MINUTES OF THE
NEW MEXICO STATE INVESTMENT COUNCIL
Santa Fe, New Mexico
January 25, 2005

ROLL CALL/INTRODUCTION OF GUESTS

A regular meeting of the New Mexico State Investment Council was called to
order on this date at approximately 9:25 a.m. in the Governor’s Cabinet of the
State Capitol Building, Santa Fe, New Mexico.

Introduction of Guests followed Roll Call:

**Members Present:**
Hon. Bill Richardson, Governor of New Mexico
Mr. Gary B. Bland, State Investment Officer
Mr. James C. Jimenez, Secretary, DFA [arriving 9:45 a.m.]
Mr. Patrick Lyons, Commissioner of Public Lands
Mr. Robert Vigil, State Treasurer
Mr. Andrew Davis, Public Member [by telephone]
Mr. David Harris, Public Member
Mr. Michael Stanford, Public Member

**Members Excused:**
Mr. Ike Kalangis, Public Member

**Legal Counsel Present:**
Mr. Zachary Shandler, Attorney General’s Office

**Staff Present:**
Mr. Bob Jacksha
Mr. Stephen Jerge
Mr. Greg Kulka
Mr. Adam Levine
Mr. Mark Valdes
Mr. Charles Wollmann

**Guests Present:**
[See Guest List.]
APPROVAL OF AGENDA

Mr. Stanford moved approval of the Agenda, as published. Mr. Harris seconded the motion, which passed by voice vote 7-0.

APPROVAL OF MINUTES: December 21, 2004

Upon motion by Commissioner Lyons, seconded by Mr. Stanford, the Minutes of the December 21 meeting were approved, as submitted, 7-0 by voice vote.

UPDATE ON NEW MEXICO PRIVATE EQUITY PROGRAM

Brian Birk, New Mexico representative for Fort Washington Capital Partners, reviewed slides which summarized NMPEIP program goals; NMPEIP allocation versus the target, and Direct Investment activity in 2004.

In reviewing allocation versus target, Mr. Birk stated that the New Mexico Private Equity Investment Program is well within current statutory limits. He said Fort Washington will continue to monitor the exposure "and expect to be able to maintain the level of investment activity that we've seen over the past few years, over the next two or three years and perhaps further, depending on how the Severance Tax Permanent Fund actually increases in value."

In reviewing the activity summary for 2004, Mr. Birk said Fort Washington completed initial review of ten funds, of which they did detailed reviews on six; and of those six, they conducted a complete due diligence analysis on two funds. He said Fort Washington made positive recommendations and closed on those two funds: Verge Seed Fund (65% of the fund up to a maximum of $10 million) and Wasatch New Mexico Fund ($12 million in capital). He said Fort Washington also completed negotiations on final terms on two additional funds that had been previously approved by the SIC: Flywheel Ventures ($15 million in capital), and Ventana V ($15 million in capital).

Mr. Birk said Fort Washington is beginning the assessment process with eight new funds that will be approaching the State for funding in the next three to six months.

In reviewing the New Mexico Co-Investment Partnership established in April 2004, Mr. Birk said Fort Washington has reviewed 66 direct investment opportunities, which resulted in due diligence for seven and investments in three
companies located in New Mexico: CoMet Solutions, a tool developer for computer-aided engineering tools; Eclipse Aviation; and Advent Solar, a photovoltaic renewable energy business.

Speaking to economic impact on New Mexico, Mr. Kulka reported that the companies that the funds and New Mexico Co-Investment Partners have invested in have created 1,000+ jobs with annual payroll and spending of $90+ million. He added that these figures are as of 9/30/04 and that the year end figures will be closer to $100 million. He also reported that the New Mexico Film Program, where the State has given approval on $45 million of projects, has resulted in 600+ jobs and spending of about $25 million. He noted that these figures include reported figures from Wildfire, which finished production at the end of November.

Mr. Kulka commented that the New Mexico program, with these different components, has now hit a high point and is “operating on all cylinders.” He added that the New Mexico Venture Capital Association has just held its organizational meeting, which was very successful. He said he thought this cooperative relationship could be expected to increase VC activity in New Mexico in the future.

Mr. Bland stated that staff is working with Aldus Equity Partners in revaluating the National Program. He noted that the program has 126 funds, a number of which are in loss positions and/or are small funds, and staff is also working with Aldus to package and sell those “tag end” pieces and make the program more efficient.

