AGENDA

Date: November 3, 2017

The regular meeting of the Dallas Police and Fire Pension System Board of Trustees will be held at **8:30 a.m. on Thursday, November 9, 2017, in the Second Floor Board Room at 4100 Harry Hines Boulevard, Dallas, Texas**. Items of the following agenda will be presented to the Board:

A. MOMENT OF SILENCE

B. CONSENT AGENDA

1. **Approval of Refunds of Contributions for the Month of October 2017**

2. **Approval of Estate Settlements**

3. **Approval of Survivor Benefits**

4. **Approval of Service Retirements**

5. **Approval of Alternate Payee Benefits**

6. **Approval of Payment of Military Leave Contributions**

7. **Spouse Wed After Retirement (SWAR)**

8. **Denial of Unforeseen Emergency Requests**

C. DISCUSSION AND POSSIBLE ACTION REGARDING ITEMS FOR INDIVIDUAL CONSIDERATION

1. **Closed Session - Board serving as Medical Committee**

   Discussion of the following will be closed to the public under the terms of Section 551.078 of the Texas Government Code:

   Disability applications

2. **Deferred Retirement Option Plan (DROP) Policy**

   Portions of the discussion under this topic may be closed to the public under the terms of Section 551.071 of the Texas Government Code.

3. **Investment-related items**

    - **a.** Investment Advisory Committee
    - **b.** Review of possible changes to Investment Policy Statement
    - **c.** Investment Policy Statement – Alternative Investments
    - **d.** Investment Policy Statement – Staff Rebalancing Authority

4. **Budget Adoption Policy**

5. **Second reading and discussion of the 2018 Budget**

6. **Ethics Policy review**

7. **Governance and Board Conduct Policy review**

8. **Significant Professional Service Advisors and Providers**

9. **Trustee Education Requirements**

10. **Board approval of Trustee education and travel**

    - **a.** Future Education and Business-related Travel
    - **b.** Future Investment-related Travel

11. Unforeseeable Emergency Requests from DROP Members

Portions of the discussion under this topic may be closed to the public under the terms of Section 551.078 of the Texas Government Code.

12. Legal issues

Portions of the discussion under this topic may be closed to the public under the terms of Section 551.071 of the Texas Government Code.

a. Potential claims involving fiduciaries and advisors
b. DPFP v. The Townsend Group and Gary Lawson
c. Eddington et al. v. DPFP
d. Rawlings v. DPFP
e. DPFP v. Columbus A. Alexander III
f. Degan et al. v. DPFP (Federal suit)
g. HB 3158

13. Quarterly financial reports

14. Requirement for Two Annual Public Meetings

D. BRIEFING ITEMS

1. **Reports and concerns of active members and pensioners of the Dallas Police and Fire Pension System**

2. **Executive Director's report**

   a. Open Government Training
   b. Associations' newsletters
   - NCPERS Monitor (October 2017)
   - NCPERS PERSist (Fall 2017)

   c. Employee recognition – Third Quarter 2017
   - Employee Service Award
   - Employee of the Quarter award

The term "possible action" in the wording of any Agenda item contained herein serves as notice that the Board may, as permitted by the Texas Government Code, Section 551, in its discretion, dispose of any item by any action in the following non-exclusive list: approval, disapproval, deferral, table, take no action, and receive and file. At the discretion of the Board, items on this agenda may be considered at times other than in the order indicated in this agenda.

At any point during the consideration of the above items, the Board may go into Closed Executive Session as per Texas Government Code, Section 551.071 for consultation with attorneys, Section 551.072 for real estate matters, Section 551.074 for personnel matters, and Section 551.078 for review of medical records.

DALLAS POLICE & FIRE PENSION SYSTEM

ITEM #A

MOMENT OF SILENCE

In memory of our Members and Pensioners who recently passed away

(September 30, 2017 – October 30, 2017)

NAME	ACTIVE/ RETIRED	DEPARTMENT	DATE OF DEATH
Mark A. Ferguson	Retired	Fire	Sep. 30, 2017
Donald E. Williams	Retired	Police	Oct. 5, 2017
Charles A. Gray	Retired	Fire	Oct. 9, 2017
Norman H. Brown	Retired	Fire	Oct. 11, 2017
David H. Coughran	Retired	Fire	Oct. 11, 2017
Stephen Washington	Retired	Fire	Oct. 14, 2017
William H. Scott	Retired	Fire	Oct. 16, 2017
Dudley S. Baker	Retired	Fire	Oct. 17, 2017
Delvis L. Taylor	Retired	Police	Oct. 18, 2017
M. W. Gray, Jr.	Retired	Fire	Oct. 22, 2017
Thomas W. Moore	Retired	Police	Oct. 28, 2017
Danny L. Morris	Retired	Fire	Oct. 30, 2017

DISCUSSION SHEET

ITEM #C1

Topic: **Closed Session - Board serving as Medical Committee**

Discussion of the following will be closed to the public under the terms of Section 551.078 of the Texas Government Code:

Disability applications

Discussion: Staff will present two applications for On-Duty disability pensions for consideration by the Board in accordance with Section 6.03 of the Plan. Additional documentation will be available at the meeting.

DALLAS POLICE & FIRE PENSION SYSTEM

DISCUSSION SHEET

ITEM #C2

Topic: **Deferred Retirement Option Plan (DROP) Policy**

Portions of the discussion under this topic may be closed to the public under the terms of Section 551.071 of the Texas Government Code.

Discussion: At the special Board meeting on November 1, the Board gave staff direction on numerous issues with respect to the DROP Policy. Staff is presenting the Board a revised DROP Policy reflecting the Board's requested changes.

Staff Recommendation: **Approve** the DROP Policy.

DISCUSSION SHEET

ITEM #C3

Topic: **Investment-related items**

a. Investment Advisory Committee
b. Review of possible changes to Investment Policy Statement
c. Investment Policy Statement – Alternative Investments
d. Investment Policy Statement – Staff Rebalancing Authority

Attendees: Rhett Humphreys (NEPC)

Discussion:

a. Section 4.07(h) of the plan added by HB 3158 requires that the Board shall establish an Investment Advisory Committee (IAC) composed of trustees and outside investment professionals, with the majority of members being non-trustees, to review investment related matters as prescribed by the Board and make recommendations to the Board. Staff will discuss the potential composition, roles and responsibilities of the IAC with the Board.

b. Staff will discuss possible changes to the Investment Policy Statement (IPS) based on the requirements of HB 3158, as well other recommended changes to clarify the roles and responsibilities of the Board, the IAC, Staff and the Investment Consultant.

c. Section 4.071 of the plan added by HB 3158 stipulates that any new "Alternative Investment" requires a 2/3rd vote of the Board for approval. NEPC and staff will discuss possible definitions of Alternative Investments.

DALLAS POLICE & FIRE PENSION SYSTEM

DISCUSSION SHEET

ITEM #C3
(continued)

d. Staff will seek direction from the Board regarding temporary rebalancing authority to invest excess cash over the interim period until the asset allocation is further studied.

Investment Advisory Committee & Investment Policy Review

Investment Policy Statement

The Investment Policy Statement (IPS), which was approved in May 2016, defines the roles and responsibilities of the Board, Investment Advisory Committee, Executive Director, staff, consultants, investment managers and the custodian. The IPS also included updated asset allocation targets and ranges.

In order to comply with HB 3158, the Board needs to make certain determinations regarding the following items in the Investment Policy Statement:

1. Structure and implementation of Investment Advisory Committee (IAC)
2. Definition of "Alternative Investments"

Investment Policy Statement Review – Roles and Responsibilities

Asset Allocation Targets and Ranges

- *Defined in the IPS with Board approval/amendment based on consultant recommendation in conjunction with staff*

Investment Strategy and Manager Hiring/Full Redemption

- *Board decision based on recommendation from both staff and consultant*

Portfolio Rebalancing

- *Staff implements, within the target asset class ranges, with consultant's concurrence and reports to Board on monthly activity*

Portfolio Due Diligence

- *Staff and consultant responsible for due diligence which is overseen by Executive Director and results reported to Board*

Operational and Implementation Issues

- *Staff responsible*

Investment Advisory Committee ("IAC")

Per HB 3158, the Board shall establish an IAC composed on trustees and outside investment professionals, to review investment related matters as prescribed by the Board and make recommendations to the Board. A majority of the IAC members shall be outside investment professionals.

Though an IAC was never established, the IPS approved in May of 2016 outlined the structure, roles and responsibilities of the IAC:

- *IAC members act as fiduciaries, serve at the discretion of the Board and the Board must approved all nominations*
- *IAC members would serve staggered 3-year terms*
- *IAC will review and vote on all investment related items including, but not limited to, annual asset allocation updates and the hiring or termination of Investment Managers, Consultant(s), and Custodian*
- *IAC chair or vice chair will update the Board with an abbreviated version of the facts and the IAC recommendation, or lack thereof, to the Board, which will accompany the Staff and Consultant recommendations*
- *IAC shall review Staff and Consultant recommendations on asset allocation targets and ranges at least annually, and provide an IAC recommendation to the Board*

Investment Advisory Committee ("IAC") – Key Questions

- How many members? What is preferred composition between outside investment professionals and Board members?

- Options on level of authority to delegate to IAC:
  - IAC has authority to make decisions on all investment-related items including Hire/Fire/Sell decisions
  - IAC reviews staff & consultants Hire/Fire/Sell recommendations and makes recommendation to Board for vote
  - IAC only opines on broad, strategic investment topics such as asset allocation, investment strategy and IPS

- How often should IAC meet? Monthly? Quarterly?

Definition of Alternative Investments

- HB 3158: "Alternative Investment" means an investment in an asset other than a traditional asset. The term includes an investment in private equity funds, private real estate, hedge funds, and infrastructure.
- Any Alternative Investment requires $2/3^{rd}$ vote of Board for approval.
- NEPC has prepared a memo outlining a framework for defining Alternative Investments.
- Board needs to define Alternative Investments going forward.
- On any new investment going forward, staff and NEPC will recommend whether an investment should be classified as an Alternative Investment based on the definition approved by the Board.

Other Recommended Changes

- Recommend clarifying the Executive Director has discretion and authority to execute contract amendments, fund extensions, limited partner governance, and to engage advisors as needed.

- Recommend adding language to rebalancing section of IPS to confirm that Staff, with Investment Consultant's concurrence, has authority to periodically rebalance the portfolio based on the asset allocation targets and ranges. Current language can be interpreted as Staff only having authority to rebalance from portfolio cash flows.

NEPC, LLC

To: Trustees & Staff
Dallas Police and Fire Pension System

From: Rhett Humphreys, CFA, Partner
Keith Stronkowsky, CFA, Sr. Consultant

Date: November 2, 2017

Subject: Defining Alternative Investments

BACKGROUND:
In response to the new legal requirements on investing in Alternative Investments, NEPC has worked to create formal definitions for Traditional and Alternative Investments. To arrive at these, we have broadly relied on a literature review of the topical area, and specifically, we are citing work and definitions from the following:

- CAIA Association,
- CFA Institute Research Foundation,
- Financial Advice and Investment Decisions: A Manifesto for Change (2013, Wilcox & Fabozzi).

TRADITIONAL ASSETS:
"Alternative Assets," as it turns out, is such a broad term that any attempt to universally define it through an inclusionary structure would likely come up short. Most attempts at defining them begin with a definition of Traditional Assets, then rely on a process of exclusion to arrive at what Alternative Assets are. Using this approach, here's a definition for Traditional Assets:

> *Traditional Assets — Assets falling under the classifications of Common Stocks, Bonds, or Cash Equivalents.*

To further expand on this, here are some definitions of each of the three areas of Traditional Assets:

1) Common Stocks — publicly-traded securities representing ownership in a corporation; also known as publicly-traded equity. Examples include publicly traded equity shares of public companies, REITs, and ADRs. Regional examples include shares of companies domiciled in the US, non-US developed markets, and emerging markets.

2) Bonds — publicly-traded securities, the holders of which serving as creditors to either governmental or corporate entities. Examples include government bonds and corporate bonds, including senior bank loans. Regional examples include US government issued bonds, non-US international developed market issued bonds, and emerging market issued bonds. Credit examples include investment grade bonds and non-investment grade bonds (e.g., high yield bonds and bank loans).

3) Cash Equivalents — short-term investments held in lieu of cash and readily converted into cash within a short time span. Examples include CDs, commercial paper, and Treasury bills.

ALTERNATIVE ASSETS:

With a working definition of Traditional Assets as background, we now define Alternative Assets using an exclusionary approach.

Alternative Assets — Assets falling outside of what are deemed 'Traditional Assets.'

We can support this baseline definition by providing two sets of lists:

- A non-exhaustive listing of some characteristics of Alternative Assets, each of which may differentiate an Alternative Asset from a Traditional Asset, and
- A supporting, non-exhaustive list of examples of Alternative Assets.

A) Some defining characteristics of Alternative Assets and their vehicles:

1. Private ownership vehicles (e.g., LPs)
2. Liquidity-constrained, and a lock-up of capital for extended time periods (e.g., one year or longer)
3. Leverage
4. Ability to take short positions
5. Use of derivatives

B) An abridged listing of Alternative Assets by category:

1. Real Assets
    - Timberland
    - Farmland
    - Commodities (although these are publicly traded)
    - Private Real Estate
    - Infrastructure

2. Hedge Funds
    - Macro or Global Macro
    - Managed Futures
    - Merger Arbitrage
    - Distressed
    - Convertible Arbitrage
    - Volatility Arbitrage
    - Fixed Income Arbitrage
    - Long/Short Equity
    - Market Neutral
    - Absolute Return
    - 120/20 or 130/30
    - Hedge Fund-of-Funds

3. Private Equity & Debt
    - Venture Capital
    - Growth Equity
    - Leveraged Buy-outs
    - Mezzanine Debt
    - Direct Lending
    - Distressed Debt
    - Private Secondaries
    - Private Equity Fund-of-Funds

4. Structured Products
    - Credit Derivatives
    - CLOs
    - CDOs

5. Others
    - Risk Parity
    - Commodities

<u>Disclaimer:</u>

Interim Rebalancing Recommendation

Based on Board direction, the $60m will be held in cash at the custodian, which is in addition to the 2% target cash allocation (~ $42.5m).

