBI in may 1991. Voyageur Asset Management has managed the bond segment of the Fund since inception. Since January 1995, GE Investment Management has managed the equity segment.

Performance Benchmarks

A custom benchmark has been established for the bond segment which reflects the duration of the liability stream and the long-term sector allocation of Voyageur Asset Management. The equity benchmark is the S&P 500 as of July 1, 1994. Prior to that date, the equity segment used a custom benchmark. The total fund benchmark is a combination of the fixed income and equity benchmarks, weighted according to the asset allocation target.

Market Value

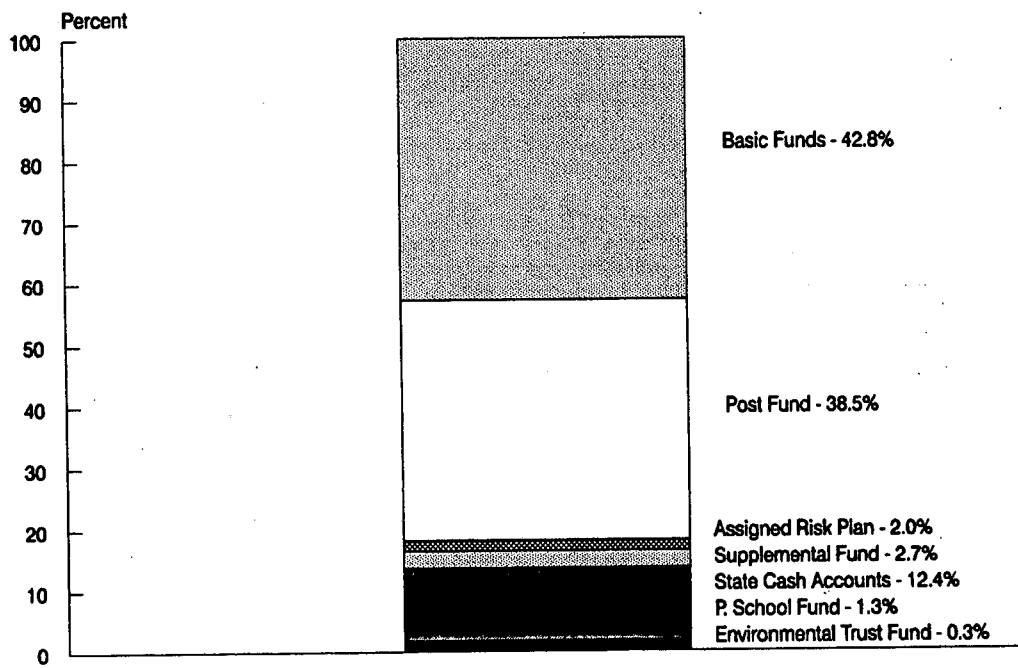
On March 31, 1996 the market value of the Assigned Risk Plan was \$542 million.



Period Ending 3/31/96

	Qtr.	Yr.	3 Yr.	Since 7/1/91
Total Fund	1.2%	14.9%	7.7%	9.4%
Composite Index	0.9	13.7	7.4	9.0
Equity Segment	6.4	32.2	12.4	12.9
Benchmark	5.5	32.3	13.7	13.6
Bond Segment	-0.5	10.2	6.1	8.4
Benchmark	-0.2	9.4	5.8	7.8

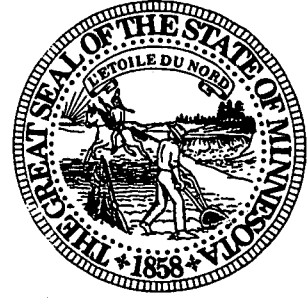
EXECUTIVE SUMMARY
Funds Under Management



3/31/96
Market Value
(Billions)

Basic Retirement Funds	\$12.8
Post Retirement Fund	11.5
Assigned Risk Plan	0.6
Supplemental Investment Fund	0.8
State Cash Accounts	3.7
Permanent School Fund	0.4
Environmental Trust Fund	0.1
Total	\$29.9

MINNESOTA STATE BOARD OF INVESTMENT



QUARTERLY INVESTMENT REPORT

First Quarter 1996
(January 1, 1996 - March 31, 1996)

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VARIOUS CAPITAL MARKET INDICES

	Period Ending 3/31/96				
	Qtr.	Yr.	3 Yr.	5 Yr.	10 Yr.
Domestic Equity					
Wilshire 5000	5.6%	32.2%	15.4%	15.0%	13.3%
Dow Jones Industrials	9.8	37.7	20.8	17.2	15.6
S&P 500	5.5	32.3	15.8	14.7	13.9
Russell 2000	5.1	29.0	14.8	16.0	10.4
Domestic Fixed Income					
Lehman Aggregate*	-1.8	10.8	6.0	8.5	8.6
Lehman Gov't./Corp.	-2.3	10.9	6.0	8.7	8.5
90 Day U.S. Treasury Bills	1.3	5.6	4.5	4.4	5.8
International					
EAFE**	2.9	12.3	13.4	8.4	11.0
Emerging Markets Free***	6.2	14.9	15.6	17.6	N/A
Salomon Non U.S. Gov't. Bond	-1.7	2.7	10.6	12.8	12.0
Inflation Measure					
Consumer Price Index****	1.4	2.8	2.7	2.9	3.6

* Lehman Brothers Aggregate Bond index. Includes governments, corporates and mortgages.

** Morgan Stanley Capital International index of Europe, Australia and the Far East (EAFE)

*** Morgan Stanley Capital International Emerging Markets Free index.

**** Consumer Price Index (CPI) for all urban consumers, also known as CPI-U.

FINANCIAL MARKETS REVIEW

DOMESTIC STOCKS

For the quarter, the stock market generated strong positive returns. The increase was due to reports of moderate inflation and economic growth as well as positive cashflows into equity mutual funds. All these factors created a strong overall equity market causing all sectors of the market, except utilities, to record positive returns. The top performing sectors were materials and service (9.4%) and capital goods (9.0%) and the weakest sector was utilities (-1.9%).

The Wilshire 5000 provided a 5.6% return for the quarter. Performance among the different Wilshire Style Indexes for the quarter is shown below:

Large Value	4.8%
Small Value	3.2
Large Growth	5.9
Small Growth	5.8

The Wilshire 5000 increased 32.2% during the latest year.

DOMESTIC BONDS

The bond market performed poorly this quarter as interest rates rose. While the market had anticipated that the Federal Reserve would lower rates, the lower rates did not materialize due to accumulating signs that the economy was expanding at a healthy pace. As a result, interest rates rose across the yield curve, especially in the shorter-maturity bonds that are most sensitive to actual and expected changes in monetary policy.

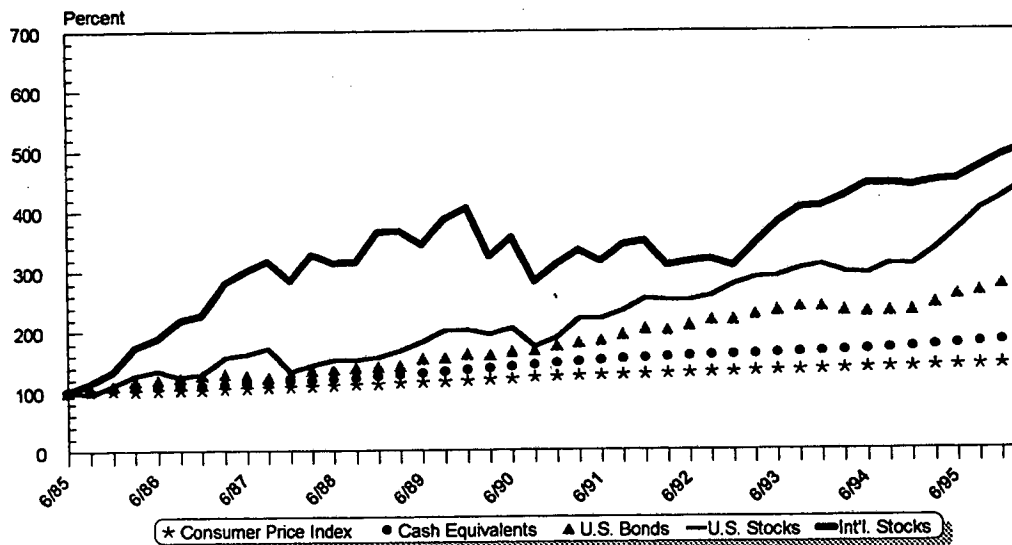
Overall, the Lehman Brothers Aggregate Bond Index declined 1.8% for the quarter. The Lehman Aggregate sector returns for the quarter were:

Treasury/Agency	-2.3%
Corporates	-2.6
Mortgages	-0.5

The Lehman Aggregate increased 10.8% for the latest year.

PERFORMANCE OF CAPITAL MARKETS

Cumulative Returns



Indices used are: Morgan Stanley's Index of Europe, Australia and the Far East (EAFE); Wilshire 5000 Index; Lehman Brothers Aggregate Bond Index; 91 Day Treasury Bills; and the Consumer Price Index.

FINANCIAL MARKETS REVIEW

INTERNATIONAL STOCKS

In aggregate, international stock markets (as measured by the EAFE index) provided a return of 2.9% for the quarter. As shown below, performance varied widely among the major markets:

Japan	0.4%
United Kingdom	0.2
Germany	5.1
France	8.7

The EAFE index increased by 12.3% during the latest year. The index is compiled by Morgan Stanley Capital International (MSCI) and is a measure of 20 markets located in Europe, Australia and the Far East (EAFE). The major markets listed above comprise about 75% of the value of the international markets in the index.

EMERGING MARKETS

Emerging markets (as measured by MSCI Emerging Markets Free index) provided a return of 6.2% for the quarter. The performance of the five largest stock markets is shown below:

Malaysia	14.4%
South Africa	-1.7
Brazil	11.3
Thailand	1.5
Mexico	10.3

The Emerging Markets Free index increased by 14.9% for the year. The index is compiled by MSCI and measures performance of 22 stock markets in Latin America, Asia and Africa. The markets listed above comprise about 65% of the value of the index.

REAL ESTATE

Nationally, many real estate markets are improving. Property types most favored by buyers at the present time include apartments, industrial parks and suburban office buildings. Shopping mall investments, however, are suffering writedowns which are reflective of the weak national retail environment.

PRIVATE EQUITY

According to the *Private Equity Analyst*, "total commitments to private equity partnerships of all kinds soared 29% in 1995 to \$27.2 billion. That's a new record, surpassing the previous peak of \$21.1 billion set in 1994." So far, 1996 looks to be another strong year for commitments to private equity partnerships.

RESOURCE FUNDS

Crude oil prices averaged \$19.50 per barrel* during the quarter compared to \$18.36 per barrel a year earlier. Natural gas prices averaged \$2.44 per thousand cubic feet* during the quarter compared to \$1.47 per thousand cubic feet during the same quarter last year.

* New York Mercantile Exchange futures prices

COMBINED FUNDS

The "Combined Funds" represent the assets of both the Basic and Post Retirement Funds. While the Combined Funds do not exist under statute, the Board finds it instructive to review asset mix and performance of all defined benefit pension assets under its control. This more closely parallels the structure of other public and corporate pension plan assets and therefore allows for more meaningful comparison with other pension fund investors.

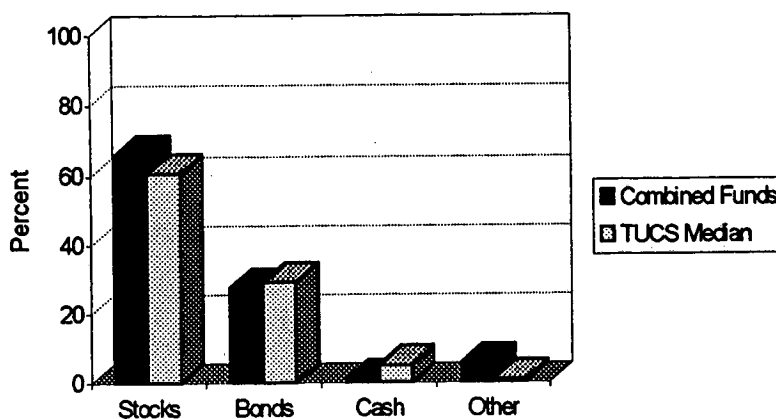
The comparison universe used by the SBI is the Master Trust portion of the Trust Universe Comparison Service (TUCS). This universe contains information on more than 200 public and corporate pension and trust funds with a balanced asset mix.

Asset Mix Compared to Other Pension Funds

On March 31, 1996, the actual asset mix of the Combined Funds was:

Comparisons of the Combined Funds' asset mix to the median allocation to stocks, bond and other assets of the public and corporate funds in TUCS on March 31, 1996 are shown below:

	\$ Millions	%
Domestic Stocks	\$12,775	52.6%
International Stocks	3,214	13.2
Bonds	6,705	27.6
Alternative Assets	1,330	5.5
Unallocated Cash	269	1.1
Total	\$24,293	100.0%



	Stocks*	Bonds*	Cash	Other
Combined Funds	65.8%	27.6%	1.1%	5.5%
Median Allocation in TUCS	60.5	29.2	5.0	0.8

* Both domestic and international.

**COMBINED FUNDS
Performance Compared to Other Pension Funds**

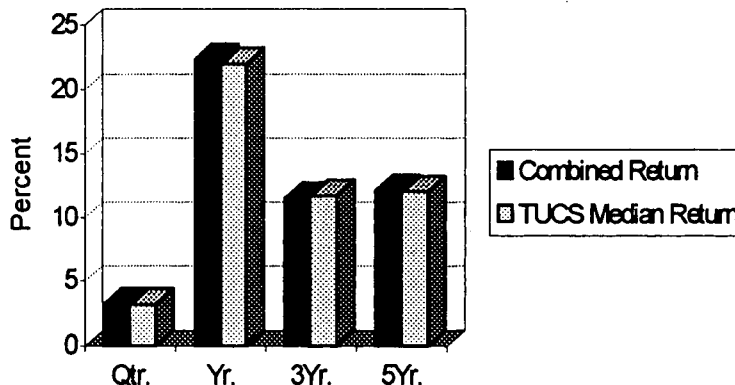
While the SBI is naturally concerned with how its returns compare to other pension investors, universe comparison data should be used with great care. There are several reasons why such comparisons will provide an “apples to oranges” look at performance:

- **Differing Treatment of Fees.** All SBI returns in this report are shown *after* all management fees while TUCS data is reported *before* fees. If the SBI reported returns before fees, its returns and rankings would be *higher* than those shown in this report.
- **Differing Allocations.** Asset allocation will have a dominant effect on return. The allocation to stocks among the funds in TUCS typically ranges from 20-90%, a very wide range for meaningful comparison.

In addition, it appears that many funds do not include alternative asset holdings in their reports to TUCS. This further distorts comparisons among funds.

- **Differing Goals/Liabilities.** Each pension fund structures its portfolio to meet its own liabilities and risk tolerance. This will result in different choices on asset mix. Since asset mix will largely determine investment results, a universe ranking is not relevant to a discussion of how well a plan sponsor is meeting its long-term liabilities.

With these considerations in mind, the performance of the Combined Funds compared to other public and corporate pension funds in TUCS are shown below:



Period Ending 3/31/96

	Annualized			
	Qtr.	Yr.	3 Yr.	5 Yr.
Combined Funds Return*	3.2%	22.3%	11.5%	12.1%
TUCS Median Fund Return**	3.2	22.0	11.7	12.0
Percentile Rank in TUCS	51st	47th	55th	47th

* After fees. Includes Basic Funds only through 6/30/93, Basic and Post thereafter.

** Before fees.

The SBI’s stated performance objective is that the Combined Funds will rank in the top half of the universe (above the 50th percentile) over the most recent

five year period. The SBI will strive to achieve performance which ranks in the top third (above the 33rd percentile).

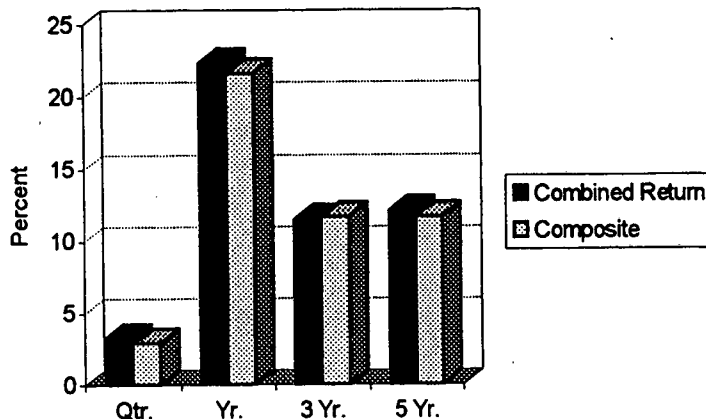
COMBINED FUNDS
Performance Compared to Composite Index

The Combined Funds' performance is evaluated relative to a composite of market indices. The composite is

weighted in a manner that reflects the asset allocation of the Combined Funds:

	Market Index	Combined Index Weights 1Q96*
Domestic Stocks	Wilshire 5000	50.7%*
Int'l. Stocks	EAFE-Free	13.1*
Bonds	Lehman Aggregate	28.9*
Alternative Assets	Wilshire Real Estate	2.1*
	Venture Capital Funds	2.9*
	Resource Funds	0.4*
Unallocated Cash	91 Day T-Bills	1.9
		100.0%

* Alternative asset, bond and domestic equity weights are reset in the composite at the start of each quarter to reflect the amount of unfunded commitments in alternative asset classes.



Period Ending 3/31/96

	Annualized			
	Qtr.	Yr.	3 Yr.	5 Yr.
Combined Funds**	3.2%	22.3%	11.5%	12.1%
Composite Index***	2.9	21.6	11.7	11.7

**Includes performance of Basic Funds through 6/30/93, Basic and Post Funds thereafter.

*** Adjusted to reflect the SBI's restrictions on liquor and tobacco stocks through 3/31/93 and AHP restriction through 10/31/93.

BASIC RETIREMENT FUNDS

Investment Objectives

The Basic Retirement Funds are composed of the retirement assets for currently working participants in eight statewide retirement funds. The Funds serve as accumulation pools for the pension contributions of public employees and their employers during the employees' years of active service. Approximately 250,000 public employees participate in the Basic Funds.

Employee and employer contribution rates are specified in state law as a percentage of an employee's salary. The rates are set so that contributions plus expected investment earnings will cover the projected cost of promised pension benefits. In order to meet these

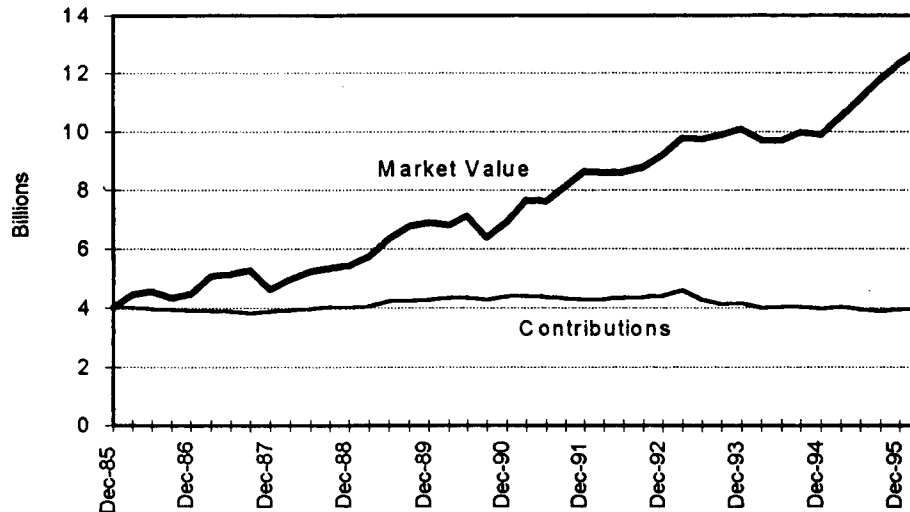
projected pension costs, the Basic Retirement Funds must generate investment returns of at least 8.5% on an annualized basis, over time.

Normally, pension assets will accumulate in the Basic Retirement Funds for thirty to forty years during an employee's years of active service. This provides the Basic Funds with a long investment time horizon and permits the Board to take an aggressive, high expected return investment policy which incorporates a sizeable equity component in order to meet or exceed its actuarial return target.

Asset Growth

The market value of the Basic Retirement Funds' assets increased 3.7% during the first quarter of 1996.

Positive net contributions and investment returns accounted for the increase.



Last Five Years

	In Millions					Latest Qtr.
	12/91	12/92	12/93	12/94	12/95	3/96
Beginning Value	\$6,919	\$8,639	\$9,191	\$10,086	9,890	\$12,338
Net Contributions	-92	-34	-239	-206	-29	35
Investment Return	1,812	586	1,134	-10	2,477	424
Ending Value	\$8,639	\$9,191	\$10,086	\$9,890	12,338	\$12,797

BASIC RETIREMENT FUNDS

Asset Mix

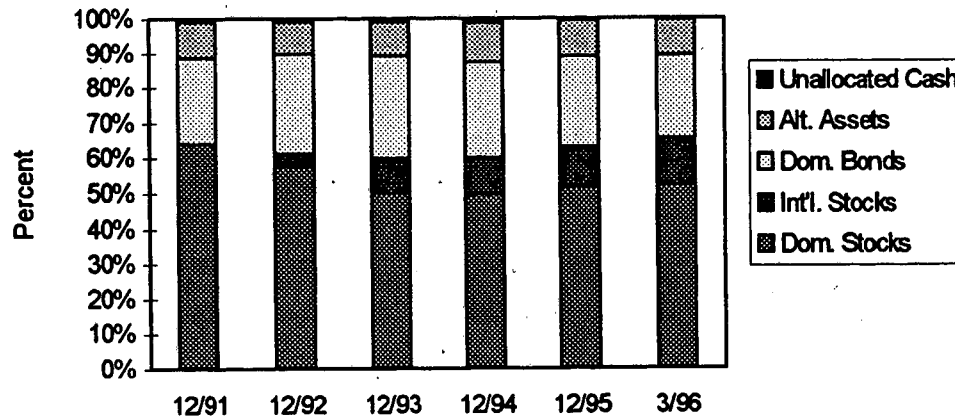
The long-term asset allocation of the Basic Funds is based on the superior performance of common stocks over the history of the capital markets. The asset allocation policy is designed to add value to the Basic Funds over their long-term investment time horizon.

Domestic Stocks	45.0%
Int'l. Stocks	15.0
Bonds	24.0
Alternative Assets*	15.0
Unallocated Cash	1.0

The actual asset mix changed from the prior quarter due to market movements and asset rebalancing.

In October 1995, the Board revised its long term asset allocation targets for the Basic Funds, increasing international stocks from 10% to 15% and decreasing domestic stocks from 50% to 45%. The change will be implemented over several quarters. Strong performance of the domestic stock market during recent quarters has also contributed to the overweighting in that category.

*Alternative assets include real estate, venture capital and resource funds. Any uninvested allocation is held in domestic stocks.



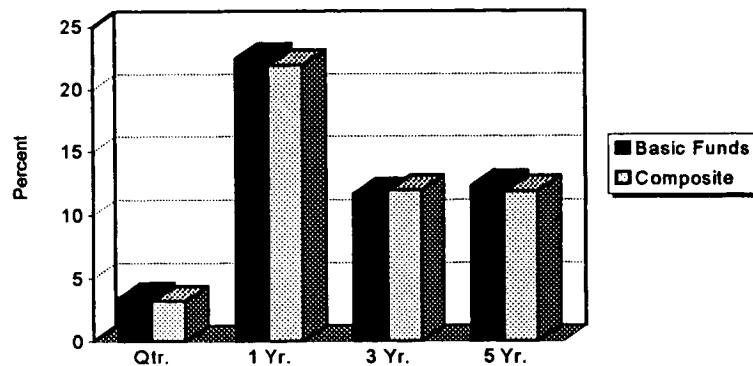
	Last Five Years					Latest Qtr.
	12/91	12/92	12/93	12/94	12/95	3/96
Domestic Stocks	63.9%	57.9%	49.9%	49.7%	51.7%	52.3%
Int'l. Stocks	0.0	3.2	10.0	10.3	11.3	13.2
Bonds	24.7	28.5	29.4	27.5	26.1	23.9
Real Estate	4.8	4.2	4.1	4.6	4.1	3.9
Private Equity	4.7	4.2	4.6	5.6	5.4	5.5
Resource Funds	1.1	1.2	1.1	0.9	0.7	0.7
Unallocated Cash	0.8	0.8	0.9	1.4	0.7	0.5
Total	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%

BASIC RETIREMENT FUNDS
Total Fund Performance

The Basic Funds' performance is evaluated relative to a composite of market indices. The composite is weighted in a manner that reflects the long-term asset allocation of the Funds:

	Basics Target	Market Index	Basics Composite 1Q96
Domestic Stocks	45.0%	Wilshire 5000	51.2%*
Int'l. Stocks	15.0	EAFE-Free	13.0
Bonds	24.0	Lehman Aggregate	24.5
Alternative Assets	15.0	Wilshire Real Estate Private Equity Funds Resource Funds	4.0* 5.5* 0.8*
Unallocated Cash	1.0	91 Day T-Bills	1.0
	100.0%		100.0%

* Alternative asset and domestic stock weights are reset in the composite each quarter to reflect the uninvested portion of the allocation to alternative assets.



Period Ending 3/31/96

	Annualized			
	Qtr.	Yr.	3 Yr.	5 Yr.
Basic Funds	3.4%	22.4%	11.6%	12.2%
Composite Index**	3.2	21.9	11.9	11.8

**Adjusted to reflect the SBI's restrictions on liquor and tobacco stocks through 3/31/93 and AHP restriction through 10/31/93.

Effective July 1, 1993, the Basic and Post Funds share the same stock, domestic bond and international stock managers. See page 14 for the performance of these asset pools. Performance of the Basic Funds' alternative assets is on page 15.

POST RETIREMENT FUND

The Post Retirement Investment Fund contains the pension assets of retired public employees covered by statewide retirement plans. Approximately 60,000 retirees receive monthly annuities from the assets of the Fund.

Upon an employee's retirement, a sum of money sufficient to finance the fixed monthly annuity is transferred from accumulation pools in the Basic Funds to the Post Fund. In order to support promised benefits, the Post Fund must "earn" at least 5% on its invested assets on an annualized basis. If the Post Fund exceeds this earnings rate, excess earnings are used to finance permanent benefit increases for eligible retirees.

Through fiscal year 1992, unrealized capital gains (or losses) were excluded from the statutory definition of

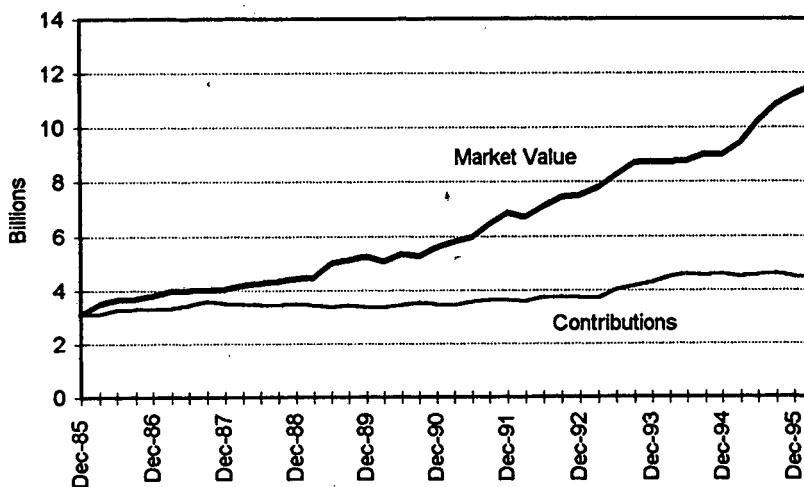
earnings. For this reason the Post Fund previously was not designed to maximize long-term total rates of return. Rather, the SBI attempted to generate a high, consistent stream of realized earnings for the Post Fund that maintained current benefits, as well as produced benefit increases over time.

Since fiscal year 1993, the post retirement benefit increase formula has been based on total return rather than realized earnings. As a result, the Board has adopted a new long-term asset allocation strategy for the Post Fund which incorporates a substantial commitment to common stocks. The transition to a 50% allocation to domestic stocks was completed by the end of fiscal year 1993.

Asset Growth

The market value of the Post Retirement Fund increased by 2.5% during the first quarter of 1996.

The increase was due to positive investment returns.



	In Millions					Latest Qtr.
	12/91	12/92	12/93	12/94	12/95	3/96
Beginning Value	\$5,590	\$6,855	\$7,500	\$8,766	9,001	\$11,216
Net Contributions	162	95	386	314	-102	-55
Investment Return	1,103	550	880	-79	2,317	335
Ending Value	\$6,855	\$7,500	\$8,766	\$9,001	11,216	\$11,496

POST RETIREMENT FUND
Asset Mix

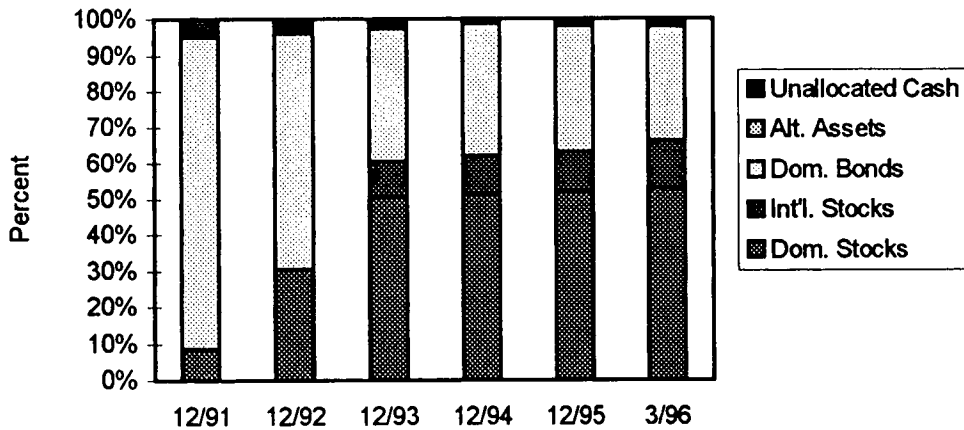
The Board adopted a new asset allocation strategy for the Post Fund in fiscal year 1993 which reflects the new post retirement benefit increase formula recently enacted by the Legislature. Throughout fiscal year 1993, the actual asset mix of the Post Fund moved toward a 50% allocation to common stocks. In fiscal year 1994, the Board added allocations to international stocks and alternative investments.

The large allocation to common stocks will allow the Fund to increase the long-term earning power of its assets and allow the Fund to focus on generating higher long-term total rates of return.

The actual asset mix changed from the prior quarter due to market movements and asset rebalancing.

In October 1995, the Board revised its long term asset allocation targets for the Post Fund, increasing international stocks from 10% to 15% and decreasing bonds from 32% to 27%. The change will be implemented over several quarters. Strong performance of the domestic stock market during recent quarters has also contributed to the overweighting in that category.

Domestic Stocks	50.0%
Int'l. Stocks	15.0
Bonds	27.0
Alternative Assets	5.0
Unallocated Cash	3.0
Total	100.0%



	Last Five years					Latest Qtr.
	12/91	12/92	12/93	12/94	12/95	3/96
Dom. Stocks	8.5%	30.6%	50.5%	51.2%	51.9%	52.9%
Int'l. Stocks	0.0	0.0	10.0	11.0	11.4	13.3
Bonds	86.5	65.6	36.9	36.5	34.7	31.7
Alt. Assets	0.0	0.0	0.0	0.1	0.2	0.3
Unallocated Cash	5.0	3.8	2.6	1.2	1.8	1.8
Total	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%

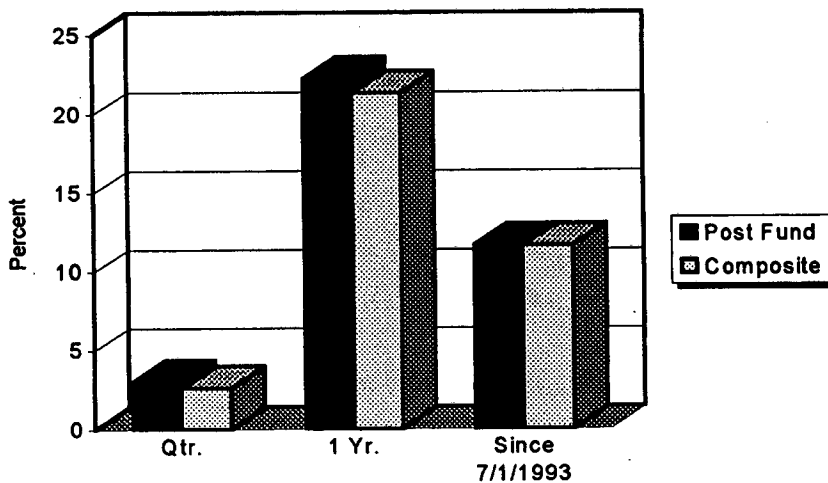
POST RETIREMENT FUND
Total Fund Performance

The Post Fund's performance is evaluated relative to a composite of market indices. The composite is weighted in a manner that reflects the long-term asset allocation of the Fund:

Asset Class	Post Target	Market Index	Post Composite 1Q96*
Domestic Stocks	50.0%	Wilshire 5000	50.0%
Int'l. Stocks	15.0	EAFE-Free	13.2
Bonds	27.0	Lehman Aggregate	33.8*
Alternative Assets	5.0	---	0.0*
Unallocated Cash	3.0	91 Day T-Bills	3.0
	100%		100.0%

*Alternative assets and bonds are reset in the composite each quarter to reflect the uninvested portion of the allocation to alternative assets.

The asset mix of the Post Fund moved to a 50% stock allocation during fiscal year 1993. The performance of the fund since 7/1/93 is shown below.



	Qtr.	1 Yr.	Since 7/1/93
Post Fund	3.0%	22.2%	11.6%
Composite Index	2.6	21.3	11.6

Effective July 1, 1993, the Basic and Post Funds share the same domestic stock, domestic bond and international stock managers. See page 14 for the performance of these asset pools.

STOCK AND BOND MANAGERS
Performance of Asset Pools

Domestic Stock Pool

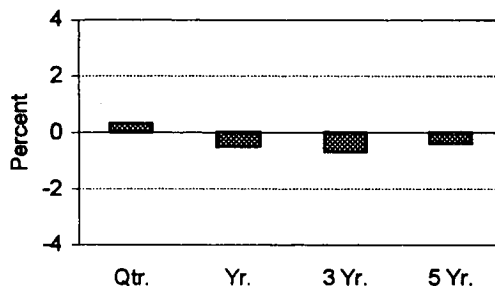
Target: Wilshire 5000 Adjusted*

Expectation: If half of the pool is actively managed and half is passively and semi-passively managed, the entire pool is expected to exceed the target by +.25-.55% annualized, over time.

	Qtr.	Yr.	Annualized	
			3 Yrs.	5 Yrs.
Stock Pool	5.9%	31.7%	14.6%	14.5%
Wilshire 5000*	5.6	32.2	15.3	14.9

*Adjusted for liquor and tobacco restrictions through 3/31/93 and AHP restriction through 10/31/93.

Value Added to Wilshire 5000 Adjusted



Bond Pool

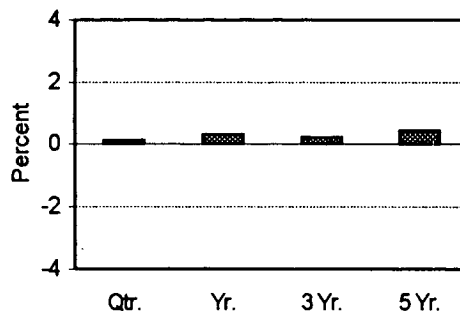
Target: Lehman Brothers Aggregate Bond Index

Expectation: If half of the pool is actively managed and half is managed semi-passively, the entire pool is expected to exceed the target by +.20-.35% annualized, over time.

	Qtr.	Yr.	Annualized	
			3 Yrs.	5 Yrs.
Bond Pool	-1.7%	11.1%	6.3%	9.0%
Lehman Agg.*	-1.8	10.8	6.1	8.6

* Prior to July 1, 1994, the Salomon Broad Investment Grade Bond Index was used.

Value Added to Lehman Aggregate*



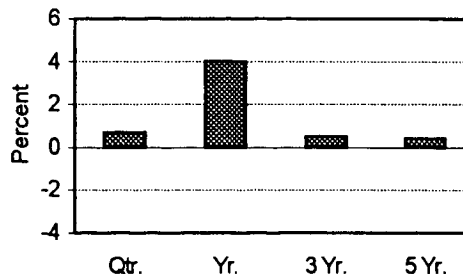
International Stock Pool

Target: EAFE-Free

Expectation: If half of the pool is managed actively and half managed passively, the entire pool is expected to exceed the target by +.25-.75% annualized, over time.

	Qtr.	Yr.	3 Yr.	Since 10/1/92
Int'l. Pool	3.6%	16.5%	14.0%	14.2%
EAFE-Free	2.9	12.5	13.5	13.8

Value Added to EAFE



ALTERNATIVE ASSET MANAGERS

Performance of Asset Pools

Real Estate Pool (Basic Funds only)

Expectation: Real estate investments are expected to exceed the rate of inflation by 3-5% annualized, over the life of the investment.

The Wilshire Real Estate Index contains returns of 30 commingled funds. The index does not include returns from funds that are less than 3 years old or are not fully invested.

	Qtr.	Yr.	Annualized	
			3 Yrs.	5 Yrs.
Real Estate	-1.6%	3.0%	2.5%	-1.9%
Real Estate Index	-1.6	-0.6	0.5	-3.6
Inflation	1.4	2.8	2.7	2.9

Private Equity Pool (Basic Funds only)

Expectation: Private equity investments are expected to provide annualized returns at least 3% greater than historical public equity returns, over the life of the investment. This equates to an absolute return of approximately 13-14% annualized.

The SBI began its private equity program in the mid-1980's. Some of the investments, therefore, are relatively immature and returns may not be indicative of future results.

	Qtr.	Yr.	Annualized	
			3 Yrs.	5 Yrs.
Private Equity	7.9%	24.8%	17.5%	18.3%

Resource Pool (Basic Funds only)

Expectation: Resource investments (primarily oil and gas) are expected to exceed the rate of inflation by 3-5% annualized, over the life of the investment.

The SBI began its resource program in the mid-1980's. Some of the investments, therefore, are relatively immature and returns may not be indicative of future results.

	Qtr.	Yr.	Annualized	
			3 Yrs.	5 Yrs.
Resource Funds	0.5%	21.0%	8.4%	8.0%

ASSIGNED RISK PLAN

Investment Objectives

The Assigned Risk Plan has two investment objectives: to minimize the mismatch between assets and liabilities and to provide sufficient liquidity for the payment of on-going claims and operating expenses.

Asset Mix

The Assigned Risk Plan is invested in a balanced portfolio of common stocks and bonds. The actual asset mix will fluctuate in response to changes in the Plan's liability stream.

	3/31/96 Target	3/31/96 Actual
Stocks	20.0%	25.3%
Bonds	80.0	74.1
Unallocated Cash	0.0	0.6
	100.0%	100.0%

Investment Management

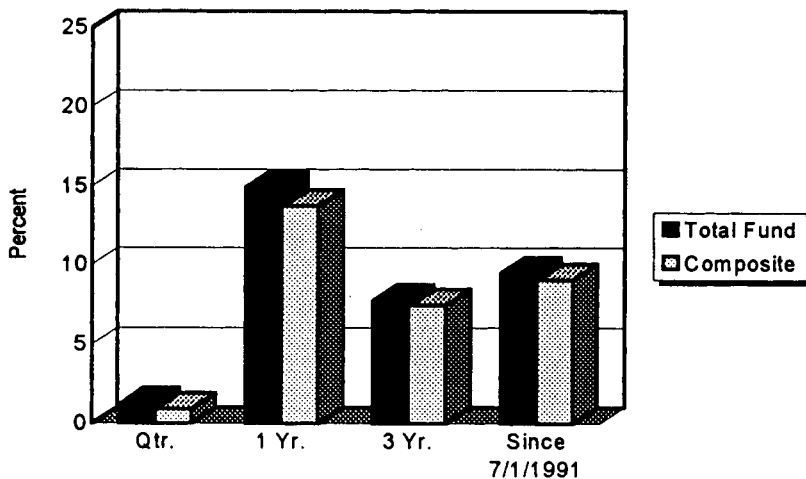
The portfolio was transferred from the Department of Commerce to the SBI on May 1, 1991. Voyager Asset Management has managed the bond segment of the Fund since inception. Since January 1995, GE Investment Management has managed the equity segment.

Performance Benchmarks

A custom benchmark has been established for the fixed income portfolio. It reflects the duration of the liability stream and the long-term sector allocation of Voyager Asset Management. The equity benchmark is the S&P 500 as of July 1, 1994. Prior to that date, the segment used a custom benchmark. The total fund benchmark is a combination of the fixed income and equity benchmarks, weighted according to the asset allocation target.

Market Value

On March 31, 1996 the market value of the Assigned Risk Plan was \$542 million.



	Period Ending 3/31/96			
	Qtr.	Yr.	3 Yr.	Since 7/1/91
Total Account	1.2%	14.9%	7.7%	9.4%
Composite	0.9	13.7	7.4	9.0
Equity Segment	6.4	32.2	12.4	12.9
Benchmark	5.5	32.3	13.7	13.6
Bond Segment	-0.5	10.2	6.1	8.4
Benchmark	-0.2	9.4	5.8	7.8

SUPPLEMENTAL INVESTMENT FUND

The Minnesota Supplemental Investment Fund is a multi-purpose investment program that offers a range of investment options to state and local public employees. The different participating groups use the Fund for a variety of purposes:

1. It functions as the investment manager for all assets of the Unclassified Employees Retirement Plan, Public Employees Defined Contribution Plan and Hennepin County Supplemental Retirement Plan.
2. It is one investment vehicle offered to employees as part of the state's Deferred Compensation Plan, the Individual Retirement Account Plan and College Supplemental Retirement Plan.
3. It serves as an external money manager for a portion of some local police and firefighter retirement plans.

A wide diversity of investment goals exists among the Fund's participants. In order to meet those needs, the Fund has been structured much like a "family of mutual funds." Participants may allocate their investments among one or more accounts that are appropriate for their needs, within the statutory requirements and rules established by the participating organizations. Participation in the Fund is accomplished through the purchase or sale of shares in each account.

The investment returns shown in this report are calculated using a time-weighted rate of return formula. They are net of investment management fees but they do *not* include a deduction for asset based charges used to defray costs of the administering retirement organizations.

On March 31, 1996 the market value of the entire fund was \$778 million.

Investment Options

Income Share Account - a balanced portfolio utilizing both common stocks and bonds.

Growth Share Account - an actively managed, all common stock portfolio.

Common Stock Index Account - a passively managed, all common stock portfolio designed to track the performance of the entire U.S. stock market.

International Share Account - a portfolio of non U.S. stocks that incorporates both active and passive management.

Bond Market Account - an actively managed, all bond portfolio.

Money Market Account - a portfolio utilizing short-term, liquid debt securities.

Fixed Interest Account - an option utilizing guaranteed investment contracts (GIC's), which offer a fixed rate of return for a specified period of time.

SUPPLEMENTAL INVESTMENT FUND
Income Share Account

Investment Objective

The primary investment objective of the Income Share Account is similar to that of the Combined Funds. The Account seeks to maximize long-term real rates of return, while limiting short-run portfolio return volatility.

Asset Mix

The Income Share Account is invested in a balanced portfolio of common stocks and bonds. Common stocks provide the potential for significant capital appreciation, while bonds act as a deflation hedge and provide portfolio diversification.

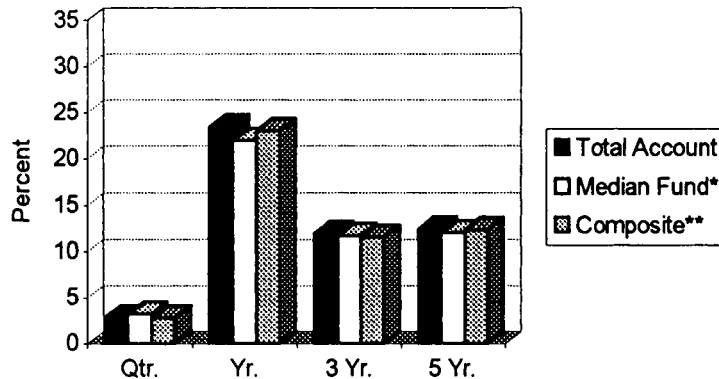
	Target	Actual
Stocks	60.0%	60.7%
Bonds	35.0	33.1
Unallocated Cash	5.0	6.2
	100.0%	100.0%

Investment Management

The Account combines internal and external management. SBI staff manage the entire fixed income segment. Throughout the period shown below, the entire stock segment has been managed as part of a passively managed index fund designed to track the Wilshire 5000. The current manager for these assets is BZW Barclays Global Investors. Prior to April 1988, a significant portion of the stock segment was actively managed.

Market Value

On March 31, 1996 the market value of the Income Share Account was \$381 million.



	Period Ending 3/31/96			
	Qtr.	Yr.	3 Yr.	5 Yr.
Total Account	2.8%	23.4%	11.9%	12.4%
Median Fund*	3.2	22.0	11.7	12.0
Composite**	2.8	23.0	11.5	12.3
Equity Segment	5.6	31.1	15.5	15.1
Wilshire 5000***	5.6	32.2	15.3	14.9
Bond Segment	-1.6	12.0	6.4	9.0
Lehman Agg.****	-1.8	10.8	6.1	8.6

*TUCS Median Master Trust

**60% Wilshire 5000/35% Lehman Aggregate Bond Index/5% T-Bills Composite. Wilshire 5000 is adjusted as noted below.

*** Buy/hold index adjusted for liquor and tobacco restrictions through 3/31/93 and AHP restriction through 10/31/93.

**** Prior to 7/1/94 the Salomon BIG was the benchmark and a component of the Composite.

SUPPLEMENTAL INVESTMENT FUND
Growth Share Account

Investment Objective

The Growth Share Account's investment objective is to generate above-average returns from capital appreciation on common stocks.

Asset Mix

The Growth Share Account is invested almost entirely in common stocks. Generally, the small cash equivalents component represents the normal cash reserves held by the Account as a result of net contributions not yet allocated to stocks or held in reserve to accommodate withdrawals.

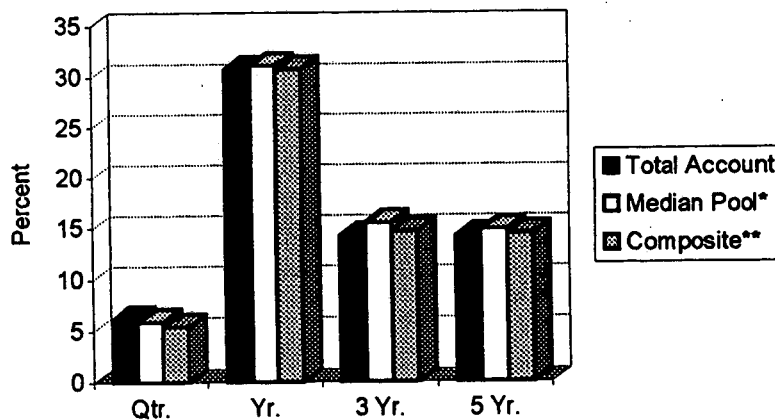
Investment Management

Throughout the period shown below, the entire Account has been managed by the same group of active external stock managers utilized by the Basic and Post Retirement Funds. Prior to April 1988, other active managers controlled a substantial portion of the account.

Market Value

On March 31, 1996 the market value of the Growth Share Account was \$151 million.

	Target	Actual
Stocks	95.0%	94.7%
Unallocated Cash	5.0	5.3
	100.0%	100.0%



Period Ending 3/31/96

	Annualized			
	Qtr.	Yr.	3 Yr.	5 Yr.
Total Account	6.1%	30.7%	14.2%	14.2%
Median Pool*	5.9	31.1	15.5	14.8
Composite**	5.4	30.7	14.7	14.4

* TUCS Median Equity Pool

** 95% Wilshire 5000/5% T-Bills Composite. Wilshire 5000 buy/hold index is adjusted for liquor and tobacco restrictions through 3/31/93 and AHP restriction through 10/31/93.

SUPPLEMENTAL INVESTMENT FUND
Common Stock Index Account

Investment Objective and Asset Mix

The investment objective of the Common Stock Index Account is to generate returns that match those of the U.S. common stock market. The Account is designed to track the performance of the Wilshire 5000, a broad-based equity market indicator.

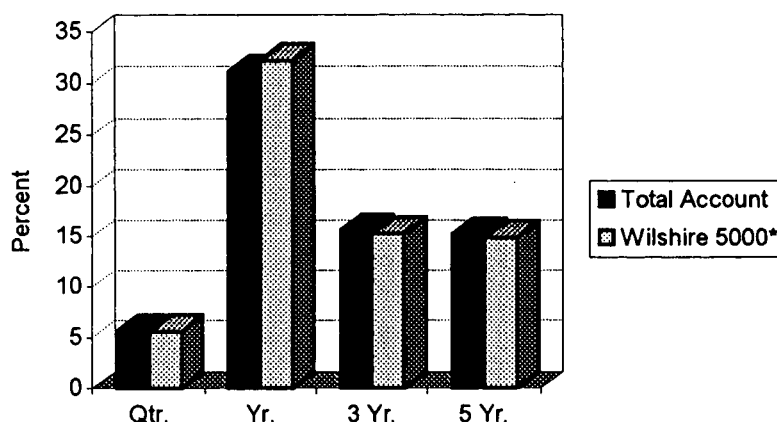
The Account is invested 100% in common stock.

Investment Management

Until July 1995, the entire Account was managed by Wilshire Associates as part of a passively managed index fund. Since July 1995, the Account has been managed by BZW Barclays Global Investors (formerly Wells Fargo Nikko).

Market Value

On March 31, 1996 the market value of the Common Stock Index Account was \$89 million.



Period Ending 3/31/96

Annualized

Qtr. Yr. 3 Yr. 5 Yr.

Total Account	5.6%	31.1%	15.6%	15.2%
Wilshire 5000*	5.6	32.2	15.3	14.9

*Buy/hold index adjusted for liquor and tobacco restrictions through 3/31/93 and AHP restriction through 10/31/93.

SUPPLEMENTAL INVESTMENT FUND
International Share Account

Investment Objective and Asset Mix

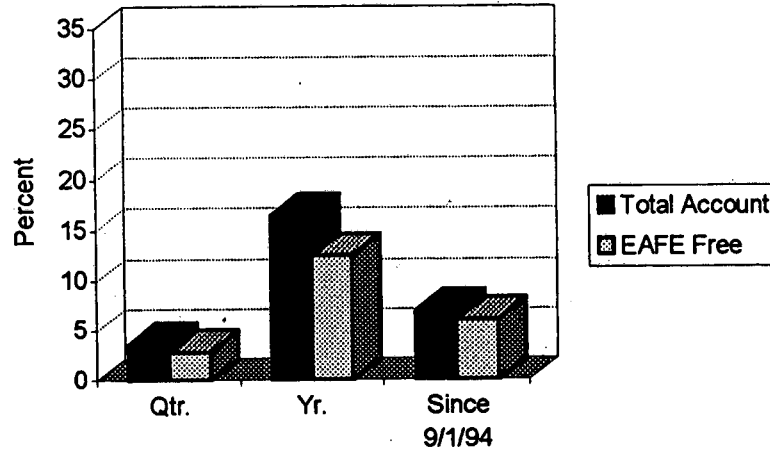
The investment objective of the International Share Account is to earn a high rate of return by investing in the stock of companies outside the U.S. Approximately half of the Account is "passively managed" and is designed to track the return of 20 markets included in the Morgan Capital International index of Europe, Australia and the Far East (EAFE-Free). The remainder of the Account is "actively managed" by several international managers who buy and sell stocks in an attempt to maximize market value.

Investment Management

The Account was opened for contributions in September 1994. Beginning October 1994, the Account uses the same group of international active and passive international stock managers as the Basic and Post Retirement Funds.

Market Value

On March 31, 1996 the market value of the International Share Account was \$13 million.



	Period Ending 3/31/96		
	Qtr.	Yr.	Since 9/1/94
Total Account	3.6%	16.4%	6.9%
EAFE Free	2.9	12.5	6.1

SUPPLEMENTAL INVESTMENT FUND
Bond Market Account

Investment Objective

The investment objective of the Bond Market Account is to earn a high rate of return by investing in fixed income securities.

Asset Mix

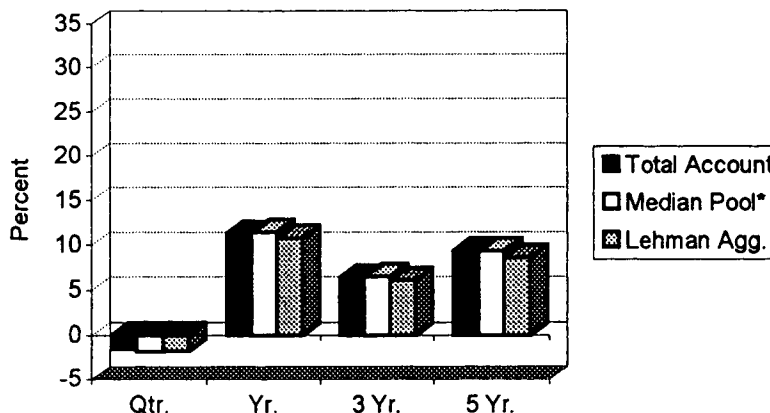
The Bond Market Account invests primarily in high-quality, government and corporate bonds that have intermediate to long-term maturities, usually 3 to 20 years.

Investment Management

The entire Account is managed by the same group of active external bond managers utilized by the Basic and Post Retirement Funds.

Market Value

On March 31, 1996 the market value of the Bond Market Account was \$24 million.



Period Ending 3/31/96
Annualized

	Qtr.	Yr.	3 Yr.	5 Yr.
Total Account	-1.6%	11.3%	6.4%	9.3%
Median Pool*	-1.9	11.4	6.5	9.3
Lehman Aggregate**	-1.8	10.8	6.1	8.6

* TUCS Median Fixed Income Pool

** Prior to July 1, 1994, the Salomon Broad Investment Grade Index was used.

SUPPLEMENTAL INVESTMENT FUND
Money Market Account

Investment Objective

The investment objective of the Money Market Account is to purchase short-term, liquid fixed income investments that pay interest at rates competitive with those available in the money markets.

Asset Mix

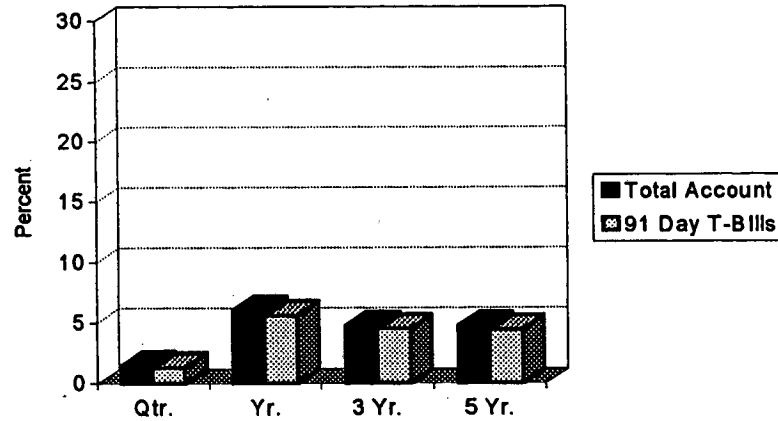
The Money Market Account is invested entirely in high quality short-term investments such as U.S. Treasury Bills, bank certificates of deposit, repurchase agreements, and high grade commercial paper. The average maturity of these investments is 30 to 60 days.

Investment Management

The Money Market Account is managed by State Street Bank and Trust Company. State Street manages a major portion of the Board's cash reserves.

Market Value

On March 31, 1996 the market value of the Money Market Account was \$51 million.



	Period Ending 3/31/96			
	Qtr.	Yr.	3 Yr.	5 Yr.
Total Account	1.4%	6.0%	4.7%	4.7%
91 Day T-Bills	1.3	5.6	4.5	4.4

SUPPLEMENTAL INVESTMENT FUND

Fixed Interest Account

Investment Objectives

The investment objectives of the Fixed Interest Account are to protect investors from loss of their original investment and to provide competitive interest rates using somewhat longer term investments than typically found in a money market account.

Asset Mix

The Fixed Interest Account is invested in guaranteed investment contracts (GIC's) offered by major U.S. insurance companies and banks and GIC type investments. Effective November 1, 1994 new contributions into the Account are deposited into a new pool of GIC's and GIC-type investments. The pool has a blend of maturities and a credited interest rate that changes monthly. The remaining GIC will mature in October 1996.

Investment Management

Since November 1, 1994, the new portfolio of GIC's and GIC-type investments has been managed by Galliard Capital Management (formerly Norwest Investment Management).

Market Value

On March 31, 1996 the market value of the Fixed Interest Account was \$69 million.

Existing 3 Year Contracts

Contract Period	Annual Effective Interest Rate	Manager
Nov. 1, 1993-Oct. 31, 1996	4.625% (blended rate)	Principal Mutual/Hartford Life

Blended Portfolio	Annualized Credited Interest Rate	Period Ending 3/31/96		
		Qtr.	Yr.	Since 11/1/94
Nov. 94	5.750%			
Dec.	6.790			
Jan. 95	6.790			
Feb.	7.310	Total Pool	1.6%	6.9%
Mar.	6.910			6.9%
Apr.	6.900			
May	6.690			
Jun.	7.012			
Jul.	6.822			
Aug.	7.001			
Sep.	6.983			
Oct.	6.826			
Nov.	6.664			
Dec.	6.493			
Jan. 96	6.482			
Feb.	6.678			
Mar.	6.863			

PERMANENT SCHOOL FUND

Investment Objectives

The objective of the Permanent School Fund is to provide a high, consistent stream of income to assist in offsetting state expenditures on school aid while maintaining adequate portfolio quality.

The Permanent School Fund's investment objectives have been influenced by the legal provisions under which its investments must be managed. These provisions require that the Permanent School Fund's principal remain inviolate. Further, any net realized equity and fixed income capital gains must be added to principal. Moreover, if the Permanent School Fund realizes net capital losses, these losses must be offset against interest and dividend income before such income can be distributed. Finally, all interest and dividend income must be distributed in the year in which it is earned.

These legal provisions have limited the investment time horizon over which the Permanent School Fund is managed. Long-run growth in its assets is difficult to achieve without seriously reducing current spendable income and exposing the spendable income stream to unacceptable volatility. The SBI, therefore, has invested the Permanent School Fund's assets to produce the maximum amount of current income, within the constraint of maintaining adequate portfolio quality.

Asset Mix

The Permanent School Fund is invested entirely in a portfolio of fixed income securities to maximize current income.

Investment Management

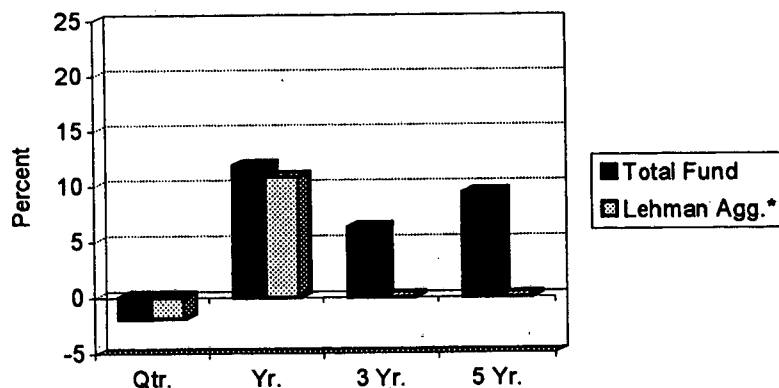
The Permanent School Fund is managed internally by SBI staff. The investment approach utilizes sector trading and relative spread analysis of both sectors and individual issues. The portfolio weightings in mortgage and corporate securities are consistently equal to or greater than the market weightings. The portfolio duration remains close to the benchmark duration but may be slightly shorter or longer depending on the economic outlook. (Prior to July 1993 the fund used a buy and hold, laddered maturity structure).

Performance Benchmarks

Since July 1994 the Lehman Aggregate Index has been the benchmark for the Permanent School Fund. Prior to that date, an acceptable benchmark for the laddered portfolio was not available.

Market Value

On March 31, 1996 the market value of the Permanent School Fund was \$421 million.



Period Ending 3/31/96
Qtr. Yr. 3 Yr. 5 Yr.

Total Fund	-1.9%	11.8%	6.2%	9.3%
Lehman Agg.	-1.8	10.8	NA	NA

ENVIRONMENTAL TRUST FUND

Investment Objective

The Environmental Trust Fund's objective is to produce a growing level of spendable income, within the constraints of maintaining adequate portfolio quality and liquidity.

Asset Mix

The Environmental Trust Fund is invested in a balanced portfolio of common stocks and bonds. Common stocks provide the potential for significant capital appreciation, while bonds act as a deflation hedge and provide portfolio diversification.

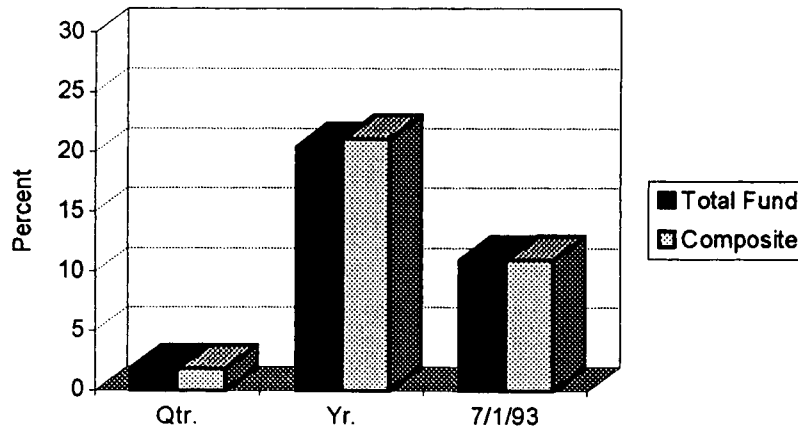
Investment Management

SBI staff manage all assets of the Environmental Trust Fund. The bond segment is actively managed to add incremental value through sector, security and yield curve decisions. The stock segment is passively managed to track the performance of the S&P 500.

Market Value

On March 31, 1996 the market value of the Environmental Trust Fund was \$132 million.

	Target	Actual
Stocks	50.0%	49.1%
Bonds	50.0	46.8
Unallocated Cash	0.0	4.1
	100.0%	100.0%



	Period Ending 3/31/96		
	Qtr.	1 Yr.	Since 7/1/93
Total Fund	1.8%	20.4%	10.9%
Composite	1.8	21.1	11.0
Equity Segment	5.4	32.0	17.1
S&P 500	5.5	32.3	17.1
Bond Segment	-1.9	10.8	6.0
Lehman Agg.	-1.8	10.8	5.6

STATE CASH ACCOUNTS

Description

State Cash Accounts represent the cash balances in more than 400 separate accounts that flow through the Minnesota State Treasury. These accounts range in size from \$5,000 to over \$400 million.

Most accounts are invested by SBI staff through two short-term pooled funds:

1. Trust Fund Pool contains the cash balances of retirement-related accounts managed internally and cash balances in the Permanent School Fund.
2. Treasurer's Cash Pool contains the cash balances of special or dedicated accounts necessary for the operation of certain State agencies and the balance of the Invested Treasurer's Cash.

In addition, each State of Minnesota bond sale requires two additional pools; one for bond proceeds and one for the debt reserve transfer.

Because of special legal restrictions, a small number of cash accounts cannot be commingled. These accounts are invested separately.

Investment Objectives

Safety of Principal. To preserve capital.

Competitive Rate of Return. To provide a high level of current income.

Liquidity. To meet cash needs without the forced sale of securities at a loss.

Asset Mix

The SBI maximizes current income while preserving capital by investing all cash accounts in high quality, liquid short term investments. These include U.S. Treasury and Agency issues, repurchase agreements, bankers acceptances, commercial paper, and certificates of deposit.

Investment Management

All state cash accounts are managed by the SBI investment staff. As noted above, most of the assets of the cash accounts are invested through two large commingled investment pools.

Period Ending 3/31/96

	Market Value (Millions)	Qtr.	Yr.	3 Yrs. Annualized
Treasurer's Cash Pool	\$3,113	1.2%	6.2%	4.8%
Trust Fund Cash Pool	111	1.4	6.1	4.9
Benchmark*		1.1	6.5	4.8
91-Day T-Bills		1.3	5.6	4.5

* 75% State Street Short Term Investment Fund/25% 1-3 Year Treasuries. This benchmark was established in April 1993. The Investment Advisory Council (IAC) intend to review the appropriateness of this benchmark in FY96. Until that time, the IAC believes that the pools should continue to be monitored against 91-Day T-Bills.

Tab B

PORTFOLIO STATISTICS

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I. Composition of State Investment Portfolios 3/31/96	1
II. Cash Flow Available for Investment 12/31/95 - 3/31/96	4
III. Monthly Transactions and Asset Summary - Retirement Funds	5

MINNESOTA STATE BOARD OF INVESTMENT
Composition of State Investment Portfolios By Type of Investment
Market Value March 31, 1996 (in Millions)

	Cash And Short Term Securities	Bonds Internal	Bonds External	Stocks Internal	Stocks External	External Int'l.	Alternative Assets	Total
BASIC RETIREMENT FUNDS:								
Teachers Retirement Fund	\$43,864 0.80%	-0-	\$1,317,730 23.80%	-0-	\$2,889,054 52.18%	\$727,940 13.14%	\$558,351 10.08%	\$5,536,939 100%
Public Employees Retirement Fund	\$11,549 0.43%	-0-	\$645,486 23.90%	-0-	\$1,413,432 52.34%	\$356,581 13.20%	\$273,492 10.13%	\$2,700,540 100%
State Employees Retirement Fund	\$54 0.00%	-0-	\$617,448 24.01%	-0-	\$1,351,453 52.55%	\$341,092 13.26%	\$261,612 10.18%	\$2,571,659 100%
Public Employees Police & Fire Fund	\$5,415 0.42%	-0-	\$305,127 23.90%	-0-	\$668,143 52.34%	\$168,559 13.21%	\$129,286 10.13%	\$1,276,530 100%
Highway Patrol Retirement Fund	\$4 0.00%	-0-	\$44,148 24.02%	-0-	\$96,559 52.53%	\$24,388 13.27%	\$18,706 10.18%	\$183,805 100%
Judges Retirement Fund	\$66 0.48%	-0-	\$3,275 23.89%	-0-	\$7,171 52.31%	\$1,809 13.20%	\$1,388 10.12%	\$13,709 100%
Public Employees P.F. Consolidated	\$76 0.02%	\$2,265 0.60%	\$90,349 24.04%	\$25 0.01%	\$194,934 51.86%	\$49,913 13.28%	\$38,290 10.19%	\$375,852 100%
Correctional Employees Retirement	\$667 0.48%	-0-	\$32,985 23.89%	-0-	\$72,228 52.31%	\$18,222 13.20%	\$13,976 10.12%	\$138,078 100%
POST RETIREMENT FUND	\$207,107 1.80%	-0-	\$3,645,882 31.72%	\$35,542 0.31%	\$6,081,730 52.90%	\$1,525,691 13.27%	-0-	\$11,495,952 100%
TOTAL BASIC & POST	\$268,802 1.11%	\$2,265 0.01%	\$6,702,430 27.59%	\$35,567 0.15%	\$12,774,704 52.58%	\$3,214,195 13.23%	\$1,295,101 5.33%	\$24,293,064 100%

	Cash And Short Term Securities		Bonds		Stocks		External Int'l.		Alternative Assets		Total
	Internal	External	Internal	External	Internal	External	Internal	External	Internal	External	
MINNESOTA SUPPLEMENTAL FUNDS:											
Income Share Account	\$23,454 6.16%	\$126,153 33.15%	-0-	-0-	-0-	\$230,943 60.69%	-0-	-0-	-0-	-0-	\$380,550 100%
Growth Share Account	\$7,955 5.28%	-0-	-0-	-0-	-0-	\$142,760 94.72%	-0-	-0-	-0-	-0-	\$150,715 100%
Money Market Account	\$51,260 100%	-0-	-0-	-0-	-0-	-0-	-0-	-0-	-0-	-0-	\$51,260 100%
Common Stock Index Account	-0-	-0-	-0-	-0-	-0-	\$89,433 100%	-0-	-0-	-0-	-0-	\$89,433 100%
Bond Market Account	-0-	-0-	-0-	\$24,333 100%	-0-	-0-	-0-	-0-	-0-	-0-	\$24,333 100%
International Share Account	-0-	-0-	-0-	-0-	-0-	-0-	\$12,576 100%	-0-	-0-	-0-	\$12,576 100%
Fixed Interest Account	-0-	-0-	-0-	\$68,665 100%	-0-	-0-	-0-	-0-	-0-	-0-	\$68,665 100%
TOTAL SUPPLEMENTAL FUNDS	\$82,669 10.63%	\$126,153 16.22%	-0-	\$92,998 11.96%	-0-	\$463,136 59.57%	\$12,576 1.62%	-0-	-0-	-0-	\$777,532 100%
TOTAL RETIREMENT FUNDS	\$351,471 1.40%	\$128,418 0.51%	\$6,795,428 27.11%	\$35,567 0.14%	\$13,237,840 52.80%	\$3,226,771 12.87%	\$1,295,101 5.17%				\$25,070,596 100%

	Cash And Short Term Securities	Bonds Internal	Bonds External	Stocks Internal	Stocks External	External Int'l.	Alternative Assets	Total
ASSIGNED RISK PLAN	\$11,379 2.10%	-0-	\$399,808 73.77%	-0-	\$130,810 24.13%	-0-	-0-	\$541,997 100%
ENVIRONMENTAL FUND	\$5,364 4.06%	\$61,891 46.84%	-0-	\$64,874 49.10%	-0-	-0-	-0-	\$132,129 100%
PERMANENT SCHOOL FUND	\$12,737 2.96%	\$417,116 97.04%	-0-	-0-	-0-	-0-	-0-	\$429,853 100%
TREASURERS CASH	\$3,116,949 100%	-0-	-0-	-0-	-0-	-0-	-0-	\$3,116,949 100%
HOUSING FINANCE AGENCY	\$67,545 29.09%	\$164,686 70.91%	-0-	-0-	-0-	-0-	-0-	\$232,231 100%
MINNESOTA DEBT SERVICE FUND	\$8,132 29.35%	\$19,576 70.65%	-0-	-0-	-0-	-0-	-0-	\$27,708 100%
MISCELLANEOUS ACCOUNTS	\$93,907 27.31%	\$249,915 72.69%	-0-	-0-	-0-	-0-	-0-	\$343,822 100%
GRAND TOTAL	\$3,667,484 12.27%	\$1,041,602 3.48%	\$7,195,236 24.07%	\$100,441 0.34%	\$13,368,650 44.72%	\$3,226,771 10.79%	\$1,295,101 4.33%	\$29,895,285 100%

**STATE OF MINNESOTA
STATE BOARD OF INVESTMENT**

**Net Cash Flow Available For Investment
January 1, 1996 - March 31, 1996**

Teachers Retirement Fund	\$47,200,000.00
Public Employees Retirement Fund	(1,500,000.00)
State Employees Retirement Fund	(13,000,000.00)
Public Employees Police & Fire	3,450,000.00
Highway Patrol Retirement Fund	(1,000,000.00)
Judges Retirement Fund	0.00
Public Employees P&F Consolidated	289,591.32
Correctional Employees Retirement Fund	0.00
Post Retirement Fund	(54,767,156.65)
Supplemental Retirement Fund - Income	317,669.80
Supplemental Retirement Fund - Growth	283,371.10
Supplemental Retirement Fund - Money Market	(2,363,256.74)
Supplemental Retirement Fund - Index	3,358,663.30
Supplemental Retirement Fund - Bond Market	(217,478.58)
Supplemental Retirement Fund - Fixed Interest,	(2,114,436.03)
Supplemental Retirement Fund - International	1,312,599.17
Total Retirement Funds Net Cash Flow	(18,750,433.31)
Assigned Risk Plan	(1,382,754.29)
Permanent School Fund	(3,177,918.32)
Total Net Cash Flow	(\$23,311,105.92)

**STATE OF MINNESOTA
STATE BOARD OF INVESTMENT
Transaction and Asset Summary**

Retirement Funds

	Net Transactions			Asset Summary (at Market Value)				Total Mkt. Value (Millions)
	Bonds (Millions)	Stocks (Millions)	Total (Millions)	Cash Flow (Millions)	Short-Term % of Fund	Bonds % of Fund	Equity % of Fund	
January 1994	-1	1	0	14	2.1	32.3	65.6	20,105
February	-26	-25	-51	10	2.5	32.1	65.4	19,735
March	-3	14	11	1	2.5	32.4	65.1	19,051
April	37	186	223	132	2.0	31.9	66.1	19,285
May	0	-24	-24	-11	2.1	31.8	66.1	19,349
June	-13	0	-13	-6	2.1	32.2	65.7	19,038
July	0	4	4	25	2.2	32.0	65.8	19,507
August	0	-1	-1	-18	2.1	31.3	66.6	19,982
September	0	25	25	-30	1.8	31.5	66.7	19,581
October	0	2	2	22	1.9	30.9	67.2	19,824
November	0	0	0	-41	1.7	31.8	66.5	19,324
December	2	14	16	7	1.7	31.7	66.6	19,493
January 1995	1	10	11	-11	1.5	32.0	66.5	19,681
February	1	0	1	-1	1.5	31.8	66.7	20,249
March	2	18	20	-18	1.3	31.5	67.2	20,607
April	1	-305	-304	-6	2.7	31.2	66.1	21,049
May	0	13	13	14	2.6	31.5	65.9	21,681
June	8	-12	-4	-3	2.6	31.3	66.1	22,028
July	1	13	14	19	2.5	30.4	67.1	22,646
August	(1)	14	13	(25)	2.3	30.5	67.2	22,814
September	0	13	13	(21)	2.1	30.1	67.8	23,369
October	1	(3)	(2)	(20)	2.1	30.6	67.3	23,294
November	(5)	87	82	(20)	1.6	30.1	68.3	23,975
December	11	(6)	5	(6)	1.5	30.2	68.3	24,304
January 1996	0	12	12	-4	1.4	29.9	68.7	24,721
February	-301	303	2	4	1.4	28.0	70.6	24,859
March	0	-14	-14	-15	1.4	27.6	71.0	25,070

Tab C

EXECUTIVE DIRECTOR'S ADMINISTRATIVE REPORT

DATE: May 28, 1996

TO: Executive Director's Administrative Report
Members, State Board of Investment

FROM: Howard Bicker

1. Reports on Budget and Travel

A report on the SBI's administrative budget for the period ending April 30, 1996 is included as **Attachment A**.

A report on travel for the period from February 16 - May 15, 1996 is included as **Attachment B**.

2. Authorization for Deferred Compensation Consultant RFP

The SBI has responsibilities concerning four different deferred compensation type programs. Each of these programs requires the SBI to conduct a selection process for outside product providers and monitor those selected. These programs are:

- State Deferred Compensation Plan
- MnSCU defined contribution plan
- school districts 403(b) annuity matching contributions
- Historical Society defined contribution plan

To assist it in these efforts, the SBI retains a Deferred Compensation Programs consultant. The contract for the consultant expires on December 1996. The current consultant, Kim McCarrell of PRIMCO Capital Management, was first retained in December 1993 following a request for proposal (RFP) process in the fall of that year. PRIMCO chooses not to continue its consulting relationships. Therefore, the SBI must select a new consultant during the second half of 1996.

Staff has suggested the following timetable for the RFP process:

Committee review and approval of RFP	August
RFP sent out	September
Responses received and reviewed	September-October
Committee review and recommendation	October-November
Board review of recommendation	December

This timetable was discussed with the Deferred Compensation Review Committee at their meeting on May 23, 1996.

RECOMMENDATION:

I recommend that the SBI authorize the Deferred Compensation Review Committee to conduct a search for a deferred compensation programs consultant through a request for proposal process. The Committee should report on the results of the RFP by December 1996.

3. Approval of Vendor Contract for Historical Society Retirement Plan

Laws of Minnesota for 1996, Chapter 438, Article 7 authorizes the Historical Society employees to participate in the Minnesota State Colleges and Universities (MnSCU) Retirement Plan. The law provides that the Historical Society will administer the plan for their employees.

The MnSCU Plan is a defined contribution plan with four outside insurance company product providers selected by the SBI. Chapter 438 provides that the Historical Society may choose up to two of these product providers for their employees. The law also sets forth certain SBI responsibilities, among which is the requirement that the SBI must approve any contract.

Staff has received a letter from the Historical Society stating their choice of TIAA-CREF as product provider. Staff has been working with TIAA-CREF on contract terms and hopes to forward final contract language to the Board before the SBI meeting on June 5, 1996.

Copies of the Chapter 438 language and the letter from the Historical Society are in **Attachment C**.

The Deferred Compensation Review Committee discussed this issue at their meeting on May 23, 1996. Given the Historical Society's desire to put the program in place for their employees on July 1, 1996, the Committee is forwarding the following recommendation at this time.

RECOMMENDATION:

The Deferred Compensation Review Committee recommends that the SBI approve a contract between TIAA-CREF and the Minnesota Historical Society provided it incorporates substantively the same terms and conditions as the existing contract between TIAA-CREF and the Minnesota State Colleges and Universities (MnSCU).

4. Reappointment of IAC members

The terms of the following Board Appointees to the Investment Advisory Council (IAC) have expired:

**Kenneth Gudorf
P. Jay Kiedrowski
Judith Mares
Deborah Veverka**

The vacancies were announced in the State Register through the Open Appointments Process. The application deadline was March 26, 1996.

Mr. Gudorf, Mr. Kiedrowski and Ms. Mares have applied for reappointment. Ms. Veverka has declined to submit an application at this time.

I reviewed this matter with the SBI Deputies/Designees who suggested that the Board take action on the three applications for reappointment at the June 5, 1996 meeting. Candidates for the remaining vacancy could be considered during the next quarter and a recommendation brought to the Board in September 1996.

RECOMMENDATION:

I recommend that the SBI appoint the following individuals to new terms on the IAC:

**Kenneth Gudorf
P. Jay Kiedrowski
Judith Mares**

Further, I recommend that the SBI Deputies/Designees be authorized to consider candidates for the remaining vacancy and to make a recommendation to the SBI at its meeting in September 1996.

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ATTACHMENT A

**STATE BOARD OF INVESTMENT
FISCAL YEAR 1996 ADMINISTRATIVE BUDGET REPORT
GENERAL FUND APPROPRIATION
FISCAL YEAR TO DATE THROUGH APRIL 30, 1996**

ITEM	FISCAL YEAR 1996 BUDGET	FISCAL YEAR 1996 EXPENDITURES
PERSONAL SERVICES		
FULL TIME EMPLOYEES	\$ 1,519,000	\$ 1,183,212
SEVERENCE PAYOFF	0	3,120
WORKERS COMPENSATION INSURANCE	0	437
MISCELLANEOUS PAYROLL	0	694
SUBTOTAL	\$ 1,519,000	\$ 1,187,463
STATE OPERATIONS		
RENTS & LEASES	88,550	73,791
REPAIRS/ALTERATIONS/MAINTENANCE	13,000	9,691
BONDS AND INSURANCE	0	0
PRINTING & BINDING	15,950	14,991
PROFESSIONAL/TECHNICAL SERVICES	50,000	1,531
COMPUTER SYSTEMS SERVICES	202,500	151,965
COMMUNICATIONS	27,000	15,656
TRAVEL, IN-STATE	3,000	2,717
TRAVEL, OUT-STATE	50,000	28,034
SUPPLIES	48,000	32,038
EQUIPMENT	30,000	29,545
EMPLOYEE DEVELOPMENT	5,000	6,122
OTHER OPERATING COSTS	40,000	26,989
SUBTOTAL	\$ 573,000	\$ 393,070
TOTAL GENERAL FUND	\$ 2,092,000	\$ 1,580,533

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- 6 -

ATTACHMENT B**STATE BOARD OF INVESTMENT****Travel Summary by Date
February 16, 1996 - May 15, 1996**

<u>Purpose</u>	<u>Name(s)</u>	<u>Destination and Date</u>	<u>Total Cost</u>
Manager Monitoring Alternative Investments: KKR Meeting	H. Bicker J. Griebenow	Chicago, IL 2/26	\$1,220.00
Manager Monitoring International Manager: Baring Asset Management Conference	K. Vnuk	Dallas, TX 3/18-3/21	\$824.00
Manager Monitoring Domestic Equity Manager: BZW Barclays Global Investors	M. Menssen	San Francisco, CA 3/21-4/3	\$625.63
Manager Monitoring Alternative Investments: Golder, Thoma, Cressey, Rauner, Inc., (Zell) Equity Institutional Investors, Inc. Manager Search Alternative Investments: McCaffery Real Estate Partners, L.P.,	J. Griebenow	Chicago, IL 4/8-4/10	\$938.00
Staff Conference "Eighteenth Annual Client Conference" sponsored by State Street Bank & Trust	H. Bicker M. Schmitt	Miami, FL 4/12-4/17	\$1,005.00
Manager Monitoring Alternative Investments: KKR Investors Annual Meeting	M. Regal	Palm Springs, CA 4/27-5/1	\$935.70
Staff Education "Equity Portfolio Management Seminar" sponsored by BARRA	L. Buermann	Sonoma, CA 4/28-5/1	\$1,593.30

<u>Purpose</u>	<u>Name(s)</u>	<u>Destination and Date</u>	<u>Total Cost</u>
Manager Monitoring Alternative Investments: First Reserve Corporation Manager Search Alternative Investments: Starwood Opportunity Fund IV, L.P.	J. Griebenow	New York, NY 4/30-5/2	\$1,014.00
Manager Monitoring Alternative Investments: T.A. Associates Realty, Manager Search Alternative Investments: HLM Management Company, PRISM Venture Partners Staff Education "Private Equity Conference" sponsored by Institute for International Research	M. Regal	Boston, MA 5/12-5/15	\$249.00

ATTACHMENT C



MINNESOTA HISTORICAL SOCIETY

May 9, 1996

Mr. Howard Bicker
Executive Director
State Board of Investment
105 MEA Building
55 Sherburne Ave.
St. Paul, MN 55155

Dear Howard:

Thank you for meeting with Pat Gaarder and me last week to discuss the steps the Minnesota Historical Society needs to take to implement the defined contribution plan available to its staff through legislation passed in 1996 (Laws 1996, Chapter 438, Article 7). That legislation enables us to "...approve up to two financial institutions...to provide annuity products..." to eligible staff. As plan administrator we, however, wish to deal with only one provider; we have chosen TIAA/CREF. Provisions similar to those contained in the contract between MNSCU and TIAA/CREF will meet the needs of the Historical Society. That contract has been sent to our outside counsel and we do not anticipate any problems from that review. Items that we have a particular interest in include loan provisions, provision by TIAA/CREF of informational materials, and surrender costs. Assuming that we will receive a favorable opinion from our counsel, we request that you negotiate a similar contract on our behalf.

Because we are choosing to deal with only one vendor, we believe that our administrative costs will be fairly low; please build in \$1,000 per year for plan administration.

I trust this information will enable you to proceed with the administrative requirements of your Board and subsequent contract negotiations with TIAA/CREF on our behalf. If there is anything else we need to provide to you, please call me at 297-7849. Thank you for your assistance in this matter.

Sincerely,

Charles W. Lawrence
Assistant Director
Finance and Administration

CWL/6/82/gk

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1 Sec. 6. [DEFINED CONTRIBUTION AND DEFINED BENEFIT PLAN
2 STUDY.]

3 The legislative commission on pensions and retirement shall
4 report to the legislature by February 15, 1997, on the relative
5 advantages and disadvantages, including any federal taxation
6 considerations, of defined benefit pension plans and of defined
7 contribution pension plans.

8 Sec. 7. [REPEALER.]

9 Minnesota Statutes 1994, section 353D.11, is repealed.

10 Sec. 8. [EFFECTIVE DATE.]

11 Sections 1 to 7 are effective the day following final
12 enactment.

13 ARTICLE 7

14 INDIVIDUAL RETIREMENT ACCOUNT PLANS DEFINED
15 CONTRIBUTION PLAN COVERAGE FOR HISTORICAL
16 SOCIETY EMPLOYEES

17 Section 1. Minnesota Statutes 1995 Supplement, section
18 354D.02, subdivision 2, is amended to read:

19 Subd. 2. [ELIGIBILITY.] Eligible employees are:

20 (1) any supervisory or professional employee of the state
21 arts board; and

22 (2) any supervisory or professional employee of the
23 Minnesota humanities commission; or

24 (3) any employee of the Minnesota historical society.

25 Sec. 2. Minnesota Statutes 1995 Supplement, section
26 354D.03, is amended to read:

27 354D.03 [SOCIAL SECURITY COVERAGE.]

28 Plan participants remain are members of the general state
29 retirement plan for purposes of social security coverage only
30 remain, and are covered by the applicable agreement entered into
31 under section 355.02 but are not members of the general state
32 retirement plan for any other purpose while employed in covered
33 employment.

34 Sec. 3. Minnesota Statutes 1995 Supplement, section
35 354D.04, is amended to read:

36 354D.04 [PLAN COVERAGE.]

1 An election made under this section is irrevocable.
2 Eligible employees under section 354D.02, subdivision 2, shall
3 elect to participate in either the individual retirement account
4 plan or their respective retirement plan as follows:

5 (1) ~~An eligible employee first-employed-after-the-effective~~
6 ~~date-of-laws-1994, chapter-508, in-covered-employment~~ with no
7 prior allowable service as a member of the Minnesota state
8 retirement system, the public employees retirement association,
9 or the teachers retirement association may elect retirement
10 coverage under either their respective state retirement plan or
11 the individual retirement account plan within 60 days of the
12 start of covered employment. ~~An election made under this~~
13 ~~subdivision is irrevocable.~~

14 (2) An eligible employee with prior allowable service as a
15 member of the Minnesota state retirement system, the public
16 employees retirement association, or the teachers retirement
17 association may elect prospective coverage by the individual
18 retirement account plan. If individual retirement account plan
19 coverage is elected, accumulated employer and employee
20 contributions and allowable service credit shall remain with the
21 applicable retirement association or system. Notwithstanding
22 any provision of law to the contrary, an individual who has
23 transferred coverage for the same employment to the individual
24 retirement account plan is entitled to an augmented deferred
25 retirement annuity from the prior plan based on the amount
26 representing the employer and employee contributions made on the
27 individual's behalf in the retirement association or system in
28 which the individual was formerly enrolled without regard to
29 whether or not the individual meets the service credit vesting
30 requirements of the applicable retirement association or
31 system. An election made under this subdivision clause must be
32 made within 120 days ~~and is irrevocable~~ following the date the
33 eligible employee first becomes eligible to make the election.