Mr. Bland reported that, for FY 2004, the increase in value in the National Program is about $20 million, or about $15 million to the Land Grant Permanent Fund and $5 million to the Severance Tax Permanent Fund. He said the total valuation of the National Program is about $373 million at this point, but it will be another three to four months before all of the numbers are in for 2004 and market value can be calculated. He said staff anticipates no major changes, however.

DISCUSSION AND VOTE ON FIRST SNOW FILM INVESTMENT — PETER DEKOM

Appearing before the SIC were New Mexico Film Investment Advisor Peter Dekom; New Mexico Film Office Director Lisa Strout; Film Office Deputy Director Patti J. Bushee, and Yari Film Group CFO Bernd Stephan.

Mr. Dekom stated that this motion picture was approved for recommendation to the SIC by the Private Equity Investment Advisory Committee on January 12, 2005 and the amount of the loan was $7,350,080. He said the PEIAC approved
two alternative structures, of which the company elected for a payback date of 18 months from drawdown with a 3% profit share.

Mr. Dekom stated that Bob Yari Productions, which has been involved with some very successful motion pictures, "is exactly the kind of company that does the kind of budget level motion picture production that is very beneficial to the State... They don’t make movies unless they know they’ve got at least 80 percent of the motion picture budget pretty much covered through international presales, excluding domestic territory. Their philosophy is predicated on, let’s cover the cost of the production out of the international marketplace and look to the domestic marketplace for upside. They have been wildly successful in this particular endeavor.” He added that, as of today, First Snow “is already pretty much going to be in profits unless it goes over budget. And we do have a completion bond, Film Finances [an approved New Mexico guarantor], which should cover that reality as well.”

Mr. Dekom stated that Bob Yari Productions (BYP) has raised approximately $900,000 in equity from MHF Sweite Academy Film GMBH & Co, a German tax-incented media production fund. He added, however, that under German law, the German company has to own and control the copyright and has to be the physical production entity (“in other words, they have to write all the checks”), so the upshot is a complicated group of companies and sub-companies “just to make this happen.” Mr. Dekom said a special purpose company, Happy Endings Productions (HEP), is being formed for this motion picture as “sort of the straw man distribution company,” whereas First Snow Productions, LLC, is the physical production entity. In addition, he said, BYP will use Syndicate Films International, LLC, as its foreign sales distributor.

Mr. Dekom remarked, “It’s complicated to look at all these things. Just understand that... in order to get this $900,000 contribution, this structure has been necessitated. It’s good for us, because it’s softer money, they don’t get much of a rate of return, and we are very happy to launch films that are smart enough to figure all this out.”

Mr. Dekom said that, in addition to the budget, about $1.5 million in deferments will go to third party producer BYP and the star, Guy Pearce.

Mr. Dekom described the plot of First Snow, a psychological thriller.

Mr. Stephan explained that when an independent production runs out of money, “studios will try to grab the product for peanuts.” He said they are holding back on domestic distribution because their downside is covered through international distribution, and this strategy gives them much better leverage to negotiate and “shop the product” with the studios.
Mr. Dekom stated that, while the producers want this to receive an MPAA rating of PG-13, both he and the Film Office feel this could go into a possible R rating, which the PEIAC approved.

Ms. Strout added that a couple of scenes in the film could result in a soft R rating, and it would be prudent to anticipate that.

Ms. Strout said filming will begin in Albuquerque on February 14 and go for 29 days. She stated that there are 107 total BTL crewmembers, 85 of whom are New Mexicans. She said BTL payroll is currently at 69%, well above the required 60%. She said 14 department heads are from New Mexico.

Mr. Kulka stated that Imperial Capital Bank, which will be issuing the letter of credit, is well known for doing entertainment financing and acquired most of the assets of the Lou Horowitz organization, along with three-quarters of its people, in October 2002. He added that, although Imperial is not officially A-rated, "we and other SIC staff — particularly, our equity portfolio manager that covers the financial sector — looked at Imperial Capital Bank relative to other A-rated banks. For example, we have accepted a letter of credit from Comerica Bank, which is an A-rated bank; so the comparison we did was with Comerica, and we also did it with other smaller capitalized banks. Imperial Capital Bank is about a $2 billion institution and approximately 75-80% of their loans are floating rate commercial real estate loans. Our opinion was that it was of a caliber at least equal to, if not slightly above, that of other A-rated banks.