Staff would like direction from the Board on temporary rebalancing authority to invest excess cash above the ~ $102.5m level that may occur due to sales, distributions, etc. As detailed at the October meeting, staff does not expect these amounts to be significant based on the cash flow forecast.

Staff recommends:

1. Excess cash would be invested across liquid Global Equity, EM Equity and Fixed Income investments based on the asset allocations versus the target at the time.
2. Any cash needs will be met by using the cash on hand rather than withdrawing proceeds from liquid investment sources until such time that cash reaches the 2% target allocation.

INVESTMENT POLICY STATEMENT

As Amended through May 12, 2016

INVESTMENT POLICY STATEMENT

Adopted April 14, 2016
As Amended through May 12, 2016

TABLE OF CONTENTS

INVESTMENT POLICY STATEMENT

Adopted April 14, 2016
As Amended through May 12, 2016

Section I. Introduction and Purpose

This policy statement shall guide investment of the assets of the Dallas Police and Fire Pension System (DPFP). This investment policy statement (IPS) is issued for the guidance of the Dallas Police and Fire Pension System Board of Trustees (Board), Investment Advisory Committee (IAC), Executive Director, Staff, Consultant(s), Custodian, and Investment Managers. This IPS is intended to set forth an appropriate set of goals and objectives for DPFP. It will define guidelines to assist fiduciaries and Staff in the supervision of the investments of DPFP. The investment program processes and procedures are defined in the various sections of the IPS by:

A. Stating in a written document DPFP's expectations, objectives and guidelines for the investment of assets;

B. Setting forth an investment structure for managing the portfolio. This structure includes assigning various asset classes, investment management styles, asset allocation and acceptable ranges that, in total, are expected to produce an appropriate level of overall diversification and total investment return over the investment time horizon;

C. Encouraging effective communications between the Board, IAC, Staff, Consultant(s), Investment Managers and Custodian(s);

D. Set forth policy that will consider various factors, including inflation, consumption, taxes, liquidity and administrative expenses, that will affect the portfolio's short and long term total expected returns and risk;

E. Establishing formal criteria to select, evaluate, monitor, compare, and attribute the performance of Investment Managers on a regular basis; and

F. Complying with all applicable fiduciary and due diligence requirements experienced investment professionals would utilize, and with all applicable laws, rules and regulations from various local, state, federal, and international political entities that can impact DPFP.

Section II. Design, Goals, and Objectives

Staff and the Consultant(s) are expected to deliver excess return beyond the Policy Benchmark[1] through manager selection and asset allocation adjustments. By achieving allocation and performance objectives consistently, the long term investment goals of DPFP are expected to be achieved.

A. Goals

1. Ensure funds are available to meet current and future obligations of the plan when due while earning a long-term, net of fees investment return greater than the actuarial return assumption.

2. To consistently rank in the top half of the public fund universe over the rolling three-year period, net of fees.

B. Objectives

1. To maintain a diversified asset allocation;

2. To provide for an appropriate risk adjusted rate of return;

3. To allow for both passive and active investment management;

4. To monitor quarterly manager performance;

5. To monitor monthly asset allocation changes;

6. To outperform the Policy Benchmark over rolling three year periods;

7. To control and monitor the costs of administering and managing the investments;

8. Establish guidelines and procedures for selecting, monitoring and replacing investment vehicles; and

9. Re-evaluate annually the policies defined in this IPS.

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[1] The Policy Benchmark represents the return of the investable and non-investable indices as defined in Appendix A, at the target allocation for each asset class.

Section III. Standards of Conduct and Fiduciary Responsibility

The following are standards of conduct for the Board, Investment Advisory Committee, Staff, Investment Managers, Consultant(s) and all investment related other service providers of DPFP:[2]

A. Place the interest of DPFP above personal interests;

B. Act with integrity, competence, diligence, respect, and in an ethical manner;

C. Use reasonable care, diligence, and exercise independent professional judgment when conducting analysis, making recommendations, and taking actions;

D. Promote the integrity of and uphold the rules governing DPFP;

E. Comply with all applicable laws, rules, and regulations of any government agency, regulatory organization, licensing agency, or professional association governing their professional activities;

F. Not assist or knowingly participate in any violation of governing laws, rules, or regulations;

G. Not accept gifts, benefits, or compensation that could be expected to compromise independence and objectivity;

H. Must not knowingly make any statement that misrepresents facts relating to investment analysis, recommendations, actions, or other professional activities;

I. Not engage in conduct involving dishonesty, fraud, deceit; and

J. Make full disclosure (annually) of all matters that could reasonably be expected to impair independence and objectivity with their respective duties to DPFP.

Section IV. Core Beliefs and Long Range Acknowledgements

This section outlines the core beliefs and long range acknowledgements for the overall governance of DPFP. These beliefs and acknowledgements will serve as guiding principles in the decision making and implementation of DPFP's investment mandate.

A. A well-defined governance structure with clearly delineated responsibilities is critical in achieving consistent, long term performance objectives.

B. The strategic asset allocation determines the risk reward profile of the portfolio and thus drives overall portfolio volatility.

[2] *These are informed by the CFA Institute and the Center for Fiduciary Studies.*

Section IV. Core Beliefs and Long Range Acknowledgements (continued)

C. The opportunity for active manager outperformance (alpha) is not uniformly distributed across asset classes or Investment Managers' strategies.

D. Leverage may improve a risk / return profile when structured appropriately.

E. Portfolio cash flow and income will be used to rebalance the asset allocation.

Section V. Roles and Responsibilities

A. Board

The Board is made up of twelve (12) Trustees. The Board has a fiduciary role as the representative of DPFP. The Board recognizes its fiduciary duty and acknowledges its responsibility to ensure that the management of plan and DPFP's fund is in compliance with state and federal laws. Additionally, the Board:

1. Establishes investment objectives consistent with the needs of DPFP and prepares the IPS of DPFP;

2. Prudently diversifies, selects, and maintains a general investment strategy consistent with allocation ranges and investment guidelines including an agreed upon risk/return profile;

3. Approves strategic asset allocation targets and ranges;

4. Prudently hires, monitors, & terminates Consultant(s), Investment Managers and other vendors;

5. Reviews investment related expenses;

6. Approves Board travel related to investment monitoring, and in exceptional cases due diligence;

7. Approves any expansion or renewals of the DPFP leverage facility and reviews existing facility;

8. Adopts the IPS and annually reviews in the last quarter of each calendar year and revises as needed; and

9. Avoids prohibited transactions and conflicts of interest.

Section V. Roles and Responsibilities (continued)

B. Investment Advisory Committee

1. IAC Composition, Selection and Criteria:

   a. The IAC serves at the discretion of the Board of Trustees;

   b. The IAC is composed of seven members and represented by three constituent groups: Dallas Police Department, Dallas Fire Department, and Dallas City Council.

   c. Each constituent group will nominate at least one and up to two outside investment professionals to represent their group on the IAC;

   d. One of the two representatives from each group may be filled by an existing Board member;

   e. The Executive Director will nominate one additional outside investment professional to the IAC;

   f. The Board will vote on and approve all IAC nominations;

   g. To be eligible to serve on the IAC, an individual must live or work any county that contains a portion of the City of Dallas;

   h. An IAC meeting requires a quorum of at least four members, of which, at least two members must be outside investment professionals;

   i. An IAC member will serve staggered terms of three years. It is contemplated that the outside investment members of the IAC will sign an agreement and be compensated as determined to be reasonable by the Board. Compensation and expenses are reimbursable under the Education and Travel Policies and Procedure. The IAC selects a chair and vice chair from its members, for a two-year term, to serve as liaison to the Board and to preside over IAC meetings;

   j. Each outside investment professional member of the IAC will respond annually to a disclosure questionnaire, which the Board will review for any independence issues or potential conflicts of interest;

   k. If the Executive Director learns that potential ground for removal of an IAC member exists, the Executive Director shall notify the Chair of the Board of the potential grounds for removal;

Section V. Roles and Responsibilities (continued)

B. Investment Advisory Committee (continued)

1. IAC Composition, Selection and Criteria: (continued)

   l. The Board of Trustees may elect to dismiss a member of IAC for any reason; and

   m. The IAC will meet at least quarterly at duly noticed public meetings.

2. IAC Roles and Responsibilities:

   a. The IAC will review all investment related items including, but not limited to, annual asset allocation updates and the hiring or termination of Investment Managers, Consultant(s), and Custodian;

   b. The IAC will vote on each investment related action item;

   c. The IAC chair or vice chair will update the Board with an abbreviated version of the facts and the IAC recommendation, or lack thereof, to the Board, which will accompany the Staff and Consultant recommendations;

   d. The IAC shall review Staff and Consultant recommendations on asset allocation targets and ranges at least annually, and provide an IAC recommendation to the Board; and

   e. Acts as fiduciaries to DPFP.

C. Staff

1. Executive Director

   a. The Executive Director is authorized to administer the operations and investment activities of DPFP under policy guidance from the Board;

   b. Manages the day to day operations of DPFP;

   c. Reports to Board when strategic asset allocation breaches target allocation bands;

   d. Oversees and reports to Board on investment and due diligence processes and procedures;

   e. Approves/declines all Staff travel related to all manager pre-hire & on-site due diligence;

Section V. Roles and Responsibilities (continued)

C. Staff (continued)

1. Executive Director (continued)

    f. Approval of Investment Staff recommendations for presentation to the IAC and Board; and

    g. Is not a fiduciary to DPFP.

2. Investment Staff

    The Staff is responsible for manager due diligence and recommendations, portfolio implementation consistent with the Board approved asset allocation, and will assess the activities of the Consultant(s). The Staff helps the Board to oversee Investment Managers, Consultant(s), Custodian(s), and vendors. Additionally, the Staff:

    a. Reports to Executive Director when portfolio asset classes exceed allowable strategic boundaries;

    b. Notifies Consultant(s) in writing of rebalancing needs and recommended implementation, so as to employ periodic cash flows to asset classes within target allocation ranges;

    c. Instructs Investment Managers to implement Consultant approved re-balance instructions;

    d. Submits to Executive Director for review, on annual basis, recommended asset allocation targets and ranges & oversees implementation of the approved asset allocation;

    e. Monitors and reports portfolio asset class balances;

    f. Assists in the preparation and annual review of IPS;

    g. Reviews Consultant(s)'s Investment Manager due diligence and recommendations;

    h. Prepares Staff Investment Manager recommendations, submits Staff and Consultant(s) recommendations to Executive Director for review;

    i. After Board approval of investment, Staff approves Investment Manager Strategy guidelines which will be outlined in the Investment Manager agreements, as applicable;

Section V. Roles and Responsibilities (continued)

C. Staff (continued)

2. Investment Staff (continued)

   j. Monitors all investments, Investment Managers and vendors;

   k. Monitors adherence to quantitative due diligence criteria;

   l. Accounts for and reviews annually all external management fees and investment expenses;

   m. Reviews, every two years, the eligibility status of members of the IAC;

   n. Ensures all fiduciaries to DPFP are aware of their fiduciary obligations annually;[3] and

   o. Is not a fiduciary to DPFP.

D. Consultant(s)

The Consultant(s) should monitor qualitative and quantitative criteria related to Investment Managers and aggregate portfolio activity and performance. The Consultant(s), through its continuous and comprehensive responsibilities to DPFP should acknowledge in its contract, its fiduciary responsibility to DPFP. Additionally, the Consultant(s):

1. Recommends annually to IAC and Board strategic asset allocation targets, ranges, and benchmarks for asset classes;

2. Documents asset allocation recommendations with asset class performance expectations including standard deviation, expected return and correlations for each asset class used by DPFP;

3. Establishes and follows due diligence procedures for Investment Manager candidate searches;

4. Conducts screens and searches for Investment Manager candidates;

5. Assists in the selection process and monitoring of Investment Managers;[4]

6. Reviews and recommends Investment Managers and peer groups to IAC and Board;

[3] *Verification of this may be through contract, agreement, or annual fiduciary acknowledgement letter.*
[4] *The specific screening criteria for investment managers can be found in Appendix B.*

Section V. Roles and Responsibilities (continued)

D. Consultant(s) (continued)

7. Documents and delivers to Staff written recommendations on Investment Manager new hire, hold and termination reviews;

8. Any new hire recommendation from the Consultant should include a recommended benchmark and an assessment of appropriate asset class and sub-allocation;

9. Approves and verifies in writing each of Staff's rebalancing recommendations and implementation;[5]

10. Reviews whether rebalancing was done consistent with best practices;

11. Monitors the diversification, quality, duration, and risk of holdings as applicable;

12. Assists Staff in negotiation of terms of vendor contracts;

13. Prepares quarterly investment reports, which include the information outlined in Appendix C; and

14. Acts as a fiduciary to DPFP.

E. Investment Managers

1. <u>Public Investment Managers</u>

   a. Acknowledge in writing acceptance of the objectives, guidelines, and standards of performance;

   b. Invest the assets of DPFP in accordance with its objectives, guidelines and standards;

   c. Exercise full discretionary authority as to all buy, hold and sell decisions for each security under management, subject to the guidelines as defined in this Statement;

   d. If managing a separate account, send trade confirmations to the Custodian;

   e. For separately managed accounts, deliver monthly report to Consultant(s)/Staff describing portfolio asset class weights, investment performance, security positions, and transactions;

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[5] *Evidence of approval may be in electronic format*

E. Investment Managers (continued)

1. Public Investment Managers (continued)

   f. For commingled assets, this statement should show unit position and unit value;

   g. Adhere to best execution and valuation policies;

   h. Prices and fair market valuations will be obtained from a third party reporting service provider;

   i. Communicate to Executive Director any material changes at firm;

   j. Inform DPFP, as soon as practical, in writing of any breach of investment guidelines, ethic violations or violations of self-dealing;

   k. Communicate significant changes in the ownership, organizational structure, financial condition, or personnel staffing; and

   l. Acts as a fiduciary to DPFP.

2. Private Investment Managers

   a. Acknowledge in writing acceptance of the objectives, strategy guidelines, and standards of performance as evidenced in investment manager, operating or partnership agreement;

   b. Will ensure that financials statements undergo annual audits and that investments are reported at fair market value, as outlined in the Investment Management, Partnership or Operating Agreement(s);

   c. Communicate to Executive Director any material changes in the ownership or management of the firm, and or the stability of the organization;

   d. Inform DPFP, as soon as practical, in writing of any breach of investment guidelines, ethic violations or violations of self-dealing; and

   e. Acts as fiduciary to DPFP, unless specified and acknowledged by Board at time of hire.