34 Sec. 4. Minnesota Statutes 1995 Supplement, section
35 354D.06, is amended to read:

36 354D.06 [ADMINISTRATION.]

1 (a) The Minnesota state university system or its successor
2 shall administer the individual retirement account plan for
3 eligible employees listed in section 354D.02, subdivision 2,
4 clauses (1) and (2), in accordance with sections 354B.01 to
5 354B.05.

6 (b) The Minnesota historical society or its successor shall
7 administer the individual retirement account plan for eligible
8 employees listed in section 354D.02, subdivision 2, clause (3),
9 in accordance with section 354D.08.

10 Sec. 5. [354D.08] [INDIVIDUAL RETIREMENT ACCOUNT PLAN
11 ADMINISTRATION; MINNESOTA HISTORICAL SOCIETY.]

12 Subdivision 1. [GENERAL GOVERNANCE.] The Minnesota
13 historical society is the plan administrator and has the
14 administrative responsibility for the individual retirement
15 account plan for those eligible employees listed in section
16 354D.02, subdivision 2, clause (3).

17 Subd. 2. [ANNUITY CONTRACTS AND CUSTODIAL ACCOUNTS.] (a)
18 The plan administrator shall arrange for the purchase of fixed
19 annuity contracts, variable annuity contracts, a combination of
20 fixed and variable annuity contracts, or custodial accounts from
21 financial institutions which have been selected by the state
22 board of investment and approved by the plan administrator under
23 subdivision 3, as the investment vehicle for the retirement
24 coverage of plan participants and to provide retirement benefits
25 to plan participants. Custodial accounts from financial
26 institutions shall include open-end investment companies
27 registered under the federal Investment Company Act of 1940, as
28 amended.

29 (b) The annuity contracts or accounts must be purchased
30 with contributions under section 354D.05, or with money or
31 assets otherwise provided by law by authority of the Minnesota
32 historical society and deemed acceptable by the applicable
33 financial institution.

34 Subd. 3. [SELECTION OF FINANCIAL INSTITUTIONS.] The plan
35 administrator may approve up to two financial institutions
36 selected by the state board of investment under section 354B.25,

1 subdivision 3, to provide annuity products and custodial
2 accounts for those employees listed in section 354D.02,
3 subdivision 2, clause (3). Only those financial institutions
4 selected by the state board of investment and approved by the
5 plan administrator may provide annuity products and custodial
6 accounts for those employees listed in section 354D.02,
7 subdivision 2, clause (3).

8 The state board of investment must periodically review at
9 least every three years each financial institution selected.

10 The state board of investment may retain consulting services to
11 assist in the periodic review, may establish a budget for its
12 costs in the periodic review process, and may charge a
13 proportional share of those costs to each financial institution
14 selected. All contracts must be approved by the state board of
15 investment before execution by the Minnesota historical
16 society. The state board of investment shall also establish
17 policies and procedures under section 11A.04, clause (2), to
18 carry out this subdivision.

19 Subd. 4. [BENEFIT OWNERSHIP.] The retirement benefits
20 provided by the annuity contracts and custodial accounts of the
21 individual retirement account plan are held for the benefit of
22 plan participants and must be paid according to this chapter and
23 the plan document.

24 Subd. 5. [INDIVIDUAL RETIREMENT ACCOUNT PLAN
25 ADMINISTRATIVE EXPENSES; MINNESOTA HISTORICAL SOCIETY.] (a) The
26 reasonable and necessary administrative expenses of the
27 individual retirement account plan for those employees
28 enumerated in section 354D.02, subdivision 2, clause (3), must
29 be paid by plan participants. The plan administrator may charge
30 to plan participants purchasing annuity contracts and custodial
31 accounts pursuant to subdivision 2, paragraph (a), an
32 administrative expenses assessment of a designated amount, not
33 to exceed two percent of member and employer contributions, as
34 those contributions are made.

35 (b) Any administrative expense charge that is not actually
36 needed for the administrative expenses of the individual

1 retirement account plan must be refunded to member accounts.

2 Sec. 6. [EFFECTIVE DATE.]

3 Sections 1 to 5 are effective the day following final
4 enactment.

5 ARTICLE 8

6 VOLUNTEER FIREFIGHTER FIRE PREVENTION SERVICE

7 Section 1. Minnesota Statutes 1994, section 424A.001, is
8 amended by adding a subdivision to read:

9 Subd. 8. [FIREFIGHTING SERVICE.] "Firefighting service,"
10 if the applicable municipality approves for a fire department
11 that is a municipal department, or if the contracting
12 municipality or municipalities approve for a fire department
13 that is an independent nonprofit firefighting corporation,
14 includes service rendered by fire prevention personnel.

15 Sec. 2. Minnesota Statutes 1994, section 424A.001, is
16 amended by adding a subdivision to read:

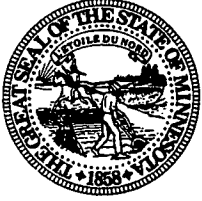
17 Subd. 9. [SEPARATE FROM ACTIVE SERVICE.] "Separate from
18 active service" means to cease to perform fire suppression
19 duties, to cease to perform fire prevention duties, to cease to
20 supervise fire suppression duties, and to cease to supervise
21 fire prevention duties.

22 Sec. 3. Minnesota Statutes 1994, section 424A.01, is
23 amended by adding a subdivision to read:

24 Subd. 5. [FIRE PREVENTION PERSONNEL.] (a) If the fire
25 department is a municipal department and the applicable
26 municipality approves, or if the fire department is an
27 independent nonprofit firefighting corporation and the
28 contracting municipality or municipalities approve, the fire
29 department may employ or otherwise utilize the services of
30 persons as volunteer firefighters to perform fire prevention
31 duties and to supervise fire prevention activities.

32 (b) Personnel serving in fire prevention positions are
33 eligible to be members of the applicable volunteer firefighter
34 relief association and to qualify for service pension or other
35 benefit coverage of the relief association on the same basis as
36 fire department personnel who perform fire suppression duties.

Tab D



**STATE OF MINNESOTA
OFFICE OF THE STATE TREASURER**

303 State Administration Building
50 Sherburne Avenue
Saint Paul, Minnesota 55155

MICHAEL A. McGRATH
Treasurer

(612) 296-7091
Fax (612) 296-8615

DATE: May 28, 1996

TO: Members, State Board Investment

FROM: Michael A. McGrath, Chair
SBI Administrative Committee

SUBJECT: Report for the SBI Administrative Committee

The SBI Administrative Committee met on May 24, 1996 and took action on the following items:

1) Executive Director's FY97 Workplan

Mr. Bicker presented his proposed workplan for FY97. Like the previous workplans, the FY97 plan follows the same category order found in the Executive Director's position description. The plan is a compilation of on-going responsibilities as well as the new initiatives the Executive Director will undertake during the next fiscal year.

A summary of the proposed plan is shown in **Attachment A**. Supporting information was sent to each Board member as part of the FY97 Management and Budget Plan document.

RECOMMENDATION:

The Committee recommends that the SBI approve the FY97 Executive Director's Workplan. Further, the Committee recommends that the work plan serve as the basis for the Executive Director's performance evaluation for FY97.

2) FY97 Administrative Budget Plan

The SBI's administrative budget is funded by a legislative appropriation from the general fund. All expenditures are billed back to the various funds under the supervision of the SBI and the receipts are deposited in the general fund as non-dedicated revenue.

An overview and summary of the budget is in **Attachment B**. Supporting information was sent to each Board Member as part of the FY97 Management and Budget Plan.

RECOMMENDATION:

The Committee recommends that the SBI approve the FY97 Administrative Budget Plan and that the Executive Director have the flexibility to reallocate funds between budget categories in the event budgeting needs change during the year.

3) Fiduciary Education Plan

Minnesota Statutes Chapter 356A requires each public pension plan to establish a continuing education plan for its fiduciaries. The plan approved by the Committee is in **Attachment C**. Please note that the travel allocation policy for Board members and their designees is included in the plan.

RECOMMENDATION:

The Committee recommends that the SBI adopt the attached Continuing Fiduciary Education Plan.

4) Process for Executive Director's FY96 Evaluation

The Committee discussed the process that will be used by the Board to evaluate the Executive Director for FY96. The Committee members agreed that the performance reviews should be completed prior to the September 1996 meeting of the SBI and should follow the process used in the past.

RECOMMENDATION:

The Committee recommends that the SBI adopt the following process for the Executive Director's FY96 performance evaluation:

- **The evaluation will be completed prior to the September 1996 meeting of the SBI and will be based on the results of the Executive Director's workplan for FY96.**
- **The SBI deputies/designees will develop an appropriate evaluation form for use by each member which will reflect the categories in the Executive Director's position description and workplan.**
- **As the chair of the Board, the Governor's representative (Department of Finance), will coordinate distribution and collection of the evaluation forms and will forward the completed forms to the Executive Director. Board Members are encouraged to meet individually with the Executive Director to review their own evaluation.**

ATTACHMENT A

**STATE BOARD OF INVESTMENT
Executive Director's Proposed Workplan**

FY97

(Categories A, B, C, D, E correspond to the position description)

	Projected Time Frame
A. DEVELOPMENT OF INVESTMENT POLICIES	
1. Review the structure of the deferred compensation programs and recommend changes, if necessary.	Jul. - Jun.
2. Review the investment policy of the Assigned Risk Plan.	Jan. - Jun.
3. Review investment policy of the Permanent School Fund.	Jan. - Jun.
B. IMPLEMENTATION OF INVESTMENT POLICIES APPROVED BY THE SBI	
1. Meet or exceed the performance objectives established for the Basics, Post, and Combined Funds.	On-going, reported quarterly
• Obtain returns that are 3-5 percentage points over inflation over the last 10 years (FY88-FY97) for the Combined Funds.	
• Outperform the median fund from the TUCS universe of Master Trusts over the last 5 years (FY93-FY97) for the Combined Funds.	
• Outperform a composite of market indices over the last 5 years (FY93-FY97). Separate composites are constructed for the Combined, the Basics and the Post Funds.	
3. Implement Manager Monitoring Programs for domestic stocks, international stocks and domestic bonds.	On-going
4. Consider additional investments with new/existing alternative investment managers.	On-going

C. REVIEW AND CONTROL OF INVESTMENT POLICIES

1. Review the results of the Emerging Manager Program and recommend changes, if appropriate. Jul. - Jun.
2. Conduct a search for one or more investment consultants through an RFP process. Jan. - Jun.
3. Conduct a search for a deferred compensation consultant through a request for proposal (RFP) process. Jul. - Dec.
4. Monitor insurance company vendors retained for the Deferred Compensation Plan (457), teacher tax sheltered annuities (403b) and Higher Education plans (401a). On-going
5. Monitor and evaluate active manager performance in accordance with the SBI's Manager Continuation Policy. On-going
6. Review investment guidelines for stock and bond managers on an annual basis. Apr. - Jun.
7. Monitor implementation of the Board's guidelines on international investing. On-going
8. Monitor implementation of Northern Ireland mandate. On-going
9. Monitor implementation of proxy voting procedures. On-going
10. Provide staff support for initiatives assigned to the Proxy Committee. As needed

D. ADMINISTRATION AND MANAGEMENT OF STAFF OPERATIONS

1. Cooperate in all respects with the annual audit of SBI operations by the Legislative Auditor. Jul. - Dec.
2. Coordinate police and fire fund consolidations. As needed

- | | |
|---|-------------|
| 3. Conduct internal review/assessment of data collection and monitoring processes for accounting and performance data. | Jul. - Jun. |
| 4. Select an external vendor for the SBI's accounting and portfolio management system through an RFP process, if necessary. | Jan. - Jun. |
| 5. Prepare and seek approval of the SBI's legislative proposals for 1997 Legislative Session, if needed. | Oct. - May |
| 6. Prepare FY98 Management and Budget Plan. | Mar. - Jun. |

E. COMMUNICATION AND REPORTING

- | | |
|--|----------------------------|
| 1. Prepare reports on investment results. | Quarterly |
| 2. Prepare status reports on the Executive Director's FY97 workplan for review by the SBI, IAC and Consultant, as requested. | As requested |
| 3. Meet with the SBI and IAC on a quarterly basis and at other times as required. | Quarterly, or as requested |
| 4. Meet with the Board's designees on a monthly basis, as requested. | Monthly, or as requested |
| 5. Prepare FY96 Annual Report. | Jul. - Feb. |
| 6. Coordinate round table discussions with SBI's external managers. | Periodic, 2-3 per year |

ATTACHMENT B

**Administrative Budget
FY 97 Budget Plan
Overview**

The FY97 budget plan is based on the SBI's FY96-97 Biennial Budget Request:

	FY96 Projected	FY97 Plan	Difference
Personal Services	\$1,489,565	\$1,527,000	+\$37,435
Operating Expenses	598,217	566,000	-32,217
	\$2,087,782	\$2,093,000	+\$5,218

Personal Services: 73% of the budget
Salaries, retirement, insurance, FICA, severance

Personnel costs will be approximately \$37,500 more than in FY96. This is due primarily to salary increases negotiated by the Department of Employee Relations and the various bargaining units that represent SBI employees. These contracts/agreements provided an increase of approximately 2.5% over FY96.

Operating Expenses: 27% of the budget
Rents, leases, printing, data processing
Professional/technical contracts
Communications, travel, employee development, misc. fees
Office equipment, furnishings, supplies

In order to fund the increased personnel costs noted above, operating expenses will be approximately \$32,000 lower than in FY96. The largest differences within expenditure categories are noted below:

Category	FY97 vs. FY96
professional/technical services	+\$26,000
communications	+3,000
printing	-4,500
travel	-10,000
equipment/supplies	-48,000

Professional/technical services were increased to reflect greater activity by the deferred compensation consultant over the next year. Communications were increased due to predicted cost increases in mail and delivery services. Allocations for printing, travel and equipment were reduced over the level expended in the FY96 to make up the balance.

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**STATE BOARD OF INVESTMENT
FISCAL YEARS 1997 BUDGET PLAN
GENERAL FUND SUMMARY**

DESCRIPTION	FY1994 ACTUAL	FY 1995 ACTUAL	FY1996 PROJECTED	FY 1997 BUDGET
PERSONAL SERVICES				
FULL TIME EMPLOYEES	\$ 1,417,084	\$ 1,445,664	\$ 1,470,200	\$ 1,505,000
PART TIME EMPLOYEES	0	0	14,837	0
SEVERENCE PAYOFF	24990	0	3,118	20,000
WORKERS COMPENSATION INSURANCE	985	906	510	1,000
MISCELLANEOUS PAYROLL	4,345	1,666	900	1,000
SUBTOTAL	\$ 1,447,404	\$ 1,448,236	\$ 1,489,565	\$ 1,527,000
STATE OPERATIONS				
RENTS & LEASES	81,950	101,699	88,550	90,500
REPAIRS/ALTERATIONS/MAINTENANCE	11,086	12,697	11,974	13,000
BONDS AND INSURANCE	959	895	673	1,000
PRINTING & BINDING	13,628	10,546	20,450	16,000
PROFESSIONAL/TECHNICAL SERVICES	41,320	40,707	24,000	50,000
COMPUTER SYSTEMS SERVICES	202,500	202,540	202,750	202,500
COMMUNICATIONS	25,093	22,227	24,582	27,000
TRAVEL, IN-STATE	729	79	3,608	3,000
TRAVEL, OUT-STATE	35,908	47,829	65,000	55,000
SUPPLIES	30,718	45,741	47,000	42,000
EQUIPMENT	45,091	70,341	70,000	25,000
EMPLOYEE DEVELOPMENT	9,037	6,944	6,800	8,000
OTHER OPERATING COSTS	29,817	35,977	32,830	33,000
SUBTOTAL	\$ 527,836	\$ 598,222	\$ 598,217	\$ 566,000
TOTAL GENERAL FUND	\$ 1,975,240	\$ 2,046,458	\$ 2,087,782	\$ 2,093,000

3.6% 2.0% 0.2%

PERCENT INCREASE OVER PRIOR YEAR

ATTACHMENT C

CONTINUING FIDUCIARY EDUCATION PLAN

REQUIRED BY MS 356A.13

The State Board of Investment (SBI) undertakes the following activities related to fiduciary education. Taken as a group, these activities shall constitute the plan for continuing fiduciary education required by Minnesota Statutes 356A.13 (copy attached). In addition, pursuant to statutory requirements of qualification, the SBI executive director and many members of the Board's Investment Advisory Council (IAC) can be reasonably considered to be experts with respect to their duties as fiduciaries.

1. Briefing for New Board/IAC Members

Shortly after election to the Board or appointment to the IAC, each new member is briefed on SBI operations and policies. As part of the briefing, SBI's legal counsel will review the member's fiduciary obligations and responsibilities as specified in Minnesota Statutes Chapters 11A and 356A.

2. Development and Review of Investment Policies

The SBI adopts comprehensive investment policies for each fund under its control. The policies cover investment objectives, asset allocation, management structure and performance evaluation. Policy papers or reports on these topics are developed and written by SBI staff in conjunction with the IAC and consultants. Relevant research and analyses from the academic and professional investment fields are used to formulate these policy guidelines.

After they are formally adopted by the Board, these written policies guide the management of all assets under the SBI's control. The SBI intends to review its stated investment policies periodically. This review may occur within the framework of the SBI's regular quarterly meetings or may take place at special meetings or seminars specifically designated for this purpose.

3. Input from Board's Consultants

The SBI retains outside investment consultants to advise the Board members on a wide variety of investment management issues. As part of their contracts with the SBI, the consultants offer to meet with the Board members or their designees to discuss investment-related issues. These individual consultations occur throughout the year. In addition, the general consultant is available at each meeting of the Board and IAC. These meetings are supplemented by quarterly reports on investment performance prepared by the general consultant.

4. Manager "Round Tables"

The SBI intends to convene small groups of its external money managers to discuss issues related to investment management and the financial markets. These "round table" discussions will be held periodically throughout the year and will be open to Board members and their designees, IAC members and other interested parties. It is anticipated that 2-3 round tables will be held each year.

5. Travel Allocation

The SBI allocates \$2,500 annually to each Board member (or their designee) for costs associated with attendance at investment-related seminars and conferences. This allocation is used at the discretion of each Board member.

Date: May, 1996

1994 Minnesota Statutes

356A.13. CONTINUING FIDUCIARY EDUCATION.

Subdivision 1. **Obligation of fiduciaries.** A fiduciary of a covered pension plan shall make reasonable effort to obtain knowledge and skills sufficient to enable the fiduciary to perform fiduciary activities adequately. At a minimum, a fiduciary of a covered pension plan shall comply with the program established in accordance with subdivision 2.

Subd. 2. **Continuing fiduciary education program.** The governing boards covered pension plans shall each develop and periodically revise a program for the continuing education of any of their board members and any of their chief administrative officers who are not reasonably considered to be experts with respect to their activities as fiduciaries. The program must be designed to provide those persons with knowledge and skills sufficient to enable them to perform their fiduciary activities adequately.

Tab E

COMMITTEE REPORT

DATE: May 28, 1996

TO: Members, State Board of Investment
Members, Investment Advisory Council

FROM: Domestic Manager Committee

The Domestic Manager Committee met on May 16, 1996 to consider the following agenda items:

- Review of manager performance for the period ending March 31, 1996
- Update on candidates included in the Manager Monitoring Program for future equity and fixed income manager searches
- Annual review of active stock manager benchmarks
- Annual review of investment manager guidelines
- Approval to renew a contract for the bond manager for the Assigned Risk Plan, Voyageur Asset Management
- Authorization to terminate the contract with an active stock manager, Jundt Associates, to provide funds for asset allocation changes and total fund rebalancing

Board action is requested on the final two (2) items.

INFORMATION ITEMS:

1. Review of manager performance

- *Stock Managers*

For the quarter ending March 31, 1996, the domestic stock manager program outperformed its aggregate benchmark and the Wilshire 5000. For the latest year and five years, the **current** managers outperformed the benchmark and the Wilshire 5000. For the latest three years, the **current** managers underperformed the benchmark but outperformed the Wilshire 5000.

Time Period	Total Program	Wilshire 5000*
Quarter	5.9%	5.6%
1 Year	31.7	32.2
3 Years	14.6	15.3
5 Years	14.6	14.9

Current Mgrs. Only	Aggregate Benchmark
5.9%	5.6%
32.7	31.3
15.6	15.9
15.8	15.2

* Adjusted for SBI's restrictions, as appropriate.

Performance was mixed among the active manager group for the quarter; eight of the managers outperformed and five underperformed their benchmarks. The consumer non-durable bets made by several managers contributed the majority of the program's outperformance during the quarter.

Staff noted that all the semi-passive managers have outperformed their benchmark since inception. As a group, the new managers have added value to their completeness fund benchmark and exceeded performance expectations.

The performance evaluation reports for the stock managers start on **page 89** of this Tab. Manager Commentaries are in **Tab I**.

- ***Bond Managers***

For the period ending March 31, 1996, the total bond program and current managers outperformed the Lehman Aggregate and the aggregate benchmark for the quarter and the latest one year, three year and five year periods.

Time Period	Total Program	Lehman Aggregate*
Quarter	-1.7%	-1.8%
1 Year	11.1	10.8
3 Years	6.3	6.1
5 Years	9.0	8.6

Current Mgrs. Only	Aggregate Benchmark
-1.7%	-1.8%
11.1	10.8
6.4	6.1
9.1	8.6

* Reflects Salomon BIG index prior to 7/94.

The performance evaluation reports for the bond managers start on **page 123** of this Tab. Manager Commentaries are in **Tab I**.

2. Update on candidates for the Manager Monitoring Program

The SBI has established a Manager Monitoring Program to identify potential candidates for future domestic equity and fixed income manager searches. The candidate firms are intended to serve as the starting point for any active or semi-passive manager search deemed necessary during the coming fiscal year. Up to 10 firms are to be identified for each manager group.

The firms recommended by staff in various categories are shown below. Please refer to the attached "Manager Fact Sheets" for more information on each firm.

Active Stock Managers (begin on page 9)

Boatmen's Trust Company
Enhanced Investment Technologies, Inc. (INTECH)
First Asset Management
Jacobs Levy Equity Management, Inc.
Lazard Freres Asset Management
Pacific Investment Management Company (PIMCO)
Wellington Management Company

Semi-Passive Stock Managers (begin on page 27)

Goldman Sachs Asset Management
Investment Research Company Asset Management (IRC)
Martingale Asset Management
Panagora Asset Management
Weiss, Peck & Greer, L.L.C. (WP&G)

Bond Managers (begin on page 43)

Brinson Partners, Inc.
Durkee Capital Advisors
J.P. Morgan Investment Management, Inc.
Loomis Sayles & Co.
Nicholas Applegate Capital Management
Pacific Investment Management Company (PIMCO)
T. Rowe Price Associates, Inc.
Washington Square Advisors

The Committee discussed the above lists and did not suggest any additions or deletions at this time.

3. Annual review of active stock manager benchmarks

The SBI's Manager Continuation Policy requires staff to review all custom benchmarks for active domestic stock managers on an annual basis. The purpose of the analysis is to determine whether a benchmark adequately reflects the manager's unique investment style and therefore can be used as a valid performance measurement standard for the manager.

The Committee discussed the staff report and concurred with the staff's findings concerning the adequacy of the current benchmarks. Staff found that the current benchmarks were satisfactory in most areas. Higher than desired levels of turnover were noted in several benchmarks, but staff believe that the affected managers are taking steps to correct the concerns noted.

A summary of the benchmark quality analysis begins on **page 59**. The Committee reviewed additional detail on each benchmark which is not included in this report but is available from staff, upon request.

4. Annual review of investment manager guidelines

The SBI has established guidelines for the external managers which govern their investment actions. While these guidelines may be changed at any time, they are part of the formal contractual agreement between the SBI and manager. The guidelines address return objectives, benchmarks, authorized investments, performance evaluation, communication and reporting requirements. Staff and the Committee review the guidelines annually for accuracy and completeness.

No changes were deemed necessary for the passive stock manager, the semi-passive bond managers or the active bond managers. The Committee concurred with a staff recommendation for minor changes in the following guidelines:

- *Active stock managers.* Preferred stocks, equity options and warrants have been added to the general authorization of eligible securities. The use of these instruments is consistent with active stock management strategies. The addition of convertible bonds and deletion of bonds is a technical correction in the current guidelines.
- *Semi-passive stock managers.* Preferred stocks, equity options and warrants have been added to the general authorization of eligible securities. Staff believe that it is appropriate for the semi-passive managers to have these instruments available as well.

The complete guidelines for each manager group are attached beginning on **page 63**. Additions to the current guidelines are noted by underline and deletions are indicated by ~~strike-out~~.

ACTION ITEMS:

- 1. Recommendation to renew a contract with Voyager Asset Management for bond management in the Assigned Risk Plan.**

The contract for the fixed income segment of the Assigned Risk Plan managed by Voyager Asset Management will expire on June 30, 1996. Staff proposed that the contract be renewed for a five year period with a change in the termination provision. Currently, the contract provides that the agreements may be terminated with 30 days notice. Staff proposes that a change be made to the new contract to provide for immediate termination. All other terms conditions of the contract are expected to remain unchanged.

RECOMMENDATION:

The Committee recommends that SBI authorize the Executive Director, with assistance from SBI's legal counsel, to negotiate and execute a contract renewal for a five year period ending June 30, 2001 with Voyager Asset Management for active bond management in the Assigned Risk Plan, subject to inclusion of a provision which provides for immediate termination.

- 2. Authorization to terminate a contract with an active stock manager, Jundt Associates, to provide funds for asset allocation changes and total fund rebalancing**

The SBI must raise additional funds from the domestic equity program for asset allocation changes and total fund rebalancing. Staff recommended that the SBI's relationship with Jundt Associates, an active domestic stock manager, be terminated to provide funds for these purposes.

Background on Asset Allocation Change

In October 1995, the SBI increased its allocation to international stocks in the Combined Funds from 10% to 15%. In the Basic Funds, the new target will be funded by reducing the allocation to domestic stocks from 50% to 45%. In the Post Fund, the new target will be funded by reducing the allocation to fixed income from 35% to 30%. The total amount added to the international program in the Combined Funds will be in excess of \$1.3 billion.

Due to the exceptionally strong performance of the domestic stock market in recent quarters, stocks are currently overweighted in both funds. This means a larger amount will be withdrawn from domestic stocks than from bonds in order to reach the new asset allocation targets and rebalance the Combined Funds.

Funding Needed from the Domestic Stock Program

Within the domestic stock program, assets have been/will be raised by reducing the actively managed portion of the pool:

<i>Firm</i>	<i>Action</i>	<i>Amount</i>
Lynch & Mayer	terminated 10/95	\$316 million
Alliance Capital	withdrew funds 2/95	\$250 million
Waddell & Reed	withdrew funds 4/96	\$100 million
Jundt Associates	withdrew funds 4/96	\$100 million
<i>Total raised through 5/96</i>		<i>\$766 million</i>
<i>Additional needed</i>		<i>\$200 million (approximately)</i>

The changes noted above will reduce the actively managed portion of the domestic stock program from about 50% to about 43% over the course of FY96. This is consistent with the SBI's goal to equalize allocations to active, semi-passive and passive management within the domestic stock pool, over time.

Source for Additional Funds Within the Domestic Stock Program

Staff recommended that the SBI's relationship with Jundt Associates be terminated to provide additional funds from the domestic stock program. Several issues prompted the recommendation:

- **Underperformance.** Jundt Associates has underperformed its benchmark significantly since the inception of the SBI account in July 1993 (11.0% actual vs. 16.8% benchmark, annualized).
- **Change in management team.** A key member of Jundt's portfolio team left the organization shortly after the SBI retained the firm in 1993. An investment professional from outside of the company was brought in as a replacement.
- **Account losses.** Within the last year, Jundt has lost several accounts. One of these accounts was a "fund of funds" run by a major consulting organization. Staff believe that this will cause other clients to re-evaluate their relationship with the firm as well.

In light of the above, staff's confidence in the firm's organization and investment process has deteriorated. Given the current need to raise additional funds from the domestic equity program, staff believe that it is appropriate to terminate the relationship at this time.

After discussion, the Committee concurred with staff's recommendation. The balance in the portfolio is approximately \$170 million. The Committee agreed that these assets

should be liquidated and redirected to other asset classes for asset allocation and rebalancing purposes.

RECOMMENDATION:

The Committee recommends that the SBI terminate its contractual relationship with Jundt Associates for active domestic stock management. The balance in the portfolio should be liquidated and used as a source of funds for asset allocation changes and rebalancing activity.

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MANAGER FACT SHEET

Manager: Boatmen's Trust Company

Investment Philosophy and Process

Boatmen's philosophy and approach to equity investments begins with fundamental company analysis conducted by their in-house financial analysis. Their analysts evaluate the financial strength, management strategies, and future growth potential of the nearly 350 companies in their universe. This research leads to critical long-term projections for profitability, dividends, and earnings growth that allows Boatmen to determine each company's long-term fundamental value. They compare these projected fundamental values to prevailing market prices to calculate the expected return for each stock in their universe.

Boatmen also analyzes the systematic risk characteristics of each stock. Their assessment of risk focuses on evaluating the potential price volatility of each stock by monitoring its sensitivity to various market and economic factors such as oil prices and interest rates. They use this analysis to segregate their universe of stocks in to three risk classifications. Within each risk classification, all stocks are then ranked on the basis of relative expected return and classified within one of three distinct valuation categories (buy, sell, or hold).

The resulting two dimensional framework allows them to objectively identify the stocks offering superior relative value while limiting portfolio risk. Boatmen's portfolios typically contain 35 to 45 stocks. In constructing the portfolio, they evaluate sector and industry diversification as well as the critical subjective issues which may impact the price of a stock. Boatmen's process also incorporates a strict sell discipline, ensuring that as a stock follows the market tendency to become fairly valued or overvalued, it will be sold and replaced with a more attractive purchase candidate.

Research

Boatmen employs 13 analysts who are responsible for evaluating each company in their universe. They also purchases data from Zachs, Ibis, Value Line, Standard & Poor's, and Bridge which is used to augment their analysis.

Trading

Boatmen's trading staff is responsible for trading large blocks of equities, smaller equity trades, convertibles, options, and futures. Their traders are also responsible for communicating transactions and market conditions to their portfolio managers. Trades are

Boatmen's Trust Company (Con't)

allocated to an individual trader based on the liquidity of the issue, the sensitivity of the issue, and the level of difficulty/expertise required to execute the trade. Boatmen's engages in block trades and crossing where possible.

Ownership

Boatmen's is a wholly owned subsidiary of Boatmen's Bancshares.

Total Number of Equity Portfolio Managers / Analysts: 59

Total Number of Equity Traders: 8

Total Tax-exempt Equity Assets Managed: \$ 4,515 MM

Total Tax-exempt Equity Assets Managed in this Style: \$ 4,210 MM

Total Number of Tax-exempt Equity Accounts in this Style: 58

Three Largest Tax-exempt Equity Accounts in this Style:

Public Schools Retirement System of Missouri	\$1,203 MM
Non-Teachers Retirement System of Missouri	\$ 227 MM
Union Electric	\$ 126 MM

MANAGER FACT SHEET

Manager: Enhanced Investment Technologies, Inc. (INTECH)

Investment Philosophy and Process

INTECH uses a mathematical investment strategy based on stock volatility and correlation. They believe their system is mathematically proven to outperform a passive index in the long term. Their system is not based on market inefficiencies nor does it depend on return forecasts for individual stocks. INTECH's strategy generates excess returns from the relative movement of stock prices, and as long as stock prices continue to vary relative to one another, they believe their process will add value over a large capitalization passive benchmark like the S&P 500.

INTECH believes that for mature, high capitalization stocks the long term growth rate is the same. They claim based on their research that for approximately the largest 1000 market cap stocks, there is no statistical difference in the long term growth rate. The variation in the stocks short term performance is caused entirely by the random nature of the stock price process and not due to different underlying growth rates.

Research

INTECH specializes in mathematical and statistical research on stock, portfolio, and market behavior. They use computers to carry out their financial research in a scientific fashion by conducting experiments and testing hypotheses. The primary data base they use is the Center for Research in Securities Prices of the University of Chicago where they obtain all their historical pricing information. INTECH does not perform any traditional fundamental research on individual companies to attempt to discover mis-priced securities.

Portfolio Construction

INTECH's objective is to generate about 2% average annual excess return over the S&P 500 while controlling risk through several means including assigning a high priority to minimize tracking error in the optimization process, holding beta close to benchmark beta, and weighting stock in the portfolio no more than 1% from the weighting of that stock in the benchmark. The investment process ultimately produces a portfolio with no significant factor bets.

In constructing the portfolio, INTECH wants to hold the stocks that have high volatility and low correlation between them. The return volatility of the individual stocks is based on the most recent 365 days of pricing history. Once the portfolio is constructed, they will rebalance, on a weekly basis, the stocks in the portfolio back to their assigned weight until they rerun the optimization program, which is done on a quarterly basis using the updated pricing information. Over the long run they believe this investment process will beat a

Enhanced Investment Technologies, Inc. (Con't)

large cap benchmark because they incrementally sell/buy stocks in the portfolio that are currently performing better/worse than the long term average. Eventually they must perform worse/better so in the long run their growth rate equals the long term average. In essence, it is a buy low/sell high strategy.

The investment process begins with the screening of the S&P 500 to eliminate bankruptcy candidates and securities that do not meet their liquidity requirements. These screens seldom remove more than 30 stocks. A mathematical formula is used to generate optimal portfolio weightings from the universe resulting in a portfolio of 200 to 400 stocks.

Trading

INTECH uses an automated system to determine trades based on the execution of programs created by the Chief Financial Officer. This automation minimizes the time frame from the determination of the trade until the submission for execution. Generally, these are small incremental changes to the portfolio. Larger transactions result from the quarterly optimizations. These larger trades are offered to principal brokers in a bidding arrangement. If satisfactory bids are received, the lowest bidder is selected for execution. If no bids are satisfactory, the trades will be executed on an agency basis. Trading costs are monitored by INTECH for both internal trades and for trades executed by a broker based on their deviation from the target price established for that trade.

Ownership

INTECH is an independent investment advisory subsidiary of The Prudential Insurance Company of America.

Total Number of Equity Portfolio Managers / Analysts: 2

Total Number of Equity Traders: 1

Total Tax-exempt Equity Assets Managed: \$ 4,182 MM

Total tax-exempt Equity Assets Managed in this Style: \$ 4,182 MM

Total number of tax-exempt Equity Accounts in this Style: 36

Three Largest Tax-exempt Active Domestic Equity Accounts:

Public Fund	\$ 516.3 MM
Corporation	\$ 396.0 MM
Public Fund	\$ 369.0 MM

MANAGER FACT SHEET

Manager: First Asset Management - Large Cap

Investment Philosophy and Process

First Asset Management's (FAM) Large Cap Equity Style uses a disciplined approach to investing in companies whose value is not recognized by the market. By identifying those companies that possess a catalyst that will cause the market to recognize the undervaluation, FAM believes they can provide superior long-term performance.

The primary drivers of FAM's large cap value investment discipline are 1) finding companies which are undervalued; 2) anticipating change; 3) determining the fair value of a stock; and 4) uncovering the catalysts that should bring the company to fair value.

The way in which they apply this discipline continues to evolve. They currently define undervalued stocks as those which trade below market-price-to-normalized-earnings ratios and below price-to-normalized-book ratios. Anticipating change is where they look for companies that are (or will in the near term) generate accelerating earnings growth. They determine fair value using a number of methods including a dividend discount model, which incorporates projected earnings and relative price-to-earnings ratios. Catalysts typically include company restructuring, new management, and cost reduction programs.

As the market cycles, they expect different catalysts will emerge. The changes are incorporated into their process as they discover more and more companies with those traits.

Research

Approximately 80% of all research is internally generated. The portfolio managers are responsible for portfolio management, and they have industries that they monitor. One of the portfolio managers is the in-house economist. They also have an array of on-line information sources, street and regional brokerage coverage, and appropriate business and investment journals to support their investment process.

Portfolio Construction

The portfolio consists of 50 to 60 stocks with positions ranging from 1% to 3%. The portfolio is diversified in industry and sector weightings in line with the S&P 500.

First Asset Management (Con't)

Trading

The Autex System and daily broker calls are used to assist in determining the broker most capable of executing a specific stock transaction. A time stamp system is used to monitor and ensure timely execution of trades from the time the trade request is received by the trading desk to the time of execution.

Ownership

First Asset Management is a division of First Bank National Association. First Bank N.A. is a subsidiary of First Bank System (FBS), a regional bank holding company headquartered in Minneapolis.

Total Number of Equity Portfolio Managers / Analysts: 12

Total Number of Equity Traders: 3

Total Tax-exempt Equity Assets Managed: \$ 3,400 MM

Total tax-exempt Equity Assets Managed in this Style: \$ 2,200 MM

Total number of tax-exempt Equity Accounts in this Style: 78

Three Largest Tax-exempt Active Domestic Equity Accounts:

First American Stock Fund	\$ 363 MM
FBS Retirement	\$ 167 MM
Northwest Area Foundation	\$ 127 MM

MANAGER FACT SHEET

Manager: First Asset Management - Small Cap

Investment Philosophy and Process

First Asset Management's (FAM) Small Cap Equity Style uses a value oriented approach to buy stocks with market caps below \$1 billion. They believe that small cap companies possess significant growth prospects, and that a company's potential value and stock price are inefficiently linked when investment community sponsorship is low. Their approach enables them to profit by uncovering and closely monitoring unrecognized opportunities.

Research

Approximately 80% of all research is internally generated. Since the universe of stocks in this style are located in the midwest, the portfolio manager's proximity to these companies offers substantial benefits in uncovering, analyzing, and monitoring unrecognized opportunities. The most important factor in the stock selection process is face-to-face meetings with management. The portfolio managers visit over 100 companies each year.

Portfolio Construction

A bottom-up, disciplined, analytical process is used to identify attractively-valued small companies that have growth potential. Meeting management and discussing critical issues are crucial to the process by helping to sort out the potential winners from the losers.

On average, the portfolio contains 50 to 60 company names. The stated universe for this style are companies with market caps of under \$1 billion, in the following states: Minnesota, Wisconsin, Iowa, South Dakota, North Dakota, Nebraska, Montana, Colorado, Illinois, and Michigan. This universe has a total market cap of approximately \$110 billion.

Trading

The Autex System and daily broker calls are used to assist in determining the broker most capable of executing a specific stock transaction. A time stamp system is used to monitor and ensure timely execution of trades from the time the trade request is received by the trading desk to the time of execution.

First Asset Management (Con't)

Ownership

First Asset Management is a division of First Bank National Association. First Bank N.A. is a subsidiary of First Bank System (FBS), a regional bank holding company headquartered in Minneapolis.

Total Number of Equity Portfolio Managers / Analysts: 2

Total Number of Equity Traders: 3

Total Tax-exempt Equity Assets Managed: \$ 3,400 MM

Total tax-exempt Equity Assets Managed in this Style: \$ 180 MM

Total number of tax-exempt Equity Accounts in this Style: 4

Three Largest Tax-exempt Active Domestic Equity Accounts:

First American Regional Equity Fund	\$125 MM
Hormel	\$ 40 MM
Northwest Area Foundation	\$ 24 MM

MANAGER FACT SHEET

Manager: Jacobs Levy Equity Management, Inc.

Investment Philosophy and Process

Jacobs Levy believes that the investment market is very complex, and that it requires sophisticated modeling techniques to disentangle and isolate each market effect from other market influences. They feel that market inefficiency, stock characteristics, and industry affiliations are important determinants of stock pricing. Using their proprietary modeling techniques, they believe they can produce expected return predictions that are consistent and reliable.

Jacobs Levy's investment process uses a database of company fundamental, pricing, earnings, and macroeconomic data. Their valuation models consist of 32 equity attributes such as earnings, size, growth, volatility, etc., and 38 industry classifications. Jacobs Levy forms valuation models for each equity attribute and industry return series. The return series are of two general types 1) those providing consistent rewards over time; and 2) those driven by economic conditions. Rigorous statistical procedures are used to filter out strong, meaningful, and recurring relationships. They apply this system to a universe of approximately 3000 stocks to arrive at a stock ranking according to attractiveness based on expected returns.

The portfolio construction process uses an optimizer to achieve the plan sponsor's level of risk. The optimizer manages portfolio risk by controlling the active bets of the 32 equity attributes and 38 industry classifications. The portfolio construction process tries to maximize expected return given a desired level of risk relative to a selected benchmark.

Stocks are swapped out of the portfolio when their attractiveness based on stock attributes, exposure to market inefficiencies, and industry affiliation, is surpassed by other stocks. In addition, the optimizer may at times suggest a partial sale of a position to better orient the overall risk/return profile of the portfolio. In all cases, a transaction cost hurdle is applied in determining appropriate stock sales, to ensure that only economical trades occur. After lists of suggested purchases and sales have been generated, they review recent company news in a "reality check," ensuring that circumstances are not inappropriate for the desired trades.

Research

Jacobs Levy obtains its data and information through computer-readable services such as Compustat, EBIS, and U.S. government electronic bulletin boards. The research and modeling are performed internally on proprietary systems.

Jacobs Levy Equity Management, Inc. (Con't)

Trading

Jacobs Levy uses electronic networks to minimize transaction costs including a DOT machine, Instinet, Posit, and Arizona Stock Exchange. They also have a proprietary system of accessing Wall Street's upstairs order flow that reveals brokers' trading desires. In an effort to control transaction costs, an internal monitoring system calculates transaction costs in real-time. In addition, they use the outside services of Abel Noser and Plexus to monitor costs. Jacobs Levy uses the flexibility of their investment approach to substitute names when the cost warrants. They also use working orders, block orders, and principal package trades for more urgent trades.

Ownership

Jacobs Levy Equity Management, Inc. is 100% owned by Bruce Jacobs and Kenneth Levy on a 50/50 basis.

Total Number of Semi-Passive Equity Portfolio Managers / Analysts: 8

Total Number of Semi-Passive Equity Traders: 3

Total Tax-exempt Equity Assets Managed: \$ 2,749 MM

Total tax-exempt Domestic Equity Assets Managed in this Style: \$ 1,405 MM

Total number of tax-exempt Domestic Equity Accounts in this Style: 9

Three Largest Tax-exempt Semi-Passive Domestic Equity Accounts:

IBM	\$ 531 MM
NYNEX	\$ 352 MM
Deere & Company	\$ 284 MM

MANAGER FACT SHEET

Manager: Lazard Freres Asset Management

Investment Philosophy and Process

Lazard Freres' philosophy is based on bottom-up value stock selection achieved by focusing on companies which are financially productive yet inexpensively priced. They believe they add value by evaluating companies the same way managements measure their own performance, by focusing on financial productivity and the long-term sustainability of returns (return on equity, return on assets, operating margins) rather than just price/earnings multiples and earnings projections.

Lazard Freres uses a stock selection process incorporating three levels of investment research. Level 1 screens 4,500 companies in the Compustat Database for companies with characteristics that indicate under valuation versus various market indices. Screens identify companies that have high financial returns (return on equity and return on assets), yet are attractively priced.

That initial screening results in approximately 900 issues that satisfy Lazard Freres' definition of value. Level 2 is an accounting validation to determine that the companies' financial productivity is accurately stated, to look for and take advantage of pricing anomalies, and to discover opportunities, including hidden asset values not recognized in the market price.

Level 3 is fundamental analysis conducted on approximately 450 names to ensure the sustainability of returns, to discover hidden value, and to identify a catalyst for price revaluation. The fundamental variables include quality and depth of management, competitive position, sensitivity to economic/market cycles, margin and sales trends, brand name strength, geographical breakdown, and macro environment in which company operates.

In constructing the portfolio, the investment team must agree on the merits of each security before a security can be added to the 55-70 name portfolio. A security may be sold if its price rises to a level where it no longer reflects value, the underlying investment assumptions are no longer valid, or the market itself becomes overvalued.

Research

The firms full-time equity analysts are responsible for following the issues that have satisfied the initial fundamental screening process (approximately 900). After further analysis, 450 securities are monitored more closely. Earnings estimates are updated and distributed monthly, and reports are prepared and distributed quarterly. The securities are

Lazard Freres (con't)

also computer tracked to monitor their price relationships to overall market conditions. Approximately 85% of the research ideas are generated internally by the portfolio managers/analysts and research analysts. Outside research is acquired and used for verification purposes.

Trading

Lazard Freres uses both individual stock orders and program trades. Program trades are used to invest the initial funding of a portfolio or a significant contribution to an existing client portfolio. They use approximately 110 different broker/dealers per year. Brokers are selected for their ability to provide best execution including the clearing and settlement of trades. Traders are responsible for seeking the best execution which is considered to be the most favorable combination of price and quantity. Lazard Freres utilizes SEI's Trading Cost Summary to monitor commission rates and market impact on client performance.

Ownership

Lazard Freres Asset Management (LFAM) is the asset management division of Lazard Freres & Co. LLC (LF&Co.). Effective May 1, 1995, L&F Co. elected to convert from a limited partnership to a limited liability company statute. There was no change in the ownership or control of LF&Co. as a result of the conversion to LLC status. LF&Co. has 67 general members and 20 limited members. Eight of Lazard Freres & Co.'s general members are assigned to LFAM.

Total Number of Equity Portfolio Managers/Analysts: 29

Total Number of Equity Traders: 6

Total Tax-exempt Equity Assets Managed: \$ 13,926 MM

Total tax-exempt Equity Assets Managed in this Discipline: \$ 7,792 MM

Total number of tax-exempt Equity Accounts in this Discipline: 95

Three Largest Tax-exempt Domestic Equity Accounts:

State Board of Admin. of Florida	\$ 1,028 MM
General Motors Master Retirement Trust	\$ 702 MM
I.A.M. National Pension Fund	\$ 294 MM

MANAGER FACT SHEET

Manager: Pacific Investment Management Company

Investment Philosophy and Process

Pacific Investment Management Company's (PIMCO) investment philosophy is based on the principle that stock index futures, when used as a non-leveraged vehicle for obtaining long-term equity exposure, offer an attractive means for enhancing equity market returns. They believe that stock index futures contracts are typically used as a means to gain market exposure over short, uncertain time horizons. Thus, the contracts must be backed with relatively risk-free debt securities which provide nearly perfect liquidity, since the entire portfolio could be liquidated on a moment's notice. This is why, in practice, the computation of the fair value of a stock index futures contract uses a riskless T-bill rate with a maturity equal to the expiration date of the futures contract. By maintaining constant exposure, PIMCO believes their skill as a fixed income manager gives them an advantage to seek out higher returns on the high quality fixed income securities they use to back the futures contracts. They actively manage the duration of the fixed income portfolio within a range of zero to one year with six months being a neutral duration target. They feel the six month neutral point represents a very efficient point on the yield curve.

PIMCO's investment process involves going long S&P 500 index futures in an amount sufficient to cover 100% of the value of a client's investment. This requires an initial margin deposit in the form of T-bills equal to approximately 5% of the value of the investment. They use the remaining 95% to construct a portfolio of high quality (a minimum quality per issue of Baa) fixed income securities.

They use the same process for determining the duration in the equity portfolios as they use in all their other fixed income accounts. The process to construct a fixed income portfolio begins with an annual, secular economics forum in which all investment professionals participate to establish a duration target for the portfolio. During the forum internal and external professionals present information on long-term economic, geopolitical, fiscal, monetary, and demographic trends. On a quarterly basis, they define the exact duration target during an economics forecasting session. This session focuses on near-term outlook for GDP, inflation, business, cycle position, and Federal Reserve policy. The portfolio's strategy is carried out by consensus of the team.

Research

PIMCO relies primarily on in-house research for decision making. They maintain several databases using data provided by the Bureau of Economic Analysis, the Commerce Department, the Congressional Budget Office, the Federal Reserve Board, the OECD, and

Pacific Investment Management Company (Con't)

others. They also have developed and maintain over 30 computer models and programs to evaluate the treasury coupon and strip curves, options embedded in various mortgage and corporate securities, and financial futures. PIMCO also performs credit analysis internally on every issue held in the portfolio. They focus on those issues that show improving credit profiles and the potential for upgrades by the rating agencies giving them greater appreciation potential.

Portfolio Construction

PIMCO's fixed income portfolio group works on a team or consensus basis to develop and implement portfolio strategy. The group's structure can best be described as a hub and spoke system, with five senior generalist portfolio managers being the hub, receiving input from several specialists (governments, corporates, mortgages, derivatives, international, etc.). The generalists have responsibility for implementing strategy in specific portfolios, while the specialists assist them with expertise and execution in their respective areas.

Trading

The portfolio managers conduct all the trading and have constant access to live trading information through Telerate, Bloomberg, Quotron, etc. They also have direct lines to all the major dealers. PIMCO executes all trades on a best efforts basis and maintains relationships with those brokers who are able to make the best markets.

The portfolio management team monitors the trading and execution efficiency. They attempt to use PIMCO's size in the fixed income markets as an advantage in demanding tight markets from the dealer community. PIMCO also believes they have the ability to operate rapid-fire competitive bidding processes for trades when appropriate.

Ownership

Pacific Investment Management Company (PIMCO) is wholly-owned by publicly traded PIMCO Advisors L.P. who in turn is owned 18.4% by the public; 38.2% by senior management; and 43.4% by Pacific Mutual. Forty-five percent of the profits of each investment management subsidiary, including PIMCO, are kept at the subsidiary level for distribution among key professionals.

Pacific Investment Management Company (Con't)

Total Number of Equity Portfolio Managers / Analysts: 17

Total Number of Equity Traders: 0 (Executed by portfolio manager)

Total Tax-exempt Equity Assets Managed: \$ 7,317 MM

Total tax-exempt Equity Assets Managed in this Style: \$ 7,232 MM

Total number of tax-exempt Equity Accounts in this Style: 18

Three Largest Tax-exempt Equity Accounts in this Style:

Limited Partnership	\$ 1,691 MM
Public	\$ 1,056 MM
Multi-Employer	\$ 658 MM

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MANAGER FACT SHEET

Manager: Wellington Management Company

Investment Philosophy and Process

Wellington Management's objective is to produce superior returns by investing in a carefully researched portfolio of temporarily out-of-favor large capitalization companies that provide above average dividend yields and sell at below average P/E multiples. Their primary focus is on the valuation and selection of individual stocks based on intensive in-house fundamental research.

Portfolio Construction

Wellington Management's primary investment universe consists of companies with large market capitalization and below average price/earnings multiples. Companies that pass an initial review are subjected to intensive fundamental research. They scrutinize the companies' financial statements looking for hidden values and particularly for signs of an inflection point in profits. Detailed earnings forecast models on each company are maintained and updated frequently.

Security selection is driven by the "Fact Sheet", an investment discipline which ranks stocks (both current holdings and purchase candidates) by their appreciation potential. New positions are added to the portfolio when they compare favorably with holdings near the top of the Fact Sheet. Existing holdings are sold as they move to the bottom, reflecting a diminishing opportunity for incremental relative return. The Fact Sheet is computed daily with inputs being constantly reviewed. Company management is also contacted at least monthly.

Sector and industry diversification is essentially the result of individual security selection, although no more than 20% of the portfolio would typically be committed to a single industry. Portfolio industry weights may vary widely from benchmark weights. Portfolios typically hold 60 to 80 stocks, with the exposure to a single stock typically limited to 7%.

Research

Wellington Management Company does approximately 85% - 90% of their research internally. They feel their independent evaluation and ability to establish their own research priorities are central to their ability to produce superior returns for their clients. The value/yield team is a portfolio manager and four analysts dedicated to the value/yield product. In addition, Wellington Management has 23 global industry analysts, 22 equity portfolio managers managing other products, 22 research analysts assigned to other

Wellington Management Company (Con't)

investment specialty teams and the sell-side as information sources and to complement / supplement its own work.

Trading

Wellington Management traders assume a proactive approach to trading, seeking low commissions and best execution. They typically retain control of orders and work them rather than delegating responsibility to outside brokers. The selection responsibility lies with the individual trader but is reviewed daily by the head trader and semiannually by the Wellington Management Company Trading Panel to evaluate trading costs and brokerage placement. Trading tends to be gradual. They use scale buying and selling, and they limit orders extensively. They tend to buy on weakness and sell into strength.

Ownership

Wellington Management Company is an employee-owned partnership whose sole business is investment management. The firm is owned by 52 general partners, all active employees of the firm.

Total Number of Equity Portfolio Managers / Analysts: 82

Total Number of Equity Traders: 10

Total Tax-exempt Equity Assets Managed: \$ 19,331 MM

Total tax-exempt Equity Assets Managed in this Style: \$ 2,474 MM

Total number of tax-exempt Domestic Active Equity Accounts: 10

Three Largest Tax-exempt Active Domestic Equity Accounts:

AT&T	\$ 810 MM
J. Paul Getty Trust	\$ 385 MM
Fortune 10 Company	\$ 367 MM

MANAGER FACT SHEET

Manager: Goldman Sachs Asset Management

Investment Philosophy and Process

Goldman Sachs' investment philosophy states that markets are not totally efficient and that investment insights can lead to superior performance. Their approach combines fundamental analysis with quantitative valuation modeling to identify attractive securities and construct portfolios. The fundamental analysis is performed by in-house research analysts with detailed, hands-on knowledge and the ability to evaluate nonquantitative factors, while the quantitative model uses consensus estimates to generate its predictions. Goldman Sachs believes that these two independent sources of expected returns provides added confidence in their combined return forecasts.

Goldman Sachs' investment process involves three steps. First, in-house fundamental research is done to scour the equity universe to uncover the most attractive stocks. Second, quantitative analysis uses a multifactor model to analyze securities for attractiveness in value, potential growth and earnings, timeliness, volatility of earnings and price, and liquidity.

In February 1995, Goldman Sachs added two enhancements to the quantitative multifactor model: 1) Dynamic Factor Weights - relates performance of various stock selection strategies to events in the general economy, and 2) Nonlinear Estimation - in deriving an estimation, it allows variables to respond to changing economic conditions in different increments depending on their initial level rather than assuming a constant rate of change no matter what the situation is.

The net result of the fundamental research and quantitative analysis is a single expected return forecast for each security. Using this forecast for each security's expected return, Goldman Sachs builds a portfolio with the use of portfolio optimization techniques to evaluate risk/reward profiles of potential portfolios. The portfolio selected is that which best fits a client's investment objectives and risk tolerance.

Research

Fundamental research for the Goldman Sachs' strategy is generated completely internally through the resources of Goldman Sachs' Equity Investment Research Department. Nearly 130 professionals are on staff to cover more than 1,700 companies in over 60 industries. In addition, Goldman Sachs' models utilized data from I/B/E/S, FirstCall, Compustat, Value Line, and FactSet to evaluate individual securities. They use Muller

Goldman Sachs Asset Management (con't)

and Telstat as pricing sources for securities. Finally, their optimization process utilizes such risk-controlling tools as the BARRA E2 Model and Salomon Brothers' Risk Attribution Model (RAM) data and software.

Trading

Goldman Sachs believes that cost effective trading strategies are especially important for a semi-passive product. They employ a variety of trading strategies including cross trades, incentive agency trades, blind strike bids (packaged trades), market orders, and limit orders. Goldman Sachs evaluates the relationship between commission, market impact, and missed opportunities before deciding the trading strategy to implement.

Ownership

Goldman Sachs Asset Management is a division of Goldman, Sachs & Co., a partnership.

Total Number of Semi-Passive Equity Portfolio Managers/Analysts: 8

Total Number of Semi-Passive Equity Traders: 1

Total Tax-exempt Equity Assets Managed: \$ 4,994 MM

Total tax-exempt Domestic Semi-Passive Equity Assets Managed: \$ 2,816 MM

Total number of tax-exempt Domestic Semi-Passive Equity Accounts: 19

Three Largest Tax-exempt Passive Domestic Equity Accounts:

Western Conference of Teamsters	\$667 MM
New York City Teachers	\$376 MM
GTE Services Corp.	\$345 MM

MANAGER FACT SHEET

Manager: Investment Research Company Asset Management (IRC)

Investment Philosophy and Process

Investment Research Company's (IRC) investment philosophy is premised on the belief that excess performance can best be achieved by applying a structured and disciplined quantitative process to identify a portfolio that is likely to outperform the selected benchmark. The objective of IRC's models is to select the best performing stocks within each of their nineteen industry sectors and to assign each sector a weight equal to the sector's weight in the benchmark. IRC's Benchmark Enhancement product is a customized strategy designed to produce excess return subject to client-specified tracking error.

The investment process begins with the client-specified benchmark universe. They partition the universe into nineteen distinct and non-overlapping industry sectors. As a risk control measure, the weightings of each industry sector in the portfolio will match the weightings of the benchmark universe. In each of these industry sectors, a three step process is employed to construct a sector portfolio.

The first step is to apply a dividend filter which will eliminate the low dividend yielding stocks of the sector. This filter is primarily used for risk control as low dividend stocks tend to be more volatile and more vulnerable in market downslides.

The second step employs a proprietary optimizer which selects portfolios with historically low volatility and favored style/capitalization attributes as defined by the market based on the previous 40 weeks of total return data. In particular, stocks are processed through IRC's optimization model on the basis of four considerations: 1) relative strength (momentum) over the past 40 weeks, 2) volatility of stock returns, 3) covariance of returns among all stocks in the sector, and 4) departures of real world returns from the simplistic normal curve assumption. The output of this optimization, in each sector, is an optimal 8 to 10 stock portfolio.

Step three of the process employs a price-to-earnings screen to eliminate stocks with the highest price-to-earnings ratio (relative to other stocks in the sector). This final step has been successful in protecting the portfolio in periods of market corrections as the overvalued stocks in a sector are the most vulnerable. The final stock weights are then determined by recalculating the optimized weights. The tracking error of the final optimized portfolio is quantitatively controlled by requiring that each stock in the benchmark universe is held at a weight which is within a specified tolerance (such as +/- 0.3%) of that stock's weight in the benchmark universe.

Investment Research Company Asset Management (IRC) (Con't)

To achieve time diversification and minimize turnover, one third of the portfolio assets are rebalanced quarterly. This rebalancing determines new optimal stock holdings based upon the previously described process. Stocks identified as more attractive candidates are purchased to replace less attractive stocks.

Research

Most of the firm's research is conducted internally and is proprietary to IRC. The firm applies state-of-the-art statistical and computer techniques to research and develop equity selection models. Outside information sources include data vendors such as McGraw-Hill and various other data repository sources.

IRC currently produces valuation rankings for approximately 1000 stocks. Their expertise is primarily large cap equities; although, IRC's quantitative models are capable of analyzing any US stock. Approximately 450 stocks are owned by IRC's clients across the entire firm.

Trading

IRC applies a structured disciplined process to trading. All purchase and sell transactions are continuously monitored against their "strike" prices (i.e., the prices prevailing in the market immediately prior to the decision to buy or sell). Nearly all trades are executed within four business days of the decision date. IRC evaluates its brokers with external and internal tools to ensure compliance with the firm's objectives for timely and effective execution.

IRC staggers its quarterly re-balancing for its client portfolios throughout the quarter. They analyze and attempt to avoid situations where its purchase or sale quantities might have significant market impact. In rare cases where the firm must execute large transactions, IRC's preference is to employ passive crossing networks.

Investment Research Company Asset Management (IRC) (Con't)

Ownership

Investment Research Company became a wholly-owned subsidiary of United Asset Management (UAM) in March, 1994.

Total Number of Semi-Passive Equity Portfolio Managers / Analysts: 3

Total Number of Semi-Passive Equity Traders: 2

Total Tax-exempt Equity Assets Managed: \$ 1,781 MM

Total tax-exempt Domestic Semi-Passive Equity Assets Managed: \$ 1,566 MM

Total number of tax-exempt Domestic Semi-Passive Equity Accounts: 16

Three Largest Tax-exempt Semi-Passive Domestic Equity Accounts:

Ameritech Corporation	\$ 316 MM
Virginia Retirement System	\$ 260 MM
A regional Bell holding co.	\$ 243 MM

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MANAGER FACT SHEET

Manager: Martingale Asset Management

Investment Philosophy and Process

Martingale's philosophy is to buy stocks that are cheap relative to their peers based on a multifactor valuation model. They feel the systematic application of stock valuation judgment and rigorous control of portfolio exposure to industry and investment characteristics relative to the selected benchmark results in investment success.

Martingale's investable universe of approximately 1400 stocks is determined by the intersection of coverage by Value Line, Compustat, and IBVEAS. The raw data for the investable universe is used as an input to the Martingale Valuation Model. Martingale's Valuation Model is a combination of fundamental analyst and statistician. There are five investment characteristics that we emphasize; low P/E (based on current earnings), low P/E (based on earnings 3 to 5 years out), low P/B, high sustainable growth, and positive earnings estimate revision. Stocks are scored on each dimension with an aggregate score given to each stock. The weight of each factor is determined by their expected value added, volatility and correlation with the other factors. More weight is given to a factor with high expected value added, low volatility and low correlation with the other factors.

To construct the portfolio, Martingale uses an optimizer that builds a portfolio to obtain the highest positive alpha while closely matching the industry and common factor risk of the selected benchmark. Martingale monitors the portfolio's risk characteristics and individual asset performance on a continuous basis. The BARRA USE2 Equity Risk Model is used to estimate tracking volatility.

Research

Martingale attempts to obtain full data coverage for all publicly traded equities through external information sources including IBES, Value Line, Horizon Investment Research, Compustat, BARRA, and Factset. All internal research is directed at improving the valuation model so that it more accurately defines the most undervalued stocks in its universe.

Martingale's data base contains data on approximately 6000 stocks. They produce primary valuation estimates for 1400 companies and secondary valuations for an additional 1200 companies. Their semi-passive portfolios typically hold 100 to 150 stocks. Firm-wide they own over 500 companies.

Martingale (con't)

Trading

As part of rebalancing a portfolio, Martingale calculates the liquidity of each stock in the universe and converts that information into upper and lower bounds to assure that no recommended trade exceeds liquidity targets. The recommended trades are reviewed for

special situations and then the list is separated into stocks that can be packaged together and those that must be handled separately. The final trade list is put for competitive bids.

Martingale uses crossing networks, packaged trades with and without guaranteed prices, and brokers to execute individual trades. Martingale evaluates each trade to measure the cost of that trade, and they measure the opportunity cost of the trades that they have not made yet.

Ownership

Martingale Asset Management is an Investment Advisor which is 60% owned by Commerz International Capital Management, 37.5% by employees of the firm, and 2.5% by a limited partner. Commerz International Capital Management, a worldwide asset management subsidiary of Commerzbank, Germany's third largest bank, became a general partner in the fall of 1995.

Total Number of Semi-Passive Equity Portfolio Managers / Analysts: 6

Total Number of Semi-Passive Equity Traders: 1

Total Tax-exempt Equity Assets Managed: \$ 397 MM

Total tax-exempt Domestic Semi-Passive Equity Assets Managed: \$ 122 MM

Total number of tax-exempt Domestic Semi-Passive Equity Accounts: 3

Three Largest Tax-exempt Semi-Passive Domestic Equity Accounts:

The Investment Fund for Foundations	\$ 49 MM
Saint-Gobain Corporation	\$ 48 MM
Accessor Funds, Inc.	\$ 25 MM

MANAGER FACT SHEET

Manager: PanAgora Asset Management - Semi-Passive

Investment Philosophy and Process

PanAgora's semi-passive equity strategy is structured to provide incremental returns in comparison to a client-specified benchmark. Their investment models are used to produce one month forecasted returns for the stocks in their universe. They divide the universe on growth and value criteria. Investment models are used to produce individual stock forecasts for stocks contained in the universe as well as a more general forecast to estimate which style group (growth or value) will outperform the other. Portfolios are then constructed using a portfolio optimization program, which maximizes returns while adjusting for a given level of risk and transaction costs.

PanAgora's investment process involves six steps. First, they divide the clients stock universe into growth and value style groups based on price/book. (Their database contains approximately 3100 securities.)

Second, they produce a one-month forecast of returns for each stock within the divided universe using criteria that drive performance in this style grouping. Growth stock forecasts are produced by looking at long term earnings adjusted for dividends. For value stocks, book to price is used in forecasting value stock price movements. Other criteria applicable to all stocks include earnings revisions, capitalization, and earnings momentum.

Third, they produce one-month forecasted returns for the growth universe and for the value universe based on macroeconomic variables such as the risk premium, industrial production and aggregated financial ratios such as book to price and price to sales.

Fourth, they combine the forecasts in step two and step three.

Fifth, the forecast's alphas are then put into an optimization process which creates the final risk / return portfolio versus a predetermined benchmark. Optimization for the semi-passive product is base on Advanced Portfolio Theory and is performed through a Northfield Optimizer. The risk model measures each security's exposure to macroeconomic events such as changes in interest rates, price changes, and the stage of the business cycle. The portfolio exposure to these factors is constrained, resulting in an expected tracking variance of about 100 basis points versus the benchmark.

Lastly, they take the output from the optimizer and check for recent news items to ensure that they are not about to buy a stock which had a significant event that will adversely

PanAgora Asset Management - Semi-Passive (Con't)

affect the stock price. Then sells and buys are implemented. This process occurs monthly or if there is a very significant market movement.

Research

Approximately 90% of PanAgora's research is done internally. PanAgora supports an in-house research group of full-time investment professionals who conduct research and develop new or improve upon existing quantitatively structured investment products. In addition, an Academic Advisory Committee provides inputs to the research efforts including: 1) early indications of innovations being developed within academics, 2) act as an intellectual audit of their research, and 3) periodically collaborate with PanAgora on specific research issues.

To complement their internal research, PanAgora subscribes to external quantitative research services including: Wall Street investment resources, Stockfacts, Barra, Value Line, First Call and Zacks.

PanAgora currently produces a valuation ranking for 3100 domestic stocks. They manage assets to over 70 different benchmarks, and own approximately 2500 domestic stocks across the entire firm.

Trading

PanAgora's five portfolio managers perform all of the trading for the accounts. The trading tactics employed range from direct crossing with other market participants to broker-at-risk packages. They utilize package trading, automated trading networks, basis trades, and crossing networks, to minimize transaction costs. They use both existing direct crossing services, POSIT, Instinet, The Crossing Network, as well as the informal crossing network that exists among passive and semi-passive market participants. Sixty percent of their equity products' trades are done through crossing networks.

PanAgora Asset Management - Semi-Passive (Con't)

Ownership

The ownership structure is an equal partnership between Lehman Brothers, Inc. (50%) and Nippon Life Insurance Company (50%). PanAgora is solely responsible for the management of client portfolios and their owners have played a passive role.

Total Number of Semi-Passive Equity Portfolio Managers / Analysts: 10

Total Number of Semi-Passive Equity Traders: 0

Total Tax-exempt Equity Assets Managed: \$ 5,783 MM

Total tax-exempt Domestic Semi-Passive Equity Assets Managed: \$ 1,408 MM*

Total number of tax-exempt Domestic Semi-Passive Equity Accounts: 22*

Three Largest Tax-exempt Semi-Passive Domestic Equity Accounts:

Smith Barney/TRAK*	\$ 755 MM
Schlumberger	\$ 143 MM
Hartford Life Insurance	\$ 40 MM

* This account has both tax-exempt and taxable assets.

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MANAGER FACT SHEET

Manager: Weiss, Peck & Greer, L.L.C. (WP&G)

Investment Philosophy and Process

WP&G investment philosophy is to manage portfolios using Modern Portfolio Theory's risk reduction techniques to maximize return. Diversification is the primary goal, which according to Modern Portfolio Theory, is accomplished in a portfolio by overweighting the stocks whose returns tend to be uncorrelated to one another and underweighting the stocks that are highly correlated. The end result of the diversification techniques is the creation of portfolios that have higher returns, lower betas, lower absolute variance and outstanding defensive characteristics versus a relevant benchmark.

To implement this overall strategy, WP&G compiles the historical price data of all stocks in the benchmark portfolio. WP&G builds a complete matrix, using historical price data, and then examines all possible relationships between these stocks in the benchmark portfolio.

Using software programs and risk modeling, a number of portfolios, consisting of stocks in the benchmark, are constructed that they believe have the optimized risk/reward ratios. The risk/reward ratio is simultaneously optimized from both an absolute risk reduction perspective, as well as from a relative perspective to achieve the desired benchmark tracking objective. From these alternative portfolios, WP&G selects the combination of stocks, together with their appropriate weightings, that WP&G believes will comprise the optimal portfolio based on the client's specification. This optimal portfolio is designed to have a return greater than, but highly correlated to, the return of the benchmark portfolio.

After the optimal portfolio is constructed, the portfolio is rebalanced monthly to maintain the original optimal weights. WP&G will sell a stock when the stock's weight within the portfolio becomes significantly greater than its optimal weight. WP&G will buy a stock when the stock's weight within the portfolio becomes significantly less than its optimal weight.

WP&G repeats the entire optimization process as often as necessary to achieve appropriate benchmark tracking objectives but at least every six months.

Weiss, Peck & Greer, L.L.C. (WP&G) (Con't)

Research

At WP&G, research is conducted by the Principals and Co-Directors of Research & Development in the areas of return attribution analysis, product and software development, and improved modeling techniques. Between 1985 and 1992, they created the software and modeling techniques needed to apply Modern Portfolio Theory to the creation of their quantitative investment products. Currently, they are working on improving their estimation procedures and on a risk measure that can be used in understanding which market environments are better suited for their diversification strategy.

WP&G maintains an internal database of approximately 10,000 securities which contains daily pricing data which goes back approximately 25 years. They use the DAIS, Compustat, and Merrill Lynch databases for security pricing updates. Approximately 700 different stocks are owned by the firm across equity styles.

Trading

The goal of WP&G's quantitative equity trading operation is to establish portfolios with the lowest transactions costs in an appropriate time frame. They use four main types of trading facilities. They are 1) high technology brokers; 2) crossing networks; 3) principal brokers; and 4) client-directed brokers.

To effectively execute large trades, WP&G generally use packaged (or program) agency trades when dealing with sophisticated brokers capable of monitoring portfolios electronically on a real time basis, frequently with the option to switch to crossing networks to handle as much as 50% of the trades when they feel it is appropriate.

WP&G measures the performance of each significant trade that they make by establishing a benchmark for each portfolio trade, taking aggregate pre- and post-trade prices into account. This allows them to evaluate their brokers, the strategy they have implemented, and their alternatives going forward.

Ownership

The firm is a Limited Liability Company owned primarily by its 46 principal employees. Each WP&G Principal owns a percentage interest in the firm and is actively involved in the day-to-day operations of the firm. Lloyds America Security Corporation, a subsidiary of Lloyds Bank, Plc., of London acquired an interest in WP&G in 1987 and remains a non-managing principal of the firm.

Weiss, Peck & Greer, L.L.C. (WP&G) (Con't)

Total Number of Semi-Passive Equity Portfolio Managers / Analysts: 7

Total Number of Semi-Passive Equity Traders: 2

Total Tax-exempt Equity Assets Managed: \$2,677 MM

Total tax-exempt Domestic Semi-Passive Equity Assets Managed: \$1,041 MM

Total number of tax-exempt Domestic Semi-Passive Equity Accounts: 35

Three Largest Tax-exempt Semi-Passive Domestic Equity Accounts:

US Large Equity Fund	\$ 195 MM
Quantitative Equity Fund	\$ 145 MM
So. Nevada Bartenders & Culinary Workers	\$ 124 MM

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BOND MANAGER FACT SHEET

Manager: *Brinson Partners, Inc.*

Investment Approach

Brinson uses a highly quantitative, disciplined process, with an emphasis on risk management. They add value by actively managing interest rate sensitivity, yield curve positioning, sector exposure and individual security selection. Each of these four factors are key determinants in the construction of the optimal client portfolio. In addition to managing U.S. portfolios, Brinson has international portfolio construction expertise.

Brinson adds value first by actively managing interest rate risk. The process begins with determining an equilibrium asset return. This is the long-term normal market return required of an asset to compensate the investor for its risk. The factors that go into determining this return are the real risk free rate, the inflation premium and the risk premium for a particular asset. Once the equilibrium asset return, or required rate is calculated, it is compared to current market yields. This drives the duration decision. The firm does not take large bets, but will adjust the portfolio for perceived differences in required returns and those observed in the market. Portfolio duration averages 4.5 years.

Next, the firm adds value by incorporating expected changes in the shape of the yield curve. In their analysis, the "normal" yield curve is plotted against the current yield curve. This helps uncover relative over/under valuations along sections of the curve.

Sector strategies are implemented based on a comparison of current market yield spreads with estimates of equilibrium yield spreads for particular segments of the U.S. bond market. Equilibrium yield spreads take into account credit risks, the value of imbedded options, mortgage prepayments, etc.

Having established the overall maturity, yield curve and sector exposures, the portfolio manager searches for individual bonds which will give these macro-characteristics at the lowest cost. In-house credit research is an important element within the corporate bond sector, and analysis of pre-payments and option adjusted spreads are crucial to the mortgage security selection.

Ownership

In April of 1995, Brinson Partners, Inc. and Swiss Bank Corporation combined their respective investment management organizations into a single investment management business which is managed by Brinson Partners, Inc. Brinson Partners, Inc. remains a completely independent organization within Swiss Bank Corporation, enabling the firm to preserve the integrity of its investment process and management structure. Brinson Partners, Inc. has direct control of the combined investment operation and Gary P. Brinson, CFA, is the Chief Investment Officer and Chief Executive Officer.

Brinson Partners (con't)

<u>Assets Under Management</u>	<u>12/31/95</u>
Total fixed income assets managed:	\$14.0 billion
Total fixed income assets managed in the core fixed income style:	\$4.4 billion
Total number of fixed income accounts managed for this style:	31

Three largest tax-exempt accounts managed in this style:	<u>Account Type</u>	<u>Market Value</u>
	Corporate	\$457 million
	Union	\$346 million
	Public	\$340 million

BOND MANAGER FACT SHEET

Manager: *Durkee Capital Advisors*

Investment Approach

Durkee Capital Advisors was founded in 1989 to manage fixed income securities using a variety of quantitative investment techniques. These techniques were developed and refined by the founding partner, Edward Durkee, prior to establishing the firm.

The firm's investment style is termed "Reactive Allocation." The objective of Reactive Allocation is to earn excess returns over a given benchmark index. Portfolios are indexed during periods of price dormancy, and adjusted to exploit price trends in up or down markets through security selection and dynamic trading. Their approach eliminates any type of forecasting or "betting." It makes small changes to portfolios purely in reaction to market events that have already occurred. These changes alter duration slightly and take advantage of the convexity effect.

Reactive Allocation is an objective, structured, quantitative strategy which rejects any type of anticipation. It relies solely on observed price movements to determine portfolio adjustment. It assumes future price changes are unknowable; it simply adjusts to such changes as they happen. Capital is preserved by automatically shortening maturities during period of declining prices. The strategy is adaptable to managing domestic or international portfolios of short, intermediate or long duration.

Portfolio quality is primary and approximately 75% of each portfolio is comprised of U.S. Treasury and Agency bonds. Any corporate securities used are restricted to issues rated AA or better. They don't purchase callable or redeemable securities. While many managers with such high quality portfolios have difficulty competing for overall return, Durkee Capital attempts to combine safety with performance. Their standard deviation is very close to that of the Lehman Government/Corporate Bond Index. Durkee reports that their Reactive Allocation has outperformed the Lehman Index in all but one year since inception (gross of fees).

Ownership

Durkee Capital is 50% employee owned and 50% owned by external, passive investors previously associated with Chicago Research & Trading.

Durkee Capital (con't)

<u>Assets Under Management</u>	<u>12/31/95</u>
Total fixed income assets managed:	\$916 million
Total fixed income assets managed in the core fixed income style:	\$309 million
Total number of fixed income accounts managed for this style:	13

Three largest tax-exempt accounts managed in this style:	<u>Account Type</u>	<u>Market Value</u>
	San Diego Employees' Retirement System	\$118 million
	Daughters of Charity National Health System	\$80 million
	Building Laborers' Pension Fund	\$54 million

BOND MANAGER FACT SHEET

Manager: *J.P. Morgan Investment Management, Inc.*

Investment Approach

J.P. Morgan's active fixed income investment style seeks to maximize yield as a reliable source of excess return, and add only moderate additional value from inherently riskier duration decisions. The firm makes only modest duration bets, emphasizes rigorous credit analysis, quantitative research, active sector and security selection and well-executed trading as consistent sources of value.

In order to make the duration decision, several factors that affect interest rates are analyzed. On a monthly basis, interest rate and volatility forecasts are developed for optimistic, pessimistic and most likely economic scenarios. In addition, the likelihood of non-parallel shifts in the yield curve are incorporated in the analysis. Having assessed these factors, the firm positions the maturity and structure of the portfolio. Portfolio duration is rarely greater than +/- one year of the client benchmark portfolio.

Sector allocation and security selection are also important aspects of the investment process. Morgan analyzes the current spreads versus historical norms as well as utilizes market and credit research to assess fair value and the likelihood of sector spreads widening or narrowing. Securities are selected by the portfolio managers with substantial input coming from the trading desk and fixed income research area.

To achieve outperformance and diversify risk in the actively managed fixed income accounts, Morgan participates in the entire fixed income market. They complement the use of traditional instruments by investing in corporate private placements, directly placed mortgages, non-dollar securities, financial futures, and bond options. The firm's research shows that using these extended markets in conjunction with the traditional securities provides higher returns, improves creditworthiness and reduces risk in actively managed portfolios. In general, they have been overweighted in corporates and mortgages versus the aggregate benchmark over time.

Ownership

J.P. Morgan Investment management is a wholly-owned subsidiary of JP. Morgan & Company, Inc., a bank holding company which also owns Morgan Guaranty Trust Company, J.P. Morgan Securities, Inc. and J.P. Morgan Futures.

J.P. Morgan (con't)

<u>Assets Under Management</u>	<u>12/31/95</u>
Total fixed income assets managed:	\$62.1 billion
Total fixed income assets managed in the core fixed income style:	\$20.7 billion
Total number of fixed income accounts managed for this style:	182

Three largest tax-exempt accounts managed in this style:	<u>Client Type</u>	<u>Market Value</u>
	Corporate Pension	\$2.3 billion
	Corporate Pension	\$719 million
	Public Pension	\$700 million

BOND MANAGER FACT SHEET

Manager: *Loomis, Sayles & Co.*

Investment Approach

Loomis Sayles' investment grade fixed income portfolios offer above average yield as well as capital gains potential by focusing on discount, investment grade, corporate bonds. By leveraging off the firm's significant commitment to credit research, their investment grade style primarily seeks to add value through "bond picking" in the BBB and A markets. Additionally, they attempt to add value by building structural advantages into their portfolios which include; 1) yield advantage, 2) credit bias, and 3) call protection. The common objective for investment grade accounts is to deliver superior performance while limiting portfolio volatility.

By accepting the credit risk of corporate bonds, Loomis' investment grade portfolios attempt to capture the yield advantage of BBB and single A issuers. In a low turnover portfolio that is well call protected, they will attempt to lock-in yield premiums which over time materialize as total return. Loomis' in-house credit research capability seeks to go beyond the major credit agencies to identify and anticipate likely credit movements. By constructing portfolios with credit bias in mind, they seek to participate in upgrades and avoid downgrades.

Loomis monitors yield spreads over the maturity Treasury bonds to evaluate sectors, industries and issues on their current relative value. Using this information, they will overweight industries and sectors they perceive offer the most value. Loomis does limit investment in a single issuer to five percent of the portfolio.

Loomis does not make significant duration moves. Portfolio durations are adjusted gradually and are moderated by their normal bias for intermediate long term securities.

Ownership

Loomis, Sayles is a wholly owned, but autonomous subsidiary of New England Investment Companies, L.P. New England Investment Companies, L.P. is the parent to nine other investment firms. Assets are managed in ten regional offices around the country.

Loomis, Sayles (con't)

<u>Assets Under Management</u>	<u>3/31/96</u>
Total fixed income assets managed:	\$16.7 billion
Total fixed income assets managed in the core fixed income style:	\$3.5 billion
Total number of fixed income accounts managed for this style:	38

Three largest tax-exempt accounts managed in this style:	<u>Account Type</u>	<u>Market Value</u>
	Arkansas Public Employees	\$565 million
	Massachsettes Teachers	\$452 million
	Iowa Public Employees	\$289 million

BOND MANAGER FACT SHEET

Manager: *Nicholas-Applegate Capital Management*

Investment Approach

Nicholas-Applegate's investment philosophy emphasizes interest rate decisions, selection of the appropriate part(s) of the yield curve, shifts among sectors of the bond market and selection of individual issues. Nicholas-Applegate's objective in managing fixed income portfolios is to maximize total return over full market cycles consistent with client objectives and risk constraints.

Portfolio structure is controlled by "Return Duration," a numerical measure of the future change in the total return of a bond or portfolio of bonds for any change in the level of interest rates over any time period. A proprietary computerized management system, Portfolio Characterization, is used to optimize portfolio structure decisions for maturity, sectors, coupon and quality to maximize return/risk for a desired level of interest rate exposure, as measured by "Return Duration."

The "Return Duration" of fully discretionary portfolios is adjusted to reflect Nicholas-Applegate's interest rate outlook and is set relative to a bond index or market benchmark, typically the Lehman Aggregate index. A portfolio "Return duration" target greater than the benchmark "Return Duration" indicates an expectation of lower interest rates, while a forecast for rising interest rates would result in a portfolio "Return Duration" lower than the "Return Duration" of the index.

Selection of the appropriate part(s) of the yield curve on which to invest is influenced by the expected future shape of the curve. Nicholas-Applegate devotes considerable resources to analyzing expected changes in the shape of the yield curve and structuring portfolios that will benefit the most from these changes.

Sector selection is a critical aspect in the management of fixed income portfolios. Sector selection will generally have a greater impact on total return in a period of flat or moderately changing interest rates than during periods of significant changes in rates when price changes are the dominant influence on performance results.

Nicholas-Applegate's investment approach has a very high-quality orientation. Securities utilized include Treasury issues, agencies, mortgage pass-throughs, collateralized mortgage obligations (CMOs), investment grade corporate bonds, other asset-backed securities and cash equivalents. maturities will range from cash equivalents to thirty years.

Nicholas-Applegate (con't)

Ownership

Organized as a partnership, the general partner of Nicholas-Applegate is Nicholas-Applegate Capital Management Holdings, L.P. The firm is approximately 97 percent-owned by active employees.

Assets Under Management

12/31/95

Total fixed income assets managed: \$12.0 billion

Total fixed income assets managed
in the core fixed income style: \$9.0 billion

Total number of fixed income
accounts managed for this style: 77

Three largest tax-exempt accounts
managed in this style:

Account Type

Market Value

Illinois Municipal
Retirement Fund

\$874 million

Mississippi Public Employee
Retirement Fund

\$805 million

Nevada Public Employees
Retirement Fund

\$803 million

BOND MANAGER FACT SHEET

Manager: *Pacific Investment Management Company*

Investment Approach

Pacific Investment Management Company (PIMCO) fixed income philosophy includes three key principles: 1. Portfolio strategy is driven by long term trends; 2. PIMCO avoids extreme swings in duration; 3. PIMCO adds value through sector, coupon and quality selection. PIMCO also uses futures and options extensively.

PIMCO emphasizes long term trends (three to five years) recognizing that demographics, political factors, and structural changes in the domestic and international economy exert sustained influences on interest rates. Thus, PIMCO annually updates their interest rate outlook and determines their duration range for the portfolio. The duration is never extreme and normally ranges between three and six years.

PIMCO uses all sectors of the bond market including hedged foreign bonds. They make significant sector shifts depending on changes in relative valuations and spreads. PIMCO's internally developed software assists in sector and individual security analysis.

PIMCO's average portfolio quality varies from A to Aaa depending on their outlook for rates and quality spreads. PIMCO performs thorough credit analysis on all holdings, enabling them to distinguish more accurately between levels of quality published by the outside rating services.

Ownership

PIMCO is wholly-owned by publicly traded PIMCO Advisors L.P., who in turn is owned 18% by the public; 38% by senior management; and 43% by Pacific Mutual. In addition to actual equity, senior professionals enjoy significant additional phantom equity. Forty five percent of PIMCO's profits get kept at the subsidiary level for distribution amongst key professionals.

Pacific Investment Management (con't)

<u>Assets Under Management</u>	<u>3/31/96</u>
Total fixed income assets managed:	\$69.2 billion
Total fixed income assets managed in the core fixed income style:	\$46.0 billion
Total number of fixed income accounts managed for this style:	177

Three largest tax-exempt accounts managed in this style:	<u>Account Type</u>	<u>Market Value</u>
	Public Plan	\$1.8 billion
	Public Plan	\$1.1 billion
	Public Plan	\$.9 billion

BOND MANAGER FACT SHEET

Manager: *T. Rowe Price*

Investment Approach

T. Rowe first develops an overall economic and business cycle outlook. From this, they identify several broad investment themes that may unfold. They meet three times a week to discuss these topics and develop a portfolio strategy from their outlook. Meeting participants are members of the economics, research, portfolio management and trading teams. T. Rowe's market view is continuously modified with changing market and economic conditions.

Once the portfolio strategy has been established, T. Rowe then evaluates the benchmark in two different ways. First, they define the duration, yield, credit quality, option adjusted spread, and convexity of the index. Next, they break the index down into its components and analyze each subsector. T. Rowe needs to analyze and understand each component and subsector of the index because they build a portfolio employing a sampling portfolio construction technique using several hundred bonds to replicate an index containing up to five thousand bonds.

T. Rowe's quantitative fixed income strategy adds value through credit analysis, mortgage security analysis, sector rotation, yield curve positioning and duration shading.

T. Rowe feels corporate credit analysis and proprietary research are critical elements of their investment process. Credit research is important because their portfolios are constructed using a sampling technique where individual security selection adds value to the portfolio. T. Rowe's portfolio managers utilize a dedicated fixed income credit team of 19 professionals and also have access to T. Rowe's 31 equity industry analysts.

