

February 13, 2008

MEMORANDUM TO: State Investment Council

FROM: William G. Clark
Director

SUBJECT: **Proposed Private Equity Investment in Tenaska Power Fund II, L.P.**

This due diligence memorandum is presented to the State Investment Council (the “Council”) pursuant to N.J.A.C. 17:16-69.9 (a) to report on two proposed private equity investments: a \$100 million commitment to the Tenaska Power Fund II (TPF II), L.P.

Please note that this investment will be authorized pursuant to Articles 69 and 90 of the Council’s regulations. These investments are considered to be a “Buyout Fund” investment as defined under N.J.A.C. 17:16-90.1.

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, Deputy Director and myself).

Based on this due diligence, the Division has determined that the proposed investment meets the criteria for investments set forth in the Council’s Alternative Investment Policy.

Tenaska Power Fund II (TPF II), L.P. – Tenaska is a power development company and energy marketer with expertise in power plant development, ownership and operation, natural gas, biofuels and electric power marketing and fuel procurement. Tenaska was founded in 1987 as, and remains today, a privately held, employee-owned company. The company is headquartered in Omaha with additional offices in Dallas, Denver and Calgary, Canada.

TPF II intends to make primarily controlling acquisitions in a diverse group of power and energy-related companies and assets in the United States. TPF II's investment activities will be focused in the following areas of the energy and power industries: 1) Power generation, 2) Natural gas storage, pipeline and other gas midstream, 3) Energy and power infrastructure goods and services, 4) Electric and gas transmission and distribution, and 5) Biofuels, wind and geothermal ("Renewables")

The investment philosophy and strategy for TPF II will be similar to TPF I. The investment team intends to build a diversified portfolio consisting of primarily controlling interests in high quality power and energy assets and companies in the United States.

As a result of internal and external sourcing, the DOI Investment Committee identified the proposed investment. As a result, SIS and Division staff proceeded to undertake extensive due diligence on the proposed investment. 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 the proposed investments meet the criteria for investments set forth in the Alternative Investments Policy.

A formal written due diligence report for this proposed investment was sent to each member of the Investment Policy Committee of the Council on February 8, 2008, and a meeting of the Committee was held on February 13, 2008. In addition to the formal written due diligence reports, all other information obtained by the Division on this investment was made available to the Investment Policy Committee.

After review of the extensive due diligence, the Investment Policy Committee of the Council decided to report on the 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.

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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 the other general partner.

We look forward to discussing the proposed private equity investment at the Council's February 21, 2008 meeting.

WGC:cpp
Attachment