Section V. Roles and Responsibilities (continued)

F. Custodian

1. Safekeep and hold all of DPFP's assets in the appropriate domestic accounts and provide highly secure storage of physical stock certificates and bonds such that there is no risk of loss due to theft, fire, or accident;[6]

2. Maintain separate accounts by legal registration;

3. Arrange for timely execution and settlement of Investment Manager securities transactions made for DPFP;

4. Provide for receipt and prompt crediting of all dividend, interest and principal payments received as a result of DPFP portfolio holdings or securities lending activities;

5. Monitor income receipts to ensure that income is received when due and institute investigative process to track and correct late or insufficient payments, including reimbursement for any interest lost due to tardiness or shortfall;

6. At the direction of the Staff, expeditiously transfer funds into and out of specified accounts.

Section VI. Authorized Asset Classes & Investments Guidelines

A. Asset Class Guidelines

1. Asset allocation is the primary driver of the volatility of portfolio return. To achieve the goals and objectives of DPFP, the fund's assets will be invested in the categories listed in Appendix A. The assets shall be diversified, in order to minimize the concentration risk, both by asset class and within an asset class.

2. The strategic asset allocation shall be monitored on an ongoing basis and rebalanced when the lower and upper bounds on the ranges are breached, understanding the timing of the rebalancing may be delayed depending the liquidity of the asset class and costs of rebalancing, and otherwise at the discretion of Staff with concurrence of the Consultant.

3. Securities lending is permissible for separately managed accounts and commingled vehicles.

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[6] *Electronic transfer records at the Depository Trust Company ("DTC'') are preferred.*

Section VI. Authorized Asset Classes & Investments Guidelines (continued)

B. Authorized Investments

1. Equities: Equity represents residual ownership of public and private companies after obligations to debt holders have been satisfied.

2. Fixed Income: Fixed-income instruments are securities or debt obligations issued by governments, government-related entities, structured debt facilities and public and private companies that contain contractual obligations from the issuer to make interest and/or principal repayments to investors over the duration of the negotiated term agreement.

3. Real Assets (Liquid and Illiquid): Liquid real assets are investments in tradable tangible/physical assets or related claims that may display a positive correlation to the rate of inflation. Illiquid real assets (natural resources and infrastructure) represent ownership claim to an actual, finite asset or property.

4. Global Asset Allocation: An investment strategy that actively invests in a variety of liquid assets including cash, equity, fixed income, credit, derivatives (interest rate, currency, index) and commodities.

5. Private Equity: A non-financial asset that is relatively illiquid and non-transparent. Private equity funds make investments directly into private companies.

6. Private Debt: Private debt funds typically provide capital to private sector borrowers.

7. Real Estate: Real estate represents investment in a range of properties which provide income and/or appreciation potential. Investments in real estate can be structured as public or private debt and/or equity, and can be in the U.S. or foreign countries.

8. Other Authorized Investments: Trade finance and reinsurance based strategies;

Section VII. Investment Due Diligence & Monitoring

A. Investment Due Diligence

Staff and Consultant(s) are responsible for recommending external Investment Managers to the IAC and Board for review for potential hiring. The following will be implemented:

1. Investment Manager candidate due diligence will be conducted by Staff & Consultant(s).

2. Due diligence criteria are defined in Appendix B.

Section VII. Investment Due Diligence & Monitoring (continued)

A. Investment Due Diligence (continued)

3. Selected candidate(s) will be presented to the IAC.

4. IAC will communicate their recommendation, or lack thereof, on the candidate(s) for consideration and final approval by the Board.

B. Investment Monitoring

1. Staff and Consultant(s) are responsible for monitoring external public & private Investment Managers. Public and private Investment Managers will be monitored relative to peers and benchmarks monthly and quarterly, respectively. Additionally, each current manager is expected to satisfy the due diligence criteria outlined in Appendix B. If the following criteria are not met, an Investment Manager is to be considered an underperformer:

   a. Investment Managers' 3 year rolling returns in excess of peer group average;

   b. Investment Managers' 3 year rolling risk-adjusted returns in excess of peer group average;

   c. Investment Managers' qualitative requirements must be satisfied at all time periods, as determined by Staff or Consultant;

2. Based on the criteria outlined above, the Consultant will highlight underperforming Investment Managers in their quarterly report to Board. If an Investment Manager is considered an underperformer, Staff and Consultant will provide recommendations to IAC and Board regarding whether to "hold" or "sell".

Section VIII. Risk Management

The Staff will work within these policies in order to mitigate the risk of capital loss. By implementing these policies the Board has addressed:

A. Custodial Risk for both public and private holdings;[7]

B. Interest Rate Risk through fixed income duration and credit monitoring;[8]

C. Concentration and Credit Risk through asset allocation targets and ranges, rebalancing, and the monitoring of investment guidelines.

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[7] *Please review Custodian responsibilities in Section V.*
[8] *Please review Annual Review of IPS and Investment Manager strategy guidelines reviewed and approved by Staff.*

Section VIII. Risk Management (continued)

Through these policies, Staff has necessary monitoring criteria established for Custodian, Consultant(s) and Investment Managers, such that DPFP has in place policies that will mitigate interest rate, custody, concentration and credit risks.

APPROVED on May 12, 2016 by the Board of Trustees of the Dallas Police and Fire Pension System.

[signature]

____
Samuel L. Friar
Chairman

Attested:

[signature]

____
Kelly Gottschalk
Executive Director

SECTION IX.

APPENDICES

Appendix A

STRATEGIC ASSET ALLOCATION TARGETS & RANGES

Asset Class	Policy Benchmark	Target	Range
Cash	90-day T Bills	**2.0%**	**0% – 5%**
Plan Level Leverage	(LIBOR + 300)	**0%**	**0% - 15%**
Equity		**30.0%**	**20% – 40%**
Global Equity	MSCI AC World (gross)	20.0%	10% – 23%
EM Equity	MSCI EM Equity (gross)	5.0%	0% – 8%
Private Equity	R3000 +3% (Rolling 3 Mo.)	5.0%	4% – 15%
Fixed Income		**33.0%**	**15% – 38%**
Short-Term Core Bonds	Barclays UST 1-3 Year	2.0%	0% – 5%
Global Bonds	Barclays Global Aggregate	3.0%	0% – 6%
High Yield	Barclays Global HY	5.0%	2% – 8%
Bank Loans	S&P Leveraged Loan Index	6.0%	3% – 9%
Structured Credit & Absolute Return	HFRI RV: FI (50/50-ABS/Corp)	6.0%	0% – 9%
EMD (50/50)	50% JPM EMBI/50% JPM GBI-EM	6.0%	0% – 9%
Private Debt	Barclays Global HY + 2% (Rolling 3 Mo.)	5.0%	2% – 7%
Real Assets		**25.0%**	**20% – 45%**
Natural Resources	S&P Global Nat Res (Rolling 3 Mo.)	5.0%	3% – 10%
Infrastructure	S&P Global Infra (Rolling 3 Mo.)	5.0%	3% – 10%
Real Estate	NCREIF	12.0%	10% – 25%
Liquid Real Assets	CPI + 5.00%	3.0%	0% – 6%
Asset Allocation		**10.0%**	**5% – 15%**
Risk Parity	60% MSCI ACWI/40% Barclays Global Aggregate	5.0%	2% – 8%
GTAA	60% MSCI ACWI/40% Barclays Global Aggregate	3.0%	0% – 6%
Absolute Return	HFRX Abs Ret Index	2.0%	0% – 5%
	TOTAL	100.0%	

Appendix B

The public market Investment Manager screening criteria include:

1. Lead portfolio manager tenure/experience at least 5 years.
2. Firm level assets under management: 75 million or more under management.
3. Investment style should consistently match what is approved and outlined in the Investment Manager’s guidelines, and will be compared and analyzed against peers/sub-asset class category.
4. Sharpe ratio generally would exceed .3, which may not be possible following a prolonged bear market in that respective market, and must exceed 50% of its peer group over a three year rolling period.
5. Three year rolling total return, on a net of fee basis, must exceed 50% of its peer group.
6. On site due diligence meeting is recommended.
7. Fiduciary acceptance and acknowledgement.

The private Investment Manager screening will focus on the key areas of:

1. Alignment of Interests: management fees and expenses, carry/waterfall, term of fund, General Partner commitment.
2. Governance: team, investment strategy, fiduciary duty, Limited Partner Advisory Committee responsibilities and makeup, changes of the fund.
3. Transparency: risk management, financial information, disclosure related to the GP, management and other fees.
4. Track Record: the firm or lead portfolio manager should have a track record of at least 5 years.
5. Performance: a majority of previous funds should rank in the top 50% of their vintage year and strategy fund universe.

The hedge-fund Investment Manager screening criteria include:

1. Lead portfolio manager tenure/experience at least 5 years.
2. Utilization of independent third-party administrator.
3. Sharpe ratio should exceed .5 and must exceed 50% of its peer group over a three year rolling period.
4. Three year rolling total return must exceed 50% of its peer group.
5. A well-defined and documented risk management process.
6. Leverage terms should be appropriate to strategy.
7. Liquidity of assets should match liquidity of fund.
8. Redemption terms consistent with peers.
9. Expected return compensates for illiquidity.

If any of the above due diligence criteria are not met, the Staff and Consultant will disclose this in their recommendations to the IAC and Board, along with an explanation of why the investment is still appropriate.

Appendix C

Investment Consultant Reporting Requirements

The investment consultant is required to provide the Board with quarterly investment information for portfolio monitoring purposes. Generally these are as follows:

Quarterly (due in advance of the Investment Advisory Committee meeting)

1. A review of the current investment market environment.
2. DPFP's actual asset allocation relative to its target asset allocation as defined in Appendix A.
3. DPFP's return relative to its Policy Benchmark return as defined in Appendix A and other public pension funds.
4. DPFP's risk adjusted returns relative to the policy and other public pension funds.
5. Asset class performance relative to the benchmarks as defined in Appendix A.
6. Individual Investment Manager returns relative to their stated benchmark.
7. Report will specifically acknowledge any underperforming Investment Managers based on the criteria outlined in Section VII of the Investment Policy Statement.
8. Any reportable events affecting any of DPFP's Investment Managers.
9. Private Markets reports which covers Private Debt, Private Equity, Infrastructure, Real Assets and Real Estate.

DISCUSSION SHEET

ITEM #C4

Topic: **Budget Adoption Policy**

Discussion: Staff is proposing changes to the Budget Adoption Policy to conform to the changes to Section 4.01 of Article 6243a-1 as set forth in HB 3158.

Such provisions call for submission of the approved annual budget to the City Manager for comment as opposed to the prior requirement for submission to the City's budget office. In addition, HB 3158 removed the requirement for a letter from the DPFP actuary stating whether or not the budget will have an adverse effect on the payment of benefits.

Staff Recommendation: **Approve** the Budget Adoption Policy as amended.

DALLAS POLICE & FIRE PENSION SYSTEM

BUDGET ADOPTION POLICY

As Amended Through ~~August 18, 2016~~__________, 2017

DALLAS POLICE AND FIRE PENSION SYSTEM

BUDGET ADOPTION POLICY
Adopted November 17, 1994
As amended through ~~August 18, 2016~~______, 2017

The fiscal year shall be January 1 through December 31 of each year. Each fiscal year, staff shall present a proposed budget to the Board of Trustees (Board) according to the following schedule:

1. At the October Board Meeting, the staff shall present to the Board the proposed budget for the following fiscal year. The Board may propose changes to the budget and shall approve a budget to be presented to the membership for review via the DPFP website.

2. At the November Board Meeting, members will be given the opportunity to comment on the proposed budget. The Board or staff may propose changes to the budget ~~in response to member comments.~~. The Board shall either approve the final budget or direct staff to make adjustments ~~based on member comments~~ and bring a revised budget to be presented to the December Board meeting for final approval.

In all cases, the final budget shall be approved by December 31 each fiscal year.

~~Included with the budget will be a letter from DPFP's actuary stating whether or not the budget will have an adverse effect on the payment of benefits per Section 4.01(a) of the Combined Pension Plan.~~

~~In accordance with Sec.~~In accordance with Section 4.01 (a) of Article 6243a-1 of Vernon's Revised Civil Statutes ("the Combined Pension Plan"), the Board shall approve all costs of administration to be paid out of the income from the fund when the Board considers such costs necessary, including but not limited to the following:

(a) salaries and benefits of the Executive Director and administrative staff;
(b) office expenses;
(c) expenses associated with securing adequate office space and associated utilities; and
(d) compensation for consultants, investment managers or other persons providing professional services. Fees to investment managers include base management fees, performance or incentive fees, and any disposition fees paid to the investment manager. The budget does not include any carried interest or profit sharing paid to any person or entity managing a "closed-end fund" where such person or entity is not a fiduciary to the Board pursuant to Section 802.203 of the Texas Government Code.

In accordance with Section 4.01 (d) of ~~the Combined Pension Plan Document~~Article 6243a-1, the approved budget will be submitted to the City of Dallas City Manager for comment. The ~~City's budget office~~City Manager may request the Board to reconsider the appropriation for any expenditure at a Board meeting, but the Board shall make the final determination concerning any appropriation.

DALLAS POLICE & FIRE PENSION SYSTEM

At any time during the year the staff may recommend to the Board changes to the budget necessary for the efficient and effective operations of DPFP. Any such changes to the budget must be approved by the Board.

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Board approval of the budget and any changes to the budget, if applicable, is authorization for staff to pay expenditures up to the total amount budgeted.

Each August, staff will present to the Board a detailed, mid-year analysis of actual expenditures versus the budget.

APPROVED on **~~August 18, 2016~~_______, 2017** the Board of Trustees of the Dallas Police and Fire Pension System.

~~Samuel L. Friar~~

William F. Quinn
Chairman

Attested:

Kelly Gottschalk
Secretary

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DALLAS POLICE & FIRE PENSION SYSTEM

BUDGET ADOPTION POLICY

As Amended Through __________, 2017

DALLAS POLICE AND FIRE PENSION SYSTEM

BUDGET ADOPTION POLICY

Adopted November 17, 1994
As amended through ______, 2017

The fiscal year shall be January 1 through December 31 of each year. Each fiscal year, staff shall present a proposed budget to the Board of Trustees (Board) according to the following schedule:

1. At the October Board Meeting, the staff shall present to the Board the proposed budget for the following fiscal year. The Board may propose changes to the budget and shall approve a budget to be presented to the membership for review via the DPFP website.