T. Rowe analyzes mortgage securities on both a macro and micro level. On a macro level, they choose securities based on demographic and geographic trends in combination with their long term interest rate outlook. On a micro, pool specific basis, they look at seasoning and prepayment trends to determine relative value.

T. Rowe analyzes spreads in each sector and overweights undervalued sectors and underweights overvalued sectors relative to their benchmark weights. T. Rowe also makes slight yield curve and duration decisions depending on the economic forecast.

T. Rowe Price (con't)

Ownership

T. Rowe Price is a publicly traded company. Currently, approximately 25% of all shares outstanding are owned by active employees. Employees also participate in a significant stock option program representing another 15%.

<u>Assets Under Management</u>	<u>3/31/96</u>
Total fixed income assets managed:	\$5.6 billion
Total fixed income assets managed in the core fixed income style:	\$3.0 billion
Total number of fixed income accounts managed for this style:	14

Three largest tax-exempt accounts managed in this style:	<u>Account Type</u>	<u>Market Value</u>
	New York City Retirement Systems	\$1.5 billion
	State of Alaska	\$750 million
	Entergy	\$280 million

BOND MANAGER FACT SHEET

Manager: *Washington Square Advisers, Inc.*

Investment Approach

Washington Square Advisers, Inc. (WSA) believes that fixed-income corporate and mortgage-backed securities offer attractive value relative to Treasury securities over an economic cycle, and that credit and options risk analysis provides greater value than interest rate forecasting.

WSA's fixed-income investment approach is yield oriented and relies on thorough analysis of credit and options risk. WSA seeks out relative value within the fixed-income markets. WSA favors intermediate durations and annual portfolio turnover rates average 20-30%. The approach capitalizes on the full power of coupon compounding by remaining fully invested most of the time.

A typical WSA portfolio will consist of approximately 40-60 issues. Portfolio duration will be maintained very close to the duration of its benchmark -- a deviation of more than 10% either side of the benchmark duration would be unusual. Although intermediate maturities are favored, WSA does not normally make major yield curve bets, preferring to get duration exposure along the yield curve roughly equivalent to that of the benchmark. Consistent with the firm's philosophy and relative value approach, corporate bonds and mortgage-backed securities constitute the majority of its clients' holdings. U.S. Treasury and government agency holdings typically average 3-5% of the portfolio and would not usually exceed 10% of portfolio holdings.

Ownership

WSA is an independent subsidiary of ReliaStar Financial Corp. WSA's investment professionals have a 20% effective equity participation in the firm.

Washington Square Advisers (con't)

<u>Assets Under Management</u>	<u>12/31/95</u>
Total fixed income assets managed:	\$2.6 billion
Total fixed income assets managed in the core fixed income style:	\$2.5 billion
Total number of fixed income accounts managed for this style:	16

Three largest tax-exempt accounts managed in this style:	<u>Account Type</u>	<u>Market Value</u>
	ReliaStar Financial Pension Fund	\$60 million
	John A. Hartford Foundation	\$52 million
	Minneapolis Employees' Retirement System	\$46 million

**Benchmark Analysis
Summary Grid**

	Alliance	Brinson	Forstmann	Franklin	GeoCapital
Coverage	Meets Standard	Exceeds Standard	Exceeds Standard	Exceeds Standard	Meets Standard
Active Positions	Meets Standard	Exceeds Standard	Exceeds Standard	Exceeds Standard	Meets Standard
Turnover	Meets Standard	Exceeds Standard	Needs Improvement	Meets Standard	Needs Improvement
Active Risk	Exceeds Standard	Meets Standard	Exceeds Standard	Exceeds Standard	Exceeds Standard
Correlation Anal.					
EXM/MFT	Meets Standard	Meets Standard	Meets Standard	Exceeds Standard	Exceeds Standard
MFT/VAM	Exceeds Standard	Exceeds Standard	Exceeds Standard	Exceeds Standard	Meets Standard
Relative Style Plot	Meets Standard	Exceeds Standard	Meets Standard	Exceeds Standard	Meets Standard

Overall Assessment of Benchmark Quality:

Alliance: Satisfactory

Brinson: Satisfactory.

Forstmann: Satisfactory, but must address the high level of turnover.

Franklin: Satisfactory.

GeoCapital: Satisfactory, but must address the high level of turnover.

Summary Grid (con't)

	IAI	IDS	Independence	Jundt	Lincoln
Coverage	Meets Standard	Exceeds Standard	Exceeds Standard	Meets Standard	Exceeds Standard
Active Positions	Needs Improvement	Exceeds Standard	Meets Standard	Exceeds Standard	Meets Standard
Turnover	Exceeds Standard	Meets Standard	Exceeds Standard	Needs Improvement	Meets Standard
Active Risk	Exceeds Standard	Meets Standard	Meets Standard	Exceeds Standard	Meets Standard
Correlation Anal.					
EXM/MFT	Exceeds Standard	Meets Standard	Meets Standard	Exceeds Standard	Meets Standard
MFT/VAM	Meets Standard	Exceeds Standard	Exceeds Standard	Meets Standard	Meets Standard
Relative Style Plot	Meets Standard	Meets Standard	Meets Standard	Meets Standard	Meets Standard

Overall Assessment of Benchmark Quality:

IAI: Satisfactory. New benchmark in place on April 1, 1995.

IDS: Satisfactory.

Independence: Satisfactory.

Jundt: Satisfactory, but must address the high level of turnover.

Lincoln: Satisfactory.

Summary Grid (con't)

	Oppenheimer	Waddell	Weiss Peck
Coverage	Exceeds Standard	Meets Standard	Meets Standard
Active Positions	Exceeds Standard	Exceeds Standard	Exceeds Standard
Turnover	Exceeds Standard	Meets Standard	Needs Improvement
Active Risk	Meets Standard	Exceeds Standard	Exceeds Standard
Correlation Anal.			
EXM/MFT	Meets Standard	Exceeds Standard	Exceeds Standard
MFT/VAM	Meets Standard	Meets Standard	Exceeds Standard
Relative Style Plot	Meets Standard	Meets Standard	Meets Standard

Overall Assessment of Benchmark Quality:

Oppenheimer: Satisfactory.

Waddell: Satisfactory.

Weiss Peck: Satisfactory, but must address high level of turnover.

APPENDIX

Discussion of Terms

Benchmark coverage measures the percentage of securities held in the actual portfolio which also are contained in the benchmark portfolio. If a benchmark truly captures the securities on which the manager has an investment opinion, it will have a high coverage ratio. Coverage ratios vary according to the level of discipline exhibited in a manager's definition and implementation of the investment process. A valid benchmark should produce a coverage ratio of 80% or greater.

An **active position** is the difference between the actual portfolio weight of a security less the corresponding benchmark weight of the same security. A good benchmark will generate positive active positions with very rare exceptions. The weighting of each holding in the active portfolio should exceed the corresponding weights assigned to the same securities in the benchmark because if a manager finds a particular stock attractive, he will hold more than the benchmark position. Conversely, if a manager feels a security is unattractive, he will not hold the security at all.

Benchmark turnover measures the proportion of the benchmark's market value allocated to purchases and reinvestment of income during a periodic rebalancing. A valid and investable benchmark should experience reasonable levels of turnover. Semi-annual turnover in the 20 to 30% range is consistent with a passive investment in the benchmark.

Active Risk analysis is a useful measure in determining explanatory power of a customized benchmark. It is the variability (standard deviation) of the manager's active return (active portfolio return less benchmark return). Since a customized benchmark is constructed to capture a manager's investment style, a good benchmark should produce lower active risk than using a market index as the benchmark. This indicates that the benchmark more effectively screens out random noise associated with factors unrelated to a manager's investment style. To indicate the amount of return the manager generates relative to the risk they take, an information ratio (IR) can be calculated. An IR is calculated by dividing the Value of Active Management (VAM or active return) by the active risk. Holding everything else constant, the lower active risk resulting from a valid benchmark will produce a higher information ratio (IR) than a market index. In general, the higher the information ratio the shorter the time frame needed to determine whether the manager can or cannot add value at a statistically significant level.

Correlation analysis: The explanatory power of a manager's benchmark can also be evaluated by looking at the correlation between three residual return series: the manager's actual returns versus those of the market (EXM), the benchmark returns versus those of the market (MFT), and the actual portfolio returns versus those of the benchmark (VAM).

A good benchmark should exhibit significantly positive correlation between EXM and MFT because when the manager's benchmark, or investment style, performs well relative to the market, the actual portfolio should also do well relative to the market. A good benchmark will have an EXM/MFT correlation greater than 0.60.

If a manager's investment style is accurately reflected in the benchmark, the manager's ability to add value relative to the benchmark should not be affected by the performance of its investment style relative to the market. Therefore, the correlation between MFT and VAM should be essentially zero over time.

MINNESOTA STATE BOARD OF INVESTMENT

INVESTMENT GUIDELINES EXTERNAL EMERGING DOMESTIC COMMON STOCK MANAGERS

The investment actions of State Board of Investment (SBI) external active domestic common stock managers will be governed and evaluated by the following guidelines:

1. RETURN/RISK OBJECTIVES

The external common stock managers are expected to deliver cumulative returns that exceed a predetermined benchmark portfolio by at least 1.0 percentage point, net of fees, annually (see Benchmarks below). Over time, each manager will be expected to produce portfolios which differ from the manager's benchmark portfolio in the following manner:

- (a) The actual portfolio will realize active risk (annualized residual standard deviation), relative to the benchmark, in excess of one (1) percent.
- (b) The actual portfolio will generate positive cumulative excess returns significant enough to compensate the SBI for the active risk assumed. Generally, the ratio of annualized excess return to active risk in (a) above should be .50 or greater.

2. BENCHMARKS

Each manager must provide an initial published index benchmark agreed upon by both manager and SBI prior to the effective date of the contract, for purpose of performance evaluation and risk measurement. The published index must be representative of the manager's investment style.

Within 24 months of retention, each manager must provide benchmark (normal) portfolio, agreed upon by both manager and SBI, for the purpose of performance evaluation and risk measurement. The benchmark portfolio provided by the manager must satisfy the following characteristics:

- (a) **Unambiguous.** The names and weights of securities comprising the benchmark are clearly delineated.
- (b) **Investable.** The option is available to forego active management and simply hold the benchmark portfolio.
- (c) **Measurable.** It is possible to readily calculate the benchmark's return on a monthly basis.

- (d) **Appropriate.** The benchmark is consistent with the manager's investment style or biases.
- (e) **Reflective of current investment opinions.** The manager has current investment opinions (be they positive, negative, or neutral) on the securities which make up the benchmark.
- (f) **Specified in advance.** The benchmark must be available prior to the start of an evaluation period.

3. ELIGIBLE INVESTMENTS

The investment managers will be restricted to holding common and preferred stocks, convertible bonds, equity options, warrants, stock index futures and cash equivalents. The investments of each manager must satisfy the following criteria and constraints.

- (a) The stocks held must be issued by corporations organized under the laws of the U.S. or its states, the Dominion of Canada or its provinces and/or be listed on the New York Stock Exchange (NYSE) or American Stock Exchange. These include American Depositary Receipts (ADR's) traded on the NYSE and the ASE, but exclude ADR's traded over-the-counter.
- (b) Total SBI holdings in any one corporation shall not exceed five (5) percent of the total outstanding shares of that corporation. Individual investment manager holdings will be monitored by the SBI staff to assure compliance.
- (c) Cash equivalent reserves shall be invested in the SBI's STIF fund, managed by its custodian bank.
- (d) Individual manager holdings in convertible bonds shall not exceed five (5) percent of the total market value of the portfolio.
- (e) Investment Managers are not constrained regarding:
 - (1) transaction turnover
 - (2) use of covered call options as hedging devices
 - (3) liquidity requirements
 - (4) number of individual equity issues which must be held at any given time
 - (5) the percentage of assets held in cash reserves which must be held at any given time
 - (6) the use of stock index futures to adjust the effective equity exposure of the portfolio from 0 to 100%. In addition, all commodity futures transactions must be done on a fully collateralized basis.

4. PERFORMANCE EVALUATION

Manager performance will be evaluated according to the guidelines established in the SBI's Manager Continuation Policy. These guidelines assist the SBI in its decisions concerning retention and termination of investment managers.

Manager performance will be compared against an agreed upon published index until completion of a customized benchmark. Upon completion of an acceptable custom benchmark, return comparisons will be restated back to the date the investment manager's relationship began with the SBI.

5. COMMUNICATION

The SBI requires its investment managers to communicate with SBI staff on a regular basis. Managers are expected to meet with staff to review the results of the manager's investment decision-making process at least annually. In reviewing past and current investment strategies and performance, the manager is expected to present the analysis relative to the agreed upon benchmark. The SBI requires a quarterly written report containing information as requested by the SBI for each account under the investment management supervision of the manager.

6. PROXY VOTING

The SBI is responsible for proxy voting.

7. COMMODITY FUTURES TRADING

Any commodity futures trading agreement entered into by the Manager must provide that SBI liability for margin requirements, commissions and fees is limited solely to the total funds of the SBI manager and does not constitute a general obligation of the State of Minnesota. The total SBI liability for margin requirements, commissions and fees among all brokers for any individual SBI manager is limited to the total market value of the assets for that manager.

8. FUTURE MODIFICATIONS

The SBI reserves the right to modify these investment guidelines at any time. Managers will be notified in advance of changes to the investment guidelines.

Date: May 1996

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MINNESOTA STATE BOARD OF INVESTMENT
INVESTMENT GUIDELINES
EXTERNAL PASSIVE DOMESTIC COMMON STOCK MANAGER

The investment actions of State Board of Investment (SBI) external passive domestic common stock manager will be governed and evaluated by the following guidelines:

1. RETURN/RISK OBJECTIVES

The external passive common stock manager is expected to deliver cumulative returns that closely track the predetermined index provided to the Manager. The Manager is expected to achieve the following:

- (a) The actual portfolio will realize tracking error, relative to the benchmark, no greater than ± 60 basis points over any twelve month period.
- (b) Over a 3 to 5 year period, the return should be no more than negative 10 basis points relative to the predetermined benchmark due to fees, transaction costs, etc.

2. BENCHMARK INDEX

The initial benchmarks will be the Wilshire 5000 and a tilted index/customized benchmark furnished by a consultant retained by SBI. SBI reserves the right to change these benchmarks upon notification to manager.

3. ELIGIBLE INVESTMENTS

The investment manager will be restricted to holding common stocks, stock index futures, and cash equivalents. The investments must satisfy the following criteria and constraints.

- (a) The stocks held must be issued by corporations organized under the laws of the U.S. or its states and/or be listed on the New York Stock Exchange or American Stock Exchange.
- (b) Total SBI holdings in any one corporation shall not exceed five (5) percent of the total outstanding shares of that corporation. Individual investment manager holdings will be monitored by the SBI staff to assure compliance.
- (c) Cash equivalent reserves shall be invested in the SBI's STIF fund, managed by its custodian bank.

(d) Investment Managers are not constrained regarding:

- (1) transaction turnover
- (2) use of covered call options as hedging devices
- (3) liquidity requirements
- (4) number of individual equity issues which must be held at any given time
- (5) the percentage of assets held in cash reserves which must be held at any given time
- (6) the use of stock index futures to adjust the effective equity exposure of the portfolio from 0 to 100%. In addition, all commodity futures transactions must be done on a fully collateralized basis.

4. PERFORMANCE EVALUATION

Manager performance will be evaluated according to qualitative and quantitative guidelines established by SBI. These guidelines, which may change from time to time, assist the SBI in its decisions concerning retention and termination of this investment manager. The quantitative guideline will assess performance relative to the return/risk objectives in #1 above.

5. COMMUNICATION

The SBI requires its investment managers to communicate with SBI staff on a regular basis. Managers are expected to meet with staff to review the results of the manager's investment decision-making process at least annually. In reviewing past and current investment strategies and performance, the manager is expected to present the analysis relative to the benchmark portfolio. The SBI requires a quarterly written report containing information as requested by SBI for each Account under the investment management supervision of the Manager.

6. PROXY VOTING

The SBI is responsible for proxy voting.

7. COMMODITY FUTURES TRADING AGREEMENT

Any commodity futures trading agreement entered into by the Manager must provide that SBI liability for margin requirements, commissions and fees is limited solely to funds of the SBI and does not constitute a general obligation of the State of Minnesota. The total SBI liability for margin requirements, commissions and fees among all brokers for any individual SBI manager is limited to the total market value of the assets for that manager.

8. FUTURE MODIFICATIONS

The SBI reserves the right to modify these investment guidelines at any time. Managers will be notified in advance of changes to the investment guidelines.

Revised: May 1995

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**MINNESOTA STATE BOARD OF INVESTMENT
EXTERNAL ACTIVE FIXED INCOME MANAGER INVESTMENT GUIDELINES**

The investment actions of State Board of Investment (SBI) external active fixed income managers will be governed and evaluated using the following guidelines:

1. RISK/RETURN OBJECTIVES

A manager's portfolio is expected to differ from the benchmark in a way consistent with its investment philosophy. Staff will evaluate differences based on characteristics such as duration, sector weighting, industry weighting, and coupon and company selection.

A manager's portfolio is expected to deliver annualized returns of at least 25 basis points above the benchmark, over time, after fees. Excess returns should be commensurate with portfolio risk measured using annualized standard deviation.

2. BENCHMARKS

- A manager's benchmark is used to evaluate performance and measure risk.
- Managers who invest in all sectors of the investment grade bond universe are compared to the Lehman Brothers Aggregate Bond Index (Lehman Aggregate), or its appropriate subset in the case of a sector specialist.

These indices satisfy the following characteristics:

- a) *Unambiguous.* The securities comprising the benchmarks are clearly delineated.
- b) *Investable.* The option is available to forego active management and hold the benchmark portfolios.
- c) *Measurable.* It is possible to calculate each benchmark's return on a monthly basis.
- d) *Appropriate.* The benchmarks are consistent with the investment styles of the SBI's active managers.
- e) *Specified in Advance.* The benchmarks are established prior to the start of the evaluation period.

3. ELIGIBLE INVESTMENTS

The investment managers may hold fixed income instruments, fixed income options and futures, and cash equivalents. The investments of each manager must satisfy the following criteria and constraints:

- a) Government obligations of the U.S. or its agencies, Canada or its provinces, or obligations of other U.S. sponsored organizations must be payable in U.S. dollars and comply with the provisions of Minnesota Statutes 11A.24 subdivision 2.
- b) U.S. and Canadian corporate obligations must be payable in U.S. dollars, be rated among the top four quality categories by a nationally recognized rating agency, and comply with all provisions of Minnesota Statutes 11A.24 subdivision 3.
- c) Other obligations not specified in (a) or (b) must meet the provisions of Minnesota Statutes 11A.24 subdivision 4, clauses 1 through 5.
- d) Total portfolio duration must stay within a 3 to 7 year band.
- e) Cash equivalent reserves shall be invested in the SBI's STIF fund, managed by its custodian bank.
- f) Investments can be made in Yankee bonds. This market encompasses those foreign-domiciled issuers who register with the SEC and borrow U.S. dollars via issues underwritten by a U.S. syndicate for delivery in the United States and payable in U.S. dollars. The obligations must be rated among the top four quality categories by a nationally recognized rating agency.

Investment managers are not constrained regarding:

- 1) transaction turnover.
- 2) use of covered call options as hedging devices.
- 3) liquidity requirements.
- 4) number of fixed income issues held.
- 5) the percentage of assets held in cash reserves.
- 6) the use of bond index futures to adjust the effective fixed income exposure of the portfolio from 0 to 100%. In addition, all commodity futures transactions must be done on a fully collateralized basis.

4. PERFORMANCE EVALUATION

Manager performance is evaluated using the guidelines established in the SBI's Manager Continuation Policy. These guidelines help the SBI decide whether to continue or terminate investment managers.

5. COMMUNICATION

The SBI requires its investment managers to communicate with SBI staff on a regular basis. Managers are expected to meet with staff to review the results of the manager's investment decision-making process at least annually. In reviewing past and current investment strategies and performance, the manager is expected to present the analysis relative to the agreed upon benchmark. The SBI requires a quarterly written report containing information as requested by the SBI for each account under the investment management supervision of the manager.

6. COMMODITY FUTURES TRADING AGREEMENT

Any commodity futures or options trading agreement entered into by a manager must provide that SBI liability for margin requirements, commissions and fees is limited solely to funds of the SBI and does not constitute a general obligation for the State of Minnesota.

7. FUTURE MODIFICATIONS

The SBI reserves the right to modify these investment guidelines at any time to insure the managers, both individually and collectively, are in compliance with Minnesota statutes and SBI policy. Managers will be notified in advance of changes to these guidelines.

Revised: May 1995

Active Fixed Income Manager Guidelines
Possible Amendments to Section 3

The investment guidelines for an active fixed income manager may be amended to incorporate any or all of the following authorities. The additional authority is granted on a manager-by-manager basis according to the experience and expertise of the individual firm.

Amendment to Section 3 of External Active Fixed Income Manager Investment Guidelines:

In addition to the investments allowed under Section 3, the external active fixed income manager is authorized to:

- g) invest up to 10% of the portfolio in foreign fixed income securities. The Manager has discretion to hedge the currency exposure up to the 10% limit using currency forwards, futures or options. In addition, all currency transactions must be done on a fully collateralized basis.
- h) invest up to 10% of the portfolio in dollar denominated fixed income instruments rated BB or B by Standard and Poor's or an equivalent rating by another nationally recognized rating agency.
- i) invest up to 5% dollar denominated non-rated securities which, if rated by a nationally recognized rating agency, would have a rating of BBB or better.
- j) use the following market neutral strategies for the simultaneous purchase and sale of options and futures:
 - 1) Hedged volatility transactions
 - 2) Inter-market spreads
 - 3) Calendar spreads
 - 4) Box spreads

At no time shall the combined market exposure of all enhanced cash strategies in place exceed 100% of the current portfolio market value. In addition, all transactions must be done on a fully collateralized basis.

The manager may invest in puts and call options and future contracts traded on a contract market regulated by a governmental agency or by a financial institution regulated by a governmental agency. This allows the manager to invest in the following:

- 1) U.S. or foreign stock index futures
- 2) U.S. or foreign stock index options
- 3) U.S. or foreign options on stock index futures
- 4) U.S. or foreign forward exchange contracts
- 5) U.S. or foreign currency options
- 6) U.S. or foreign currency futures

Revised: May 1996

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MINNESOTA STATE BOARD OF INVESTMENT

INVESTMENT GUIDELINES EXTERNAL SEMI-PASSIVE FIXED INCOME MANAGERS

The investment actions of Minnesota State Board of Investment (SBI) external semi-passive fixed income managers will be governed and evaluated by the following guidelines:

1. RISK/RETURN OBJECTIVES

The SBI expects external semi-passive fixed income managers to develop and manage the index portfolio with characteristics similar to the Lehman Brothers Aggregate Bond Index (Lehman Aggregate). The specific manager risk tolerances are specified below in the section on investment parameters. These parameters should generate only moderate tracking errors from index performance and are consistent with an enhanced index strategy.

The management objective is to provide a return above the Lehman Aggregate index performance. The manager will be expected to generate minimum returns of 10 basis points above the Lehman Aggregate index return on an annualized basis.

2. ELIGIBLE INVESTMENTS

The investment managers may hold fixed income instruments, fixed income index options and futures, and cash equivalents. The investments of each manager must satisfy the following criteria and constraints:

- (a) Government obligations of the U.S., its agencies, Canada, its provinces, or U.S. sponsored organizations must be payable in U.S. dollars and comply with the provisions of SBI investment guidelines 11A.24 subdivision 2.
- (b) U.S. and Canadian corporate obligations must be payable in U.S. dollars, be rated among the top four quality categories by a nationally recognized rating agency, and comply with all provisions of 11A.24 subdivision 3.
- (c) Other obligations not specified in (a) or (b) must meet the provisions of 11A.24 subdivision 4.
- (d) Cash equivalent reserves shall be invested in the SBI's STIF fund, managed by its custodian bank.
- (e) Investments can be made in Yankee bonds. This market encompasses those foreign-domiciled issuers who register with the SEC and borrow U.S. dollars via

issues underwritten by a U.S. syndicate for delivery in the United States and payable in U.S. dollars. The obligations must be rated among the top four quality categories by a nationally recognized rating agency.

Investment managers are not constrained regarding:

- (1) transaction turnover
- (2) use of covered call options as hedging devices
- (3) liquidity requirement
- (4) number of fixed income issues which must be held at any given point in time
- (5) the use of bond index futures to adjust the effective fixed income exposure of the portfolio from 0 to 100%. In addition, all commodity futures transactions must be done on a fully collateralized basis.

3. INVESTMENT PARAMETERS

The investment parameters are based on contribution to duration. Contribution to duration is the sector percentage multiplied by the sector duration.

Sector Weighting Guidelines

Treasury/Agency Sector	$\pm 75\%$ of the Lehman Brothers Government sector contribution to duration
Mortgage Sector	$\pm 75\%$ of the Lehman Brothers Mortgage-Backed sector contribution to duration
Corporate Sector	$\pm 75\%$ of the Combined Lehman Brothers Corporate and Asset-Backed sectors contribution to duration
Issues Outside the Index*	Maximum 10% of the Lehman Brothers Aggregate contribution to duration

- * Issues collateralized by securities that are part of the index are not considered to be outside the index. For instance, CMO's collateralized by mortgages that are part of the index are not considered to be outside the index.

Corporate Credit Guidelines

AAA/AA $\pm 75\%$ of the combined Lehman Brothers Corporate AAA and AA contribution to duration

A/BBB $\pm 75\%$ of the combined Lehman Brothers Corporate A and BBB contribution to duration

Duration Guidelines

\pm 0.2 years of the Lehman Brothers Aggregate duration

4. PERFORMANCE EVALUATION

Manager performance is evaluated using the guidelines established in the SBI's Manager Continuation Policy. These guidelines help the SBI decide whether to continue or terminate investment managers.

5. COMMUNICATION

The SBI requires its investment managers to communicate with SBI staff on a regular basis. Managers are expected to meet with staff to review the results of the manager's investment decision-making process at least annually. In reviewing past and current investment strategies and performance, the manager is expected to present the analysis relative to the agreed upon benchmark. The SBI requires a quarterly written report containing information as requested by the SBI for each account under the investment management supervision of the manager.

6. COMMODITY FUTURES TRADING AGREEMENT

Any commodity futures or options trading agreement entered into by a manager must provide that SBI liability for margin requirements, commissions and fees is limited solely to funds of the SBI and does not constitute a general obligation for the State of Minnesota.

7. FUTURE MODIFICATIONS

The SBI reserves the right to modify these investment guidelines at any time to insure the managers, both individually and collectively, are in compliance with Minnesota statutes and SBI policy. Managers will be notified in advance of changes to these guidelines.

Revised: May 1996

**Semi-Passive Fixed Income Manager Guidelines
Possible Amendment to Section 3**

The investment guidelines for a semi-passive fixed income manager may be amended to incorporate the following investments. The authorities will be granted on a manager-by-manager basis according to the experience and expertise of the individual firm.

The guidelines of Minnesota State Board of Investment (SBI) external semi-passive fixed income managers shall incorporate the following modifications:

Amendment to Section 3 of External Semi-Passive Fixed Income Manager Investment Guidelines:

The investment parameter relating to Issues Outside of Index is modified as follows:

Issues Outside the Index*	Maximum 10% of the Lehman Brothers Aggregate contribution to duration.
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* Issues in this category may include:

- a) foreign bonds.
- b) dollar denominated fixed income securities rated BB or B by Standard and Poor's or an equivalent rating by another nationally recognized rating agency.

Revised: May 1996

MINNESOTA STATE BOARD OF INVESTMENT

INVESTMENT GUIDELINES EXTERNAL ACTIVE DOMESTIC COMMON STOCK MANAGERS

The investment actions of State Board of Investment (SBI) external active domestic common stock managers will be governed and evaluated by the following guidelines:

1. RETURN/RISK OBJECTIVES

The external common stock managers are expected to deliver cumulative returns in excess of a predetermined benchmark portfolio (see Benchmarks below). Over time, each manager will be expected to produce portfolios which differ from the manager's benchmark portfolio in the following manner:

- (a) The actual portfolio will realize active risk (annualized residual standard deviation), relative to the benchmark, in excess of one (1) percent.
- (b) The actual portfolio will generate positive cumulative excess returns significant enough to compensate the SBI for the active risk assumed. Generally, the ratio of annualized excess return to active risk in (a) above should be .50 or greater.

2. BENCHMARKS

Each manager must provide and maintain a customized benchmark (normal) portfolio, agreed upon by both manager and SBI, for the purpose of performance evaluation and risk measurement. The benchmark portfolio provided by the manager must satisfy the following characteristics:

- (a) **Unambiguous.** The names and weights of securities comprising the benchmark are clearly delineated.
- (b) **Investable.** The option is available to forego active management and simply hold the benchmark portfolio.
- (c) **Measurable.** It is possible to readily calculate the benchmark's return on a monthly basis.
- (d) **Appropriate.** The benchmark is consistent with the manager's investment style or biases.
- (e) **Reflective of current investment opinions.** The manager has current investment opinions (be they positive, negative, or neutral) on the securities which make up the benchmark.

- (f) **Specified in advance.** The benchmark must be available prior to the start of an evaluation period.

3. ELIGIBLE INVESTMENTS

The investment managers will be restricted to holding common stocks, preferred stocks, equity options, warrants, convertible bonds, stock index futures, ~~bonds~~, and cash equivalents. The investments of each manager must satisfy the following criteria and constraints.

- (a) The stocks held must be issued by corporations organized under the laws of the U.S. or its states, the Dominion of Canada or its provinces, and/or be listed on the New York Stock Exchange or American Stock Exchange.
- (b) Total SBI holdings in any one corporation shall not exceed five (5) percent of the total outstanding shares of that corporation. Individual investment manager holdings will be monitored by the SBI staff to assure compliance.
- (c) Cash equivalent reserves shall be invested in the SBI's STIF fund, managed by its custodian bank.
- (d) Individual Manager holdings in convertible bonds shall not exceed five (5) percent of the total market value of the portfolio.
- (e) Investment Managers are not constrained regarding:
 - (1) transaction turnover
 - (2) use of covered call options as hedging devices
 - (3) liquidity requirements
 - (4) number of individual equity issues which must be held at any given time
 - (5) the percentage of assets held in cash reserves which must be held at any given time
 - (6) the use of stock index futures to adjust the effective equity exposure of the portfolio from 0 to 100%. In addition, all commodity futures transactions must be done on a fully collateralized basis.

4. PERFORMANCE EVALUATION

Manager performance will be evaluated according to the guidelines established in the SBI's Manager Continuation Policy. These guidelines, which may change from time to time, assist the SBI in its decisions concerning retention and termination of investment managers.

5. COMMUNICATION

The SBI requires its investment managers to communicate with SBI staff on a regular basis. Managers are expected to meet with staff to review the results of the manager's investment decision-making process at least annually. In reviewing past and current investment strategies and performance, the manager is expected to present the analysis relative to the benchmark portfolio. The SBI requires a quarterly written report containing information as requested by the SBI for each account under the investment management supervision of the manager.

6. PROXY VOTING

The SBI is responsible for proxy voting.

7. COMMODITY FUTURES TRADING AGREEMENT

Any commodity futures trading agreement entered into by the Manager must provide that SBI liability for margin requirements, commissions and fees is limited solely to funds of the SBI and does not constitute a general obligation of the State of Minnesota. The total SBI liability for margin requirements, commissions and fees among all brokers for any individual SBI manager is limited to the total market value of the assets for that manager.

8. FUTURE MODIFICATIONS

The SBI reserves the right to modify these investment guidelines at any time. Managers will be notified in advance of changes to the investment guidelines.

Revised: May 1995

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MINNESOTA STATE BOARD OF INVESTMENT

INVESTMENT GUIDELINES EXTERNAL SEMI-PASSIVE DOMESTIC COMMON STOCK MANAGER

The investment actions of State Board of Investment (SBI) external semi-passive domestic common stock managers will be governed and evaluated by the following guidelines:

1. RETURN/RISK OBJECTIVES

The Manager is expected to deliver cumulative returns in excess of the predetermined benchmark provided to the Manager. The Manager is expected to achieve the following:

- (a) The actual portfolio will realize active risk (annualized residual standard deviation), relative to the benchmark, in excess of one (1) percent, but no more than one and one half (1.5) percent.
- (b) The actual portfolio will generate positive cumulative excess returns significant enough to compensate the SBI for the active risk assumed. Generally, the ratio of annualized excess return to active risk in (a) above should be 0.10 or greater.

2. BENCHMARK INDEX

The initial benchmark will be a tilted index/customized benchmark furnished by a consultant retained by SBI. SBI reserves the right to change the benchmark index upon notification to Manager.

3. ELIGIBLE INVESTMENTS

The Manager will be restricted to holding common stocks, preferred stocks, equity options, warrants, stock index futures, and cash equivalents. The investments must satisfy the following criteria and constraints.

- (a) The stocks held must be issued by corporations organized under the laws of the U.S. or its states and/or be listed on the New York Stock Exchange or American Stock Exchange.
- (b) Total SBI holdings in any one corporation shall not exceed five (5) percent of the total outstanding shares of that corporation. Individual Manager holdings will be monitored by the SBI staff to assure compliance.
- (c) Cash equivalent reserves shall be invested in the SBI's STIF fund, managed by its custodian bank.

(d) Manager is not constrained regarding:

- (1) transaction turnover
- (2) use of covered call options as hedging devices
- (3) liquidity requirements
- (4) number of individual equity issues which must be held at any given time
- (5) the percentage of assets held in cash reserves which must be held at any given time
- (6) the use of stock index futures to adjust the effective equity exposure of the portfolio from 0 to 100%. In addition, all commodity futures transactions must be done on a fully collateralized basis.

4. PERFORMANCE EVALUATION

Manager performance will be evaluated according to guidelines established in the SBI's Manager Continuation Policy. These guidelines, which may change from time to time, assist the SBI in its decisions concerning retention and termination of this investment manager.

5. COMMUNICATION

The SBI requires its investment managers to communicate with SBI staff on a regular basis. The Manager is expected to meet with staff to review the results of the Manager's investment decision-making process at least annually. In reviewing past and current investment strategies and performance, the Manager is expected to present the analysis relative to the benchmark portfolio. The SBI requires a quarterly written report containing information as requested by SBI for each Account under the investment management supervision of the Manager.

6. PROXY VOTING

The SBI is responsible for proxy voting.

7. COMMODITY FUTURES TRADING AGREEMENT

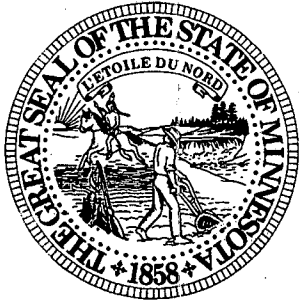
Any commodity futures trading agreement entered into by the Manager must provide that SBI liability for margin requirements, commissions and fees is limited solely to funds of the SBI and does not constitute a general obligation of the State of Minnesota. The total SBI liability for margin requirements, commissions and fees among all brokers for any individual SBI manager is limited to the total market value of the assets for that manager.

8. FUTURE MODIFICATIONS

The SBI reserves the right to modify these investment guidelines at any time. The Manager will be notified in advance of changes to the investment guidelines.

Revised: May 1995

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STATE BOARD OF INVESTMENT

Stock Manager Evaluation Reports

First Quarter, 1996

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DOMESTIC STOCK MANAGERS
Period Ending 3/31/96

Current Managers	Quarter		1 Year		3 years		5 Years		Since (1) Inception		Market Value (in millions)	Pool %
	Actual %	Bmk %	Actual %	Bmk %	Actual %	Bmk %	Actual %	Bmk %	Actual %	Bmk %		
Alliance	5.7	6.7	35.3	32.2	15.2	14.4	16.4	13.3	17.7	12.8	\$763.15	5.8%
Brinson	7.7	5.8	38.7	30.1					18.9	16.1	\$399.35	3.0%
Forstmann-Leff	11.6	7.2	33.6	30.7	14.6	14.6	13.1	14.1	13.5	12.8	\$420.12	3.2%
Franklin Portfolio	9.7	6.0	32.3	29.9	16.3	15.2	16.6	15.8	15.2	14.4	\$539.81	4.1%
GeoCapital	5.4	4.8	25.9	35.6	14.9	23.5	15.2	20.3	16.2	19.2	\$347.57	2.7%
IAI	4.2	5.1	29.6	29.2					16.8	17.3	\$159.98	1.2%
IDS	3.1	5.8	32.5	32.6	15.0	16.4	15.4	16.5	15.2	15.0	\$525.54	4.0%
Independence	5.0	5.8	32.3	32.7	15.0	15.6			15.2	15.3	\$527.08	4.0%
Jundt Associates	3.4	2.7	18.8	26.1					11.0	16.8	\$271.96	2.1%
Lincoln	6.8	5.3	37.2	31.5					19.6	17.7	\$396.00	3.0%
Oppenheimer	8.0	6.3	37.9	31.2					19.5	16.3	\$404.96	3.1%
Waddell & Reed	4.7	6.8	26.9	30.8	14.7	17.4	14.4	16.0	12.6	12.9	\$518.74	4.0%
Weiss Peck & Greer	8.9	4.3	43.3	32.5					15.9	17.9	\$302.69	2.3%
Emerging Managers (2)	7.0	5.3	29.6	33.1					20.2	22.6	\$390.77	3.0%
Semi-Passive (3)												
Franklin Portfolio	6.0	5.1	31.9	31.1					33.5	33.1	\$1,113.61	8.5%
JP Morgan	5.4	5.1	32.2	31.1					34.1	33.1	\$1,144.88	8.7%
BZW Barclays	5.2	5.1	34.9	31.1					36.2	33.1	\$1,143.63	8.7%
Passive												
BZW Barclays (4)	5.6	5.6							20.2	20.2	\$3,728.04	28.5%
									Since 1/1/84			
Current Aggregate	5.9	5.6	32.7	31.3	15.6	15.9	15.8	15.2	15.8	13.9	\$13,097.89	100.0%
Historical Aggregate (5)	5.9	5.6	31.7	31.4	14.6	15.4	14.6	15.0	14.2	14.5		
Wilshire Adjusted		5.6		32.2		15.3		14.9		14.5		
Wilshire 5000		5.6		32.2		15.4		15.0		14.8		

- (1) Since retention by the SBI. Time period varies for each manager.
(2) Aggregate of emerging manager group.
(3) Semi-passive managers retained 1/95. All use completeness fund benchmark.
(4) Passive manager retained 7/95 to manage a Wilshire 5000 index fund.
(5) Includes the performance of terminated managers.

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ALLIANCE CAPITAL MANAGEMENT
 Period Ending 3/31/96

Portfolio Manager: Jack Koltes

Assets Under Management: \$763,152,708

Investment Philosophy

Alliance searches for companies likely to experience high rates of earnings growth, on either a cyclical or secular basis. Alliance invests in a range of medium to large growth and cyclically sensitive companies. There is no clear distinction on the part of the firm as to an emphasis on one particular type of growth company over another. However, the firm's decision-making process appears to be much more oriented toward macroeconomic considerations than is the case with most other growth managers. Accordingly, cyclical earnings prospects, rather than secular, appear to play a larger role in terms of stock selection. Alliance is not an active market timer, rarely raising cash above minimal levels.

**Qualitative Evaluation
 (reported by exception)**

Exceptional strengths:

- Highly successful and experienced professionals.
- Organizational continuity and strong leadership.
- Well-acquainted with needs of large clients.
- Investment style consistently and successfully applied over a variety of market environments.

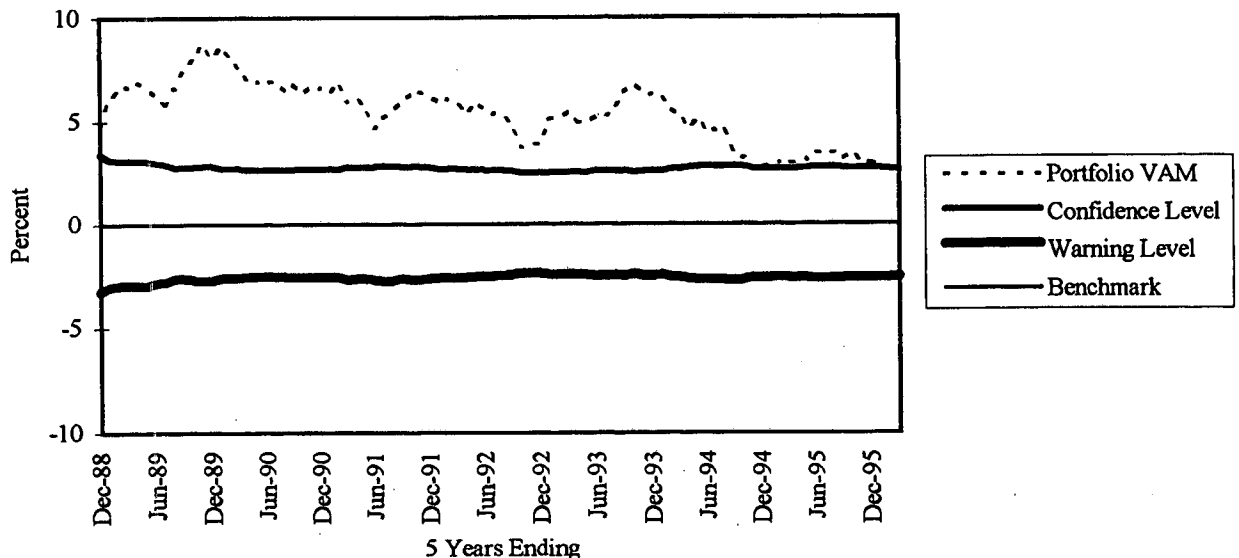
Quantitative Evaluation

	Actual	Benchmark
Last Quarter	5.7%	6.7%
Last 1 year	35.3	32.2
Last 2 years	22.5	22.4
Last 3 years	15.2	14.4
Last 4 years	15.9	13.6
Last 5 years	16.4	13.3
Since Inception (1/84)	17.7	12.8

Recommendation

No action recommended.

ALLIANCE CAPITAL MANAGEMENT
 Rolling Five Year Time Periods



BRINSON PARTNERS
Period Ending 3/31/96

Portfolio Manager: Jeff Diermeier

Assets Under Management: \$399,350,349

Investment Philosophy

Brinson Partners uses a relative value approach to equity investing. They believe that the market price will ultimately reflect the present value of the cash flows that the security will generate for the investor. They also believe both a macroeconomic theme approach and a bottom-up stock selection process can provide insight into finding opportunistic investments. Brinson uses their own discounted free cash flow model as their primary analytical tool for estimating the intrinsic value of a company.

**Qualitative Evaluation
 (reported by exception)**

Exceptional strengths:

- Familiar with the needs of large institutional clients.
- Highly successful and experienced professionals.
- Investment style consistently and successfully applied over a variety of market environments.

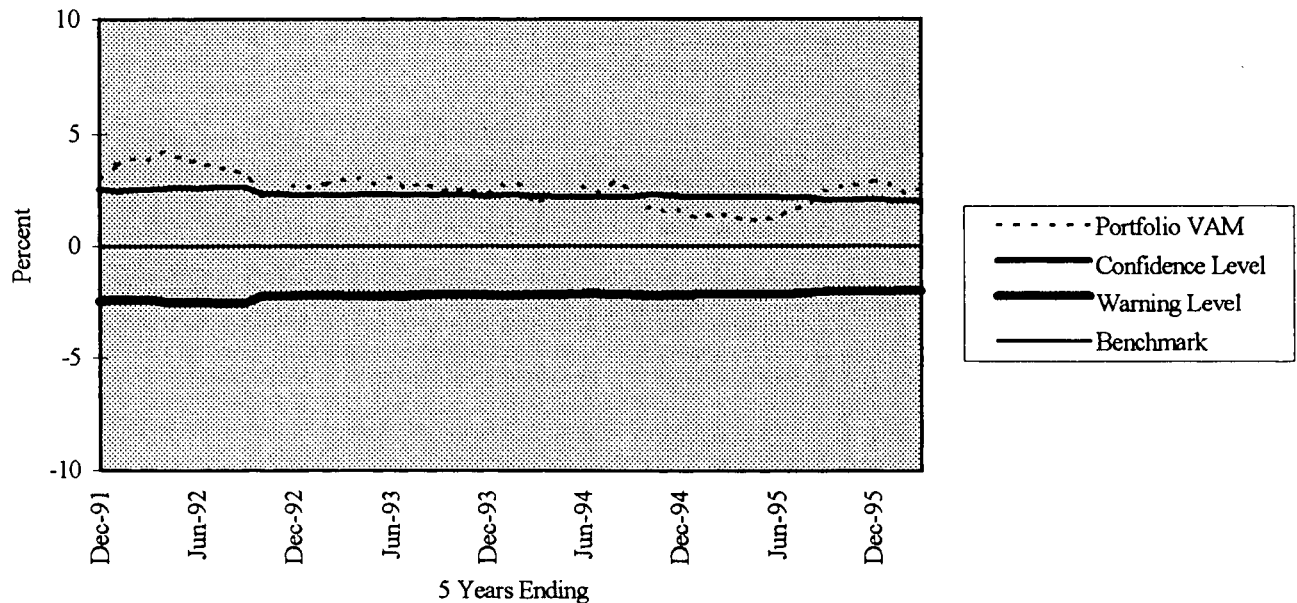
Quantitative Evaluation

	Actual	Benchmark
Last Quarter	7.7%	5.8%
Last 1 year	38.7	30.1
Last 2 years	26.0	21.4
Last 3 years	N.A.	N.A.
Last 4 years	N.A.	N.A.
Last 5 years	N.A.	N.A.
Since Inception (7/93)	18.9	16.1

Recommendation

No action recommended.

BRINSON PARTNERS
Rolling Five Year Time Periods



Note: Shaded area includes performance prior to managing the SBI account.
 Graph uses 80/20 confidence interval.

FORSTMANN LEFF ASSOCIATES
 Period Ending 3/31/96

Portfolio Manager: Joel Leff

Assets Under Management: \$420,121,309

Investment Philosophy

Forstmann Leff is a classic example of a "rotational" manager. The firm focuses almost exclusively on asset mix and sector weighting decisions. Based upon its macroeconomic outlook, the firm will move aggressively into and out of equity sectors over the course of a market cycle. The firm tends to purchase liquid, medium to large capitalization stocks. In the past, Forstmann Leff has made sizable market timing moves at any point during a market cycle.

**Qualitative Evaluation
 (reported by exception)**

Exceptional strengths:

- Highly successful and experienced leadership.
- Well acquainted with needs of large clients.

Concerns:

- Portfolio VAM appears to have diminished, over time.

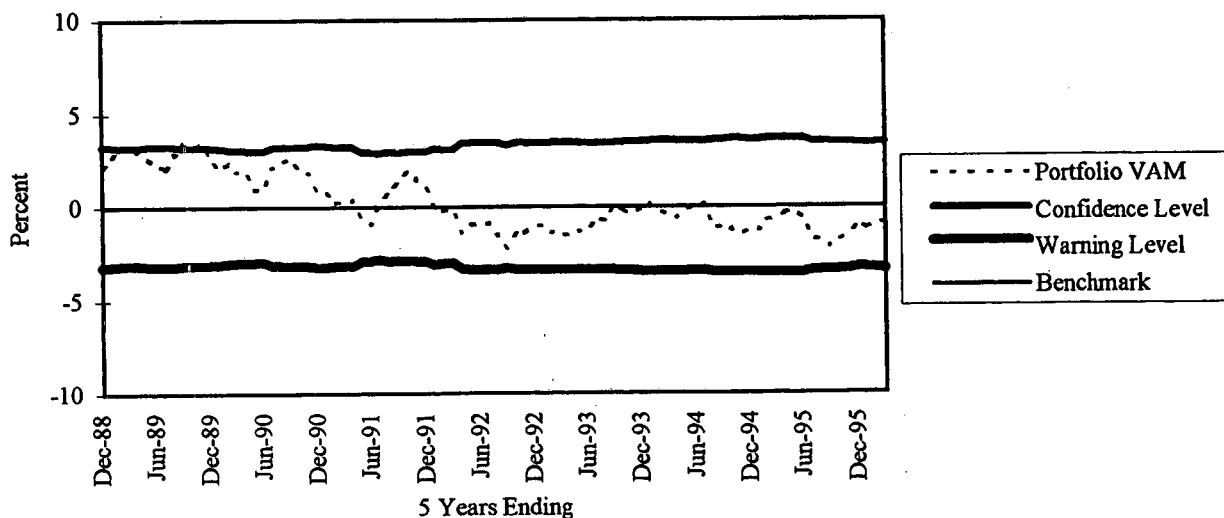
Quantitative Evaluation

	Actual	Benchmark
Last Quarter	11.6%	7.2%
Last 1 year	33.6	30.7
Last 2 years	19.3	21.5
Last 3 years	14.6	14.6
Last 4 years	12.7	14.2
Last 5 years	13.1	14.1
Since Inception (1/84)	13.5	12.8

Recommendation

No action recommended at this time. The firm was recommended for continuation after a formal re-interview in August of 1995. Staff continues to monitor the firm closely.

FORSTMANN-LEFF ASSOCIATES
 Rolling Five Year Time Periods



Note: Graph uses 80/20 confidence interval.

FRANKLIN PORTFOLIO ASSOCIATES

Period Ending 3/31/96

Portfolio Manager: John Nagorniak

Assets Under Management: \$539,807,887

Investment Philosophy

Franklin believes that rigorous and consistent application of fundamentally based valuation criteria will produce value added investment returns. Franklin builds a portfolio by using a series of more than 30 integrated computer models that value a universe of 3500 stocks. Their models rank each security based on fundamental momentum, relative value, future cash flow, and supplementary models, then a composite ranking provides one ranked list of securities reflecting their relative attractiveness. Stocks that fall below the median ranking are sold and proceeds reinvested in stocks from the top deciles in the ranking system. They use the BARRA E.2 risk model to monitor the portfolio's systematic risk and industry weightings relative to the selected benchmark to achieve a residual risk of 3.0% to 4.0 for the active portfolio.

Qualitative Evaluation (reported by exception)

Exceptional strengths:

- Familiar with the needs of large institutional clients.
- Firms investment approach has been consistently applied over a number of markets cycles.
- Highly successful and experienced professionals.
- Organizational continuity and strong leadership.

Quantitative Evaluation

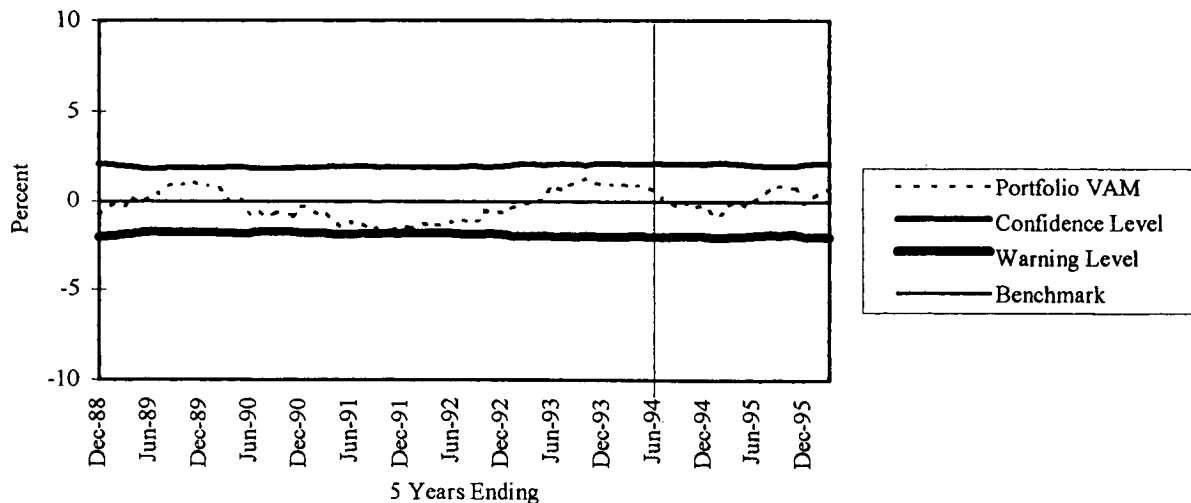
	Actual	Benchmark
Last Quarter	9.7%	6.0%
Last 1 year	32.3	29.9
Last 2 years	22.1	21.5
Last 3 years	16.3	15.2
Last 4 years	18.1	16.2
Last 5 years	16.6	15.8
Since Inception (4/89)	15.2	14.4

Recommendation

No action recommended.

FRANKLIN PORTFOLIO ASSOCIATES

Rolling Five Year Time Periods



Note: Area through 6/94 includes performance prior to managing SBI account. Graph uses 80/20 confidence interval. Area to the left of the vertical line includes performance prior to retention by the SBI.

GEOCAPITAL CORP.
Period Ending 3/31/96

Portfolio Manager: Barry Fingerhut

Assets Under Management: \$347,565,283

Investment Philosophy

GeoCapital invests primarily in small capitalization equities with the intent to hold them as they grow into medium and large capitalization companies. The firm uses a theme approach and an individual stock selection analysis to invest in the growth/technology and intrinsic value areas of the market. In the growth/technology area, GeoCapital looks for companies that will have above average growth due to a good product development and limited competition. In the intrinsic value area, the key factors in this analysis are corporate assets, free cash flow, and a catalyst that will cause a positive change in the company. The firm generally stays fully invested, with any cash positions due to the lack of attractive investment opportunities.

**Qualitative Evaluation
 (reported by exception)**

Exceptional strengths:

- Investment style consistently and successfully applied over a variety of market environments.
- Attractive, unique investment approach.
- Highly successful and experienced professionals.

Concerns:

- Performance pattern has been very volatile, over time.

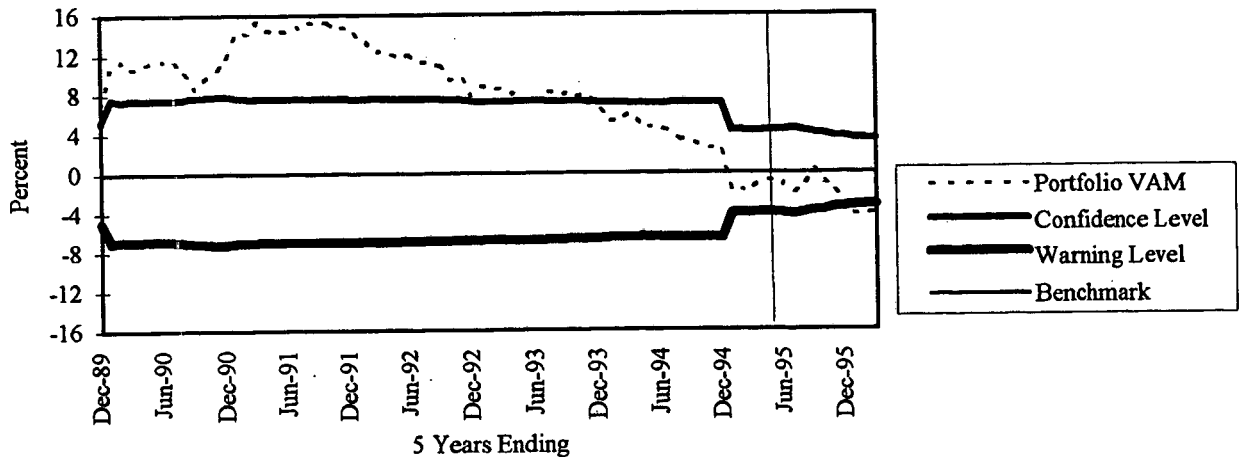
Quantitative Evaluation

	Actual	Benchmark
Last Quarter	5.4%	4.8%
Last 1 year	25.9	35.6
Last 2 years	15.9	27.9
Last 3 years	14.9	23.5
Last 4 years	12.2	20.5
Last 5 years	15.2	20.3
Since Inception (4/90)	16.2	19.2

Recommendation

No action recommended at this time. Staff continues to monitor the firm closely due to performance concerns.

GEOCAPITAL
Rolling Five Year Time Periods



Note: Area through 6/95 includes performance prior to managing SBI account. Scale differs from other manager VAM graphs. Graph uses 80/20 confidence interval. Area to the left of vertical line includes performance prior to retention by the SBI.

INVESTMENT ADVISERS INC.

Period Ending 3/31/96

Portfolio Manager: Mark Hoonsbeen

Assets Under Management: \$159,981,215

Investment Philosophy

IAI's investment philosophy is to own the highest quality companies which demonstrate sustainable growth. IAI tries to achieve this objective by investing at least 80% of the portfolio in companies which have their headquarters in Minnesota, Wisconsin, Illinois, Iowa, Nebraska, Montana, North Dakota and South Dakota. Twenty percent of the portfolio can be used to purchase large capitalization stocks that display the same quality and growth characteristics but have headquarters outside this region.

**Qualitative Evaluation
(reported by exception)**

Exceptional strengths:

- Attractive, unique investment approach.
- Investment style successfully applied over a number of market cycles.

Concerns:

- Previous portfolio manager retired on December 31, 1995.
- Portfolio VAM was below warning level for past 4 quarters. However, performance prior to April 1995 does not reflect recent revisions to the firm's benchmark.

Quantitative Evaluation

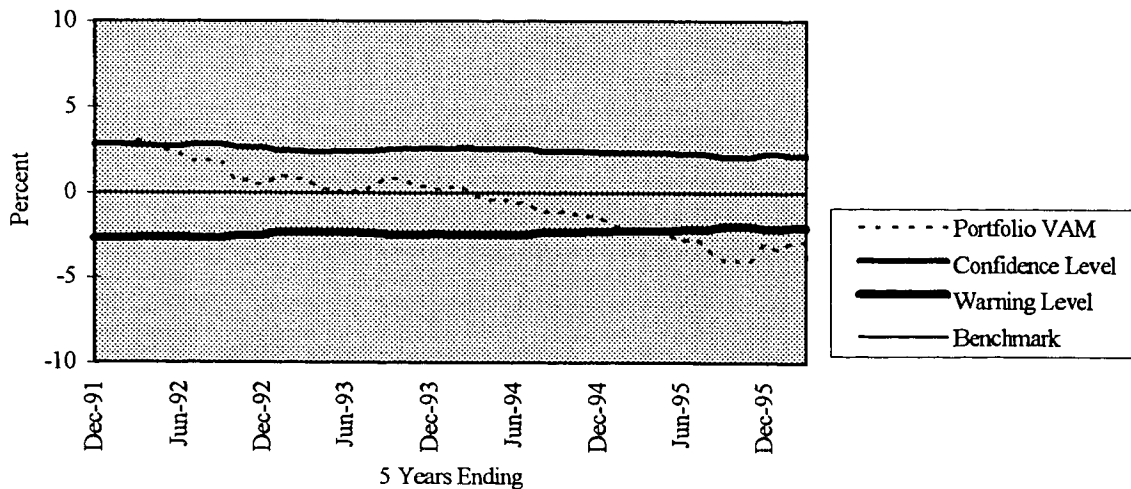
	Actual	Benchmark
Last Quarter	4.2%	5.1%
Last 1 year	29.6	29.2
Last 2 years	19.5	22.3
Last 3 years	N.A.	N.A.
Last 4 years	N.A.	N.A.
Last 5 years	N.A.	N.A.
Since Inception (7/93)	16.8	17.3

Recommendation

IAI was placed on probation at the March 1996 meeting. Staff will continue to monitor for any affects of the TSB/Lloyds Bank merger on IAI and the transition from Bing Carlin to Mark Hoonsbeen as the SBI portfolio manager. Staff will report back the end of next quarter, as required by the Manager Continuation Policy, with any recommendations.

INVESTMENT ADVISERS INC.

Rolling Five Year Time Periods



Note: Shaded area includes performance prior to managing the SBI account.
Graph uses 80/20 confidence interval.

IDS ADVISORY
Period Ending 3/31/96

Portfolio Manager: Pete Anderson

Assets Under Management: \$525,535,219

Investment Philosophy

IDS employs a "rotational" style of management, shifting among industry sectors based upon its outlook for the economy and the financial markets. The firm emphasizes primarily sector and industry weighting decisions. After the sector weightings have been determined IDS will select the best companies in those sectors based on fundamental analysis by their in-house analysts to reach the desired weightings. Moderate market timing is also used. Over a market cycle, IDS will invest in a wide range of industries. It tends to buy liquid, large capitalization stocks. While IDS will make occasional significant asset mix shifts over a market cycle, the firm is a less aggressive market timer than most rotational managers.

Qualitative Evaluation
(reported by exception)

Exceptional strengths:

- Investment style consistently and successfully applied over a variety of market environments.
- Familiar with the needs of large institutional clients.

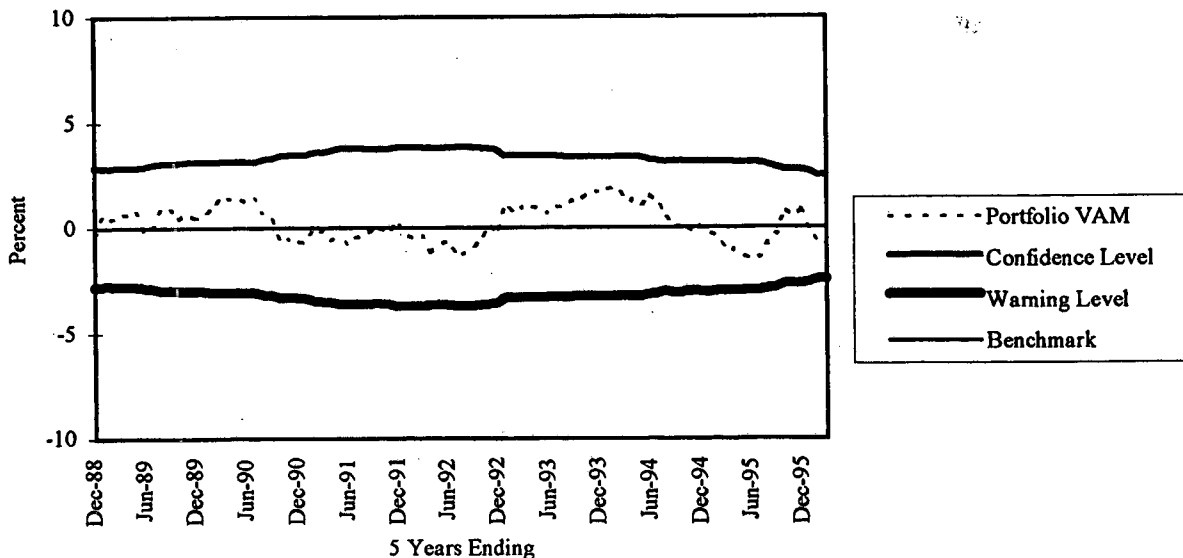
Quantitative Evaluation

	Actual	Benchmark
Last Quarter	3.1%	5.8%
Last 1 year	32.5	32.6
Last 2 years	20.8	23.4
Last 3 years	15.0	16.4
Last 4 years	15.7	16.9
Last 5 years	15.4	16.5
Since Inception (1/84)	15.2	15.0

Recommendation

No action recommended.

IDS ADVISORY
Rolling Five Year Time Periods



Note: Graph uses 80\20 confidence interval.

INDEPENDENCE INVESTMENT ASSOCIATES

Period Ending 3/31/96

Portfolio Manager: **Bill Fletcher**

Assets Under Management: **\$527,079,584**

Investment Philosophy

Independence believes that individual stocks which outperform the market always have two characteristics: they are intrinsically cheap and their business is in the process of improving. Independence ranks their universe using a multifactor model. Based on input primarily generated by their internal analysts, the model ranks each stock based on 10 discreet criteria. Independence constricts their portfolio to the top 60% of their ranked universe. The portfolio is optimized relative to the benchmark selected by the client to minimize the market and industry risks. Independence maintains a fully invested portfolio and rarely holds more than a 1% cash position.

Qualitative Evaluation (reported by exception)

Exceptional strengths:

- Attractive, unique investment approach.
- Highly successful and experienced professionals.
- Attractive, unique investment approach.

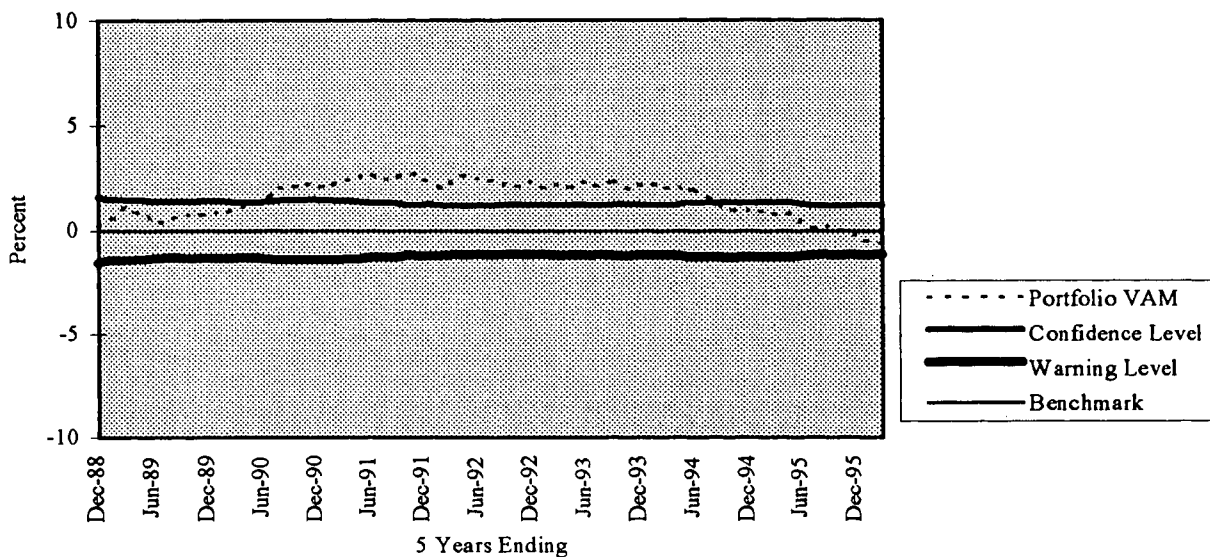
Quantitative Evaluation

	Actual	Benchmark	No action recommended.
Last Quarter	5.0%	5.8%	
Last 1 year	32.3	32.7	
Last 2 years	22.1	23.8	
Last 3 years	15.0	15.6	
Last 4 years	N.A.	N.A.	
Last 5 years	N.A.	N.A.	
Since Inception (2/92)	15.2	15.3	

Recommendation

INDEPENDENCE INVESTMENT ASSOCIATES

Rolling Five Year Time Periods



Note: Shaded area includes performance prior to managing SBI account.
Graph uses 80/20 confidence interval.

JUNDT ASSOCIATES
 Period Ending 3/31/96

Portfolio Manager: James Jundt

Assets Under Management: \$271,964,889

Investment Philosophy

Jundt Associates' investment philosophy is growth oriented with a focus on companies generating significant revenue increases. They concentrate on larger-capitalization companies, with at least half the equity securities consisting of companies with annual revenues over \$750 million. Within these parameters, the firm's mission is to establish equity positions in 30 to 50 of the fastest growing corporations in America. Particular emphasis is placed on companies the firm believes will achieve annual revenue growth of 15% or greater. Jundt utilizes a bottom-up stock selection process combined with a top-down theme overlay. The firm attempts to identify five to seven investment themes and typically invests three to five stocks in each theme.

Qualitative Evaluation
 (reported by exception)

Exceptional strengths:

- Attractive, unique investment approach.
- Investment style has been consistently applied over a number of market cycles.

Concerns:

- Significant underperformance since inception of the SBI account.
- Loss of several accounts over the last year.

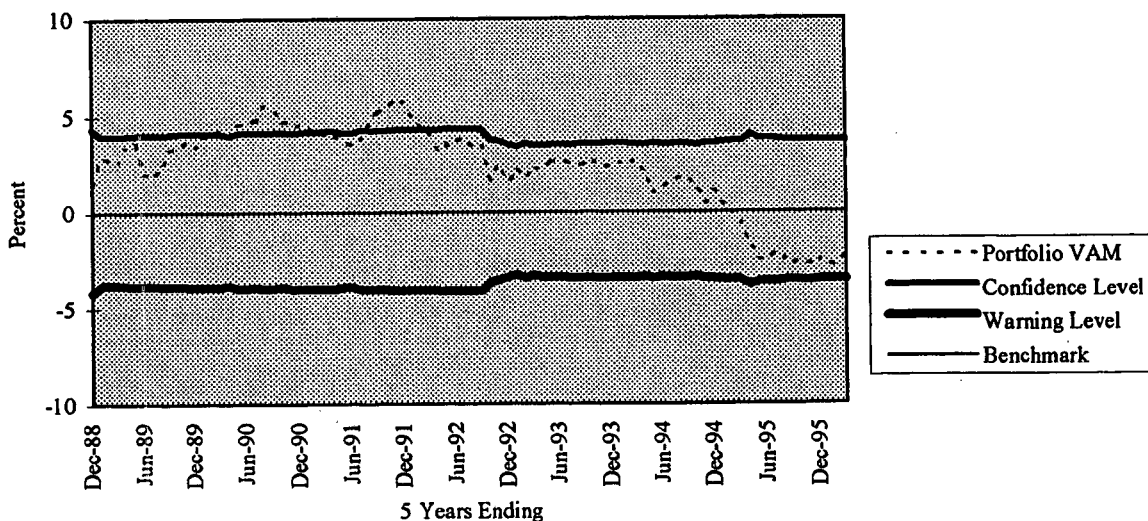
Quantitative Evaluation

	Actual	Benchmark
Last Quarter	3.4%	2.7%
Last 1 year	18.8	26.1
Last 2 years	14.0	21.1
Last 3 years	N.A.	N.A.
Last 4 years	N.A.	N.A.
Last 5 years	N.A.	N.A.
Since Inception (7/93)	11.0	16.8

Recommendation

Staff recommends that the SBI terminate its relationship with Jundt. Assets need to be withdrawn from the active manager program to fund asset allocation changes and total fund rebalancing. Given the concerns cited above, this portfolio is an appropriate funding source.

JUNDT ASSOCIATES
 Rolling Five Year Time Periods



Note: Shaded area includes performance prior to managing the SBI account.
 Graph uses 80/20 confidence interval.

LINCOLN CAPITAL MANAGEMENT
 Period Ending 3/31/96

Portfolio Manager: Parker Hall

Assets Under Management: \$395,997,594

Investment Philosophy

Lincoln Capital concentrates on established medium to large capitalization companies that have demonstrated historically strong growth and will continue to grow. The firm uses traditional fundamental company analysis and relative price/earnings valuation disciplines in its stock selection process. In addition, companies held by Lincoln generally exhibit premium price/book ratios, high return on equity, strong balance sheets and moderate earnings variability.

**Qualitative Evaluation
(reported by exception)**

Exceptional strengths are:

- Organizational continuity and strong leadership.
- Familiar with the needs of large clients.
- Investment style has been consistently applied over a number of market cycles.

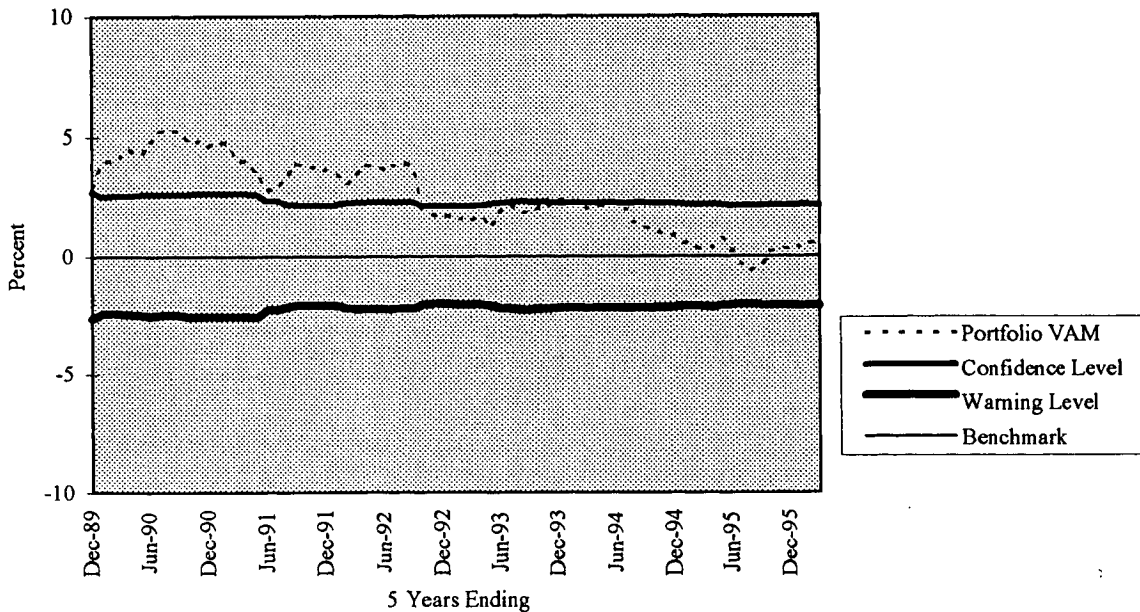
Quantitative Evaluation

	Actual	Benchmark
Last Quarter	6.8%	5.3%
Last 1 year	37.2	31.5
Last 2 years	27.4	24.6
Last 3 years	N.A.	N.A.
Last 4 years	N.A.	N.A.
Last 5 years	N.A.	N.A.
Since Inception (7/93)	19.6	17.7

Recommendation

No action recommended.

LINCOLN CAPITAL MANAGEMENT
 Rolling Five Year Time Periods



Note: Shaded area includes performance prior to managing the SBI account.
 Graph uses 80/20 confidence interval.

OPPENHEIMER CAPITAL
 Period Ending 3/31/96

Portfolio Manager: John Lindenthal

Assets Under Management: \$404,957,229

Investment Philosophy

Oppenheimer's objectives are to: 1) preserve capital in falling markets; 2) manage risk in order to achieve less volatility than the market; and 3) produce returns greater than the market indices, the inflation rate and a universe of comparable portfolios with similar objectives. The firm achieves its objectives by purchasing securities considered to be undervalued on the basis of known data and strict financial standards and by making timely changes in the asset mix. Based on its outlook on the market and the economy, Oppenheimer will make moderate shifts between cash and equities. Oppenheimer focuses on five key variables when evaluating companies: management, financial strength, profitability, industry position and valuation.

Qualitative Evaluation
 (reported by exception)

Exceptional strengths are:

- Highly successful and experienced professionals.
- Familiar with the needs of large institutional clients.
- Investment style has been consistently applied over a number of market cycles.

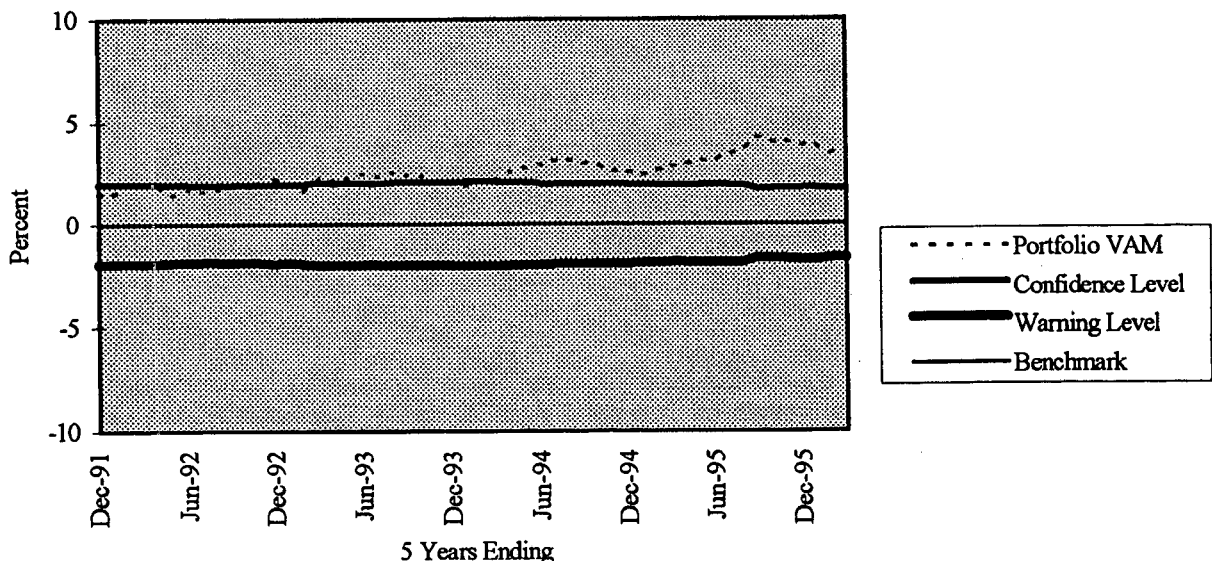
Quantitative Evaluation

	Actual	Benchmark
Last Quarter	8.0%	6.3%
Last 1 year	37.9	31.2
Last 2 years	26.4	22.2
Last 3 years	N.A.	N.A.
Last 4 years	N.A.	N.A.
Last 5 years	N.A.	N.A.
Since Inception (7/93)	19.5	16.3

Recommendation

No action recommended.

OPPENHEIMER CAPITAL
 Rolling Five Year Time Periods



Note: Shaded area includes performance prior to managing the SBI account.

Graph uses 80/20 confidence interval.

WADDELL & REED ASSET MANAGEMENT
 Period Ending 3/31/96

Portfolio Manager: Henry Herrmann

Assets Under Management: \$518,744,469

Investment Philosophy

Waddell & Reed focuses its attention primarily on smaller capitalization growth stocks. However, the firm has demonstrated a willingness to make significant bets against this investment approach for extended periods of time and has been very eclectic in its choice of stocks in recent years. The firm is an active market timer and will raise cash to extreme levels at various points in the market cycle.

**Qualitative Evaluation
 (reported by exception)**

Exceptional strengths are:

—Highly successful and experienced professionals.

Current concerns are:

—Significant organizational changes have occurred at the firm in the past year.

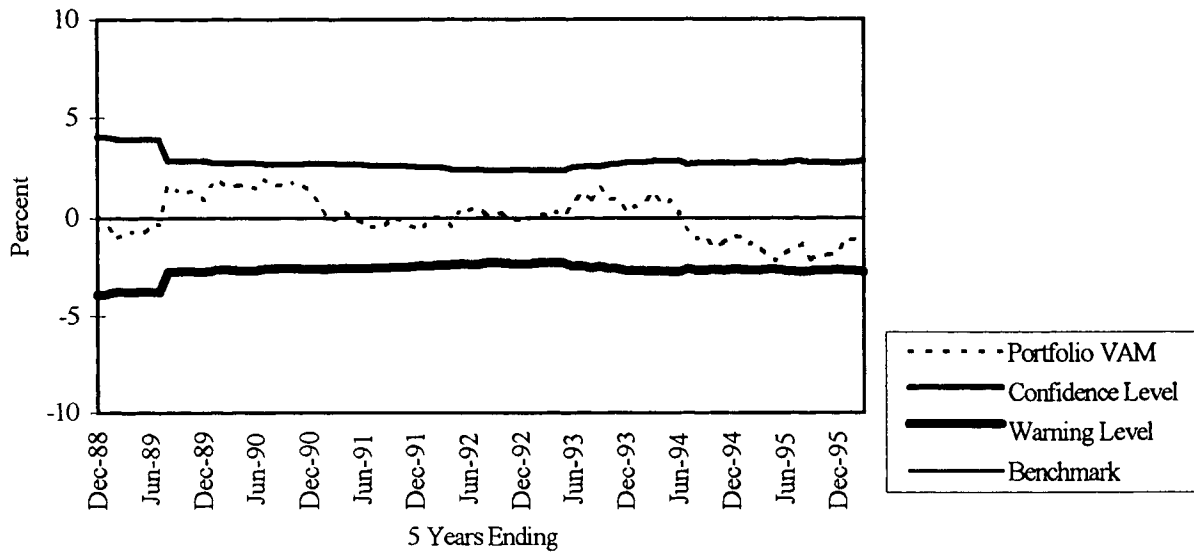
Quantitative Evaluation

	Actual	Benchmark
Last Quarter	4.7%	6.8%
Last 1 year	26.9	30.8
Last 2 years	15.3	20.4
Last 3 years	14.7	17.4
Last 4 years	14.3	16.2
Last 5 years	14.4	16.0
Since Inception (1/84) (1/84)	12.6	12.9

Recommendation

No action recommended at this time. The firm was recommended for continuation after a formal re-interview in August of 1995.

WADDELL & REED ASSET MANAGEMENT
 Rolling Five Year Time Periods



Note: Graph uses 80/20 confidence interval.

WEISS, PECK & GREER
 Period Ending 3/31/96

Portfolio Manager: Melville Straus

Assets Under Management: \$302,687,759

Investment Philosophy

Weiss, Peck & Greer's dynamic growth process concentrates on small to medium size growth companies that have demonstrated consistent superior earnings growth rates. The process emphasizes companies in new or dynamic, rapidly growing industries where there is a potential for a major acceleration in earnings growth. The firm also believes that superior stock selection can be achieved through in-depth fundamental company research.

Qualitative Evaluation
 (reported by exception)

Exceptional strengths are:

- Highly successful and experienced professionals.
- Investment style has been consistently applied over a number of market cycles.

Concerns:

- Performance pattern has been very volatile, over time.

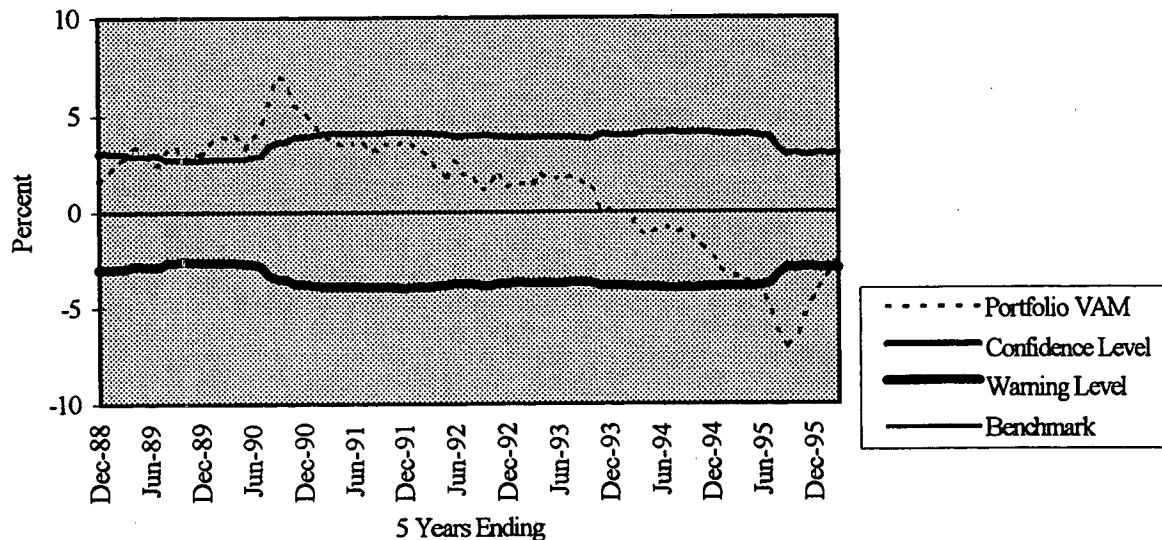
Quantitative Evaluation

	Actual	Benchmark
Last Quarter	8.9%	4.3%
Last 1 year	43.3	32.5
Last 2 years	21.2	21.6
Last 3 years	N.A.	N.A.
Last 4 years	N.A.	N.A.
Last 5 years	N.A.	N.A.
Since Inception (7/93)	15.9	17.9

Recommendation

No action recommended at this time. The firm was reviewed by the Domestic Manager Committee in August 1995 due to recent downturns in performance. Since that time, performance relative to the benchmark has been positive.

WEISS, PECK & GREER
 Rolling Five Year Periods



Note: Shaded area includes performance prior to managing the SBI account.
 Graph uses 80/20 confidence interval.

FRANKLIN PORTFOLIO ASSOCIATES

Period Ending 3/31/96

Portfolio Manager: John Nagorniak

Assets Under Management: \$1,113,614,385

**Investment Philosophy
Semi-Passive**

Franklin believes that rigorous and consistent application of fundamentally based valuation criteria will produce value added investment returns. Franklin builds a portfolio by using a series of more than 30 integrated computer models that value a universe of 3500 stocks. Their models rank each security based on fundamental momentum, relative value, future cash flow, and supplementary models, then a composite ranking provides one ranked list of securities reflecting their relative attractiveness. Stocks that fall below the median ranking are sold and proceeds reinvested in stocks from the top deciles in the ranking system. They use the BARRA E.2 risk model to monitor the portfolio's systematic risk and industry weightings relative to the selected benchmark. For this semi-passive mandate, they seek to achieve a residual risk of 1.5% or less. The firm remains fully invested at all times.

**Qualitative Evaluation
(reported by exception)**

Exceptional strengths are:

- Familiar with the needs of large institutional clients.
- Firm's investment approach has been consistently applied over a number of markets cycles.
- Highly successful and experienced professionals.
- Organizational continuity and strong leadership.

Quantitative Evaluation

	Actual	Benchmark*
Last Quarter	6.0%	5.1%
Last 1 year	31.9	31.1
Last 2 years	N.A.	N.A.
Last 3 years	N.A.	N.A.
Last 4 years	N.A.	N.A.
Last 5 years	N.A.	N.A.
Since Inception (1/95)	33.5	33.1

Recommendation

No action recommended.

* Completeness Fund

VAM graph will be created for period ending 12/31/96.

BZW BARCLAYS GLOBAL INVESTORS
Period Ending 3/31/96

Portfolio Manager: Nancy Feldkircher

Assets Under Management: \$1,143,631,257

Investment Philosophy
Semi-Passive

The Core Alpha Model desegregates individual equity returns for each of the 3500 stocks in their universe into three components (fundamental, expectation, and technical). The fundamental factors look at measures of underlying company value including earnings, book value, cash flow, and sales. These factors help identify securities that trade at prices below their true economic value. The expectational factors incorporate future earnings and growth rate forecasts made by over 2500 security analysts. The technical factors provide a measure of recent changes in company fundamentals, consensus expectations, and performance. An alpha is then calculated. The estimated alphas are used in a portfolio optimization algorithm to identify the optimal portfolio.

