

October 21, 2010

MEMORANDUM TO: State Investment Council

FROM: Timothy Walsh  
Director

SUBJECT: **Proposed Investment in Sheridan Production Partners II, LP.**

This memorandum is presented to the State Investment Council (the "Council") pursuant to N.J.A.C. 17:16-69.9 to report on a proposed investment of \$100 million in an oil and gas exploration and production (E&P) fund, Sheridan Production Partners II, LP.

Please note that this investment is authorized pursuant to Articles 69 and 71 of the State Investment Council's regulations. This investment is considered "real assets" as defined under N.J.A.C. 17:16-71.1.

The Division of Investment ("Division") Staff and its consultant, Strategic Investment Solutions, undertook 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.

- Sheridan Production Partners II, LP will pursue a strategy of (i) acquiring a portfolio of currently producing properties characterized by primarily proved reserves and a balance between oil and gas in geographically diverse areas onshore in the United States and on the Gulf of Mexico shelf; (ii) optimizing the operation of those properties through production acceleration and recovery enhancement, appropriate use of capital reinvestment and aggressive cost control; and (iii) providing investors with relatively low risk, long-term cash distributions through prudent hedging and leverage strategies.

In August 2007, New Jersey invested \$50 million in Sheridan Production Partners, LP (Fund I), which has performed extremely well in comparison to similar funds raised in that vintage. Therefore, we believe that the Sheridan team has the breadth and depth of experience to execute this strategy again. Additionally, since the time of Fund I, Sheridan management has built the organization into a fully functional oil and gas company with over 230 employees, half of which are working in field operations.

Sheridan Production Partners II, LP  
Investment Policy Committee  
October 8, 2010

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).

## \*SIC Investment Committee Fund Review Memo

**To:** State Investment Council  
**From:** SIC Investment Committee  
**Date:** October 21, 2010  
**Subject:** Sheridan Production Partners II, L.P. Recommendation

### Fund Facts

Fund Name:	Sheridan Production Partners II, L.P.
Fund Type:	Real Asset fund focused on oil and gas E&P
Current Fund Size:	\$1.6 billion
Previous Fund Size/Vintage:	\$1.3 billion
Final Close:	October-10
Fund Address:	9 Greenway Plaza, Suite 1300 Houston, TX 77046

### GP Contact Info

Name:	Lisa Stewart
Telephone:	713-548-1000
Email:	<a href="mailto:lstewart@sheridanproduction.com">lstewart@sheridanproduction.com</a>

### Summary of Terms and Investment Strategy

Investment Strategy:	The Fund will primarily make equity investments in a diverse portfolio of oil and gas properties across various U.S. basins and fields.
Geographic Focus:	United States
GP Co-Investment Amount:	5% or \$77 million
Terms:	
Term:	15 years from initial closing date with two 1-year extensions
Investment period:	6 years
Management Fee:	1.5% during the investment period based on capital commitments. After investment period management fees will step down to 1.25% per annum of the lesser of capital commitments and the fair value of the limited partners' equity accounts. The management fees will step down at the earlier of the end of the investment period and the raising of a successor Sheridan fund.
Other Fees:	<ul style="list-style-type: none"> <li>*All transaction fees &amp; other fees will be offset 100%.</li> <li>*Partnership will bear all expenses associated with its investment program &amp; operations.</li> <li>*Partnership will pay up to \$2 million in organizational expenses</li> </ul>
Hurdle Rate:	8%

### NJ AIP Program:

Recommended Allocation:	\$100 million
% of Fund:	6.25%

LP Advisory Board Membership:	Yes
Consultant Recommendation:	Yes
Compliance with SIC "Pay to Play" Reg:	Yes

\*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.