2. At the November Board Meeting, members will be given the opportunity to comment on the proposed budget. The Board or staff may propose changes to the budget. The Board shall either approve the final budget or direct staff to make adjustments and bring a revised budget to be presented to the December Board meeting for final approval.

In all cases, the final budget shall be approved by December 31 each fiscal year.

In accordance with Section 4.01 (a) of Article 6243a-1 of Vernon's Revised Civil Statutes ("the Combined Pension Plan"), the Board shall approve all costs of administration to be paid out of the income from the fund when the Board considers such costs necessary, including but not limited to the following:

(a) salaries and benefits of the Executive Director and administrative staff;
(b) office expenses;
(c) expenses associated with securing adequate office space and associated utilities; and
(d) compensation for consultants, investment managers or other persons providing professional services. Fees to investment managers include base management fees, performance or incentive fees, and any disposition fees paid to the investment manager. The budget does not include any carried interest or profit sharing paid to any person or entity managing a "closed-end fund" where such person or entity is not a fiduciary to the Board pursuant to Section 802.203 of the Texas Government Code.

In accordance with Section 4.01 (d) of Article 6243a-1, the approved budget will be submitted to the City of Dallas City Manager for comment. The City Manager may request the Board to reconsider the appropriation for any expenditure at a Board meeting, but the Board shall make the final determination concerning any appropriation.

At any time during the year the staff may recommend to the Board changes to the budget necessary for the efficient and effective operations of DPFP. Any such changes to the budget must be approved by the Board.

Board approval of the budget and any changes to the budget, if applicable, is authorization for staff to pay expenditures up to the total amount budgeted.

Each August, staff will present to the Board a detailed, mid-year analysis of actual expenditures versus the budget.

APPROVED on **_______, 2017** the Board of Trustees of the Dallas Police and Fire Pension System.

____

William F. Quinn
Chairman

Attested:

____

Kelly Gottschalk
Secretary

DISCUSSION SHEET

ITEM #C5

Topic: **Second reading and discussion of the 2018 Budget**

Discussion: Attached is the budget proposal for Calendar Year 2018.

The budget has been prepared in total for both the Combined Pension Plan and the Supplemental Plan. Total expenses are then allocated to the Supplemental Plan based on plan asset allocation as reported by JPMorgan.

Due to changes to Section 4.01(a) of the Plan effective September 1, 2017, fees to investment managers and other investment portfolio operating expenses, such as legal, valuation and tax expenses, are now included in the budget for Board approval.

The proposed budget, net of expenses allocated to the Supplemental Plan, totals $27.3M which is a decrease of 5.1% compared to the equivalent projected actual expenses for 2017 and a decrease of 19.1% compared to the equivalent 2017 budget (excluding investment expenses not budgeted for in the prior year.) Including investment expenses, the 2018 budget is 5.9% lower than projected 2017 actual expenses.

Significant variances from the prior year budget and/or projected 2017 actual expenses are explained in the comments accompanying the proposed budget.

Staff Recommendation: **Direct** staff to address any proposed amendments and present the amended budget to the Board at the December 14, 2017 Board meeting.

Dallas Police & Fire Pension System
Operating Budget
Calendar Year 2018

	Description	2017 Budget	2017 Projected Actual	2018 Budget	$ Change vs Prior Yr Budget	% Change vs Prior Yr Budget	$ Change vs Prior Yr Proj. Actual	% Change vs Prior Yr Proj. Actual
Administrative Expenses								
1	Salaries and benefits	4,199,476	4,190,000	3,728,000	(471,476)	(11.2%)	(462,000)	(11.0%)
2	Employment expenses	3,009	450	151,125	148,116	4922.4%	150,675	33483.3%
3	Memberships and dues	17,600	17,600	17,040	(560)	(3.2%)	(560)	(3.2%)
4	Staff meetings	1,000	-	1,000	-	0.0%	1,000	N/A
5	Employee service recognition	1,960	1,200	-	(1,960)	(100.0%)	(1,200)	(100.0%)
6	Member educational programs	2,500	1,500	2,500	-	0.0%	1,000	66.7%
7	Member outreach programs	720	-	-	(720)	(100.0%)	-	N/A
8	Board meetings	13,360	7,000	10,100	(3,260)	(24.4%)	3,100	44.3%
9	Conference registration/materials - Board	51,615	10,000	14,400	(37,215)	(72.1%)	4,400	44.0%
10	Travel - Board	128,335	15,000	25,000	(103,335)	(80.5%)	10,000	66.7%
11	Mileage - Board	5,000	3,100	5,000	-	0.0%	1,900	61.3%
12	Conference/training registration/materials - Staff	32,450	6,800	27,050	(5,400)	(16.6%)	20,250	297.8%
13	Travel - Staff	60,550	32,000	47,000	(13,550)	(22.4%)	15,000	46.9%
14	Liability insurance	447,667	440,000	510,000	62,333	13.9%	70,000	15.9%
15	Communications (phone/internet)	64,312	57,000	49,100	(15,212)	(23.7%)	(7,900)	(13.9%)
16	Information technology projects	20,000	3,000	75,000	55,000	275.0%	72,000	2400.0%
17	IT subscriptions/services/licenses	122,950	84,000	147,100	24,150	19.6%	63,100	75.1%
18	IT software/hardware	39,800	9,400	17,000	(22,800)	(57.3%)	7,600	80.9%
19	Building expenses, incl capitalizable fixed assets	599,266	450,000	337,337	(261,929)	(43.7%)	(112,663)	(25.0%)
20	Repairs and maintenance	97,508	120,000	110,092	12,584	12.9%	(9,908)	(8.3%)
21	Office supplies	31,800	32,000	30,500	(1,300)	(4.1%)	(1,500)	(4.7%)
22	Leased equipment	20,500	24,000	24,500	4,000	19.5%	500	2.1%
23	Postage	27,700	30,000	25,800	(1,900)	(6.9%)	(4,200)	(14.0%)
24	Printing	5,635	5,000	6,370	735	13.0%	1,370	27.4%
25	Subscriptions	2,510	1,200	2,020	(490)	(19.5%)	820	68.3%
26	Records storage	1,200	1,200	1,560	360	30.0%	360	30.0%
27	Administrative contingency reserve	-	150	-	-	N/A	(150)	(100.0%)

Dallas Police & Fire Pension System
Operating Budget
Calendar Year 2018

	Description	2017 Budget	2017 Projected Actual	2018 Budget	$ Change vs Prior Yr Budget	% Change vs Prior Yr Budget	$ Change vs Prior Yr Proj. Actual	% Change vs Prior Yr Proj. Actual
Investment Expenses								
28	Investment management fees	N/A	17,416,000	17,522,000	N/A	N/A	N/A	N/A
29	Investment consultant and reporting	575,000	489,000	505,000	(70,000)	(12.2%)	16,000	3.3%
30	Bank/security custodian services	328,600	262,000	260,000	(68,600)	(20.9%)	(2,000)	(0.8%)
31	Other portfolio operating expenses (legal, valuation, tax)	N/A	2,187,000	860,000	N/A	N/A	N/A	N/A
Professional Services Expenses								
32	Actuarial services	600,000	550,000	150,000	(450,000)	(75.0%)	(400,000)	(72.7%)
33	Accounting services	59,000	59,000	59,000	-	0.0%	-	0.0%
34	Independent audit	149,500	149,500	152,500	3,000	2.0%	3,000	2.0%
35	Legal fees	2,514,800	1,610,000	2,000,000	(514,800)	(20.5%)	390,000	24.2%
36	Legislative consultants	324,000	307,000	271,000	(53,000)	(16.4%)	(36,000)	(11.7%)
37	Public relations	290,000	245,000	-	(290,000)	(100.0%)	(245,000)	(100.0%)
38	Pension administration software & WMS	271,000	250,000	291,000	20,000	7.4%	41,000	16.4%
39	Business continuity	13,500	15,000	13,500	-	0.0%	(1,500)	(10.0%)
40	Network security	35,000	15,000	33,000	(2,000)	(5.7%)	18,000	120.0%
41	Disability medical evaluations	12,500	7,000	30,000	17,500	140.0%	23,000	328.6%
42	Elections	10,000	32,000	-	(10,000)	(100.0%)	(32,000)	(100.0%)
43	Miscellaneous professional services	122,000	108,000	18,300	(103,700)	(85.0%)	(89,700)	(83.1%)
	Total without Investment Expenses not previously budgeted for	*11,303,323*	*9,640,100*	*9,147,894*	*(2,155,429)*	*(19.1%)*	*(492,206)*	*(5.1%)*
	Gross Total	11,303,323	29,243,100	27,529,894	N/A	N/A	(1,713,206)	(5.9%)
	Less: Allocation to Supplemental Plan Budget*	75,246	251,608	236,867	N/A	N/A	(14,740)	(5.9%)
	Total Combined Pension Plan Budget	**11,228,077**	**28,991,492**	**27,293,027**	**N/A**	N/A	**(1,698,466)**	(5.9%)

** Allocation to Supplemental is based on JPM allocation between accounts as of 9/30/17 of .8604%*

Management Fee Budget - 2018

Asset Category	Asset Class	2018 Management Fee Budget*	Fee as a % of Market Value
Equity	Global Equity	$ 2,400,000	0.57%
	Emerging Markets Equity	364,000	0.70%
	Private Equity	4,145,000	1.54%
Fixed Income	Liquid Fixed Income^	1,973,000	0.48%
	Private Debt	207,000	1.61%
GAA	Risk Parity	837,000	0.84%
	GTAA	287,000	1.00%
	Absolute Return	1,356,000	3.80%
Real Assets	Natural Resources	1,726,000	0.98%
	Infrastructure	1,378,000	2.10%
	Real Estate	2,848,000	0.57%
	TOTAL	**$ 17,522,000**	**0.83%**

* - The Management Fee Budget does not include any carried interest or profit sharing paid to the General Partner ("GP"), which is typical in private equity and debt structures. The budget includes management fees, performance/incentive fees & disposition fees paid to the fiduciary investment manager, as well as the base management fees payable to the GP.

^ - Liquid Fixed Income combines the following asset classes for presentation purposes due to their similar fee levels: Short-Term Core Bonds, Global Bonds, High Yield, Bank Loans & Emerging Markets Debt.

Significant Budget Changes - 2018

	Item	2017 Budget	2017 Projected Actual**	2018 Budget	$ Change vs Prior Yr Budget	% Change vs Prior Yr Budget	$ Change vs PY Proj Actual	% Change vs PY Proj Actual	Explanation
	INCREASES:								
1	Information technology projects	20,000	3,000	75,000	55,000	275.0%	72,000	2400.0%	Network storage device is end of life and requires replacement.
2	IT subscriptions/services/licenses	122,950	84,000	147,100	24,150	19.6%	63,100	75.1%	Increase in cost for proposed file sharing software for Board materials.
3	Employment expenses	3,009	450	151,125	148,116	4922.4%	150,675	33483.3%	Potential use of search firms for hiring of vacant positions.
4	Liability insurance	447,667	440,000	510,000	62,333	13.9%	70,000	15.9%	Increase due to market factors, as well as claims experience for fiduciary coverage.
	REDUCTIONS:								
5	Salaries and benefits	4,199,476	4,190,000	3,728,000	(471,476)	(11.2%)	(462,000)	(11.0%)	Due to payment of one-time employment contract related amounts in 2017.
6	Conference/training registration/materials - Board	51,615	10,000	14,400	(37,215)	(72.1%)	4,400	44.0%	Reduction in anticipated Board participation in conferences.
7	Travel - Board	128,335	15,000	25,000	(103,335)	(80.5%)	10,000	66.7%	Reduction in anticipated Board participation in conferences.
8	Legal fees	2,514,800	1,610,000	2,000,000	(514,800)	(20.5%)	390,000	24.2%	Legal fees in 2017 were partially offset by insurance recoveries totalling $940K. Total legal expenses are estimated to decrease in 2018.
9	Public relations	290,000	245,000	-	(290,000)	(100.0%)	(245,000)	(100.0%)	Staff is proposing the hiring of an internal communications position in 2018.
10	Miscellaneous professional services	122,000	108,000	18,300	(103,700)	(85.0%)	(89,700)	(83.1%)	In 2017, the budget included leasing commissions for 4100 Harry Hines space available for lease. The space is now fully leased.
11	Actuarial services	600,000	550,000	150,000	(450,000)	(75.0%)	(400,000)	(72.7%)	In 2017, the volume of actuarial services were driven by Plan changes.
12	Building expenses, incl capitalizable fixed assets	599,266	450,000	337,337	(261,929)	(43.7%)	(112,663)	(25.0%)	In 2017,actual tenant improvements for leased space were less than anticipated. Also, continuous cost cutting measures with service provider contracts.
13	Investment consultant and reporting	575,000	489,000	505,000	(70,000)	(12.2%)	16,000	3.3%	Reduction vs PY budget is due to reduced total average NAV.
14	Bank/security custodian services	328,600	262,000	260,000	(68,600)	(20.9%)	(2,000)	(0.8%)	Reduction vs PY budget is due to reduced number of assets and accounts. Anticipated to be in line with actual 2017 fees.

DISCUSSION SHEET

ITEM #C6

Topic: **Ethics Policy review**

Discussion: Section 3.01(r) of Article 6243a-1 requires the Board to adopt a code or codes of ethics consistent with Section 825.212 of the Texas Government Code. Section 1.54(a)(1) of HB 3158 requires the Board to adopt the code or codes no later than January 1, 2018.

Staff is presenting for the Board's review and comment two draft policies (Ethics Policy and Contractor's Statement of Ethics) intended to comply with this requirement.

DISCUSSION SHEET

ITEM #C7

Topic: **Governance and Board Conduct Policy review**

Discussion: Section 1.53(g) of HB 3158 requires the Board to, not later than the 90th day after the date all trustees have been appointed or elected "…vote on and, if the board determines it is appropriate, amend the existing rules relating to the governance and conduct of the board."