Qualitative Evaluation
(reported by exception)

Exceptional strengths are:

- Familiar with the needs of large institutional clients.
- Highly successful and experienced professionals.
- Attractive, unique investment approach.

Quantitative Evaluation

	Actual	Benchmark*
Last Quarter	5.2%	5.1%
Last 1 year	34.9	31.1
Last 2 years	N.A.	N.A.
Last 3 years	N.A.	N.A.
Last 4 years	N.A.	N.A.
Last 5 years	N.A.	N.A.
Since Inception (1/95)	36.2	33.1

Recommendation

No action recommended.

* Completeness Fund

VAM graph will be created for period ending 12/31/96.

J.P. MORGAN INVESTMENT MANAGEMENT, INC.
Period Ending 3/31/96

Portfolio Manager: Rick Nelson

Assets Under Management: \$1,144,882,785

Investment Philosophy
Semi-Passive

J.P. Morgan believes that superior stock selection is necessary to achieve excellent investment results. To accomplish this objective, they use fundamental research and a systematic valuation model. Analysts forecast the earnings and dividends for the 650 stock universe and enter these into a stock valuation model that calculates an expected return for each security. The stocks are ranked according to their expected return within their economic sector. Stocks most undervalued are placed in the first quintile. The portfolio includes stocks from the first four quintiles always favoring the highest ranked stocks whenever possible and sells those in the fifth quintile. In addition, the portfolio will closely approximate the sector, style, and security weightings of the index chosen by the plan sponsor. The firm remains fully invested at all times.

Qualitative Evaluation
(reported by exception)

Exceptional strengths are:

- Familiar with the needs of large institutional clients.
- Highly successful and experienced professionals.
- Organizational continuity and strong leadership.

Quantitative Evaluation

	Actual	Benchmark*
Last Quarter	5.4%	5.1%
Last 1 year	32.2	31.1
Last 2 years	N.A.	N.A.
Last 3 years	N.A.	N.A.
Last 4 years	N.A.	N.A.
Last 5 years	N.A.	N.A.
Since Inception (1/95)	34.1	33.1

Recommendation

No action recommended.

* Completeness Fund

VAM graph will be created for period ending 12/31/96.

BZW BARCLAYS GLOBAL INVESTORS
Period Ending 3/31/96

Portfolio Manager: Andrew R. Olma

Assets Under Management: \$3,728,041,073

Investment Philosophy
Passive

Wells Fargo's passively manages the portfolio against the Wilshire 5000 by minimizing tracking error and trading costs, and maximizing control over all investment and operational risks. Their strategy is to fully replicate the larger capitalization segments of the market and to use an optimization approach for the smaller capitalization segments. The optimizer weighs the cost of a trade against its contribution to expected tracking error to determine which trades should be executed.

Qualitative Evaluation
(reported by exception)

Exceptional strengths are:

- Familiar with the needs of large institutional clients.
- Highly successful and experienced professionals.

Quantitative Evaluation

	Actual	Benchmark
Last Quarter	5.6%	5.6%
Last 1 year	N.A.	N.A.
Last 2 years	N.A.	N.A.
Last 3 years	N.A.	N.A.
Last 4 years	N.A.	N.A.
Last 5 years	N.A.	N.A.
Since Inception (7/95)	20.2	20.2

Recommendation

No action required.

Tracking graph will be created for period ending 7/31/97.

GE INVESTMENT MANAGEMENT - Assigned Risk Plan
Period Ending 3/31/96

Portfolio Manager: Gene Bolton

Assets Under Management: \$137,198,576

Investment Philosophy
Assigned Risk Plan

GE Investment's Multi-Style Equity program attempts to outperform the S&P 500 consistently while controlling overall portfolio risk through a multiple manager approach. Five portfolio managers with different styles ranging from growth to value are supported by 10 industry analysts. The five portfolios are combined to create a well diversified equity portfolio while maintaining low relative volatility and a style-neutral position between growth and value. All GE managers focus on stock selection from a bottom-up prospective.

Qualitative Evaluation
(reported by exception)

Exceptional strengths are:

- Familiar with the needs of large institutional clients.
- Firms investment approach has been consistently applied over a number of markets cycles.
- Highly successful and experienced professionals.
- Organizational continuity and strong leadership.

Quantitative Evaluation

	Actual	Benchmark
Last Quarter	6.4%	5.5%
Last 1 year	32.2	32.3
Last 2 years	N.A.	N.A.
Last 3 years	N.A.	N.A.
Last 4 years	N.A.	N.A.
Last 5 years	N.A.	N.A.
Since Inception (1/95)	34.5	34.7

Recommendation

No action recommended.

VAM graph will be created for period ending 12/31/96.

INTERNAL STOCK POOL - Trust/Non-Retirement Assets
Period Ending 3/31/96

Portfolio Manager: Mike Menssen

Assets Under Management: \$64,874,267

Investment Philosophy
Environmental Trust Fund

The Internal Equity Pool is managed to closely track the S&P 500 Index. The strategy used replicates the S&P 500 by owning all of the names in the index at the weightings of the index. The optimization model's estimate of tracking error with this strategy is 4 to 6 basis points per year.

Qualitative Evaluation
(reported by exception)

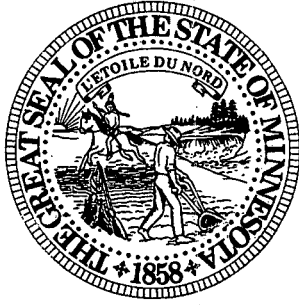
Quantitative Evaluation

Recommendation

	Actual	Benchmark	No action recommended.
Last Quarter	5.5%	5.5%	
Last 1 year	32.0	32.3	
Last 2 years	23.7	23.7	
Last 3 years	N.A.	N.A.	
Last 4 years	N.A.	N.A.	
Last 5 years	N.A.	N.A.	
Since Inception (7/93)	17.1	17.1	

Tracking graph will be created for period ending 6/30/98.

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STATE BOARD OF INVESTMENT

Emerging Stock Manager Evaluation Reports

First Quarter, 1996

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EMERGING EQUITY MANAGERS
Period Ending 3/31/96

Current Managers	Quarter		1 Year		3 years		5 Years		Since Inception		Market Value (in millions)	Pool %
	Actual Bmk %	Bmk %	Actual Bmk %	Bmk %	Actual Bmk %	Bmk %	Actual Bmk %	Bmk %	Actual Bmk %	Bmk %		
CIC Assets	7.4	6.8	34.7	31.9					22.4	23.2	\$44.91	11.5%
Cohen, Klingenstein, & Marks	8.6	6.5	32.7	30.3					24.7	21.0	46.62	11.9%
Compass Capital	7.5	8.1	27.4	29.1					22.8	20.7	45.21	11.6%
Kennedy Capital	9.5	7.2	32.8	29.2					17.1	15.6	41.11	10.5%
New Amsterdam	8.1	5.4	28.6	25.7					17.4	19.9	41.33	10.6%
Valenzuela Capital	7.4	6.8	27.5	28.7					18.6	19.8	42.23	10.8%
Wilke/Thompson	3.4	6.7	31.0	29.6					22.1	18.6	44.73	11.4%
Winslow Capital	6.0	6.4	23.0	29.0					18.9	20.6	42.37	10.8%
Zevenbergen Capital	5.8	5.3	29.3	27.0					18.7	20.1	42.26	10.8%
Current Aggregate	7.0	6.6 *	29.6	29.2 *					20.5	20.1 *		
Historical Aggregate	7.0	6.6 *	29.6	29.2 *					20.2	20.3 *	\$390.77	100.0%

Note:

Inception date for all managers is 4/1/94.

All benchmarks are customized since inception date.

* weighted average of above benchmarks

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CIC ASSET MANAGEMENT
Period Ending 3/31/96

Portfolio Manager: Jorge Castro

Assets Under Management: \$44,907,440

Investment Philosophy

CIC Asset Management (CIC) uses a disciplined relative value approach to managing equities. CIC believes that purchasing companies at attractive prices provides superior long-term performance with lower volatility. This investment process is designed for clients who desire equity market exposure with both incremental value added and downside protection due to reasonable dividend yields, moderate price to book values and low normalized price to earnings ratios. Finally, the process provides a synergy between quantitative valuation techniques and "Graham & Dodd" fundamental analyses.

Quantitative Evaluation

	Actual	Benchmark*
Last Quarter	7.4%	6.8%
Last 1 Year	34.7	31.9
Since Inception (4/94)	22.4	23.2

* Custom benchmark since inception date.

COHEN KLINGENSTEIN & MARKS INCORPORATED
Period Ending 3/31/96

Portfolio Manager: George Cohen

Assets Under Management: \$46,624,303

Investment Philosophy

Cohen Klingenstein & Marks Inc. (CKM) seeks to outperform the market by focusing on two variables: 1) economic cycles; and 2) security valuation. Within economic cycles, they believe that stocks exhibit predictable patterns that reflect changing expectations on corporate profits and interest rates. Similarly, they believe that stock prices normally reflect earnings expectations. CKM exploits short run inefficiencies through an unbiased process that relates the price of a stock to the consensus earnings expectations.

Quantitative Evaluation

	Actual	Benchmark*
Last Quarter	8.6%	6.5%
Last 1 Year	32.7	30.3
Since Inception (4/94)	24.7	21.0

* Custom benchmark since inception date.

COMPASS CAPITAL MANAGEMENT
Period Ending 3/31/96

Portfolio Manager: Charles Kelley

Assets Under Management: \$45,213,409

Investment Philosophy

Compass Capital Management (CCM) combines aspects of growth and value investing to achieve the proper blend of return (growth) and risk (value). They use a computer based data network to screen for large, well established companies whose earnings grow in spite of a weak economy and companies whose earnings have grown well over long time periods, but which may experience earnings pressure with downturns in the economy. Particular focus is given to growth in sales, earnings, dividends, book value and the underlying industry. Due to their "growing company" orientation, their portfolios generally hold no utility, bank, deep cyclical (auto companies for example), or oil and gas stocks.

Quantitative Evaluation

	Actual	Benchmark*
Last Quarter	7.5%	8.1%
Last 1 Year	27.4	29.1
Since Inception (4/94)	22.8	20.7

* Custom benchmark since inception date.

KENNEDY CAPITAL MANAGEMENT
Period Ending 3/31/96

Portfolio Manager: Richard Sinise

Assets Under Management: \$41,105,699

Investment Philosophy

Kennedy Capital Management (KCM) is dedicated to exploiting pricing inefficiencies in under-followed and misunderstood small capitalization stocks. They believe that stocks are efficiently priced where there is a proper distribution of information. However, many emerging growth companies suffer from lack of analytical coverage and information flow, and therefore, are "invisible" to institutional investors. KCM believes it is this lack of information which creates pricing inefficiencies. They anticipate that by closing this information gap they can transform these holdings into attractive institutional candidates. This, in turn, will increase the price of the stock.

Quantitative Evaluation

	Actual	Benchmark*
Last Quarter	9.5%	7.2%
Last 1 Year	32.8	29.2
Since Inception (4/94)	17.1	15.6

* Custom benchmark since inception date.

NEW AMSTERDAM PARTNERS
Period Ending 3/31/96

Portfolio Manager: Michelle Clayman

Assets Under Management: \$41,333,267

Investment Philosophy

New Amsterdam Partners believe that investment results are evaluated by actual return, and therefore, investment opportunities should be evaluated by expected return. They believe that all valid techniques depend on forecasts of the amounts and timing of future cash flows. Thus, the firm focuses on forecasted earnings growth, yield, price-to-book ratio, and forecasted return on equity. They believe that the disciplined application of their valuation techniques in conjunction with sound financial analysis of companies, is the key to understanding and maximizing investment returns.

Quantitative Evaluation

	Actual	Benchmark*
Last Quarter	8.1%	5.4%
Last 1 Year	28.6	25.7
Since Inception (4/94)	17.4	19.9

* Custom benchmark since inception date.

VALENZUELA CAPITAL MANAGEMENT
Period Ending 3/31/96

Portfolio Manager: Peter McCarthy

Assets Under Management: \$42,228,448

Investment Philosophy

Valenzuela Capital Management's (VCM) believes that stock selection and adherence to valuation analysis are the backbone of superior performance. Their investment philosophy is one of risk averse growth. VCM seeks companies undergoing strong rates of change in earnings, cash flow and returns. These companies are experiencing positive changes in revenues, gross and operating margins and financial structure. To be considered for investment, these stocks must sell at or below market valuations. VCM believe that below market valuations provide downside protection during weak market periods. In strong markets the portfolios will be driven by both earnings growth and multiple expansion.

Quantitative Evaluation

	Actual	Benchmark*
Last Quarter	7.4%	6.8%
Last 1 Year	27.5	28.7
Since Inception (4/94)	18.6	19.8

* Custom benchmark since inception date.

WILKE/THOMPSON CAPITAL MANAGEMENT INC.
Period Ending 3/31/96

Portfolio Manager: Mark Thompson

Assets Under Management: \$44,727,183

Investment Philosophy

The investment philosophy of Wilke/Thompson (W/T) is to invest in high quality growth companies that demonstrate the ability to sustain strong secular earnings growth, notwithstanding overall economic conditions. W/T's investment approach involves a bottom-up fundamental process. The stock selection process favors companies with strong earnings, high unit growth, a proprietary market niche, minimum debt, conservative accounting and strong management practices. They formulate investment ideas by networking with the corporate managers of their current and prospective holdings, as well as with regional brokers, venture capitalists, and other buy-side portfolio managers.

Quantitative Evaluation

	Actual	Benchmark*
Last Quarter	3.4%	6.7%
Last 1 Year	31.0	29.6
Since Inception (4/94)	22.1	18.6

* Custom benchmark since inception date.

WINSLOW CAPITAL MANAGEMENT
Period Ending 3/31/96

Portfolio Manager: Clark Winslow

Assets Under Management: \$42,374,594

Investment Philosophy

Winslow Capital Management (WCM) believes that investing in companies with above average earnings growth provide the best opportunities for superior portfolio returns over time. WCM believes that a high rate of earnings growth is often found in medium capitalization growth companies of \$1 to \$10 billion market capitalization. Thus, to seek superior portfolio returns while maintaining good liquidity, Winslow Capital emphasizes a growth strategy buying securities of both medium and large cap companies. The objective is to achieve a weighted average annual earnings growth rate of 15-20% over a 2-3 year time horizon.

Quantitative Evaluation

	Actual	Benchmark*
Last Quarter	6.0%	6.4%
Last 1 Year	23.0	29.0
Since Inception (4/94)	18.9	20.6

* Custom benchmark since inception date.

ZEVENBERGEN CAPITAL INC
Period Ending 3/31/96

Portfolio Manager: Nancy Zevenbergen

Assets Under Management: \$42,255,970

Investment Philosophy

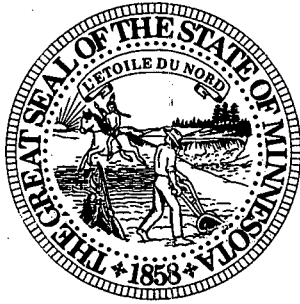
Zevenbergen is an equity growth manager. The investment philosophy is based on the belief that earnings drive stock prices while quality provides capital protection. Hence, portfolios are constructed with companies showing above-average earnings growth prospects and strong financial characteristics. They consider diversification for company size, expected growth rates and industry weightings to be important risk control factors. Zevenbergen uses a bottom-up fundamental approach to security analysis. Research efforts focus on finding companies with superior products or services showing consistent profitability. Attractive buy candidates are reviewed for sufficient liquidity and to potential diversification. The firm emphasizes that they are not market timers.

Quantitative Evaluation

	Actual	Benchmark*
Last Quarter	5.8%	5.3%
Last 1 Year	29.3	27.0
Since Inception (4/94)	18.7	20.1

* Custom benchmark since inception date.

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STATE BOARD OF INVESTMENT

Bond Manager Evaluation Reports

First Quarter, 1996

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BOND MANAGERS
Period Ending 3/31/96

	Quarter		1 Year		3 years		5 Years		Since (1) Inception		Market Value (in millions)	Pool %
	Actual	Bmk	Actual	Bmk	Actual	Bmk	Actual	Bmk	Actual	Bmk		
	%	%	%	%	%	%	%	%	%	%		
Current Managers												
BEA	-1.3	-1.8	10.7	10.8					5.6	5.6	\$324.11	4.8%
IAI	-2.0	-1.8	9.2	10.8	5.5	6.1	8.9	8.6	11.5	11.3	522.72	7.8%
IDS	-3.2	-1.8	11.5	11.5					5.8	5.7	278.36	4.1%
Miller	-1.0	-1.8	11.9	10.8	6.6	6.1	9.7	8.6	11.6	11.3	592.49	8.8%
Standish	-1.5	-1.8	11.1	10.8					5.2	5.6	528.61	7.9%
Western	-1.8	-1.8	12.2	10.8	7.3	6.1	9.9	8.7	12.5	11.3	1,007.04	15.0%
Semi-Passive												
Goldman	-1.6	-1.8	11.0	10.8					6.0	5.6	1,177.65	17.5%
Lincoln	-1.8	-1.8	10.6	10.8	6.1	6.1	8.7	8.6	9.3	9.3	1,160.37	17.2%
											\$6,726.76*	100.0% *
									Since 7/1/84			
Current Aggregate	-1.7	-1.8	11.1	10.8	6.4	6.1	9.1	8.6	11.8	11.3		
Historical Aggregate (2)	-1.7	-1.8	11.1	10.7	6.3	6.1	9.0	8.6	11.2	11.2		
Lehman Aggregate (3)		-1.8		10.8		6.1		8.6		10.7		

(1) Since retention by the SBI. Time period varies for each manager.

(2) Includes performance of terminated managers

(3) Prior to July 1994, this index reflects the Salomon BIG

* TCW and Fidelity portfolios are included in total figures and within the Historical Aggregate.

TCW's assets were liquidated during the quarter and subsequently transferred out of the bond program as part of an asset allocation transition. Fidelity's assets were transferred to a new semi-passive manager on April 1, 1996.

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BEA ASSOCIATES
Period Ending 3/31/96

Portfolio Manager: Bob Moore

Assets Under Management: \$324,107,885

Investment Philosophy

BEA's investment approach focuses on individual bond selection and on sector selection rather than short term interest rate forecasting. BEA keeps the duration close to the benchmark but may be slightly longer or shorter depending on their long-term economic outlook. BEA's approach is distinguished by 1) a quantitative approach which avoids market timing; 2) contrarian weightings of bond sectors; and 3) rigorous call and credit analysis rather than yield driven management.

**Qualitative Evaluation
 (reported by exception)**

Exceptional strengths are:

- Highly successful and experienced professionals.
- Extensive option analysis capabilities.

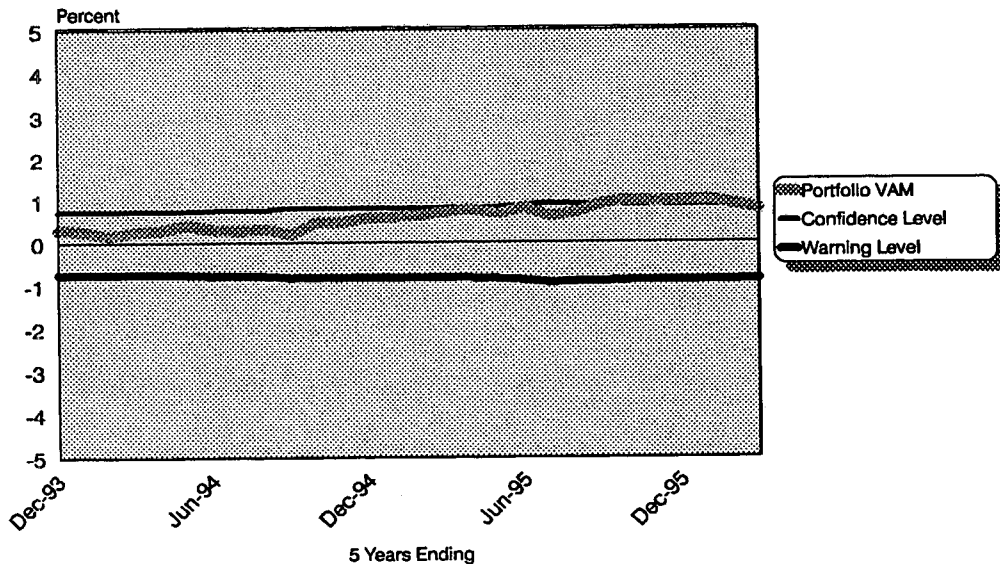
Quantitative Evaluation

	Actual	Benchmark
Last Quarter	-1.3%	-1.8%
Last 1 year	10.7	10.8
Last 2 years	7.7	7.9
Last 3 years	N/A	N/A
Last 4 years	N/A	N/A
Last 5 years	N/A	N/A
Since Inception (7/93)	5.6	5.6

Recommendations

No action recommended.

BEA ASSOCIATES
Rolling Five Year Time Periods



Notes: Shaded area includes performance prior to managing the SBI account. Graph uses 80/20 confidence interval.

INVESTMENT ADVISERS
Period Ending 3/31/96

Portfolio Manager: Larry Hill

Assets Under Management: \$522,715,426

Investment Philosophy

Investment Advisers is a traditional top down bond manager. The firm's approach is oriented toward correct identification of the economy's position in the credit cycle. This analysis leads the firm to its interest rate forecast and maturity decisions, from which the firm derives most of its value-added. Investment Advisers is an active asset allocator, willing to make rapid, significant moves between cash and long maturity investments over the course of an interest rate cycle. Quality and sector choices are made through yield spread analyses consistent with the interest rate forecasts. Individual security selection receives very limited emphasis and focuses largely on specific bond characteristics such as call provisions.

**Qualitative Evaluation
 (reported by exception)**

The current evaluation notes the following:

—The manager's duration decisions have added value over the long term. Recently, this strategy has not been as successful.

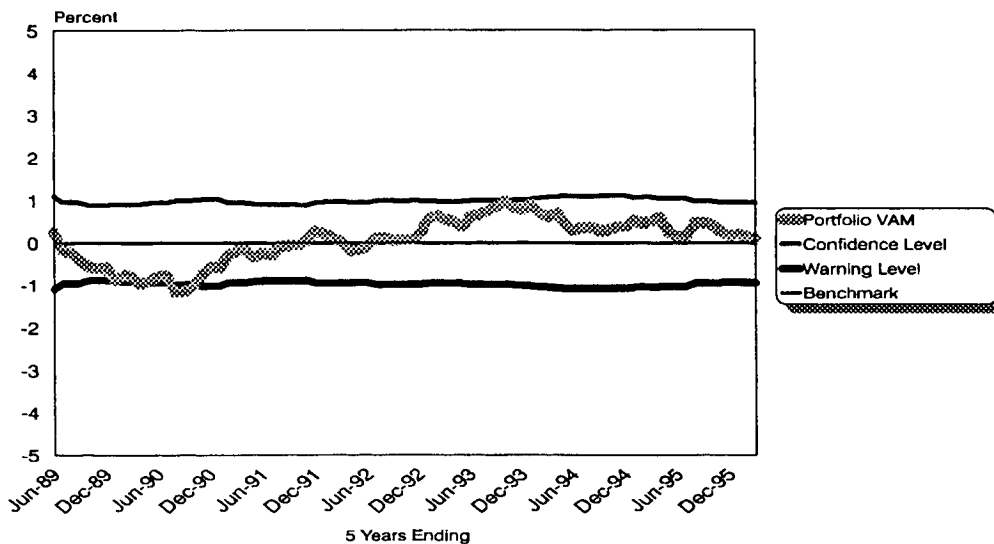
Quantitative Evaluation

	Actual	Benchmark
Last Quarter	-2.0%	-1.8%
Last 1 year	9.2	10.8
Last 2 years	6.7	7.9
Last 3 years	5.5	6.1
Last 4 years	8.2	7.9
Last 5 years	8.9	8.6
Since Inception (7/84)	11.5	11.3

Recommendations

No action recommended.

INVESTMENT ADVISERS
Rolling Five Year Time Periods



Note: Graph uses 80/20 confidence interval.

IDS ADVISORY GROUP
Period Ending 3/31/96

Portfolio Manager: Ed Labenski

Assets Under Management: \$278,362,939

Investment Philosophy

Until December 31, 1995, IDS managed a corporate and treasury portfolio for the SBI. Beginning January 1, 1996, IDS manages corporates, treasuries and mortgages. The firm uses duration management combined with in-depth fundamental analysis of the corporate sector to add value to the portfolio. Active duration management begins with an economic overview and interest rate outlook. These factors help IDS determine the direction of both short and long-term interest rates which leads to the portfolio duration decisions. After IDS determines duration, they use their extensive corporate research capabilities to determine corporate sector allocation and to select individual issues.

**Qualitative Evaluation
 (reported by exception)**

Exceptional strengths are:

- Highly successful and experienced professionals.
- Extensive corporate research capabilities.

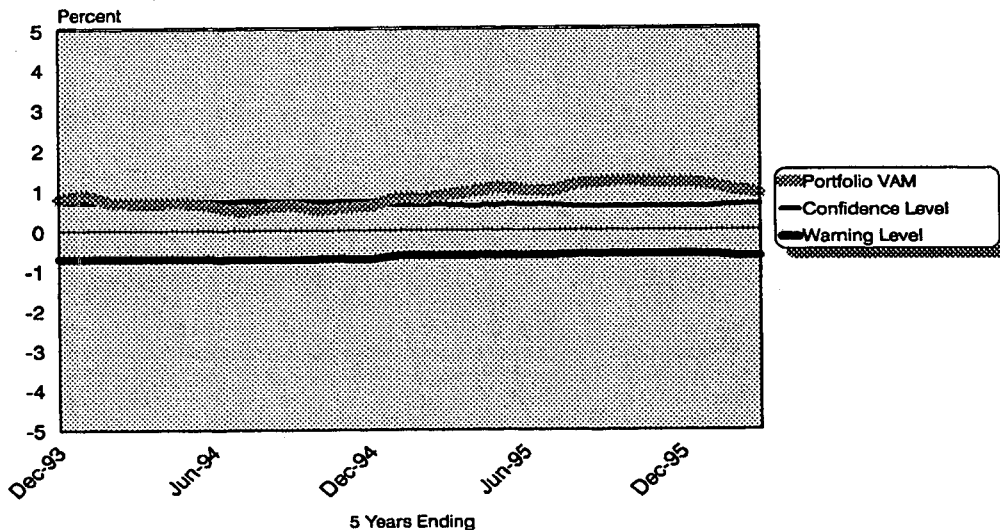
Quantitative Evaluation

	Actual	Benchmark
Last Quarter	-3.2%	-1.8%
Last 1 year	11.5	11.5
Last 2 years	8.1	8.0
Last 3 years	N/A	N/A
Last 4 years	N/A	N/A
Last 5 years	N/A	N/A
Since Inception (7/93)	5.8	5.7

Recommendations

No action recommended.

IDS ADVISORY GROUP
Rolling Five Year Time Periods



Note: Shaded area includes performance prior to managing the SBI account. Graph uses 80/20 confidence interval.

MILLER ANDERSON & SHERRERD
 Period Ending 3/31/96

Portfolio Manager: Tom Bennett

Assets Under Management: \$592,487,468

Investment Philosophy

Miller Anderson focuses its investments in misunderstood or under-researched classes of securities. Over the years this approach has led the firm to emphasize mortgage-backed and specialized corporate securities in its portfolios. Based on its economic and interest rate outlook, the firm establishes a desired maturity level for its portfolios. Changes are made gradually over an interest rate cycle and extremely high cash positions are never taken. Total portfolio maturity is always kept within an intermediate three-to-seven year duration band. Unlike other firms that invest in mortgage securities, Miller Anderson intensively researches and, in some cases, manages the mortgage pools in which it invests.

**Qualitative Evaluation
 (reported by exception)**

The firms strengths continue to be:

- Highly successful and experienced professionals.
- Extensive securities research process.

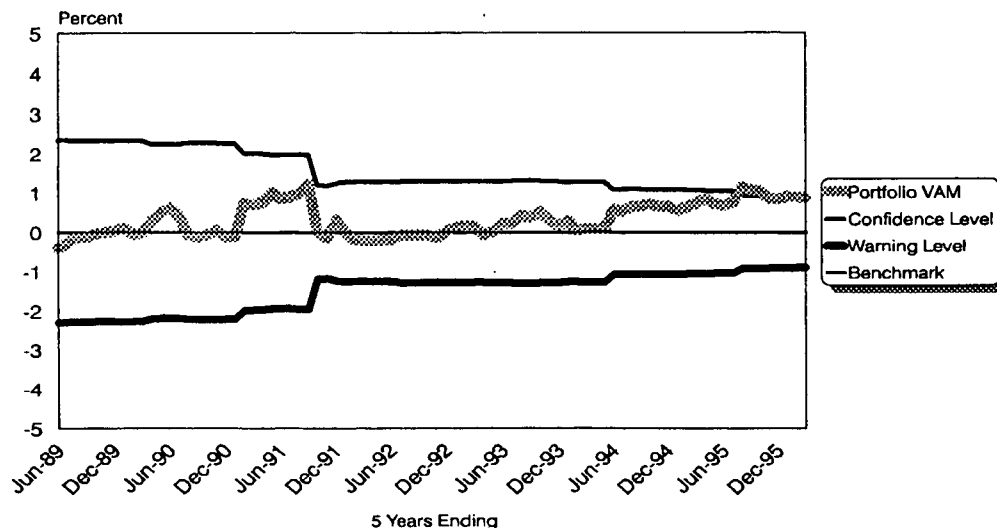
Quantitative Evaluation

	Actual	Benchmark
Last Quarter	-1.0%	-1.8%
Last 1 year	11.9	10.8
Last 2 years	7.8	7.9
Last 3 years	6.6	6.1
Last 4 years	8.6	7.9
Last 5 years	9.7	8.6
Since Inception (7/84)	11.6	11.3

Recommendations

No action recommended.

MILLER ANDERSON
 Rolling Five Year Time Periods



Note: Graph uses 80/20 confidence interval.

STANDISH, AYER & WOOD
 Period Ending 3/31/96

Portfolio Manager: Austin Smith

Assets Under Management: \$528,613,571

Investment Philosophy

Standish adds value by capitalizing on market inefficiencies and trading actively through intra and inter-sector swapping. The firm does not forecast interest rates but adds value to the portfolio by buying non-Treasury issues. Key to the approach is active sector trading and relative spread analysis of both sectors and individual issues. In addition to sector spreads, the firm also analyzes how secular trends affect bond pricing. The firm believes that 65% of its value added comes from inter-sector swapping in non-government sectors.

**Qualitative Evaluation
 (reported by exception)**

Exceptional strengths are:

- Highly successful and experienced professionals
- Extensive corporate research capabilities.

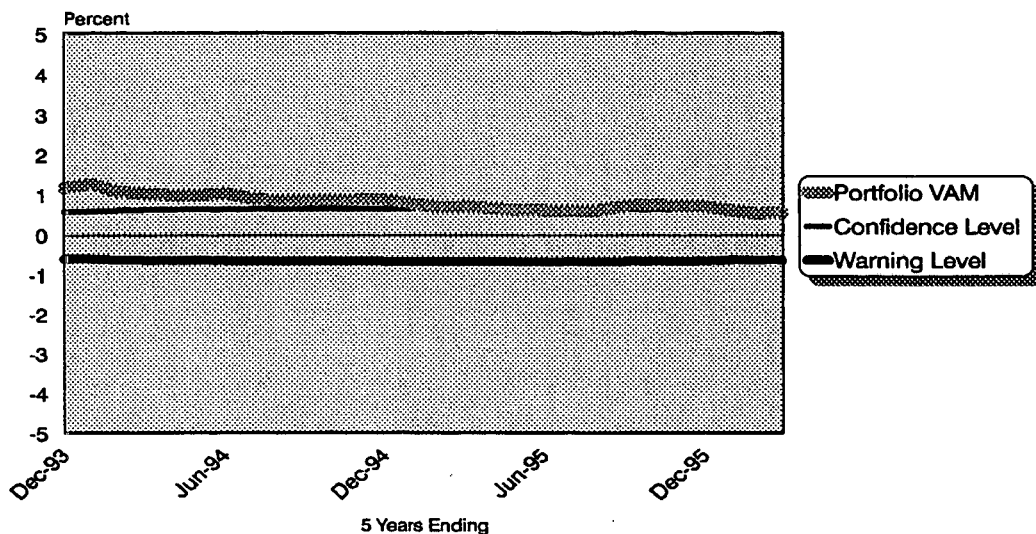
Quantitative Evaluation

	Actual	Benchmark
Last Quarter	-1.5%	-1.8%
Last 1 year	11.1	10.8
Last 2 years	7.4	7.9
Last 3 years	N/A	N/A
Last 4 years	N/A	N/A
Last 5 years	N/A	N/A
Since Inception (7/93)	5.2	5.6

Recommendations

No action recommended.

STANDISH, AYER & WOOD
 Rolling Five Year Time Periods



Note: Shaded area includes performance prior to managing the SBI account. Graph uses 80/20 confidence interval.

WESTERN ASSET MANAGEMENT
 Period Ending 3/31/96

Portfolio Manager: Kent Engel

Assets Under Management: \$1,007,037,560

Investment Philosophy

Western recognizes the importance of interest rate changes on fixed income portfolio returns. However, the firm believes that successful interest rate forecasting, particularly short run forecasting, is extremely difficult to accomplish consistently. Thus, the firm attempts to keep portfolio maturity in a narrow band near that of the market, making only relatively small, gradual shifts over an interest rate cycle. It prefers to add value primarily through appropriate sector decisions. Based on its economic analysis, Western will significantly overweight particular sectors, shifting these weights as economic expectations warrant. Issue selection, like maturity decisions, are of secondary importance to the firm.

**Qualitative Evaluation
 (reported by exception)**

The firm's exceptional strengths continue to be:
 —Highly successful and experienced professionals.
 —Extensive securities research process.

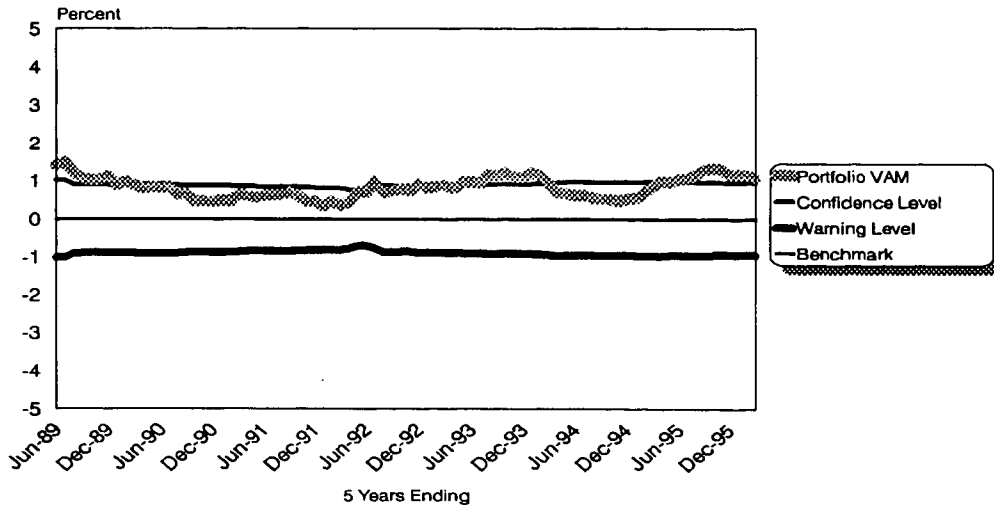
Quantitative Evaluation

	Actual	Benchmark
Last Quarter	-1.8%	-1.8%
Last 1 year	12.2	10.8
Last 2 years	8.5	7.9
Last 3 years	7.3	6.1
Last 4 years	9.1	7.9
Last 5 years	9.9	8.7
Since Inception (7/84)	12.5	11.3

Recommendations

No action recommended.

WESTERN ASSET MANAGEMENT
 Rolling Five Year Time Periods



Note: Graph uses 80/20 confidence interval.

GOLDMAN SACHS
Period Ending 3/31/96

Portfolio Manager: Sharmin Mossavar Rahmani

Assets Under Management: \$1,177,649,149

Investment Philosophy

Goldman is an enhanced index manager who focuses on security selection. When analyzing treasuries, the firm models Treasury coupons with an arbitrage based pricing model. This model determines the spread between actual and intrinsic market yields and determines whether the security is rich or cheap. Goldman takes a highly quantitative and analytical approach to value mortgage securities as well. Goldman uncovers undervalued securities using proprietary research and internally developed models. In the corporate sector, Goldman performs its own credit review of each issue. Goldman adds value to the corporate sector with extensive research, market knowledge, and trading skill.

**Qualitative Evaluation
 (reported by exception)**

Exceptional strengths are:

- Highly successful and experienced professionals.
- Quantitative capabilities.

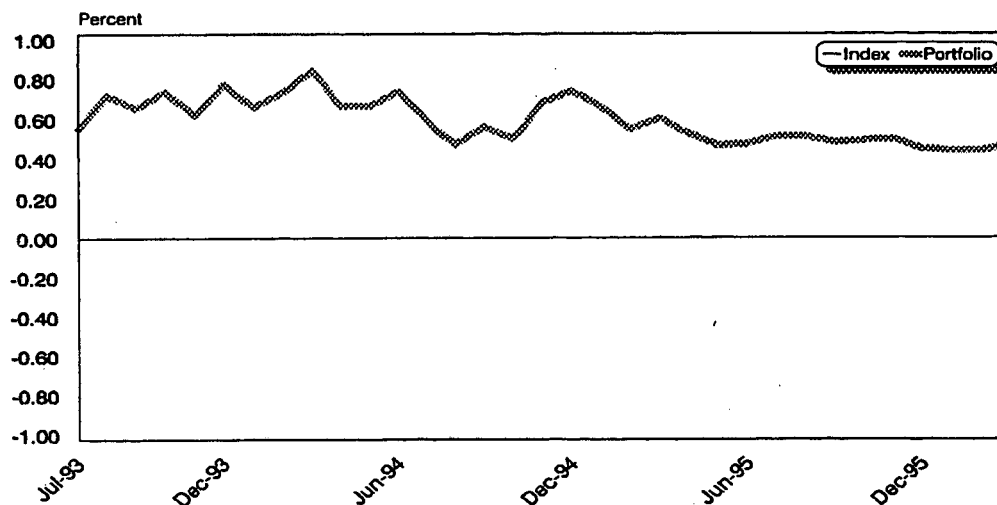
Quantitative Evaluation

	Actual	Benchmark
Last Quarter	-1.6%	-1.8%
Last 1 year	11.0	10.8
Last 2 years	8.1	7.9
Last 3 years	N/A	N/A
Last 4 years	N/A	N/A
Last 5 years	N/A	N/A
Since Inception (7/93)	6.0	5.6

Recommendations

No action recommended.

GOLDMAN SACHS
Cumulative Annualized Tracking Report



LINCOLN CAPITAL MANAGEMENT
Period Ending 3/31/96

Portfolio Manager: Andrew Johnson

Assets Under Management: \$1,160,365,596

Investment Philosophy

Lincoln is an enhanced index manager that uses a quantitative approach to managing the portfolio. Lincoln calculates the index's expected return for changes in 54 variables. These variables include interest rates, yield curve shape, call features and sector spreads. Lincoln then constructs a portfolio to match the expected returns for a given change in any of the variables. Lincoln relaxes the return tolerances, defined as the difference between the portfolio's expected returns and that for the index, for an enhanced index fund. The portfolio's securities are selected from a universe of 250 liquid issues using a proprietary risk-valuation model. A linear program or portfolio optimizer then constructs the most undervalued portfolio that still matches the return characteristics of the index.

**Qualitative Evaluation
 (reported by exception)**

The firm's strengths are:

- Highly successful and experienced professionals.
- Extensive quantitative capabilities.

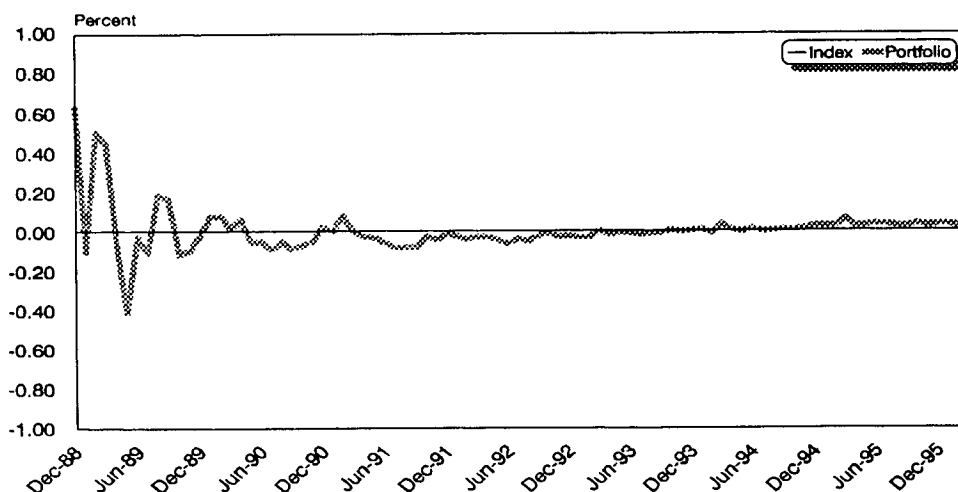
Quantitative Evaluation

	Actual	Benchmark
Last Quarter	-1.8%	-1.8%
Last 1 year	10.6	10.8
Last 2 years	7.9	7.9
Last 3 years	6.1	6.1
Last 4 years	7.9	7.9
Last 5 years	8.7	8.6
Since Inception (7/88)	9.3	9.3

Recommendations

No action recommended.

LINCOLN CAPITAL MANAGEMENT
Cumulative Annualized Tracking Report



VOYAGEUR ASSET MANAGEMENT - Assigned Risk Plan
Period Ending 3/31/96

Portfolio Manager: Jane Wyatt

Assets Under Management: \$401,427,364

Investment Philosophy
Assigned Risk Plan

Voyageur uses a top-down approach to fixed income investing. Their objective is to obtain superior long-term investment returns over a pre-determined benchmark that reflects the quality constraints and risk tolerance of the Assigned Risk Plan. Due to the specific liability requirement of the plan, return enhancement will focus on sector analysis and security selection. Yield curve and duration analysis are secondary considerations.

Qualitative Evaluation
(reported by exception)

Exceptional strengths are:

- Familiar with the needs of large institutional clients.
- Firms investment approach has been consistently applied over a number of markets cycles.
- Highly successful and experienced professionals.
- Organizational continuity and strong leadership.

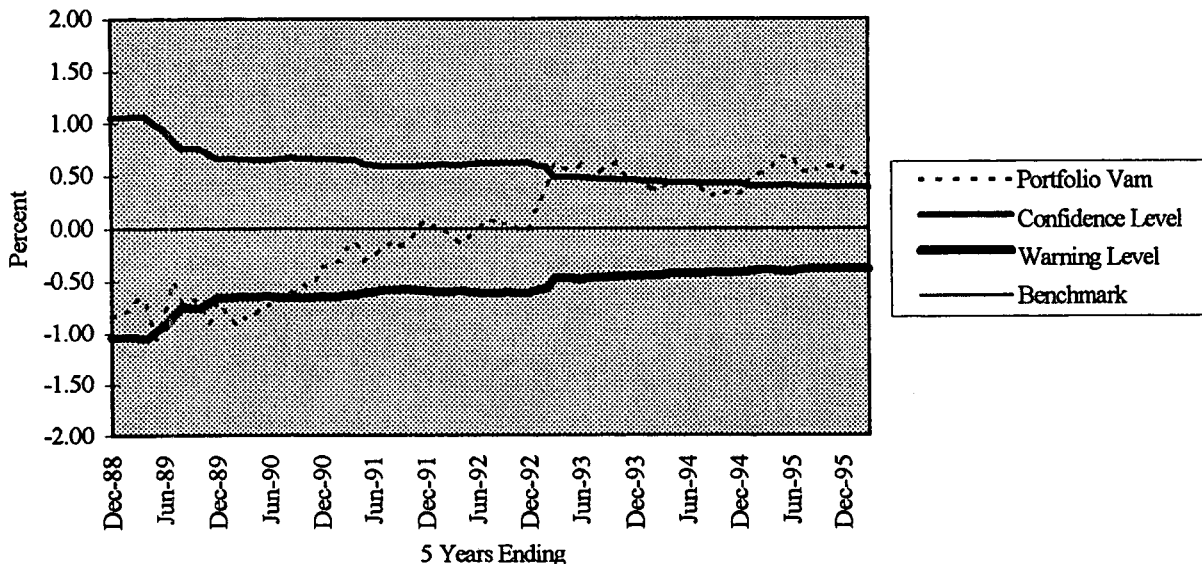
Quantitative Evaluation

	Actual	Benchmark
Last Quarter	-0.5%	-0.2%
Last 1 year	10.2	9.4
Last 2 years	7.5	7.3
Last 3 years	6.1	5.8
Last 4 years	7.4	7.1
Last 5 years	N.A.	N.A.
Since Inception (5/91)	8.4	7.8

Recommendation

No action recommended.

VOYAGEUR ASSET MANAGEMENT
Rolling Five Year Time Periods



Notes: Shaded areas includes performance prior to managing the SBI account.
 Graph uses 80/20 confidence interval.

INTERNAL BOND POOL - Income Share
Period Ending 3/31/96

Portfolio Manager: Jim Lukens

Assets Under Management: \$126,152,816

Investment Philosophy
Income Share Account

The internal bond portfolio's investment approach emphasizes sector and security selection. The approach utilizes sector trading and relative spread analysis of both sectors and individual issues. The portfolio weightings in mortgage and corporate securities are consistently equal to or greater than the market weightings. The portfolio duration remains close to the benchmark duration but may be shorter or longer depending on the economic outlook.

Qualitative Evaluation
(reported by exception)

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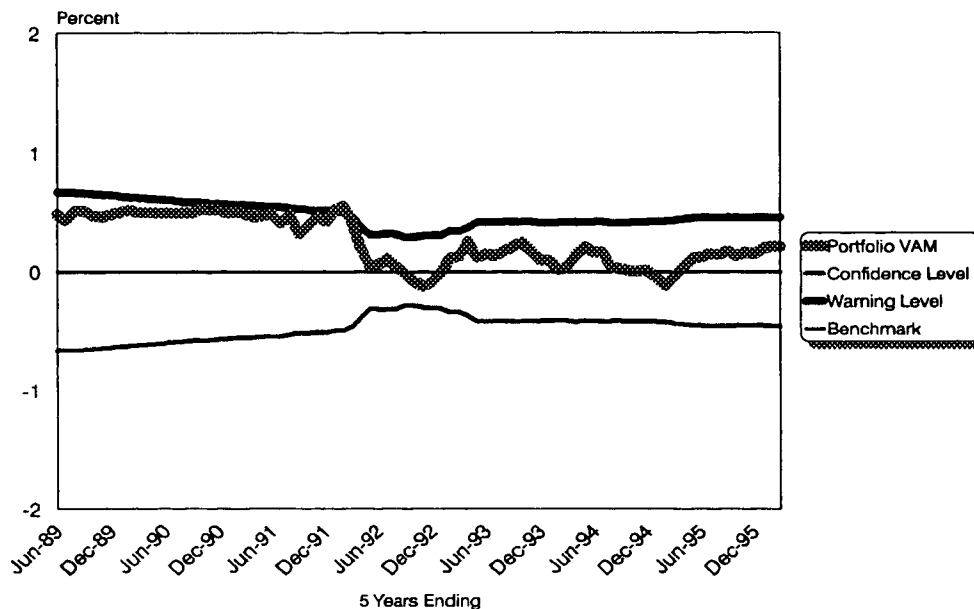
Quantitative Evaluation

	Actual	Benchmark
Last Quarter	-1.6%	-1.8%
Last 1 year	12.0	10.8
Last 2 years	8.1	7.9
Last 3 years	6.4	6.1
Last 4 years	8.4	7.9
Last 5 years	9.0	8.6

Recommendation

No action recommended.

INTERNAL BOND POOL - Income Share
Rolling Five Year Time Periods



Note: Graph uses 80/20 confidence interval.

INTERNAL BOND POOL - Trust/Non-Retirement Assets
Period Ending 3/31/96

Portfolio Manager: Jim Lukens

Assets Under Management: \$479,006,712

Investment Philosophy
Environmental Trust Fund
and Permanent School Trust Fund

Qualitative Evaluation
(reported by exception)

The internal bond portfolio's investment approach emphasizes sector and security selection. The approach utilizes sector trading and relative spread analysis of both sectors and individual issues. The portfolio weightings in mortgage and corporate securities are consistently equal to or greater than the market weightings. The portfolio duration remains close to the benchmark duration but may be shorter or longer depending on the economic outlook.

Quantitative Evaluation

Recommendation

	Actual	Benchmark	No action recommended.
Last Quarter	-1.7%	-1.8%	
Last 1 year	12.0	10.8	
Last 2 years	N/A	N/A	
Last 3 years	N/A	N/A	
Last 4 years	N/A	N/A	
Last 5 years	N/A	N/A	
Since Inception (7/94)*	10.5	9.7	

* Date started managing the Permanent School Fund against the Lehman Aggregate.

Tracking graph will be created for period ending 6/30/96.

Tab F

COMMITTEE REPORT

DATE: May 28, 1996

TO: Members, State Board Investment
Members, Investment Advisory Council

FROM: International Manager Committee

The International Manager Committee met on May 15, 1996 to discuss the following agenda items:

- Review of manager performance for the period ending March 31, 1996
- Annual review of investment manager guidelines
- Update on emerging markets manager funding
- Upcoming emerging markets manager "round table"
- Approval of contract renewals with existing managers

Board action is requested on the last item.

INFORMATION ITEMS:

1. Review of manager performance

For the period ending March 31, 1996, the international stock program outperformed the EAFE-Free index by 0.7 percentage point for the quarter. The program outperformed the index by 4.0 percentage points for the latest year and by 0.4 percentage point annualized for the last three years. The program has outperformed the EAFE-Free index by 0.4 percentage point annualized since inception (3.5 years).

Time Period	Actual	EAFE-Free
Quarter	3.6%	2.9%
1 Year	16.5	12.5
3 Years	13.9	13.5
Since Inception (10/92)	14.2	13.8

All of the six active managers outperformed for the quarter and for the year. Performance evaluation reports begin on **page 21** and Manager Commentaries are in **Tab I**.

Performance attribution for the quarter shows the following for the entire program:

	Actual	EAFE	Value Added
Local Currency	+5.79	+5.37	+0.42
Country Selection			+0.16
Security Selection			+0.26
Currency Impact	-2.04	-2.36	+0.32
Currency Effect			+0.14
Hedging Activity			+0.18
US Dollar Return	+3.64	+2.89	+0.75

Source: State Street Analytics

The Committee also discussed the status of the currency overlay program which is currently being phased-in. Summary data are shown below. A more complete review is included in the Manager Commentary section under **Tab I**. Given the small size of the hedge as of 3/29/96, the overlay program has had minimal impact on the performance of the entire international pool. Additional information which details the actual performance of the currency overlay program relative to the agreed upon benchmark should be available for the quarter ending June 30, 1996.

	Currency Exposure* 3/29/96	Assets Covered by Overlay Program** 3/29/96		Assets Hedged as of 3/29/96	
Yen	\$665.6 mill	\$228.3 mill	34.30%	\$86.1 mill	12.94%
Sterling	281.1 mill	91.3 mill	32.48	0.0 mill	0.00
Mark	121.9 mill	40.7 mill	33.35	20.1 mill	16.52
Fr. Franc	108.4 mill	35.7 mill	32.90	0.0 mill	0.00
Sw. Franc	105.0 mill	34.5 mill	32.89	13.1 mill	15.34
Total	\$1,282.1 mill	\$430.5 mill	33.58%	\$122.4 mill	9.54%

* Based on currency exposure of the SBI's EAFE index fund.

** Assets covered will be less than exposure during phase-in period. One twelfth of the exposure will be added to the overlay program each month from December 1995 through November 1996.

2. Annual review of investment manager guidelines

The SBI has established guidelines for the external international managers which govern their investment actions. While these guidelines may be changed at any time, they are part of the formal contractual agreement between the manager and the SBI.

The guidelines address return objectives, benchmarks, authorized investments, performance evaluation, communication and reporting requirements. Staff review the guidelines annually for accuracy and completeness.

No changes were deemed necessary for the EAFE index fund manager. The modifications for the remaining manager groups can be summarized as follows:

- *active managers*. Language was added to prohibit the use of private placements and to cap exposure to emerging markets. This change corresponds to the policy adopted by the SBI in December 1995 when it accepted the position paper on emerging markets investing.
- *currency overlay manager*. The rebalancing guidelines are being changed to reflect the procedures used by the manager.
- *emerging markets managers*. Language clarifying the use of certain securities has been added to address specific issues that have arisen during the funding process.

The Committee reviewed the proposed changes and did not recommend further modifications at this time. However, the Committee and staff agreed that standards used to evaluate the effectiveness of the currency overlay program should be studied over the coming months. This analysis should differentiate the value added/lost by the SBI's decision to employ a hedging strategy from value added/lost by the manager's implementation process.

The complete guidelines for each manager group are attached beginning on page 5. Additions to the current guidelines are noted by underline and deletions are indicated by ~~strikeout~~.

3. Update on emerging markets manager funding

Contracts for all three emerging markets managers have now been executed. Genesis Asset Managers and Montgomery Asset Management received their initial funding in May 1996 and a schedule for the remainder of the allocation has been agreed upon with both firms. Funding for the City of London will be determined after custody issues regarding that firm's proposed investments in Taiwan have been resolved.

4. Upcoming "round table" with emerging markets managers

Staff will host a "round table" discussion with the newly retained emerging markets managers on the afternoon of June 24, 1996. Further information on time and location should be available shortly.

The SBI Administrative Committee will also meet on the same date to update the country groupings in the SBI's international investing guidelines. Staff expect to add

several countries to the groupings to address all the markets that the emerging markets managers are considering for investment. In addition, the managers will review their current and proposed investments in "Group III" countries.

ACTION ITEM:

1. Approval of contract renewals with existing managers

On September 30, 1996 the contract with State Street Global Advisors, the SBI's EAFE index fund manager, will expire. The contracts with Marathon Asset Management, Rowe Price-Fleming International, Scudder, Stevens & Clark, and Templeton will expire on October 31, 1996.

Staff recommended that all five contracts be renewed for five year periods ending September 30, 2001. Staff also proposed that the contracts be amended to reduce the termination clause from 30 days notice to immediate termination. All other terms of the contracts will remain unchanged.

RECOMMENDATION:

The Committee recommends that the SBI authorize the Executive Director, with assistance from SBI legal counsel, to negotiate and execute contract renewals for five year periods ending September 30, 2001 with the following international stock managers, subject to inclusion of a provision which provides for immediate termination.

- **State Street Global Advisors**
- **Marathon Asset Management**
- **Rowe Price-Fleming International**
- **Scudder, Stevens & Clark**
- **Templeton Investment Counsel**

MINNESOTA STATE BOARD OF INVESTMENT
INVESTMENT GUIDELINES
ACTIVE INTERNATIONAL EQUITY MANAGER

The investment actions of the State Board of Investment (SBI) active international and active country/passive stock managers will be governed by the following guidelines:

1. RETURN OBJECTIVE

The manager is expected to deliver returns that exceed the benchmark, net of fees, by at least 1 percentage point annually, over time.

2. PERFORMANCE BENCHMARK

Until a benchmark that is more representative of the Manager's style is developed, the performance benchmark for the portfolio will be the Morgan Stanley Capital International (MSCI) Index of Europe, Australia and the Far East (EAFE), capitalization weighted, excluding those securities that US investors are not allowed to own. This is commonly referred to as EAFE "Free" by MSCI.

3. PRICING AND PERFORMANCE MEASUREMENT

The Account will be priced by the SBI's custodian bank and such prices will be used to measure performance of the SBI account. The Manager agrees to accept the prices established by the custodian. The Manager will review the custodian's pricing on a monthly basis and report any differences or discrepancies to the custodian and the SBI.

4. PERFORMANCE EVALUATION

Manager will be evaluated according to the guidelines set forth in the SBI's Manager Continuation Policy.

5. ELIGIBLE MARKETS

Subject to the constraints in #6 below, the Manager is authorized to purchase securities in the following markets:

Group I. The Manager is not restricted regarding publicly traded securities in the following markets:

Australia	Germany	Netherlands	Spain
Austria	Greece	New Zealand	Sweden
Belgium	Hong Kong	Norway	Switzerland
Canada	Hungary	Poland	United Kingdom
Czech Republic	Italy	Portugal	Uruguay
Denmark	Ireland	Singapore	
Finland	Japan	Slovak Republic	
France	Luxembourg	Slovenia	

Group II. The Manager may purchase publicly traded securities in the following markets if the Manager believes it would be a breach of fiduciary responsibility not to do so. If the Manager chooses to invest in one or more of these markets, the manager must notify the SBI in writing of its decision to do so.

Argentina	Israel	South Africa
Brazil	Jamaica	Sri Lanka
Chile	Korea, Rep. of	Taiwan
Colombia	Malaysia	Thailand
Ecuador	Mauritius	Trinidad & Tobago
Egypt	Mexico	Turkey
Estonia	Philippines	Venezuela
India	Russia	Zimbabwe

Group III. The Manager may invest in publicly traded securities in the following markets if the Manager believes it would be a breach of fiduciary responsibility not to do so. If the Manager chooses to invest in one or more of these markets, the Manager must appear at a meeting of the SBI to present its reason(s) for the decision to do so.

China	Morocco
Croatia	Nigeria
Indonesia	Peru
Jordan	Pakistan
Kuwait	Vietnam

6. ELIGIBLE SECURITIES

Subject to the constraints in #5 above, the Manager may hold stocks, warrants, convertibles, common trust funds, open-end country funds registered under the Investment Company Act of 1940, equity options, currency futures and options, financial and commodity futures, and commodities and options thereon, currency forwards and cash equivalents provided:

- All securities held must be covered by the authorization in Minnesota Statutes Chapter 11A.24.
- US cash equivalent reserves shall be invested in the SBI's STIF fund, managed by its custodian bank.
- Convertibles shall not comprise more than 5% of the Account.
- No more than 15% of the Account may be held in the stock of companies domiciled in emerging markets. For this purpose, emerging markets are defined as Malaysia plus all non-EAFE, non-North American markets.
- The stock of companies domiciled in the US shall not be held in the Account.
- Non-US stock index futures may be used to adjust the effective equity exposure of the Account from 0 to 100%. In addition, all transactions must be done on a fully collateralized basis.
- Currency forwards and futures and options may be used to adjust the effective non US currency exposure of the portfolio from 0 to 100%. In addition, all transactions must be done on a fully collateralized basis.

The Manager is not constrained regarding:

- transaction turnover
- use of covered call options as hedging devices
- liquidity requirements
- number of individual equity issues which must be held at any given time

7. COMMUNICATION

The SBI requires its investment managers to communicate with SBI staff on a regular basis.

- The Manager is expected to meet with staff to review the results of the Manager's investment decision-making process on at least an annual basis.

- The Manager is expected to provide SBI staff with a "Manager Commentary" as described in the SBI's Manager Continuation Policy on a quarterly basis (see #4 above). The Commentary will summarize performance results over the most recent quarter and year and highlights any organizational changes which may impact management of the SBI's Account.

8. PROXY VOTING

The SBI retains the right to vote its proxies directly. Unless the SBI notifies the Manager that it is exercising this right, the Manager shall vote all proxies on behalf of the SBI according to guidelines provided to the manager by the SBI. The Manager shall report periodically on its voting practices with respect to the SBI Account. The SBI represents that such delegation of voting rights is consistent with applicable Minnesota Statutes. The SBI agrees to instruct the Custodian to forward all proxy materials to the Manager upon receipt. Manager shall not be liable with regard to voting of proxies in the event proxy materials are not received by the Manager in a timely manner.

9. COMMODITY FUTURES TRADING AGREEMENT

Any commodity futures or options trading agreement entered into by the Manager must provide that SBI liability for margin requirements, commissions and fees is limited solely to funds of the SBI and does not constitute a general obligation of the State of Minnesota.

10. FUTURE MODIFICATIONS

The SBI reserves the right to modify these investment guidelines at any time. The Manager will be notified in advance of changes to the investment guidelines.

Revised: May 1996

**MINNESOTA STATE BOARD OF INVESTMENT
INVESTMENT GUIDELINES
EAFE INDEX FUND MANAGER**

The investment actions of the State Board of Investment (SBI) EAFE Index Fund Manager will be governed by the following guidelines:

1. RETURN/TRACKING ERROR OBJECTIVE

The manager is expected to deliver returns that track the benchmark index within ± 20 basis points on an annual basis before management fees, custody charges and return enhancements such as securities lending income.

2. BENCHMARK INDEX

The benchmark index will be the Morgan Stanley Capital International (MSCI) Index of Europe, Australia and the Far East (EAFE), capitalization weighted, excluding those securities that US investors are not allowed to own. This is commonly referred to as EAFE "Free" by MSCI.

3. PRICING AND PERFORMANCE MEASUREMENT

The portfolio will be priced by the SBI's custodian bank and such prices will be used to measure the performance of the SBI account. The manager agrees to accept the prices established by the custodian. The manager will review the custodian's pricing on a monthly basis and report any differences or discrepancies to the custodian and the SBI.

4. ELIGIBLE INVESTMENTS

The manager may hold stocks, stock index futures, bonds and cash equivalents subject to the following constraints:

- All securities held must be covered by the authorization in Minnesota Statutes Chapter 11A.24.
- Cash equivalent reserves shall be invested in the SBI's STIF fund, managed by its custodian bank.
- The use of stock index futures may be used to adjust the effective equity exposure of the portfolio from 0 to 100%. In addition, all transactions must be done on a fully collateralized basis.

The manager is not constrained regarding:

- transaction turnover
- use of covered call options as hedging devices
- liquidity requirements
- number of individual equity issues which must be held at any given time

5. COMMUNICATION

The SBI requires its investment managers to communicate with SBI staff on a regular basis.

- The manager is expected to meet with staff to review the results of the manager's investment decision-making process on at least an annual basis.
- The manager is expected to provide SBI staff with a status report pertaining to number of accounts, assets under management, and relevant personnel and ownership changes on a quarterly basis.

6. PROXY VOTING

The SBI is responsible for proxy voting. The SBI may delegate responsibility for proxy voting in certain countries to the Manager. If so, such delegation will be made in writing along with appropriate voting policy direction.

7. COMMODITY FUTURES TRADING AGREEMENT

Any commodity futures trading agreement entered into by the Manager must provide that SBI liability for margin requirements, commissions and fees is limited solely to funds of the SBI and does not constitute a general obligation of the State of Minnesota.

8. FUTURE MODIFICATIONS

The SBI reserves the right to modify these investment guidelines at any time. The Manager will be notified in advance of changes to the investment guidelines.

Date: May 1995

INVESTMENT GUIDELINES CURRENCY OVERLAY

The investment actions of the Manager will be governed by the following guidelines:

1. Implementation

The SBI directs the Manager to construct in-house options using strike prices set at 2% out-of-the-money on the start date of each tranche for each currency.

The SBI directs the Manager to use its standard implementation schedule involving the regular setting of in-house options. This process establishes twelve tranches for each currency included in the program, except the Japanese Yen, and constructs in-house options in monthly increments. For the Japanese Yen, twenty four tranches will be constructed using semi-monthly intervals. Implementation for the currencies included in the program will not be completed until mid month of month eleven of the contract period.

The Manager will rebalance outstanding currency positions when the value of the underlying stock in the corresponding market advances or declines by ~~4 percentage points or more. When such rebalancing is necessary, it will be implemented in approximately equal increments across all tranches for the corresponding currency.~~ 2 percentage points or more of the total value of SBI's EAFE Index Fund. When such rebalancing is necessary, it will be implemented as follows: For declines in value, all tranches in that currency will be reduced pro-rata; for advances in value, out-of-the money options will be increased pro-rata, and in-the-money options will be increased only after their next trade, if any.

2. Objectives

The currency overlay program has the following objectives. The objectives are based upon scenario analysis completed by the Manager at the request of the SBI:

- Over a full cycle of dollar strength and weakness, the Manager is expected to add at least 1 percentage point annualized to the return of the benchmark in #3, net of all costs.
- In periods when the US dollar strengthens relative to the currencies listed in #3, the Manager is expected to outperform the benchmark in #3. The extent of the outperformance will be dependent upon the extent of the dollar's move relative to the currencies included in the program; the greater the move in the dollar, the greater the participation in the available outperformance.

- In periods when the US dollar weakens or is trendless (flat/choppy) relative to the currencies listed in #3, the Manager is expected to underperform the benchmark in #3 by no more than 3 percentage points annualized.
- In all periods, the Manager is expected to minimize the costs associated with providing the above protection. The average annual cost is expected to be approximately 2 percentage points.

3. Benchmark

The Manager's benchmark will be measured in US dollars and will be comprised of the unhedged return of the following currencies:

- Japanese Yen
- British Pound Sterling
- German Mark
- French Franc
- Swiss Franc

The weights given each currency will be based upon their proportionate weight in the EAFE index and will be rebalanced at the start of each calendar quarter based on the index weights on the last day of the previous quarter. The SBI's international consultant will be responsible for determining the weights in the benchmark and for calculating benchmark return.

4. Pricing and Performance Measurement

The account will be priced by the SBI's custodian bank and such prices will be used to measure the performance of the SBI account. Any cash equivalents held in the account will be included in the calculation of performance.

5. Eligible Investments

The Manager is authorized to take currency positions using spot foreign exchange contracts, forward foreign exchange contracts, and options and futures on foreign currencies. These securities may be over-the-counter or exchange traded and are subject to the following constraints:

- Hedging foreign currency exposure back to the US dollar is the only type of hedge that is authorized. Cross hedging and proxy hedging are prohibited.

- Net long or short currency positions are prohibited. The prohibition on net long positions means that all transactions must be executed on a fully collateralized basis and the currency exposure of the underlying stock position may not be leveraged. The prohibition on net short positions means that that the Manager cannot have negative exposure to any foreign currency.
- All currency positions must mature/expire within one year or less from the date of execution.
- Any cash equivalent reserves held in the account shall be invested in the SBI's STIF fund and managed by its custodian bank.
- The Manager is not authorized to hold any stock or bond, US or foreign, or any derivative instrument related to such securities.

In addition to the above, all transactions undertaken on behalf of the SBI must be covered by the authorization in *Minnesota Statutes* Section 11A.24.

6. Communication

The SBI requires its investment managers to communicate with SBI staff on a regular basis:

- The Manager is expected to meet with SBI staff to review the results of the Manager's investment process on at least an annual basis.
- The Manager is expected to provide SBI staff with a status report pertaining to number of accounts, assets under management and personnel and ownership changes on a quarterly basis.

7. Counterparty Banks

Each counterparty bank used by the Manager to execute currency transactions must have a credit rating of A1/P1 or better from each of the following rating organizations: S&P, Moody's and IBCA.

The Manager will maintain facilities on behalf of the SBI with a minimum of six and maximum of ten banks. In no case may the netted value of outstanding positions with a single bank exceed \$400 million.

Any agreement entered into must provide that SBI liability for settlement, commissions and fees is limited solely to funds of the SBI and does not constitute a general obligation of the State of Minnesota.

The Manager is responsible for monitoring both the long term and short term credit ratings of each counterparty bank and the Manager will notify the SBI of any downgrade in either rating promptly.

The SBI reserves the right to withdraw the Manager's authority to use the facility established with any counterparty bank. The Manager may add or delete counterparty banks with the knowledge and approval of the SBI.

8. Commodity Futures Trading Agreements

Any commodity futures trading agreement entered into must provide that SBI liability for margin requirements, commissions and fees is limited solely to funds of the SBI and does not constitute a general obligation of the State of Minnesota.

9. Future Modifications

The SBI reserves the right to modify these investment guidelines at any time. The Manager will be notified in advance of changes to the investment guidelines.

Revised: May 1996

MINNESOTA STATE BOARD OF INVESTMENT

INVESTMENT GUIDELINES EMERGING MARKETS EQUITY MANAGER

The investment actions of the State Board of Investment (SBI) emerging markets equity managers will be governed by the following guidelines:

1. RETURN OBJECTIVE

Manager is expected to deliver returns that exceed the benchmark, net of fees and transaction costs, by at least 1 percentage point annually, over time. SBI acknowledges that Manager gives no assurance that these returns will, in fact, be achieved.

2. PERFORMANCE BENCHMARK

The performance benchmark for the Account will be the Morgan Stanley Capital International Emerging Markets Free (MSCI EMF) index.

3. PRICING AND PERFORMANCE MEASUREMENT

The Account will be priced by the SBI's custodian bank and such prices will be used to measure performance. The Manager agrees to accept the prices established by the Custodian. The Manager will review the Custodian's pricing on a monthly basis and report any differences or discrepancies to the Custodian and the SBI.

4. PERFORMANCE EVALUATION

Manager will be evaluated according to the guidelines set forth in the SBI's Manager Continuation Policy.

5. ELIGIBLE MARKETS

Subject to the constraints in #6 below and as otherwise provided in #6 below, the Manager is authorized to purchase securities in the following markets:

Group I. The Manager is not restricted regarding publicly traded securities in the following markets:

Australia	Germany	Netherlands	Spain
Austria	Greece	New Zealand	Sweden
Belgium	Hong Kong	Norway	Switzerland
Canada	Hungary	Poland	United Kingdom
Czech Republic	Italy	Portugal	Uruguay
Denmark	Ireland	Singapore	
Finland	Japan	Slovak Republic	
France	Luxembourg	Slovenia	

Group II. The Manager may purchase publicly traded securities in the following markets if the Manager believes it would be a breach of fiduciary responsibility not to do so. If the manager chooses to invest in one or more of these markets, the manager must notify the SBI in writing of its decision to do so.

Argentina	Israel	South Africa
Brazil	Jamaica	Sri Lanka
Chile	Korea, Rep. of	Taiwan
Colombia	Malaysia	Thailand
Ecuador	Mauritius	Trinidad & Tobago
Egypt	Mexico	Turkey
Estonia	Philippines	Venezuela
India	Russia	Zimbabwe

Group III. The Manager may invest in publicly traded securities in the following markets if the Manager believes it would be a breach of fiduciary responsibility not to do so. If the manager chooses to invest in one or more of these markets, the manager must appear at a meeting of the SBI Administrative Committee to present its reason(s) for the decision to do so.

China	Morocco
Croatia	Nigeria
Indonesia	Peru
Jordan	Pakistan
Kuwait	Vietnam

6. ELIGIBLE SECURITIES

Subject to the constraints in #5 above, the Manager may hold stocks, warrants, convertibles, common trust funds, closed-end country or regional funds (or open-end country or regional funds that have been converted from closed-end funds held by the account), equity options, currency futures and options, financial and commodity futures, and commodities and options thereon, currency forwards and cash equivalents provided:

- All securities held must be covered by the authorization in Minnesota Statutes Chapter 11A.24.
- US cash equivalent reserves shall be invested in the SBI's STIF fund, managed by its custodian bank.
- Private placements may not be held in the Account.
- Debt securities, except cash equivalents, may not be held in the Account.
- The stock of companies domiciled in any of the following countries shall not be held in the account: U.S.; Canada; all EAFE markets, except Malaysia, Singapore and Hong Kong. Notwithstanding the foregoing sentence, Manager may invest in ADR's, GDR's hold closed-end country or regional funds (or open-end country or regional funds that have been converted from closed-end funds held by the Account), provided all or substantially all of the assets of such instruments or funds satisfy this constraint.
- ADR's, GDR's and 144(A) securities may be held in the Account provided they are issued by a company domiciled in an emerging market, are depository eligible and can be priced on a daily basis. In addition, 144(A) securities must be traded in the US or UK.
- The stock of companies domiciled in Russia shall not be held in the Account without the express approval of the SBI.
- Non-US stock index futures may be used to adjust the effective equity exposure of the Account from 0 to 100%. In addition, all transactions must be done on a fully collateralized basis.
- Currency forwards and futures and options may be used to adjust the effective non US currency exposure of the Account from 0 to 100%. In addition, all transactions must be done on a fully collateralized basis. Manager has no obligation to hedge currency risk and will not be required to do so.

The Manager is not constrained regarding:

- transaction turnover
- liquidity requirements
- number of individual issues which must be held at any given time

7. COMMUNICATION

The SBI requires its investment managers to communicate with SBI staff on a regular basis.

- The Manager is expected to meet with staff to review the results of the manager's investment decision-making process on at least an annual basis.
- The Manager is expected to provide SBI staff with a "Manager Commentary" as described in the SBI's Manager Continuation Policy on a quarterly basis (see #4 above). The Commentary will summarize performance results over the most recent quarter and year and highlights any organizational changes which may impact management of the SBI's account.

8. PROXY VOTING

The SBI retains the right to vote its proxies directly. Unless the SBI notifies the Manager that it is exercising this right, the Manager shall vote all proxies on behalf of the SBI according to guidelines provided to the Manager by the SBI. The Manager shall report periodically on its voting practices with respect to the SBI portfolio. The SBI represents that such delegation of voting rights is consistent with applicable Minnesota Statutes. The SBI agrees to instruct the Custodian to forward all proxy materials to the Manager upon receipt. Manager shall not be liable with regard to voting of proxies in the event proxy materials are not received by the Manager in a timely manner.

9. COMMODITY FUTURES TRADING AGREEMENT

Any commodity futures or options trading agreement entered into by the Manager must provide that SBI liability for margin requirements, commissions and fees is limited solely to funds of the SBI and does not constitute a general obligation of the State of Minnesota.

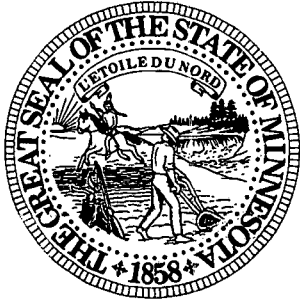
10. SEPARATE ACCOUNT AND DAILY PRICING

Manager will manage the portfolio on a separate account basis. All assets will be held in custody by the SBI's custodian bank and its network of sub-custodians. All securities held in the Account must be capable of being priced on a daily basis. Commingled vehicles may not be held in the Account without the express approval of the SBI.

11. FUTURE MODIFICATIONS

The SBI reserves the right to modify these investment guidelines at any time. The Manager will be notified in writing in advance of changes to the investment guidelines.

Revised: May 1996



STATE BOARD OF INVESTMENT

International Manager Evaluation Reports

First Quarter, 1996

INTERNATIONAL STOCK MANAGERS
Period Ending 3/31/96

Current Managers	Quarter		1 Year		3 years		5 Years		Since Inception		Market Value (in millions)	Pool %
	Actual	Bmk	Actual	Bmk	Actual	Bmk	Actual	Bmk	Actual	Bmk		
	%	%	%	%	%	%	%	%	%	%		%
Baring (1)	3.7	2.9	17.2	12.5	14.2	13.5			14.2	13.5	\$215.55	6.7%
Brinson (1)	3.3	2.9	25.0	12.5	11.5	13.5			11.5	13.5	304.49	9.4%
Marathon (2)	4.4	2.9	16.4	12.5					11.2	8.1	296.61	9.2%
Rowe Price (2)	5.0	2.9	19.1	12.5					10.3	8.1	292.14	9.1%
Scudder (2)	6.5	2.9	24.8	12.5					10.7	8.1	196.03	6.1%
Templeton (2)	4.8	2.9	21.4	12.5					11.4	8.1	198.49	6.1%
State Street (3)	2.9	2.9	12.8	12.5	13.5	13.5			13.9	13.8	1,723.03	53.4%
Current Aggregate*	3.6	2.9	16.5	12.5	13.9	13.5			14.2	13.8	\$3,226.77	100.0%

(1) Active country/passive stock. Retained April 1, 1993

(2) Fully active. Retained November 1, 1993

(3) Index. Retained October 1, 1992

* Includes impact of currency overlay unrealized gain/loss

BARING INTERNATIONAL INVESTMENT LTD.
Period Ending 3/31/96

Portfolio Manager: Philip Bullen

Assets Under Management: \$215,553,629

Investment Philosophy

Barings manages an active country/passive stock portfolio for the SBI. Barings' strategic policy team is responsible for the country and currency decisions. Country allocation decisions are made using a macroeconomic framework which seeks to identify growing economies as evidenced by positive changes in GDP and interest rates. The team uses multiple inputs including regional specialists, local market valuations and a computer model that functions as an audit of the qualitative valuation process. Currency specialists within Barings provide assessments on flow of funds, currency rates, monetary policy, inflation and interest rates. Barings uses country index funds managed by State Street Global Advisors to implement their country allocations. At Barings' direction, State Street also implements currency/hedging strategies for the portfolio.

**Qualitative Evaluation
(reported by exception)**

Exceptional strengths are:

- Highly successful and experienced professionals.
- Familiar with the needs of large institutional clients.

Current concerns are:

- New ownership by ING effective February 1995.

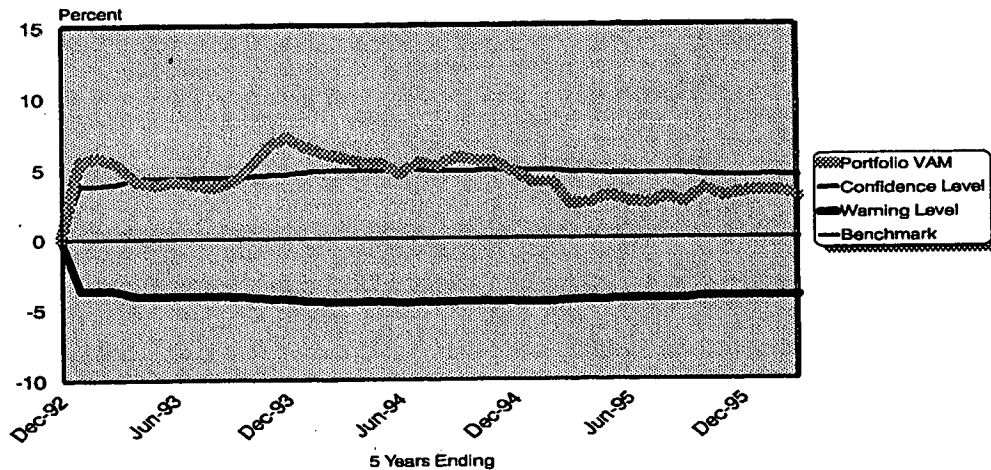
Quantitative Evaluation

	Actual	Benchmark
Last Quarter	3.7%	2.9%
Last 1 year	17.2	12.5
Last 2 years	10.2	9.3
Last 3 years	14.2	13.5
Last 4 years	N/A	N/A
Last 5 years	N/A	N/A
Since Inception (4/93)	14.2%	13.5%

Recommendations

No action recommended.

BARING INT'L. INVESTMENT LTD.
Rolling Five Year Time Periods



Note: Shaded area includes performance prior to managing SBI account. Graph uses 80/20 confidence interval.

BRINSON PARTNERS
Period Ending 3/31/96

Portfolio Manager: Richard Carr

Assets Under Management: \$304,491,666

Investment Philosophy

Brinson manages an active country/passive stock portfolio for the SBI. The firm uses a proprietary valuation model to rank the relative attractiveness of individual markets based on fundamental considerations. Inputs include forecasts for growth, inflation, risk premiums and foreign exchange movements. Quantitative tools are used to monitor and control portfolio risk, while qualitative judgments from the firm's professionals are used to determine country allocations. Brinson establishes an allocation range around the target index to define the limits of their exposure to individual countries and to assure diversification. Brinson constructs its country index funds using a proprietary optimization system.

Brinson utilizes currency equilibrium bands to determine which currencies are over or under valued. The firm will hedge to control the potential risk for real losses from currency depreciation.

**Qualitative Evaluation
 (reported by exception)**

Exceptional strengths are:

- Highly successful and experienced professionals.
- Familiar with the needs of large institutional clients.

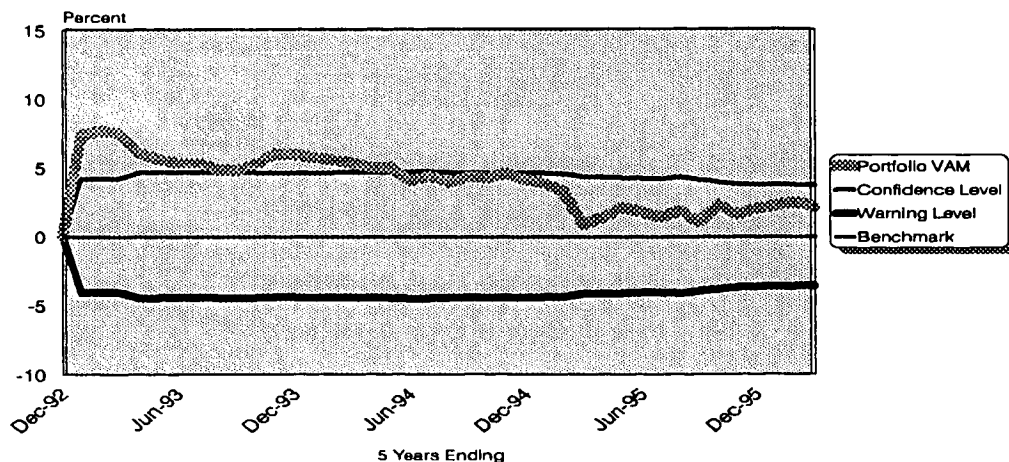
Quantitative Evaluation

	Actual	Benchmark
Last Quarter	3.3%	2.9%
Last 1 year	25.0	12.5
Last 2 years	12.1	9.3
Last 3 years	11.5	13.5
Last 4 years	N/A	N/A
Last 5 years	N/A	N/A
Since Inception (4/93)	11.5%	13.5%

Recommendations

No action recommended.

BRINSON PARTNERS, INC. (INT'L.)
Rolling Five Year Time Periods



Note: Shaded area includes performance prior to managing SBI account. Graph uses 80/20 confidence interval.

MARATHON ASSET MANAGEMENT
 Period Ending 3/31/96

Portfolio Manager: William Arah

Assets Under Management: \$296,610,141

Investment Philosophy

Marathon uses a blend of flexible, qualitative disciplines to construct portfolios which exhibit a value bias. Style and emphasis will vary over time and by market, depending on Marathon's perception of lowest risk opportunity. Since they believe that competition determines profitability, Marathon is attracted to industries where the level of competition is declining and they will hold a sector position as long as the level of competition does not increase. At the stock level, Marathon tracks a company's competitive position versus the attractiveness of their products or services and attempts to determine whether the company is following an appropriate reinvestment strategy for their current competitive position.

**Qualitative Evaluation
 (reported by exception)**

Exceptional strengths are:

—Attractive, unique investment approach.

Current concerns are:

—The firm has experienced significant client growth over the last two years.

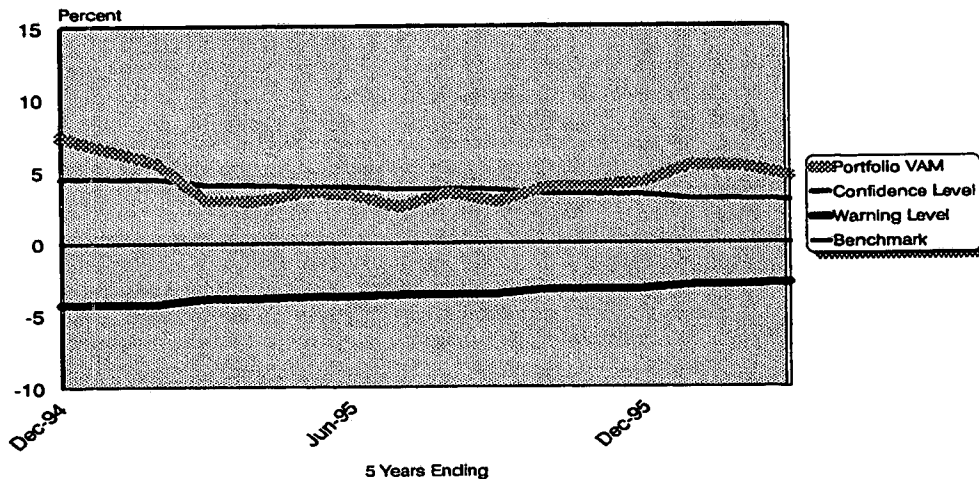
Quantitative Evaluation

	Actual	Benchmark
Last Quarter	4.4%	2.9%
Last 1 year	16.4	12.5
Last 2 years	8.7	9.3
Last 3 years	N/A	N/A
Last 4 years	N/A	N/A
Last 5 years	N/A	N/A
Since Inception (11/93)	11.2%	8.1%

Recommendations

No action recommended.

MARATHON ASSET MANAGEMENT
 Rolling Five Year Time Periods



Note: Shaded area includes performance prior to managing SBI account. Graph uses 80/20 confidence interval.

ROWE PRICE-FLEMING INTERNATIONAL, INC.
 Period Ending 3/31/96

Portfolio Manager: Martin Wade

Assets Under Management: \$292,140,567

Investment Philosophy

Rowe Price-Fleming (RPF) believes that world stock markets are segmented. The firm attempts to add value by identifying and exploiting the resulting pricing inefficiencies. In addition, they believe that growth is frequently under priced in the world markets. RPF establishes its economic outlook based largely on interest rate trends and earnings momentum. The portfolio management team then assesses the country, industry and currency profile for the portfolio. Within this framework, stock selection is the responsibility of regional portfolio managers. Stocks are selected using fundamental analysis that emphasizes companies with above-market earnings growth at reasonable valuations. Information derived from the stock selection process is a key factor in country allocation as well.

**Qualitative Evaluation
 (reported by exception)**

Exceptional strengths are:

- Extensive securities research process.
- Successful investment approach which has been consistently applied over a number of market cycles.
- Familiarity with the needs of large institutional clients.