“So under the third clause in our statute that allows us to accept a guarantor that is a significantly financially strong and similar to the other two ratings, that we feel that this is a similar type of guarantee, and we’re very comfortable with accepting a letter of credit from Imperial Capital Bank.”

Mr. Kulka noted that the PEIAC expressed no concerns about the guarantor.

The Summary section of Mr. Dekom’s memorandum recommended that this transaction (a $7,350,080 loan with an outside payback date of 18 months with 3% of the Film’s defined profits to the State) be approved by the State Investment Council, subject to SIC approval of the possible R-rating, pending finalization of all relevant documentation in accordance with the following parameters:

1. Securing the loan guarantee (letter of credit) from Imperial Capital Bank (or other SIC-approved guarantor) for the full amount of the $7,350,080 loan to HEP from New Mexico in accordance with the above payback/recoupment structure in a form reasonably acceptable to the SIC appointed legal counsel.

2. Securing the relevant completion bond as described above from Film Finances.
3. Securing the necessary written commitments to pay the State directly (with underlying security agreements as recommended by counsel to the SIC) from the various sales agents and other distributors of the film as to recoupment of above principal amount and negotiated upside.

4. Finalizing agreements with Guy Pearce (or a lead actor who sustains or exceeds the international presale/advance estimates from the international distributor) and the director.

5. Finalizing an agreement or agreements with both HEP (and to the extent that legal counsel deems necessary, the above-noted German fund’s designated entity) and Syndicate setting forth: their detailed compliance obligations to insure that all relevant statutes and regulations are followed, the State’s right of recoupment from the cash flow of the film as set forth above, the State’s right to participate in the upside percentage from the film’s revenues, if such upside is in fact generated, together with normal auditing and accounting provisions, verification and the relevant representations that all promised distribution arrangements are in fact finalized and in place, normal and customary representations and warranties that the chain of title is intact, that production of the film will not violate any third party rights, full indemnification of the State against claims, verification that all necessary insurance is in place and such other and customary provisions that are contained in agreements of this type are appropriately set forth. The State will accept a reasonable structure which may be required to access the German entity set forth above, subject to approval by its legal counsel, that may allocate physical production responsibility and/or ownership in the name of MHF Sweite Academy Film GMBG & Co. KG.

Mr. Bland moved that the State Investment Council consider an R-rated film investment for First Snow. Governor Richardson seconded the motion and it passed 8-0 by voice vote.

Mr. Bland moved approval of a recommendation to loan $7,350,080 from the New Mexico Film Investment Program with a final maturity of 18 months at zero interest, plus a 3% profit participation to Bob Yari Productions/Happy Endings Productions/First Snow Productions for the production of First Snow contingent on Items 1 through 5 in the Summary section of Peter Dekom’s Recommendation and subject to negotiation of final terms and conditions and completion of appropriate paperwork.

Mr. Harris seconded the motion.

Responding to questioning from Mr. Stanford on whether Imperial Bank is actually the guarantor, i.e., is there a third party that does the letter of credit
through them, Mr. Stephan said Imperial itself will issue the letter of credit, but only after the money from the German fund is given to them as cash collateral, along with all of the foreign distribution contracts, and after they undergo a tedious legal process that includes reviewing the credit worthiness of all of the distributors.

Mr. Stephan said the bank receives a benefit through legal fees and a commitment fee of 1.75%.

Mr. Davis requested that, as a matter of record in the future, film investment reviews include a little more discourse on the analysis done by staff on the bank or lending institution involved.

The motion passed 8-0 by voice vote.

STATE INVESTMENT OFFICER’S REPORT

Mr. Bland said staff’s financial remediation plan is nearing completion and should be delivered to the State Auditor in a few days.

Mr. Bland stated that the February meeting will include an extensive performance review by NEPC, which he hoped would include the final audited results for the fiscal year as well as results for the calendar year. He said staff has some questions about performance calculations.

Mr. Bland reported the following fund values for the 2004 calendar year: $8.2 billion for the LGPF; $3.8 billion for the STPF; and $80 million for the Tobacco Settlement Fund. He added that there is about $380 million in client assets, the largest piece being the retiree health fund, which is now under review.

OLD BUSINESS

None.

NEW BUSINESS

None.
ADJOURNMENT

Its business completed, the State Investment Council adjourned the meeting at approximately 10:10 a.m.

Approved by:

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Hon. Bill Richardson, Governor

Respectfully submitted:

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Judith S. Beatty, Council Reporter