Staff is presenting for the Board's review and comment a draft Governance and Board Conduct Policy.

DISCUSSION SHEET

ITEM #C8

Topic: **Significant Professional Service Advisors and Providers**

Discussion: Staff will review significant professional service advisors and providers (Service Providers) of the Board. In 2015, the Board gave direction to conduct a competitive selection process for Service Providers every five years unless the Board explicitly waives or extends the requirement. A phased-in approach was put in place by the Board for existing Service Providers.

Staff Recommendation: Service Providers in this context includes the actuary, auditor, legal counsel (fiduciary and tax), investment and legislative consultants.

Significant Professional Service Advisors and Providers

November 9, 2017

Significant Professional Service Advisors and Providers

Service	Firm	Initial/Last Renewal	Fees
Actuarial	Segal	2016 - Term ends 12-31-2020, termination with 30 days notice even prior to 12-31-2020	$78,000 (2018 annual valuation, GASB 67 & 68, other services extra) 2017 estimate: $550k, 2018 Budget request: $ 150k.
Audit	BDO USA	2014/2017, annual renewal	$147,000 - 2017 plus $2,500 expenses
Legal - Fiduciary	Jackson Walker	August 2016 - Termination at any time	Hourly Rates
Legal – Tax Counsel	Ice Miller	July 2016 - Termination at any time	Hourly Rates

Significant Professional Service Advisors and Providers

Service	Firm	Initial/Last Renewal	Fees
General Investment Consulting	NEPC	2006/2016, termination with 30 days notice	1.5 basis points on the first $1 billion, 1.2 basis points above $1 billion. Excludes private assets and real estate, natural resources. 2017 estimate $282k.
Alternative Strategies Advisor	NEPC	2015, termination with 30 days notice	Added Alternative Strategies in 2015, for an additional $200,000. Scope of services expanded – no prior advisor offering a similar scope of services.
Real Estate & Natural Resources Advisor	NEPC	2016, termination with 30 days notice	Upon the termination of prior real estate consultant, NEPC added Real Estate and Natural Resources consulting for a fee of $100k and lowered the fee for Alternative Strategies to $100k. Fees to be revisited in 2018.

Significant Professional Service Advisors and Providers

Service	Firm	Initial/Last Renewal	Fees
Legislative Consulting	Locke Lord	2000/12-2016 – Expires 12-31-17, termination at any time	$162,000 ($13,500 per month), expenses capped at $250 per month
Legislative Consulting	Hillco Partners	1999/12-2016 - Expires 11-30-18, termination with 30 days notice	$120,000-$150,000 plus expenses. ($15,000 per month during January-June '17, $10,000 per month non-legislative session months. Expenses capped at $500 non-legislative session months, $1,000 per month legislative session months.

Other Professionals Providing Services

- Custodian Bank- JPMorgan Chase Bank, Hired 2002, numerous contract amendments since 2002, automatic renewal annually. Cancellable upon 15 day notice of either party. Annual fee estimate for 2017 is $257K.
- Investment Accounting Firm- STP Investment Services (formerly Financial Control Systems, Inc.) Annual fee $59K. Cancellable upon 60 day notice of either party.
- Public Relations - Fleishman Hilliard, Hired 2017, monthly maximum, billed only when using services, no minimum fee, 15 day cancellation.

2015 Board Direction

- Advisors to the Board – Not less than every five years, on a rotational basis, the Board shall conduct a competitive selection process for each of the significant professional service providers to the Board.
  - Actuary
  - Auditor
  - Legal – Fiduciary and Tax Counsel
  - Investment consultants
  - Legislative consultants
- The initial review requirement was to implement in a phased timeframe.
- This requirement may be waived or timeframe extended with explicit action of the Board.

2015 Board Direction

- Other Professionals Providing Service – A competitive selection for these services will be conducted as needed and as recommended by staff on a case-by-case basis.

2015 Board Direction and Status

- Legal – Q1 2016: Completed Q3 2016
- Real Estate Consultant – Q3 2016: Completed Q1 2016. Terminated existing real estate consultant, NEPC assumed the role at the same time.
- General Investments – Q2 2017 – postponed due to Board Change
- Actuary – Q3 2017: Completed Q1 2017
- Legislation State & Federal – Q1 2018
- Auditor – Q3 2018

DISCUSSION SHEET

ITEM #C9

Topic: **Trustee Education Requirements**

Discussion: Staff will discuss Trustee education and training requirements.

Education Requirements for Trustees

November 9, 2017

Open Government Training

- Open Meetings Act and Public Information Act training
- Required by Texas Government Code 551.005 and 552.012
- 2 online videos on the Attorney General's website
  https://texasattorneygeneral.gov/og/open-government-training
- Training must be complete within 90 days of the beginning of the Trustee's term
- After the completion of each video, please print the certificate of completion and provide it to DPFP to keep on file
- No cost

Minimum Educational Training Requirements (METs)

- Required by the Texas Government Code
- Core training must be completed within 1 year of the start of the Trustee's service
  - 7 hours in the areas of Fiduciary Matters, Governance, Ethics, Investments, Actuarial Matters, Benefits Administration, and Risk Management.
  - The 7 hours must include training in all of the 7 content areas. No less than half a credit hour and no more than 2 credit hours may be earned in any one core content area.
- Continuing Education is required every two years, beginning after the first year
  - 4 hours must be completed every two years in the Core subject areas listed above or non-core areas which include: Compliance, Legal and Regulatory Matters, Pension Accounting, Custodial Issues, Plan Administration, Texas Open Meetings Act, and Texas Public Information Act.

Minimum Educational Training Requirements (METs) - continued

- Options for METs training:
  - completing training courses from an accredited sponsor
    - TEXPERs & other sponsors
    - TEXPERs has offered to provide a special training for the new Board
  - attending training that has been approved to receive credit with the Individual Course Approval Application (ICAA). The ICAA may be used by either the sponsoring organization or by the system on the behalf of the trustees or system administrator.
  - Online classes offered by the Pension Review Board, no cost

HB 3158 Required Training

Training program required annually – Section 3.013, must include:

(1) the law governing the pension system's operations;

(2) the programs, functions, rules, and budget of the pension system;

(3) the scope of and limitations on the rulemaking authority of the board;

(4) the results of the most recent formal audit of the pension system;

(5) the requirements of:

(A) laws relating to open meetings, public information, administrative procedure, and disclosing conflicts of interest; and

(B) other laws applicable to a trustee in performing the trustee's duties, including the board's fiduciary duties

HB 3158 Required Training - continued

(6) the code or codes of ethics adopted under Section 3.01(r) and any applicable ethics policies adopted by the Texas Ethics Commission; and

(7) financial training regarding the risks of investing in alternative investments.

The executive director shall create a training manual that includes the information required. The executive director shall distribute a copy of the training manual annually to each trustee. On receipt of the training manual, each trustee shall sign and submit to the executive director a statement acknowledging receipt of the training manual.

Recommendations

- Complete the Open Government training online within the required 90 days
- METs training - either select a date to have TEXPERs provide the required Core 7 hour training to DPFP for the full Board, Trustees individually complete the Pension Review Board online course or individual Trustees attend sponsored training courses
- HB 3158 Training – address this requirement in the spring/summer of 2018.
- Revise the Education and Travel Policy and Procedure to address the Board approval and reporting protocol

DISCUSSION SHEET

ITEM #C10

Topic: **Board approval of Trustee education and travel**

a. Future Education and Business-related Travel
b. Future Investment-related Travel

Discussion:

a. Per the Education and Travel Policy and Procedure, planned Trustee education and business-related travel and education which does not involve travel requires Board approval prior to attendance.

Attached is a listing of requested future education and travel noting approval status.

b. Per the Investment Policy Statement, planned Trustee travel related to investment monitoring, and in exceptional cases due diligence, requires Board approval prior to attendance.

There is no future investment-related travel for Trustees at this time.

Future Education and Business Related Travel
Regular Board Meeting – November 9, 2017

ATTENDING APPROVED

1. **Conference:** **NCPERS Legislative Conference**
   Dates: January 28-30, 2018
   Location: Washington, DC
   Est. Cost: TBD

2. **Conference:** **TEXPERS - Basic Trustee Training Class**
   Dates: April 14-15, 2017
   Location: South Padre Island, TX
   Est. Cost: TBD

3. **Conference:** **TEXPERS Annual Conference**
   Dates: April 15-18, 2017
   Location: South Padre Island, TX
   Est. Cost: TBD

4. **Conference:** **PRB: MET Online Core Training: Actuarial Matters**
   Dates: Online - Anytime
   Location: http://www.prb.state.tx.us

5. **Conference:** **PRB: MET Online Core Training: Benefits Administration**
   Dates: Online - Anytime
   Location: http://www.prb.state.tx.us

6. **Conference:** **PRB: MET Online Core Training: Ethics**
   Dates: Online - Anytime
   Location: http://www.prb.state.tx.us

7. **Conference:** **PRB: MET Online Core Training: Fiduciary Maters**
   Dates: Online - Anytime
   Location: http://www.prb.state.tx.us

8. **Conference:** **PRB: MET Online Core Training: Governance**
   Dates: Online - Anytime
   Location: http://www.prb.state.tx.us

9. **Conference:** **PRB: MET Online Core Training: Risk Management**
   Dates: Online - Anytime
   Location: http://www.prb.state.tx.us

DISCUSSION SHEET

ITEM #C11

Topic: **Unforeseeable Emergency Requests from DROP Members**

Portions of the discussion under this topic may be closed to the public under the terms of Section 551.078 of the Texas Government Code.

Discussion: The Executive Director is seeking Board direction on an Unforeseeable Emergency Request which relates to replacement of personal property as a result of a natural disaster.

The DROP Unforeseeable Emergency Policy allows for a DROP distribution for the repair of damage to a DROP account holder's primary residence not covered by insurance as the result of a natural disaster. The Policy does not directly address the replacement of personal property (which was located in the primary residence in the case of this request) due to damage as a result of a natural disaster.

Staff Recommendation: To be provided at the meeting.

DISCUSSION SHEET

ITEM #C12

Topic: **Legal issues**

Portions of the discussion under this topic may be closed to the public under the terms of Section 551.071 of the Texas Government Code.

a. Potential claims involving fiduciaries and advisors
b. DPFP v. The Townsend Group and Gary Lawson
c. Eddington et al. v. DPFP
d. Rawlings v. DPFP
e. DPFP v. Columbus A. Alexander III
f. Degan et al. v. DPFP (Federal suit)
g. HB 3158

Discussion: Counsel will brief the Board on these issues.

DISCUSSION SHEET

ITEM #C13

Topic: **Quarterly financial reports**

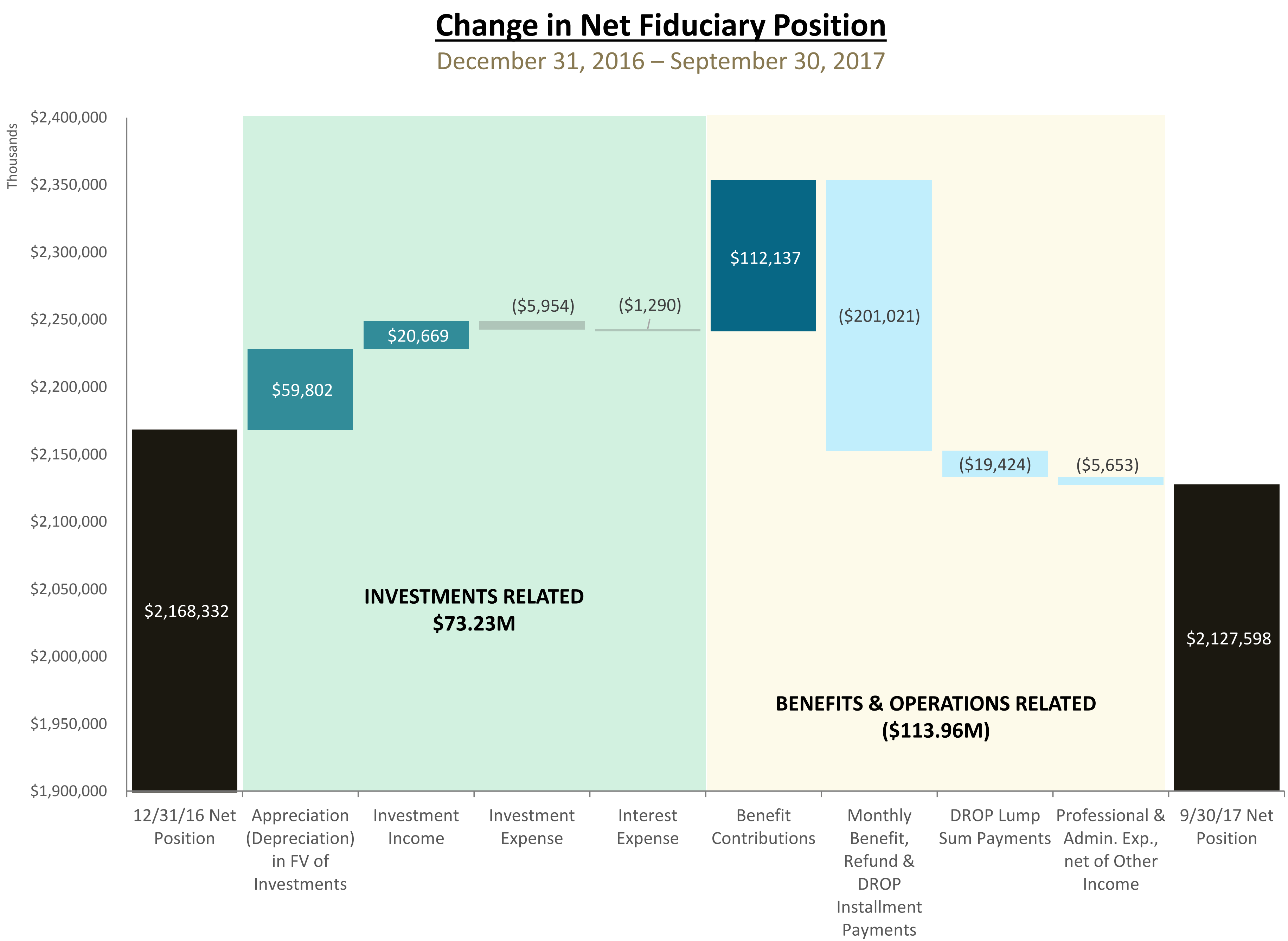
Discussion: The Chief Financial Officer will present the third quarter 2017 financial statements.