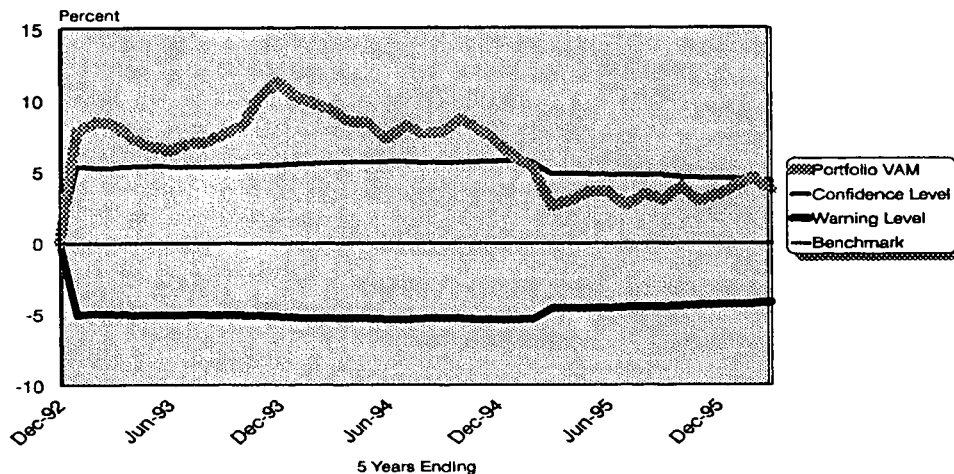
Quantitative Evaluation

	Actual	Benchmark
Last Quarter	5.0%	2.9%
Last 1 year	19.1	12.5
Last 2 years	10.0	9.3
Last 3 years	N/A	N/A
Last 4 years	N/A	N/A
Last 5 years	N/A	N/A
Since Inception (11/93)	10.3%	8.1%

Recommendations

No action recommended.

ROWE PRICE-FLEMING
 Rolling Five Year Time Periods



Note: Shaded area includes performance prior to managing SBI account. Graph uses 80/20 confidence interval.

SCUDDER, STEVENS & CLARK
 Period Ending 3/31/96

Portfolio Manager: Nicholas Bratt

Assets Under Management: \$196,031,629

Investment Philosophy

Scudder believes that successful international investing requires knowledge of each country's economy, political environment and financial market obtained through continuous and thorough research of individual markets and securities. The investment process focuses on three areas: country analysis, global themes and unique situations. Ideas from all three areas are integrated into Scudder's research universe. Using their own internal research, the firm seeks companies with potential for earnings and dividend growth, strong or improving balance sheets, superior management, conservative accounting practices and dominant position in growing industries.

**Qualitative Evaluation
 (reported by exception)**

Exceptional strengths are:

- Strong leadership.
- Extensive securities research capabilities.
- Successful investment approach which has been consistently applied over a number of market cycles.

Current concerns are:

- Growth plan appears aggressive.
- Staffing and organizational changes are being made in response to growth.

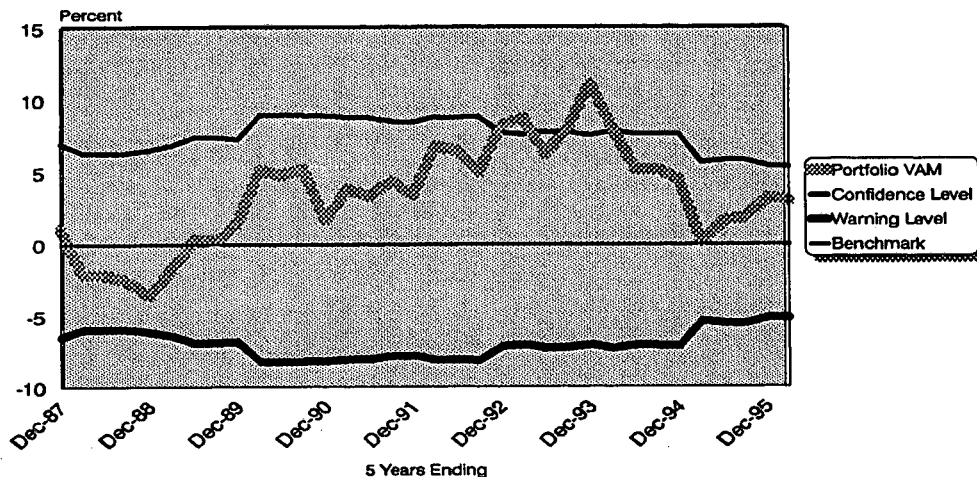
Quantitative Evaluation

	Actual	Benchmark
Last Quarter	6.5%	2.9%
Last 1 year	24.8	12.5
Last 2 years	12.3	9.3
Last 3 years	N/A	N/A
Last 4 years	N/A	N/A
Last 5 years	N/A	N/A
Since Inception (11/93)	10.7%	8.1%

Recommendations

No action recommended.

SCUDDER, STEVENS & CLARK
 Rolling Five Year Time Periods



Note: Shaded area includes performance prior to managing SBI account. Graph uses 80/20 confidence interval. Uses quarterly returns. Monthly composite returns prior to the inception of the SBI account are unavailable.

TEMPLETON INVESTMENT COUNSEL, INC.
 Period Ending 3/31/96

Portfolio Manager: Jim Chaney

Assets Under Management: \$198,494,408

Investment Philosophy

Templeton's goal is to identify those companies selling at the greatest discount to future intrinsic value. The firm takes a long-term approach to investing and believes that, over time, markets are efficient and patience will reward those who have identified undervalued stocks. Stock selection dominates Templeton's investment approach; country, sector and industry weightings are a residual of the stock selection process. Stock ideas are obtained from a worldwide network of research sources and screens of their own global database. From this preliminary list, analysts conduct fundamental analysis to distinguish a "cheap" stock from a "bargain." Templeton seeks stocks that are cheap relative to their own price history, their global industry and their domestic market. Each stock on the resulting "bargain list" has established buy and sell price targets and is purchased and sold accordingly.

**Qualitative Evaluation
 (reported by exception)**

Exceptional strengths are:

- Extensive securities research process.
- Successful investment approach which has been consistently applied over a number of market cycles.

Current concerns are:

- Growth plan appears aggressive.
- Staff has been expanded significantly over the last two years.

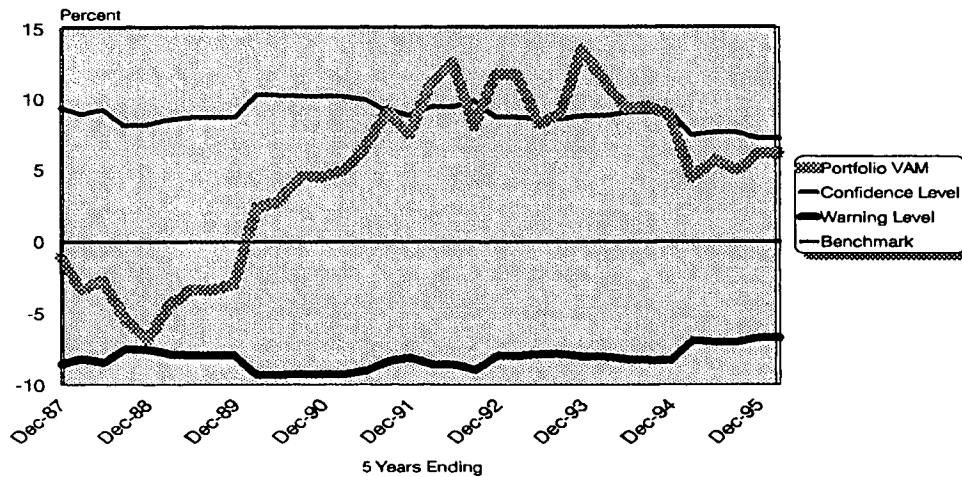
Quantitative Evaluation

	Actual	Benchmark
Last Quarter	4.8%	2.9%
Last 1 year	21.4	12.5
Last 2 years	12.3	9.3
Last 3 years	N/A	N/A
Last 4 years	N/A	N/A
Last 5 years	N/A	N/A
Since Inception (11/93)	11.4%	8.1%

Recommendations

No action recommended.

TEMPLETON INVESTMENT COUNSEL, INC.
 Rolling Five Year Time Periods



Note: Shaded area includes performance prior to managing SBI account. Graph uses 80/20 confidence interval. Uses quarterly returns. Monthly composite returns prior to the inception of the SBI account are unavailable.

Tab G

COMMITTEE REPORT

DATE: May 28, 1996

TO: Members, State Board of Investment
Members, Investment Advisory Council

FROM: **Alternative Investment Committee**

The Alternative Investment Committee met during the quarter to review the following information and action items:

- Review of current strategy.
- Results of a review session with an existing private equity manager, Coral Group.
- Additional investment for the Basic Retirement Funds with an existing private equity manager, KKR.
- Additional investment for the Basic Retirement Funds with an existing private equity manager, Golder Thoma.
- Investment for the Post Retirement Fund with a new real estate manager, Starwood Capital.

Board action is requested on the last three (3) items.

INFORMATION ITEMS:

1) Review of current strategy.

To increase overall portfolio diversification, 15% of the Basic Retirement Funds and 5% of the Post Retirement Fund are allocated to alternative investments. Alternative investments include real estate, private equity and resource investments where Minnesota State Board of Investment (SBI) participation is limited to commingled funds or other pooled vehicles. A chart summarizing the Board's current commitments is attached (see Attachments A and B).

Basic Funds

- The real estate investment strategy calls for the establishment and maintenance of a broadly diversified real estate portfolio comprised of investments that provide overall diversification by property type and location. The main component of this portfolio consists of investments in diversified open-end and closed-end commingled funds. The remaining portion of the portfolio can include investments in less diversified, more focused (specialty) commingled funds. Currently, the SBI has committed \$616 million to twenty-one (21) commingled real estate funds.
- The private equity investment strategy is to establish and maintain a broadly diversified private equity portfolio comprised of investments that provide diversification by industry type, stage of corporate development and location. To date, the SBI has committed to thirty (30) commingled private equity funds for a total commitment of \$923 million.
- The strategy for resource investment requires that investment be made in resource investment vehicles that are specifically designed for institutional investors to provide an inflation hedge and additional diversification. Individual resource investments will include proved producing oil and gas properties, royalties and other investments that are diversified geographically and by type. Currently, the SBI has committed \$138 million to eight (8) commingled oil and gas funds.

Post Fund

- The Post Fund assets allocated to alternative investments will be invested separately from the Basic Funds' alternative investments to assure that returns are accounted for appropriately. Because the Post Fund invests the retired employee's pension assets, an allocation to yield oriented alternative investments will be emphasized. The Basic Retirement Funds' invest the active employees' pension assets and have less concern regarding the current yield for their alternative investments. Since 1994, the SBI has committed \$175 million to six (6) yield oriented private equity funds for the Post Fund.

2) Results of review session with an existing manager.

During the quarter, staff held a review session with one of the SBI's private equity managers, Coral Group.

The meeting went well and produced no major surprises.

A summary of the review session is included as **Attachment C** of this Committee Report.

ACTION ITEMS:

- 1) Additional Investment for the Basic Retirement Funds with an existing private equity manager, Kohlberg Kravis Roberts, & Co. L.P. (KKR), in KKR 1996 Fund.**

KKR is seeking investors in a new \$4-5 billion private equity fund, KKR 1996 Fund. Through various predecessor funds, KKR has invested in excess of \$10 billion in equity capital in more than 50 transactions. Similar to prior funds, KKR 1996 fund will acquire companies and make investments that are larger than those typically pursued by other private equity funds.

More information on the KKR 1996 fund is included as **Attachment D**.

RECOMMENDATION:

The Committee recommends that the SBI authorize the Executive Director, with assistance from the SBI's legal counsel, to negotiate and execute a commitment of up to \$200 million or 20%, whichever is less, in KKR 1996 fund. This commitment will be allocated to the Basic Retirement Funds.

Approval by the SBI of this potential commitment is not intended to be, and does not constitute in any way, a binding or legal agreement or impose any legal obligations on the State Board of Investment and neither the State of Minnesota, the State Board of Investment or its Executive Director have any liability for reliance by KKR upon this approval. Until a formal agreement is executed by the Executive Director on behalf of the SBI, further due diligence and negotiations may result in the imposition of additional terms and conditions on KKR or reduction or termination of the commitment.

- 2) Additional Investment for the Basic Retirement Funds with an existing private equity manager, Golder, Thoma, Cressey, Rauner, Inc. (Golder Thoma), in Golder, Thoma, Cressey, Rauner Fund V.**

Golder Thoma is seeking investors in a new \$500 million private equity fund, Golder Thoma Fund V. This Fund is the fifth fund raised and managed by Golder Thoma. Since 1980, the Golder Thoma principals have invested \$707 million in four different private equity funds. Golder Thoma Fund V will focus, like prior funds, on opportunities to create large businesses in previously fragmented industries.

More information on the Golder Thoma Fund V is included as **Attachment E**.

RECOMMENDATION:

The Committee recommends that the SBI authorize the Executive Director, with assistance from the SBI's legal counsel, to negotiate and execute a commitment of up to \$32 million or 20%, whichever is less, in Golder, Thoma, Cressey, Rauner Fund V. This commitment will be allocated to the Basic Retirement Funds.

Approval by the SBI of this potential commitment is not intended to be, and does not constitute in any way, a binding or legal agreement or impose any legal obligations on the State Board of Investment and neither the State of Minnesota, the State Board of Investment or its Executive Director have any liability for reliance by Golder Thoma upon this approval. Until a formal agreement is executed by the Executive Director on behalf of the SBI, further due diligence and negotiations may result in the imposition of additional terms and conditions on Golder Thoma or reduction or termination of the commitment.

- 3) Investment for the Post Retirement Fund with a new real estate manager, Starwood Capital Group L.L.C. (Starwood), in Starwood Opportunity Fund IV.**

Starwood is seeking investors in a new \$750 million real estate fund, Starwood Opportunity Fund IV. This Fund is one of a series of funds raised and managed by Starwood. Since 1991, the Starwood principals have invested over \$700 million in real estate equity and real estate mezzanine investments. Starwood Opportunity Fund IV fund will target a majority of its capital towards high-yielding real estate-related mezzanine debt investments which satisfy the yield orientation of Post Fund alternative investments.

More information on Starwood Opportunity Fund IV is included as **Attachment F**.

RECOMMENDATION:

The Committee recommends that the SBI authorize the Executive Director, with assistance from the SBI's legal counsel, to negotiate and execute a commitment of up to \$50 million or 20%, whichever is less, in Starwood Opportunity Fund IV. This commitment will be allocated to the Post Retirement Fund.

Approval by the SBI of this potential commitment is not intended to be, and does not constitute in any way, a binding or legal agreement or impose any legal obligations on the State Board of Investment and neither the State of Minnesota, the State Board of Investment or its Executive Director have any liability for reliance by Starwood upon this approval. Until a formal agreement is executed by the Executive Director on behalf of the SBI, further due diligence and negotiations may result in the imposition of additional terms and conditions on Starwood or reduction or termination of the commitment.

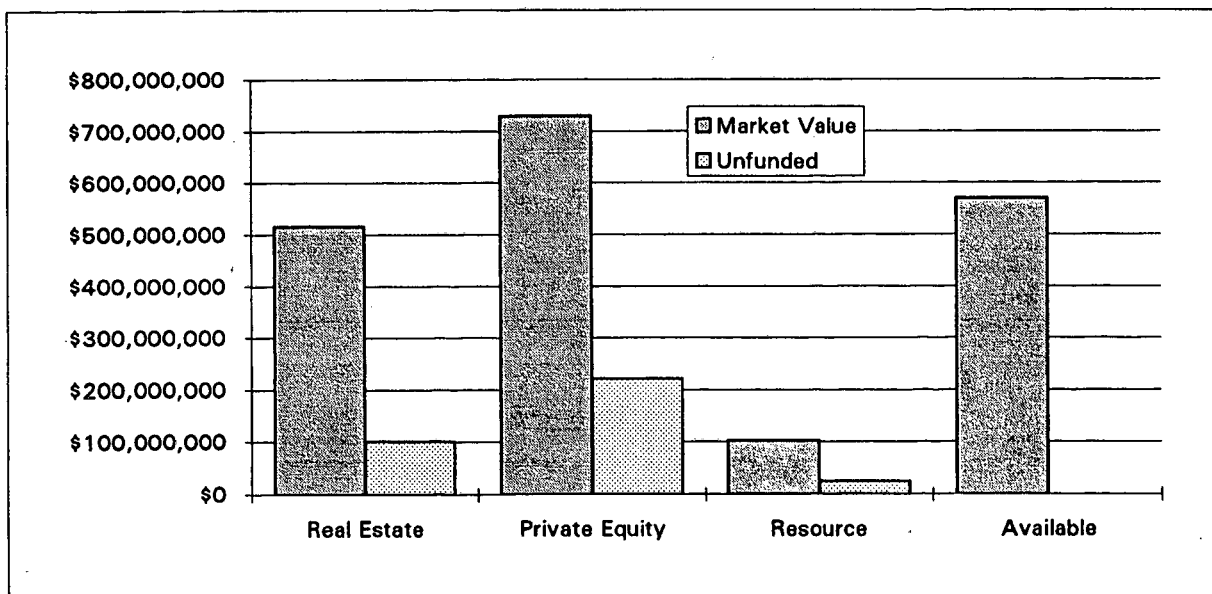
ATTACHMENT A

Minnesota State Board of Investment
Alternative Investments Basic Retirement Funds
 March 31, 1996

Market Value of Basic Retirement Fund (Basic)	\$12,797,112,158
Amount Available For Investment	\$570,403,014

	<i>Current Level</i>	<i>Target Level</i>	<i>Difference</i>
Market Value	\$1,349,163,809	\$1,919,566,824	\$570,403,014
MV + Unfunded	\$1,696,484,395	\$2,559,422,432	\$862,938,036

Asset Class	Market Value	Unfunded Commitment	Total
Real estate	\$516,047,085 4.0%	\$102,305,649 0.8%	\$618,352,734 4.8%
Private Equity	\$729,935,157 5.7%	\$220,480,117 1.7%	\$950,415,274 7.4%
Resource	\$103,181,568 0.8%	\$24,534,820 0.2%	\$127,716,388 1.0%
Total	\$1,349,163,809 10.5%	\$347,320,586 2.7%	\$1,696,484,395 13.3%



STATE OF MINNESOTA
ALTERNATIVE INVESTMENTS - BASIC FUNDS
March 31, 1996

	INCEPTION DATE	TOTAL COMMITMENT	FUNDED COMMITMENT	MARKET VALUE	DISTRIBUTIONS	UNFUNDED COMMITMENT	IRR (%)	PERIOD (YEARS)
REAL ESTATE								
AETNA 013420	Sep-94	2,376,529	2,376,529	3,018,896	0	0	9.08	1.5
AETNA 007367	Apr-82	40,000,000	40,000,000	68,133,863	0	0	4.26	13.9
AEW III	Sep-85	20,000,000	20,000,000	15,943,136	5,065,395	0	0.49	10.6
AEW IV	Sep-86	17,400,000	15,000,000	3,991,722	829	2,400,000	-13.26	9.5
AEW V	Dec-87	15,000,000	15,000,000	9,241,810	2,280,980	0	-3.33	8.3
AMERICAN REPUBLIC COLONY INVESTORS II EQUITABLE	Feb-90	1	1	1	0	0	0.00	6.2
FIRST ASSET REALTY	Apr-95	40,000,000	9,655,098	9,005,800	132,104	30,344,904	-18.48	1.0
HEITMAN I	Oct-81	40,000,000	40,000,000	72,809,244	0	0	4.58	14.5
HEITMAN II	Apr-94	916,185	916,185	740,941	211,639	0	2.04	1.9
HEITMAN III	Aug-84	20,000,000	20,000,000	9,575,151	12,326,998	0	1.36	11.6
HEITMAN V	Nov-85	30,000,000	30,000,000	20,650,893	15,737,884	0	2.56	10.4
LASALLE	Jan-87	20,000,000	20,000,000	11,765,524	8,812,360	0	0.42	9.2
REALTY ASSOCIATES FUND III	Dec-91	20,000,000	20,000,000	22,000,057	3,134,906	0	6.78	4.3
RREEF	Sep-91	15,000,000	14,644,401	15,027,372	1,414,298	355,599	5.84	4.5
TCW III	Jun-94	40,000,000	36,000,000	37,341,310	9,389,515	4,000,000	9.93	1.8
TCW IV	May-84	75,000,000	75,000,000	63,292,372	34,237,012	0	3.09	11.9
ZELL/MERRILL LYNCH II	Aug-85	40,000,000	40,000,000	29,142,643	13,419,745	0	0.74	10.7
ZELL/MERRILL LYNCH III	Nov-86	30,000,000	30,000,000	21,853,951	3,424,813	0	-2.14	9.4
ZELL/MERRILL LYNCH IV	Nov-91	50,000,000	40,388,854	57,673,200	2,585,484	9,611,146	14.56	4.3
	Jan-94	50,000,000	44,406,000	44,839,200	755,163	5,594,000	2.93	2.2
	Apr-96	50,000,000	0	0	0	50,000,000	0.00	0.0
TOTAL REAL ESTATE		615,692,715	513,387,066	516,047,085	112,928,925	102,305,649		

PRIVATE EQUITY								
ALLIED	Sep-85	5,000,000	5,000,000	1,901,260	4,049,543	0	3.05	10.5
BANK FUND III TRUST	Oct-92	20,000,000	19,000,000	21,521,568	1,421,758	1,000,000	10.63	3.4
BANK FUND IV TRUST	Feb-96	25,000,000	1,931,250	1,931,250	0	23,068,750	0.00	0.1
BLACKSTONE PARTNERS II	Nov-93	50,000,000	17,667,027	21,529,000	19,080,810	32,332,973	80.89	2.4
BRINSON	May-88	5,000,000	5,000,000	1,978,927	6,028,632	0	10.83	7.9
BRINSON II	Nov-90	20,000,000	16,411,018	7,820,895	19,340,008	3,588,982	24.28	5.3
CHURCHILL CAPITAL PARTNERS II	Oct-92	20,000,000	15,400,000	11,847,020	5,633,377	4,600,000	8.72	3.4
CORAL PARTNERS I SUPERIOR	Jun-86	7,011,923	7,011,923	3,465,967	4,685,814	0	2.88	9.8
CORAL PARTNERS II	Jul-90	10,000,000	8,500,000	10,676,672	1,579,857	1,500,000	6.83	5.7
CORAL PARTNERS IV	Jul-94	15,000,000	4,500,000	4,803,248	0	10,500,000	5.30	1.7
DSV	Apr-85	10,000,000	10,000,000	9,179,581	6,243,827	0	4.57	11.0
FIRST CENTURY	Dec-84	10,000,000	10,000,000	5,819,350	9,410,459	0	8.39	11.3
GOLDER THOMA III	Oct-87	14,000,000	14,000,000	22,507,744	14,924,875	0	25.12	8.4
GOLDER THOMA IV	Jan-94	20,000,000	12,200,000	11,969,489	463,026	7,800,000	1.47	2.2
HELLMAN & FRIEDMAN III	Sep-94	40,000,000	9,559,530	9,073,097	0	30,440,470	-7.98	1.5
IAI VENTURES I	Mar-91	1,146,890	1,146,890	434,078	1,122,037	0	16.47	5.1
IMR PARTNERSHIP	Aug-92	15,000,000	1,524,900	1,279,217	38,997	13,475,100	-6.10	3.7
INMAN BOWMAN	Jun-85	7,500,000	7,500,000	2,564,519	6,991,810	0	3.45	10.8
KKR I	Jun-84	25,000,000	25,000,000	33,822,523	91,327,655	0	28.93	11.8
KKR II	Apr-86	18,365,339	18,365,339	79,469,755	57,855,607	0	26.77	10.0
KKR III	Nov-87	145,950,000	145,950,000	252,305,133	123,582,727	0	11.70	8.4
KKR IV	Dec-93	150,000,000	94,192,910	104,851,071	30,681,293	55,807,090	5.99	2.3
MATRIX II	Aug-85	10,000,000	10,000,000	2,139,883	18,693,726	0	13.62	10.6
MATRIX III	May-90	10,000,000	10,000,000	13,950,705	47,495,790	0	73.07	5.9
NORTHWEST	Jan-84	10,000,000	10,000,000	2,000,344	12,793,949	0	5.23	12.2
SUMMIT I	Dec-84	10,000,000	10,000,000	752,783	19,405,571	0	13.12	11.3
SUMMIT II	May-88	30,000,000	28,500,000	6,986,222	56,664,495	1,500,000	27.77	7.9
T. ROWE PRICE	Nov-87	139,049,382	139,049,382	35,844,833	112,030,377	0	11.57	8.4
WARBURG PINCUS	Dec-94	50,000,000	17,250,000	16,127,000	83,650	32,750,000	-9.56	1.2
ZELL/CHILMARK	Jul-90	30,000,000	27,883,248	31,382,048	9,731,441	2,116,752	7.24	5.7
TOTAL PRIVATE EQUITY		923,023,534	702,543,417	729,935,157	681,360,710	220,480,117		

RESOURCES								
AMGO I	Sep-81	15,000,000	15,000,000	7,531,768	3,614,536	0	-2.61	14.5
AMGO II	Feb-83	7,000,000	7,000,000	8,609,559	2,325,453	0	4.54	13.2
AMGO IV	May-88	12,300,000	12,300,000	15,673,581	7,571,921	0	10.77	7.9
AMGO V	May-90	16,800,000	16,408,222	26,870,209	8,729,562	391,778	16.46	5.9
APACHE III	Dec-86	30,000,000	30,000,000	7,390,179	38,866,786	0	11.52	9.3
MORGAN OIL & GAS	Aug-88	15,000,000	15,000,000	13,936,323	1,664,933	0	0.73	7.6
SIMMONS OFS II	Aug-91	17,000,000	14,547,829	19,805,920	838,169	2,452,171	11.48	4.7
SIMMONS OFS III	Jul-95	25,000,000	3,309,129	3,364,029	0	21,690,871	-7.27	0.8
TOTAL RESOURCES		138,100,000	113,565,180	103,181,568	63,611,360	24,534,820		
TOTAL PORTFOLIO		1,676,816,249	1,329,495,663	1,349,163,809	857,900,995	347,320,586		

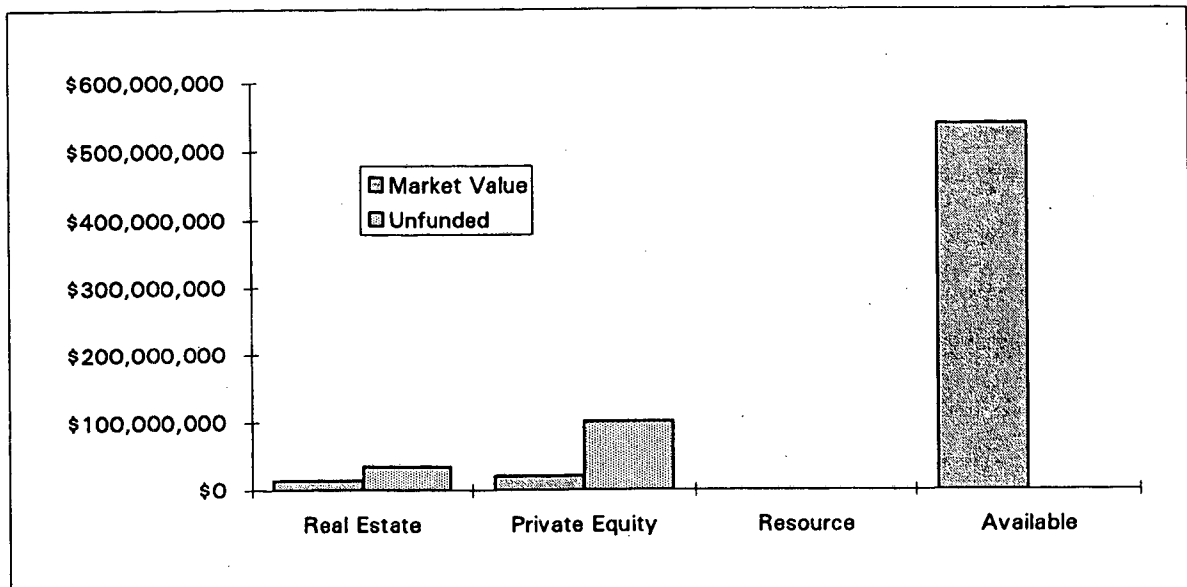
ATTACHMENT B

Minnesota State Board of Investment
Alternative Investments Post Retirement Fund
 March 31, 1996

Market Value of Post Retirement Fund (Post)	\$11,496,951,958
Amount Available For Investment	\$539,631,257

	<i>Current Level</i>	<i>Target Level</i>	<i>Difference</i>
Market Value	\$35,166,341	\$574,797,598	\$539,631,257
MV + Unfunded	\$171,062,819	\$1,149,595,196	\$978,532,377

Asset Class	Market Value	Unfunded Commitment	Total
Real estate	\$14,392,342 0.1%	\$34,781,211 0.3%	\$49,173,553 0.4%
Private Equity	\$20,773,999 0.2%	\$101,115,267 0.8%	\$121,889,266 1.0%
Resource	\$0 0.0%	\$0 0.0%	\$0 0.0%
Total	\$35,166,341 0.3%	\$135,896,478 1.1%	\$171,062,819 1.3%



STATE OF MINNESOTA
ALTERNATIVE INVESTMENTS - POST FUND
March 31, 1996

	INCEPTION DATE	TOTAL COMMITMENT	FUNDED COMMITMENT	MARKET VALUE	DISTRIBUTIONS	UNFUNDED COMMITMENT	IRR (%)	PERIOD (YEARS)
REAL ESTATE								
CB COMMERCIAL MTG FUND II	Jul-95	10,000,000	5,563,693	5,386,542	232,980	4,436,307	2.97	0.6
COLONY INVESTORS II	Dec-94	40,000,000	9,655,096	9,005,800	132,104	30,344,904	-18.48	1.0
TOTAL REAL ESTATE		50,000,000	15,218,789	14,392,342	365,084	34,781,211		
PRIVATE EQUITY								
CITICORP MEZZANINE	Dec-94	40,000,000	11,843,067	9,845,646	3,236,113	28,156,934	12.89	1.2
CRESCENT / TCW MEZZANINE	Apr-96	40,000,000	0	0	0	40,000,000	0.00	0.0
KLEINWORT BENSON	Jul-95	25,000,000	1,041,667	1,041,667	0	23,958,333	0.00	0.5
SUMMIT SUB-DEBT FUND	Mar-94	20,000,000	11,000,000	9,886,686	3,777,253	9,000,000	28.01	2.0
TOTAL PRIVATE EQUITY		125,000,000	23,884,733	20,773,999	7,013,366	101,115,267		
RESOURCES								
TOTAL RESOURCES		0	0	0	0	0		
TOTAL PORTFOLIO		175,000,000	39,103,522	35,166,341	7,378,450	135,896,478		

ATTACHMENT C

REVIEW SUMMARY CORAL VENTURE CAPITAL GROUP MAY 8, 1996

MANAGER REPRESENTATIVES: Yuval Almog, Linda Watchmaker

SBI ASSETS UNDER MANAGEMENT: \$18,945,885

BACKGROUND AND DESCRIPTION:

The Coral Group Inc. comprised the professional staff of IAI Venture Capital Group prior to the spinout of that group from Investment Advisors, Inc. in the fall of 1993. The SBI has investments in four funds managed by the Coral Group Inc. The first fund, IAI Venture Partners I, is a \$50 million venture capital limited partnership that was acquired by the SBI in a fire and police fund consolidation in 1991. It was formed in 1983 with an eleven year term which now has been extended 2 years. The second fund, Coral Partners I - Superior is a \$36 million venture capital limited partnership that was formed in 1986 and has an eleven year term. Coral Partners II, the third fund, is a \$63 million venture capital limited partnership which was formed in 1990 and has a ten year term. The fourth fund, Coral Partners IV is a \$78 million venture capital limited partnership that was formed in 1994 and has a ten year term. All four funds diversify nationally but emphasize Minnesota-based investments.

QUALITATIVE EVALUATION:

IAI Venture Partners and Coral Partners I are currently in the liquidation phase of their term and the General Partner expects them to achieve projected net annualized IRR's (internal rates of return) of 8-10% and 12-15%, respectively.

Coral II is currently in a fully invested/build value stage. It is anticipated that Coral II will achieve a projected net annualized IRR (internal rate of return) of 25% over its term.

Coral IV is currently in an invest/build value stage and has drawdown approximately 30% of its committed capital for investments. The initial investment pace for Coral Partners IV has been ahead of plan with one to three additional investments planned for the remainder of 1996. At this time it is too early to tell what the Coral IV's ultimate IRR will be.

The Coral Funds General Partner is expecting significant portfolio gains over the next year as several portfolio companies are in the process of undergoing initial public offerings.

The Coral Group recently hired Bill Baumel as an investment associate. Bill had been with Brinson Partners Private Equity Group prior to his joining Coral in December 1995.

QUANTITATIVE EVALUATION:

	IAI I**	CORAL I	CORAL II	CORAL IV
COMMITMENT *	\$1.1	\$7.0	\$10.0	\$15.0
FUNDED COMMITMENT *	\$1.1	\$7.0	\$8.5	\$4.5
MARKET VALUE OF FUNDED COMMITMENT *	\$0.4	\$3.5	\$10.7	\$4.8
CASH DISTRIBUTIONS *	\$1.1	\$4.7	\$1.6	\$0
INCEPTION DATE(S)	March 1991	June 1986	July 1990	July 1994
INTERNAL RATE OF RETURN (IRR): (annualized, since inception)	16.5%	2.9%	6.8%	5.3%

* All dollars in millions

** Received from police and fire consolidations

DIVERSIFICATION PROFILE

LOCATION	PERCENTAGE
Minnesota	33%
West	41
Midwest	17
East	<u>8</u>
	100%

STAGE OF DEVELOPMENT	PERCENTAGE
Seed	6%
Development	27
Introduction	22
Expansion	2
Public	<u>43</u>
	100%

INDUSTRY	PERCENTAGE
Technical	63%
Healthcare	32
Consumer	<u>5</u>
	100%

ATTACHMENT D

PRIVATE EQUITY MANAGER SUMMARY PROFILE

I. *Background Data*

Name of Fund: KKR 1996 Fund, L.P.

Type of Fund: Private Equity Limited Partnership

Total Fund Size: \$3.0-5.0 billion

Fund Manager: Kohlberg, Kravis, Roberts & Co.
9 West 57th Street
Suite 4200
New York, NY 10019
Phone (212) 750-8300
Fax (212) 750-0003

Manager Contact: George Roberts, Perry Golkin

II. *Organization & Staff*

Kohlberg Kravis Roberts & Co. ("KKR") was founded in 1976 by Jerome Kohlberg, Henry Kravis and George Roberts.¹ Prior to establishing KKR, the three founding principals were partners in the corporate finance department of Bear Stearns & Co.

KKR has been the largest and most active participant in the buyout market since the mid 1970s. The firm has invested, on behalf of itself and its investors, over \$10 billion of equity capital in more than 50 transactions. The total financing raised by KKR (including equity) for these management buyouts and other investments exceeds \$83 billion.

KKR employs 95 individuals, including 33 professionals who are responsible for investment transactions; accounting and tax matters; and administering the various KKR funds.

III. *Investment Strategy*

KKR specializes in management buyouts and is one of only a few organizations that specialize in larger transactions. The 1996 Fund will seek to provide investors with long-term capital appreciation through the acquisition of companies and by making other selective equity and equity-related securities. Typically, KKR utilizes debt when appropriate to finance a significant portion of a transaction, with a view toward enhancing

¹ Mr. Kohlberg left KKR in 1987.

the rates of return received by its investor group. The Fund will not engage in hostile transactions.

IV. Investment Performance

Fund performance as of March 31, 1996 is shown below. The SBI has invested in all of the listed funds.

Fund Name	Inception Date	Total Equity Commitments	SBI Commitment	IRR from Inception
KKR 1984 Fund	6/84	\$1.00 billion	\$ 25.0 million	28.93%
KKR 1986 Fund	4/86	\$0.67 billion	\$ 18.4 million	26.77%
KKR 1987 Fund	11/87	\$5.60 billion	\$146.0 million	11.70%
KKR 1993 Fund	12/93	\$1.95 billion	\$150.0 million	5.99%

V. General Partner's Investment

The General Partner, directly or through one or more affiliates, will commit \$125 million to the Fund.

VI. Term

The Investment Period of the Fund will be six years. The General Partner must sell or distribute the securities of each investment no later than the twelfth anniversary of the date such investment was made.

VII. Takedown Schedule

Upon at least ten business days prior written notice, capital contributions will be called from Limited Partners as needed to make investments and to pay management fees and expenses payable by the Fund.

VIII. Management Fee

During the Investment Period (i.e., years one through six), the Limited Partners will make capital contributions to the Fund to enable the Fund to pay KKR an annual management fee in an amount equal to the sum of 1.5% of the first \$3 billion of committed capital, plus 0.75% of the next \$1 billion of such capital, plus 0.50% of all capital committed thereafter

For years seven through ten, the management fee will be payable quarterly at an annual rate equal to the weighted average of 0.75% of the cost basis of capital invested (or committed to be invested) at the end of the Investment Period up to the first \$3 billion, 0.375% for the next \$1 billion of such capital and 0.25% for all such capital committed thereafter.

For years 11-14, the management fee will be payable quarterly at an annual rate equal to the weighted average of 0.50% of the cost basis of capital invested (or committed to be invested) at the end of the Investment Period up to the first \$3 billion, 0.25% for the next \$1 billion of such capital and 0.1667% for all such capital thereafter.

For the remaining term of the Fund (years 14-18), the management fee will be payable quarterly at an annual rate equal to the weighted average of 0.25% of the cost basis of capital invested (or committed to be invested) at the end of the Investment Period up to the first \$3 billion, 0.125% for the next \$1 billion of such capital and 0.0833% for all such capital thereafter.

IX. Management Fee Credit

KKR will credit 80% of the amount of transaction fees and monitoring fees (net of expenses) in excess of \$6 million per portfolio company against payment by the Fund of future management fees. KKR also will credit 80% of the amount of any "break up" or similar fees received by KKR (net of expenses) against payment by the Fund of future management fees.

X. Investment Restrictions

The Fund will invest no more than 25% of the aggregate capital commitments of the Partners in a single portfolio company, except that the Fund may invest up to 30% of the aggregate capital commitments of the Partners in any single portfolio company, but in such event no other investment in any single portfolio company may exceed 20% of the aggregate capital commitments of the Partners.

The Fund will invest no more than 20% of the aggregate capital commitments of the Partners in portfolio companies which are headquartered outside the United States or Canada and which have the majority of their assets and revenues outside the United States and Canada.

XI. Bridge Financing

The Fund may temporarily provide financing to companies in order to facilitate permanent investments therein by the Fund. Bridge financings refinanced within 18 months will be restored to the Partners' unused commitments and will be available to be recalled for future investments during the Investment Period.

XII. Distributions

The General Partner intends to distribute all cash proceeds from dispositions of portfolio company securities, net of expenses and appropriate reserves. The Fund may reinvest, rather than distribute, all or any portion of such cash proceeds in the portfolio company, but only if such reinvestment occurs within three years of the date of the initial investment in the portfolio company and (i) the reinvestment was contemplated in connection with the initial investment, or (ii) the General Partner determines that such reinvestment is in the best interests of the Fund and the Fund is committed to make such reinvestment at the time of receipt of the cash proceeds.

Generally, for dispositions of securities of a portfolio company:

- First to all Partners in proportion to their participation in such investment until the proceeds equal the aggregate of (i) the cost basis and the amount of capital contributions from the Partners used to pay Fund expenses allocable to the securities so disposed of (that have not been recouped from prior distributions made after a writedown with respect to such securities, or otherwise recouped), (ii) the amount of realized losses on any Fund investment allocated to such Partners (that has not been previously recouped) and (iii) the writedown amount for securities of any portfolio company,
- thereafter 80% to the Partners in proportion to their participation in such investment and 20% to the General Partner;

Generally, for dividend and interest income (except as otherwise provided below):

- First to all Partners in proportion to their participation in the investment until the proceeds equal (i) the amount of capital contributions from the Partners used to pay Fund expenses allocable to the investment that produced such dividend or interest income (that has not been previously recouped), (ii) the amount of realized losses on any Fund investment allocated to such Partners (that has not been previously recouped) and (iii) the writedown amount for securities of any portfolio company,
- thereafter 80% to the Partners in proportion to their participation in such investment and 20% to the General Partner.

Dividend and interest income with respect to bridge financings, and interest income with respect to cash held short term prior to investment or distribution, will be distributed to all Partners pro rata to their participation in such investments.

XII. Exclusion from Certain Investments

A Limited Partner will not be obligated to contribute capital toward any investment if such investment is, in the opinion of counsel reasonably satisfactory to the General Partner,

reasonably likely to be illegal for such Limited Partner. A tax-exempt limited partner will not be obligated to contribute capital to the extent such contribution would be used to make an investment which the General Partner has notified the Limited Partners is likely to generate unrelated business taxable income. A Limited Partner will not be permitted to contribute capital toward any investment if the General Partner determines that such contribution is reasonably likely to result in a violation of law or have certain material adverse effects on the Fund, any Partner or any portfolio company. An excused or excluded Limited Partner's capital commitment will not be reduced as a result of such excuse or exclusion.

ATTACHMENT E

PRIVATE EQUITY MANAGER SUMMARY PROFILE

I. Background Data

Name of Fund: Golder Thoma Cressey Rauner Fund V

Type of Fund: Private Equity Limited Partnership

Total Fund Size: \$500 million

Fund Manager: Golder, Thoma, Cressey, Rauner, Inc.
233 Wacker Drive
6100 Sears Tower
Chicago, IL 60606-6402
Phone (312) 382-2200
Fax (312) 382-2201

Manager Contact: Carl Thoma

II. Organization & Staff

Golder Thoma Cressey Rauner, Inc. (GTCR) was established in 1980 by Bryan Cressey, Stanley Golder and Carl Thoma when they left First Chicago Corporation's venture capital group. Mr. Golder was the president of the venture capital group and Messrs. Cressey and Thoma were senior executives.

GTCR's three active named principals (Mr. Golder reduced his involvement during Fund III) average eighteen years of private equity investment experience and have worked together for over fifteen years. GTCR's staff of seven principals, seven associates and fourteen administrative/support personnel carry on a nationwide investment program from an office located in Chicago.

III. Investment Strategy

GTCR's primary focus centers around consolidating investments within a fragmented industry. The industry consolidation method is both an investment process and a way to create additional value. The strategy involves making an investment at a much earlier stage than traditional venture capital and leveraged buyouts practices. It also involves proactively searching out under-valued and fragmented industry niches, excellent management teams and less competitive transactions. These three factors are then assembled by GTCR to create operating companies that can become major competitors in their industries. In this way, GTCR uses the industry consolidation process as a way to create, as opposed to merely transfer ownership of, valuable companies.

IV. Investment Performance

Previous fund performance as of March 31, 1996 is shown below. An asterisk (*) indicates a fund in which the SBI has invested capital.

Fund Name	Inception Date	Total Equity Commitments	SBI Commitment	IRR from Inception
GTCR Fund I	1980	\$60.0 million	N/A	31.0% #
GTCR Fund II	1984	\$100.0 million	N/A	19.17%
GTCR Fund III *	1987	\$235.0 million	\$14 million	25.1%
GTCR Fund IV *	1994	\$312.0 million	\$20 million	1.5%

Fund I is completed and all gains have been recognized.

V. General Partner's Investment

GTCR will invest approximately \$20 million in Fund V, in part as a Limited Partner and in part as General Partner, and will receive a corresponding ownership interest.

VI. Takedown Schedule

Each Limited Partner's commitment will be payable when called by GTCR. It is currently anticipated that no monies will be payable at closing.

VII. Management Fee

Fund V will pay to GTCR in advance on a quarterly basis, an annual management fee equal to 1.5% of committed capital in year one, 1.75% in year two, 2% in year three and 2.25% in years four through seven. During years eight through ten, the management fee will decrease 10% per year from the prior year's level.

Fund V will pay organizational expenses of up to \$500,000, the management fee, portfolio expenses, legal and accounting expenses, auditing expenses and extraordinary expenses such as litigation. GTCR will bear the normal expenses in managing the Fund, including salaries, rent, travel and other administrative expenses.

VIII. Term

Fund V will have a ten year initial term, with the General Partner having the option to extend the Fund for up to three additional one year terms to permit orderly dissolution, subject to a majority of the Limited Partners vetoing the extension.

IX. Distributions

Securities, income, gains, losses and expenses will generally be allocated 80% to the accounts of all Partners in proportion to their capital contributions and 20% to the account of GTCR. Short-term interest will be allocated according to capital accounts.

Proceeds from the sale of securities will be distributed:

- prior to the time that the Limited Partners have received distributions equal to their capital contributions, in proportion to the allocations set forth above. GTCR will not be entitled to receive any distribution (other than to pay taxes) unless the Limited Partners' fair value capital accounts (plus amounts previously distributed to Limited Partners) are at least 120% of the Limited Partners' capital contributions, and
- after the Limited Partners have received distributions equal to their capital contributions, or if the Limited Partners' fair market capital accounts are at least 120% of the Limited Partners' capital contributions, in proportion to capital accounts.

In no event will GTCR receive a distribution which would reduce its capital account below zero (other than to pay taxes).

XII. Other Funds

GTCR may raise a captive subordinated debt fund to co-invest with Fund V or other GTCR Funds within 12 months of closing Fund V. The Principals believe that this fund could assist in growing its companies while proving the subordinated debt fund's partners with an acceptable return. The subordinated debt fund should also enhance the return on investments made by Fund V.

ATTACHMENT F

REAL ESTATE MANAGER SUMMARY PROFILE

I. Background Data

Name of Fund: Starwood Opportunity Fund IV

Type of Fund: Real Estate Limited Partnership

Total Fund Size: \$750 million

Fund Manager: Starwood Capital Group, L.L.C
Three Pickwick Plaza
Suite 250
Greenwich CT. 06830
Phone (203) 861-2100
Fax (203) 861-2130

Manager Contact: Barry Sternlicht

II. Organization & Staff

Starwood Capital, Inc. incepted in 1991, is a real estate investment firm.

Starwood Capital employs twenty-nine individuals, seven of whom are principal investment and management professionals. Additionally, Starwood has formed an asset management subsidiary to oversee asset management and operations of real estate investments. The activities of Starwood Asset Management are controlled by Starwood and managed by Greystone Realty Corporation. Greystone is a wholly owned subsidiary of New York Life and currently manages over \$1 billion of properties nationwide.

The Fund will have a three-person Limited Partner Advisory Committee to advise the General Partner and resolve conflict of interest situations if they arise.

Starwood Fund IV will be one of a series of funds raised and managed by the General Partner. Previous funds are listed below:

Fund Name	Date Formed	Equity Capitalization
Starwood Opportunity Fund I	Feb 92	\$52 million
Starwood Opportunity Fund II	Nov 93	\$102 million
Starwood Mezzanine	Nov 94	\$220 million
Starwood Hotel Investors Trust	Jan 95	\$83 million
Starwood Westin	May 95	\$78 million
Other transactions	various	\$176 million

III. Investment Strategy

Generally, Starwood Fund IV is being organized to make equity and debt investments in real estate properties including rental apartment buildings, office properties, zoned residential land and other real properties located primarily in the United States. Areas of investment focus will include undervalued or distressed real estate, real estate in need of market repositioning and high yielding real estate-related debt instruments. In addition, the Partnership will focus on selected hotel debt investments and may make equity or debt investments in real estate-related businesses or companies, as well as in development opportunities.

In particular, the Partnership intends to target a significant amount of its capital toward high yielding, attractively structured, real estate-related mezzanine debt investments. With an anticipated \$300 billion of real estate loans rolling over between 1996 and 1998, and an increasingly conservative underwriting standard in place at most first mortgage lenders, many borrowers will require mezzanine financing to cover a projected funding gap at the time of refinancing. In addition, as both the size and complexity of real estate transactions continues to grow, the need for a mezzanine capital provider with both strong underwriting capabilities and transactional experience continues to increase. This combination of events has created an attractive investment opportunity for providing capital positioned between institutional senior financing and entrepreneurial equity in the capital structure.

In 1994, Starwood was among the first investors to identify a significant demand developing for mezzanine capital in the real estate markets and formed a \$220 million partnership, Starwood Mezzanine Investors L.P., to specifically target real estate mezzanine opportunities. With Starwood Mezzanine now almost fully invested, the General Partner believes that this sector currently offers some of the most compelling risk-adjusted returns in real estate, and that mezzanine investing capitalizes on the core strengths developed and demonstrated by Starwood over the past four years.

IV. Investment Performance

Previous fund performance as of December 31, 1995 is shown below.

Fund Name	Date Formed	Equity Capitalization	IRR From Inception
Starwood Opportunity Fund I	Feb 92	\$52 million	80%
Starwood Opportunity Fund II	Nov 93	\$102 million	17%
Starwood Mezzanine	Nov 94	\$220 million	12%
Starwood Hotel Investors Trust	Jan 95	\$83 million	87%
Starwood Westin	May 95	\$78 million	284%
Other transactions	various	\$176 million	60%

V. General Partners Investment

The greater of \$17.5 million or 3% of the Partnership's total contributed capital will be provided by the General Partner.

VI. Takedown Schedule

Commitments will be drawn down as needed with at least 10 days notice.

VII. Management Fee

The Partnership will pay to the General Partner semiannually in advance an annual management fee equal to 1.5% of the commitments during the commitment period (three years from final closing), and thereafter, 1.5% of the funded commitments. The management fee will commence as of the date of the initial closing regardless of when a Limited Partner is actually admitted.

The General Partner will be responsible for all expenses incurred for its own activities in connection with identifying and consummating Partnership investments and all other day-to-day expenses of the General Partner, including compensation of its employees. Fees and expenses of third parties and direct Partnership operating expenses will be paid by the Partnership including organizational and offering expenses incurred in the formation of the Partnership up to an amount equal to \$1 million.

In connection with an investment, the Partnership will generally retain Starwood Asset Management, L.L.C., an affiliate of the general Partner, as asset manager. In such event, this entity will be responsible for the day-to-day asset management or servicing of such investment and will be paid fees not exceeding third-party market rates for such services. Additionally, the Partnership may engage third parties to provide the services of trustees, servicers, property managers, paying agents or other services as necessary, the costs of which will be borne by the Partnership.

VIII. Term

The Fund will be established with an eight year life, unless extended, at the discretion of the General Partner, for up to two one year periods.

IX. Leverage

The Partnership intends, where appropriate, to employ leverage in order to enhance returns to the Partnership. Long term financing, on a portfolio-wide basis, may not exceed 80% of total property cost.

X. Distributions

The Partnership's net proceeds from all investments, including, but not limited to, net operating or capital proceeds from equity investments and net proceeds from debt investments, will be distributed in the following order of priority:

- (a) First, to provide all Partners with a 9% cumulative preferred return, compounded annually, on their unreturned Funded Commitments;
- (b) Second, to return the Partners their unreturned Funded Commitments;
- (c) Third, 50% to the Partners and 50% to the General Partner until such time as the general Partner has received under this paragraph 20% of the sum of the aggregate distributions made under paragraph (a) above and under this paragraph; and
- (d) Fourth, 80% to the Partners and 20% to the General Partner.

Tab H

COMMITTEE REPORT

DATE: May 28, 1996

TO: Members, State Board of Investment

FROM: Proxy Committee

At the March 1996 Board meeting, the Governor requested the Executive Director to provide the Board with background information concerning holdings in tobacco companies and tobacco industry issues.

The Executive Director provided the attached report to the Proxy Committee when it met on May 23, 1996. The Committee took no action at that time and is forwarding the entire report to the Board for its consideration.

**MINNESOTA
STATE
BOARD OF
INVESTMENT**



Board Members:

Governor
Arne H. Carlson

State Auditor
Judi Dutcher

State Treasurer
Michael A. McGrath

Secretary of State
Joan Anderson Growe

Attorney General
Hubert H. Humphrey III

Executive Director:

Howard J. Bicker

Suite 105, MEA Bldg.
55 Sherburne Avenue
St. Paul, MN 55155
(612)296-3328
FAX (612)296-9572

*An Equal Opportunity
Employer*

DATE: May 24, 1996

TO: Members, Proxy Committee

FROM: Howard Bicker

SUBJECT: Tobacco Issues

At the March 19, 1996 meeting of the State Board of Investment (SBI), the Governor requested that the Executive Director provide the Board with general information on holdings in tobacco companies and related issues.

This report provides a history of the Board's policy on tobacco, lists current SBI holdings of tobacco company stocks, summarizes current industry research reports on the tobacco industry and identifies actions being taken by other public pension funds concerning tobacco investments.

Please note that the report incorporates information available to SBI staff as of the above date.

The report is divided into several sections:

	Page
I. History of SBI Policies Regarding Tobacco	5
II. Recent Legal/Regulatory Environment	6
III. Current SBI Holdings in Tobacco Stocks	8
IV. Current Tobacco Industry Research Reports	11
V. Activity at Other Public Pension Funds	11

I. History of SBI Policies Regarding Tobacco

Prior to March 1993, the State Board of Investment (SBI) had a long-standing policy of not holding stock of any company which obtained more than 50 percent of its revenues from the sale of liquor or tobacco. The history on this policy is quite sketchy. To the best of staff's knowledge, there is no formal resolution of the Board on record which delineates the policy or rationale. Based on references in SBI minutes, it appears to have been in place sometime before the mid 1970's.

In June 1992, the Investment Advisory Council (IAC) reviewed information that showed that the restriction reduced returns of the Wilshire 5000 stock index by approximately 0.4% annualized from January 1980-March 1992. As a result, the IAC recommended the SBI's restriction on liquor and tobacco stocks be dropped. At that time, the SBI did not take action and referred the matter to another committee for further review.

In December 1992, the Proxy Committee provided its report to the Board. (See Attachment A for a copy of the complete report.)

- It stated: "Arguments for the policy included concerns that companies primarily engaged in alcohol and tobacco were imprudent investments because of their exposure to potential liability for damages from litigation regarding health risks and because investment in these companies could lead to an increase in long term costs attributable to health risks of alcohol and tobacco borne by beneficiaries, the taxpayers of the state and the state as a whole."
- It presented data that showed that for the period January 1980-September 1992 the restriction reduced returns of the Wilshire 5000 by 0.41% on an annualized basis. The report also noted that "the impact on the actively managed portion of the SBI's stock portfolio is more difficult to determine since active stock managers may or may not have chosen to include tobacco stocks in their portfolios if they had not been restricted by the SBI."
- Based on its review, the Committee recommended "that the SBI lift its investment restrictions concerning liquor and tobacco companies." At the same time, the Committee cited potential liability associated with pending litigation and urged the SBI to become a more active shareholder on issues associated with liquor and tobacco.

Also in December 1992, the IAC reported the following motion to the SBI: "Consistent with our fiduciary duty to plan beneficiaries, taxpayers and the State of Minnesota, the [IAC] recommends that the [SBI] act in a timely manner to remove all investment restrictions, except those resulting from objective risk/return considerations or required by statute, on the investment of employee benefit assets

for which the Board has fiduciary responsibility. Further, the IAC recommends that no such new restrictions should be undertaken.”

In March 1993, the SBI voted to rescind the liquor and tobacco policy and also directed the Proxy Committee “where feasible, to sponsor, cosponsor and support shareholder resolutions that call for a company to reduce its involvement in liquor and tobacco production, product marketing and other related lines of business in order to diversify its business in a manner that will reduce or eliminate potential liability to legal claims associated with liquor and tobacco that may negatively impact the value of the SBI’s holdings.” This directive was part of the Proxy Committee’s recommendation in its December 7, 1992 report.

In October 1995, the Chair of the Proxy Committee, in a verbal report to the Board, stated that the Committee had met with a group of private citizens concerning the SBI’s policy regarding investments in tobacco related companies. The Chair indicated that the Committee had requested additional background information and would be making a further report to the Board.

In December 1995, the Proxy Committee reported that it had reviewed its proxy voting record with respect to its current directive from the Board. (See **Attachment B** for a complete copy of the report.) The Committee stated that the SBI voted to support a range of tobacco related resolutions in 1995. The Proxy Committee also agreed to cosponsor a shareholder resolution submitted to Albertson’s, a leading Western states grocery store chain, at its December 1995 annual meeting. The Committee also reported that it plans to cosponsor additional resolutions on tobacco related issues for the 1997 proxy season. The Committee concluded that it is “taking appropriate action to carry out the SBI’s directive of March 1993 concerning tobacco holdings and recommends no change in the policy at this time.”

II. Current Legal/Regulatory Environment

The tobacco industry has been subject to increasing scrutiny and criticism during the 1990’s. The following statement is typical of the sentiment expressed by many market commentators: “It is difficult to recall a period during which attacks from antismoking advocates, government officials, and the news media represented as much of an all-out assault as we have seen during the past few weeks. We find it equally hard to pinpoint when the pressure will subside, for that matter” (from “The Tobacco Handbook,” Goldman Sachs Global Research, April 8, 1994, page 4.)

Public awareness was heightened in 1994 when the FDA (Food and Drug Administration) proposed to regulate nicotine as a drug and Congress held hearings on the tobacco industry. According to various external news and research services, the tobacco industry continues to face at least the following legal/regulatory issues:

- Proposed FDA restrictions on tobacco advertising and promotions.
- Justice Department inquiries into whether industry executives illegally conspired to obstruct a Congressional investigation into how much the companies knew about nicotine and its risks. These inquiries include five federal grand juries currently weighing criminal charges against the companies or their executives.
- Lawsuits filed by Attorneys General of eight states seeking reimbursement for Medicaid expenditures due to the health consequences of cigarette smoking. There are reports that several states are considering taking similar action.
- Several class action lawsuits alleging nicotine addiction or health risks.

In 1994, Minnesota Attorney General Humphrey, on behalf of the State of Minnesota, filed suit with Blue Cross-Blue Shield against a number of tobacco companies seeking damages for medical claims paid on cases arising from use of tobacco products.

In mid-March 1996, Bennett LeBow, Chief Executive Officer of Brooke Group, Ltd., owner of Liggett Group, a small producer of cigarettes, announced an out of court settlement with plaintiffs in the Castano case and with four state Medicaid suits. (The Castano case is a class action suit on nicotine addiction, and the state Medicaid suits are actions brought by several states seeking reimbursement from tobacco companies for Medicaid expenses related to smoking.) The payments to settle the Castano class action case would fund quit-smoking programs, but the settlement is contingent upon federal court approval. Payment of a portion of pretax profits of Liggett Group would settle the cases of Attorneys General in Mississippi, West Virginia, Florida and Massachusetts (Minnesota declined to participate in the settlement). However, Liggett has the right to nullify the settlements under certain conditions. (See **Attachment C** for an outline of the proposed settlement.)

On May 23, 1996, the Fifth U.S. Court of Appeals dismissed the Castano class action suit. The decision, which has been described as the most serious liability threat ever to confront cigarette makers, was expected by many industry analysts. The timing, however, came several months sooner than anticipated. The case had been the largest class action in U.S. history. Preliminary reports indicate that the Court of Appeals decision will not affect the Liggett settlement. (See **Attachment C** for news articles about the decision.)

While it is different from the legal and regulatory activities described, shareholder activism concerning tobacco issues is another area requiring tobacco industry attention. According to the Investor Responsibility Research Center (IRRC), Washington, D.C., 42 proposals were submitted for 1996 to tobacco companies and companies having ties to the industry. This is a larger number than have been

proposed in previous years. These proposals cover a range of topics and call for a variety of actions:

- voluntarily comply with FDA proposal
- donate a percentage of tobacco profits to fund a youth antismoking campaign
- identify nicotine levels in cigarettes and reduce those levels
- end business ties with tobacco industry
- make health insurer portfolios tobacco-free
- spin off non-tobacco businesses

For more information, see the IRRC report, "Tobacco Production and Marketing," dated January 18, 1996 in **Attachment D**.

On April 23, 1996 the American Medical Association (AMA) urged investors to sell holdings in mutual funds that invest in tobacco companies. The AMA announced that it would publish annually a list of mutual funds that have tobacco industry investments. (See the news article in **Attachment E**.)

In May 1996, Philip Morris (with support from UST, Inc.) proposed that the Congress adopt laws to reduce teenage smoking by banning vending machine cigarette sales and restricting advertisements and promotions. Their proposal would include elimination of promotional giveaways, ban transit advertising and place restrictions on billboard and stadium advertising and certain sports event sponsorships. In addition, the companies proposed that the tobacco industry spend \$250 million over a five year period to enforce these restrictions on youth smoking. These proposals cover only domestic business, not international activities. The proposal also would preclude the FDA from regulating tobacco products. The FDA is reported to have immediately rejected the proposal. Media reports suggest an uncertain reception in the Congress. (See the news articles in **Attachment F** for further detail.)

R.J. Reynolds Tobacco, a unit of RJR Nabisco and the second largest cigarette maker, was not aware of the announcement by Philip Morris, and had no position on the proposal as it was announced. BAT Industries' Brown & Williamson unit, the country's third largest cigarette maker, is reported to be studying the proposal.

III. SBI Holdings of Tobacco Company Stock

Since there is no commonly accepted definition of what constitutes "tobacco company," determining the extent of the SBI's tobacco holdings is somewhat problematic.

The lawsuit filed by Attorney General Humphrey names eight defendants (see **Attachment G**). The publicly traded companies affected by the suit are:

American Brands	Loews
BAT Industries	Philip Morris
Brooke Group, Ltd.	RJR Nabisco

In its recent announcement, the AMA cited thirteen companies with tobacco operations:

American Brands	RJR Nabisco
Brooke Group, Ltd	Sara Lee
Culbro	Schweitzer-Mauduit Int'l
Dimon	Standard Commercial
Loews	UST
Mafco Consolidated Group	Universal
Philip Morris	

The most comprehensive list of companies engaged in the tobacco business that staff has identified is a group of companies profiled by the IRRC. The IRRC has identified twenty five (25) "public companies around the world that manufacture tobacco products, or process or distribute tobacco as a major business activity." Their report, entitled "The Tobacco Industry, 1995 Edition," profiles publicly traded companies "whose stock US institutional investors are realistically likely to own." State owned or controlled firms outside the US are not included unless they are traded on a major US stock exchange or there is clear evidence of significant ownership by US institutional investors. The 25 companies are:

Amer Group Ltd.	Loews Corp.
American Brands Inc.	Philip Morris Cos. Inc.
American Maize-Products	Rembrandt Group Ltd.
B.A.T. Industries PLC	RJR Nabisco Holdings Corp.
Brooke Group Ltd.	Sara Lee Corp
Compagnie Financiere Richemont AG	Schweitzer-Mauduit International Inc.
Culbro Corp.	Societe Nationale des Tabacs (SEITA)
Dimon Inc.	Standard Commercial Corp.
Empresas La Moderna SA de CV	Tabacalera SA
Glatfelter (P.H.) Co.	Universal Corp.
Hanson PLC	UST Inc.
Imasco Ltd.	Volvo AB
Japan Tobacco Inc.	

The SBI holds stock in 19 of these 25 companies identified by the IRRC. Please note that the significance of tobacco operations as a source of revenue for each firm varies widely:

**SBI Stock Holdings
in Tobacco Companies Identified by the IRRC
March 31, 1996**

Company	Percent Revenue from Tobacco in 1994	SBI Shares 3/31/96	SBI Cost Value 3/31/96	SBI Market Value 3/31/96
Amer Group	8.0%	112,825	\$ 2,103,082	\$ 1,801,849
American Brands	53.4	147,700	6,094,984	6,258,787
American Maize	27.0	0	0	0
BAT	63.2	1,303,663	9,915,838	9,630,233
Brooke Group	97.2	9,900	65,372	89,100
Compagnie Fin..	66.2	0	0	0
Culbro	47.6	10,600	356,900	650,575
Dimon	74.6	23,899	392,891	421,219
Empresas	55.0	0	0	0
Glatfelter	n/a	66,800	1,288,067	1,160,650
Hanson PLC	8.3	2,708,824	9,145,227	7,917,274
Imasco Ltd.	16.4	0	0	0
Japan Tobacco	96.0	0	0	0
Loews	14.2	400,200	23,517,749	30,265,125
Philip Morris	44.0	1,732,285	113,302,025	152,008,008
Rembrandt	n/a	0	0	0
RJR Nabisco	49.9	805,478	11,383,168	11,480,549
Sara Lee	<5	579,105	15,466,446	18,893,300
Schweitzer-Maud.	93.0	16,210	314,388	445,775
SEITA	83.1	19,600	595,253	813,358
Standard Comm'l	64.4	12,369	161,682	111,321
Tabacalera SA	53.3	74,050	2,618,858	3,460,419
Universal Corp.	70.5	87,900	2,066,142	2,208,487
UST	86.5	276,300	7,893,094	8,807,062
Volvo AB	5.1	281,200	5,500,949	6,559,213
Total		8,668,908	\$212,182,114	\$262,982,200

Sources: List of companies and percent of revenue are from "The Tobacco Industry, 1995 Edition," IRRC, Washington D.C. SBI holdings data are from SBI bank records.

For information on the other lines of business operated by the above companies, please refer to **Attachment H**.

For a breakdown of holdings held in the active and passive portfolios, see **Attachment I**.

IV. Current Tobacco Industry Research Reports

The legal environment and proposed Liggett settlement raise questions about the market's valuation of tobacco company stocks.

Tobacco industry research reports gathered by staff during mid 1995 generally concluded that the potential for adverse claims against tobacco companies was already factored into current market prices (See the information included in **Attachment B** for highlights of these reports.) Similar reports issued in late 1995 and early 1996 generally reflect the same conclusion (See **Attachment J**).

Reports covering the proposed Liggett settlement generally conclude that the settlement:

- makes economic sense for Liggett, a small participant in the market, but it does not make economic sense for the larger participants in the market;
- has little impact on the valuation of tobacco company stocks; and
- is perceived as an action intended to strengthen the position of Bennett LeBow in his attempted takeover of RJR.

Bennett LeBow sought to gain management control of the tobacco operations of RJR Nabisco and spin off Nabisco as a separate company. LeBow and other company insiders control about 60 percent of voting stock of Brooke Group, Ltd. His Brooke Group proposal to have an alternate slate of directors approved for RJR Nabisco was defeated at the April 17, 1996 annual meeting of RJR Nabisco.

V. Activity at Other Public Pension Funds

The following items are based on media reports and discussion with IRRC regarding activity at other public pension funds:

- In early 1996, the **Massachusetts** Attorney General asked money managers for the Massachusetts pension funds to be more active shareholders. Similarly, the **Florida** Attorney General, with support from the Florida Governor, has urged that state's pension fund to address tobacco companies as shareholders in order to reduce tobacco advertising to youth.

- In March 1996, the New York State Comptroller, sole fiduciary for the **New York State and Local Retirement Systems**, announced that its active equity managers have been instructed not to purchase additional shares of tobacco company stocks. The Systems will continue to hold tobacco stocks in its passively managed portfolios. In addition, the Fund will become a more active shareholder in order to pursue tobacco industry support for initiatives to reduce youth access to tobacco products.

- In April 1996, **Maryland State Retirement Systems** sold tobacco holdings because of concerns about the long term financial outlook for the industry. The Systems sold stock holdings in four companies and a single company bond investment. The executive director of the Systems reported that the sale was a “strategic investment decision” and that the fund had not adopted a policy prohibiting investments in tobacco companies. The executive director added that the fund would reevaluate investing in tobacco stocks if lawsuits and other negative publicity concerning the industry are settled.

- In late April 1996, **New York State Teachers Retirement System (NYSTRS)** announced a three point action plan concerning its investment in tobacco stocks. NYSTRS decided to take action to:
 - communicate with tobacco companies to reduce potential exposure by improving youth antismoking efforts;
 - support “reasonable” proxy proposals directed at spinning off nontobacco related businesses; and
 - reduce its tobacco exposure by underweighting the tobacco sector of its Russell 3000 index fund by up to 25 percent. This action will be done over a period of time in conjunction with semi-annual rebalancing of the index.

- In late April 1996, a California Assembly Committee voted against a bill to force **California** public pension funds to divest their tobacco stocks. A bill has been introduced in the Massachusetts House to require that state’s funds to divest their tobacco holdings in a timely fashion. No action has been taken on the Massachusetts bill.

- The **Texas** Attorney General is reportedly reviewing that state’s investment in tobacco stocks. Similarly, the **New York City Employees Retirement System (NYCERS)** is reported to be reviewing its position on holding tobacco stocks.

ATTACHMENT A

**Attachment A is the December 7, 1992 Proxy Committee Report to the Board.
The Report has its own attachments.**

COMMITTEE REPORT

DATE: December 7, 1992

TO: Members, State Board of Investment

FROM: Proxy Committee

At its meeting in June 1992, the State Board of Investment (SBI) received a report from the Investment Advisory Council (IAC) which recommended that the SBI's investment restriction on liquor and tobacco companies be eliminated. In response, the Board referred the issue to a committee of the SBI for further review. The Proxy Committee has completed its review and is now making its report to the Board.

Impact of Existing Policy on Liquor and Tobacco

The SBI has had a long standing policy of not holding the stock of any company which obtains more than 50% of its revenues from the sale of liquor or tobacco. This restriction has been in place for more than two decades. Arguments which have been made for the policy include concerns that companies obtained more than 50% of revenues from alcohol and tobacco are imprudent investments because of the companies exposure to potential liability for damages from litigation regarding health risks and because investment in such companies could lead to an increase in long term costs to beneficiaries, the taxpayers of the state and the state as whole which are attributable to health risks of alcohol and tobacco.

The IAC's recommendation to lift the restriction on liquor and tobacco was based on data that compared the returns of the Wilshire 5000 stock index with and without the restricted securities from January 1, 1980 through March 31, 1992. The data showed that the restrictions reduced returns of the index by approximately 0.4% on an annualized basis during that period.

The Proxy Committee reviewed similar data for the period from January 1, 1980 through September 30, 1992 (see Attachment A). The data show that during the first half of the 1980's, the impact of the restriction was positive in some years and negative in others. Since the mid 1980's, the impact has been consistently negative. For the entire period, the restriction reduced returns of the Wilshire 5000 by 0.41% (41 basis points) on an annualized basis. The impact on the actively managed portion of the stock segment is more difficult to determine since active stock managers may or may not have chosen to include some of the securities in their portfolios if they had not been restricted by the SBI.

It is not possible to determine whether the impact of the SBI's liquor and tobacco policy will be positive or negative in future periods. The actual result will depend, in large part, on prevailing business and economic conditions. However, the Proxy Committee notes that tobacco companies are exposed to potential liability for damages arising from ongoing litigation concerning the health risks associated with smoking. The recent U.S. Supreme Court decision in *Cicilalone v. Liggett Group, Inc.*, 112 S. Ct. 2608 (1992) permitting claims based on express warranty, intentional fraud, misrepresentation or conspiracy to be asserted against the tobacco industry has only served to heighten these concerns. Since the damage claims associated with the outstanding lawsuits are potentially very large, future verdicts or settlements adverse to tobacco companies may have a negative impact on the value of the companies and their stock.

Action of Other Pension Funds

The Committee also attempted to determine what action other pension funds have taken with respect to this issue.

As you know, the SBI relies on research from the Investor Responsibility Research Center (IRRC) on a variety of corporate governance and social responsibility issues. IRRC is not aware of any state pension fund with laws or regulations which prohibit investments in liquor or tobacco companies. They have identified one municipal pension fund that has a tobacco restriction in effect at the present time. A copy of IRRC's response to our inquiry on this matter is in Attachment B.

Several pension funds, primarily those affiliated with church or religious groups, have initiated shareholder resolutions which call for companies to stop or curtail their involvement in tobacco production, cigarette marketing, and other tobacco-related lines of business. Consistent with spirit of the SBI's policy to restrict the SBI's investment in liquor and tobacco companies, the Proxy Committee has voted SBI shares in support of many of these resolutions. Shareholder activism in this area has grown in recent years and the Proxy Committee expects that these efforts to affect corporate behavior will gain support among other shareholder groups as well.

Alternatives Identified by the Committee

The Proxy Committee identified several alternatives concerning the SBI's policy on liquor and tobacco:

- Make no changes to the current restriction policy.
- Withdraw the current restrictions for the entire portfolio.
- Change the current policy prohibiting ownership of the affected securities to a policy that focuses on the actively managed portfolio similar to the SBI's policy concerning companies with direct investment in South Africa, i.e. active managers may purchase

restricted securities if the managers informs the SBI that they believe it would be a breach of their fiduciary responsibility not to do so.

Conclusion

Based on its review, the Proxy Committee recommends that the SBI lift investment restrictions concerning liquor and tobacco companies. However, due to the potential liability associated with pending litigation against several of these companies, the Proxy Committee strongly urges the SBI to become a more active shareholder on issues associated with liquor and tobacco.

The Committee recommends that the SBI direct the Proxy Committee, where feasible, to sponsor, co-sponsor and support shareholder resolutions that call for a company to reduce its involvement in liquor and tobacco production, product marketing and other related lines of business in order to diversify its business in a manner that will reduce or eliminate potential liability to legal claims associated with liquor and tobacco that may negatively impact the value of the SBI's holdings.

ATTACHMENT A

**Liquor and Tobacco Restrictions
Impact on Wilshire 5000 Returns**

Year	Wilshire Restricted (1)	Wilshire 5000	Difference
1980	32.75%	33.66%	(0.91%)
1981	(4.87)	(3.75)	(1.12)
1982	20.00	18.69	1.31
1983	22.80	23.45	(0.65)
1984	3.19	3.04	0.15
1985	32.17	32.57	(0.40)
1986	15.15	16.09	(0.94)
1987	1.93	2.27	(0.34)
1988	17.53	17.93	(0.40)
1989	28.59	29.18	(0.59)
1990	(6.84)	(6.18)	(0.66)
1991	33.89	34.21	(0.32)
1992 thru 9/30	1.27	1.58	(0.31)
Period Ending 9/30/92			
Qtr.	2.54	3.07	(0.47)
1 yr.	9.98	10.41	(0.43)
3 yr.	8.29	8.75	(0.46)
5 yr.	7.98	8.44	(0.46)
Since 1/1/80	14.61	15.02	(0.41)

(1) Securities restricted by the SBI's policy on liquor and tobacco i.e., companies who obtain more than 50% of their revenue from the sale of liquor and tobacco.

Investor
Responsibility
Research
Center Inc.

Via Facsimile Transmission

December 1, 1992

Arthur Blauzda
Senior Investment Analyst
Minnesota State Board of Investment
55 Sherburne Ave. - Suite 105
St. Paul, Minnesota 55155
Fax: (612) 296-9572

Dear Mr. Blauzda:

This letter confirms our conversation earlier today. You requested the name of any state public pension system that has prohibited investment of its funds in tobacco or alcoholic beverage companies. To the best of my knowledge, no state fund has any kind of formal or informal policy prohibiting such investments. The only public fund to formally prohibit investments in such stocks at all is the Cambridge (Mass.) Retirement System, which divested of tobacco stocks in 1990. While there may be some state or municipal systems out there that do have restrictions of this kind, we have not yet discovered them.

While a number of legislatures and city councils have considered and continue to consider the idea of prohibiting investments in tobacco or alcoholic beverage companies, to my knowledge no laws or regulations that would actually affect the investment of state funds have resulted. We will certainly keep looking for future policies in this area.

Sincerely,



Trex Proffitt
Research Analyst
Social Issues Service

**Investment Restrictions
Impact on Wilshire 5000 Returns
Through 12/31/92**

Year	Wilshire Restricted *	Wilshire 5000	Difference
1980	32.75%	33.66%	(0.91%)
1981	(4.87)	(3.75)	(1.12)
1982	20.00	18.69	1.31
1983	22.80	23.45	(0.65)
1984	3.37	3.04	0.33
1985	32.19	32.57	(0.42)
1986	15.22	16.09	(0.87)
1987	1.94	2.27	(0.33)
1988	17.45	17.93	(0.48)
1989	28.60	29.18	(0.58)
1990	(6.51)	(6.18)	(0.33)
1991	33.99	34.21	(0.22)
1992	9.50	8.97	0.53

Period Ending 12/31/92

Qtr.	7.47%	7.28%	0.19%
1 yr.	9.50	8.97	0.53
3 yr.	11.11	11.12	(0.01)
5 yr.	15.68	15.89	(0.21)
Since 1/1/80	15.05	15.34	(0.29)

	AHP*	Liquor*	Tobacco*	Wilshire 5000
Period Ending 12/31/92				
5 yrs. (1988-1992)	17.90%	15.31%	24.33%	15.9%
10 yrs. (1983-1992)	16.66	18.70	22.94	15.4
12 yrs. (1981-1992)	19.32	19.91	22.46	13.9

* Securities restricted by the SBI's policy on American Home Products (AHP) as well as liquor and tobacco (i.e., companies who obtain more than 50% of their revenue from the sale of liquor and tobacco). Data obtained from Wilshire Associates.

February 1993

ATTACHMENT B

**Attachment B is the December 18, 1995 Proxy Committee Report to the Board.
The Report has its own attachments.**

COMMITTEE REPORT

DATE: December 18, 1995

TO: Members, State Board Investment

FROM: Proxy Committee

At the State Board of Investment (SBI) meeting on October 10, 1995, the Chair of the Proxy Committee gave a verbal report to the Board concerning a request it had received from Mr. Mike Ravnitzky, a private citizen, concerning the SBI's policy regarding investments in tobacco related companies. At that time, the Chair indicated that the Committee had met with Mr. Ravnitzky and other individuals and had requested additional background information before making a further report to the Board.

Background

On September 26, 1995, the Committee met with Mr. Ravnitzky; Dr. Tracy Toomey, Director of Epidemiology, University of Minnesota; and Dr. Stuart Hanson, President, Park Nicollet Medical Foundation. The three presented information on the health effects of tobacco and asked that the SBI review its current policy concerning tobacco holdings.

At the Committee's request, staff gathered research reports on tobacco stocks. The reports generally conclude that the potential for adverse claims against tobacco companies have already been factored into the current market price of these stocks. (Attachment A.)

Current Directive to the Proxy Committee

When the Board voted to lift the restriction in March 1993, the SBI also accepted a report from the Proxy Committee which recommended that "SBI direct the Proxy Committee where feasible, to sponsor, co-sponsor and support shareholder resolutions that call for a company to reduce its involvement in liquor and tobacco production, product marketing and other related lines of business in order to diversify its business in a manner that will reduce or eliminate potential liability to legal claims associated with liquor and tobacco that may negatively impact the value of the SBI's holdings."

Recent Voting Activity by the Committee

The Proxy Committee reviewed the record over the last calendar year and determined that it voted on 15 tobacco-related shareholder resolutions during 1995. The SBI voted to support resolutions calling for the development of guidelines for accepting cigarette ads, the development of reports on manipulation of nicotine content, placement of warning labels on tobacco product logos, assistance to convert tobacco farms to other crops, and sale of tobacco business.

Preliminary information on the 1996 proxy season indicates that the SBI will have the opportunity to vote on several similar resolutions during the next year. The above directive will continue to guide the votes on those resolutions.

In addition, the Proxy Committee has agreed to co-sponsor a shareholder resolution submitted to Albertson's, a leading Western states grocery store chain, at its annual meeting in December 1995. The resolution calls for the company to take specific action to eliminate cigarette sales to youth in its outlets. (Attachment B.)

The Committee plans to co-sponsor additional resolutions on tobacco-related issues for the 1997 proxy season. Efforts to identify other co-sponsorship opportunities will intensify during the summer months in anticipation of filing deadlines in the last quarter of calendar 1996.

Conclusion

The Committee believes that it is taking appropriate action to carry out the SBI's directive of March 1993 concerning tobacco holdings and recommends no change in the policy at this time.

ATTACHMENT A

MINNESOTA
STATE
BOARD OF
INVESTMENT



Board Members:

Governor
Arne H. Carlson

State Auditor
Judi Dutcher

State Treasurer
Michael A. McGrath

Secretary of State
Joan Anderson Growe

Attorney General
Hubert H. Humphrey III

Executive Director:

Howard J. Bicker

Suite 105, MEA Bldg.
55 Sherburne Avenue
St. Paul, MN 55155
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An Equal Opportunity
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DATE: November 29, 1995

TO: Members, Proxy Committee

FROM: Jim Heidelberg

SUBJECT: Tobacco Industry Research Reports

The following are some highlights taken from recent tobacco industry research reports prepared by various investment industry analysts. The company comments are in no particular order.

1. **Sanford Bernstein:** July 21, 1995 research memorandum concludes that the analysts "prefer Philip Morris to UST, given the former's better international growth prospects, higher quality of earnings (volume, not pricing), and a stock price that already incorporates litigation risk." August 3, 1995 research memorandum concludes that "We point out that valuations already incorporate a very hefty discount for litigation risk; adding potential FDA legislative risk, which similarly shortens the life of tobacco's cash flow stream, shouldn't add incrementally to this discount." In this research memo the analysts reiterate their conclusion to buy Philip Morris and RJR. Their overall opinion of court actions is that they will be favorable to the tobacco industry.
2. **Goldman Sachs:** June 8, 1995 research memorandum recommends purchase of Philip Morris and RJR. Philip Morris seen as "offering good potential for P/E improvement." Sum-of-the-parts analysis of RJR "suggests that tobacco operations are deeply discounted." In the same report, the analysts conclude that "significant new restrictive legislation is highly unlikely before next year's presidential election." They further observe that "we have been strongly encouraged by virtually every major legal development that has transpired" since several class action lawsuits against tobacco companies were certified by state and federal courts.
3. **Dean Witter:** July 20, 1995 research memorandum on Philip Morris maintains a buy recommendation on the stock. The memo also concludes that "Investment in tobacco stocks, however, should be restricted to higher-risk portfolios, in our view, because of the unique attributes associated with the tobacco industry. These include unpredictable litigation developments and potential changes in government regulations." In its July 28, 1995 research report on RJR, the firm finds RJR's second quarter 1995 results "uninspiring" and maintains a neutral rating on RJR. The report concludes that "...due to

the wide variety of tobacco-specific investment concerns (litigation, legislation, FDA and OSHA, among others), we feel that the market will likely continue to penalize tobacco companies that lack strong operating fundamentals."

4. **Salomon Brothers:** July 18, 1995 research memorandum has a buy recommendation for RJR Nabisco because of "negative value accorded RJR's domestic tobacco business". Concerning Philip Morris, the analysis states: "Because of lingering class action risk, we expect Philip Morris to trade in the bottom half of its ten through 17 price/earnings range that prevailed in the 1990-93 time period, when litigation was quiet. Thus, Philip Morris shares can have a 70% variation in any year because of investor psychology related to litigation risk."
5. **Rodman & Renshaw Inc.:** July 10, 1995 research memorandum recommends buying Philip Morris and RJR and UST, the leading seller of chewing tobacco. The report concludes that "...negative news will likely surface intermittently and impact the tobacco stocks. Such events should provide buying opportunities for those who favor purchasing consistent growth at extremely discounted valuations." In sum, this analyst remains very positive on litigation: "We continue to believe that as litigation news filters through over the next several months, the propensity will be for favorable news rather than unfavorable." July 28, 1995 research memorandum of RJR concludes that "The common, under pressure from the rash of antitobacco press in recent days, remains an attractive BUY..."
6. **Brown Brothers Harriman & Co.:** June 21, 1995 research memorandum on Philip Morris recommends buying the stock. The report concludes that "Notwithstanding the ongoing (effectively, permanent) smoking -and-health issue, we view MO (Philip Morris) as a 13%-15% average annual EPS grower (earnings per share) from the estimated 1995 base through 2000..."
7. **Oppenheimer & Co., Inc.:** June 2, 1995 report, "Tobacco Industry Outlook," concludes that since American Brands sold American Tobacco Company to B.A.T., a British company, "American Brands no longer is exposed to litigation issues, a factor that historically has depressed stock price valuations of domestic tobacco manufacturers." About Philip Morris which the firm recommends as a "buy", the report notes that "Litigation fears have caused temporary stock price weakness in the past, creating periodic buying opportunities." The report also states that "We believe that as concern about the potential threat of litigation dissipates, investors will refocus their attention on the company's strong earnings visibility."

8. **Warburg:** In a July 1995 report, "Tobacco Stocks & Markets", this British firm states about tobacco stocks that "In terms of US litigation we conclude the risk is one of share price volatility rather than material cash payments." The report also states that "In general, tobacco earnings are understood to be low growth and high risk but with above average cash generation." The report further observes that "The principal negative concerns are declining cigarette consumption, rising taxation and potential litigation. Product liability litigation has so far been largely a US phenomena, but it has influenced the valuation of tobacco businesses with no material US exposure..."

ATTACHMENT B

ALBERTSON'S, INC.

WHEREAS, President Clinton has declared nicotine addiction a *pediatric disease*;

- Each day 3000 children begin smoking regularly; most of these become addicted smokers and nearly 1000 of these will die of diseases caused by smoking;
- More than 4 million children and adolescents smoke cigarettes and 1 million adolescent boys use smokeless tobacco;
- Addiction to nicotine is the most common drug addiction problem among young people today;
- From 1991 to 1994, smoking increased 30 percent among eighth graders and 20 percent among 10th graders;
- Studies show that cigarettes and smokeless tobacco products are routinely sold to minors in violation of state laws by retail outlets;
- The promotional items and catalogues with tobacco product logos and images have proven to be very popular among youth;
- A recent California study found that point-of-purchase advertising or tobacco products was more likely to take place in places closer to schools than not;
- 30 percent of 9th graders who use tobacco report having shoplifted cigarettes;
- Teens purchase the most-heavily advertised cigarettes; these also tend to be highly promoted at point-of-purchase in our stores;
- Federal law requires states to enforce laws prohibiting sales to minors;
- The Attorney General of Massachusetts recently sued three major grocery store chains under the State's Consumer' Protection Law for selling cigarettes to minors and recovered \$77,000 from them;
- In California, unfair business practice actions have been taken against retail businesses for selling cigarettes to minors; Our Company could be held liable for the harm caused to minors to whom we illegally sell tobacco products from our store outlets;
- Tobacco industry-sponsored campaigns to prevent the illegal sale of cigarettes to children have proven to be ineffective in eliminating sales to minors. These include such tobacco industry campaigns as "*It's the Law*" and the *Jaycees Against Youth Smoking Program*;

RESOLVED that shareholders request the Board , to curb illegal sales of tobacco products in our grocery stores, to create a policy with implementation steps to assure shareholders to enforce efforts to curb underage access to cigarettes in our stores.

