State of New Jersey
DEPARTMENT OF THE TREASURY
DIVISION OF INVESTMENT
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February 10, 2006

MEMORANDUM TO: State Investment Council

FROM: William G. Clark
Director

SUBJECT: **Proposed Private Equity Investments in Partnerships Managed by JP Morgan and Oaktree Capital Management**

This due diligence memorandum is presented to the State Investment Council (the "Council") pursuant to N.J.A.C. 17:16-69.12 (a) to report on two proposed private equity investments: a $50 million commitment to JP Morgan Venture Capital Institutional Investors III and a $50 million commitment to OCM Mezzanine Fund II (managed by Oaktree Capital Management).

Please note that these investments will be authorized pursuant to Articles 69 and 90 of the Council's regulations which became effective on June 20, 2005. The JP Morgan Venture Capital Institutional Investors III will be considered a "Venture Capital Investment" and the OCM Mezzanine Fund II investment will be considered a "Debt-related Investment" as defined under N.J.A.C. 17:16-90.2 (a).

The Alternative Investments Procedures adopted by the Council on January 20, 2005 require any potential alternative investment opportunities to be identified and initially evaluated by the Head of Alternative Investments of the Division (myself in an acting capacity) and the applicable Asset Class Consultant (Strategic Investment Solutions for private equity, or "SIS") in coordination with the DOI Investment Committee (Ike Michaels acting as Deputy Director and myself).

As a result of internal and external sourcing, the DOI Investment Committee identified these proposed investments. SIS and Division staff then proceeded to undertake extensive due diligence on these two proposed investments. We completed the same due diligence process as with all the other alternative investment opportunities presented to the Council.

Based on this due diligence, the Division has determined that each of the proposed investments meets the criteria for investments set forth in the Alternative Investment Procedures.

The investments that we are proposing focus on the early stage venture capital market (JP Morgan Venture Capital Institutional Investors III) and the mezzanine debt market (OCM Mezzanine Fund II).

JP Morgan Venture Capital Institutional Investors III is a venture capital commingled fund-of-funds focusing on early stage companies, emphasizing the technology, communications and life sciences sectors. The general partner seeks to identify partnerships with successful investment teams, high quality deal flow and a proven ability to build companies. The general partner has a proven track record of executing its strategy and generating top-quartile returns as well as proven access and established relationships with top tier venture firms. The JP Morgan team is composed of dedicated private equity professionals with venture capital experience and relationships dating back 25 years. The general partner has substantial capital committed to the Fund, thus aligning our interests with those of the general partner. We believe the management fees are reasonable, and all other legal and economic terms are fair and consistent with market standards.

Oaktree Capital Management, the general partner for OCM Mezzanine Fund II, operates with a focus on fundamental credit analysis and a bias for conservative deal structures. OCM Mezzanine Fund II will seek inefficient markets offering high returns after intensive due diligence and deal structuring to produce a risk-controlled investment portfolio. The general partner has a history of making successful mezzanine investments and has demonstrated the ability to generate top-quartile returns. The general partner will be investing a significant amount in the Fund, ensuring that the limited partners' interests are aligned with those of the general partner. The management fees are reasonable, and all the legal and economic terms associated with the partnership are fair and consistent with market standards.

A formal written due diligence report for each of the proposed investments was sent to each member of the Investment Policy Committee of the Council on February 5, 2006, and a meeting of the Committee was held on February 9, 2006. In addition to the formal written due diligence reports, all other information obtained by the Division on these two investments was made available to the Investment Policy Committee.

After reviewing this extensive due diligence, the Investment Policy Committee of the Council decided to report on these proposed investments to the full Council pursuant to Step 4 of the Alternative Investments Procedures. Under these procedures, the Council may adopt or otherwise act on this report.

We will work with representatives of the Division of Law and outside counsel to review and negotiate specific terms of the legal documents to govern each investment. In addition, each proposed investment must comply with the Council's "pay to play" regulation (N.J.A.C. 17:16-4). While we are confident that we will work through these issues, the potential exists that a successful resolution will not be reached with one or the other of these general partners.

We look forward to discussing these proposed private equity investments at the Council's February 16, 2006 meeting.

WGC:cae
Attachments

*SIC Investment Committee Fund Review Memo

To:	**State Investment Council**
From:	**SIC Investment Committee**
Date:	**February 16, 2006**
Subject:	**JP Morgan Recommendation**

Fund Facts

Fund Name:	J.P. Morgan Venture Capital Institutional Investors III, LLC
Fund Type:	Comingled Venture Capital Fund of Funds
Current Fund Size:	$1.5 billion
Previous Fund Size/Vintage:	$2.1 billion
Final Close:	June-06
Fund Address:	522 Fifth Avenue New York, NY 10036

GP Contact Info

Name:	Lawrence M. Unrein
Telephone:	212-837-2225
Email:	lawrence.unrein@jpmorgan.com

Summary of Terms and Investment Strategy

Investment Strategy:	Early stage venture capital focus, commingled fund of funds emphasizing the technology, communications and life sciences sectors.
Geographic Focus:	US
GP Co-Investment Amount:	1% of fund or $15 million
Terms:	13 years with up to 2 one-year extensions
Commitment Period:	Target 3 year commitment period to underlying fund managers (maximum 5).
Management Fee:	1.1% of committed capital - reduced by 10% in the 9th year and thereafter.
Carry:	0% Partnerships, 10% Secondaries and 20% Directs
Hurdle Rate:	0%

NJ AIP Program:

Recommended Allocation:	$50 million
% of Fund:	3.33%
% of New Jersey State Pension Plan*:	0.07%
% of AIP Private Equity Allocation ($3.5b)*:	1.43%
% of Buyout Allocation FY 06 ($1.75b)*:	2.86%

LP Advisory Committee Membership:	Yes
Consultant Recommendation:	Yes
Compliance with SIC "Pay to Play" Reg:	Side letter required

*This review memorandum was prepared in accordance with the State Investment Council rules governing the Alternatives Investment Program and the policies and procedures related thereto.