DALLAS POLICE & FIRE PENSION SYSTEM
Combined Statements of Fiduciary Net Position

	9/30/2017 (unaudited)	12/31/16 (audited)
Assets		
Investments, at fair value		
Short-term investments	$ 194,007,725	$ 7,153,792
Fixed income securities	283,585,812	269,888,410
Equity securities	386,644,086	154,659,095
Real assets	838,002,157	1,128,965,069
Private equity	228,741,775	264,779,617
Alternative investments	139,336,231	134,898,311
Forward currency contracts	(85,533)	(286,788)
Total investments	2,070,232,253	1,960,057,506
Invested securities lending collateral	15,505,843	21,671,395
Receivables		
City	4,410,395	1,288,353
Members	1,396,189	279,469
Interest and dividends	2,763,312	2,944,626
Investment sales proceeds	33,356,898	24,710,879
Other receivables	156,290	154,528
Total receivables	42,083,084	29,377,855
Cash and cash equivalents	38,706,842	326,784,552
Prepaid expenses	493,222	459,784
Capital assets, net	12,771,769	12,041,464
Total assets	2,179,793,012	2,350,392,557
Liabilities		
Notes payable	-	130,000,000
Payables		
Securities purchased	33,717,511	24,352,550
Securities lending obligations	15,505,843	21,671,395
Accounts payable and other accrued liabilities	2,971,353	6,036,482
Total liabilities	52,194,707	182,060,427
Net position		
Net investment in capital assets	12,771,769	12,041,464
Unrestricted	2,114,826,536	2,156,290,666
Net position held in trust - restricted for position benefits	$ 2,127,598,305	$ 2,168,332,130

DALLAS POLICE & FIRE PENSION SYSTEM
Combined Statementsof Changes in Fiduciary Net Position

	9 Months Ended 9/30/2017 *(unaudited)*	9 Months Ended 9/30/2016 *(unaudited)*
Contributions		
City	$ 91,254,840	$ 91,923,499
Members	20,881,704	19,430,163
Total contributions	112,136,544	111,353,662
Investment income		
Net appreciation (depreciation) in fair value of investments	59,802,352	125,098,845
Interest and dividends	20,590,071	43,182,412
Total gross investment income	80,392,423	168,281,257
less: investment expense	(5,953,622)	(7,169,036)
Net investment income	74,438,801	161,112,221
Securities lending income		
Securities lending income	145,083	537,591
Securities lending expense	(66,057)	(211,483)
Net securities lending income	79,026	326,108
Other income	1,856,377	136,662
Total additions	188,510,748	272,928,653
Deductions		
Benefits paid to members	217,694,352	547,614,960
Refunds to members	2,750,720	2,095,361
Interest expense	1,290,356	3,708,575
Professional and administrative expenses	7,509,145	7,172,040
Total deductions	229,244,573	560,590,936
Net decrease in net position	(40,733,825)	(287,662,283)
Net position		
Beginning of period	2,168,332,130	2,699,581,009
End of period	$ 2,127,598,305	$ 2,411,918,726


Change in Net Fiduciary Position
December 31, 2016 – September 30, 2017
Thousands
$2,400,000
$2,350,000
$2,300,000
$2,250,000
$2,200,000
$2,150,000
$2,100,000
$2,050,000
$2,000,000
$1,950,000
$1,900,000
$2,168,332
$59,802
$20,669
($5,954)
($1,290)
$112,137
($201,021)
($19,424)
($5,653)
$2,127,598
INVESTMENTS RELATED
$73.23M
BENEFITS & OPERATIONS RELATED
($113.96M)
12/31/16 Net Position
Appreciation (Depreciation) in FV of Investments
Investment Income
Investment Expense
Interest Expense
Benefit Contributions
Monthly Benefit, Refund & DROP Installment Payments
DROP Lump Sum Payments
Professional & Admin. Exp., net of Other Income
9/30/17 Net Position

DISCUSSION SHEET

ITEM #C14

Topic: **Requirement for Two Annual Public Meetings**

Discussion: Section 3.01(j-9) of Article 6243a-1 states "At least twice each year, the board shall have a meeting to receive public input regarding the pension system and to inform the public about the health and performance of the pension system…"

Staff will discuss this requirement with the Board.

Staff Recommendation: **Hold** the two required meetings in February and August of each year in conjunction with the Regular and Supplemental Board meetings. The required public meeting will follow the Regular and Supplemental meetings and will provide an opportunity for the public to provide input to the Board.

DISCUSSION SHEET

ITEM #D1

Topic: **Reports and concerns of active members and pensioners of the Dallas Police and Fire Pension System**

Discussion: This is a Board-approved open forum for active members and pensioners to address their concerns to the Board and staff.

DALLAS POLICE & FIRE PENSION SYSTEM

DISCUSSION SHEET

ITEM #D2

Topic: **Executive Director's report**

a. Open Government Training
b. Associations' newsletters
- NCPERS Monitor (October 2017)
- NCPERS PERSist (Fall 2017)

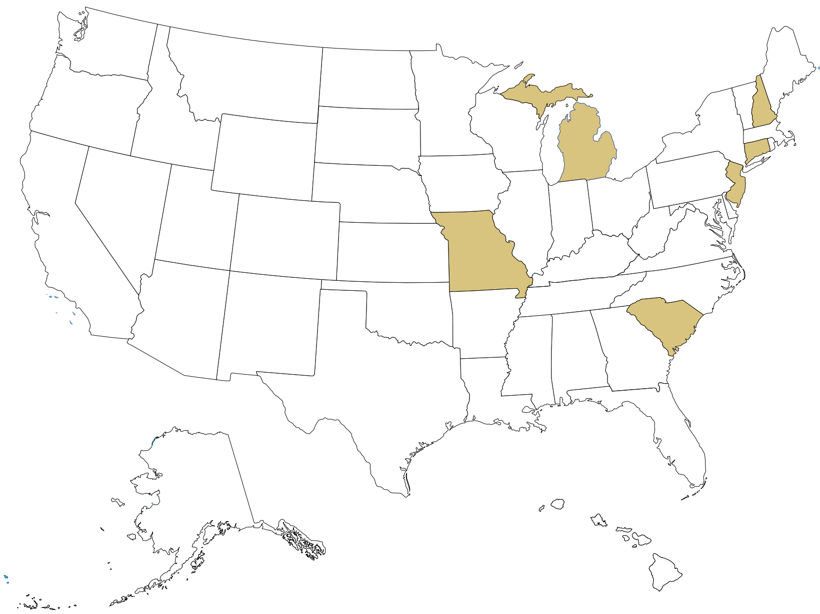
c. Employee recognition – Third Quarter 2017
- Employee Service Award
- Employee of the Quarter award

Discussion: The Executive Director will brief the Board regarding the above information.

THE NCPERS
MONITOR
The Latest in Legislative News
OCTOBER 2017

In This Issue

State Update



Since our June installment, many of the harmful pension alteration bills have not moved. Bills in Colorado, Connecticut, Maryland, Nebraska, Nevada, North Carolina, Oklahoma, Oregon, Virginia and West Virginia, have all stalled or died in committee. That being said, there are still harmful bills that NCPERS is paying close attention to such in as Michigan and South Carolina. Details on specific state legislation are as follows:

Connecticut: On July 31, 2017, the Senate passed Senate Resolution 51, which approved a new public employee's labor contract that will save the state a projected $1.2 billion in mostly pension concessions. The deal, sponsored by Senator (Sen.) Martin Looney (D), extends pension and healthcare provisions through 2027, which will save $24 billion over 20 years. It brings higher employee pension contributions, ties the annual cost-of-living adjustment (COLA) to the Consumer Price Index, and wages are frozen for three years until 2019.

Michigan: Governor Rick Snyder (R) signed Senate Bill (SB) 401 on August 16, 2017. The bill, sponsored by Senator Phillip Pavlov (R), will default new public school employees into a 401(k) style plan and offer a choice of a new combination plan that includes cost sharing between employers and employees. In addition, Gov. Snyder has made municipal

CONTINUED ON PAGE 5

Inspired by Secure Choice, States and Cities Maintain Momentum

Variations on the Secure Choice model for retirement savings are continuing to gain momentum, with Seattle emerging as the latest hotspot, Oregon expanding its pilot program, and New Mexico sounding out ideas.

On September 25, one week into his tenure as Seattle's new mayor, Tim Burgess put a stake in the ground for workplace retirement programs. Unveiling his fiscal year 2018 city budget, Mayor Burgess threw his support behind legislation to establish a Seattle Retirement Savings Plan for workers who don't have access to a workplace retirement plan. The initiative would provide approximately 200,000 Seattle workers –40% of the city's private sector employees – with a path to save for retirement.

"It'll be a huge win for workers and for business and it makes sense for economic stability. People who have adequate resources during retirement participate in the economy more than people who are struggling to make ends meet," Mayor Burgess told the *Seattle Times.*

The initial steps will include a market feasibility study and a legal analysis of the proposed savings plan, the Mayor's Office announced.

The city program is expected to dovetail with a statewide initiative, the Washington State Small Business Retirement Marketplace. Aimed at small businesses, the state marketplace provides a web portal and search tool to connect businesses with financial services providers.

Oregon, meanwhile, is building on its status as the first state in the nation to create an auto-IRA workplace retirement program for the private sector.

It was my pleasure last month to host Lisa Massena, executive director of OregonSaves in an NCPERS Facebook Live interview.

"It'll be a huge win for workers and for business and it makes sense for economic stability. People who have adequate resources during retirement participate in the economy more than people who are struggling to make ends meet."

Massena noted that the small pilot group of workers that went live with the program on July 1 had amassed $24,000 in savings in just two months. An expanded pilot group will be starting by October 1, she noted.

OregonSaves is expected to be available to more than 1 million people – more than half of Oregon's 1.8 million workers who lack workplace retirement plans, Massena said. The results so far, though on a small scale, "show the power" of having a retirement savings program available at work, she said.

By taking the time to ramp up, OregonSaves is fine-tuning its procedures and communications, Massena said. "We are finding you can't make anything too obvious" in the enrollment process, she said, underscoring that crisp, clean communications are key. It takes employers about 45 minutes to become involved in program, she added, and more than 200 are already online.

CONTINUED ON PAGE 5

Unified Framework for Tax Reform

By Tony Roda

Photo Illustration © 2017, Depositphotos

On September 27, the Trump Administration and the Republicans on the House Ways and Means and Senate Finance Committees released a unified framework on tax reform. The document, while still extremely short on details, particularly negative details, will be the starting point for a legislative process that will take many months.

Many observers foresee serious pitfalls as the committees begin to write the actual legislation. One major question is whether Congress will attempt to make the bill revenue neutral or pay for part or most of it through high economic growth assumption rates that lift revenue projections. A revenue neutral bill necessarily means that many current deductions and credits, all of which are cherished by their beneficiaries, will have to be eliminated. This, of course, increases the political pain involved in supporting the overall bill. The flip side is that, instead of eliminating more deductions and credits, Congress is not able to make the tax rate reductions as significant.

Another major question is whether the Democrats, who are in the minority in both chambers of Congress, will be allowed a seat at the table when the bill is being written. Most Democrats on Capitol Hill are skeptical that they will be allowed to have any real input into the details of the tax legislation. However, Sen. Joe Donnelly (D-IN) was alongside President Trump in Indianapolis the day the framework was released. Also, the President has been blunt in his criticism of the GOP Congressional Leadership's unsuccessful efforts to pass legislation to repeal and replace the Affordable Care Act. In contrast, the President was ecstatic with the favorable media attention he received after agreeing with Minority Leaders Nancy Pelosi (D-CA) and Chuck Schumer (D-NY) on a debt ceiling, hurricane relief and stop-gap funding bill.

Regarding retirement policy, the upshot of the unified framework is the few words that follow: *The framework retains tax benefits that encourage work, higher education and retirement security. The committees are encouraged to simplify these benefits to improve their efficiency and effectiveness. Tax reform will aim to maintain or raise retirement plan participation of workers and the resources available for retirement.*

Of course, the devil will be in the details and the public pension community long has been on alert of some potential challenges ahead. First, Senate Finance Committee Chairman Orrin Hatch's (R-UT) annuity accumulation retirement plan proposal (included in S. 2381, 114th Congress) could be a part of a tax reform bill. This federal enabling legislation would permit state and local plan sponsors to establish annuity accumulation plans. The plans would provide for the purchase of single-year, fixed rate annuity contracts for each employee. Employer contributions are the only funding stream for the plan. In practice, if a plan sponsor went down this path, they would likely freeze their existing defined benefit plan.

Proponents of the Public Employee Pension Transparency Act (PEPTA), including Chairman Hatch and House Ways and Means Committee member Rep. Devin Nunes (R-CA), may advocate for its inclusion in a tax reform bill. PEPTA would require for the first time that state and local governmental plan sponsors report their funded status to the federal Treasury Department. The reports would be based on two different sets of numbers: (1) the plan's current assumed rate of return; and (2) a Treasury bond yield curve. The latter method will result in a significantly lower funding level on paper as well as more negative media attention on the funded status of public plans.

House Republicans are also considering making it a requirement that all new contributions to defined contribution plans (e.g., IRAs, 401(k), 457(b) and 403(b) plans) be made under the rules related to Roth accounts. Those rules require that contributions be made with after-tax dollars but are tax-free at distribution. Because a full or partial Roth mandate would accelerate taxable income into the 10-year federal budget window, the proposal would generate new revenues to offset tax rate reductions. This proposal warrants attention by our community.

CONTINUED ON PAGE 6

Pensions Are Healthier Than Many Think, Brown University Scientist Tells Conference

Brown University data scientist Tom Sgouros is taking aim at the conventional wisdom that pension funds should be fully funded to be considered healthy.

Photo Illustration © 2017, Depositphotos

Funding ratios are too imprecise to be a useful measure of the capacity of a system to fulfill its obligations, because many assumptions are built in, Sgouros said in a speech to the NCPERS Public Pension Funding Forum, which was held September 10-12 in San Francisco.

"Why would you take a number as imprecise as that and combine it with numbers that you can know to a much higher degree of certainty, such as accounts payable, and expect to get a meaningful number?" he asked.