SUPPORTING STATEMENT

In implementing this policy, the shareholders ask the Board to assure our retailers will:

- 1. inspect a photo ID of customers for who might be under 18 years of age;**
- 2. eliminate cigarette self-service displays;**
- 3. not sell cigarettes in packages of less than 20 sticks;**
- 4. not carry catalogues or promotional offers for tobacco products or promotional items such as t-shirts, caps, and lighters;**
- 5. not display any advertising for tobacco products other than black and white ads relating to prices charged.**

ATTACHMENT C

Attachment C contains:

- the proposed settlement terms between Liggett Group, Ltd. and plaintiffs in four of five state Medicaid damages suits and the so-called Castano class action lawsuit against tobacco industry companies. These terms are excerpted from a Smith Barney Research report, dated March 13, 1996.
- news article concerning the Fifth U.S. Court of Appeals dismissal of the Castano case.

LIGGETT'S PROPOSED SETTLEMENT

1) Liggett Group would agree to pay 5% of pretax income (with a ceiling of \$50 million a year) to settle the Castano class-action case. The payments would fund quit-smoking programs. Such a settlement is contingent upon federal-court approval.

2) Liggett Group would settle attorney generals' cases of Mississippi, West Virginia, Florida and Massachusetts seeking reimbursement for smoking-related Medicaid costs. This would require Liggett to pay each state \$1 million and 2% to 7% of pretax income for 24 years, depending on how many other states initiate claims. (States that have currently agreed to settle would split 2% of Liggett's pretax income; other states that initiate suits would split a pool of 5% of Liggett's pretax income depending upon the number of Medicaid patients in that state.)

3) Liggett Group will voluntarily comply with certain proposals put forth by the FDA concerning advertising and marketing. In an attempt to reduce underage smoking, Liggett would agree to halt the passage of free samples of tobacco products where minors are present and eventually discontinue ads believed to be particularly attractive to youths.

4) The above agreements would apply even if the Liggett Group or Brooke Group, its parent company, merges with one of the other tobacco companies in the industry, except Philip Morris. If such a merger takes place, the new entity would pay 5% of pretax income for the settlement of the Castano class-action case for 25 years (with a ceiling of \$50 million a year). Concerning the attorney generals' suits, the four states that agreed to settle would share \$100 million plus legal fees, and additional states would share another \$25 million. The states would again split 2% to 7% of pretax income for 24 years, depending on how many other states initiate claims, but would not receive less than \$20 to \$25 million a year. In addition, the states would share a \$3 million fund dedicated to childrens' smoking issues.

5) The plaintiffs involved in the Castano case and the four attorney general cases involved in this settlement will agree not to sue to prevent a spin-off of Nabisco if LeBow's nominees are elected to the board.

6) Liggett Group has the right to nullify the above settlements under certain conditions. If other tobacco companies are victorious in their suits against the same plaintiffs, Liggett can terminate parts of its settlement. Liggett can back out of its Castano agreement if enough smokers decide not to agree to the terms or if the class-action certification is revoked on appeal. Also, Liggett can strike down the deal with the attorney generals if too few other states join in.

Appeals Court Throws Out Tobacco Class-Action Suit

Decision in Castano Case Over Nicotine Addiction Eases Liability Threat

By MILO GEYELIN
And SUEIN L. HWANG

Staff Reporters of THE WALL STREET JOURNAL

A federal appeals court in New Orleans threw out the huge class-action liability lawsuit brought against the tobacco industry on behalf of millions of allegedly addicted smokers.

The ruling removes the most serious liability threat ever to confront cigarette makers.

The 39-page decision is the second major blow to class-action lawsuits this month, coming only 13 days after a major asbestos class-action settlement was rejected by an appeals court in Philadelphia. The three-judge panel in Louisiana found there were too many differences in the plaintiffs' circumstances and too many conflicts among state laws that would have to be resolved for the case to go to a jury.

While the industry still faces regulatory and legal challenges, Wall Street greeted the news enthusiastically, sending tobacco stock prices up sharply.

Plaintiffs in the case, who were seeking damages to recoup the cost of their alleged addictions to nicotine, will now have to proceed individually or as members of class actions filed in state courts.

But the consortium of 60 plaintiffs law firms that had financed the case, known as Castano after the lead plaintiff, immediately vowed to continue its fight against the industry. The group said it would begin filing class actions in state courts around the country today, though it was unclear where or in how many states.

'Plan B' Ready to Go

"We do have Plan B for this contingency," said John Coale, a lawyer acting as spokesman for the Castano Plaintiffs Legal Committee. "We would have liked to have won this decision, but we're not going to go away."

The speed of the panel's decision was greeted with cheers on Wall Street, which had been predicting the suit would be thrown out this summer. "This doesn't surprise a lot of us," said Mary Aronson, a Washington-based analyst. "The panel is a fairly conservative panel in a fairly conservative circuit."

Still, despite widespread belief that the largest class-action lawsuit in history wouldn't be allowed to proceed, the news sent shares of market leader Philip Morris Cos. up \$6.25 to \$103.875, in New York Stock Exchange composite trading. RJR Nabisco Holdings Corp. shares ended at \$33.125, up \$2. Shares of Brooke Group Ltd., which owns Liggett Group Inc., rose 75 cents to \$6.875.

Tobacco analysts said the rally could mark the beginning of a major shift in investors' attitudes toward the \$45 billion tobacco industry, which has been buffeted

The Castano Catalyst

	STOCK CLOSE		PERCENT CHANGE
	3/30/94	5/23/96	
R.J. Reynolds	29.375	33.125	+12.8%
B.A.T	13.375	16.5	+23.4
Philip Morris	50.75	103.875	+104.7
Lorillard (Lowe's)	32.625	82.125	+151.7
U.S. Tobacco	25.125	34.375	+36.8

Source: TradeLine

in recent months by litigation and regulatory attacks. They said panel's decision marks the first major victory for the industry in its battle against the latest wave of litigation, which, in contrast to earlier attacks, is focused on novel legal theories involving nicotine addiction.

"The emergence of Castano and other class-action lawsuits really triggered a whole new set of doubts and concerns about the legal outlook for this industry, and catalyzed debate among investment managers about what amount of legal exposure was appropriate," said Marc Cohen, analyst at Goldman, Sachs & Co. in New York. "A move to decertify is really the first tangible piece of information the investment managers can use to draw the conclusion the threat is not as significant as they feared."

Some See Major Setback

Some on Wall Street now say any effort to bring any class-action lawsuit on behalf of smokers has been dealt a major blow. They also predict that any appeal of the decision will be rejected. "Forget addiction class action—it's gone," declared Gary M. Black of Sanford Bernstein & Co. in New York. He further predicted that shares of Philip Morris could go as high as \$120 in the next few weeks, but others were more cautious, pointing out that Wall Street had been expecting the Castano case to be stubbed out for some time.

Philip Morris and Brown & Williamson Tobacco Corp. both said the ruling sends a message to other courts that cases like

Tobacco Class-Action Suit Is Thrown Out By an Appeals Court

Continued From Page A3

Castano shouldn't be certified as class actions. "The judicial system was not designed as a lawyer-enrichment device, which is becoming the typical result of today's class action lawsuits," Brown & Williamson, a unit of B.A.T Industries PLC, said in a statement.

Liggett Group, the only tobacco company to break ranks with the industry and settle the Castano and state cases earlier this year, is considering its options but remains committed to the idea of a settlement, according to a spokesman for its parent, Brooke Group. "We continue to believe that responsible compromise is in the best interests of Liggett and the entire tobacco industry," he said.

Under the Liggett settlement, Brooke Group can walk away, continue it as is, or apply it to any future litigation that the Castano class or its attorneys bring.

But Daniel W. Donahue, deputy general counsel for R.J. Reynolds Tobacco, said, "The industry has never looked upon any class-action litigation as a settlement opportunity."

The tobacco industry still faces formidable legal and regulatory challenges. Eight states have filed suits seeking billions of dollars in damages to recoup the public health-care cost of treating smokers with tobacco-related illnesses. The Food and Drug Administration, meanwhile, continues to seek jurisdiction to regulate cigarettes as a drug on grounds that they are engineered to deliver nicotine. And five federal criminal inquiries of the indus-

try are under way.

State class-action suits modeled after the Castano complaint would have the advantage of obviating the biggest legal hurdle that confronted the case — how to merge 50 different and, in some cases conflicting, state laws — so it could be tried under uniform legal standards, according to John Coffee, a Columbia University law professor. Defending a large number of class-action lawsuits in different states could also prove daunting and costly, even for the tobacco industry.

"Now it's going to go from one global war to 50 local wars," Mr. Coffee said.

But the Castano plaintiffs lawyers appeared unsure yesterday exactly how they planned to move ahead. Mr. Coale said initially that, over the next two weeks, the group would file 10 to 20 state class action suits a week and that it planned to file in all 50 states plus Puerto Rico by mid-June.

Other lawyers in the group said they would likely forgo suits in tobacco-rich states such as North Carolina, Virginia and Kentucky. Mr. Coale later said that 11 states are currently under consideration for immediate filings. They include Florida, Maryland, New York, Pennsylvania, California and Indiana.

How those suits will fare, if they are filed, will depend largely on whether the Castano plaintiffs group can sustain a cohesive centralized management of all the litigation. "Obviously you can't have as centralized a focus as you would in a national class action, and you could have varying results," said Ron Motley, a plaintiffs lawyers in Charleston, S.C., who is active in the Castano case.

The cost of proceeding in numerous individual states is also likely to exceed what the Castano case would have cost plaintiffs, and to work against them far more than against the tobacco companies, Mr. Coffee said.

ATTACHMENT D

**Attachment D is the Investor Responsibility Research Center report:
Social Issues Service, 1996 Background Report F: Tobacco Production and Marketing**

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Social Issues Service 1996 Background Report F

Tobacco Production and Marketing

For the seventh year, shareholder proponents will ask tobacco and non-tobacco companies to take a variety of actions related to tobacco production and marketing.

- In 1993, 25 percent of American adults smoked. Smoking rates among high school seniors rose from 27.8 percent in 1992 to 31.2 percent in 1994.

MAJOR DEVELOPMENTS IN 1995

- The U.S. Food and Drug Administration declared that cigarettes are a "drug-delivery device" and announced a sweeping proposal to limit youth's access to tobacco. Tobacco companies and others are fighting the FDA proposal in court.
- A stream of industry documents were leaked to the FDA and the press that show tobacco companies control nicotine levels in cigarettes. The companies say nicotine adds flavor and is not addictive.
- Massachusetts became the fifth state to sue tobacco companies in an effort to recoup Medicaid costs for treating smoking-related illnesses.
- Kimberly-Clark agreed to spin-off its tobacco operations and Knight-Ridder issued new guidelines for accepting tobacco advertising, after shareholder resolutions came to votes on these issues in 1995.
- Philip Morris announced a new initiative against youth smoking that includes withholding merchandising benefits from stores selling cigarettes to minors and an end to free cigarette sampling.

THE SHAREHOLDER CAMPAIGN

27 resolutions for 1996: This year's tobacco-related resolutions fall into nine major categories:

- Four companies face a new resolution asking them to comply voluntarily with the new FDA proposal.
- Five companies face a new resolution asking that a portion of their tobacco-related profits be donated to a youth anti-smoking advertising campaign.
- Four tobacco companies face a resolution asking them to publicize new nicotine ratings and reduce nicotine levels in their products.
- Three companies are being asked to break business ties with the tobacco industry.
- Two health insurance companies are being asked to divest their holdings in tobacco companies.
- Two tobacco companies are being asked to spin off their non-tobacco businesses.
- Two fast-food companies are being asked to make their restaurants smoke-free.
- Five miscellaneous tobacco resolutions have been filed on various other topics. Three of these resolutions are new.

FACTS ON FILE

- Smoking is the single most preventable cause of death in the United States, causing more than 415,000 deaths in 1990. U.S. smoking-related health care costs exceed \$50 billion annually.

Previous resolutions and support levels			
	1993	1994	1995
Voted on	9	15	17
Withdrawn	4	7	13
Average support	5.5%	4.8%	6.7%

by Doug Cogan
Jan. 18, 1996

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Tobacco Production and Marketing

Tobacco-related resolutions are coming to votes for the seventh consecutive year in 1996, in what promises to be a busy proxy season for anti-smoking shareholder activists. Church sponsors and health-care advocates have filed 42 proposals, 27 of which are still pending. (Ten of the proposals have been withdrawn, and the Securities and Exchange Commission has issued no-action letters allowing companies to omit two forms of resolutions on ordinary business grounds.) Eleven of the 15 companies where resolutions are still pending are not engaged directly in tobacco manufacturing but have other ties to the industry. Last year at this time, 23 proposals were pending at 13 companies; 17 of those proposals came to votes.

In 1995, the biggest triumph for antismoking shareholder proponents was Kimberly Clark's decision to spin off its tobacco operations—just as proponents had requested in a resolution that got 8.7 percent support at the company's annual meeting. Kimberly Clark said its decision to spin off its tobacco operations was not related to the shareholder proposal. Another shareholder victory came at Knight-Ridder, where a shareholder proposal asking the company to adopt a new tobacco advertising policy got 14.2 percent support. Knight-Ridder announced a new policy last fall that discourages its newspapers from running certain kinds of tobacco advertisements. Knight-Ridder said it decided to take "a fresh look" at its advertising policy because of "significant" support for the shareholder proposal and the "forceful but measured manner" in which it was presented.

Institutional investors have grown increasingly concerned about the tobacco industry's future, especially in the United States. Representatives of a half-dozen large pension funds met with Philip Morris executives in the fall of 1994 to hear how the company viewed mounting health litigation claims against the industry and the growing prospect that the Food and Drug Administration would regulate tobacco as a drug. At the end of 1994, institutional shareholders generally applauded American Brands' decision to sell its domestic tobacco subsidiary to the British conglomerate B.A.T Industries for \$1 billion in cash. In 1995, shareholders turned their attention to RJR Nabisco, where investors Carl Icahn and Bennett LeBow launched a bid to separate the company's food business from its tobacco business. Religious investors also filed a shareholder proposal in 1995 seeking a spinoff. The re-

submitted proposal will draw extra attention this year, now that Icahn and LeBow have mounted a proxy fight to complete the spinoff. (For more on this proxy fight, see Section III of this Background Report, especially pp. 19-20).

Historically, institutional support for tobacco shareholder resolutions has been low compared with votes on other social issues. Last year's proposals garnered average support of 6.7 percent of the shares voted. But revelations about the industry's ability to manipulate nicotine levels in tobacco products as well as a new FDA proposal on tobacco advertising and promotion could give the tobacco shareholder campaign a boost in 1996. The sweeping FDA proposal announced last August includes a number of elements that antismoking shareholder activists have been recommending for years—including greater restrictions on tobacco advertising and promotion and restricting youth's access to cigarettes through vending machines and self-service displays. Institutional shareholders generally have lent the most support to resolutions seeking to discourage minors from smoking.

As in past years, Father Michael Crosby of the Province of St. Joseph of the Capuchin Order in Milwaukee, Wisc., is coordinating the tobacco shareholder campaign on behalf of the Interfaith Center on Corporate Responsibility. Religious institutions affiliated with the Interfaith Center are primary sponsors of 20 of the resolutions now pending. Four of the remaining resolutions are being sponsored by Dr. Gregory Connolly of the Massachusetts Department of Public Health, and the other three are being sponsored by Dr. John Slade of St. Peter's Medical Center in Brunswick, N.J. Drs. Connolly and Slade have been sponsoring shareholder resolutions on tobacco issues since 1991 and coordinate their efforts with the Interfaith Center.

1996 Resolutions

The 27 proposals pending for 1996 can be broken into eight types of resolutions, including one category with five miscellaneous proposals. Two of the resolution types are new: compliance with the FDA proposal and donating a percentage of profits to fund an antismoking campaign. Each of the resolution types is summarized below, with the new resolutions listed first. Prior-year votes cast in favor of resubmitted proposals appear in parentheses.

Comply voluntarily with FDA proposal: Proposals are pending at two media companies—3M (which owns a

billboard business) and **Time Warner**—and two retail companies that sell cigarettes—**Albertsons** and **Atlantic Richfield**. A proposal to a third media company—**Gannett**—has been withdrawn.

Religious investors are asking these companies to comply voluntarily with the FDA proposal announced last August. A number of the affected industries have objected strongly to FDA's proposal, prompting the agency to extend its comment period by two months, which ended Jan. 2, 1996. Lawsuits are expected to delay implementation of final FDA regulations indefinitely.

Media companies—**Time Warner** is challenging the proposal at the SEC, and the proponents are in dialogue with 3M. Father Michael Crosby told IRRC that 3M has "expressed concern about continuing tobacco advertising." Crosby is pressing the company to establish a timeline for phasing out tobacco advertising on its billboards. The resolution itself makes other requests of media companies that are consistent with the FDA proposal:

1. Use black-and-white text only when advertising in publications with significant youth readership (under 18). By 'significant,' it is meant that readership is more than 15 percent or more than 2 million.
2. Prohibit advertising of giveaway products like caps or gym bags that carry cigarette or smokeless tobacco product brand names or logos.
3. [For 3M] Ban outdoor advertising within 1,000 feet of schools and playgrounds and permit black-and-white text only for all other outdoor advertising, including billboards as well as signs inside and outside of buses.

Retail outlets—**Albertsons** grocery stores and **Atlantic Richfield** gas station/convenience stores—two retail outlets for cigarettes—also have been asked to live up to terms of the FDA proposal. The proponents are in dialogue with **Albertsons**. Father Crosby says that **Albertsons** has a "good track record" and could "serve as a benchmark" for other stores if it can reach an agreement with the proponents. Consistent with the FDA proposal, the resolution asks cigarette retailers to:

1. Inspect a photo ID of customers who might be under 18 years of age;
2. Eliminate self-service displays for tobacco products;
3. Not sell cigarettes in packages of less than 20 sticks;
4. Not carry catalogues or promotional offers for tobacco products or promotional items such as T-shirts, caps and lighters; and

5. Not display any advertising for tobacco products other than black-and-white ads related to prices charged.

Donate a percentage of tobacco profits: Proposals are pending at three tobacco companies—**Loews**, **RJR Nabisco** and **UST**—and two media companies—**3M** and **Time Warner** (although the proposals at the media companies are not expected to come to votes). Religious investors are asking the tobacco companies to donate a percentage of their tobacco-related profits to a national advertising campaign that seeks to reduce the number of underage smokers. Implementation measures include:

1. That 3 percent of our cigarette/tobacco profits realized from sales to minors be contributed to a third party such as the American Heart Association or the American Cancer Society.
2. This third party would use the funds to run a national antismoking advertising campaign aimed at discouraging youth from smoking.
3. The goal of the campaign would be to achieve a substantial reduction in the number of underage smokers.
4. The campaign would be evaluated after three years to determine its effectiveness.

Withdrawals and omissions—An identical proposal to Philip Morris was withdrawn as part of a larger agreement between shareholder proponents and the company. Originally, proponents filed seven resolutions with Philip Morris. The company agreed to place three of the resolutions on the ballot—without contesting them at the SEC—in exchange for having the other four resolutions withdrawn.

A variation of this resolution was filed with five media companies—**Gannett**, **3M**, **Time Warner**, **Times Mirror** and **Tribune Co.**—but none of these resolutions are expected to come to votes. **Tribune Co.** received a no-action letter from the SEC allowing it to omit the proposal on ordinary business grounds, and **Time Warner** and **3M** have filed similar challenges. The proponents withdrew the proposal at **Gannett** in anticipation of a challenge, although no dialogue with the company took place. The proponents also withdrew the resolution at **Times Mirror**; dialogue there is continuing. Father Crosby told IRRC that **Times Mirror** "has demonstrated an openness that parallels the kind of dialogue we had with **Knight-Ridder** last year." Crosby is hopeful that **Times Mirror** will follow **Knight-Ridder's** lead and reform its own tobacco advertising policy.

Name and curb nicotine in tobacco products: In a variation of a nicotine manipulation resolution that first

came to votes last year, Dr. Gregory Connolly of the Massachusetts Department of Public Health is asking three cigarette manufacturers—American Brands, Philip Morris and RJR Nabisco—to better inform consumers about their use of nicotine in tobacco products. Connolly has filed a similar, but “snuff-tailored,” resolution with UST, a manufacturer of smokeless tobacco. The resolved clause of the resolution to cigarette manufacturers asks their boards of directors to:

1. Develop and publicize nicotine ratings for each of our cigarette brands and make this available in accurate information to our customers about how much nicotine they consume when smoking.
2. Determine the nicotine level in cigarettes at which nicotine addiction cannot be induced or maintained. With this information, the company shall implement a program that would gradually reduce levels of nicotine in our brands over an appropriate time period to a level that is not addictive. This effort to reduce nicotine availability would be undertaken in collaboration with independent health experts.
3. Develop and market new nicotine or nicotine-like produce that have minimal toxic agents that can be used by our consumers in lieu of cigarette smoking, and market these products as drugs or medical devices to help adult smokers quit tobacco use.

End business ties with tobacco industry: Building on the success of a shareholder resolution last year that may have contributed to Kimberly-Clark’s decision to sell off its tobacco-related businesses, three like-minded resolutions have been filed for the 1996 proxy season. **Eastman Chemical** is being asked to “take steps to accomplish a separation of the corporation’s tobacco business from all its non-tobacco businesses by Jan. 1, 1997.” **H.B. Fuller** has received a similar resolution asking its board “to adopt a policy to have no sales nor service to the tobacco industry after Jan. 1, 1997.” The third resolution, filed at **3M**, asks the board to establish “a Review Committee to undertake a thorough examination of the ways our company is involved in the process of producing and/or marketing cigarettes and tobacco products in light of their recognized health hazards” and that recommendations be made by Jan. 1, 1997, whether to remain involved “in making products for, or the promotion of, cigarettes and other tobacco products.” Church proponents are in dialogue with H.B. Fuller and 3M.

Tobacco-free insurance portfolios: Proposals are pending at **Health Systems International** and **Tenet Healthcare**, asking these health insurers to make their investment portfolios tobacco-free. An identical resolution at **Chubb** was withdrawn after the company reported to

church proponents that it had no investments in tobacco companies and has an “unwritten policy” discouraging such investments. The resolved clause of the resolution asks the insurance companies to:

initiate a policy determining no further purchases of tobacco equities in any of our portfolios until it can be proven that cigarette smoking does not cause the illnesses and deaths attributed to it. Furthermore, to ensure fiduciary interests, the company shall move to be free of all tobacco-related stock by Jan. 1, 1998.

Spin-off non-tobacco businesses: Last year, church proponents asked **Philip Morris** (3.5 percent) and **RJR Nabisco** (6.5 percent) to spin off their tobacco businesses from the rest of their operations. This year, in a twist, proponents are asking the companies to keep their tobacco businesses and spin off their other operations. The resolution at **RJR Nabisco** is taking on an added dimension now that investors **Carl Icahn** and **Bennett LeBow** are seeking to separate the company’s **R.J. Reynolds** tobacco business from its **Nabisco** food operations.

Smoke-free restaurants: Once again, religious investors are asking **PepsiCo** (6.8 percent) and **Wendy’s** to make “all our restaurants smoke-free” by 1997. A third proposal filed at **Ryan’s Family Steakhouses** was withdrawn after the company reported that all of its new restaurants are smoke-free and that it has a “gradual process” in place to make its existing restaurants smoke-free. The resolution includes a stipulation that “beginning in 1997, all new franchisees’ facilities be smoke-free and all renewals of franchise agreements include smoke-free facilities in the agreements.”

Wendy’s omitted similar resolutions from its proxy statements in 1994 and 1995, citing the ordinary business clause of the shareholder proposal rule. However, the SEC was not expressing opinions on ordinary business challenges at that time. The proponent, **Mercy Health Services**, filed a lawsuit against **Wendy’s** in 1994 that still is pending. The SEC staff denied **Wendy’s** request to sanction omission of **Mercy Health Services’** proposal in 1996, citing the pending litigation.

PepsiCo could challenge its proposal on grounds that last year’s resolution failed to receive sufficient support to be eligible for resubmission.

Miscellaneous tobacco resolutions: Five other tobacco-related resolutions have been filed on various topics, two of which are types of resolutions:

Discourage smoking by pregnant women—**Dr. John Slade**, a physician at **St. Peter’s Medical Center** in **Brunswick, N.J.**, is the primary filer of a new resolution at

RJR Nabisco. (An identical resolution was withdrawn at Philip Morris.) At RJR Nabisco's 1995 annual meeting, Chairman and Chief Executive Officer Geoffrey Bible reportedly made the comment that "I think it would be sensible for pregnant women not to smoke." Accordingly, Slade has filed a resolution at RJR Nabisco that asks the board:

to devise effective strategies to prevent harm to infants from tobacco smoke both before and after their birth. Shareholders recommend that this program be developed and implemented by Jan. 1, 1997, to help women not use our company's cigarette brands when they are pregnant or might become pregnant. In addition, shareholders request that management evaluate the effectiveness of this program on reducing the use of the company's cigarette brands by women who are or who might become pregnant and to report to requesting shareholders on progress being made in this regard by Jan. 1, 1999.

Eliminate Harley-Davidson brand cigarette—Dr. Slade also is asking Loews "to comply with its policy against having its cigarette brand names or logos on children's toys by stopping the use of the Harley-Davidson brand name and associated logo on any brand of cigarette made by the company at the earliest possible time but not later than Jan. 1, 1997." Loews reportedly sells a Harley-Davidson brand of cigarettes in four packings under license to the motorcycle and bicycle manufacturer, which also has sold its name and logo to at least three different toy manufacturers.

Place warning labels on smokeless tobacco—In a resubmission, Dr. Slade is asking UST (7.3 percent) to adopt a policy for "[a]ll advertising and promotion for our company's moist snuff brands, including all uses of the company's brand names and associated symbols for moist snuff products used in connection with sponsorship of all sorts, shall include clear, effective and prominent warnings of the addiction and disease hazards caused by these products." The resolution could be omitted on grounds that it did not receive sufficient support for resubmission.

Smoke-free pharmacies—Extending a campaign to end cigarette sales in drug store pharmacies, church sponsors are asking Rite-Aid to "create a policy of not selling any cigarettes or smokeless tobacco after Jan. 1, 1997, in any of our stores with a pharmacy. The proponents plan to enter into dialogue with Rite-Aid.

Stop challenging EPA study—This church-sponsored resubmission asks Philip Morris (6.4 percent) to "cease expenditures of funds challenging legitimate studies consistently showing the health hazards of environmental [second-hand] tobacco smoke." This proposal, now in its third year, refers to an ongoing lawsuit filed by the top two cigarette makers seeking a permanent injunction overturning the Environmental Protection Agency's 1993 finding that second-hand tobacco smoke is a known human carcinogen. Management agreed to place the resolution on the ballot even though it could have omitted it on grounds that it failed to receive sufficient support for resubmission.

The resolution is one of three proposals that Philip Morris agreed to place on the ballot, in exchange for having four others withdrawn. The withdrawn resolutions concerned development of "fire-safe" cigarettes, discouraging smoking by pregnant women, donating a percentage of profits to an antismoking advertising campaign, and subjecting allegations leveled against the company to independent analysis.

SEC Omissions

To date, the SEC has issued no-action letters on two types of tobacco-related resolutions. In each instance, SEC staff agreed with company arguments that the resolutions may be omitted on ordinary business grounds. One of the resolutions (as noted earlier) requested that media companies donate a percentage of their tobacco-advertising profits to fund a national antismoking advertising campaign aimed at youth. The other resolution for which the SEC has granted no-action requests was submitted to five companies that have top executives serving on the boards of tobacco companies. The targeted companies were Bell-South, Citicorp, Time Warner, US West and Wachovia. The resolution at Wachovia was withdrawn when management expressed a desire to maintain a dialogue with the proponents about tobacco issues. The resolved clause of this excludable resolution asks the companies to avoid board memberships that may pose "serious public relations problems or significant ethical conflicts which might compromise the interests of our company."

This Background Report discusses the following subjects:

- I. The FDA proposal to curb teenage smoking and industry responses (p. 7)
- II. Liability claims against the tobacco industry (p. 13)
- III. Tobacco industry restructuring (p. 18)

I. FDA PROPOSAL TO CURB TEENAGE SMOKING AND INDUSTRY RESPONSES

On Aug. 10, 1995, President Bill Clinton and the U.S. Food and Drug Administration announced a sweeping proposal that aims ostensibly to curb teenage smoking. Cigarette companies and media outlets have reacted angrily to the proposal, maintaining that the Clinton administration's real goal is to ban cigarette smoking and advertising altogether. Because of a deluge of comments—the FDA has received 570,000 pieces of mail, more than on any other FDA proposal—the agency extended its comment period by two months, which ended Jan. 2, 1996. Final regulations normally would be expected to go into effect within 60 to 90 days. But several companies and trade associations have filed suits against the FDA, which could tie up the proposal in court for years.

In his televised press conference on Aug. 10, President Clinton characterized cigarette smoking as a pediatric disease. "The evidence is overwhelming and the threat immediate," he said. "Cigarettes and smokeless tobacco are harmful, highly addictive and aggressively marketed to our young people." Clinton challenged the tobacco industry to "Show by your deeds as well as your words that you recognize that it is wrong as well as illegal to hook one million children a year on tobacco." Clinton cited statistics that 3,000 teens start smoking each day and that 1,000 of them eventually die of the effects.

For its part, the FDA made the case that it has the statutory authority to regulate tobacco products. By congressional mandate, the FDA's control is over drugs intended by their makers "to affect the structure or function of the body." Citing industry studies of addiction dating back 30 years, the FDA declared nicotine a drug and cigarettes a "drug-delivery device." Countering industry statements that smoking is not addictive, the FDA said: "Almost all the leading experts and public health organizations in the United States and in the international community, including the vast majority of scientists funded by the tobacco industry, now recognize nicotine's addictive effects." In addition, the agency cited findings by the FDA's own Drug Abuse Advisory Committee that "all currently marketed cigarettes" contain "addicting levels of nicotine."

Based on these arguments, the Clinton administration is attempting to enact the first major changes in federal government regulations on tobacco advertising and promotion since 1971, when cigarette manufacturers were required to place health-warning labels in their print advertisements. Specific elements of the new FDA proposal are as follows:

- *Sale of tobacco products to anyone under the age of 18 would be prohibited, and vendors would be required to check photo identification for proof of age.*

All 50 states now have laws prohibiting sales to minors, but enforcement is spotty.

- *Free samples and other "non-personal" sales methods, such as vending machines, self-service displays and mail orders, would be prohibited.* Cigarette sales through vending machines accounted for 1.2 percent of total cigarette sales in 1994, and free sampling accounted for 0.7 percent of total advertising and promotional spending in 1993.
- *Outdoor advertising, point-of-sale displays and advertising in publications with significant youth readership (15 percent under the age of 18) would be limited to black-and-white, text-only print.* Cigarette manufacturers spent \$867 million in these advertising media in 1993.
- *Outdoor advertising within 1,000 feet of schools and playgrounds would be banned altogether.* Since 1990, the billboard industry has agreed voluntarily not to carry tobacco or liquor advertising within 500 feet of churches and schools.
- *Display of brand names on T-shirts, caps and other promotional goods would be prohibited.* Cigarette manufacturers spent \$756 million on such specialty-item distribution in 1993.
- *Brand-name sponsorship of sporting, entertainment and cultural events would be prohibited, although corporate sponsorship still would be permitted.* Cigarette manufacturers spent \$84 million on sponsorship of such events in 1993.
- *The tobacco industry would be required to spend \$150 million a year to support an antismoking education campaign aimed at children.* By contrast, cigarette manufacturers spent about \$6 billion in 1993 to advertise and promote their products.
- *New health-warning labels on cigarettes and smokeless tobacco products would target young people.* One suggested message: "About 1 out of 3 kids who become smokers will die from their smoking."

Though the proposed FDA regulations would be mandatory on the tobacco industry, many elements of the plan are largely self-policing, which worries the industry's opponents. Primary responsibility for enforcement of sales restrictions would rest with tobacco products manufacturers—just as pharmaceutical manufacturers are required to do with their products. If a company were found to violate the FDA regulations, the agency would contact the product

manufacturer and then issue a warning letter to the company and/or retail outlets. If the warning letter went unheeded, the next step for the FDA would likely involve court action, seizure of the offending products, fines and possible criminal sanctions.

Legal Challenges to FDA Proposal

Tobacco and advertising industry executives are adamant that the FDA's proposed rulemaking goes too far. "Make no mistake, the real hidden agenda here is prohibition," said Philip Morris Executive Vice President Steve Parrish at a press conference coinciding with the FDA's Aug. 10 unveiling of the proposal. Parrish insisted that cigarette manufacturers can—and are—taking voluntary measures to discourage minors from smoking. As examples, he cited efforts to restrict youth access to cigarette vending machines, providing better training of retail sales clerks and requiring proof of age to purchase cigarettes. But, he said, "[FDA Commissioner] David Kessler is trying to sneak through the back door." He added that the FDA's proposal "can only be described as a Trojan horse, set forward under the guise of preventing youth smoking."

Daniel Jaffe, executive vice president of the Association of National Advertisers, echoed the tobacco industry's sentiment. He told *The Wall Street Journal* that the Clinton administration "is going farther down the censorship path than at any time in our history. These proposals constitute a virtual de facto ban on tobacco advertising." A consortium of advertisers has filed suit against the government, asserting that the FDA's proposed rules are an unconstitutional violation of their First Amendment rights. The advertisers have vowed to carry their fight all the way to the U.S. Supreme Court.

No sooner had the FDA proposal been announced than the nation's five major cigarette manufacturers—Philip Morris, RJR Nabisco, Brown & Williamson (a unit of B.A.T Industries PLC), Liggett Group (a subsidiary of Brooke Group Ltd.) and Lorillard Tobacco (a joint venture of Loews Corp.)—filed an injunction in the Federal District Court in Greensboro, N.C. Five smokeless tobacco manufacturers—including Brown & Williamson, UST Inc.'s U.S. Tobacco Co. and Conwood Co.—filed their own suit in the Greensboro court in September, alleging that FDA's proposal is "arbitrary, capricious" and a violation of their constitutional rights.

The plaintiffs said they decided to file their suits in the Greensboro court—officially the U.S. District Court of the Middle District of North Carolina—because it is the only jurisdiction where each of the companies has operations or interests. Perhaps not by coincidence, the Greensboro court also happens to be where tobacco companies have won some important legal challenges in recent years.

Judge William Osteen, one of the five federal judges in the Greensboro court, ruled in 1994 that a U.S. Environmental Protection Agency decision to classify second-hand smoke as a carcinogen could be reviewed in his court. Osteen then found in May 1995 that the tobacco industry had legal standing to bring a lawsuit against the government in an effort to overturn the EPA classification of second-hand smoke. Osteen now will preside over the new legal challenges filed against the FDA in the Greensboro court.

Congressional response: Meanwhile, in Congress, a group of tobacco-state congressmen, with 17 co-sponsors, introduced legislation last September in an effort to block the FDA proposal. Commerce Committee Chairman Thomas Bliley (R-Va.) has indicated, however, that there is no need for such legislation because he thinks Judge Osteen will scuttle the FDA proposal.

Shortly before the FDA proposal came out, Rep. Charlie Rose (D-N.C.) and Rep. Ron Wyden (D-Ore.) spearheaded an effort for a voluntary agreement to head off both mandatory federal regulations and the inevitable court challenges. Their idea was to have tobacco companies sign a binding agreement with the Department of Health and Human Services to eliminate advertising aimed at youth, support a ban on vending machines and youth-oriented promotional material, and contribute \$100 million or more annually to help finance antismoking education and enforcement programs aimed at youth. In return, the FDA would refrain from regulating tobacco but also would reserve the right to go forward with regulations if the tobacco companies failed to live up to their end of the bargain. According to press accounts, the deal fell through when industry negotiators balked at limiting certain ads to black-and-white text only. Moreover, tobacco companies had not committed to a spending target for programs to discourage underage smoking.

Accordingly, at his Aug. 10 press conference, President Clinton declared that "it is wrong to believe we can take a voluntary approach to this problem. And absent congressional action, and in the presence of a massive marketing and lobbying campaign by cigarette companies aimed at our children, clearly I have no alternative but to do everything I can to bring this assault to a halt."

In January 1996, 32 U.S. senators wrote President Clinton urging him to abandon the FDA proposal, breaking what had been a months-long congressional silence on the issue. At the state level, 23 attorneys general have written the president to praise the proposal, saying that "a cooperative federal and state regulatory approach is needed to effectively deal with youth and smoking."

Tobacco industry objections: On Jan. 2, 1996, the last day of an extended five-month comment period, the

five major tobacco companies filed a formal joint statement expressing their opposition to the FDA proposal. The 12-volume response runs nearly 2,000 pages, with an additional 45,000 pages of appendices. Rather than suggesting alternative ways to implement regulations to discourage underage smoking, or to achieve such goals, the companies consistently argue in their filing that the proposed rule is contrary to U.S. law and the U.S. constitution.

Legal authority—The tobacco companies' fundamental dispute is over whether the FDA has legal authority to regulate tobacco. The tobacco companies point to the law governing the FDA—the Federal Food, Drug and Cosmetic Act—and maintain that Congress has not given the FDA jurisdiction over tobacco, despite amending the law 70 times. Moreover, the companies argue, Congress has turned down legislation on 20 occasions that would have granted the FDA such regulatory authority.

Lacking this mandate, the companies accuse FDA Commissioner David Kessler, a Bush appointee, of being on a "power grab" to advance a private agenda of banning cigarettes altogether. "Make no mistake, this is the most serious threat our industry has ever seen," R.J. Reynolds warned in a packet sent to cigarette retailers. If the FDA proposal is implemented, "David Kessler and the FDA will ultimately have the power to remove cigarettes from the marketplace," the packet said.

While most observers regard the specter of a prohibition on cigarettes as highly remote and probably unenforceable, interpretation of the FDA statute could open up such a possibility. The Food, Drug and Cosmetic Act requires that drugs must be proved both "safe" and "effective" in order to be on the market, and that "habit-forming" drugs or drugs with "potentiality for harmful effects" require a physician's prescription. The FDA's *Federal Register* filing on Aug. 10 states flatly that "tobacco products plainly are not safe." Thus, strict interpretation of the FDA statute could lead to banning cigarettes from the market—but only if the FDA were to claim regulatory authority and label them as an "unsafe drug."

For his part, Commissioner Kessler has insisted that his only objective is to eliminate smoking by underage youth. But in congressional testimony in March 1994, he held out the prospect that tobacco regulation "could lead to the possible removal of nicotine-containing cigarettes from the market, limiting the amount of nicotine in cigarettes to levels that are not addictive, or otherwise restricting access to them unless the industry could show that nicotine-containing cigarettes are safe and effective." Kessler stopped short of saying that cigarettes could be withdrawn from the market altogether, however. The FDA's *Federal Register* filing last August concluded that "sudden and

total withdrawal [of cigarettes] from the market would not be in the best interests of public health."

In the same filing, the FDA said it found conclusive evidence that cigarette smoking is addictive—citing statements made by tobacco executives themselves in internal company documents. For its regulatory review, the FDA obtained 75 classified industry documents, including some with trade secrets that companies asked to be kept confidential. (For more on what these documents say, see Section II on "Recent Legal Developments.") Because the agency did not make these documents public when it proposed its rules last August, however, the tobacco companies contend that their comments on the proposal have been based on incomplete information. Under federal administrative law, a regulatory agency is supposed to disclose all information it relies upon to make a decision, giving interested parties an opportunity to respond. Tobacco industry lawyers accuse the FDA of actually relying on unpublished studies by researchers with antismoking leanings. The FDA's reference to unnamed industry documents, they say, is an attempt to legitimate unsubstantiated claims.

Product intent—In a separate legal thrust, the tobacco companies argue that the FDA should not base its decision on such internal documents in any case. They insist that manufacturers' advertising claims and public statements should be used instead. "The issue is not what the research department or the patent department or even the marketing department thinks or says internally about the product," the tobacco companies said in their written response to the FDA proposal. "Rather, the issue is what the company, as an institution, says about the product to prospective users."

The FDA disputes this argument. It cites a 1980 federal appeals court ruling that commercial intent of a product could be gauged by how the public uses it, not how the manufacturer portrays its intended use. Accordingly, private tobacco company documents explicitly characterizing nicotine as addictive would become fair game—confirming the public health record of smoking's apparent addictive effects. The industry's counter-argument, according to attorney Matt Myers of the Coalition on Smoking OR Health, an antismoking group, is "that by covering up what they knew about the role of nicotine in their products, [the tobacco industry] should forever be protected."

Nicotine manipulation—On the record, the tobacco industry is sticking by its claim that cigarette smoking is not addictive and that nicotine does not fit the legal definition of a drug. In their response to the FDA proposal, the companies point to the fact that some 43 million Americans have quit smoking over the last 25 years. Moreover, "To say that cigarettes are sold for medical purposes,

whether as a device like a pacemaker or a drug like penicillin, defies common sense," remarked Philip Morris's Steve Parrish in a Jan. 2 press conference to discuss the industry's response to the FDA proposal.

In their written response, the companies repeated their claim that they do nothing to control levels of nicotine in growing tobacco or manufacturing cigarettes. Undercutting one of the FDA's main arguments, they denied using ammonia-based chemicals to boost the pH, or alkalinity, of smoke, which in turn enhances the absorption of the nicotine smokers inhale. Their submission stated that "virtually all of the nicotine in cigarette smoke is absorbed into the bloodstream regardless of the pH of the smoke."

Regulatory costs—Finally, the tobacco companies argued in their submission that compliance with the FDA proposal would be expensive—requiring \$1 billion in start-up costs and \$1 billion more in annual costs for manufacturers and retailers. The FDA estimates that the annualized cost of its proposed rule is only \$230 million a year over 15 years. The FDA also estimates that the benefits of the regulation would be \$2.9 billion to \$4.3 billion a year, measured mainly in lives saved. (The tobacco companies did not offer an estimate of benefits that might come from the proposal.) As for the impact on investors, one tobacco industry analyst, Fred Taylor of Salomon Brothers, estimates that the mere existence of the FDA proposal is depressing the price of tobacco stocks and bonds by 20 percent.

Other Industry Responses to FDA Proposal

Tobacco companies are not the only ones objecting to FDA's proposed rulemaking. Advertisers, media companies, retail outlets and even makers of vending machines have filed suits or vehement objections to the FDA proposal. The strong stands taken by these industries involve arguments of principle—but also reveal the extent to which the tobacco industry and other sectors of the economy are linked. According to a tobacco industry-funded study by Price Waterhouse, the jobs of some 468,000 people depended on the tobacco industry as suppliers, wholesalers and retailers in 1990, in addition to 200,000 people who worked on tobacco farms or in manufacturing facilities for the \$45-billion industry.

Media advertisers: Tobacco companies spent more than \$400 million on media advertising in 1994, according to figures compiled by the Federal Trade Commission, including \$122 million on outdoor advertising and \$285 million on magazine advertising. Under the FDA proposal, outdoor billboards and kiosk tobacco ads would be limited to black-and-white text only, as would advertisements in magazines with either at least 15 percent readership or at least 2 million readers under the age of 18.

If tobacco companies stopped advertising under these restrictions, media companies would lose a significant source of revenue. Tobacco ads accounted for about 12 percent of outdoor advertising revenue in 1994, representing that industry's second largest source of income (behind entertainment and amusement ads). The magazine industry also has benefited from rising tobacco ad spending in recent years, which accounted for more than 3 percent of total magazine advertising revenue in 1994.

Companies like Time Warner (which has a shareholder resolution pending on voluntary compliance with the FDA proposal) could be especially hard hit. Time-Warner's *People* and *Sports Illustrated* magazines have more than 15 percent youth readership and, by some estimates, take in one-quarter of all cigarette advertising revenue in magazines.

In response to the FDA proposal, six advertising trade associations, including the Association of National Advertisers and the American Association of Advertising Agencies, have filed suit in the Federal District Court in Greensboro, N.C. The advertisers contend that the proposed advertising restrictions represent an unconstitutional infringement of free speech.

"The next thing you know, the government will put ice cream on the list of products to regulate because it's known to cause high cholesterol," quipped Kent Brownbridge, senior vice president of Wenner Media, publisher of *Rolling Stone* magazine. "If tobacco is so bad, why not ban it entirely?," he said in an interview with *The Wall Street Journal*. "These regulations are ridiculous. How can you have something that is legal and yet can't be advertised?," he asked.

One response to such criticisms was offered by President Clinton at his Aug. 10 press conference. "It cannot be a violation of the freedom of speech in this country to say that you cannot advertise to entice [young] people to do something which they cannot legally do," he said. John Banzhaf, a George Washington University law professor who led the fight to get antismoking ads on television free of charge in 1971, offers another rationale. "We restrict advertising of [legal] drugs," he points out. "If we are going to treat nicotine as a drug, then such restrictions are justified and needed."

Knight-Ridder initiative—While the debate over tobacco advertising continues at the national level, in the fall of 1995 one of the nation's largest media conglomerates announced new, but voluntary, guidelines for its newspapers and other print publications. Knight-Ridder Inc. issued the guidelines following a shareholder proposal that received support from 14.4 percent of the shares voted at its 1995 annual meeting. The resolution requested that

management develop new, ethical criteria for accepting tobacco ads.

Knight-Ridder's new guidelines could leave some now-familiar cigarette advertisements on the editing room floor. Tobacco ads that Knight-Ridder's management now disapproves of include those with cartoon depictions that could be interpreted as targeting children, such as R.J. Reynolds' "Joe Camel" character for Camel cigarettes. The guidelines also shun common tobacco ad references to being "cool," "alive with pleasure" or enjoying "the good life." And they call for rejection of cigarette ads giving consumers the impression "that smoking or other use of tobacco products leads to prominence, social distinction, success, sexual attraction or physical beauty." Considering that the 1994 Surgeon General's report on smoking and youth concluded that cigarette ads rely heavily on the "five Ss,"—slim, sexy, sociable, sophisticated and successful—a broad interpretation of this guideline could cause Knight-Ridder editors to reject most cigarette print advertisements. But Knight-Ridder stresses that its local newspapers still have the final say over which tobacco ads to accept, in accord with local community standards and practices.

Nationwide, cigarette companies paid \$36.2 million for newspaper advertising in 1993, accounting for less than 1 percent of total newspaper advertising revenue.

Convenience stores: Following the lead of tobacco companies and advertising media, the convenience store industry sued the FDA in October to block its plan to regulate the sale of cigarettes to minors. The suit, filed by the National Association of Convenience Stores, contends that the proposed ban on cigarette advertising inside stores violates First Amendment free-speech guarantees and represents an illegal government taking.

The FDA is especially interested in targeting convenience stores for advertising restrictions, because surveys indicate that more underage smokers, ages 13 to 17, typically buy cigarettes in convenience stores than from any other source. What is more, young- to middle-age blue-collar workers—a prime market for tobacco companies—comprise more than half of convenience stores' customer base, and adult smokers represent fully 40 percent of the stores' customer base, well above the national average of 25 percent.

The FDA's proposal would ban self-service displays for cigarettes and chewing tobacco, and would eliminate signs, posters and virtually all other tobacco advertising inside the nation's 90,000 convenience stores. The tobacco industry spent \$400 million on such in-store, point-of-sale advertising in 1993. That works out to an average of \$3,000 to \$5,000 in promotional allowances per store.

Notably, Southland Corp.'s 7-Eleven chain, which is the biggest member of the National Association of Convenience Stores, did not join the trade association's lawsuit against the FDA. When the FDA proposal was announced last August, Southland commended President Clinton for assuming leadership on the issue of restricting tobacco sales to minors—but stopped short of endorsing the FDA proposal specifically.

Philip Morris initiative—In an apparent attempt to head off the FDA proposal announced last August, Philip Morris announced a new voluntary initiative in June 1995, dubbed "Action Against Access." Under the initiative, Philip Morris pledged to deny merchandising and participation in its retail incentive program to stores that are fined or convicted of selling cigarettes to minors. The plan also calls for posting of minimum-age signs in all retail outlets and placing cigarettes for sale "within the line of sight or under the control of a sales clerk, unless access to the outlet is denied to minors." As for its own cigarette packaging, Philip Morris added a notice stating, "Underage Sales Prohibited."

The most controversial element of the new Philip Morris plan is a call for state licensing of cigarette retailers. The plan recommends that states pass "reasonable" legislation requiring all cigarette retailers to be licensed, with "fines and possible suspension or revocation of licenses" of those who are caught selling cigarettes to minors. At present, 41 states and the District of Columbia require such licensing of cigarette retailers, but only nine states include penalties leading up to revocation of a license for selling to minors, according to the Coalition on Smoking OR Health.

Cigarette retailers—which have been long-time supporters of the tobacco industry—have reacted angrily to Philip Morris's new action plan, accusing the company of trying to shift blame for underage smoking onto storekeepers. "It is disappointing that the priorities of the largest tobacco manufacturer in the nation have degenerated to posturing blame," wrote the National Association of Convenience Stores, in a stern letter to Philip Morris. "Your plan will certainly punish our industry for these events, but it will not solve the problem." Another letter written to Philip Morris by convenience store owner Bobby Sproles of Bristol, Va., tried to put the onus back on the company. "Retailer outlets handle your product because of its demand created by your high-powered advertising," Sproles charged.

Even other tobacco companies have called Philip Morris's motives into question, noting that limiting cigarette sales to areas within a clerk's sight could drastically cut shelf space for competing companies' brands.

As part of its new effort to keep cigarettes out of the hands of minors, Philip Morris also announced that it was discontinuing its practice of offering free cigarette samples to consumers, either by mail or in person. Rival R.J. Reynolds' got into trouble last year when the television program *A Current Affair* showed two girls, ages 16 and 17, successfully receiving free packs of Reynolds cigarettes at three different auto races sponsored by the company. After the program aired, Reynolds added requirements that people wanting free packs now must show proof that they are at least 21 years old, but it has not ended the practice of giving away free samples.

Vending machine operators: America's vending machine industry also has entered the fray over the FDA proposal, since it would ban vending machines that sell cigarettes. The Amusement and Music Operators Association, whose members operate about 80 percent of the nation's cigarette vending machines, argues that the FDA proposal unfairly singles out the vending machine industry because of its automated mode of transaction. The association says that 90 percent of its members' cigarette vending machines already are in age-restricted areas and that "lock-out" devices could be added to the rest to prevent cigarette purchases by minors.

In 1994, America's 400,000 cigarette vending machines dispensed about 300 million packs of cigarettes, representing 1.2 percent of all cigarettes sold. Those sales generated nearly \$2 billion of revenue for vending machine operators and accounted for 6.8 percent of all vending machine sales, according to the publication *Vending Times*.

Cigarettes are not nearly as big a business now for vending machine operators as they were in the early 1970s, however. At that time, reports the National Automated Merchandising Association (another vending machine industry group), almost 18 percent of all cigarettes sold were through vending machines, accounting for about 25 percent of all vending machine sales.

Higher prices for cigarettes sold in vending machines and proliferation of state and local vending restrictions have crimped the industry's sales of cigarettes. According to Americans for Nonsmokers' Rights, an antismoking group based in Berkeley, Calif., cigarette vending machines have been banned in 120 municipalities. Another 137 municipalities, including Chicago and Seattle, as well as the states of California, New York, Nebraska, Utah and Hawaii, restrict the machines to bars and other age-restricted facilities.

Despite the decline in cigarette vending machines sales, the anonymous sales method appeals to some young smokers who fear being "carded" by a store clerk. A recent survey by the National Automated Merchandising

Association found that 22 percent of 13-year-old frequent cigarette purchasers use vending machines often to buy cigarettes. The percentage declines to just 2 percent of 17-year-old smokers, however. "Overall, vending machines are a minor source of tobacco for [underage smokers], but they are an important source for the youngest kids," concludes Dr. Joseph DiFranza, a professor of family and community medicine at the University of Massachusetts. DiFranza has conducted several studies documenting the means by which youth gain access to tobacco products.

As part of its "Action Against Access" campaign, Philip Morris has recommended that vending machines be equipped with lock-out devices, activated by store clerks, to prevent purchase of cigarettes by minors. The vending machine industry also likes the idea, which it says make vending-machine cigarettes no more accessible to minors than those sold from behind a counter. Critics of the devices say that retailers often fail to activate the devices and are not as inclined to check identification as with face-to-face sales. Nevertheless, in their comments to the FDA, vending machine operators maintain that a combination of lock-out devices and placing vending machines in age-restricted areas puts these vendors on "equal footing" with other tobacco retailers and that they should be entitled to the same rights and privileges under the law.

Sports and entertainment industry: Sports and entertainment promoters also may feel a pinch from the FDA proposal, given its call for a ban on cigarette and smokeless tobacco brand-name sponsorship of such events. Although Philip Morris ended its 24-year sponsorship of the Virginia Slims tennis tournament in 1994—partly as a result of public pressure—cigarette companies continue to sponsor a huge number of events each year, including: the Kool Jazz Festival, the Vantage senior pro golf tour, Marlboro Cup horse racing, Salem Pro-Sail races, Benson and Hedges on Ice, Lucky Strike bowling and the Copenhagen Skoal Pro Rodeo. Even Philip Morris's connection to Virginia Slims lives on through its sponsorship of a "legends tour" that includes tennis stars like Pam Shriver and musical artists like Gladys Knight.

By far the biggest beneficiary of tobacco money has been auto racing. R.J. Reynolds, the maker of Camel and Winston brands, has sponsored the National Association of Stock Car Auto Racing's (Nascar) Winston Cup auto racing series since 1970. Over the years, Reynolds has doled out more than \$200 million in organizing funds, prize money and contributions to local tracks. Philip Morris's Marlboro brand also sponsors Indy car and Formula One auto races.

Under the FDA proposal, tobacco companies could maintain their sponsorship of sporting and entertainment

events—but only under their corporate names. Hence, the “Winston” racing circuit would become the “Reynolds” racing circuit. Moreover, brand names could still appear on sports cars—but in black-and-white text only. Other tobacco advertising at sports stadiums and outdoor arenas would be confined to text only on billboards and kiosks. While tobacco advertising remains prominent at professional baseball, basketball and football games, stadium owners have agreed to keep these ads out of view of television cameras.

The Synar Amendment

While legal wrangling over the FDA proposal to curb teenage smoking could go on for years, a separate federal regulation aimed at reducing illegal sales of tobacco to youth is about to go into effect. The regulation, known as the Synar amendment, is named after the late Rep. Mike Synar (D-Okla.), who attached the amendment to 1992 legislation authorizing the use of federal block grant funds for state efforts to reduce drug abuse. Under the amendment, the Department of Health and Human Services will reduce the size of the block grants by 10 percent for states failing to show significant reductions in illegal sales of cigarettes to children under the age of 18. Several studies have shown that up to 70 percent of children trying to buy cigarettes from sales clerks and vending machines now do so unchallenged.

Unlike the current FDA proposal, the Synar rule is in final form and is not subject to further comment by industry. (The Department of Health and Human Services is expected to issue its final regulations in the next few weeks.) The rule will require states to demonstrate compliance with their own minimum-age laws in order to receive full funding under the Alcohol, Drug Abuse and Mental Health Administration Reorganization Act, a federal program that distributes about \$1.3 billion in block grants each year. Although all 50 states have enacted laws prohibiting tobacco product sales to minors under the age of 18, enforcement and supporting legislation have varied widely. The Synar amendment’s key provisions are:

- The state must have in force a minimum-age law prohibiting the sale or distribution of any tobacco products to those under the age of 18.
- The state must conduct annual, random and targeted, unannounced inspections of both over-the-counter and cigarette vending machine outlets.
- Random inspection of sales to minors must not exceed 50 percent violations during the first applicable fiscal year, and the state must work toward a goal of reducing illegal sales to minors down to 20 percent—although it has considerable leeway in setting a timetable to achieve that goal. (Originally, the law required that the goal be met in four years.)
- To reduce the prevalence of violations, a state may institute a tobacco sales licensing system similar to that used for sales of alcoholic beverages; a graduated schedule of penalties for illegal sales or distribution culminating in loss of license; controls on tobacco vending machines in locations accessible to minors; and use of local enforcement to supplement central enforcement.

While all 50 states have passed laws bringing them into technical compliance with the Synar amendment, tobacco interests have lobbied vigorously at the state level to keep potential penalties for violations of the laws to a minimum. One common industry tactic has been to support state laws that pre-empt even tougher antismoking measures enacted at the local level. A report by the Health and Human Services inspector general found that only two states, Florida and Vermont, were providing effective statewide enforcement against sales to minors in 1994. While the Synar rule is expected to pressure states to improve their enforcement efforts, it does not appear likely to require any states to repeal existing legislation. Some states have criticized the Synar rule because it does not provide any federal funding to pay for increased implementation and enforcement programs.

II. LIABILITY CLAIMS AGAINST THE TOBACCO INDUSTRY

The greatest threat to the U.S. tobacco industry over the long term may not be regulation by the Food and Drug Administration, but evidence compiled during the course of recent FDA and congressional investigations that could lead to an increase in liability claims against tobacco companies. Documents obtained in conjunction with these federal investigations—and others leaked to the press by former industry insiders—raise serious questions about

what tobacco companies know about nicotine and its effects on the body, and how long they have known it; whether they have intentionally suppressed or destroyed such information; and whether tobacco processing methods give companies the ability to exercise precise control over the nicotine content of their products—and the amount of nicotine that smokers inhale with each cigarette.

To date, no U.S. tobacco company has yet to pay any claims as a result of tobacco product liability lawsuits, even though smoking is thought to be responsible for more than 400,000 deaths a year in the United States and adds \$50 billion a year in estimated health care costs. Most of the suits to date, however, have been brought by individuals whose legal and financial resources are no match for those of tobacco companies.

In the last 18 months, five states have filed class-action lawsuits against tobacco companies in an effort to recover costs paid out to Medicaid recipients for smoking-related illnesses. Armed with new information from the federal investigations as well as document leaks from industry insiders, these state suits pose a formidable new legal challenge for tobacco companies and even cast a shadow over their ongoing restructuring efforts. If the courts were to award damages in excess of the net worth of the tobacco companies, the plaintiffs might seek to acquire spun-off assets that companies had hoped to protect from such claims. (See Section III for more information on tobacco industry restructuring.)

Fallout from Recent Investigations

Day One report: The tobacco industry's recent legal difficulties began to mount in February 1994 when the ABC television network aired a *Day One* investigative report about the tobacco industry. In the report, a number of industry insiders, including a former manager for RJR Nabisco's cigarette operations, claimed to have detailed technical knowledge of how tobacco companies use nicotine in cigarettes. Based on these interviews and other information obtained by ABC, *Day One* correspondent John Martin reported to viewers that tobacco companies "spike" cigarettes with nicotine. Such a charge, if proven, would bolster the FDA's case that cigarette manufacturers should fall under the agency's jurisdiction, because they are able to manipulate the "dose" of nicotine that smokers ingest.

Immediately after the broadcast, Philip Morris filed a \$10 billion libel suit against ABC. The tobacco giant insisted that its cigarettes are not "spiked" with nicotine from "outside sources," but merely that nicotine removed early in the manufacturing process gets added back in. The re-injection process is necessary, Philip Morris explained, because naturally occurring levels of nicotine decline when varieties of tobacco leaf and filler (mainly tobacco stems and dust) are shredded and blended to alter a cigarette's flavor. Nicotine lost in the tobacco reconstitution process is added back in the form of a nicotine extract spray, with the restored amount of nicotine not exceeding that of unprocessed leaf tobacco, according to the company.

Philip Morris agreed to drop its lawsuit against ABC in August 1995, when the network agreed to air an unusual public apology in which it stated it was a "mistake" for *Day One* to have suggested that "Philip Morris and [R.J.] Reynolds add significant amounts of nicotine from outside sources." Philip Morris reprinted ABC's statement in full-page advertisements, adding: "As for the group of people who eagerly embraced the 'spiking' allegation to serve their ongoing crusade against the tobacco industry—we stand ready to accept their apologies as well."

Notably, however, ABC did not recant what it views as the basic message of the *Day One* broadcast: that cigarette companies use the reconstituted tobacco process to control levels of nicotine in cigarettes. To the industry's critics, the fact that existing technology enables tobacco firms to exert control over the amount of nicotine in their products brings into question why they cannot bring nicotine levels below the threshold of addiction (if that threshold can be determined)—or why cigarettes need to contain nicotine at all. The tobacco industry responds that nicotine is an essential flavoring, and that nicotine-free cigarettes would not sell. (Indeed, Philip Morris introduced a "denicotined" cigarette in 1989, but it flopped in market tests and was never broadly introduced.)

Philip Morris's lawsuit against ABC, though settled, continues to be a source of concern for the company—and the industry at large. In January 1996, *Legal Times* printed excerpts from a legal brief purportedly prepared by ABC's lawyers in the event the Philip Morris's suit went to trial. The brief, and the documents it cites, appear to back up ABC's claims that Philip Morris and other tobacco companies employ sophisticated means to inject nicotine in cigarettes—knowing full well that nicotine is addictive. Philip Morris says the brief, which remains under court seal, includes claims that are "demonstrably false and misleading." But the industry's critics insist that the brief provides further ammunition for plaintiffs in court battles who are suing tobacco companies for damages, and bolsters FDA's bid to regulate tobacco as a drug.

1994 Congressional hearings: Two months after ABC aired its controversial *Day One* broadcast, Rep. Henry Waxman (D-Calif.), then chairman of the House Subcommittee on Health and Environment, convened highly publicized hearings in which the top executives of the nation's seven largest tobacco companies testified under oath. Waxman and Rep. Ron Wyden (D-Ore.) asked the executives a series of tough, pointed questions that have dogged the industry for years: whether they knew of any compelling evidence that smoking causes disease and death, whether nicotine is addictive, whether and how their companies control the nicotine levels of their products,

and whether chemical additives used in cigarette manufacturing pose potential health risks to smokers.

In their written and oral testimony, the executives reiterated the industry's long-standing position that, while there is a statistical correlation between smoking and an increased incidence of certain illnesses, scientific evidence does not prove that smoking causes disease. Moreover, regarding nicotine and addiction, William Campbell, who was then the head of Philip Morris's tobacco unit, said that "nicotine contributes to the taste of cigarettes and the pleasures of smoking. The presence of nicotine, however, does not make cigarettes a drug or smoking an addiction."

James Johnston, chairman and chief executive officer of R.J. Reynolds Tobacco Worldwide, went even further in his written testimony. Under the FDA's definition of addiction, he said, "cigarette smoking is no more addictive than coffee, tea or Twinkies." He added, "Cigarettes are clearly not in the same class as addictive, mind-altering [drugs] like heroin and cocaine."

The congressional hearings prompted a flood of tips to Waxman's subcommittee and the FDA that the tobacco industry executives were not telling the whole truth. A federal grand jury now is looking into whether any tobacco company executives perjured themselves in their congressional testimony or other sworn statements. Prosecutors reportedly are reviewing the executives' statements in light of internal industry documents that have surfaced in months following the hearings that appear to contradict their statements about nicotine addiction and manipulation of nicotine in their tobacco products.

Following the latest allegations in the leaked ABC legal brief to the *Legal Times*, Rep. Waxman has called for Philip Morris's William Campbell to return to Capitol Hill to explain alleged discrepancies in his congressional testimony. However, Rep. Thomas Bliley (R-Va.), who now chairs the House Commerce Committee, says he has no intention of reconvening hearings on the tobacco industry. Philip Morris manufactures Marlboro cigarettes in Bliley's home district of Richmond, Va.

Leaked industry documents: One damning piece of evidence released at the time of the 1994 congressional hearings was a cache of documents reportedly stolen by a former legal aide of Brown & Williamson, the U.S. subsidiary of British tobacco giant B.A.T Industries. The documents suggested, among other things, that the company had long known that smoking was addictive and could cause lung cancer and heart disease. One passage from an internal memo written by a company official in 1963 stated, for example, "We are, then, in the business of selling nicotine, an addictive drug effective in the release of stress mechanisms."

Brown & Williamson filed subpoenas in an attempt to reclaim the leaked documents, but a federal judge in Washington, D.C., threw out the subpoenas and accused the company of trying to interfere with Waxman's congressional hearings. The company insisted that portions of documents had been cited out of context and denied ever having scientific proof that nicotine is addictive. "It has always been B&W's position—and still is—that cigarette smoking is not addictive under the standards set forth in the 1964 Surgeon General's Report," the company said in a May 1994 press release.

In the summer of 1995, the *Journal of the American Medical Association* published an analysis of the stolen B&W documents, copies of which were obtained by Dr. Stanton Glantz, a cardiologist and professor at the University of California, San Francisco. Glantz' highly critical article prompted the American Medical Association to issue 14 recommendations to reduce smoking and undercut the political and financial clout of the tobacco industry. "The evidence is unequivocal," the AMA said in an editorial accompanying Glantz' article: "The U.S. has been duped by the tobacco industry," adding, "we should force the removal of this scourge from our nation."

FDA revelations—For years, the FDA has been trying to build its case that tobacco companies know of the dangers of smoking and are effectively in the drug delivery business, manipulating nicotine levels in cigarettes. Building on the momentum of ABC's controversial *Day One* program—and in anticipation of Rep. Waxman's congressional hearings—FDA Commissioner David Kessler decided to step up his agency's own investigation in the spring of 1994. Kessler sent several FDA research teams into the field to question tobacco company executives, former industry researchers and outside experts about what they knew about nicotine's addictive effects and how tobacco companies formulated and marketed their products to optimize these effects on smokers.

The FDA's filing in the *Federal Register* on Aug. 10, 1995, culminated more than a year of intensive research. "Based on the evidence now before the agency," the FDA stated, "cigarettes and smokeless tobacco products are drug delivery systems whose purpose is to deliver nicotine to the body in a manner in which it can be most readily absorbed by the consumer...." That finding now forms the basis of FDA's assertion of regulatory authority over the promotion and marketing of cigarettes and smokeless tobacco products.

Passages from industry documents cited in the FDA's *Federal Register* filing appeared to confirm that tobacco companies have known for years about nicotine's addictive qualities, and that young people—including teenagers—are prime targets for tobacco advertising and promo-

tions. Some of the documents cited in the FDA filing date back 30 years, such as one by British American Tobacco Co. that found a smoker who is denied nicotine "craves for renewed drug intake in order to restore the physiological equilibrium. This unconscious desire explains the addiction of the individual to nicotine."

As further evidence from tobacco industry files that nicotine is addictive, the FDA cited research conducted by B.A.T Industries to determine "a smoker's daily nicotine requirement." The study, undertaken in 1981, sought to establish "the minimum dose of nicotine that can provide pharmacological satisfaction." The FDA also quoted an R.J. Reynolds tobacco executive who said in an internal memo: "In a sense, the tobacco industry may be thought of as being a specialized, highly ritualized, and stylized segment of the pharmaceutical industry."

Regarding smoking by America's youth, the FDA said in its filing that tobacco companies regard "acquiring a portion of the 'starter market'—overwhelmingly people in their teens—...as [being] essential to a company's continuing economic vitality." One cited study was a 1969 report presented to Philip Morris's board, which tried to explain what attracts young people to smoking. "The 16- to 20-year old begins smoking for psychosocial reasons," the report stated. "The act of smoking is symbolic; it signifies adulthood; he smokes to enhance his image in the eyes of his peers."

Other studies quoted in the FDA's *Federal Register* filing noted the difficulty young smokers experience when they try to quit. "However, intriguing smoking was at 11, 12 or 13," noted one report to Imperial Tobacco Co., "by age 16 or 17 many regretted their use of cigarettes for health reasons and because they feel unable to stop smoking when they want to." The FDA filing also cited a 1988 marketing plan from Imperial Tobacco that asserted, "If the last 10 years have taught us anything, it is that the industry is dominated by companies who respond most effectively to the needs of younger smokers."

Some claims made in the industry's formal response to the FDA filing also appear to be at odds with past statements made in internal company documents. A confidential 1992 Philip Morris document stated, for instance, that "the primary reason" people smoke is "to deliver nicotine to their bodies" and that nicotine is chemically "similar" to drugs like cocaine and morphine. The document addressed Philip Morris's proposal for a "safer" cigarette that would virtually eliminate tar—which contains most of the cancer-causing agents in cigarettes—while retaining nicotine, "which alters the state of the smoker." The document went on to characterize a smokeless cigarette as a "nicotine delivery device," not unlike other nicotine-containing substances, ranging from "snuff, chewing to-

bacco, cigars, pipes and conventional cigarettes to unique smoking articles, chewing gum, patches, aerosol sprays and inhalers." Lumping cigarettes with other products whose function clearly is to dispense nicotine may be useful to the FDA in its effort prove that tobacco companies are in the drug-delivery business.

In October 1995, *The Wall Street Journal* obtained copies of internal documents from Brown & Williamson that described ways in which leading tobacco companies, including Philip Morris, add ammonia-based compounds to cigarettes as a means to enhance nicotine delivery. One of the findings put forward in these documents is that cigarette manufacturers can use ammonia-based compounds to "boost" the effect of nicotine on smokers, rather than adjusting nicotine levels directly. The finding calls into question tobacco company claims that nicotine levels in cigarettes are no higher than nicotine levels in pure tobacco, since ammonia "boosts" nicotine's effect.

A 54-page B&W handbook for leaf blenders and product developers says that ammonia chemically liberates nicotine into a free state that "is associated with increases in impact and satisfaction reported by smokers." The FDA interprets words such as "impact" and "satisfaction" as euphemisms for the drug-inducing effect of nicotine. "Despite the buzzwords used by industry, what smokers are addicted to is not 'rich aroma' or 'pleasure,'" FDA Commissioner Kessler testified in Congress. "What they are addicted to is nicotine, pure and simple."

Brown & Williamson disputes this contention. "The word 'impact' doesn't have anything to do with the absorption of nicotine into the bloodstream," said Bert Rein, a Brown & Williamson lawyer. "We use the word impact to deal with transitory, sensory impact, occurring in the back of the throat—not on the central nervous system."

Marlboro and the ammonia factor—Perhaps the most intriguing argument put forth in the leaked Brown & Williamson documents is that it identifies ammonia as "the key factor" in the success of Philip Morris's Marlboro brand, the number one-selling brand of cigarettes in the world. Introduced in 1924 as a woman's cigarette, Marlboro still had a small market share in the early 1950s—and Philip Morris ranked dead last in sales among the six U.S. cigarette manufacturers. In 1954, however, Philip Morris decided to relaunch its Marlboro brand with its now-famous red-and white-box and macho advertising images of cowboys, sports car drivers, sheriffs and military officers (later reduced just to cowboys in 1963.)

Unbeknownst to Marlboro smokers, however, Philip Morris also had reformulated the cigarette—with broken tobacco leaves, stems and dust—to reduce its cost. But the reconstituted tobacco filler, known as bandcast, presented

a manufacturing problem: it tended to fall apart during processing. Philip Morris's solution was to introduce an ammonia compound called DAP, which released glue-like pectins that kept the bandcast together.

According to Brown & Williamson's handbook for tobacco leaf blenders, DAP turned out to have a serendipitous effect on Marlboro smokers, serving as an "impact booster" and "satisfaction promoter." When Philip Morris shifted to a different kind of reconstituted tobacco in the 1970s that was cheaper to produce than bandcast, Philip Morris continued to add ADP and other ammonia-releasing chemicals to maintain nicotine delivery, the B&W handbook reported. "ADP-treated bandcast is the soul of Marlboro," the handbook maintained.

The B&W handbook went on to report that Lorillard, maker of Kent and Newport cigarettes, has applied DAP directly to tobacco leaves for many years, and "we now find a considerable amount of DAP in the recon used in many Lorillard brands." The handbook also suggested that R.J. Reynolds applies ammonia to certain brands, most notably Winston. RJR officials told *The Wall Street Journal* in October 1995 that it adds "minuscule" amounts of ammonia-based compounds to tobaccos it uses in certain brands.

The B&W leaf blenders' manual also said that American Tobacco Co., acquired by Brown & Williamson in 1994, uses a filler containing DAP in some new brands. Only Liggett Group (a unit of Brooke Group Ltd.) appears not to have used ammonia technology, according to the B&W manual. Liggett is the nation's smallest U.S. tobacco firm, with a 2.3 percent market share.

Defection of Jeffrey Wigand: At present, the case drawing the most attention is that of Jeffrey Wigand. Wigand served as Brown & Williamson's vice president for research from 1989 until he was fired in March 1993. As such, he is the highest-ranking tobacco executive to divulge industry secrets. In November 1995, Wigand was prepared to go public in a CBS News *60 Minutes* report with accusations that the tobacco industry had covered up research about the hazards of tobacco and lied about the effects of nicotine on tobacco users. CBS chose not to air an interview, however, after Brown & Williamson threatened to sue the network and hold CBS responsible for any libel contained in the *60 Minutes* broadcast.

Wigand had signed a confidentiality agreement barring contacts with the media when Brown & Williamson fired him in 1993. (Wigand claims he was coerced into the agreement because he was seeking continuation of health benefits for a sick family member.) Now Brown & Williamson is suing Wigand for allegedly leaking information to *60 Minutes* and for taking documents containing "highly

confidential trade secrets" that became the subject of articles in *The Wall Street Journal* and *The Washington Post*. CBS has agreed to indemnify Wigand in Brown & Williamson's suit.

Several states and the U.S. Justice Department also have subpoenaed Wigand to support their own ongoing investigations of the tobacco industry. For example, one federal antitrust probe alleges industry "collaboration with competitors to inhibit research" on fire-safe cigarettes. Wigand wrote in a deposition last summer that "The technology to develop a cigarette with a significantly reduced ignition propensity by reducing tobacco packing density and/or circumference has been available for at least 30 years."

Federal investigators also have subpoenaed Wigand for another probe that is believed to be related to the Justice Department's criminal investigation of allegations that tobacco company executives perjured themselves in their 1994 congressional testimony. According to the *New York Daily News*, which published an account the *60 Minutes* interview with Wigand that never aired, Wigand said he believed that Brown & Williamson's former chief executive officer, Thomas Sandefur, committed perjury and knew that cigarettes were a "delivery device for nicotine." (Sandefur retired from Brown & Williamson in April 1995.)

State Lawsuits

Over the last 18 months, five states—Florida, Massachusetts, Minnesota, Mississippi and West Virginia—have filed class-action lawsuits against the tobacco industry, seeking billions of dollars in compensation for payments the states have made for Medicaid patients with smoking-related illnesses. Several other states reportedly are considering such suits, including Maryland, which estimates that it spent \$47.5 million on Medicaid in 1993 for smoking-related hospitalizations. Damage claims, if awarded in these suits, could wipe out the operating profits of most tobacco companies.

The most recent state to sue the tobacco industry for Medicaid claims is Massachusetts, which filed its complaint on Dec. 19, 1995. Attorney General Scott Harshbarger estimates that Massachusetts spends \$200 million a year in Medicaid to treat smoking-related illnesses. The suit seeks more than \$1 billion in damages. Six tobacco companies, two tobacco trade associations and two tobacco distributors are named in the Massachusetts suit, accusing them of conspiring for decades to "mislead, deceive and confuse" the public about the risks of smoking. Harvard Law School Professor Laurence Tribe, considered one of the nation's leading scholars on constitutional law, has been sworn in as a special assistant attorney

general and will serve as a chief litigator for Massachusetts. Tribe also helped prepare similar cases now going forward in Florida and Mississippi.

In Florida, like Massachusetts, state legislators have passed a law making it legal for the state to sue tobacco companies for Medicaid costs. Tobacco companies have challenged the constitutionality of the Florida law, however, and the case is now before the Florida Supreme Court. (Also in Florida, the state Board of Administration filed suit against Philip Morris in late 1994, charging that the company inflated stock prices by concealing information on the addictive properties of nicotine and the company's ability to control the nicotine levels of its products.)

Rather than building its case against the tobacco companies on state legislation, Massachusetts has grounded its arguments on common law—a tactic that the state of Mississippi has also used. The tobacco companies have responded to the suit by filing a countersuit against Attorney General Harshbarger. The countersuit alleges that Harshbarger's suit would violate tobacco companies' constitutional right to engage in commerce in Massachusetts and elsewhere.

In Mississippi, former Brown & Williamson vice president Jeffrey Wigand has been subpoenaed to address 11 topics, including whether the company conducted "marketing research on under aged teenagers and children," whether law firms representing Brown & Williamson conducted cigarette research in order to shield the company from "lawful discovery" and whether Brown & Williamson executives provided "false or materially misleading testimony" to Congress on nicotine's addictive effects.

In his first deposition in the case on Nov. 29, Wigand reportedly gave information that heightened the state's interest in former Brown & Williamson CEO Thomas Sandefur and General Counsel J. Kendrick Wells III. Mississippi state attorneys have since filed a motion to expedite depositions by Sandefur and Wells, and asked a state court for a restraining order to prevent Brown & Williamson or its attorneys from "altering, falsifying, exporting, destroying or otherwise engaging in the spoliation of documents." Attorneys representing Mississippi say they are concerned

that the company may try to destroy incriminating documents or ship them out of the country.

Private-sector legal suits: The incriminating evidence mounting against the tobacco industry also could have a bearing on two big private class-action suits now pending. A Florida state court judge granted class certification in *Engle v. R.J. Reynolds Tobacco Co. et al.* in October 1994. A federal court judge in Louisiana heard class certification arguments for *Castano v. The American Tobacco Co. et al.* in December 1994.

Both cases include plaintiffs who want to hold tobacco companies strictly liable for their alleged addiction to cigarettes and are suing for compensatory and punitive damages. The suits include charges of fraud and misrepresentation, conspiracy to commit fraud, breach of warranty and negligence. Plaintiffs in the *Castano* case are represented by \$6 million per year of billing time and materials donated by a 60-firm team of some of the country's most prominent lawyers, making it the first plaintiffs' representation in a private suit to match the tobacco industry's legal defense in sheer size and financial clout.

Finally, in a landmark case regarding exposure to second-hand smoke, a federal hearing examiner awarded death benefits in December 1995 to the widower of a Veterans Administration nurse who allegedly contracted lung cancer from exposure to second-hand smoke while treating mentally ill veterans. (Neither the nurse nor her husband smoked.) In the past, the federal government has awarded claims for respiratory illness and other ailments related to second-hand smoke, but has never awarded death benefits.

Since the ruling was made under federal workers compensation law, the judgment may have limited value as a precedent for other workers compensation claims, most of which are handled under state law. However, the Veterans Administration, which is responsible for paying the death benefits, could seek to recover its payments by suing the tobacco companies or by filing a claim against any judgment that the widower may win in his own lawsuit against the companies. The widower, Philip Wiley, has filed a separate product-defect lawsuit against all major U.S. cigarette makers in a case now pending in Indiana.

III. TOBACCO INDUSTRY RESTRUCTURING

The specter of FDA regulation, a new crop of class-action lawsuits and the release of potentially damaging internal industry documents add to problems that U.S. tobacco companies have faced in recent years. Previously, mounting restrictions on smoking in public places and President Clinton's health care reform proposal, which

recommended substantially higher federal excise taxes on cigarettes, dimmed the market outlook for tobacco companies, especially in the United States. Yet the tobacco companies have proven to be highly resilient. The stock value of market leader Philip Morris has risen about 230 percent in the last six years. Even RJR Nabisco—whose

stock price has languished since going public in 1991—still manages to generate cash earnings of nearly \$1 billion a year from its large tobacco business.

Nevertheless, U.S. tobacco companies have begun to explore restructuring options, prompted in part by concerns raised by shareholders. Indeed, some actions already have been taken. American Brands completed a partial spinoff of its tobacco operations in November 1994, selling its U.S. tobacco business, American Tobacco Co., to the British conglomerate B.A.T Industries for \$1 billion in cash. RJR Nabisco spun off 19.5 percent of its Nabisco food business in January 1995, raising about \$1.2 billion in cash. RJR now holds out the prospect of a complete spinoff of Nabisco within the next several years. Most recently, Kimberly-Clark completed a spinoff of its comparatively small tobacco business in November, saying it was “incompatible with the company’s strategic direction as a manufacturer and marketer of well-known consumer and health care brands.”

The move to separate tobacco businesses from other businesses counters the industry trend that began in the 1980s to acquire new businesses as a means of diversification. Investors have begun to balk at such conglomerations, making two basic arguments. First, from a financial standpoint, many investors have come to believe that companies should focus on what they do best, rather than venturing into unfamiliar areas that divert management’s attention. Second, some investors argue that shareholders deserve a clear choice of whether or not they wish to invest in tobacco. This is especially true of investors with ethical objections to holding tobacco stocks.

Philip Morris: Philip Morris had a major showdown with institutional investors about its tobacco business in 1994, and it faced a shareholder resolution in 1995 that requested the separation of its tobacco business from its food and beverage businesses. The low vote in favor of the proposal (3.5 percent), which will be resubmitted this year, belied the intensity of the discussion that company executives had with concerned shareholders in 1994.

Several major institutional investors spent much of that year trying to arrange a meeting with Philip Morris’s top management and members of its board of directors to express their concerns on various proposals to restructure the company. The investors first wrote then-chairman Michael Miles in May to request a face-to-face meeting. In their letter, the shareholders urged the company to take action to “contain the impact” of recent blows to its tobacco business and “preserve the health” of its non-tobacco operations—possibly by spinning off the tobacco segment into a separately listed group. (Miles reportedly

favored a separation of the company’s major business groups.)

After several false starts, a meeting did occur in September 1994 with representatives of a half-dozen state, municipal, university and organized labor pension funds. Although Philip Morris called the meeting “productive” and said that it gave the firm “an opportunity to explain firsthand the steps that we are taking to grow our company,” half of the investors walked out of the meeting in protest. They said Philip Morris had prepared a “canned presentation,” and it wasn’t the “meeting of substance” they had been promised.

The company’s new management, appointed after Miles’s resignation in June, also made clear that Philip Morris was not considering divesting its tobacco operations. No further meetings with the shareholders have taken place since September 1994, and the clamor for restructuring has since died down. A 60 percent rise in Philip Morris’ stock price since the third quarter of 1994 may be a factor in this—allaying investors’ concerns about the company’s financial health despite the legal and regulatory pressures mounting against its tobacco business.

RJR Nabisco: RJR Nabisco has not fared as well in the stock market or in the eyes of major shareholders in recent years. Its stock price is lower now than it was in the third quarter of 1994. At that time, the holding company for RJR Nabisco announced a 19.5 percent spinoff of its Nabisco food business. The company said that the Nabisco sale was “structured in a manner that preserves the option of separating such businesses on a tax-free basis at some later date should [management] consider it advisable.” The company added, however, that a complete spinoff of its Nabisco operation would not occur before the end of 1998 if that distribution would cause either the parent company’s debt rating, or that of the spunoff businesses, to fall below investment grade. On the other hand, with a go-ahead from bond ratings agencies, management said a spinoff could occur before the end of 1996.

Most shareholders appeared satisfied with this plan, if their response to a 1995 shareholder proposal filed by the Interfaith Center on Corporate Responsibility is any indication. That proposal—to spin off the company’s tobacco business by Jan. 1, 1996—was supported by only 6.5 percent of shares voted. (The resolution did garner enough votes to be eligible for resubmission this year). Management had argued in its 1995 proxy statement that it should not be “constrained by a specific program or timetable such as that suggested in this proposal.”

In 1995, however, investors Carl Icahn and Bennett Le-Bow teamed up to buy a 4.9 percent stake in RJR Nabisco. And at the beginning of 1996, they launched a proxy fight

against the company to push for an immediate spinoff of the remainder of the Nabisco food unit. In a recent consent solicitation to RJR Nabisco shareholders, Icahn and LeBow urge support for their own nonbinding resolution, which calls for an immediate spinoff, as well as a binding referendum that would reinstate the ability of shareholders to call a special meeting. (RJR Nabisco amended its by-laws in 1995 to rescind that right of shareholders.) Also in the solicitation, Icahn and LeBow have submitted the names of nine people who they hope will unseat the company's current board of directors at the next annual meeting and then carry out the spinoff.

In the solicitation letter, LeBow claims that shareholders' "investment in RJR Nabisco is languishing" and that a spinoff would boost the value of RJR shares by 25 percent or more. In a statement to the press, RJR Nabisco responded, "This is a dishonest consent solicitation, which has nothing to do with an immediate spinoff of our food business and everything to do with Messrs. LeBow and Icahn trying to take control of RJR Nabisco."

RJR Nabisco has sued LeBow and Icahn, charging they violated U.S. securities laws by secretly conspiring to form a group to acquire control of the company. The suit alleges that the investors' ultimate objective is to "deliver control of the company's tobacco subsidiary to them and their partners and combine the tobacco business with a tobacco company controlled" by LeBow. LeBow is the chairman of Brooke Group Ltd., which owns Liggett Tobacco.

Icahn and LeBow will wait for the results of the consent solicitation before deciding on whether to go forward with their proxy fight to oust RJR's board. The company has set Jan. 12, 1996, as the record date for the consent solicitation. Consents will be accepted for 60 days.

Spinning off tobacco liabilities? What can get lost in all the legal wrangling surrounding a spinoff is what happens if a plaintiff is successful in suing a company for damages allegedly caused by smoking one of its brands of cigarettes. The question is central to the debate over the RJR Nabisco spinoff, because the company wants to avoid being accused of "fraudulent conveyance" of assets in order to shield them from liability. Under a worst-case scenario, the holding company could be required to pay out billions of dollars in damage claims, throwing it into bankruptcy. If it then filed for bankruptcy protection, and a court agreed that assets were fraudulently conveyed—which otherwise could have been used to pay off the plaintiffs—investors in the spunoff company would be required to give back their shares. Directors of holding company also could be personally liable for fraud.

Accordingly, RJR Nabisco's management has made clear that it wants the financial community to be convinced of the creditworthiness of each of its operating units before spinning one of them off. According to one financial analysis by Salomon Brothers' Max Holmes, a split-up of RJR Nabisco into two companies would leave the tobacco business with approximately 4.8 times the amount of revenues needed to cover the interest payments on its debt, compared with just 2.2 times the amount needed at Nabisco. By leaving the tobacco operation with comparatively little debt, and by making that debt investment-grade at the time of the separation, management would have evidence to show the courts that its tobacco operations were far from insolvent at the time of the breakup—and that plaintiffs had no right to go after spunoff Nabisco shares. Indeed, in a prospectus prepared for the initial public offering of 19.5 percent of Nabisco shares in January 1995, management downplayed the risk of exposure to tobacco liability by Nabisco shareholders. "The risk that Nabisco's assets could be attached to satisfy [tobacco] liabilities is remote," the prospectus said.

Yet some doubts persist about whether RJR Nabisco can erect a "firewall" between its food and tobacco businesses. "I am not convinced that the eventual spinoff really does isolate the Nabisco assets in the event that a disastrous lawsuit occurs," said Robert Kleinschmidt, president of Tocqueville Asset Management, in an interview with *Business Week* in the fall of 1994.

While some industry analysts have decided that setting up a company not related to tobacco operations would virtually preclude the possibility that the new company could suffer from any tobacco judgments, others are concerned what might happen if such a spinoff is *not* completed. "It is possible that if the company had to pay out huge liability claims, that could transfer over to the Nabisco shares that the company owns 81 percent of," warns Barry Ziegler, a tobacco industry analyst for A.G. Edwards.

Gregory Jackson, a portfolio manager of Yacktman Asset Management Co., a Chicago investment firm that at one time owned three million shares of RJR Nabisco, thinks the liability issue actually could make shares in the tobacco holding company even more attractive than spunoff Nabisco shares. He told *The Wall Street Journal* in November 1994, "We would buy RJR rather than the new Nabisco offering because you're getting RJR at a significant discount to the market multiple"—roughly 10 times projected 1995 earnings instead of 17 to 20 times projected earnings for Nabisco. The food company "still bears all the potential liability" facing the tobacco operations, Jackson added, so he sees no greater risk in buying the tobacco shares with the lower earnings multiple.

AMA Wants Tobacco-Free Mutual Funds

FUND TRACK

By KAREN DAMATO

Staff Reporter of THE WALL STREET JOURNAL

The American Medical Association is prodding the mutual-fund industry to give up tobacco.

The doctors' group yesterday called on investors to ditch nearly 1,500 funds that have invested in tobacco-company stocks and bonds. The AMA said it will lean on the fund industry by publishing an annual list of offending funds—and by heaping praise on funds that agree to sign a no-tobacco pledge and to join a new "AMA Coalition of Tobacco-Free Investments."

But some fund-industry folks are predicting that the new AMA campaign will fade away like, well, a wisp of cigarette smoke in the air.

'A Long Shot'

Targeting fund investors is "a long shot" for the AMA, says John Rekenhaller, publisher of Morningstar Mutual Funds in Chicago. Lots of people feel strongly about causes such as shunning smoking or protecting the environment through recycling. But precious few expect their funds to share the mission, he says.

Witness the minuscule market share of so-called socially conscious funds that shun stocks in businesses such as tobacco and weapons-making. After at least a dozen years of existence, Morningstar says, such funds have assets equal to just 0.16% of the money in diversified U.S. stock funds.

And some fund-industry officials say such "social investing" doesn't make much sense.

FUND TRACK

Continued From Page C1

other investors with a bargain-seeking "value" bent would gobble up the shares.

Meanwhile, Mr. Yacktman says his reason for owning Philip Morris is simple: "It's the cheapest, large, profitable company on the New York Stock Exchange."

For investors buying tobacco stocks directly or through funds, meanwhile, there are certainly some big risks to consider, says fund watcher A. Michael Lipper of Lipper Analytical Services Inc. While the AMA campaign probably isn't a major threat, he says, "the biggest impact will come when and if the tobacco companies lose major lawsuits" on their products' health risks.

Have those risks prompted funds to limit their tobacco exposure? At this newspaper's request, Morningstar Inc. took a look at Philip Morris shares held by diversified U.S. funds. The conclusion of the Chicago firm: Those funds as a group are underweighted in Philip Morris shares relative to the broad stock market.

In the aggregate, the U.S. stock funds had 0.9% of assets in Philip Morris late last year. Meanwhile, that same stock represented 1.16% of the assets of the Vanguard Index Trust Total Stock Market Portfolio, a fund that aims to replicate the performance of the Wilshire 5000 Index.

The AMA is calling on investors to sell not just funds with tobacco exposure but also tobacco-company stocks and bonds they may hold directly. The group cited 13

The AMA Points Its Finger at Funds

Among the largest stock funds, these are singled out by the American Medical Association for having or not having tobacco stocks among their top 10 holdings.

UNDER FIRE

- Investment Co. of America
- Fidelity Puritan
- Fidelity Contralund
- Fidelity Growth & Income
- Income Fund of America
- Fidelity Equity Income II
- Fidelity Asset Manager
- Vanguard Windsor II

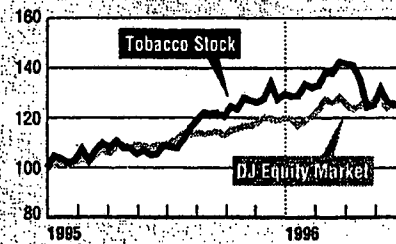
DRAWING PRAISE

- Fidelity Magellan
- Washington Mutual Investors
- 20th Century Ultra
- Vanguard Windsor
- Janus
- Vanguard Wellington

Source: Data from a recent study by nonprofit group Co-op America, cited in today's issue of the Journal of the American Medical Association.

Tobacco Stocks

DJ Tobacco Stock Index vs. the Dow Jones Equity Market; April 28, 1995=100, weekly data



At Vanguard Group, for instance, company spokesman Brian Mattes says phone representatives are told to deliver a blunt response to investors who raise concerns about tobacco holdings or other potentially objectionable investments: The funds' "sole purpose" is to pursue the maximum total return possible within their investment objectives, the script says, so funds "cannot be constrained by any special interest group's definition of acceptable investments."

Fund manager Donald A. Yacktman of the Yacktman fund dismisses social investing as "a very poor idea . . . like doing

things backwards." Mr. Yacktman's stance isn't surprising given the fact that his fund is a big tobacco investor, with about 10% of assets in Philip Morris. Still, the manager personally is a Mormon, who as a matter of religious conviction neither smokes nor drinks.

"I'd like to see fewer people smoke," Mr. Yacktman says. But he doesn't believe shunning tobacco stocks "is the right way to accomplish the job." If the AMA effort were to depress Philip Morris stock, he says, the company itself would simply buy back more shares. And mutual funds and

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companies, some well-known names and some not: American Brands, Brooke Group, Culbro, DiMon, Loews, Maeco Consolidated Group, Philip Morris, RJR Nabisco Holdings, Sara Lee, Schweitzer-Mauduit International, Standard Commercial, UST and Universal.

In an interview, Dr. Randolph Smoak Jr., AMA secretary-treasurer, said he's optimistic that many investors will demand tobacco-free funds once the matter is brought to their attention. A majority of people are opposed to tobacco use personally, he notes, so "why should they support something they don't believe in once it is brought to their attention?"

Several years ago, the AMA divested the tobacco stocks in its own portfolio. And a few other institutional investors have followed. One recent example, Dr. Smoak said: the Maryland state pension fund. The \$50 billion New York Teachers' Retirement System also is considering shedding its tobacco investments.

The Maryland Retirement and Pension System is careful to describe its April 16 decision as one based entirely on business, not public health. "We didn't do it for social reasons," Richard Dixon, state treasurer and vice chairman of Maryland Retirement's board, told Dow Jones Money Management Alert. "We had a substantial profit." Mr. Dixon says tobacco companies have been good at fighting legal battles over the years, but "sooner or later, they are going to lose."

PIMCO'S HIRE: Pimco Advisors L.P. is hiring Smith Barney Inc. executive Stephen Treadway to build its "retail"

fund business. Mr. Treadway, 48 years old, is joining Pimco as executive vice president, and as chairman of its retail fund group aimed at small investors. Pimco, which manages \$97 billion, was formed in 1994 in a merger between Pimco Investment Management Co. and Thomson Advisory Group L.P., and is currently dominated by its business of managing money for institutions. Mr. Treadway will join Pimco by May 6.

At Smith Barney, Mr. Treadway has been an executive vice president in charge of services such as retirement and stock-option plans sold by Smith Barney to corporations. Until a year ago, Mr. Treadway was chief executive officer of the Smith Barney mutual-fund group, which now is headed by Jessica Bibliowicz.

Yesterday, Pimco reported first-quarter operating profit available for distribution of \$29.7 million, up 25% from the year-earlier period.

NET NEWS: Fund giant Fidelity Investments likes marketing its funds on the Internet's World Wide Web. Now it's going to sell Internet-access services to its customers, too.

Fidelity says it will sell its customers full access to the Internet services of MCI Communications Corp. at a slight discount. Fidelity's Web sites already let Web surfers download prospectuses (albeit tediously), get fund prices and crunch numbers in financial worksheets.

—Robert McGough

ATTACHMENT F

News articles about Philip Morris proposal to limit cigarette sales to youth.

Tobacco giants pitch plan to cut teen smoking, avoid regulation

New York Times

Seeking an alternative to federal regulation of the nicotine in tobacco as an addictive drug, two leading tobacco companies proposed Wednesday that Congress adopt sweeping laws to reduce teenage smoking by banning vending sales and restricting advertisements and promotions.

But the companies — Philip Morris USA, the tobacco unit of Philip Morris Cos., the nation's largest cigarette maker, and United States Tobacco Co., the nation's largest purveyor of chewing tobacco and snuff — would support such legislation only if the Food and Drug Administration (FDA) withdrew its proposals to regulate the sale of tobacco.

The White House, which has said in the past it would accept legislation instead of FDA regulation as a way to curtail youth smoking, said it was "somewhat encouraged and slightly disappointed" by the Philip Morris plan. It praised the company for "clearly trying to be a good corporate citizen."

FDA officials were not so sanguine. Mitch Zeller, who coordinates the agency's tobacco control policy, said the agency expects any legislation to be as "comprehensive and effective" as the proposed FDA rules.

"That's the bottom line," he said. "The Philip Morris proposal falls short of this mark."

Minnesota opposition

Minnesota Attorney General Hubert Humphrey III, who is leading a lawsuit against the tobacco industry to recover smoking-related health care costs, said the offer was unacceptable.

"There is no educational component to help curb the appeal of tobacco to youth," Humphrey said. "And nowhere do they do anything about point-of-sale advertising, even at a convenience store adjacent to a grade school. Unfortunately, like many of the previously announced youth-access measures by the tobacco industry, this proposal contains a lot more smoke than substance."

Blue Cross Blue Shield of Minnesota, the other plaintiff in the state's lawsuit, said the offer indicated that the tobacco industry is feeling pressure to dampen criticism of its marketing strategies.

"But I don't think preemption of regulation by the FDA of tobacco ought to be for sale," Blue Cross lawyer Thomas Gilde said.

Ban on vending machines

The tobacco companies' proposal includes a ban on vending-machine cigarette sales, single-cigarette sales and promotional giveaways, as well as a ban on transit advertising and restrictions on billboard and stadium advertising and sports-event sponsorships.

Philip Morris and United States Tobacco also proposed a ban on the imprinting of tobacco logos on merchandise such as hats, clothing and gym bags. They also proposed that the tobacco industry spend \$250 million over the next five years to enforce restrictions on teenage smoking. The proposals would not affect international business.

Steve Parrish, spokesman for Philip Morris, termed the proposal "unprecedented and far-reaching," saying the companies "want to make it impossible for anyone to obtain any tobacco product from a manufacturer or retailer without a face-to-face transaction where proof of age can be checked."

R.J. Reynolds Tobacco Co. and Brown and Williamson Tobacco Corp. said they would reserve comment on Wednesday's proposal until they could give it further study. Lorillard Tobacco Co., a unit of Loews Corp., said it supported many of the suggestions.

'A preemptive strike'

"This announcement is obviously a preemptive strike against the FDA," said Richard Daynard, chairman of the Tobacco Products Liability Project at Northeastern University School of Law in Boston, a nonprofit anti-smoking group. "They want to make sure that the FDA has nothing to

do with regulating them."

Parrish denied that the companies were attempting to avoid more stringent restrictions. But critics of the tobacco industry said that under the companies' proposal, cigarette brand images, such as Joe Camel and the Marlboro Man, would be unaffected. Under the federal agency's plan, much advertising would be limited to black-and-white advertisements of text and not graphics. The tobacco companies have contended that such a limitation would infringe on their right of free speech.

The companies' proposal also would preclude any FDA role in enforcement of tobacco regulations. And unlike the agency's proposal, the tobacco companies' proposal would not ban tobacco brand-name sponsorship in rodeos and motor sports.

Tobacco industry supporters, such as Rep. Thomas Bliley Jr., R-Va., said the companies' proposal had "little chance" of passage in Congress because Democrats had "already promised to filibuster any legislation that would preclude the FDA from exercising jurisdiction over tobacco."

But Rep. Henry Waxman, D-Calif., a leading tobacco industry opponent, said: "I commend Philip Morris for at least suggesting a legislative proposal," adding that he would "look forward to talking with them about enacting a bill this year."

About \$2 billion worth of tobacco products were sold through 400,000 vending machines in 1994, or about 915 million packages of cigarettes, said Victor Lavay, publisher of Vending Times, a trade magazine.

Sheldon Silver, of the National Automatic Merchandising Association, said: "We oppose the ban on cigarette vending machines because it will not significantly reduce teen smoking." He cited a study showing that more than 72 percent of teenagers buy cigarettes in convenience stores and gas stations.

— Staff writer Dave Phelps contributed to this report.

Tobacco firm offers deal on smoking curbs

■ Ad, sales limits proposed if regulation plan dropped

HEALTH

Curbing smoking

THE PROPOSAL

■ In addition to banning vending machine sales and advertising within 1,000 feet of schools and playgrounds, the legislation proposed by Philip Morris would ban sales of individual cigarettes and set a minimum age of 18 for the purchase of tobacco products — all features of the FDA plan.

■ The FDA plan would ban cigarette ads in all publications where more than 15 percent of the readership is under 18, including such popular magazines as Sports Illustrated.

SHERYL STOLBERG LOS ANGELES TIMES

WASHINGTON

The nation's largest tobacco company offered Wednesday to back federal legislation to curb underage smoking — but only if the Clinton administration drops its effort to regulate nicotine as a drug.

The quid pro quo proposal, outlined by officials of Philip Morris USA at a news conference in New York, accedes to a number of provisions in — and in some cases goes beyond — a Food and Drug Administration plan that the tobacco industry is fighting in court.

As put forth by the maker of Marlboro, which is the favored brand of more than half of young people who smoke, the legislation would ban vending machine sales of cigarettes, prohibit tobacco billboards within 1,000 feet of schools and curtail, but not eliminate, industry sponsorship of some sporting events.

It would put an end to controversial T-shirt and ball cap promotions and prohibit cigarette manufacturers from paying for "product placement" in films and television shows. But it would not put any money into educational efforts, as the FDA has suggested, nor would it require cigarette manufacturers to replace their alluring ads with dull black-and-white "tombstone" type.

"The time for talk has ended," said company spokesman Steven Parrish, who was joined in his statement by the executive vice president of U.S. Tobacco, the nation's largest manufacturer of smokeless tobacco. "The time has come to ... (bring) people together to attack the problem of underage use of tobacco."

The White House, which has said in the past that it would accept legislation instead of FDA regulation as a way to curtail youth smoking, said it was "somewhat encouraged and slightly disappointed" by the Philip Morris plan. It praised

the company for "clearly trying to be a good corporate citizen."

FDA official Mitch Zeller, who coordinates the agency's tobacco control policy, said the agency expects any legislation to be as "comprehensive and effective" as the proposed FDA rules.

"That's the bottom line," he said. "The Philip Morris proposal falls short of this mark."

Where the plan goes from here is unclear. It is possible that tobacco supporters in Congress will introduce the legislation, setting the stage for an election-year battle on the issue.

Whether the plan would draw support from other tobacco companies is unknown; Reynolds, the second-largest cigarette manufacturer, said it would reserve comment on the plan until it could learn more about it.

Wednesday's announcement comes two days after a Supreme Court ruling that bolsters the free-speech rights of advertisers, a ruling that has been widely interpreted as limiting the administration's ability to restrict cigarette advertising.

In addition to banning vending machine sales and advertising within 1,000 feet of schools and playgrounds, the legislation proposed by Philip Morris would ban sales of individual cigarettes and set a minimum age of 18 for the purchase of tobacco products — all features of the FDA plan.

But where the FDA plan would eliminate tobacco sponsorship of all sporting events, the Philip Morris plan would continue to permit sponsorship of motor sports and rodeos.

Another major difference between the plans is their approach to limiting magazine advertising.

The FDA plan would ban cigarette ads in all publications where more than 15 percent of the readership is under 18.

The Philip Morris plan would base the advertising ban on subscribership, and not readership — an important distinction because many young people read the magazines to which their parents subscribe.

Philip Morris Has Its Own Youth-Smoking Plan

Philip Morris Cos. asked Congress to impose a more limited set of restrictions on cigarette sales and advertising aimed at curbing youth smoking, in an effort to derail the Food and Drug Administration's sweeping proposal to regulate cigarettes.

But politicians in both parties voiced doubts that the proposal will fly, because it falls well short of the package of restrictions backed by President Clinton and the Food and Drug Administration. The FDA immediately rejected the company's plan.

The unexpected announcement marked an effort on the part of the world's

By Wall Street Journal staff reporters Suein L. Hwang in New York and Timothy Noah and Laurie McGinley in Washington.

biggest cigarette maker to take control of the escalating fight over tobacco regulation.

Among its concessions: bans on cigarette ads on billboards within 1,000 feet of any playground or school, on cigarette vending machines and on cigarette ads in trains, buses, subways and taxis.

Philip Morris is acting amid the biggest legal and regulatory attack ever on the cigarette industry. It also faces a president who has seized on youth smoking as a popular campaign issue.

Indeed the company directly addressed the president in announcing its new proposal. "Last year the President urged all of us to put aside our differences and seek common ground," said Steven Parrish, senior vice president of corporate affairs. "In the interests of unified and effective action, we ask Congress and President Clinton to move this legislation without delay."

Michael McCurry, White House press secretary, said the Clinton Administration is "somewhat encouraged and slightly disappointed" in the proposal. The White House, he said, "would welcome further efforts by Philip Morris and by others within the industry to meet the standards that the president has set forward."

The FDA, whose proposed tobacco rule is expected to be issued in final form this summer, said the Philip Morris plan "falls short" of being a viable alternative. "The president made it clear last summer that he welcomed a legislative solution," said Mitch Zeller, the FDA's deputy associate commissioner for policy, "as long as it was

TOBACCO		
The Dueling Rules		
	PROPOSED FDA RULE	PHILIP MORRIS PROPOSAL
VENDING MACHINES	Bans vending-machine sales of tobacco products	Same
BILLBOARD ADS	Bans billboard ads for tobacco within 1,000 feet of schools or playgrounds	Goes further to restrict other billboard ads to black-and-white, text-only format
YOUTH PUBLICATIONS	Restricts ads in publications with significant (15%, or more than two million) youth readership to black-and-white, text-only. Figures apply to surveys of readership, not circulation	No tobacco ads in publications where youths account for more than 15% of subscribers
ANTISMOKING CAMPAIGN	Requires industry to fund a \$150 million-a-year antismoking media campaign	No comparable proposal
REGULATION	Tobacco products would be regulated by FDA	Tobacco products would be regulated by Justice Department, Federal Trade Commission and Department of Health and Human Services
BRAND-NAME SPONSORSHIP	Bans brand-name sponsorship of sporting events, concerts, etc.	Limits brand-name sponsorship to rodeos and motor sports where 75% of attendees are adults

as comprehensive and effective as the FDA proposal."

Indeed, the FDA last year made a landmark declaration that cigarettes are a drug-delivery device and the agency should regulate them. But the Philip Morris proposal would block the FDA from asserting jurisdiction over tobacco products.

The industry's attempt to steer regulatory authority away from the FDA is the most likely substantive deal-breaker. Al-

though the Philip Morris plan would allow the FDA's parent agency, the Health and Human Services department, to oversee the industry in conjunction with the Federal Trade Commission and the Justice Department, an administration official said the tobacco giant's plan didn't appear to give these agencies much authority. New cigarette products "would go straight to market" without prior government approval, he said.

The Philip Morris proposal also faces an uncertain future in the Republican

Congress, which is heavily funded by tobacco companies but anxious about taking a strong public stand in favor of the industry. Philip Morris is the single-largest contributor of corporate cash to the political parties (mainly to Republicans); last year, tobacco interests overall gave \$2.78 million in such "soft money" contributions, according to Common Cause.

While antismoking advocates supported certain aspects of Philip Morris's plan, they raised questions about some of its key provisions.

For instance, the FDA's proposed restrictions would limit tobacco advertising in periodicals for which minors make up more than 15% of total readers; to a black-and-white, text-only format. In the Philip Morris plan, the ban applies to periodicals for which minors make up more than 15% of total subscribers. According to Matthew Myers, general counsel for the Campaign for Tobacco-Free Kids, the Philip Morris plan would let tobacco companies advertise in several youth-friendly magazines that would fall under the FDA ban, including Rolling Stone, Mademoiselle, Sports Illustrated, Vogue and Car & Driver.

Philip Morris Proposes Its Own Plan to Curb Smoking by Youth

"Philip Morris's proposal will not result in a fundamental change in the advertising and marketing which has the greatest impact on children," said Mr. Myers. "The proposal is more smoke and mirrors than real change."

Philip Morris's Mr. Parrish said the company decided to rely on magazine subscribership because it is difficult to get accurate data on magazine readership. Readership figures, which include estimates of all individuals who read or look at a publication issue, are far higher than subscriber numbers.

Among other shortcomings tobacco foes seized on, the FDA wants to require cigarette packs to be kept behind the counter, while the Philip Morris proposal only requires them to be in the sight of an employee. The FDA would make cigarette makers responsible for ensuring retailers don't sell to kids, while the Philip Morris plan limits the responsibility to the retailers themselves.

The Philip Morris proposal would also allow cigarette brand marketers to sponsor most auto racing and rodeo events — key marketing venues covered by the FDA ban.

But smoking critics also praised some of Philip Morris's provisions, in particular the ban on billboards near schools and playgrounds, elimination of advertising on public transit and restricting the use of cigarette brand names on T-shirts and other giveaways.

"If Philip Morris were serious, this bill would be the opening of a dialogue rather than a final proposal," said Mr. Myers, of Tobacco-Free Kids. "By closing the door to FDA jurisdiction, the tobacco industry may have closed the debate before it could be opened."

Philip Morris's Mr. Parrish pointed out that many of the company's proposals have been supported by regulators and the antismoking community and said a legislative solution would eliminate the delays of a lengthy court battle over the FDA's proposals. "Are they going to oppose a bill to create tobacco ad-free zones, and if they are going to oppose it, why?" he asked.

Absent from Philip Morris's proceedings yesterday was No. 2-ranked cigarette maker R.J. Reynolds Tobacco Co. Indeed, Reynolds executives say they weren't even aware of Philip Morris's plans until the news conference yesterday. Furthermore, many point out that one of the stronger provisions of Philip Morris's plan — a total ban on cigarette sampling through the mail and most venues — would disproportionately hurt Reynolds, which relies far more heavily on cigarette giveaways.

"A number of items in the Philip Morris proposal are similar to those we have initiated," said a statement by Reynolds, which added that it can't comment further until it has seen the proposal's specifics. B.A.T Industries PLC's Brown & Williamson unit said it is reviewing the proposal "to ensure that our constitutional right to communicate with adult smokers is protected." Smokeless tobacco maker UST Inc. supported the proposal.

ATTACHMENT G

Defendants in the State of Minnesota/Blue Cross-Blue Shield Suit

The defendants in the case, *State of Minnesota and Blue Cross and Blue Shield of Minnesota v. Philip Morris Incorporated, et al.*, are:

- The American Tobacco Company
- BAT Industries
- Brown & Williamson
- Liggett Group, Inc.
- Lorillard Tobacco Company
- Philip Morris, Inc.
- R. J. Reynolds Tobacco Company
- The Council for Tobacco Research
- The Tobacco Institute

Parent company relationships, merger and acquisition activity, etc. affect several of the companies on this list:

- American Brands sold its U.S. subsidiary, American Tobacco Company, to BAT in December 1994. American Brands retains its British tobacco operation, Gallaher Ltd.
- Lorillard Tobacco Company is a subsidiary of Loews Corp.
- Brown & Williamson is a subsidiary of BAT.
- Liggett Group changed its name to Brooke Group, Ltd. in 1990.

In light of the above, there are six (6) publicly traded companies related to the suit at this time:

- American Brands
- BAT Industries
- Brooke Group, Ltd.
- Loews
- Philip Morris
- RJR Nabisco

ATTACHMENT H

Companies Engaged in the Tobacco Business Other Corporate Lines of Business

Company	Percent Revenue From Tobacco, 1994	Other Corporate Business
Amer Group	8.0%	Car Imports; Sporting Goods; Paper Wholesaling; Publishing & Printing
American Brands	53.4	Alcohol; Hardware/Home Improvements; Office Products
BAT Industries	63.2*	Insurance
Brooke Group, Ltd.	97.2	Airplane Manufacturing
Culbro	47.6	Nursery Products; Mfg. Packaging/Labeling Products and Machinery
Dimon	74.6	Imports/Wholesales Fresh Cut Flowers
Glatfelter	N/A	Specialty Paper Products
Hanson PLC	8.3	Industrial, Consumer and Building Products
Loews	14.2	Insurance; Gas & Oil Exploration; Hotels; Timepiece Mfg/Retailing
Philip Morris	44.0	Packaged Foods
RJR Nabisco	49.9	Packaged Foods
Sara Lee	<5	Packaged Foods
Schweitzer-Maud.	93.0	Specialty Paper Products
SEITA	83.1	Matches, French Telephone and Service Payment Cards
Standard Commercial.	64.4	Wool Trading/Processing; Retail Buildg Supply Centers
Tabacalera SA	53.3	Postage Stamps; Packaged Foods
Universal Corp.	70.5	Processing/Trading Agricultural Products; Mfg. and Marktg wood/Lumber Products
UST, Inc.	86.5	Wine; Home Video Entertainment
Volve AB	5.1	Autos; Food and Beverages; Pharmaceuticals

*Does not include 1994 purchase of American Tobacco Company

Source: "The Tobacco Industry, 1995 Edition," Investor Responsibility Research Center, Washington, D.C.

ATTACHMENT I

**SBI Stock Holdings
in Tobacco Companies Identified by the IRRC
March 31, 1996**

Passive And Active Portfolio Holdings

Company	Passive Shares	Passive Market Value	Active Shares	Active Market Value
Amer Group	6,700	\$107,001	106,125	\$1,694,848
American Brands	147,700	6,258,787	0	0
BAT	978,066	7,225,029	325,597	2,405,204
Brooke Group	9,900	89,100	0	0
Culbro	10,600	650,575	0	0
Dimon Inc.	23,899	421,219	0	0
Glatfelter	66,800	1,160,650	0	0
Hanson PLC	1,641,600	4,798,021	1,067,224	3,119,253
Loews	295,200	22,324,500	105,000	7,940,525
Philip Morris	1,069,360	93,836,340	662,925	58,171,668
RJR Nabisco	148,498	4,492,064	656,980	6,988,483
Sara Lee	369,505	12,055,099	209,600	6,838,201
Schweitzer-Maud.	16,210	445,775	0	0
SEITA	16,400	680,565	3,200	132,793
Standard Comm'l	12,369	111,321	0	0
Tabacalera SA	11,650	544,414	62,400	2,916,005
Universal Corp.	87,900	2,208,487	0	0
UST	141,200	4,500,750	135,100	4,306,312
Volvo AB	147,700	3,450,050	133,500	3,109,161
Total	5,201,257	\$165,359,747	3,467,651	\$97,622,453

Note: Semi-passive holdings are included in passive totals

ATTACHMENT J

Highlights from Tobacco Industry Research Reports late 1995-early 1996

The following are some highlights from recent tobacco industry research reports prepared by various investment industry analysts. The company comments are in alphabetical order.

Auerbach Pollak & Richardson, Inc.

- A November 13, 1995 research report concludes that with respect to the Castano case "We think that investors may have exaggerated the importance of the class action certification in their analysis of tobacco litigation and may overreact if the Fifth Circuit concludes that the class action certification should be rescinded or deferred."
- A January 11, 1996 research report states that "We think that these Medicaid reimbursement cases, including the Massachusetts case, will prove to be extremely troublesome for the tobacco industry over the next few years." Further, with respect to the legal issue of decertifying from class action status the Castano case, the report concludes that "we do not believe that a decertification ruling from the Fifth Circuit, if it occurs, would justify any major stock price ebullience."

Bernstein

- A January 12, 1996 research report reiterates outperform rating on Philip Morris and states that short term litigation risks have been discounted by investors.
- A January 18, 1996 research report reiterates that its outperform ratings on Philip Morris and RJR.
- A March 12, 1996 research report continues to rate Philip Morris and RJR Nabisco as "outperform."
- A March 15, 1996 report reiterates their "Outperform" ratings for Philip Morris and RJR. The report states their belief that "LeBow--or another tobacco company--will ultimately void this innovative, but impractical settlement. We believe the market--fueled by the media coverage--has incorrectly perceived that by settling with the Castano counsel, LeBow will now work closely with the Castano PLC in document discovery and advisory activities that could bring down the entire industry--in fashion similar to asbestos. We find this illogical."

Dean Witter

- A January 9, 1996 research report maintains “Accumulate” rating on Philip Morris and “Neutral” rating on RJR Nabisco. “We would not be surprised to see some short term weakness in the tobacco stocks following a negative, though not completely unexpected, Appellate Court ruling in the Broin lawsuit.” (Broin is a Florida lawsuit involving second-hand smoke and its alleged health effects on approximately 60,000 flight attendants.)
- A February 9, 1996 research report maintains their “Accumulate” rating on Philip Morris.

Goldman Sachs

- A February 1, 1996 report concludes that the decision “is NOT as negative for the tobacco industry as market participants apparently made it out to be yesterday.” Further, the report states that “The opinion does not change our view that a good chance exists that courts will eventually view class action as an inappropriate method for dealing with smoking and health lawsuits.” (A Florida appeals court affirmed certification of the Engle cigarette lawsuit as a class action, but narrowed the scope of the class and highlighted significant difficulties related to managing cigarette lawsuits in a class action fashion.)

Merrill Lynch

- A March 14, 1996 report states that “More significantly, the plaintiffs have agreed not to block any effort on RJR’s part to spin off Nabisco if Liggett can gain control of the RJR board at the April 17 RJR annual meeting....This agreement not to block a Nabisco spin-off may be the principal rationale behind LeBow’s decision to break from the other cigarette companies, as it may strengthen his attempt to gain control of the RJR Nabisco board and to spin off Nabisco.” (LeBow was unsuccessful in his attempt at the April 17 meeting.)

Morgan Stanley

- A March 14, 1996 research report states that the firm reiterates its “Outperform” rating on Philip Morris. “In our view, the proposed litigation settlement by Liggett does not increase the litigation risks facing Philip Morris...” Further the reports states, “we feel that this is an unusual situation in that the settlement would be economical only to a player as small as Liggett. In all likelihood, a settlement would not be as economical--that is, is less than legal fees--for the larger companies...”

Paine Webber

- A December 15, 1995 research report states that its rating on Philip Morris remains a buy.
- A February 2, 1996 research report states that its rating on Philip Morris remains a buy.

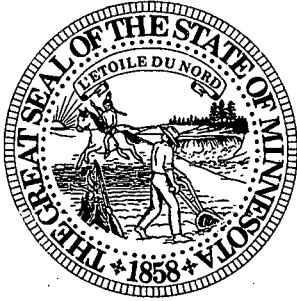
Salomon Brothers

- A March 13, 1996 report states with respect to the LeBow settlement, tobacco stocks "will probably be off 2% to 3% as the larger companies will fight this settlement because of their larger profits. We will maintain our "Buy" ratings on the group, favoring Loews first and Philip Morris next....We believe this litigation deal will be perceived as the act of a desperate individual whose company, Liggett, faces decline and who is to bargain away 9% of the profits of the company he is trying to take over for his own personal gain. This will increase tobacco volatility near term, but we expect the rest of the industry to fight vehemently."

Smith Barney

- A March 13, 1996 research report concludes that "We view this proposed settlement as another attempt by LeBow to gain control of RN." (RN is RJR Nabisco.) "We believe the fundamentals of the industry's defense are unchanged and we continue to expect a favorable ruling in Castano in 3Q96."

Tab I



STATE BOARD OF INVESTMENT

Manager Commentaries

Period Ending March 31, 1996

Domestic Stock Managers	1
Emerging Stock Managers	35
Domestic Bond Managers	53
International Stock Managers	69
Assigned Risk Plan	85
Internal Stock and Bond Pools	89

Manager Commentary
Alliance Capital Management L.P.

Period Ending:	3/31/96	Returns	Qtr.	1 Yr.
Total Firm Assets Under Management	\$148.3 Billion	Actual	5.7%	35.3%
Total Firm Assets Managed in this Discipline	\$ 15.6 Billion	Benchmark	6.7%	32.2%

1. ***Past Performance.** Summarize your performance over the last quarter and year. Specifically, what active bets did you make relative to your benchmark? Which of these bets worked/did not work and why?*

For the quarter, the underperformance versus the benchmark came primarily in the month of March. Our underweighting in the retail sector was a significant factor as these stocks were strong after a long period of underperformance. Our overweight in Philip Morris was also a factor as it declined during the month on renewed litigation concerns. We are equally weighted in healthcare but the two largest holdings, Amgen and Merck, underperformed. Our financial overweighting was a positive factor as the brokerage stocks and banks were the strongest stocks in the portfolio. Our technology overweight was mixed as the strong performance of Cisco, Microsoft and Hewlett Packard were offset by the soft performance of Intel and Applied Materials.

For the year we outperformed our benchmark. Our airline position was a significant positive as both UAL and Northwest were up sharply. Our technology overweight for the year also was a positive particularly our largest positions, i.e., Cisco +103%, Hewlett Packard +56%, and Microsoft +45%. The same was true in financials as Fannie Mae +57%, Norwest +45% and Citicorp +87% contributed to the outperformance. While we were equally weighted in healthcare and underweighted in the consumer sector, on a stock specific basis our largest holdings were excellent performers, i.e., Amgen +72%, Merck +46%, Pepsi +62%, Coca Cola +42% and McDonalds +41%.

On the negative side was our overweight in cable and cellular which continued to be negatively affected by the threat of increased competition from the telephone industry and Direct TV. Other entertainment stocks also underperformed, specifically Disney after they announced the acquisition of Capital Cities ABC.

2. ***Future Strategy.** What active bets are in place at the present time relative to your benchmark? Summarize the rationale for making these active bets.*

Our specific strategy is to increase the diversification in the portfolio slightly in reflection of the strong advance of the market over the past 15 months. Our financial overweight continues as these companies are very attractive given our scenario of "moderate growth, moderate inflation" environment. Our technology overweight is based on U.S. technology leadership and the pervasiveness of the computer. We will also continue to have large positions on a stock specific basis in selected proven growth issues in the consumer and healthcare industries.

Alliance (con't)

3. **Organizational Issues.** *Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.*

Won	Lost
New York City Fire	None
New York City Employees	
New York City Teachers	
George Washington University	
Johns Hopkins University	
Government of Singapore	
Pfizer	

4. **Other Comments.** *Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.*

None.

Staff Comments

No comments at this time.

Manager Commentary
Brinson Partners, Inc.

Period Ending:	3/31/96	Returns	Qtr.	1 Yr.
Total Firm Assets Under Management	\$52.9 Billion	Actual	7.7%	38.7%
Total Firm Assets Managed in this Discipline	\$12.9 Billion	Benchmark	5.8%	30.1%

1. *Past Performance. Summarize your performance over the last quarter and year. Specifically, what active bets did you make relative to your benchmark? Which of these bets worked/did not work and why?*

Key factors that affected the performance of the domestic equity market during the first quarter of 1996 included an increase of roughly 100 basis points in long-term interest rates, rising levels of observed market volatility and indications that corporate profitability growth, which had been strong during early 1995, has begun to slow.

Active factor exposures contributed modestly to portfolio performance during both the first quarter of 1996 and for the twelve months ending March 31, 1996. Underweighting foreign earnings exposure was positive in both periods. During the first quarter of 1996, the portfolio benefited from an overweight with respect to stocks with high earnings variability (economic sensitivity) and financial leverage. Negative contributions came from overweights with respect to the book/price measure and underweights with respect to relative strength and size. During the twelve months ending in March, the portfolio benefited from overweights with respect to the traditional value measures of book/price and earnings/price, while underweighting stocks that have a high degree of price volatility detracted from portfolio performance.

Industry weightings added meaningfully to portfolio performance during both the first quarter and year ending March 31, 1996. During the first quarter of 1996, positive returns from relative overweights in the aerospace, cosmetics and leisure sectors and from an underweight in traditional telephones more than offset negative contributions to performance from our relative overweights in non-life insurance, miscellaneous finance, railroads and pollution control issues. For the twelve months ending in March, portfolio performance benefited from overweights in aerospace, drugs and banks, while overweights in railroads, iron and steel and tires and an underweight in business machines detracted from performance. Stock selection added the largest increment to portfolio performance during the first quarter and for the year ending in March. Holdings which contributed to positive stock selection during the first three months of 1996 included Aetna, AON, Cigna, Citicorp and Sprint. Holdings which, on a stock specific basis, detracted from performance during the first quarter included Lockheed Martin, Kimberly Clark and Enron.

2. *Future Strategy. What active bets are in place at the present time relative to your benchmark? Summarize the rationale for making these active bets.*

Our process remains focused on identifying those stocks that are most attractive in price/value terms through intensive individual company analysis, which incorporates strategic themes and industry research. We continue to find that stocks strong in relative strength rank poorly, a typical result for us. The portfolio is also modestly overweighted in stocks with higher earnings variability and financial leverage characteristics. This exposure is due largely to a modest overweight in financials and a moderate underweight in utilities.

Brinson Partners, Inc. (con't)

From an industry perspective we continue to hold an overweight in financial/interest sensitive stocks. A common thread in our insurance holdings is a trend toward restructuring and improved management focus, along with our belief that uncertainty surrounding environmental liabilities for casualty insurance companies may diminish and estimated liabilities may decline.

The portfolio is underweighted utilities, including both electric utilities and the traditional telephones. We continue to see evidence that the eventual deregulation of power generation is accelerating competitive pressure from lower cost utility and non-utility generators and will increase the purchasing power of larger power users. Competition will intensify in the telecommunications and cable industries as regulatory barriers between traditional business lines are blurred and the traditional regional telephone companies are pushed toward "cost of service" pricing.

We are overweight in the non-health consumer sector including retail/apparel, durables and discretionary spending stocks, reflecting additions to the consumer sector of the portfolio in recent months. We have consciously reduced our exposure to tobacco stocks, in light of what appears to be increased litigation risk. The portfolio also remains overweighted in selected health care and drug stocks. Since we see competitive pressures in the industry, all our health care selections are companies which we believe can maintain profitability in a more competitive environment.

We are overweighted in transportation resulting entirely from an overweight in railroads. In general, we believe that secular improvement in railroad industry profitability will continue as regulatory barriers continue to fall. The portfolio is underweighted in chemicals and neutral in other basic industries. We find market prices for most commodities above our estimate of the equilibrium level, which is not unusual during the mature phase of an economic recovery. Finally, the portfolio is overweight with respect to aerospace and defense and underweight in technology and other producer goods. Key holdings include Avon, Chase Manhattan, Citicorp, Burlington Northern, Enron, Lockheed Martin, Mattell and Schering-Plough.

3. *Organizational Issues. Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.*

There have been no significant organizational changes in this past quarter.

Six US Equity accounts were gained for \$547 Million; no accounts were lost during the quarter.

4. *Other Comments. Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.*

None this quarter.

Staff Comments

No comments at this time.

Manager Commentary
Forstmann-Leff Associates Inc.

Period Ending:	3/31/96	Returns	Qtr.	1 Yr.
Total Firm Assets Under Management	\$2.8 Billion	Actual	11.6%	33.6%
Total Firm Assets Managed in this Discipline	\$1.4 Billion	Benchmark	7.2%	30.7%

1. *Past Performance. Summarize your performance over the last quarter and year. Specifically, what active bets did you make relative to your benchmark? Which of these bets worked/did not work and why?*

Performance for the first quarter was well ahead of the market. The portfolio benefited from a significant overweight in the consumer retail sector, where stock selection produced a return three times that of the index. These stocks rallied off of a disastrous fourth quarter as investors realized that profits were indeed stronger than had been feared late in the year. The consumer services sector, including the hotel/motel group, was also quite profitable, as key holdings advanced roughly 20%. An overweight to the market and strong equity returns also provided gains in the health care sector. Though not an attractive sector in the benchmark, strong stock selection in the technology sector added value over the period. An underweight in the better performing interest sensitive sector was the one weakness in the portfolio over the period.

Performance for the year was positively impacted by strong stock selection in the medical and related names, including good returns from major positions in HEALTHSOUTH Rehabilitation Corp., and Vivus Inc. Stock selection in the technology area was quite productive, producing a significant premium to the benchmark return. The major holding of note in the sector was Intel Corp. Finally, the portfolio's overweight and orientation toward the railroads, agricultural equipment manufacturers and paper and forest product companies helped to produce significant value added in the cyclicals.

2. *Future Strategy. What active bets are in place at the present time relative to your benchmark? Summarize the rationale for making these active bets.*

Current portfolio structure represents a barbell strategy encompassing mid-cap growth names, discussed in the last few letters, and global cyclicals. Significant holdings in the mid-cap growth area include names in the consumer retail and lodging groups, special situations in the health care sector, and groups within the technology area. We are starting to see the price/earnings multiple expansion anticipated in our last letter, as evidenced by the outperformance of the mid-cap growth names over the S&P 500 in the first quarter. Recent price movements have boosted multiples to 1.2 times the growth rate, up from multiples at par with growth rates observed in previous months. In our view, this cycle could well take these names to levels closer to two times their growth rates, indicating that there is much left in the play.

Forstmann (con't)

Rounding out our strategy, we favor global cyclicals which should benefit from international growth rates of close to 3%. This includes a concentration in domestic farm equipment manufacturers. Global grain stocks are currently at historical lows at the same time that demand is increasing in emerging markets. It would take two years of record harvests to rebuild normal inventory levels, suggesting that farmers will be well positioned to make capital purchases for some time. In addition, needed productivity enhancements overseas should bolster foreign sales. In spite of these favorable conditions, the group has maintained low price/earnings multiples and modest expectations among investors.

Large accumulated inventories in aluminum should reverse the year, producing a demand squeeze and attendant pricing leverage in 1997. We have made investments in the major producers in anticipation of a move in these names. Finally, we maintain a commitment to the energy service area, which should continue to benefit from the application or technological advances throughout the industry.

- 3. Organizational Issues. Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.*

No organizational changes to report.

- 4. Other Comments. Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.*

We are very pleased with the structure of the portfolio for this climate. Unless bonds stage a dramatic, unanticipated rally, we should continue to put distance between ourselves and the Benchmark. However, we should be able to anticipate difficulties within the bond market through our micro analysis, and will move quickly to raise cash in those portfolios which allow us to do so. Though we expect returns in the single digits for the S&P 500 Index, careful selection of securities such as those with attractive growth characteristics in the mid-cap segment should allow us to finish the year well ahead of the Benchmark.

Staff Comments

No comments at this time.

Manager Commentary
Franklin Portfolio Associates Trust
Active Account

Period Ending:	3/31/96	Returns	Qtr.	1 Yr.
Total Firm Assets Under Management	\$ 8.9 Billion	Actual	9.7%	32.3%
Total Firm Assets Managed in this Discipline	\$539 Million	Benchmark	6.0%	29.9%

1. *Past Performance. Summarize your performance over the last quarter and year. Specifically, what active bets did you make relative to your benchmark? Which of these bets worked/did not work and why?*

Last Quarter's Performance:

Performance for the account was ahead of the benchmark for the period. According to our performance attribution analysis stock selection was a strong positive contributor to active return. Industry exposures made a small negative contribution and risk-index exposure contributions were slightly positive. Factor and Industry contributions represent the combination of the average bets made relative to the benchmark and the performance of these factors/industries. Issues which were strong performers for the account were EMC Corp. (36%), Union Carbide (32%), Caremark International (30%), Green Tree Financial (30%), and First USA Inc. (28%). Issues which performed poorly were Pacific Gas & Electric (-21%), Unicom Corp. (-18%), Micron Technology (-16%), Autodesk (-12%), and KLA Instruments (-8%).

The risk factor bets which helped performance were positive tilts on Earnings Variability and Earnings-to-Price and a slight negative tilt on growth. Risk factors which hurt performance were a negative tilt on Size and a positive bet on Variability-in-Markets. Industry contributors to active return were positive bets in Miscellaneous Finance, Oil Service, and Air Transportation. Industry bets that hurt performance were negative bets in Retail, Hotel and Restaurants, and Health (Non-Drugs). Note that our investment process does not specifically target industry groups for over and under weighting but rather these bets arise out of our selection of individual issues.

Twelve Month Performance:

Twelve month returns were strong in an absolute sense and were also ahead of the account's benchmark. The data from our performance attribution analysis point to stock selection bets, industry bets and risk-index bets as all having contributed to active return over the period. Issues in the portfolio which were strong contributors to performance were Safeway Inc. (65%), Union Carbide (62%), Bank of New York (56%), Halliburton (46%), and Norwest Corp. (45%). Issues which hurt performance were Pacific Gas & Electric (-26%), Scientific Atlanta (-22%), Arrow Electronics (-15%), Autodesk Inc. (-13%), and American Greetings (-12%). A positive bet on the Success risk factor was the largest positive contributor to active return. However a positive tilt on Variability-in-Markets had a negative impact. Industry bets that helped performance were Food, Oil Service, Gas Utilities, and Food Stores. In all cases, the account had positive active bets in these groups and they performed well. Underweighting of Services, Retail, Health (Non-Drugs), and Beverages hurt performance.

Franklin (con't)

2. *Future Strategy. What active bets are in place at the present time relative to your benchmark? Summarize the rationale for making these active bets.*

As of March 31, 1996, the following significant active bets existed in the account relative to benchmark:

- A. Factor bets (bets stated as standard deviation from benchmark):

Success = 0.11	Earnings/Price = 0.36	Trading = 0.11
Earnings Variability = 0.11	Leverage = - 0.12	
Labor Intensity = -0.15	Variability-in-Markets = 0.14	

- B. Industry bets (bets stated as percentage deviation from benchmark weight):

5 Most Positive Bets:		5 Most Negative Bets:	
Misc. Finance	3.10%	Retail	-2.20%
Thrifts	2.40	Media	-1.74
Gas Utilities	2.24	Hotel, Restaurants	-1.60
International Oils	2.18	Food	-1.34
Air Transportation	1.96	Services	-1.32

- C. Ten largest Stock bets (bets stated as percentage deviation from benchmark weight):

Textron	2.43%	Union Carbide	2.03%
Analog Devices	2.37	Cardinal Health	2.00
IBM Corp.	2.31	MBNA Corp.	2.00
Travellers Inc.	2.22	Panenergy Corp.	1.94
Dana Corp.	2.11	Medtronic Inc.	1.93

Active portfolio bets are based on two factors - (a) the rank of individual issues as computed by Franklin's multi-factor ranking methodology, and (b) the effect of each issue on the "tracking error" or risk characteristics of the overall portfolio relative to the benchmark. The portfolio construction objective is to obtain as high a rank as possible consistent with the residual risk (tracking error relative to the benchmark) objective. We attempt to maintain a total tracking error of approximately 3% to 3.5% relative to the benchmark with the tracking error resulting from stock bets being better than 70%. As a result of the stock selection bets, the portfolio acquires the industry and risk factor bets as described above. As of quarter-end, the forecast total tracking error for the portfolio was 3.48% with 82% of the tracking coming from stock specific risk.

3. *Organizational Issues. Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.*

There were no significant personnel or organizational changes at the firm since the last quarter. There were no account gains or losses in this discipline during the period. On a firm-wide basis we gained two accounts in the period.

4. *Other Comments. Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.*

None.

Staff Comments

No comments at this time.

**Manager Commentary
GeoCapital Corporation**

Period Ending:	3/31/96	Returns	Qtr.	1 Yr.
Total Firm Assets Under Management	\$1.922 Billion	Actual	5.4%	25.9%
Total Firm Assets Managed in this Discipline	\$1.922 Billion	Benchmark	4.8%	35.6%

1. *Past Performance. Summarize your performance over the last quarter and year. Specifically, what active bets did you make relative to your benchmark? Which of these bets worked/did not work and why?*

GeoCapital outperformed the benchmark in the most recent quarter (ending 3/31/96) and underperformed for the year ending the same period. As discussed with SBI and Richards & Tierney, a new modified benchmark was installed at year end 1995. During the first quarter, we invested most of the cash present at year end in new consumer stocks and added to current technology issues.

As opposed to new purchases underperforming the rest of the portfolio in the fourth quarter of 1995, recent purchases outperformed the portfolio and overall stock market in the first quarter of 1996.

GeoCapital's portfolio vs. benchmark weightings (value added):

	Quarter Ending 3/31/96	Year Ending 3/31/96
Consumer non-durable	Positive Higher weightings/higher returns	Negative Higher weightings/lower returns
Technology	Positive Under weightings/lower returns	Negative Under weightings/slightly lower returns
Financial	Negative Higher weightings/lower returns	Negative Higher weightings/lower returns

2. *Future Strategy. What active bets are in place at the present time relative to your benchmark? Summarize the rationale for making these active bets.*

We continue to add to our technology area specifically in the application software and data networking sectors. While our total technology exposure in the portfolio is slightly above the benchmark's exposure we are actively betting that the software and networking sectors will outperform. The financial sector continues to be an active bet as our portfolio exposure is about 30% higher than the benchmark. This is mainly represented by our holding in Mercury Finance which we believe is very attractively priced relative to its outlook for growth. Our energy exposure continues to be quite a bit below the benchmark.

GeoCapital (con't)

3. **Organizational Issues.** *Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.*

No change in personnel.

No accounts were gained or lost.

4. **Other Comments.** *Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.*

With our continuing emphasis on growth companies delivering a new technology or service as a key component of our investment discipline, we were significantly overweighted in the technology sector. The first quarter is traditionally a seasonally weak quarter for technology companies as pipelines are drained in the fourth quarter and technology budgets are used up. In addition, this sector exhibited volatility in market valuations as high expectations were built into stock prices of relatively early stage opportunities. Given this environment, we generally did a good job of avoiding problems. With positive technology returns in the quarter, we outperformed some of the relevant benchmarks.

The special situation side of our blended small-capitalization approach served us well in the first quarter. As is typical for this area, the companies are not specific to one industry but are companies which share some of the investment characteristics which we believe reflect value that is currently unrecognized in the market. Some of our longer term positions in such areas as deathcare services, building maintenance, and information services added value in the quarter. In addition, our clients benefited from special situations including spin-offs and some of our consumer/retail positions.

One other area of outperformance is our education sector where we have invested in companies leading a trend toward for-profit education at the degree-granting college level and educational software companies.

In the overall market, we are experiencing high volatility seemingly driven exclusively by the interest rate outlook. While we would not deny the significance of interest rates on individual company valuations, we would also point out that the valuations will also be driven by the earnings performance and value-creating activities of the individual companies. As such, we continue to employ fundamental analysis to search out and find those opportunities where we believe we can create wealth for our clients.

Staff Comments

No comments at this time.

Manager Commentary
Investment Advisers, Inc.

Period Ending:	3/31/96	Returns	Qtr.	1 Yr.
Total Firm Assets Under Management	\$ 15 Billion	Actual	4.2%	29.6%
Total Firm Assets Managed in this Discipline	\$ 828 Million	Benchmark	5.1%	29.2%

1. ***Past Performance.** Summarize your performance over the last quarter and year. Specifically, what active bets did you make relative to your benchmark? Which of these bets worked/did not work and why?*

For the quarter ended March 31, 1996, the Portfolio returned 4.21% versus a benchmark 5.1%. Our underperformance was due to several factors. Cash above policy cost the Portfolio 0.25% of relative performance. The remaining 65 basis points of underperformance were due to very poor performance of three stocks: FSI International, Secure Computing, and Aetrium. These stocks experienced significant underperformance for the quarter, but we believe each to be significantly undervalued and we were net buyers of all three throughout the quarter. Eliminating the impact of cash and those three stocks, the balance of the Portfolio performed very well during the quarter.

For the year, the Portfolio was up 29.6% versus 29.2% for the benchmark. To ascribe our outperformance to any one factor(s) would not do justice to the variety of ebbs and flows that have defined the bull market over the last year. Throughout the year, our overweighted position in capital goods actually was a plus, even though the sector hardly distinguished itself. Our moves in and out (and then back in) the telecommunications equipment sector added performance to the Portfolio. The bulk of our performance came from individual stock selection and an adherence to our valuation discipline (which is what made telecommunications equipment a plus for us). On the negative side, our underweighting in banks, consumer nondurables, and airlines over the year certainly held back relative performance.

We have now annualized our Regional benchmark and feel our year's commentary will be more relevant to our actual universe.

2. ***Future Strategy.** What active bets are in place at the present time relative to your benchmark? Summarize the rationale for making these active bets.*

We have trimmed some of our capital goods stocks due to valuations, though we still maintain an aggregate overweighted position. We have increased our weighting in Consumer Durables, going to an overweighted position in the group. That decision was based on valuations and a very muted outlook from the street in some quality local names.

We have cut our positions in the Medical field. Mid-1995, we adjusted the portfolio in this area by de-emphasizing the large cap names in favor of smaller cap names. That decision has proven to be quite successful, but we are now seeing the private and public valuations in the medical field converge providing little upside to our smaller cap names. We have lowered the overall weighting in the group and moved into some special situations we believe have been overlooked.

IAI (con't)

3. *Organizational Issues.* Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.

None.

4. *Other Comments.* Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.

None.

Staff Comments

IAI was placed on probation in March 1996. Staff will continue to monitor for any affects of the TSB/Lloyds Bank merger on IAI and the transition of Mark Hoonsbeen as the SBI portfolio manager. Staff will report back at the end of next quarter, as required by the Manager Continuation Policy, with any recommendations if necessary.

Manager Commentary
IDS Advisory Group, Inc.

Period Ending:	3/31/96	Returns	Qtr.	1 Yr.
Total Firm Assets Under Management	\$27.1 Billion	Actual	3.1%	32.5%
Total Firm Assets Managed in this Discipline	\$ 6.7 Billion	Benchmark	5.8%	32.6%

1. *Past Performance.* Summarize your performance over the last quarter and year. Specifically, what active bets did you make relative to your benchmark? Which of these bets worked/did not work and why?

The State of Minnesota account underperformed the Normal Portfolio over the last three months and year. This underperformance in the quarter primarily reflected poor stock selection. Sector allocation and other factors were basically neutral. In particular, the technology sector had dismal performance relative to the market, and we were heavily overweighted in this area, and our stock selection was also less than stellar. To a lesser extent we were also impacted by poor stock selection in the consumer stable and consumer cyclical areas.

2. *Future Strategy.* What active bets are in place at the present time relative to your benchmark? Summarize the rationale for making these active bets.

Our sector weights are as follows:

	3/31/95	3/31/96	Benchmark 3/31/96
Technology	11.5	22.6	17.9
Consumer Stable	15.5	18.8	26.0
Consumer Cyclical	10.5	11.0	13.4
Utilities (non electric)	5.1	5.1	5.1
Financial Services	19.2	11.8	12.5
Energy	8.1	3.7	5.7
Industrial Basic	7.3	4.0	4.8
Industrial Growth	4.5	12.5	2.7
Industrial Cyclical	9.3	6.6	7.1
Equity Cash	<u>8.8</u>	<u>3.8</u>	<u>5.0</u>
	100.0	100.0	100.0

As already noted, we continue to be heavily overweighted in the technology sector. In fact, we have further increased our holdings in this sector since the close of the quarter. We strongly believe that this is the most undervalued sector of the market by a wide margin. A slowdown in PC demand has caused many portfolio managers to jettison their technology holdings. It is our belief that the introduction of Windows NT will lead to a renewed growth later this year. If such proves to be the case, earnings momentum is likely to reaccelerate and multiples once again expand. We remain confident that this sector will significantly outperform the general market before the close of the year. You will also note that the consumer stable sector is significantly underweighted relative to the benchmark. This reflects our belief that this sector is fully valued. The very portfolio managers who were selling technology appear to have been the same portfolio managers buying consumer stables. As the clouds lift over the technology sector, we think many managers will reverse course and once again move from consumer stable back to technology. We are significantly overweighted in the industrial intermediate

IDS Advisory Group, Inc. (cont'd)

growth sector. This reflects our belief that conglomerates and other "chicken cyclicals" will post better than anticipated earnings. Valuations of securities in this sector are reasonable and better than expected earnings growth should generate very positive performance. Most other sectors of the portfolio are carrying weights basically in line with the benchmark. Despite the performance of the first quarter, we are confident with our current weightings and do not anticipate major changes.

Our economic framework remains unchanged. Despite wildly gyrating economic statistics, it is our belief that the economy will grow at approximately 2% and that inflation will remain at the 3 to 3 1/2% level. Last quarter we did not subscribe to the notion that the economy was going into a depression, and this quarter we do not subscribe to the notion that the economy is overheating. Rather, we are in the camp that says the economy will muddle along. Assuming that this forecast proves accurate, interest rates should roll over and decline once again. We are forecasting a 30-year Treasury yield of 6% by year end. Based on this forecast the equity market is fairly valued despite its current multiple of 17 and its yield of 2.2%. Our dividend discount models anticipate a total rate of return over the next year of approximately 10%.

3. **Organizational Issues.** Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.

We have added two portfolio managers during the last quarter as follows:

Adele Bruce	Continental Europe
Gavin Corr	United Kingdom

There have been no significant personnel departures during the last quarter.

Product	Gains		Losses	
	# of Accounts	Assets (\$MM)	# of Accounts	Assets (\$MM)
Large Cap Equities	3	203.0	1	68.9
Balanced	4	110.9	0	0
International	0	0.0	0	0
Regional-Pacific/Far East	1	10.0	0	0
Global Ex-Australia	1	19.3	0	0
Latin America	0	0.0	0	0
Small Cap Equities	0	0.0	0	0
Mid Cap Equities	1	1.5	0	0
Research Core	0	0.0	0	0
Research Aggressive	5	86.1	0	0

* Temporary Account Arrangements

4. **Other Comments.** Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.

None.

Staff Comments

No comments at this time.

Manager Commentary
Independence Investment Associates

Period Ending:	3/31/95	Returns	Qtr.	1 Yr.
Total Firm Assets Under Management	\$22.5 Billion	Actual	5.0%	32.3%
Total Firm Assets Managed in this Discipline	\$11.4 Billion	Benchmark	5.8%	32.7%

1. *Past Performance. Summarize your performance over the last quarter and year. Specifically, what active bets did you make relative to your benchmark? Which of these bets worked/did not work and why?*

The U.S. stock market rose 5.3% in the first quarter on expectations that the slow growth, low inflation economic environment will continue. As the quarter closed, the financial markets were digesting a round of economic data which challenged this thesis. Investors must now determine if the pace of economic growth will change, and more importantly, if this is good or bad news for the financial markets. Your portfolio posted solid results over the last twelve months though lagging the S&P 500 slightly in the first quarter. The slower paced economic environment led investors to favor growth stocks early in the quarter. But in March, several pieces of economic data caused investors to rethink the strength of the economy leading to a rally in cyclicals, with the end result being that value stocks outperformed growth for the full quarter. Large capitalization stocks posted marginally better returns than small capitalization stocks. During the quarter, Basic materials, Consumer Cyclical and Financials led the market, while Utilities and Technology stocks lagged. Your portfolio's industry over/underweightings relative to the benchmark will be minimal over time. At quarter end, it was slightly overweighted in Consumer Cyclical and Financials and slightly underweighted in Consumer Service and Technology. Monsanto, Chemical Bank and PepsiCo are major holdings in your portfolios that posted solid performance during the quarter. Legal issues surrounding the tobacco industry caused Philip Morris to lag during the quarter after turning in a stellar performance in 1995. Xerox and Unicom also were significant holdings in your portfolio that trailed the market. Major purchases in the portfolio for the first quarter included AT&T, Unilever and United Technologies, while stocks such as Texas Instruments and SBC Communications were eliminated. Our composite valuation model Cybercode, which is used to rank securities for our equity portfolios, performed better later in the quarter after being random in January. Independence's intrinsic or cheapness models performed better than our momentum models in the quarter which was a switch from the fourth quarter of 1995. We continue to update the component models weights of Cybercode on a quarterly basis with an approximate 50% split between the cheapness and improving fundamental models.

Independence (con't)

2. *Future Strategy.* What active bets are in place at the present time relative to your benchmark? Summarize the rationale for making these active bets.

Independence believes that excess returns are achieved by constructing portfolios with stocks combining intrinsically attractive valuations and improving business outlooks, and will continue to manage your portfolio using this investment philosophy and our disciplined investment process. These characteristics of "cheapness and improving fundamentals" are demonstrated in your portfolio's P/E ratio of 14.4, below the S&P 500 P/E of 17.2 and by the five year projected earnings growth rate of 10% verses the benchmark's expected growth rate of 7.0%.

3. *Organizational Issues.* Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.

During the first quarter of 1996, there have not been any significant ownership or personnel changes at the firm. We are pleased to announce our first international equity funding. This EAFE benchmarked product extends Independence's quantitative, disciplined investment process into the international arena. Like our NIXDEX products, our EAFE portfolios will emphasize specific stock selection while controlling risk across countries and industries. We look forward to keeping you informed of our progress in the coming year.

4. *Other Comments.* Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.

None.

Staff Comments

In late April, Independence agreed to acquire Boston International Advisors, Inc. as a wholly owned subsidiary. Boston International Advisors provides an extensive historical database on international securities, trading and operational capabilities to boost Independence's recent entrance into management of international securities. Staff does not believe the acquisition will adversely affect the management of SBI's domestic equity account.

Manager Commentary
Jundt Associates, Inc.

Period Ending:	3/31/96	Returns	Qtr.	1 Yr.
Total Firm Assets Under Management	\$3,001 Million	Actual	3.4%	18.8%
Total Firm Assets Managed in this Discipline	\$2,440 Million	Benchmark	2.7%	26.1%

1. **Past Performance.** *Summarize your performance over the last quarter and year. Specifically, what active bets did you make relative to your benchmark? Which of these bets worked/did not work and why?*

Quarter: The funds favorable relative performance versus the benchmark portfolio in the quarter was primarily a result of its heavy overweighting in the technology sector (42% vs. 30%) and excellent stock selection (+4.5% vs. -4.0%). The largest absolute bet in the portfolio was the consumer non-durable area at 49% vs. 41% in the benchmark. Here, sector allocation and stock selection caused a slightly negative return on a value added basis. All other bets are either marginally positive or negative. Strong stocks in the quarter included: Peoplesoft, Tellabs, Worldcom, and Staples. Stocks having negative returns included: Intuit, Netscape, 3Com, and Genzyme.

Twelve Months: Twelve month relative returns were in part hurt by our higher cash position of nearly 15% vs. 8% in the benchmark and accounted for one-third of the negative value added return during the year. All other areas, except for capital goods, showed marginally positive or negative results. One stock, Nokia, as a result of poor unexpected earnings results, accounted for 25% of the negative value added during the year.

Strong stocks for the 12 month period included: Boston Market, Oxford Healthcare, Healthsource, Biogen, Microsoft, Cisco Systems, and Staples.

Weak stocks during the year included: Mobile Telecommunications, Motorola, H&R Block, Office Depot, and Netscape.

2. **Future Strategy.** *What active bets are in place at the present time relative to your benchmark? Summarize the rationale for making these active bets.*

The current cash position is less than 1%. As a result of meeting with the State representatives, future cash levels will not exceed 5%. Continued heavy areas of emphasis include consumer non-durable stocks and technology; though relative to the new benchmark, these areas are more evenly weighted. Among the largest holdings are Microsoft, Healthsource, Lilly Eli & Co., Staples, Starbucks, Worldcom and Petsmart. We think the worst is behind us in terms of the backup in interest rates, and with more cyclical companies now reporting flattish type of earnings growth, we feel that the more consistent strong growers, as we have in your portfolio, will perform relatively well over the next 12 to 18 months.

Jundt (con't)

3. *Organizational Issues.* Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.

None.

4. *Other Comments.* Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.

None.

Staff Comments

The SBI must raise additional funds for the domestic equity program for asset allocation and total fund rebalancing. Staff are recommending that the SBI's relationship with Jundt be terminated to provide funds for these purposes.

Due to significant underperformance (11.0% actual vs. 16.8% benchmark, annualized since July 1993), changes in personnel and recent account losses, staff's confidence in the firm's organization and investment process has deteriorated. Given the need to raise funds, staff believes it is appropriate to terminate the relationship at this time.

Manager Commentary
Lincoln Capital Management Company

Period Ending:	3/31/96	Returns	Qtr.	1 Yr.
Total Firm Assets Under Management	\$39 Billion	Actual	6.8%	37.2%
Total Firm Assets Managed in this Discipline	\$13 Billion	Benchmark	5.3%	31.5%

1. ***Past Performance.** Summarize your performance over the last quarter and year. Specifically, what active bets did you make relative to your benchmark? Which of these bets worked/did not work and why?*

Quarter - The portfolio exceeded the benchmark by 150 basis points, 40 of which is attributable to sector allocation and 110 to stock selection. The positive sector contribution resulted from overweights in technology and specialty chemicals, offset partly by an underweighted position in health care. Stock selection was very good in technology, specialty chemicals, entertainment, health care, and financial services.

Last 12 Months - The portfolio's return exceeded that of the benchmark by roughly 570 basis points, all of which came from stock selection. Stock selection was good in the following sectors: specialty chemicals, health care, consumer non-durables, and technology.

2. ***Future Strategy.** What active bets are in place at the present time relative to your benchmark? Summarize the rationale for making these active bets.*

Sector weightings are not significantly different from those in the benchmark. The active portfolio is meaningfully overweighted in the consumer non-durable area (beverages and tobacco specifically) and moderately underweighted in retail as well as finance. The key bets are in the concentrated weightings of the top 10-15 issues.

Lincoln (con't)

3. *Organizational Issues.* Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.

Lincoln's equity group was supplemented by one new member in the first quarter of 1996. Mike Pytosh, previously with J.P. Morgan's investment department in New York, joined us in January to work with Nancy Spady in the tech/telecomm area. This addition was previously communicated in our February monthly letter.

One account was gained in the equity area during the first quarter of calendar 1996. Another sponsor transitioned from a balanced fund to equity account mode.

4. *Other Comments.* Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.

None.

Staff Comments

No comments at this time.

**Manager Commentary
Oppenheimer Capital**

Period Ending:	3/31/96	Returns	Qtr.	1 Yr.
Total Firm Assets Under Management	\$40 Billion	Actual	8.0%	37.9%
Total Firm Assets Managed in this Discipline	\$27.4 Billion	Benchmark	6.3%	31.2%

1. *Past Performance. Summarize your performance over the last quarter and year. Specifically, what active bets did you make relative to your benchmark? Which of these bets worked/did not work and why?*

For the quarter, the portfolio was positively impacted by our conviction in undervalued stocks, particularly in the basic industry (Champion International, DuPont, Freeport McMoan, Hercules and Monsanto) and the banking sectors (Citicorp, First Interstate Bancorp and Mellon Bank). First Interstate Bancorp, one of the best performing stocks in the portfolio, has been acquired by Wells Fargo. While the stock price is significantly higher, we plan to continue to maintain the position as we believe the combined entity will continue to create significant value for shareholders. The top five contributors and detractors to performance for the first quarter follow:

<u>Top Five</u>		<u>Bottom Five</u>	
Morgan Stanley Group	29.5%	Shaw Industries	(25.0%)
First Interstate Bancorp	27.7	Nokia	(12.2)
Monsanto	26.0	Progressive	(8.6)
Citicorp	19.7	Motorola	(6.8)
Sprint	17.4	Lockheed Martin	(3.4)

For the year, the portfolio outperformed the benchmark by the significant margin of 6.7% with stock selection contributing more than 70% of the portfolio's outperformance. Stocks in the basic industry, capital goods, banks and utilities sectors have consistently performed above the benchmark over the last twelve months. Of particular strength are the stocks in the banking industry, which returned 89.1% on average vs. the benchmark return of 53.9%. Basic industry securities outpaced the benchmark by 1.5% aided in particular by Monsanto which had a return of 96.5%. While the portfolio has an overweighting in the basic industry and banking sectors we maintain our positions based on a bottom-up fundamental research process. As a result of the continued success of corporate restructuring and utilization of free cash flow, many of the names among the top ten contributors have not changed since last quarter. They are as follows:

First Interstate Bancorp	126.2%	Exel Ltd.	60.5%
Monsanto	96.5	Sprint	57.1
Citicorp	91.9	Morgan Stanley Group	56.2
Travelers	74.5	Becton Dickinson	52.9
McDonnell Douglas	66.0	Federal Home Loan Mortgage	43.3

2. *Future Strategy. What active bets are in place at the present time relative to your benchmark? Summarize the rationale for making these active bets*

We continue to emphasize the level and sustainability of a company's return on invested capital and the allocation of cash flows among reinvestment in the business, timely acquisitions, share repurchase, and dividend payments. We invest in companies that generate

Oppenheimer (con't)

high returns and create value for their shareholders through their allocation of those returns. Such companies can compound their shareholder values for extended periods, even if the increased value is not immediately reflected in the price of the stock. In today's investment world, we believe our emphasis on capital allocation provides an advantage.

We own companies whose high capital returns generate cash flows in excess of their internal needs, leaving them with free cash flows. We believe this type of investment is less risky. We do not pay a premium for the superior returns, some portion of the excess cash is returned immediately to investors through share repurchase or dividends and we enjoy the stability of a high-return business. Among our portfolio companies in this regard are Becton Dickinson, Exel Ltd, Hercules and Wells Fargo, each of which have bought back about 15% of their shares over the past three years. Buy-backs benefit shareholders by increasing the value of the remaining shares. We believe this emphasis on cash flow and capital allocation will result in superior investment performance over time. The most significant active bet continues to be the double weighting in financial stocks. We realize that in the short-term these stocks may respond to changes in interest rate expectations, but we will continue to hold them as long as value is being created by these companies and the stocks remain reasonably priced.

3. **Organizational Issues.** *Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.*

There were no changes which impacted the management of the Minnesota portfolio. However, there have been the following changes in investment professional staff:

Kurt Schansinger, Senior Vice President, left the firm to join Merrill Lynch.

Jenny Beth Jones, Senior Vice President and Small Cap Team Leader has left the firm.

Lauren B. Young, Vice President, has joined the firm as a specialist in European equities. She comes to Oppenheimer Capital from Mitchell Hutchins Asset Management/Paine Webber, Inc. where she was a international equity analyst and portfolio manager. Prior to that, she worked as a financial analyst with Donaldson, Lufkin and Jenrette, and Salomon Brothers, Inc. Ms Young holds a BA from Yale University.

CORE EQUITY ACCOUNTS GAINED/LOST:

Accounts Gained: 14 accounts with \$125.4 million in assets.

Accounts Lost: 2 accounts with \$93.9 million in assets.

4. **Other Comments.** *Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.*

None.

Staff Comments

No comments at this time.

Manager Commentary
Waddell & Reed

Period Ending:	3/31/96	Returns	Qtr.	1 Yr.
Total Firm Assets Under Management	\$25.1 Billion	Actual	4.7%	26.9%
Total Firm Assets Managed in this Discipline	\$ 6.6 Billion	Benchmark	6.8%	30.8%

1. *Past Performance. Summarize your performance over the last quarter and year. Specifically, what active bets did you make relative to your benchmark? Which of these bets worked/did not work and why?*

Our performance for the quarter ending March 31, was 2.1% below the current benchmark and 3.9% for the one year period. Our overweighting in technology led to our underperformance for the quarter and year, as the sector continued to experience pricing volatility. Specifically, Broderbund and GT Interactive, two of the portfolio's software holdings, were poor performers. Additionally, the portfolio's Electronic and Technology services holdings experienced an average 4% price decrease over the quarter.

The overall market was characterized by record inflows into equity mutual funds, particularly in January. Investments in large, defensive staple areas were dominant, and continued to drive the bull market. Some of the major stock indices, such as the Dow Jones Industrial Index, achieved all-time highs in the quarter.

From our perspective, the price-to-earnings ratios of some of the stocks leading this surge are a cause for concern. Many industrial cyclical companies, for example, have experienced earnings declines year-over-year, yet the stock prices have held. As money continues to come into the market, investors seem to be investing with a blind eye toward current valuation. Rising indices in the midst of sub-par earnings growth expectations only add to our concerns about valuations.

Given this current market activity and the fact that our economy will experience only moderate growth over the next several years, we still believe it is a sound strategy to be invested in companies that offer true, long-term growth potential. While technology has been battered in the market since September 1995, we believe growth prospects in several technology-related areas are excellent relative to the overall U.S. economy.

During the quarter, we took advantage of some record high valuations and sold some securities experiencing strong price increases. Specific security changes were:

<u>Positions Increased</u>	<u>New Stocks</u>	<u>Stocks Sold</u>	<u>Stocks Reduced</u>
Allied Waste	American Intl. Group	Adobe Systems	Amgen
CUC International	Ascend Coms.	Albertsons	Cisco Systems
Evergreen Media	Informix	MidAmerica Apts.	Computer Assoc.
Teradyne	Intuit	Nimbus CD	Fed. Natl. Mortgage
		Petersburg Long Dist.	Motorola
		Photronics	United Healthcare
		Southwest Airlines	

Our performance was positively impacted by several factors. Our Healthcare holdings experienced an average price increase of 11%. The proposed acquisition of Loral by Lockheed Martin led that stock to a 39% gain. Ascend Communications, a new addition, advanced over 32% in the quarter. Additionally, our position in Emeritus rose over 75%.

Waddell (con't)

2. **Future Strategy.** *What active bets are in place at the present time relative to your benchmark? Summarize the rationale for making these active bets.*

Working with Richards & Tierney, we have revised our benchmark effective 4/1/96. While our investment style remains unchanged, we think the new benchmark should more closely reflect our normal "pool" of stocks.

Our current weightings are as follows:

<u>Underweighted</u>	<u>Overweighted</u>
Basic Industries	Technology
Consumer & Service	Utilities
Energy	
Financial	

We think that we are late in the U.S. economic cycle. Recent strength in basic industry stocks has been driven by the outlook for inventory rebuilding, but the sustainability of production gains into 2Q96 is suspect. While energy stocks have excelled on the spike in world crude oil prices, this phenomenon, too, we think is short term in nature.

Technology remains an area of the U.S. economy with some of the best earnings growth prospects and most compelling stock valuations. Our strategy is to remain overweighted in technology. We are being highly selective in the commodity semiconductor area which has experienced much recent volatility amidst declining demand.

Our cash position is currently above the benchmark level. We think this position is appropriate relative to the extended level of stock valuations. However, we will be carefully watching the consumer (i.e., auto sales, retail sales, etc.) as an indicator of market strength and will be lowering cash as growth opportunities present themselves.

3. **Organizational Issues.** *Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.*

During the first quarter, Mr. Hai Tang, an Industry Analyst, was hired.

4. **Other Comments.** *Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.*

We have had no significant issues occur in the last quarter that would affect the SBI account.

Staff Comments

In the last year and a half, Waddell & Reed has been reviewing their benchmark to address some concerns that staff has had. Staff will continue to monitor the results of the modifications that Waddell & Reed implements, to make sure that the quality of the benchmark is improving.

Manager Commentary
Weiss Peck and Greer

Period Ending:	3/31/96	Returns	Qtr.	1 Yr.
Total Firm Assets Under Management	\$12.6 Billion	Actual	8.9%	43.3%
Total Firm Assets Managed in this Discipline	\$ 1.3 Billion	Benchmark	4.3%	32.5%

1. *Past Performance. Summarize your performance over the last quarter and year. Specifically, what active bets did you make relative to your benchmark? Which of these bets worked/did not work and why?*

We are very pleased with our first quarter results versus the benchmark. The consumer area (including durable, non-durable and miscellaneous) continues to provide us with superior returns, on both an absolute and a relative basis. This is due primarily to good stock selection in these areas. Our holdings in transportation and technology have also been a significant benefit to the total account performance, and we have had positive returns from our health care stocks as well. As a result of a market shift towards cyclical stocks during the quarter, our holdings in intermediate goods significantly outperformed the benchmark's return.

Our holdings in the financial sector underperformed for the quarter due to what we believe was a temporary price correction in some of the larger holdings. Our analysis reveals a strong fundamental case for the long term performance of these stocks so we will be maintaining our positions in them.

2. *Future Strategy. What active bets are in place at the present time relative to your benchmark? Summarize the rationale for making these active bets.*

We are still "cautiously optimistic" looking forward. However, we believe a near term market correction is likely. Since the end of the quarter we have reduced our weighting in health care, taking profits in holdings that have performed exceedingly well, particularly biotech stocks. With most of our price targets and valuations realized, our bet in this sector has paid off. We are using the proceeds to increase our focus on cyclical stocks, seeing signs of growth in the economy and a continuation of good performance in this area.

Weiss Peck (con't)

3. *Organizational Issues.* Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.

Effective March 11, John P. Callaghan, Principal and co-head of the small cap growth area, resigned from Weiss, Peck and Greer to manage a hedge fund at Odyssey Partners. Candice Eggerss, Principal and Technology Analyst, also resigned in March to join J.P. Morgan.

We are interviewing candidates and are close to hiring a technology analyst. We are also in the final interview stage for another analyst to cover healthcare and biotechnology. We believe these positions are the most important to fill immediately and we are pursuing this course before making a decision about hiring another portfolio manager. We will keep you advised of our progress on all of these positions.

We also have a new addition to our group. Adam Starr joined us in March from our hedge fund area. He will be covering industrials and financial stocks for the small cap growth area.

4. *Other Comments.* Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.

None.

Staff Comments

Staff continues to monitor the changes in investment personnel. Staff intends to meet with the new portfolio manager immediately after the hiring process is completed. In addition, staff plans to make a visit to New York later in the year and will meet with Weiss, Peck, and Greer's full staff at that time.

Manager Commentary
Franklin Portfolio Associates Trust
Semi-Passive Account

Period Ending:	3/31/96	Returns	Qtr.	1 Yr.
Total Firm Assets Under Management	\$8.9 Billion	Actual	6.0%	31.9%
Total Firm Assets Managed in this Discipline	\$1.1 Billion	Benchmark	5.1%	31.1%

1. *Past Performance. Summarize your performance over the last quarter and year. Specifically, what active bets did you make relative to your benchmark? Which of these bets worked/did not work and why?*

Last Quarter's Performance:

The account was ahead of its benchmark for the quarter. According to our performance attribution analysis, stock specific bets and industry bets were positive contributors to active return. Risk index bets were a slight negative. Issues in the portfolio which were strong performers were Claire's Stores (54%), Cincinnati Bell (50%), California Energy (37%), The Sports Authority Inc. (34%), and Great Atlantic & Pacific (33%). Portfolio issues which were particularly weak were Fleming Cos. (-31%), Community Psychiatric (-27%), Castle & Cooke (-23%), Pacific Gas & Electric (-21%), and Interface Inc. (-20%).

Because of the tight tracking of the account relative to the benchmark, contributions from risk factor bets and industry bets were minor. A small positive tilt on Growth helped performance in the period. However a positive bet on Variability-in-Markets and a negative tilt on Size detracted from performance. Positive industry bets in Oil Service, Hotel & Restaurants, Health (non-Drugs), and Miscellaneous Finance contributed to active return. Underweighting Motor Vehicles, Railroads, and Real Estate cost the account during the period. Note that our investment process does not specifically target industry groups for over and under weighting but rather these bets arise out of our selection of individual stocks.

Twelve Month Performance:

The return for the account was above its benchmark return for the past twelve months. Risk factor and industry bets helped performance for the year. Stock specific bets were a slight positive as well. Issues which were strong contributors were Cincinnati Bell (93%), Goodrich B.F. (79%), Federal Paper Board (75%), Genetics Institute (68%), and Vesta insurance (64%). Issues which were weak were Handleman Co. (-42%), Fleming Cos. (-39%), CDI Corp. (-28%), Times Mirror (-28%), and Franklin Quest (-28%). A positive tilt on Success made a positive contribution to performance and a negative tilt on Size hurt performance. Overweighting Other Insurance, Gas Utilities, Health (Non-Drugs), and Oil Service helped the account for the period. Underweighting relative to the benchmark in Services, Railroads, Telephones, and Banks hurt relative performance during the period.

2. *Future Strategy. What active bets are in place at the present time relative to your benchmark? Summarize the rationale for making these active bets.*

As of March 31, 1996, the following significant active bets existed in the account relative to the benchmark:

- A. Factor bets (bets stated as standard deviations from benchmark):

Earnings/Price = 0.14

Trading Activity = 0.10

Franklin (con't)

B. Industry bets (bets stated as percentage deviations from benchmark weight):

5 Most Positive Bets:		5 Most Negative Bets:	
Gas Utilities	1.55%	Railroads	-1.26%
Electric Utilities	1.53	Telephones	-0.97
Misc. Finance	1.05	Producer Goods	-0.93
Health (Non-Drugs)	0.97	Electronics	-0.75
Soaps	0.74	Banks	-0.57

C. Ten largest Stock bets (bets stated as percentage deviation from benchmark weight):

Cincinnati Bell	0.74%	Travellers Inc.	0.59%
Ford Motor	-0.73	American Home	-0.59
Coca Cola	-0.68	Wal-Mart Stores	-0.58
Minnesota Mining	-0.66	Edison Int'l.	0.55
Chevron	-0.63	General Motors	-0.54

Active portfolio bets are based on two factors - (a) the rank of individual issues as computed by Franklin's multi-factor ranking methodology, and (b) the effect of each issue on the "tracking error" or risk characteristics of the overall portfolio relative to the benchmark. The portfolio construction objective is to obtain as high a rank as possible consistent with the residual risk (tracking error relative to the benchmark) objective. We attempt to maintain a total tracking error of under 1.5% relative to the benchmark with the tracking error resulting from stock bets being better than 70%. As a result of the stock selection bets, the portfolio acquires the factor and industry bets as described above. As of quarter-end, the forecast total tracking error for the portfolio was 1.28% with 77% of the tracking error coming from stock specific risk.

3. Organizational Issues. *Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.*

There were no significant personnel or organizational changes at the firm since the last quarter. There were no account gains or losses in this discipline during the period. On a firm-wide basis we gained two accounts in the period.

4. Other Comments. *Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.*

None.

Staff Comments

No comments at this time.

Manager Commentary
J.P. Morgan Investment Management, Inc.

Period Ending:	3/31/96	Returns	Qtr.	1 Yr.
Total Firm Assets Under Management	\$146 Billion	Actual	5.4%	32.2%
Total Firm Assets Managed in this Discipline	\$ 6.8 Billion	Benchmark	5.1%	31.1%

1. *Past Performance. Summarize your performance over the last quarter and year. Specifically, what active bets did you make relative to your benchmark? Which of these bets worked/did not work and why?*

The Research Enhanced Index (REI) portfolio is sector and style neutral relative to the benchmark, thus the only bets are individual stock selection decisions.

The REI portfolio outperformed its custom benchmark by 30 basis points in the first quarter as the majority of JPMIM sectors surpassed their benchmarks. The drug, energy, and consumer stable sectors had the greatest impact on performance.

Specific stocks which had the greatest positive impact on performance included General Motors Hughes which rose as the value of their satellite business was boosted when AT&T purchased a stake and launched an aggressive marketing campaign for DIRECTV. Pepsico continued to show strong results in their cola, restaurant, and snack food businesses. In addition, the stock rose as investors welcomed the new chairman's aggressiveness to downsize the restaurant business. Allied Signal outperformed as they received a better than expected price from the sale of their anti-lock brake business. Eli Lilly rallied sharply as investors became more excited over their new product and research and development efforts. In addition, the company also benefited from speculation over further consolidation in the drug industry. Sprint Corporation enjoyed good earnings due to strength in their long distance, local, and cellular businesses.

For the one year period ending March 31, 1996, the REI portfolio significantly outperformed its customized benchmark due to very strong results in several sectors. The consumer stable, finance, and drug sectors had the greatest impact on performance, with the chemical, transportation, and energy sectors also making large positive contributions.

Pepsico, Eli Lilly, and General Motors Hughes were among the top performing stocks for the year as well as the quarter (see above). Also among the best performers were Service Corporation which benefited from profitable international acquisitions and continued consolidation in the funeral home business, and Schering Plough, a drug company, which enjoyed improving fundamentals as well as the potential to be acquired at a premium.

J.P. Morgan (con't)

2. **Future Strategy.** *What active bets are in place at the present time relative to your benchmark? Summarize the rationale for making these active bets.*

All of the names mentioned above remain in the top quintiles as they have above average expected returns. Our stock selection process buys/holds those stocks within each sector that have the highest DDRs and sells those with low expected returns. Since the portfolio is fully invested, sector neutral, and factor neutral, the only active bets are individual stock over and under weightings.

3. **Organizational Issues.** *Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.*

The structured equity group added a new portfolio manager. One account was gained and one was lost due to asset allocation changes.

4. **Other Comments.** *Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.*

None.

Staff Comments

No comments at this time.

Manager Commentary
BZW Barclays Global Investors
Semi-Passive Account

Period Ending:	3/31/96	Returns	Qtr.	1 Yr.
Total Firm Assets Under Management	\$290.1 Billion	Actual	5.2%	34.9%
Total Firm Assets Managed in this Discipline	\$ 7.0 Billion	Benchmark	5.1%	31.1%

1. *Past Performance.* Summarize your performance over the last quarter and year. Specifically, what active bets did you make relative to your benchmark? Which of these bets worked/did not work and why?

BGI Global Investors' Alpha Tilts Strategy, customized for the Minnesota SBI, outperformed the Minnesota Custom Benchmark by 0.12% in the first quarter of 1996, and outperformed by 3.83% over the last 12 months. This strategy systematically evaluates companies according to a broad set of investment characteristics in order to construct a risk-controlled, index-like portfolio with expected returns in excess of the benchmark. The active risk level of the portfolio is generally maintained at 1.0 - 1.5%; from inception and over the past year the realized active risk was well within this range.

The attribution of added returns in the first quarter is shown in the table below. The portfolio's use of analyst information to identify companies experiencing positive changes in earnings expectations added 0.38% during the quarter. The use of valuation measures to identify stocks trading at attractive prices relative to their underlying economic value added 0.02% in the first quarter. The use of signaling measures, which include corporate financing activity and informed insider trading, contributed -0.02% in the first quarter. As expected, industry weighting differences made only a small contribution to the portfolio's active return (0.09%), due to the tight risk controls we use in this area. Finally, the portfolio experienced negative security-specific returns in the first quarter, representing the idiosyncratic or residual returns of individual companies that cannot be explained by their industry group, style, size or other common characteristics. Over shorter measurement intervals, the returns attributable to security-specific sources can be relatively large in magnitude, but this source of tracking error risk tends to diversify toward zero over longer holding periods. The Alpha Tilts portfolio minimizes this risk through broad diversification (approximately 800 stocks) and by limiting the active positions taken in individual companies.