"In data science, imprecision is infectious," Sgouros added. "If you want inaccurate financial reports, this is an ideal way to get them."

Sgouros argued that pension funds are healthier than is generally believed. "Lots of systems are technically underfunded yet meeting their obligations," he said. However, he added, "money's coming in, money's going out, and everybody's getting paid," even with funding levels in the 40% or 50% range.

He criticized the practice of calculating unfunded liability as "an odd way to measure the health of a system if they're not planning to close it." Sgouros noted that pension plans, at their inception, started out with a large unfunded liability. Rules that require pension funds to become fully funded as a hedge against the risk of liquidation are "a waste of resources," because states and localities don't go out of business.

Likewise, he said, focusing on the present value of pension assets is misguided. "The last penny of a pension debt is due when the youngest current employee dies," Sgouros said.

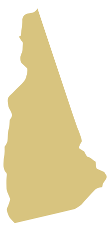
Sgouros also described a running debate over the appropriate rate of returns for public pensions as "unnecessarily heated." There is simply no way to know in advance what the ultimate rate of return will be. We do know that using too low a rate creates political pressure to reduce benefits, he added.

Videos of comments delivered by Sgouros and other speakers at the Public Pension Funding Forum are available on NCPERS's Facebook page. ◆

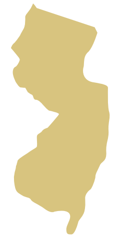
STATE UPDATE CONTINUED FROM PAGE 1

pensions one of his fall session priorities. The Responsible Retirement Reform for Local Government Task Force, (Gov. Snyder's task force on retirement reform for local government) released a report in the middle of July, calling for greater reporting and transparency, development of a fiscal stress system, and new funding requirements for long-term stability. Stay tuned for what this report could mean for Michigan pensions.

Missouri: Gov. Eric Greitens (R) signed SB 62 on July 14, 2017. The bill, sponsored by Sen. Daniel Hegeman (R) and Rep. Rusty Black (R), re-lowers the vesting period for state workers to 5 years. The bill also authorized the Missouri State Employees' Retirement System (MOSERS) to offer a Buyout Program to 17,500 beneficiaries. SB 62 aims to save $8 billion over the long term by offering to pay out a percentage of a pension's value over time and avoid administrative fees.



New Hampshire: As previously reported, House Bill (HB) 631, introduced by Rep. Neal Kurk (R) on January 5, would create a cash balance retirement plan for new hires and non- vested employees. The bill was retained in the Executive Departments and Administration Committee on February 8, but in August it retained a bill subcommittee work session.



New Jersey: Senate bill 3040 was introduced with bi-partisan support on February 28, 2017; the bill will transfer management of the Police & Fire Retirement System (PFRS) to the board of PFRS. The bill passed both chambers but was vetoed by Gov. Chris Christie (R) on May 8. Gov. Christie said he would allow lawmakers to make revisions, including a cap on sick time payouts.

South Carolina: As previously reported, Assembly 13 was signed by Gov. Henry McMaster (R) on April 25. The bill, which was approved by large bi-partisan majorities in the House and Senate, increases government employees' contributions from 8.66 percent to 9 percent and increases employer contributions by 1 percent annually until 2022. The state government will also contribute an additional 1 percent. However, Gov. McMaster does not believe these reforms go far enough. He wants to introduce a 401 (k) style plan to new state employees and increase the retirement age for current employees. At the end of August, Gov. McMaster sent a letter calling for these changes to a special 12-member legislative committee that is reviewing the future of the state's retirement system.

Stay tuned and visit www.NCPERS.org for more information on upcoming state pension reform battles. You can visit the legislation maps on www.NCPERS.org to view our latest membership feature. As always, if your state is facing pension reform efforts and you would like NCPERS' help, please let us know. ◆

MAINTAIN MOMENTUM CONTINUED FROM PAGE 2

I also had the opportunity on September 7 to present at a meeting organized by the New Mexico Retirement Income Security Task Force. Led by State Treasurer Tim Eichenberg, the task force has the statutory role of studying the preparedness of New Mexicans to retire in a financially secure manner, with a focus on private-sector workers with limited or no access to workplace retirement solutions. At held its first organizational meeting on June 29.

My testimony focused on the status of auto-IRA programs in California, Illinois, Oregon and Vermont, and featured a discussion of NCPERS's SecureChoice 2.0 white paper.

New Mexico has a compelling case for creating workplace retirement programs for the private sector. A staggering 62% of New Mexico's private-sector workers – 336,000 people – don't have access to a plan. And a third of New Mexicans age 65 or older rely on Social Security for 90% or more of their income.

We are in strong company as we continue promoting retirement security for all. Lisa Massena from OregonSaves was also on hand in New Mexico, as were numerous representatives of AARP at both the federal and state levels. ◆

TAX REFORM CONTINUED FROM PAGE 3

Finally, during a recent hearing, Chairman Hatch promoted his corporate integration tax reform proposal, which is designed to eliminate the double taxation of corporate income. Under current tax law, corporate earnings are taxed at the corporate entity level (1st level of taxation) and then if those earnings are distributed as dividends to shareholders, those dividends are taxable income to the recipient (2nd level of taxation).

Many have concluded that this double taxation leads to distortions in business decision-making, such as corporations relying on debt financing, which is tax-favored, and a shift to non-corporate business forms, such as S corporations, partnerships and sole proprietorships, which do not have entity level tax.

Depending on how Chairman Hatch structures this provision, it may have a significant impact on pension funds, endowments and other non-taxable entities that own equity shares in corporations and receive dividend income from those investments.

Under the approach currently being contemplated by Chairman Hatch, corporate earnings distributed as dividends would be taxed one time at the shareholder level. A tax withholding scheme would be created whereby the corporation would withhold tax from the dividend. The shareholder would then receive the net amount as a dividend. The proposal does not differentiate between tax-paying and non-taxable recipients of dividends. Since non-taxable entities, such as pension plans, do not currently pay tax on dividend income, they would simply receive lower dividend distributions.

Please be assured that NCPERS will monitor developments in these areas very closely as the legislative process on tax reform process evolves. ◆

__Tony Roda__ is a partner at the Washington, D.C. law and lobbying firm Williams & Jensen, where he specializes in legislative and regulatory issues affecting state and local pension plans. He represents NCPERS and individual pension plans in California, Ohio, Tennessee and Texas.

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2018 Conferences

January

Legislative Conference
January 28 – 30, 2018
Capital Hilton
Washington, DC

May

Trustee Educational Seminar (TEDS)
May 12 – 13, 2018
Sheraton Hotel
New York, NY

Annual Conference & Exhibition
May 13 - 16, 2018
Sheraton Hotel
New York, NY

The Voice for Public Pensions

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PERSist

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Message from the President

Daniel Fortuna
NCPERS President

NCPERS has concluded another successful Public Safety Conference! This year's conference took place October 1-4 in San Antonio, Texas, at the Hyatt Regency San Antonio. This program, attended by 300 public safety officials, trustees, and administrators, provided participants with important information and tools to help them deal with the unique needs and aspects of public safety plans.

Dr. Steven R. Malin of Allianz Global Investors opened the conference with a discussion on the economic outlook under Trump, the Fed and Congress. If you missed this presentation, or would like more information, we will be hosting a webinar with Dr. Malin on Tuesday, October 31 at 1:00pm ET. You can register for that webinar here.

NCPERS board member, Dan Givens, along with CorPERS member and executive board advisor, Don Heilman of Gallagher Benefit Services, led a discussion on the evolving benefits landscape for active and retirement public safety officers. You can view their presentation through Facebook Live here. The morning continued with presentations from CorPERS members J.P. Morgan on the shifting landscape in private credit and Foster & Foster on amortization payments.

The first day concluded with two presentations from Robert Klausner, of Klausner, Kaufman, Jensen & Levinson. In the first presentation he joined Jeffery Weiler, executive director of the Fairfax County Retirement Systems, for a panel discussion on headlines and trends in disability cases. The final presentation of the day was Klausner's legal update. You can view both presentations on Facebook Live here.

The agenda for the second day was equally informative. The program began with a presentation on alternatives for managing unfunded liability from Eric Atwater of Aon Hewitt, a CorPERS member. The morning continued with presentations on the benefits of global listed infrastructure with John Creswell of CorPERS member Duff & Phelps Investment Management. Anthony Roda of Williams & Jensen updated members on federal legislative and regulatory issues. Jennifer Mink of Investment Performances Services, once again led an engaging discussion on opportunistic investments. Ronald King, general counsel for the Police and Fire Retirement Systems of the City of Detroit finished out the morning with a discussion on legislative efforts to erode benefits. You can view his presentation here on Facebook Live.

The second day of programing concluded with a discussion on disaster planning with David Keller of Houston Firefighters' Relief & Retirement Fund and Steven Waas of the Houston Municipal Retirement System. You can view their engaging discussion here on Facebook Live.

The final day of the conference began with Brad Kelly and Peter

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In This Issue

An Alternative to Hedge Funds

By John Ritz

Hedge funds have flourished by offering investors the promise of consistent revenue generation with a low-risk asset correlation.

They appealed to plans looking to plug funding gaps in a world where enduring low yields on most conventional bonds and equities have led many to look further afield to meet investment requirements.

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Hedge funds' assets swelled from \$500B in 2000 to almost \$3T in 2015, but we observe that many have failed to deliver on their promises.

Disappointing Returns

The global financial crisis (GFC) showed us that many hedge funds were unable to produce the promised risk/reward profiles, and many investors endured serious capital losses. Many hedge funds exemplified headline risk—the very thing plans seek to avoid. The Credit Suisse Hedge Fund Index reveals an annualized net return of +3.75% over the 10 years ended December 31, 2016, well below the +6.75% annualized return of the S&P 500 Index.

Cutting Back the Hedge

But disappointing performance is only one reason why we believe pension plans have been reducing hedge fund exposure recently. CalPERS was the first major public pension plan to abandon hedge funds in 2014, but many have followed suit since. Specific issues relate to cost (2% fee on assets plus 20% on outperformance), complexity, lack of transparency and illiquidity.

Many hedge funds also employ a predetermined asset allocation process derived from quantitative models. It is our contention that some of these "black-box" strategies mask the rationale behind investment decisions, as well as the assets or risks to which the underlying strategy may be exposed. This opacity became an issue during the GFC, when many hedge funds suffered significant capital losses, and investors struggled to access liquidity to fund pressing liabilities. While we think there are some good hedge funds still operating, their numbers appear to be dwindling.

Introducing Liquid Alternatives

Traditional long-only asset managers are filling the gap with multi-asset class strategies (MACs), sometimes referred to as "liquid alternatives." There are four broad categories.

- **Absolute return** strategies, offering, for example, LIBOR plus 3-5% with target volatility between equities and bonds and relatively low market correlation.
- **Relative return** strategies, which offer a 60/40 split of equity and fixed income with a higher risk/return profile.
- **Risk parity** strategies, which allocate equally across asset classes based on risk, and employ leverage to boost returns.
- **Risk premia** strategies, which use a quantitative-analysis approach to produce low-volatility returns that unearth quality and value, and tend to have the highest risk/return profile.

Newton has considerable experience in both absolute and relative return MACs.

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__Jon Ritz__ leads consultant relations efforts of Newton Investment Management (North America), based in New York. He joined Newton in 2006 and has held various roles in business development and consultant relations. Prior to joining Newton he worked for Mellon Financial and PNC Bank.

Jon holds the following qualifications, CFA charter holder, Member of the New York Society of Security Analysts, MBA, Mendoza College of Business, University of Notre Dame (highest honors), BS Finance and Management Virginia Tech, FINRA (Series 24, 7 and 63). 11 years at Newton 20 years industry experience

A Revival of Corporate Interest in Environmental, Social and Governance (ESG): Awareness Matters

By Tim Barron

Interest within the U.S. institutional investor community for understanding and applying Environmental, Social and Governance (ESG) factors to their asset pools slowed substantially as they faced the economic and financial meltdown in 2008-09. When faced with dramatic negative returns affecting markets here and around the world, being laser focused on asset allocation and portfolio structure is a natural and appropriate reaction.

Now, almost a decade later, we again see investors returning to this important conversation. Investors are more universally beginning to consider the impact of such factors on the sustainability of public companies and, ultimately, on share price and companies' ability to repay debt.

Additional influences driving this discussion include the greater number of available products being offered by asset managers that integrate ESG considerations, multiple databases utilizing various methodologies for rating and ranking companies' ESG activities, and increasing outreach by the United Nation's Principles for Responsible Investing (UNPRI) team*.

Most recently, however, some are raising questions as to whether the global political environment may have an impact either upon corporate responsible actions or investors' appetites for ESG-integrated investments. We believe there are several strong reasons that support an increasing awareness by all parties for these factors.

- Sustainable practices are truly a global conversation at the company and investor level. In Europe, for example, the European Commission and the European Parliament have endorsed and directed that about 6,000 companies will be required to report on environmental, social, and employee-related, human rights, anti-corruption and bribery matters as well as the diversity policy applied for management and supervisory bodies. This reporting crosses country boundaries.
- A growing number of companies are recognizing that good practices in ESG represent sound operating principles and that both customers and investors are aware of their importance.
- There is an increasing body of evidence via numerous studies that indicate that ESG integration is not injurious to returns, and many indicate that it has a favorable impact.
- The logic that sustainability and corporate success are aligned concepts, not mutually exclusive. Consider key principles of each element.

Environmental – avoiding resource depletion, waste and pollution, and deforestation; reducing emissions

Social – diversity in the workforce; favorable working conditions that exclude slavery, child labor, and other types of worker exploitation, and promote health and safety

Photo Illustration © 2017 Alamy.com

Governance – transparency to stakeholders; accountability; fairness; responsibility

These concepts are not related to politics or parties. Involved actors can differ on the degree of importance and these considerations will shift through time, however, the basic ideals transcend elections and are about what is just and reasonable.