Active Return Attribution:

	Quarters	Past Year
Analyst inputs:	0.38%	2.21%
Fundamental value:	0.02	0.31
Technical inputs:	-0.02	0.00
Other common factors:	-0.15	-0.46
Industry weights:	0.09	0.35
Stock-specific	-0.21	1.43
Total active return:	0.12%	3.83%

BZW Barclays Global Investors (con't)

2. **Future Strategy.** *What active bets are in place at the present time relative to your benchmark? Summarize the rationale for making these active bets.*

The current Minnesota Alpha Tilts portfolio is similar in structure to the fourth quarter 1995 portfolio. Our investment process seeks to identify companies for which consensus expectations will be improving, by carefully modeling the linkage between changes in analysts' forecasts and future expectations and returns. Secondly, we emphasize companies that are trading at multiples (based on earnings and book value) that are below their industry peer group. Finally, we identify companies whose management has "signaled" their view of stock valuation to the market in the form of insider trading activity and corporate financing activity. These areas of emphasis in the portfolio are designed to be relatively consistent over time; we do not make subjective or ad hoc changes to our investment process. The rationale for these bets is based on a combination of economic/investment theory about how markets and investors operate and rigorous empirical testing to validate these ideas and determine the optimal way to incorporate them in highly risk-controlled portfolios. In general, we are seeking to capture systematic return effects that are generally overlooked by traditional investors.

3. **Organizational Issues.** *Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.*

The acquisition of Wells Fargo Nikko Investment Advisors by Barclays PLC (UK) proceeded smoothly and closed on December 31, 1995. The new firm continues to be based in San Francisco with Fred Grauer continuing in his role as Chairman and CEO. The acquisition should not impact your business with us or the relationship you have with BGI's key people, who are very supportive of this development.

We added 10 new clients in our Alpha Tilts Strategies during the first quarter, with a total funding of approximately \$2.0 billion. There were no lost clients in the Alpha Tilts Strategies during first quarter 1996.

New Alpha Tilts Clients, 1st Quarter 1996:

Georgia Pacific	Duke Power
American Chemical Society	American President Co.
Pension Benefit Guarantee Corp.	Metis Settlements
State of Connecticut	Commonwealth Edison
BellSouth	Brush Wellman

4. **Other Comments.** *Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.*

At this time, there are no special issues pertinent to the management of the SBI account.

Staff Comments

Staff recently met with BZW Barclays at their office to review their organization, investment strategy, and portfolio performance. Comments made during the meeting coincide with that made above.

Manager Commentary
BZW Barclays Global Investors
Passive Account

Period Ending:	3/31/96	Returns	Qtr.	YTD
Total Firm Assets Under Management	\$390.1 Billion	Actual	5.6%	20.2%
Total Firm Assets Managed in this Discipline	\$ 11.6 Billion	Benchmark	5.6%	20.2%

1. *Past Performance.* Summarize your performance over the last quarter and Year. Specifically, explain the reasons for the tracking error between the portfolio and the index.

BZW Barclays Global Investors' (BGI) Wilshire 5000 Strategy matched the Wilshire 5000 during the first quarter of 1996. At the end of the first quarter, the expected annual tracking error of the portfolio was 16 bps. This means that two thirds of the time the portfolio should track the index to within 8 bps per quarter and 95% of the time the portfolio should track to within 16 bps per quarter.

YTD tracking error is positive because positive tracking error due to security misweights also occurred in the fourth quarter of 1995.

2. *Future Strategy.* Going forward, what strategies, if any, do you plan to implement to control tracking error within expectations.

We continue to look for opportunities to rebalance the portfolio. We seek to rebalance on a cross only basis over time to minimize tracking error.

BZW Barclays Global Investors (con't)

3. *Organizational Issues.* Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.

No significant personnel or ownership changes took place during the last quarter.

Existing clients withdrew a net \$127 million from all US Equity market strategies during the first quarter. All monies moved to other strategies within BGI. Additionally, two new clients contributed \$95 million and two existing clients transferred \$7.3 million. Net activity for the quarter was a withdrawal of \$25.6 million.

4. *Other Comments.* Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.

During the first quarter, BGI traded approximately \$73 million (based on trade date prices) in the Wilshire 5000 portfolio. Trades were done to facilitate rebalancing, index changes, and dividend reinvestment. Of the \$73 million traded, \$38 million was crossed either with other BGI clients/funds, through Instinet/Posit, or with brokers. Approximately \$35 million was traded in the open market. Assuming that these cross transactions saved Minnesota just one half of the bid/offer spread, the amount saved was \$141 thousand (est 37 bps times the amount crossed).

Staff Comments

Staff met with BZW Barclays at their office in March 1996. During the meeting, staff was informed that Andy Olma, SBI's index strategist, plans to move to the international index side of BZW. When the new strategist is hired, staff will monitor the transition and maintenance of the SBI Wilshire 5000 index account going forward to make sure that it continues to be managed to staff's expectations.

Manager Commentary
CIC Asset Management, Inc.

Period Ending:	3/31/96	Returns	Qtr.	Year
Total Firm Assets Under Management	\$155 Million	Actual	7.4%	34.7%
Total Firm Assets Managed in this Discipline	\$155 Million	Benchmark	6.8%	31.9%

1. ***Past Performance.** Summarize your performance over the last quarter and year. Specifically, what active bets did you make relative to your benchmark? Which of these bets worked/did not work and why?*

CIC's performance in the first quarter was 7.48% versus 6.83% for the benchmark return. For the last one year CIC returned 34.85% versus 31.87% for the benchmark. CIC's strong performance came primarily from our large overweighting in consumer cyclical stocks which were up 9.6% as a sector. We also benefited from our continued heavy exposure to financial stocks which were up 8.7% for the quarter (21.04% absolute weight). On the negative side, we were hurt by our underweighting in basic industries which were up 12% for the quarter and were the best performing sector of the market. We had particularly strong performance from Sears (25.63%), Allied Signal Inc. (24.99%), Beneficial Corporation (24.71%), Dover (24.47%), and IBM (22.02%).

Portfolio Construction Table: Industry exposure and cash holdings changed as follows:

Sector	Russell Value	Portfolio	Portfolio
	3/31/96	12/31/95	3/31/96
Consumer Cyclicals	8.30%	15.73%	14.86%
Consumer Non-Durables	7.79	14.82	7.75
Technology	4.60	7.33	8.42
Energy	13.01	12.43	9.49
Basic Industries	11.95	7.30	10.45
Cap. Goods Industries	8.21	5.78	6.55
Utilities & Telephones	20.13	13.37	14.06
Financial Services	26.00	20.87	24.08
Cash	0.0	2.37	4.32
TOTAL	100.00%	100.00%	100.00%

CIC Asset Management (con't)

2. *Future Strategy. What active bets are in place at the present time relative to your benchmark? Summarize the rationale for making these active bets.*

We hold 24.08% of our portfolio in financial stocks and remain overweighted in consumer cyclicals. As it appears that the economy is improving, we have increased our basic industry weight and will continue to increase the weight as we find good ideas. We significantly reduced our weighting in consumer nondurables; and in the second quarter have lowered it further. All of these decisions are driven by our valuation model.

3. *Organizational Issues. Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.*

CIC received two new accounts during the quarter; The Plaza de la Raza Endowment Trust, and the United Farm Workers of America (AFL-CIO).

4. *Other Comments. Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.*

None.

Staff Comments

No comments at this time.

Manager Commentary
Cohen, Klingenstein & Marks Incorporated

Period Ending:	3/31/96	Returns	Qtr.	Year
Total Firm Assets Under Management	\$352.5 Million	Actual	8.6%	32.7%
Total Firm Assets Managed in this Discipline	\$352.5 Million	Benchmark	6.5%	30.3%

1. *Past Performance. Summarize your performance over the last quarter and year. Specifically, what active bets did you make relative to your benchmark? Which of these bets worked/did not work and why?*

The account increased by 8.6% (net) during the first quarter of 1996 which compares to a 6.6% gain for the benchmark. Broadly speaking, the account remained aggressive (in the context of the generally conservative large capitalization stocks that we purchase). Relative to the benchmark, we have been overweighted in Interest-Rate Sensitive stocks (reflecting a belief that rates would decline), and underweighted in Cyclical stocks (though somewhat overweighted relative to the S&P 500). This was true for the entire past twelve months as we did not meaningfully reposition the portfolio over this period. Since Interest-Rate Sensitive stocks outperformed over the past 12 months while Cyclical underperformed, Minnesota's portfolio beat the benchmark by a significant margin. (In the first quarter of 1996, however, this pattern was a bit different - Cyclical improved - and so Minnesota's edge versus the benchmark narrowed a bit). And there were other, industry/company specific reasons for the differential as well: The benchmark has more stocks from Basic Industries (which performed particularly poorly over the last 12 months) which further contributed to Minnesota's edge (again, this pattern was reversed some in the first quarter). Additionally, while the benchmark and Minnesota had similar weightings in Growth stocks (and similar weightings among Growth industries), Minnesota's better stock selection provide some of the edge. On the other hand, stock selection in the Stable sector worked to Minnesota's disadvantage.

2. *Future Strategy. What active bets are in place at the present time relative to your benchmark? Summarize the rationale for making these active bets.*

We believe that the market is fairly valued based on consensus profit and interest rate expectations. This is a change: heretofore we had been arguing that the market was undervalued. On the other hand, we believe that the consensus is too pessimistic on both rates (which we expect to fall) and profits so that we think the market can rise from current levels. Given our optimism (both near and long-term), and our belief that rates will decline some, the portfolio remains "Growthy," with above-market (i.e., above S&P 500) exposure to Interest-rate Sensitive and Cyclical stocks. On the other hand, relative to the benchmark we are underweighted in Cyclical. We sold only one position last quarter: USF&G was replaced with a credit card processor, First USA.

Cohen, Klingenstein & Marks (con't)

3. **Organizational Issues.** *Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.*

We hired one non-investment employee last quarter. Her responsibilities are administrative and involve portfolio accounting, client service, record keeping, secretarial and such - an all purpose back-up.

Accounts Gained

Accounts Lost

Two

One

Excludes additions (withdrawals) to (from) existing accounts.

4. **Other Comments.** *Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.*

None.

Staff Comments

No comments at this time.

Manager Commentary
Compass Capital Management, Inc.

Period Ending:	3/31/96	Returns	Qtr.	Year
Total Firm Assets Under Management	\$230 Million	Actual	7.5%	27.4%
Total Firm Assets Managed in this Discipline	\$118 Million	Benchmark	8.1%	29.1%

1. **Past Performance.** Summarize your performance over the last quarter and year. Specifically, what active bets did you make relative to your benchmark? Which of these bets worked/did not work and why?

Again, the primary driver of investment performance during the past three and twelve month periods, was being fully invested. Since the inception of the relationship, a very small cash position has been held. This has added to investment performance greatly.

Sectors	QUARTER		YEAR	
	Active Bets	Value Added	Active Bets	Value Added
Technology	Underweighted	Worked	Underweighted	Worked
Consumer				
Non-Durables	Equal	Did Not Work	Overweighted	Did Not Work
Consumer Durables	Overweighted	Flat	Overweighted	Did Not Work
Capital Goods	Equal	Flat	Underweighted	Flat
Financial	Underweighted	Flat	Equal	Worked
Basic Industries	Overweighted	Worked	Overweighted	Flat
Transportation	Equal	Flat	Underweighted	Flat
Miscellaneous	Underweighted	Flat	Underweighted	Flat
Energy	No Position	No Bnmk. Position	No Position	No Bnmk. Position
Utilities	No Position	No Bnmk. Position	Underweighted	Flat

Quarter

The Consumer Non-Durable sector was the primary sector that lead to negative value added during the quarter. Nine out of twelve stocks in this sector underperformed. Underperformance by two publishing stocks on poor earnings announcements, a correction in valuation by two drug stocks, and continued weakness in retailing contributed to this negative value added. However, the Technology sector added positively to performance.

Year

Both the Consumer Non-Durable and Consumer Durable sectors contributed to negative value added during the past twelve months. The main culprits were lack of consumer spending and fierce competition. However, individual stock selection in the Technology sector added greatly to performance.

Compass Capital Management (con't)

2. *Future Strategy. What active bets are in place at the present time relative to your benchmark? Summarize the rationale for making these active bets.*

The largest overweighted active bets vs. the benchmark are within the Consumer Durables and Basic Materials sectors. The largest underweighted active bet to the benchmark is Technology.

Compass Capital is a growth stock manager with a strong emphasis on value. Therefore, with the high valuation currently carried by the Technology sector, one would expect an underweighting in this sector.

The opposite would apply for Consumer Durables. With consumer spending tight and with strong competition, the valuations of these stocks look attractive. Compass is a bottoms up stock selector.

3. *Organizational Issues. Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.*

No significant ownership or personnel changes during the quarter.

Two small endowments lost.

No new accounts

4. *Other Comments. Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.*

The customized benchmark has been completed by Richards & Tierney.

Staff Comments

No comments at this time.

Manager Commentary
Kennedy Capital Management

Period Ending:	3/31/96	Returns	Qtr.	Year
Total Firm Assets Under Management	\$1,475 Million	Actual	9.5%	32.8%
Total Firm Assets Managed in this Discipline	\$ 487 Million	Benchmark	7.2%	29.2%

1. *Past Performance. Summarize your performance over the last quarter and year. Specifically, what active bets did you make relative to your benchmark? Which of these bets worked/did not work and why?*

By buying unrecognized stocks, KCM tends to be a value oriented investor and we generally are not in the "growth" sectors, e.g., we had few tech stocks in early 1995. The first quarter of 1996 was a less focused market and KCM did well. No one sector or theme dominated the returns although we were helped by some of the "IPO orphans we adopted."

2. *Future Strategy. What active bets are in place at the present time relative to your benchmark? Summarize the rationale for making these active bets.*

KCM will continue to buy small stocks that are not followed by analysts and which have low institutional ownership. Portfolio characteristics will continue to show a value tilt. See below:

	3/31/96	12/31/95	12/31/95
	Minnesota	Ru 2000	Ru 2000 Value
Trailing P/E	15.3	22.7	17.7
Price/Book	2.1	2.4	1.7
Yield	2.0%	1.5%	2.4%

Kennedy Capital Management (con't)

- 3. *Organizational Issues.*** Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.

No significant organizational changes. No accounts closed or opened.

- 4. *Other Comments.*** Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.

Staff Comments

No comments at this time.

Manager Commentary
New Amsterdam Partners L.P.

Period Ending:	3/31/96	Returns	Qtr.	Year
Total Firm Assets Under Management	\$290 Million	Actual	8.1%	28.6%
Total Firm Assets Managed in this Discipline	\$270 Million	Benchmark	5.4%	25.7%

1. *Past Performance. Summarize your performance over the last quarter and year. Specifically, what active bets did you make relative to your benchmark? Which of these bets worked/did not work and why?*

In the quarter ended March 31, 1996 the return on the portfolio was 8.1%. This compares with 5.4% for the S&P 500 Index, 6.2% for the S&P MidCap, 4.9% for the Russell 3000, 4.7% for the NASDAQ index and 5.4% for our customized benchmark. For the last twelve months your portfolio returned 28.6% compared with 25.7% for its benchmark.

Our core strategy remains the same: we use a valuation model to identify stocks with better than average forecast long-term growth and profitability selling at market or below-market multiples. Here are the characteristics of the portfolio as of March 31, 1996:

	Minnesota	S&P MidCap	S&P 500
Expected Return	14.6%	11.5%	9.0%
P/E	20.9x	21.4x	18.9x
Price to Book	4.2x	4.4x	3.6x
Yield	1.3%	1.8%	2.2%
Growth	11.1%	11.1%	6.8%
Return on Equity	22.2%	15.0%	16.9%
Wtd Avg Mkt Cap	\$12.7bn	\$2.2bn	\$32.5bn

This quarter, medium capitalization stocks did slightly better than large capitalization stocks, but aside of that, no broad factors dominated the market. The Russell Value and Growth indexes, for instance produced similar returns. Our returns were attributable to solid stock picking ability and fair to good sector selection.

Retail Trade stocks reversed their trend of the last two years, to become the best performing sector, and our overweighting in that area helped our results. Our retail stocks, in aggregate, were up +16.9%. At the same time we were underweighted in Technology stocks and Utility stocks which were among the worst performing sectors.

Within sectors, our stock selection skill appeared to be good. In particular, our Health Services, Energy Minerals, Commercial Services and Finance picks did well, relative to their peers. The areas in which we had problems were technology related and Basic Industry companies. Fortunately, however, we were underweighted in those areas.

The best performing individual securities included Green Tree Financial (+33.0%), Health Management (+32.4%), Lands' End (+28.4%), Cray Research (+27.6%) and Diamond Shamrock (+26.2%). Our worst performing securities included Cabletron (-18.2%) and Zebra Technologies (-11.1%), both of which suffered in the technology stock fall this quarter. Great Lakes Chemical (-6.3%) and Merck (-4.6%) gave back some of their earlier gains. We

New Amsterdam Partners (con't)

remain, however, committed to all of those names, believing them to represent good investment value.

- 2. *Future Strategy.*** *What active bets are in place at the present time relative to your benchmark? Summarize the rationale for making these active bets.*

We continue to maintain an overweighting in consumer and finance stocks which appear to be cheap on our model. We are underweighted in the utility area, the energy sector and capital goods and basic industry stocks. We remain fully invested in the account and continue to stick to our investment discipline which looks for companies with superior profitability and forecast growth, selling at reasonable multiples.

- 3. *Organizational Issues.*** *Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.*

There were no organizational or personnel changes in the last quarter. No accounts were gained or lost in this discipline.

- 4. *Other Comments.*** *Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.*

We remain cautiously bullish on the equity markets in 1996, despite their strong start. Our forecasts still call for a drop in interest rates, moderate GDP growth and low inflation. Although corporate profit growth in 1996 may be anemic, we believe that long run corporate profits will grow around 7% per year. This scenario, in our view, bodes well for stocks.

Staff Comments

No comments at this time.

Manager Commentary
Valenzuela Capital Management, Inc.

Period Ending:	3/31/96	Returns	Qtr.	Year
Total Firm Assets Under Management	\$881 Million	Actual	7.4%	27.5%
Total Firm Assets Managed in this Discipline	\$881 Million	Benchmark	6.8%	28.7%

- 1. Past Performance.** *Summarize your performance over the last quarter and year. Specifically, what active bets did you make relative to your benchmark? Which of these bets worked/did not work and why*

Under our "bottom up" style, each stock pick is an active bet. Gains were made throughout the portfolio, with the largest contribution to performance stemming from Consolidated Stores (adding 1.20%), whose significant acquisition is accretive to earnings, Perkin Elmer (1.18%), where a restructuring is setting the stage for significant future earnings, and W.R. Grace (0.68%), benefiting from the announced spin-off of a major subsidiary. Performance was adversely affected by Rite Aid (costing 0.32%), due to a delay in the FTC's review of the Revco acquisition, and Xerox (0.28%) and H&R Block (0.30%), where there is no change in the two companies' fundamentals but the stocks were affected by a market correction for their respective businesses. For the twelve months, the most significant gains stem from Student Loan Marketing Association (contributing 3.32%), benefiting from a shareholder oriented restructuring and acceleration of earnings growth, Perkin Elmer (1.98%), and McDonnell Douglas (1.94%), as a result of restructuring, an improved commercial aircraft market and merger expectations. The poorest performers for the period were Kmart (costing 1.33%), due to concern about deterioration in the company's financial liquidity, H&R Block (0.46%), and Temple-Inland (0.28%), where a slowing economy impacted earnings.

- 2. Future Strategy.** *What active bets are in place at the present time relative to our benchmark? Summarize the rationale for making these active bets.*

Valenzuela Capital's investment philosophy is one of "risk-averse growth." We believe that growth in earnings and cash flow fuel price appreciation and that high price-to-earnings ratios cause volatility and risk. Hence, we try to sell higher P/E stocks and buy stocks in companies whose earnings will grow but whose P/E's are at or below the market. The portfolio was slightly realigned during the quarter. We added to positions we felt still represented good value and trimmed others, largely for reasons of valuation. New investments were initiated in Foundation Health, M.A. Hanna, Leggett & Platt, Lydall, MacFrugal's Bargains, Melville, Morgan Stanley, Standard Register Company and Tosco. Realized gains were taken in ACE, Air Products & Chemicals, General Re, McCormick, and Revco. Also sold were Crompton & Knowles, facing a deteriorating earnings outlook, Manpower, due to the changing earnings outlook in Europe, and Sensormatic Electronics, where significant slowing of revenue growth is impacting earnings.

Valenzuela Capital (con't)

3. *Organizational Issues.* Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.

Donald M. Krueger, CFA, joined Valenzuela Capital Management as a shareholder, member of the Board of Directors and Executive Committee. Mr. Krueger has a background in international emerging markets and will contribute his global perspective to the firm's investment process. In time, Mr. Krueger will establish a new international effort for the firm.. SBI staff has been provided with full background on Mr. Krueger.

4. *Other Comments.* Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.

For the sixth straight quarter, the equity markets have recorded strong gains. The total gain is now about 45% since the beginning of 1995. Valuations at this juncture are quite rich. Mid-capitalization stocks outperformed large-capitalization issues after a two-year stretch of lagging noticeably. Because we concentrate our portfolios in the mid-cap area, this shift is important. The economy was lethargic in the early going, but showed signs of improvement as the quarter ended. The recent uptick has caused interest rates to rise somewhat this year. It is too early to see if this will shut down the incipient recovery, but it does impede further improvement in equity valuations. More than ever, we feel that it is important to be invested in those companies who are delivering solid earnings and whose valuations are reasonable.

Staff Comments

No comments at this time.

Manager Commentary
Wilke/Thompson Capital Management

Period Ending:	3/31/96	Returns	Qtr.	Year
Total Firm Assets Under Management	\$1,371 Billion	Actual	3.4%	31.0%
Total Firm Assets Managed in this Discipline	\$ 724 Million	Benchmark	6.7%	29.6%

1. *Past Performance. Summarize your performance over the last quarter and year. Specifically, what active bets did you make relative to your benchmark? Which of these bets worked/did not work and why?*

The equity markets weathered a rocky beginning to 1996 with excessive volatility, including a 171 point decline in the Dow Jones Industrial Average, to post impressive gains for the quarter. Large cap issues outperformed their small cap counterparts for the period. Large cap stocks in particular, and the overall equity markets in general, benefited from the enormous amount of cash that has flowed into equity mutual funds in the first quarter and for the last twelve months.

Although the strong performance has carried over from 1995, where that performance has been derived has changed. Retail stocks, which were some of the worst performers in 1995, have rebounded in the first quarter. The perceived strength in the economy and easier annual sales comparisons have propelled retail issues. Conversely, software stocks, which experienced phenomenal returns over the past twelve months, have lagged the market on fears of slower personal computer sales. Additionally, some of the larger Minnesota State Board of Investment holdings had minor corrections in the quarter.

2. *Future Strategy. What active bets are in place at the present time relative to your benchmark? Summarize the rationale for making these active bets.*

We remain positive with regard to the equity markets despite the recent strong gains. Even though treasury yields rose significantly in the first quarter, the stock market remains the most attractive investment vehicle for investors. While the level of first quarter money flows into equity stock funds is unsustainable, heavy investments will still be made into equity funds. The economy is not performing well enough to justify further interest rate hikes by the Fed and inflation still is showing no signs of renewal, which bodes well for the stock market. Volatility will still play a prominent role in the equity markets, but with the strong overall environment for equities, investors should remain fully invested in the equity markets. We continue to invest in companies with good unit growth, that provide proprietary products/services or dominate their market, and that in turn have the ability to control their pricing.

Wilke/Thompson Capital (con't)

3. *Organizational Issues.* Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.

Wilke/Thompson Capital Management had no ownership or personnel changes last quarter.

Wilke/Thompson Capital Management is presently closed to new account relationships in our Small Cap Growth product and is only accepting additional contribution from existing clients. We did not lose any clients during the first quarter.

4. *Other Comments.* Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.

Wilke/Thompson looks forward to continuing to serve the Minnesota State Board of investment as its money manager.

Staff Comments

No comments at this time.

Manager Commentary
Winslow Capital Management, Inc.

Period Ending:	3/31/96	Returns	Qtr.	Year
Total Firm Assets Under Management	\$820 Million	Actual	6.0%	23.0%
Total Firm Assets Managed in this Discipline	\$443 Million	Benchmark	6.4%	29.0%

1. *Past Performance. Summarize your performance over the last quarter and year. Specifically, what active bets did you make relative to your benchmark? Which of these bets worked/did not work and why?*

In the quarter ending March 31, 1996 the Minnesota State Board of Investment account appreciated 6.01% net of fees. Both the Russell 1000 Growth and the S&P 500 experienced returns of 5.37% during the first quarter. The performance of the SBI account over the last twelve months shows an increase of 22.97% net of fees versus 31.97% for the Russell 1000 Growth and 32.11% for the S&P 500.

The SBI's Large Cap growth portfolio continues to be overweighted in technology, telecommunications and consumer services/specialty retail. We also maintain a slight overweighting in the healthcare sector versus our benchmark. The investment process we follow is a fundamental "bottom up" approach that leads us to companies that exhibit strong earnings growth. In the most recent quarter, the average reported earnings gain for the companies in your portfolio was 27%. We continue to believe these companies have outstanding potential because they meet our strict criteria of high earnings growth at attractive valuations.

The slight underperformance Winslow Capital experienced during the first quarter can be attributed to our current sector weightings versus our benchmark "normal" portfolio. Our overweighting in healthcare companies detracted from the overall performance of the portfolio due to the relative underperformance of the sector. Although your portfolios' technology holdings appreciated strongly for the three months ending March 31, 1996, Winslow Capital was underweighted versus the benchmark. Our exposure to specialty retail/consumer services was additive during the quarter. For the last twelve months, two factors had a measurable impact on performance. First, many of the strongest performing securities over this time period were financial service companies and large stable growth (9-12% annually) companies, benefiting from the decline in interest rates and the fear of recession. Our investment philosophy precludes us from owning these slower growth stocks. While these companies experienced 50 - 60% appreciation, they achieved earnings growth of less than 13% annually. Our investment strategy maintains a *minimum* future earnings growth rate hurdle of 14%. The second factor affecting the most recent twelve months of performance was the markets bias to the largest companies. Typically your portfolio has a average weighted market capitalization that is 20 - 25% smaller than the index because companies in that capitalization range are generally faster growing. We believe that the consistent implementation of our earnings growth philosophy will produce favorable long-term results as it has in the past.

Winslow Capital (con't)

2. *Future Strategy. What active bets are in place at the present time relative to your benchmark? Summarize the rationale for making these active bets.*

In our opinion, the sectors that are likely to exhibit the best earnings growth over the next two to three years will be technology, specialty retail/consumer services, healthcare and telecommunications. Winslow Capital is overweighted in these sectors because on fundamental, "bottom-up" analysis we have identified specific companies within the aforementioned sectors that are poised to achieve strong future earnings growth. Notwithstanding the portfolio gain in the last year, we are constructive that on an absolute and a relative basis, P/E ratios remain attractive. The portfolio is currently forecasted to achieve earnings growth of 24% through 1997, while selling at only 17 times our 1997 estimates.

3. *Organizational Issues. Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.*

Winslow Capital has recently been retained by two new clients. Cox Enterprises in Atlanta has hired our firm to manage a \$55 million large Cap Growth portfolio and the Dole Food Company in Los Angeles has hired us to manage a \$30 million portfolio in the Small Company Growth style.

4. *Other Comments. Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.*

None.

Staff Comments

No comments at this time.

**Manager Commentary
Zevenbergen Capital, Inc.**

Period Ending:	3/31/96	Returns	Qtr.	Year
Total Firm Assets Under Management	\$350 Million	Actual	5.8%	29.3%
Total Firm Assets Managed in this Discipline	\$350 Million	Benchmark	5.3%	27.0%

1. ***Past Performance.** Summarize your performance over the last quarter and year. Specifically, what active bets did you make relative to your benchmark? Which of these bets worked/did not work and why?*

The Minnesota State Board of Investment account continued on 1995's positive course for first quarter of 1996 with a 5.8% return, versus the custom benchmark gain of 5.3%. The primary outperforming sectors included financial services, producer durables and technology with 17.7%, 10.5% and 7.0% returns, respectively. The lagging sectors for the quarter included telecommunications services and healthcare. Healthcare took a respite from last year's stellar rise, while the telecommunications sector sorted out the new telecommunications bill and it's accompanying ramifications.

For the year ending March 31, 1996, the MSBI account outperformed the custom benchmark in all sectors, with the exception of energy/materials and telecom services. Historically, ZCI (and other growth managers) has underweighted the energy sector. Rising oil prices throughout the year have been the driver to performance in this sector, which in our view is not a secular trend. The telecom services sector underperformed the benchmark, due to the telecom equipment providers pushing out Personal Communications System orders until the latter-half of 1996 and early 1997.

ZCI's original research on telecommunications and technology stocks led us to take early positions in Loral, Hughes Electronics and Rockwell International, companies at the forefront of technological advances being used in other industries. As these organizations continue to shed lackluster businesses, spin-off high growth product lines and consolidate to generate efficiencies, we expect the market will recognize their superior prospects and value them at higher levels, similar to technology stocks.

2. ***Future Strategy.** What active bets are in place at the present time relative to your benchmark? Summarize the rationale for making these active bets.*

Although it appears that ZCI weights all sectors similar to the custom benchmark, it is important to point out the significant differences of investments within the sectors. Software and services are among the issues which ZCI overweights in the technology sector in comparison to the custom benchmark. Technologies which are difficult to differentiate or do not have a significant market niche or market share are not considered long term investment candidates. ZCI's healthcare sector has a significant overweighting in the biotechnology area, where superior product pipelines create greater growth opportunities. In the consumer discretionary group, entertainment and services are heavily weighted, whereas retail is underweighted in contrast with the custom benchmark. We believe the retail environment cannot sustain growth in it's current, highly competitive environment. Pricing flexibility is key to future growth in the retail industry, a factor which has been absent since 1993.

Zevenbergen Capital (con't)

ZCI has, through our fundamental research, uncovered new growth opportunities in areas other than the large-capitalization arena. We believe the market has also begun to focus on other cap ranges for growth opportunities, as 1995 generated most of the S&P 500 return from large-cap issues. Premium prices-relative-to-growth rates for larger-cap companies led us to invest in new growth equity issues within other cap ranges at more attractive valuations.

New portfolio issues in the small-to-mid-cap area include APAC Teleservices (marketing and customer service by telephone) and First USA Paymentech (merchant processing).

3. *Organizational Issues.* Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.

There were no personnel issues to report for the first quarter of 1996.

4. *Other Comments.* Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.

None.

Staff Comments

No comments at this time.

Manager Commentary
BEA Associates

Period Ending:	3/31/96	Returns	Qtr.	Year
Total Firm Assets Under Management	\$24.5 Billion	Actual	-1.3%	10.7%
Total Firm Assets Managed in this Discipline	\$ 4.0 Billion	Benchmark	-1.8%	10.8%

1. ***Past Performance.** Summarize your performance over the last quarter and year. Specifically, what active bets did you make relative to your benchmark? Which of these bets worked/did not work and why?*

The performance for the first quarter of 1996 was -1.22% gross of fees versus the Lehman Aggregate index return of -1.78%. The 56 basis points of outperformance came from a variety of sources with volatility trades adding approximately 40 basis points and with mortgages and high yield adding 16 basis points to the fixed income portfolio.

As BEA had expected, dollar/yen volatility continued to decline and the related decline in option premium benefited the portfolio given our short volatility position. After the recent dollar appreciation, the markets now believe the dollar to be fairly valued and do not have a strong conviction as to the next move.

A sharp turn in treasury sentiment created several opportunities during the first quarter. The market had been discounting several more Fed rate cuts and the possibility of a recession. While these drastic fluctuations did not impact our duration decision, as we stay close to the index, they impacted the currency, mortgage and corporate sectors. The incremental returns generated from the cash position came from successful sector rotation in the mortgage backed portion of the portfolio and modest gains from the municipal bond arbitrage. Perpetual floating rate bank notes also outperformed because of rising short-term rates and the debt buyback programs that are finally taking hold in European banks.

2. ***Future Strategy.** What active bets are in place at the present time relative to your benchmark? Summarize the rationale for making these active bets.*

In the coming quarters, we will realize the gains from the short volatility trades and the municipal bond positions. Our security selection will continue to focus on deleveraging stories (airlines, cables, and banks) in light of the fact that generic corporate bonds appear fully valued. The utility bond sector provides several opportunities, as the winners and losers in the trend toward national competition becomes more apparent. While we continue to be underweighted in utilities, we do favor select, higher yielding companies that have discounted the downside of deregulation.

The mortgage overweight of approximately 10% should continue to generate excess returns in the second quarter as managers increase their allocation to this historically cheap sector and interest rate volatility declines.

BEA Associates (con't)

3. *Organizational Issues. Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.*

On April 1, 1996 BEA announced that it will be integrating Credit Suisse Investment Management. The integration will broaden the range of products BEA can offer our current and future clients, in addition to expanding upon our Global Fixed Income expertise, as approximately \$23 billion* is in Global/International Fixed Income.

*as of December 31, 1995

4. *Other Comments. Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.*

None.

Staff Comments

BEA began to add below investment grade securities to the portfolio during 1996. Below investment grade securities added approximately 5 basis points to the portfolio during the quarter.

Manager Commentary
Investment Advisers, Inc.

Period Ending:	3/31/96	Returns	Qtr.	Year
Total Firm Assets Under Management	\$15.0 Billion	Actual	-2.0%	9.2%
Total Firm Assets Managed in this Discipline	\$ 4.5 Million	Benchmark	-1.8%	10.8%

1. ***Past Performance.** Summarize your performance over the last quarter and year. Specifically, what active bets did you make relative to your benchmark? Which of these bets worked/did not work and why?*

The portfolio underperformed the benchmark during the first quarter of 1996. ABS holdings and BBB-rated corporate holdings enhanced portfolio returns; yield curve positioning detracted from portfolio performance. Our more positively convex MBS holdings lagged negatively convex MBS in the first quarter market selloff. The portfolio underperformed its benchmark for the trailing 12-month period due to a defensive duration stance in the second quarter of 1995.

2. ***Future Strategy.** What active bets are in place at the present time relative to your benchmark? Summarize the rationale for making these active bets.*

Relative to the benchmark, the portfolio is currently duration-neutral. Structurally, the portfolio is overweighted in intermediate-maturity bonds in anticipation of a steepening of the yield curve. With regard to sector weightings, the portfolio is overweighted in ABS, underweighted in Federal agencies, and neutrally weighted in Treasuries, MBS, and corporates. The portfolio is overweighted in Baa-rated corporates and has a positive convexity in its MBS positions.

Our rationale for these active bets is based on several factors. First, the Fed is now in a stable policy mode and is not likely to continue its mid-cycle easing unless the economy weakens significantly. Second, cyclical inflation pressures are now beginning to overpower the positive secular forces for low inflation. A stable Fed combined with rising inflation fears should steepen the yield curve. Third, the economy will strengthen during 1996, allowing corporate profitability and cash flow to remain strong, biasing corporate credit spreads to narrow.

Investment Advisors, Inc. (con't)

3. *Organizational Issues. Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.*

In December of 1995, IAI's owner, TSB merged with Lloyds Bank to form Lloyds TSB Group plc, a publicly traded company in the U.K. IAI does not anticipate that the change in ownership of our parent company will have any effect on our activities.

IAI gained no fixed income accounts and lost four fixed income accounts with \$95.2mm in assets. In this discipline, IAI gained no accounts and lost no accounts.

4. *Other Comments. Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.*

None

Staff Comments

No comments at this time.

Manager Commentary
Miller, Anderson & Sherrerd

Period Ending:	3/31/96	Returns	Qtr.	Year
Total Firm Assets Under Management	\$35.7 Billion	Actual	-1.0%	11.9%
Total Firm Assets Managed in this Discipline	\$17.8 Billion	Benchmark	-1.8%	10.8%

1. **Past Performance.** *Summarize your performance over the last quarter and year. Specifically, what active bets did you make relative to your benchmark? Which of these bets worked/did not work and why?*

Over the last quarter, your portfolio has provided a return of (0.8)% (net of fees) versus a benchmark return of (1.8)%. Over the last twelve months, your portfolio has provided a 12.5% return (net of fees) versus a 10.8% return for its benchmark.

Interest rates increased during the first quarter and the yield curve steepened. We began the quarter with a duration or interest rate sensitivity about equal to that of your benchmark, corporates at 17% of the portfolio, a 10% currency hedged exposure to foreign bonds and mortgages at 62% of the portfolio, with the latter two sectors being overweighted relative to your benchmark.

During the first quarter, the yield curve anticipated additional easing by the Federal Reserve and intermediate securities appeared to be relatively expensive in comparison to longer maturity securities. We added to the duration of the portfolio as rates rose and moved the portfolio towards a barbell position by purchasing long maturity securities and reducing your portfolio's exposure to short and intermediate maturity securities. During the quarter, the duration and yield curve decisions added value, the mortgage holdings were modestly positive, and the corporate and foreign holdings added to returns.

Over the last year, the duration, yield curve, corporate and foreign holdings added to your returns, while the overweighting in mortgage securities detracted.

2. **Future Strategy.** *What active bets are in place at the present time relative to your benchmark? Summarize the rationale for making these active bets.*

Interest rates have risen to levels such that the value within the fixed income market place, as measured by real interest rates and the shape of the yield curve, is above average. We continue to add to the duration or interest rate sensitivity of the portfolio such that the duration is about half a year longer than your index. In addition, yields on foreign fixed income securities have fallen while U.S. rates have risen. Consequently, we have begun to reduce the foreign holdings within your portfolio. Corporate securities remain attractive and we continue to add to our medium and lower quality holdings.

Mortgage securities are cheap on an option-adjusted yield basis, and we have maintained mortgages at 62% of the portfolio.

Miller, Anderson & Sherrerd (con't)

Because of the reshaping of the yield curve, we have reduced the barbell exposure within the portfolio such that your overall yield curve exposure is relatively close to that of your benchmark.

3. *Organizational Issues. Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.*

During the first quarter, the credit team from Morgan Stanley Asset management joined the Miller, Anderson & Sherrerd fixed income team in Conshohocken. The addition of three experienced professionals will allow us to expand our credit research and increase our ability to add value to our client portfolios.

During the quarter, we lost one investment professional to retirement and hired one.

We gained two fixed income accounts during the quarter and lost one account, not due to poor performance, but because Morgan Stanley Asset management had a fiduciary role for that client.

4. *Other Comments. Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.*

None

Staff Comments

Miller began to add below investment grade securities to the portfolio during 1996. The addition of below investment grade bonds had a positive impact on first quarter results.

Staff visited Miller's offices in July 1995. The review conducted at that time did not raise any particular concerns.

Manager Commentary
Standish, Ayer & Wood

Period Ending:	3/31/96	Returns	Qtr.	Year
Total Firm Assets Under Management	\$29.0 Billion	Actual	-1.5%	11.1%
Total Firm Assets Managed in this Discipline	\$11.5 Billion	Benchmark	-1.8%	10.8%

1. *Past Performance. Summarize your performance over the last quarter and year. Specifically, what active bets did you make relative to your benchmark? Which of these bets worked/did not work and why?*

First Quarter and Year Attribution (Rel. to Lehman Aggregate)

	1ST QUARTER	LAST 12 MONTHS
Duration	-.28	-.10
Yield Curve	.04	-.05
Domestic Sectors	.50	.86
Non-Dollar	.06	.11
Fees	-.05	-.20

- Corporate spreads tighter. Below investment grade begins to kick in.
- Overweighting in mortgages helps in first quarter.
- Non dollar very strong.

2. *Future Strategy. What active bets are in place at the present time relative to your benchmark? Summarize the rationale for making these active bets.*

<u>Sector</u>	<u>Weighting Strategy</u>	<u>Rationale</u>
Mortgages	Strong overweight	Spreads remain reasonably wide even after good relative performance.
Corporates	Reduced overweight	High grade industrial spreads very narrow. But newly allowed below investment grade better value.
International	Average weighting	Europe countries to look strong, rates declining.
Treasuries	Underweight	Sector offers no special value.

Standish (con't)

3. *Organizational Issues.* Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.

Personnel additions:	Robin Buhrer Andrew L. Beja	Market/Client Service Small Cap Analyst
Departures:	James W. Copley William Lupoletti Wilfred Talbot	Short Term Manager Short Term Manager International Bond Analyst
Accounts:	Gained 2 Pension Lost 1 State pension	\$120 Million \$306 Million

4. *Other Comments.* Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.

None

Staff Comments

Standish began to add below investment grade securities to the portfolio during 1996. During the first quarter, below investment grade securities added approximately 8 basis points to the SBI portfolio.

Manager Commentary
Western Asset Management

Period Ending:	3/31/96	Returns	Qtr.	Year
Total Firm Assets Under Management	\$20.1 Billion	Actual	-1.8%	12.2%
Total Firm Assets Managed in this Discipline	\$11.6 Billion	Benchmark	-1.8%	10.8%

1. *Past Performance.* Summarize your performance over the last quarter and year. Specifically, what active bets did you make relative to your benchmark? Which of these bets worked/did not work and why?

Market-level performance in the first quarter as the product of mixed results for major portfolio strategies. Sharply higher interest rates were the major negative factor, since the portfolio's duration was longer than its benchmark throughout the quarter. This was offset, however, by the positive impact of a flatter yield curve on the portfolio's barbell exposure to maturities, particularly at the long end of the yield curve, and by the portfolio's overweight exposure to both corporate and mortgage-backed securities, since a narrowing of spreads in both sectors led to positive performance.

Outperformance over the past year remains substantial, however, due primarily to the success of all major portfolio strategies. The portfolio held a long duration posture throughout the year, and this contributed to returns since interest rates are on balance lower than they were a year ago. Yield curve positioning has contributed to overall results, since the portfolio has held a barbell exposure for most of the past year and the yield curve has flattened. Mortgage underweighting in the latter part of last year was a positive as mortgages trailed other sectors, and moving to an overweight position early this year was rewarded by strong relative performance in the mortgage sector. Corporate overexposure throughout the past year added importantly to returns, particularly the emphasis on the lower end of the investment quality scale, as these issues turned in very strong performances.

2. *Future Strategy.* What active bets are in place at the present time relative to your benchmark? Summarize the rationale for making these active bets.

With forward rates now calling for several Fed tightenings by year-end, we feel that yields are now sufficiently high relative to inflation fundamentals to warrant a more aggressive duration posture. We think the market's growth-phobia should be assuaged by summer, as the impact of higher rates once again takes a bite out of demand. This year's rise in interest rates is already working to dampen interest-sensitive demand, as evidenced by a 75% decline in mortgage refinancings since early February. Meanwhile, the manufacturing sector remains in the doldrums, business investment spending is flagging, and the inventory cycle has not yet run its course. Fears of an incipient wage and commodity price inflation are overdone, since pressure from unions and politicians to increase labor's share of the productivity gains of previous years will, assuming continued restraint on the part of the Fed, more likely cause a squeeze on margins and earnings than be passed on in the form of a general rise in the price level or result in a net stimulus to the economy. Recent increases in food and energy prices will similarly take a bite out of consumers' disposable income. Non-perishable commodity prices, meanwhile, remain quite stable.

Western Asset (con't)

We continue to hold a barbell exposure to maturities, though it is less aggressive now that the yield curve has flattened. Going forward, long-term rates should be marginally freer to follow Fed, which is very unlikely to lower rates near term, and to the economy, where a clear picture will not emerge for at least a month or two. Clearly, the bond market is magnifying even the slightest vibrations in economic activity, rather than focusing on the secular decline in inflation and the much-reduced volatility in inflation we have experienced in recent years. Eventually, financial market volatility should subside, as it becomes clear that the economy is not on an overheating track. This argues for reducing portfolio convexity, since high implied options volatility makes it quite expensive currently, primarily by maintaining an overweight exposure to the mortgage sector, with emphasis on discount coupons to minimize exposure to falling interest rates. With corporate spreads still relatively narrow, we will likely maintain a modest overweighting to the sector, with a view to paring back positions if spreads narrow even more.

3. *Organizational Issues. Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.*

Personnel Additions:

Joseph C. Carieri, Client service Executive

Accounts Gained:

Three

4. *Other Comments. Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.*

None.

Staff Comments

Western began adding below investment grade bonds during 1996. This strategy had a positive impact on performance during the quarter.

Manager Commentary
IDS Advisory (IDS Fixed-Income Advisors)

Period Ending:	3/31/96	Returns	Qtr.	Year
Total Firm Assets Under Management	\$27.1 Billion	Actual	-3.2%	11.5%
Total Firm Assets Managed in this Discipline	\$4.2 Billion	Benchmark	-1.8%	11.5%

1. ***Past Performance.** Summarize your performance over the last quarter and year. Specifically, what active bets did you make relative to your benchmark? Which of these bets worked/did not work and why?*

In the quarter ended March 29, 1996, investment performance on your portfolio registered a negative return of 3.2% compared with a negative return of 1.8% on the Lehman Brothers Aggregate Bond Index. For the twelve months ended March 29, 1996, your account returned +11.8% as compared to the +10.8% return of the Lehman Brothers Aggregate Bond Index. Investment performance was aided during the most recent quarter by high yield securities used in your account for the first time. The absolute return on high yield investments during the quarter was +2.41% which contributed a +0.13% return to the whole portfolio. A copy of the attribution analysis is attached.

The underperformance for the quarter and the overperformance for the past twelve months can, in the most part, be attributed to our maintenance of duration levels near those permitted by guidelines for most the period.

2. ***Future Strategy.** What active bets are in place at the present time relative to your benchmark? Summarize the rationale for making these active bets.*

While yield spreads between Investment Grade Corporate and Treasuries remain stubbornly narrow we will be moving closer to the 10% permitted on High-Yield securities by investment guidelines. We also intend to introduce a modest exposure to mortgage pass-throughs to the portfolio in the months ahead. Mortgage investments, while not one of our favorite investment vehicles, will allow us to increase portfolio yield more advantageously than corporate bonds at the present time.

IDS (con't)

3. **Organizational Issues.** Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.

We have added two portfolio managers during the last quarter as follows:

Adele Bruce	Continental Europe
Gavin Corr	United Kingdom

There have been no significant personnel departures during the last quarter.

Product	First Quarter 1996		Losses	
	Gains # of Accounts	Assets (\$MM)	# of Accounts	Assets (\$MM)
Large Cap Equities	3	203.0	1	68.9
Fixed Income	1	5.0	2*	296.2*
Balanced	4	110.9	0	0
International	0	0	0	0
Regional - Pacific	1	10.0	0	0
Global Ex-Australia	1	19.3	0	0
Latin America	0	0	0	0
Small Cap Equities	0	0	0	0
Mid Cap Equities	1	1.5	0	0
Research Core	0	0	0	0
Research Aggressive	5	86.1	0	0
Global Bonds	1	6.5	0	0
Structured Fixed Income	0	0	0	0

* Temporary Account Arrangement

4. **Other Comments.** Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.

None at this time.

Staff Comments

The IDS benchmark was revised from the Lehman Government Corporate Index to the Lehman Aggregate as of January 1, 1996.

Staff visited the manager during the quarter. There are no concerns at this time.

Manager Commentary
Goldman Sachs Asset Management

Period Ending:	3/31/96	Returns	Qtr.	Year
Total Firm Assets Under Management	\$50.9 Billion	Actual	-1.6%	11.0%
Total Firm Assets Managed in this Discipline	\$14.4 Billion	Benchmark	-1.8%	10.8%

1. *Past Performance. Summarize your performance over the last quarter and year. Specifically, what active bets did you make relative to your benchmark? Which of these bets worked/did not work and why?*

In the first quarter, the portfolio outperformed the Lehman Aggregate by 23 bps. This outperformance is due primarily to the corporate and mortgage sectors.

For the past 12 months, the mortgage sector detracted about 3 bps from incremental return due to prepayment fears caused by the rally in the Treasury market. In the first quarter, the mortgage sector added about 10 bps to incremental return, primarily due to spread tightening of the portfolio's collateral and CMO securities.

For the past 12 months, term structure detracted about 8 bps from incremental return due to the barbelled portfolio structure, and the portfolio's Treasury securities added approximately 4 bps to incremental return. Agencies added about 6 bps due to security selection. In the first quarter, the portfolio's Treasury securities added approximately 1 bp to incremental return.

For the past 12 months, the corporate sector added about 15 bps to incremental return primarily due to the outperformance of the portfolio's industrial and financial holdings. In the first quarter, the corporate sector added about 7 bps to incremental return, primarily due to spread tightening of the portfolio's industrial and financial securities and sector OAS advantage of the portfolio's industrial securities.

For the past 12 months, the emerging market sector added about 8 bps to incremental return. In the first quarter, the emerging market sector added about 4 bps to incremental return due to a combination of spread tightening and OAS advantage.

1Q96

Duration/Term Structure/Convexity	-3.7	Emerging Markets	3.8
Treasury	0.6	Mortgage	9.6
Agency	0.2	Municipal	0.0
Asset-Backed	1.6	Index Price Mismatch	1.1
Corporate	7.4	Residual	<u>2.3</u>
		Total	23.0

2. *Future Strategy. What active bets are in place at the present time relative to your benchmark? Summarize the rationale for making these active bets.*

The duration/term structure of the portfolio is targeted to that of the benchmark. In Agencies, the portfolio is slightly underweighted (2%) vs. the benchmark in favor of other higher-yielding spread sectors.

Goldman (con't)

30% allocation to the mortgage sector (1% overweighting). Neutral outlook due to recent tightening. Substantial overweight in discount coupons ($\leq 7.0\%$) due to recent cheapening. Overweight seasoned securities in the premium coupons (9.0% - 10.0%) although less so due to recent outperformance. Underweight newly issues premiums due to unattractive spreads relative to lower coupons. Continue to add CMOs when attractive relative to pass-throughs.

31% allocation to the corporate sector (14% overweighting). Our outlook for corporate spreads is cautiously optimistic due to continued economic growth. Current spreads are narrow but technicals remain positive due to heavy inflows into corporate and high yield mutual funds as well as cash coming from other fixed income sectors, notably mortgages. 11% allocation to asset-backed sector (10% overweighting), which should continue to benefit from strong investor demand for short-duration paper with incremental yield and low spread volatility.

4% allocation to the emerging market sector (4% overweighting). We continue to maintain a cautious approach regarding Republic of Columbia bonds due to near-term political risk. The Colombian economy continues to perform well and we are monitoring political developments closely. We continue to like CAF for the incremental spread that a 5-year BBB at 110 bps can provide. We added Panamco during 1Q96 based on its strong earnings record and the equity ownership by Coke.

3. *Organizational Issues.* Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.

There were no changes in the ownership of GSAM. There was one change to our U.S. fixed income portfolio management staff. Ted Sotir was promoted and has left the U.S. Fixed Income management team to join GSAM's London office as Resident Manager and Director of International Marketing.

U.S. Fixed Income Accounts Gained: 2	U.S. Fixed Income Accounts Lost: 4
U.S. Clients 2	U.S. Clients 2
Non-U.S. Clients 0	Non-U.S. Clients 2

Three non-pension accounts needed money for corporate purposes. One pension account changed asset allocation.

4. *Other Comments.* Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.

None

Staff Comments

No comments at this time.

Manager Commentary
Lincoln Capital Management Company

Period Ending:	3/31/96	Returns	Qtr.	Year
Total Firm Assets Under Management	\$39.1 Billion	Actual	-1.8%	10.6%
Total Firm Assets Managed in this Discipline	\$13.6 Billion	Benchmark	-1.8%	10.8%

1. *Past Performance.* Summarize your performance over the last quarter and year. Specifically, what active bets did you make relative to your benchmark? Which of these bets worked/did not work and why?

	1st Quarter 1996		12 Months Ended 3/31/96	
	<u>Active Strategy</u>	<u>Value Added</u>	<u>Active Strategy</u>	<u>Value Added</u>
Mortgages	Overweighted	+0.02%	Overweighted	-0.06%
Corporates	Neutral	0.00	Neutral	-0.02
BBBs	Neutral	0.00	Neutral	0.00
Asset-Backeds	Overweighted	0.00	Overweighted	+0.02
Agencies	Overweighted	0.00	Overweighted	0.00
Miscellaneous				
Rebalancing Transaction Cost	N/A	-0.01%	N/A	-0.04%
Security Selection	N/A	+0.01	N/A	+0.17
Less Fees		<u>-0.01</u>		<u>-0.04</u>
Total		+0.01%		+0.03%

On a net-of-fee basis, your portfolio outperformed the Lehman Brothers Aggregate Index by 1 basis point for the first quarter 1996 and 3 basis points for the 12-month period ending March 31, 1996.

For the one-year period, the value added from security selection was offset by the mortgage overweighting. For the better part of this period, mortgage spreads widened as lower rates raised expectations for refinancing, which limited price appreciation. Mortgage spreads remain close to 4-year wides, offering an attractive value added opportunity; hence our continued overweighting.

In the first quarter of 1996, the mortgage overweighting added value, allowing us to recapture a portion of the value lost in 1995. During this period, we halved our overweighting, and locked in the value added for the portion sold.

Lincoln (con't)

2. **Future Strategy.** *What active bets are in place at the present time relative to your benchmark? Summarize the rationale for making these active bets.*

Future Strategy	Strategy	Rationale
Government Trust Certificates Resolution Funding Corporation	Overweighted vs Treasuries	1. Government Guarantee 2. Attractive Yield 3. Certain Cash Flow
Asset-Backed	Overweighted vs Treasuries	1. High Quality 2. Attractive Yield 3. Low Event Risk 4. Low Prepayment Risk
Current Coupon Year Mortgages	Overweighted vs Treasuries	1. Agency Quality 2. Low Prepayment Risk 3. Wide Nominal Spreads

3. **Organizational Issues.** *Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.*

	Number	Market Value (\$ millions)
Accounts Gained	1	\$80
Accounts Lost	1	\$84

Pamela Allen, Vice President, joined Lincoln in March of 1996 as a fixed income portfolio manager/analyst.

Michael Pytosh, Vice President, joined Lincoln in February of 1996 as an equity portfolio manager/analyst.

4. **Other Comments.** *Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.*

There are no issues or developments that would impact the SBI account.

Staff Comments

No comments at this time.

Manager Commentary
Baring Investment Services

Period Ending:	3/31/96	Returns	Qtr.	Year
Total Firm Assets Under Management	\$12.0 Billion	Actual	3.7%	17.2%
Total Firm Assets Managed in this Discipline	\$ 2.3 Billion	Benchmark	2.9%	12.5%

1. *Past Performance. Summarize your performance over the last quarter and year. Specifically, what active bets did you make relative to your benchmark? Which of these bets worked/did not work and why?*

The following figures show a breakdown of the returns for the last quarter:

	Total Return	Currency	Market Weighting	Tracking Error
	%	%	%	%
Minnesota State Board	3.7	-1.8	5.5	0.0
MSCI EAFE Index	2.9	-2.4	5.4	---
Relative Return	0.8	0.6	0.1	0.0

Currency (Relative return 0.6%): The underweight yen exposure added significant value while overweighting the deutschemark detracted. The overweight Hong Kong dollar was beneficial as was exposure to non-index Korean won but very underweight Australian dollar position detracted.

Market Weighting (Relative return 0.1%): The exposure to the Hong Kong market added value as did the overweight position in France and the near zero exposure to poor performing Australia. Exposure to Korea detracted as did underexposure to the Swiss market.

Tracking Error (Relative return 0.0%): Positive tracking error from Thailand and Japan was offset by Hong Kong.

2. *Future Strategy. What active bets are in place at the present time relative to your benchmark? Summarize the rationale for making these active bets.*

The main features of your portfolio are:

Overweight: Japan, France, Hong Kong, Korea, Thailand and US Dollars

Underweight: Germany, UK, Yen and European currencies

Our outlook and policy has changed very little from the previous quarter. We remain overweight in Japan as we forecast both the economy and corporate profits to rebound over the coming twenty four months. The liquidity the Bank of Japan injected into the financial system has turned around both the economy and the stock market and prevented a collapse of the banking system. Further, it caused the much needed weakening of the Yen which will further boost corporate profits. We believe that Japan is in the first year of a four to five year profits recovery cycle which makes valuations look more attractive on a prospective basis. We continue to hedge your Yen exposure although we have reduced the size of the hedge as the dollar appreciated during the quarter.

Baring (con't)

Our focus in South East Asia is now solely on Hong Kong where we have a significant overweighting. Economic fundamentals are improving in China as the Chinese economy starts to emerge from its growth recession. Hong Kong is the prime beneficiary of any improvement in the mainland's fortunes. The Korean and Thai markets remain attractive because of compelling value and a recovery in profits growth.

Finally, our focus in Europe is shifting more towards the peripheral markets of France, Italy and Sweden which we believe will be the beneficiary of lower interest rates in Germany where the economy remains depressed. Our concern over the UK stock market is increasing as the country nears an election where the Labour Party is almost certain to be voted into power.

3. *Organizational Issues. Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.*

Peter Hartley, Chairman of Baring Asset Management, Inc. and member of the Strategic Policy Committee retired.

In the Active/Passive Discipline:

No accounts were gained or lost, however, existing clients contributed \$56 million in new funding during the first quarter.

4. *Other Comments.*

None.

Staff Comments

Peter Hartley took an early retirement. Staff met with Peter and other Barings members in March to discuss his pending retirement. Staff does not feel that Peter's departure will unduly affect the Strategic Policy Committee, but we will monitor this situation carefully.

Performance attribution relative to EAFE for the quarter is shown below:

	Jan. - Mar. 1996
Country selection*	0.07
Stock selection*	0.17
Currency effect	-0.12
Hedging activity	0.67
Total Value Added to EAFE	0.82

Source: State Street Analytics * in local currency

Manager Commentary
Brinson Partners, Inc.

Period Ending:	3/31/96	Returns	Qtr.	Year
Total Firm Assets Under Management	\$52.9 Billion	Actual	3.3%	25.0%
Total Firm Assets Managed in this Discipline	\$12.6 Billion	Benchmark	2.9%	12.5%

1. *Past Performance. Summarize your performance over the last quarter and year. Specifically, what active bets did you make relative to your benchmark? Which of these bets worked/did not work and why?*

The portfolio modestly outperformed the benchmark in the quarter, growing 3.3% in dollar-adjusted terms versus 2.9% for the MSCI EAFE unhedged Index, and significantly outperformed during the one-year period, earning 25.0% against a benchmark unhedged return of 12.5%. Market allocation was negative in both the fourth quarter and the full year. The portfolio was hurt in the quarter by underweights or lack of a position in several strong markets (Hong Kong, Japan and Switzerland), as well as overweights in the weak New Zealand and Australian markets. On the other hand, overweighting France and the Netherlands made a positive contribution. Strategic cash detracted from performance. The underweights of Japan, Hong Kong and Switzerland reduced full year returns, as did overweights in Australia and New Zealand, but the overweight in the Netherlands added to results. Strategic cash had a negative impact.

Currencies added considerable value both during the quarter and the year, playing a significant part in both periods' outperformance. The most important factor in both periods was the strategy of being underweight yen, as the latter continued to weaken in the first quarter and has declined over 23%* in the twelve month period. Other important positives for the quarter and the year have been the overweights of the dollar bloc currencies (U.S., Canada, Australia and NZ), all of which continued to strengthen during the quarter and the year, and overweights of several peripheral currencies.

* Decline represents the full currency effect, incorporating differences in short-term cash.

2. *Future Strategy. What active bets are in place at the present time relative to your benchmark? Summarize the rationale for making these active bets.*

There is a 5% strategic cash allocation, slightly higher than last quarter. This is based on our view that most non-U.S. equity markets are overvalued. The scale of the Japan underweight has been increased, as this market has been quite strong. Proceeds were used to raise cash and the All Other markets. Within the AO market, we have initiated a position in Finland and increased Malaysia, while scaling back on Canada and the U.K. Finland has been relatively weak, largely on the back of the underperformance of Nokia, which appears attractively priced. Current overweights are in the Netherlands, France, Belgium, Spain, New Zealand and Australia; underweights are held in Japan, Hong Kong and Switzerland. Several currency changes were made. The Canadian dollar was reduced in February, adding to the U.S. dollar. At the end of February, the yen allocation was raised 10%, reducing the scale of the underweight; this was funded from the U.S. dollar. The weakness of the yen and relative strength of the dollar has lessened the degree of comparative attractiveness of these two

Brinson (con't)

currencies. We continue to believe, however, that the U.S. dollar offers the most attractive return potential, while the yen and DM-bloc currencies, the portfolio's major underweights, remain overvalued.

3. *Organizational Issues.* Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.

There have been no significant organizational changes and no turnover of our senior investment professionals in this past quarter.

4. *Other Comments.* Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.

None this quarter.

Staff Comments

In February, Brinson received an additional allocation of \$100 million as part of the increased international allocation.

Performance attribution relative to EAFE for the quarter is shown below:

	Jan. - Mar. 1996
Country selection*	-0.46
Stock selection*	-0.82
Currency effect	0.44
Hedging activity	1.23

Total Value Added to EAFE 0.49

Source: State Street Analytics * in local currency

Manager Commentary
Marathon Asset Management

Period Ending:	3/31/96	Returns	Qtr.	Year
Total Firm Assets Under Management	\$4.9 Billion	Actual	4.4%	16.4%
Total Firm Assets Managed in this Discipline	\$3.1 Billion	Benchmark	2.9	12.5%

1. ***Past Performance.** Summarize your performance over the last quarter and year. Specifically, what active bets did you make relative to your benchmark? Which of these bets worked/did not work and why?*

The Fund outperformed in the first quarter of 1996, rising 4.4% versus a 2.9% rise in the MSCI EAFE Index. Outperformance was primarily due to the strong rebound seen in economically sensitive sectors in Continental Europe and high stock returns in the U.K. Changes in country allocation over the quarter largely reflected relative market movements with the increase in cash (from 2.8% to 5.1%) a result of incremental funding during the quarter.

2. ***Future Strategy.** What active bets are in place at the present time relative to your benchmark? Summarize the rationale for making these active bets.*

Holdings in Europe remained largely unchanged from a sectoral bias but the geographical shift towards hard currency markets continued, reflecting both the rising pressures within the EMU bloc (and resultant growing likelihood of a positive swing in the relative growth rates within Europe towards Germany and France) and the attractive relative valuations of related companies. Activity elsewhere was dominated by Japan where the sectoral bias was brought more into line with Marathon's late cycle global growth model. Hence exposure to growth/high ROE stocks (Yamaha Corp., Dai Nippon Printing, Aiwa, Fuji Photo), technology (Fujitsu), and defensives (N.T.T., Yamazaki Baking, Wacoal) was reduced with a shift towards economically sensitive, domestic, low ROE sectors. New holdings have in particular focused on three areas - domestic capex (particularly auto related), energy related and heavy industrial (calbe, shipbuilding, defense) - all of which performed well during similar economic periods (1970-73, 1977 80, 1986-87). As a result of the total Fund sectoral exposure to materials rose to 14.2% (versus an index weighting of 11.0%) and to capital equipment to 17.0% (index weighting 12.8%), with corresponding declines in the consumer and financial sectors.

Marathon (con't)

3. **Organizational Issues.** Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.

Personnel: Hired Japanese Equities Analyst

Accounts Gained: 2

Accounts Lost: None

4. **Other Comments.** Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.

None.

Staff Comments

The two accounts they gained were separate accounts of \$150 million each. Marathon is also a finalist for one public fund. As we have been concerned about their growth, we will continue to monitor carefully all accounts added for consistency with their stated growth plan.

In February, they received an additional allocation of \$100 million as part of the increased international allocation. Staff met with William Arah in March. According to him, the funding went well.

Last year's poor performance was due to their expectation that commodity prices and U.S. interest rates would rise. These increases did not occur last year, therefore they expect they will occur this year. The portfolio is currently positioned to take advantage of these increases. So far, this strategy seems to be working for them.

Performance attribution for the quarter relative to EAFE is shown below:

	Jan. - Mar. 1996
Country selection*	-0.13
Stock selection*	1.76
Currency effect	-0.04
Hedging activity	0.04
Total Value Added to EAFE	1.59

Source: State Street Analytics * in local currency

Manager Commentary
Rowe Price-Fleming International

Period Ending:	3/31/96	Returns	Qtr.	Year
Total Firm Assets Under Management	\$24.7 Billion	Actual	5.0%	19.1%
Total Firm Assets Managed in this Discipline	\$18.3 Billion	Benchmark	2.9%	12.5%

1. ***Past Performance.** Summarize your performance over the last quarter and year. Specifically, what active bets did you make relative to your benchmark? Which of these bets worked/did not work and why?*

Country allocation was positive over the quarter. Value was added in Europe, Asia and Latin America with the overweight in the Netherlands and underweighting in Japan particularly helpful amongst larger markets. The weightings in developing markets were generally positive with exposure to Brazil, Mexico and Malaysia most beneficial.

Stock selection was also positive over the quarter. Most value was added in Europe with the Netherlands and France best while stock selection in Latin America and South East Asia was also good. Medium sized and smaller companies performed well in most markets with the exception of Japan.

2. ***Future Strategy.** What active bets are in place at the present time relative to your benchmark? Summarize the rationale for making these active bets.*

Current position and outlook

International markets have started the year well and we are hopeful that this trend will continue through the balance of 1996. Certainly, the economic back-drop remains reasonable, corporate earnings growth is good, bond markets should not weaken from present levels and valuations are generally acceptable. We believe that the smaller markets of Asia and Latin America can make further progress this year while attractive investment opportunities are to be found in both Japan and Europe.

Rowe Price (con't)

3. *Organizational Issues.* Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.

There have been no changes in the ownership of RPFII.

During the first quarter of 1996, RPFII gained one new account in the fully international discipline.

4. *Other Comments.* Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.

None.

Staff Comments

In February, Rowe Price-Fleming received an additional allocation of \$100 million as part of the increased international allocation.

Performance attribution relative to EAFE for the quarter is shown below:

	Jan. - Mar. 1996
Country selection*	0.88
Stock selection*	1.20
Currency effect	0.22
Hedging activity	-0.02
Total Value Added to EAFE	2.25

Source: State Street Analytics * in local currency

Manager Commentary
Scudder, Stevens and Clark

Period Ending:	3/31/96	Returns	Qtr.	Year
Total Firm Assets Under Management	\$103.0 Billion	Actual	6.5%	24.8%
Total Firm Assets Managed in this Discipline	\$ 10.0 Billion	Benchmark	2.9%	12.5%

1. ***Past Performance.** Summarize your performance over the last quarter and year. Specifically, what active bets did you make relative to your benchmark? Which of these bets worked/did not work and why?*

During the first quarter of 1996, MSBI gained 6.5% compared with a 2.9% increase by the EAFE benchmark. Major world stock markets all appreciated in their local currencies. For US investors, a stronger dollar offset less than half the local index gains.

We lightened your exposure to the semiconductor industry and, as a result, your Japan weighting fell slightly to 27% (or two-thirds EAFE). In March we closed out all dollar-yen forwards, leaving no hedges in place. We raised weightings in Europe and to a lesser extent in Asia ex-Japan. Within your European investments, the primary focus has been on additional restructuring opportunities.

2. ***Future Strategy.** What active bets are in place at the present time relative to your benchmark? Summarize the rationale for making these active bets.*

The fundamental investment strategy for your portfolio remains unchanged. The Japanese portion of your portfolio continues to focus on the beneficiaries of global competition, ongoing domestic recovery and a weakening yen. Among your European investments, globally competitive companies and candidates for industry restructuring are heavily represented. Our longer term currency outlook calls for some further strengthening of the dollar. As such, your overall stock mix reflects a US dollar bias.

3. ***Organizational Issues.** Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.*

Personal Gained:

Name	Title	Responsibility
Diego Espinosa	Vice President	Latin America Equity Country Analyst
Joseph B. Swaider	Vice President	Equity Industry Analyst
Judith Anderson	Vice President	Equity Industry Analyst
Patrick Besnehan		Limited Volatility Bond Portfolio Manager
Cynthia McKinley	Vice President	Trader

Scudder (con't)

Personnel Lost:

<u>Name</u>	<u>Title</u>	<u>Responsibility</u>	<u>Reason</u>
Jose G. Medrano	Vice President	Emerg. Markets Bond Analyst	Left to pursue other opportunities
Lincoln Y. Rathman	Managing Director	Emerging Markets Bond Product Leader	Left to pursue other opportunities
Mark Greenberg	Vice President	Equity Industry Analyst	Left to pursue other opportunities
Roy Hong	Vice President	Equity Industry Analyst	Left to pursue other opportunities
Wayne Johnson	Vice President	Equity Industry Analyst	Left to pursue other opportunities

International Accounts Gained/Lost:	<u>Gained</u>	<u>Lost</u>
	*	*

* First quarter data will be sent as soon as available.

4. *Other Comments. Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.*

None.

Staff Comments

Although Scudder lost five people this quarter, the impact on international EAFE portfolios was minimal. Two of the people added will have a minor impact on EAFE portfolio. We will continue to monitor personnel gained/lost.

Performance attribution relative to EAFE for the quarter is shown below:

	Jan. - Mar. 1996
Country selection*	0.94
Stock selection*	2.03
Currency effect	0.32
Hedging activity	0.46

Total Value Added to EAFE	3.75
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Source: State Street Analytics * in local currency

Manager Commentary
Templeton Investment Counsel, Inc.

Period Ending:	3/31/96	Returns	Qtr.	Year
Total Firm Assets Under Management	\$59.7 Billion	Actual	4.8%	21.4%
Total Firm Assets Managed in this Discipline	\$19.2 Billion	Benchmark	2.9%	12.5%

1. ***Past Performance.** Summarize your performance over the last quarter and year. Specifically, what active bets did you make relative to your benchmark? Which of these bets worked/did not work and why?*

The portfolio outperformed the MSCI EAFE index this quarter and over the past year. This result is primarily attributed to two factors. Firstly, the portfolio's emerging markets holdings continued to rebound after having underperformed for two years. Secondly, an underweighting in Japanese securities was also beneficial given continued underperformance of the Japanese market. These factors, however, were somewhat mitigated by a general weakening of major currencies vis-a-vis the US Dollar because the portfolio remains unhedged.

2. ***Future Strategy.** What active bets are in place at the present time relative to your benchmark? Summarize the rationale for making these active bets.*

Our investment strategy remains unchanged. It is a long-term bottom-up stock-picking value approach. Portfolio turnover and transactions costs therefore remain below industry norms. Your portfolio's P/E, P/BV and P/CF are also estimated to be lower than the benchmark index while it's dividend yield is higher than the benchmark index. The portfolio, as noted, also remains underweighted in Japan and overweighted in Europe with a residual weighting in emerging markets. Furthermore, your investments will remain unhedged despite the near-term possibility of continued foreign exchange market volatility.

Templeton (con't)

3. *Organizational Issues.* Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.

There have been no ownership or personnel changes at the firm over the last quarter.

ACCOUNTS GAINED AND LOST:

International Equity-Separate - 7 Accounts/\$86.20 Million - Gained

Commingled, Institutional Fund - 0 - Lost

4. *Other Comments.* Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.

There are no other comments.

Staff Comments

Performance attribution relative to EAFE for the quarter is shown below:

	Jan. - Mar. 1996
Country selection*	0.91
Stock selection*	-0.30
Currency effect	1.33
Hedging activity	0.00
Total Value Added to EAFE	2.01

Source: State Street Analytics * in local currency

Manager Commentary
State Street Global Advisors

Period Ending:	3/31/96	Returns	Qtr.	Year
Total Firm Assets Under Management	\$210.0 Billion	Actual	2.9%	12.8%
Total Firm Assets Managed in this Discipline	\$ 48.0 Billion	Benchmark	2.9%	12.5%

- 1. Past Performance.** *Summarize your performance over the last quarter and year. Specifically, explain the reasons for the tracking error between the portfolio and the index.*

In the first quarter, the portfolio underperformed the benchmark by 11 basis points. Approximately 1.5 basis points of the tracking error is attributed to cash and receivables held in the portfolio; 2.3 basis points is due to stock and country misweights and the remainder of the first quarter tracking error is because of dividend yield smoothing. For the last twelve months, the portfolio also underperformed by 0.11% due primarily to transactions costs incurred at the end of 1995.

- 2. Organizational Issues.** *Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.*

There were no significant ownership or personnel changes during the first quarter end of 1996. During the first three months of 1996, we added three EAFE clients with total assets of \$1.3 billion. There were no accounts lost last quarter.

State Street (con't)

3. *Other comments.* Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.

None.

Staff Comments

Note: Performance from State Street Global Advisors may vary from the custodian's reported performance due to the time of day that currency exchange prices are calculated.

Performance attribution relative to EAFE for the quarter is shown below:

	Jan. - Mar. 1996
Country selection*	-0.01
Stock selection*	-0.02
Currency effect	0.03
Hedging activity	0.00
Total Value Added to EAFE	0.00

Source: State Street Analytics * in local currency

Manager Commentary
Record Treasury Management

Period Ending:	3/31/96
Total Assets Under Management	\$1.7 billion
Total Currency Overlay	\$1.3 billion

1. Performance/Strategy. Summarize your currency positions.

	Currency Exposure* 3/29/96	Assets Included in Overlay Program** 3/29/96	Assets Hedged*** as of 3/29/96
Yen (JPY)	\$665.6 mill	\$228.3 mill 34.30%	\$86.1 mill 12.94%
Sterling (GBP)	281.1 mill	91.3 mill 32.48	0.0 mill 0.00
Mark (DEM)	121.9 mill	40.7 mill 33.35	20.1 mill 16.52
Fr. Franc (FRF)	108.4 mill	35.7 mill 32.90	0.0 mill 0.00
Sw. Franc (CHF)	105.0 mill	34.5 mill 32.89	13.1 mill 15.34
Total	\$1,282.1 mill	\$430.5 mill 33.58%	\$122.4 mill 9.54%

* Based on currency exposure of the SBI's EAFE index fund.

** Assets included will be less than exposure during phase-in period. One twelfth of the exposure will be added to the overlay program each month from December 1995 through November 1996.

*** Strike rates for the hedges are set at 2% out-of-the-money. This requires a 2% strengthening of the USD to trigger a hedge.

The US dollar had a mixed quarter. January saw it strengthen against all currencies only to lose most of its gains by the end of February, then it strengthened back in March leaving it slightly stronger overall by the end of the quarter. Against the Japanese Yen, the initial USD strength took it from 103 to 107 by early February and then back to 104 by the end of the month. It finished the quarter back up at 107. The weakness of the JPY is reflected in the value of the hedge open positions. This pattern was repeated for the other currencies but as the moves were less volatile, the open positions are of less value. USD/GBP and FRF/USD had not weakened sufficiently to have any cover in place as at the end of the quarter.

2. Organizational Issues. Describe any significant ownership or personnel changes at the firm over the last quarter. List currency overlay accounts gained or lost over the same time period.

There have been no major ownership or personnel changes.

A contract has been executed in respect of a new \$700 million mandate. There have been no client losses.

3. Other Comments. Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.

None to report.

Record (con't)

Detail on Positions, by Currency as of 3/29/96

Spot Rate 3/29/96	JPY 106.46	GBP 1.5251	DEM 1.4752	FRF 5.0293	CHF 1.1896
Tranche Dates	Marked to Market*	Marked to Market*	Marked to Market*	Marked to Market*	Marked to Market*
Dec. 11, 1995	1,221,375	(166,770)	(187,963)	(48,319)	(32,690)
Dec. 24	770,947	--	--	--	--
Jan. 8, 1996	(556,813)	(276,930)	(270,747)	(384,969)	(169,346)
Jan. 24	0	--	--	--	--
Feb. 7	0	0	0	0	0
Feb. 22	0	--	--	--	--
Mar. 8	0	0	0	0	0
Mar. 22	0	--	--	--	--
Apr. 7					
Apr. 22					
May 7					
May 22					
Jun. 7					
Jun. 22					
Jul. 7					
Jul. 22					
Aug. 7					
Aug. 22					
Sep. 7					
Sep. 22					
Oct. 7					
Oct. 22					
Nov. 7					
Nov. 22					
Total (Not discounted)	\$1,435,509	(\$443,700)	(\$458,710)	(\$433,288)	(\$202,036)

* Marked to Market value reflects the actual cost to close out each tranche and is calculated using the forward rate at the end of the reporting period to the position's value date.

Profit (Loss) During Quarter **(\$63,009)**
Profit(Loss) Since Inception (Dec. 1995) **(\$102,227)**

Staff Comments

Staff are working with Record, the SBI's custodian and the SBI's consultants to establish appropriate reporting and performance measurement methodologies. As a result, future commentaries may differ in format or content.

Please note that the dollar values reported here reflect the exchange and forward rates used by Record and may differ from those used by the custodian due to timing differences.

Manager Commentary
GE Investment Management, Inc.
Assigned Risk Plan - Stocks

Period Ending:	3/31/96	Returns	Qtr.	YTD
Total Firm Assets Under Management	\$53.5 Billion	Actual	6.4%	32.2%
Total Firm Assets Managed in this Discipline	\$ 9.5 Billion	Benchmark	5.5%	32.3%

1. *Past Performance. Summarize your performance over the last quarter and year. Specifically, what active bets did you make relative to your benchmark? Which of these bets worked/did not work and why?*

GE Multi-Style was ahead of the benchmark S&P 500 by nearly 100 basis points net of fees in the first quarter of 1996. This outperformance was due to good stock selection which has been our historical strength. The greatest value added came in the Technology Sector where our holdings in IBM, Reuters and Perkin Elmer all did well. We also avoided some of the more volatile and poorly performing technology stocks that had significant corrections during the quarter. Other sectors where stock selection added value included; Consumer Stable where we had large holdings of Pepsi and American Home Products, Consumer Cyclical where Sears and International Cable Tel did well and Capital Goods, where we were helped by large holdings in Allied Signal, Dover, Textron, United Technologies and Deere. We also benefited from underweighting in the Utility sector as that group was hurt by rising interest rates. Over the last twelve months we were helped by our underweighting in Consumer Cyclical stocks and were hurt by holding approximately 4% in cash. At the end of 1995 we changed our targeted cash balance for each manager to one percent or less. Individual managers will still be allowed to go up to 5% for short periods of time, but will be expected to average one percent or less over time.

2. *Future Strategy. What active bets are in place at the present time relative to your benchmark? Summarize the rationale for making these active bets.*

We currently are overweighted in the financial and capital goods sectors. During the quarter, we slightly lowered our capital goods overweighting and increased our weighting in consumer stable, although we are still underweighted there. We also increased our weighting in energy and lowered our weighting in basic materials. While valuation is always the primary driver of our transactions, we also suspect that the economy will remain fairly slow for the remainder of the year and thus have been looking for stocks with defensive characteristics that also had attractive valuations. We believe that in the current uncertain economic environment the market will be more volatile than in recent years and thus our style neutral approach with respect to value and growth is particularly appropriate.

GE Investment Management (con't)

3. *Organizational Issues.* Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.

Account Gained: Employers Reinsurance (GE Capital affiliate)

Account Lost: US West

4. *Other Comments.* Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.

None.

Staff Comments

No comments at this time.

Manager Commentary
Voyageur Asset Management
Assigned Risk Plan - Bonds

Period Ending:	3/31/96	Returns	Qtr.	1 Yr.
Total Firm Assets Under Management	\$ 7.2 Billion	Actual	-0.5%	10.2%
Total Firm Assets Managed in this Discipline	\$ 7.6 Billion	Benchmark	-0.2%	9.4%

- 1. Past Performance.** *Summarize your performance over the last quarter and year. Specifically, what active bets did you make relative to your benchmark? Which of these bets worked/did not work and why?*

The fixed income portfolio for the Assigned Risk Plan outperformed its custom benchmark over the past year however, underperformed for the most recent quarter.

To recap:

Through most of 1995, the portfolio remained overweighted in spread product; that is, the sector allocations to corporates / asset-backed and mortgages exceeded those in the benchmark. In the final quarter of the year (October - December), we started to scale back our exposure to corporates / asset-backed and boosted our allocation to mortgages and Treasuries. We continued that strategy through the first quarter of 1996, reflecting our belief that corporates were expensive relative to other sectors and their associated credit risks, and that mortgages represented fair value. Corporates, on a duration weighted basis performed well versus Treasuries over this period, while mortgages lagged in the final quarter of 1995, although have improved considerably over the first three months of this year.

- 2. Future Strategy.** *What active bets are in place at the present time relative to your benchmark? Summarize the rationale for making these active bets.*

Going forward, we will maintain our underweighting in the Treasury sector, adding to the corporate / asset-backed sector to bring it to, at a minimum, its benchmark weighting (42%). Our exposure will remain short, allowing us to add income while minimizing the risks of any spread widening. We will also remain overweighted in liquid mortgage product (specifically, agency-backed pools). Whereas the duration of the portfolio will generally reflect our view of interest rates, we will continue, as always, to add value through sector rotation rather than any explicit interest rate bet. At quarter-end (and currently), the portfolio was marginally long to the benchmark (+105%), consistent with our constructive view for the longer term trend for interest rates. We expect the economy to grow at a manageable 2 - 2 1/2% rate with little pressure on prices (inflation should come in below 3%).

Voyageur (con't)

3. **Organizational Issues.** *Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.*

Personnel changes during first quarter, 1996, are as follows:

Additions:

None

Losses:

2/96 Christopher R. Dougall, CFA, Vice President, Tax-Exempt Fixed Income Portfolio Manager.

Accounts Gained in this discipline:

Tax-Exempt Clients: Pension Plan for Hourly-Rate Employees of Crenlo, Inc.
International Brotherhood of Painters & Allied Trades Union (U.S.)

Accounts Lost in this discipline:

None.

4. **Other Comments.** *Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.*

There were no other issues or events which occurred at Voyageur which would directly affect the management of the SBI account.

However, of note was Voyageur's purchase of 80% ownership of The Clifton Group in March, 1996. The Clifton Group is a Minneapolis based investment advisor and commodity trading advisor which specializes in the use of derivative securities as a tool for risk reduction, return enhancement and asset allocation for both institutional and individual accounts. Portfolio management for Voyageur and Clifton group clients is separate and distinct. Only some marketing and administrative functions are shared between the companies.

Staff Comments

Staff does not believe the acquisition of the Clifton Group will adversely affect the management of the Assigned Risk Plan's account.

Manager Commentary
Internal Stock Pool
Trust/Non-Retirement Assets

Period Ending:	3/31/96	Returns	Qtr.	YTD
Total Firm Assets Under Management	\$64.8 Million	Actual	5.5%	32.0%
Total Firm Assets Managed in this Discipline	\$64.8 Million	Benchmark	5.5%	32.3%

1. *Past Performance.* Summarize your performance over the last quarter and year. Specifically, explain the reasons for the tracking error between the portfolio and the index.

For the quarter, the index fund matched the benchmark. For the year, it had negative tracking error of 22 basis points (32.04% vs. 32.76%). The negative was due to residual cash (0.5% or \$279,000) and trading and other. Some cash levels will always be maintained in the account because the dollar value is too small to equitize with futures. (Currently one futures contract will equitize \$325,000.) In a strong stock market this will cause some negative tracking error. In addition, trading activity induced by cash flows, dividends or corporate actions will contribute to tracking error. Over time, this activity will generate a small negative bias due to transaction costs.

2. *Future Strategy.* Going forward, what strategies, if any, do you plan to implement to control tracking error within expectation.

Staff purchased futures to equitize a \$2 million cashflow received on February 1, 1996. Staff plans to maintain the future position until enough cash has been built up to construct a reasonable stock purchase package. The S&P 500 index continues to incur a fair amount of merger activity. However, dividend cashflow has been sufficient to cover the purchase of new additions to the index.

Internal Equity Index Pool (con't)

- 3. *Organizational Issues.*** Describe any significant ownership or personnel changes at the firm over the last quarter. List accounts gained and lost in this discipline over the same time period.

No other comments.

- 4. *Other Comments.*** Highlight any other issues/events that are pertinent to the management of the SBI account at your firm.

None

**Manager Commentary
Internal Bond Portfolios**

Period Ending:	03/31/96	Returns	Qtr.	Year
		Actual	-1.7%	12.0%
Assets Managed in this Discipline	\$0.61 billion	Benchmark	-1.8%	10.8%

1. *Past Performance. Summarize your performance over the last quarter and year. Specifically, what active bets did you make relative to your benchmark? Which of these bets worked/did not work and why?*

Performance, Fourth Quarter '95

The above returns reflect the combined bond segments of the Environmental Trust Fund, the Income Share Account, and the Permanent School Fund. Collectively, the funds outperformed the index returns.

- A shorter duration than the market enhanced returns as interest rates increased.
- An underweighted Treasury position and overweighted mortgage position enhanced returns since mortgage securities performed well during the quarter.
- A slightly barbelled portfolio decreased returns as the yield curve steepened during the quarter.
- A neutral to underweighted corporate position detracted from performance since corporate securities performed well as spreads tightened.
- An underweighted mortgage pass-through position and overweighted CMO position within the mortgage sector detracted from performance as pass-through spreads tightened more than CMO spreads.

Performance for the Year

Collectively, the funds outperformed the index. Most of the value added occurred during the 2Q95 of the year.

- A longer duration than the benchmark increased performance as interest rates declined. After the 2Q95, the duration was shortened to a neutral position which maintained returns as interest rates rose.
- A barbelled structure enhanced performance as the yield curve flattened.

- An overweighted position in positively convex CMO securities increased returns as interest rates fell.
- An underweighted position in negatively convex pass-through mortgages enhanced returns as interest rates fell but detracted as interest rates rose.
- A neutral to underweighted Corporate position decreased returns since the corporate sector performed well.

2. *Future Strategy. What active bets are in place at the present time relative to your benchmark? Summarize the rationale for making these active bets.*

Yield Curve Strategy

With the recent increase in interest rates, real US interest rates have increased significantly. If you assume that inflation will be 3% next year, the real yield on the ten year Treasury is around 3.8 %. At this level, bonds are more attractive than at the beginning of the quarter. At these levels, the portfolio duration will be neutral to slightly longer than the market.

We will move to add more bonds in the middle part of the curve and reduce the barbelled position because we believe there is more value here than at the beginning of the quarter.

Corporate Strategy

Corporate spreads are still tight and we will remain neutral to underweighted in them. We will look to selectively add corporates to the portfolio throughout the quarter if spreads widen.

Mortgage Strategy

We will remain overweighted in mortgages. With the recent increase in rates, mortgages have become more positively convex and should perform well if interest rates move in either direction.