In the not too distant future, ESG factors will be akin to valuations, free cash flow and dividends – items any fiduciary/analyst must be aware of in order to complete a 360-degree evaluation of any investment opportunity. ◆

Tim Barron *is the Chief Investment Officer of Segal Marco Advisors where he manages the firm's Research Department and oversees all investment activities. He has over 35 years of experience in the investment industry. Mr. Barron also chairs Segal Marco Advisors' Investment Committee and is on the Governing Committee of the Global Investment Research Alliance.*

The Administrative Trials and Tribulations of Alternative Assets Investing

By Paul Finlayson and Najiba Miraki

Photo illustration © 2017 Depositphoto.com

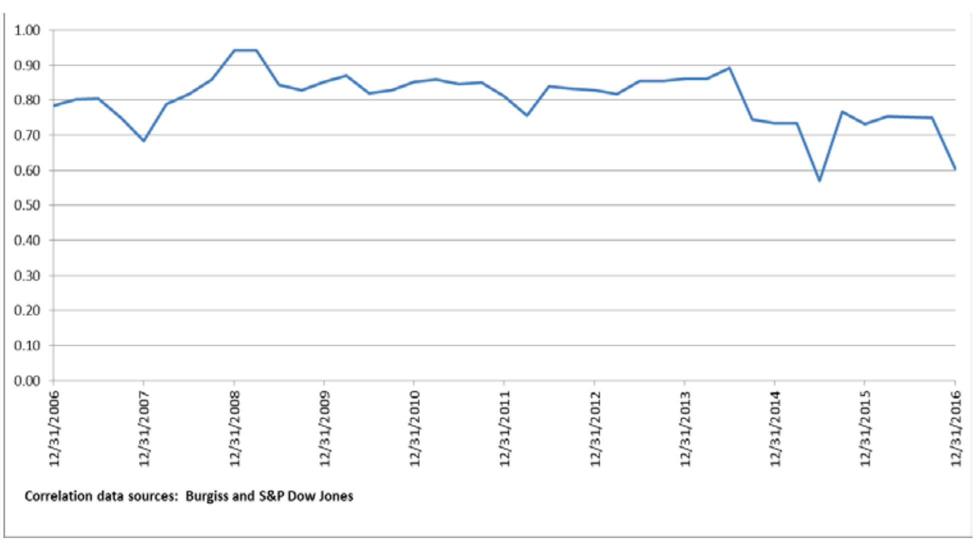
There was a time when non-market traded, or so-called alternative, assets were a small, sleepy portion of the institutional investment plan. With plans seeking return sources greater than traded securities, alternative allocations have increased substantially in the past decade. Commensurate with alternative asset allocation increases, there has been escalation in internal and external diligence demands on investment plans owning these operationally demanding assets.

Non-market traded assets such as private equity, hedge funds, infrastructure and real estate share a common data challenge: the manager is the source of information, including activity details and valuation appraisals. The depth and quality of the information for accounting and analysis depends on the willingness, and sometimes the ability, of the manager to disclose information. Managers are increasingly responding to the demands, but the asset owner thirst for data has only increased due to audit, analytical and regulatory reporting requirements.

The depth and quality of alternative assets data has improved. Studies indicate private equity fair valuations have improved but remain conservative, with returns continuing to move with public markets. Similarly, hedge fund estimated valuations track nicely with final valuations. Accounting granularity of fundings and distributions has increased and providing more information has become part of the manager reporting routine.

Despite meaningful improvements, data and statement standardization challenges remain. Information continues to arrive in an array of statement formats via disparate delivery or retrieval channels. Valuations typically arrive long after the period they represent and are not consistent in composition. These industry realities require the investor to deploy specialized talent, time and systems infrastructure to collect, ingest, validate and report information. The increased asset owner demands on the manager have created a fiduciary dichotomy between asset owner needs and plan performance requirements.

S&P 500 and Pooled PE/VC Returns Correlation (3 years rolling)



To help address alternative assets diligence needs, an entire industry of specialized service providers has emerged. Valuation and fee verification services exist. Fund news data flows freely and daily from specialist arms of traditional news outlets. Emerging technologies, such as blockchain, hold promise of efficient and secure information exchange. Traditional public market transfer agency channels are now offering secure exchange. The success of these capabilities

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Does your pension fund have a Business Continuity Management System? (BCMS)

By John Reidy

Planning for continued business operations in the aftermath of a disaster is a complex task. Preparation for, response to, and recovery from a disaster affecting the administrative functions of an institution requires the cooperative efforts of many in partnership with the functional areas supporting the “business” of the institution.

Photo Illustration © 2017, Depositphoto.com

A BCMS is part of an organization’s overall management system. A BCMS is a set of interrelated elements that organizations use to establish, implement, operate, monitor, review, maintain, and improve their business continuity capabilities. These elements include people, policies, plans, procedures, processes, structures, and resources. All of these elements are used to ensure that operations continue and that products and services are delivered at predefined levels, and that the reputations and interests of key stakeholders are safeguarded whenever disruptive incidents occur1.

One sub-set of BCMS is a business continuity plan (BCP) which is comprised of documented procedures. Organizations use these procedures to respond to disruptive incidents, to guide recovery efforts, to resume prioritized activities, and to restore operations to acceptable predefined levels. Business continuity plans usually identify the services, activities, and resources needed to ensure that prioritized business activities and functions can continue whenever disruptions occur1.

In the past, daily back-up and offsite storage of data was considered a sufficient disaster recovery plan. Today, as evidenced by the recent events in Texas, data backups are just one of many tasks that should be completed on a consistent basis to ensure that your pension fund is meeting its fiduciary responsibility to protect the financial assets and personally identifiable information of your membership. In addition, temporary facilities, such as an offsite business operations center should be predetermined where members of the various business contingency teams and others within your company assemble immediately after they receive notification.

It is important to understand that BCP’s are not boiler plate documents that can be replicated from one pension fund to another. Although public employee pension funds might have a number of similarities between them, they all have unique characteristics with different threat levels and exposure points. For example, a pension fund utilizing web based pension administration software will have a different plan than one relying on an installed application hosted in the pension office. Additionally, pension funds are each governed by their own Board of Trustees and each board will have their own view on how to handle certain situations.

Practicing the procedures of a BCP will help your pension fund become more resistant to potential threats and more resilient and adaptable to change or disaster. Most importantly, a BCP will help protect a pension fund’s reputation during a time of crisis which ensures that the pension fund is viewed in a positive light. ◆

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[1]ISO 22301:2012

__John Reidy__ is one of the Principle founders of the Pension Technology Group (PTG). Founded in 2006, PTG is a technology company that provides web based pension administration software solutions to public employee pension funds. John has participated in nearly 150 pension administration software projects at public employee pension funds throughout the United States. John lives with his family in South Boston, MA.

MESSAGE FROM PRESIDENT THE CONTINUED FROM PAGE 1

Landers, of CorPERS members Global Governance Advisors. Kelly and Landers led a discussion on the financial benefits and importance of good corporate governance. You can view their presentation on Facebook Live here.

The morning continued with Tim Barron of Segal Marco Advisors and Brad Ramirez of CorPERS member Segal Consulting, with a presentation asking what comes first the actuarial assumption or the investment allocation. Aakar Vachhani of Fairview Capital Partners discussed the next generation investment opportunities available to public safety plans.

Mark Dearman of CorPERS member Robbins Geller Rudman & Dowd LLP led a discussion on the opioid epidemic. Ronald King presented for a second time, now discussing the risk cyber security poses for public safety plans. The final presentation of the conference was given by Wally Gomma of ACAP Health, on healthcare costs and what can be done.

The full presentations from the conference can be viewed at www.NCPERS.org/psc. The 2018 Public Safety Conference will be held in Las Vegas, Nevada at Caesar's Palace. ◆

HEDGE FUNDS CONTINUED FROM PAGE 2

MACs may appeal to a broad range of institutional clients seeking a return stream with low correlation to risk assets. In our view, in contrast to hedge funds, they should be inexpensive, offer daily liquidity and low leverage levels, and should not short individual securities. They should also seek to reduce overall portfolio volatility.

We believe transparent security selection, asset flexibility across global markets unconstrained by indices, and a focus on capital preservation are also key requirements.

Conclusion

In our view, MACs can be a viable alternative to hedge funds for institutional investors and we believe the credentials of Newton's absolute return and relative return MACs are worthy of consideration. However, we advise investors to review each MACs category to determine which type best fits their investment requirements. ◆ Disclosures Link

[1]Financial Times, December 28, 2016.

ALTERNATIVE ASSETS CONTINUED FROM PAGE 4

requires the cooperation of the asset manager considerate of impacts on their primary business of generating returns.

Industry-wide data standards, data availability and workflow technology are all improving. However, the non-standard nature and escalating transparency demands of alternative assets will continue to exact a tangible administrative cost on the plan. For the foreseeable future, the asset owner must consider and quantify the erosive effects of non-marketable administration expense on the alpha promised by these attention intensive investments. Transparency, standardization and technology advances have been made, but it is a process that will take time to fully actualize, requiring the cooperation of both the asset owner and manager as well the evolution and adaption of new technology. ◆

__Paul Finlayson__ is a Senior Vice President and Alternative Assets Service Product manager with Northern Trust.

__Najiba Miraki__ is a Vice President and Alternatives Asset Service Product Manager with Northern Trust.

Disclosure:

Northern Trust Corporation, Head Office: 50 South La Salle Street, Chicago, Illinois 60603 U.S.A., incorporated with limited liability in the U.S. Global legal and regulatory information can be found at www.northerntrust.com/disclosures.

Fiduciary Duty and Divestment - Can They Mix?

By Robert D. Klausner, NCPERS General Counsel

For several years there has been increasing pressure for retirement systems to make retirement decisions based on political and social concerns, separate and apart form traditional investment concerns. Divestment moves have included tobacco, firearms, private prisons and fossil fuels.

In the recent weeks, the New York City pension funds made a decision to divest of stocks in private prisons. This has long been a practice in faith-based retirement plans such as church plans where investment practices and articles of faith often cross paths. Unlike church plans which are free from judicial or legislative control on First Amendment grounds, public pension plans do not enjoy that luxury.

Photo Illustration © 2017 DepositPhotos.com

In deciding to follow or decline a divestiture mandate, retirement systems have looked to whether the effect on the portfolio is "de minimis."

De minimis non curat lex - "The law does not concern itself with trifles." At least one state, New York, rejected this maxim in the context of a fiduciary duty. In *Sorin v. Shahmoon Industries*, 220 N.Y.S.2d 760 (N.Y. App. 1961), a waste of corporate assets challenge, the court held that where a fiduciary's duty to account is at issue, it is a question of "principle," not principal. When a fiduciary is to account for funds entrusted to his or her care, it means all funds "not some, or even most." This would seem to suggest that there is no de minimis exception (at least in New York), highlighting the confused and unsettled state of the law.

The leading (and really the only) case in this context remains *Board of Trustees v. Mayor and City Council*, 562 A.2d 720 (Md. 1989). The trustees of the City pension fund sued to challenge ordinances requiring divestiture of holding in companies doing business with the Apartheid government of South Africa. In upholding the ordinances the Court observed that given "vast power that pension funds exert in American society, it would be unwise to bar trustees from considering the social consequences of investment decisions," where the cost was de minimis. In the Baltimore case, the trial court found that the initial cost of divestment was 1/32 percent (3 basis points) and the on-going cost was 1/20 percent (2 basis points. To date this remains the only public pension case giving some concrete definition to the term "de minimis" in the divestment context.

A similar case concerned an action by the Oregon Board of Higher Education passing a divestiture resolution relating to investment of endowment funds. The State Investment Council declined to adopt the resolution finding it contrary to prudent investment standards. Various student groups whose members received endowment-funded scholarships sued. An Oregon trial court held that the Board of Higher Education and not the State Investment Council controlled the endowment funds but agreed that divestiture was a violation of the prudent investor standard. The decision was over turned on appeal when student plaintiffs were found to lack standing. The trial court decision was contrary to the result reached in Maryland. Significantly, the Maryland decision was employer driven and the Oregon case was driven by Board of Higher education policy.

The Florida Attorney General opined that a decision by the State Board of Investment (which acts as the fiduciary for the Florida Retirement System) could not adopt an administrative rule on divestiture based on ethical considerations in the absence of enabling legislation. The opinion continued, however, that instability in a region (here, South Africa) would be a legitimate consideration in making an investment decision because of the potential effect on economic considerations.

In a post-South Africa Attorney General opinion, Maryland considered whether Iran and Sudan divestiture was inconsistent with the State Retirement Board's fiduciary duty. The AG concluded it was not under the following conditions: (1) Fair market value was received for the divested interests; (2) substitute investments had comparable return and risk; (3) timing and manner of divestment

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LEGAL REPORT CONTINUED FROM PAGE 7

transactions were prudent; and (4) the effect was de minimis as compared to "total fund assets."

Viewing the de minimis nature of an event in the context of "total plan assets" would have a different effect in the context of based on the individual plan.

Last year, the California Legislature adopted California Government Code 7513.75 calling on the state retirement systems to divest thermal coal holdings, subject to their constitutionally mandated fiduciary duty. The Legislature made express findings that divestiture from thermal coal was in the long term economic benefit to California, although not expressly in relation to the retirement systems. More recently, Montgomery County, Maryland voted to divest fossil fuel holdings in its retirement systems.

In virtually all of these cases, the decision to divest had legislative origins. This frees the plan fiduciary from having to balance public political or social sentiment with its core purpose of protecting the retirement system. The U.S. withdrawal from the Paris Climate Accords has only accelerated politically driven divestment initiatives. To remain true to their fiduciary duty to the members and beneficiaries of the retirement plans, it is best for trustees if these decisions are made by the political branches of the government which must also raise the revenue to offset any divestment related increase in cost. ◆

This article is a regular feature of PERSIST. ***Robert D. Klausner****, a well-known lawyer specializing in public pension law throughout the United States, is General Counsel of NCPERS as well as a lecturer and law professor. While all efforts have been made to insure the accuracy of this section, the materials presented here are for the education of NCPERS members and are not intended as specific legal advice. For more information go to www.robertdklausner.com.*

Calendar of Events 2018

January

Legislative Conference
January 28 – 30
Washington, DC

May

NCPERS Accredited Fiduciary Program (All modules)
May 12 – 13
New York, NY

Trustee Educational Seminar
May 12 – 13
New York, NY

Annual Conference & Exhibition
May 13 – 16
New York, NY

June

CIO Summit
June 14-15
Chicago, IL

September

Public Pension Funding Forum
September 10 – 12
Cambridge, MA

October

Public Safety Conference
October 7 – 10
Las Vegas, NV

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