

- I. Process Name: Hiring Investment Managers Process**
II. Process Number: INV 0080
III. Contact Person: Bryan Lewis
Chief Investment Officer
717-787-9008

IV. Required Resources

A) Systems/Consultants:

- Public Markets: eVestment
- Public Markets and Fund-of Hedge Funds: RVK, Inc.
- Private Equity: StepStone Group
- Real Estate: NEPC

B) Materials:

All asset classes: SERS Master Due Diligence Questionnaire (DDQ)

Public Markets (equity and fixed income)

- SERS DDQ - Public Markets
- SERS Public Market Managers Initial Due Diligence Checklist

Fund-of Hedge Funds (FoHFs)

- SERS DDQ - FoHFs
- SERS Public Market Managers Initial Due Diligence Checklist

Direct Hedge Funds

- SERS DDQ - Direct Hedge Fund
- SERS Public Market Managers Initial Due Diligence Checklist

Private Equity

- SERS DDQ - Private Equity
- SERS Private Market Managers Initial Due Diligence Checklist

Closed-end Real Estate Funds

- SERS Due Diligence Questionnaire - Closed-end Real Estate Funds
- SERS Due Diligence Questionnaire - Supplement for Closed-end and Open-end Real Estate Funds
- SERS Due Diligence Questionnaire - Annex for Open-end and Closed-end Real Estate Funds
- SERS Private Market Managers Initial Due Diligence Checklist

Open-end Real Estate Funds

- SERS Due Diligence Questionnaire - Open-end Real Estate Funds
- SERS Due Diligence Questionnaire - Supplement for Closed-end and Open-end Real Estate Funds

- SERS Due Diligence Questionnaire - Annex for Open-End and Closed-End Real Estate Funds
- SERS Private Market Managers Initial Due Diligence Checklist

C) Special Notes:

- Investment managers and funds may be procured on a sole source basis pursuant to Section 515 (8) of the Procurement Code, and do not need Comptroller's Office approval for payment.

V. Introduction

A) Purpose of Process:

It is the practice of the SERS Board to use external investment managers¹ to directly manage Fund assets. In accordance with the Statement of Investment Policy, the Board continually seeks to employ investment managers that possess superior capabilities in the management of institutional assets. The Investment Office is responsible for coordinating all investment activities and matters for SERS, including conducting due diligence with respect to potential investment managers. At the direction of the Board, the Investment Office staff work with SERS' investment consultants to perform Investment Manager searches to satisfy the needs of the investment program.

B) Customer:

- State Employees' Retirement Board (SERB)

C) Who Performs:

- SERB
- SERS Investment Office
- SERS Legal Office

D) External Participants:

- SERS General Investment Consultant
- SERS Real Estate Consultant
- SERS Private Equity Consultant
- Investment Managers

E) Additional Information:

Contract provisions require coordination between SERS Legal Office and the Investment Office during negotiations and the draft phase. Coordination is also required with SERS Office of Finance and Administration to set up custodial accounts, ensure accounts are reported in the appropriate custodian composite reports, reconciliation with the Fund's custodian, fee billings, and other accounting related matters.

¹ Throughout this document, the term "Manager" and "Investment Manager" may refer to a General Partner of a Limited Partnership, a manager of a SERS-specific portfolio, or a manager of a commingled account.

VI. Related Information

A) Related Policies:

- Investment Manager Monitoring Policy

B) Related Processes:

- Establishing an Asset Allocation Process
- Benchmarking Investment Managers Process
- Evaluating Investment Manager Performance

C) Definitions:

N/A

D) Materials:

- SERS Ethical Conduct Policy and Ethics & Fiduciary Requirements Affecting Board Members
 - Recusal Policy Update to Board
- Main Statement of Investment Policy
- Private Equity Statement of Investment Policy
- Real Estate Statement of Investment Policy
- Strategic Investment Plan
- Policy Regarding Investment Managers Insurance
- SERS Derivatives Investment Policy Statement

E) Special Notes:

N/A

VII. Document Properties

A) Document Owner: Bryan Lewis

B) Document Author: William Truong

C) Summary of Changes:

Date	Version	Author	Summary
3/17/2005	1	Jim Gross	Drafted final process
2/20/2015	2	Bill Hutcheson and William Truong	Updated process documentation to reflect current consultants, policies, materials and asset class names
8/19/2015	3	William Truong / Jim Nolan	Added recommendations from SERS' Legal Team (Chris Houston, Karen Damiano and David Sedlak). Added criteria from Horizon Impact Fund to page 7. Added Investment Recommendation Standards for SERS' investment staff.

9/29/2016	4	William Truong	Updated CIO contacts. Removed direct hedge fund consultant. Updated asset class names to reflect changes in new asset class structures.
6/29/2018	5	William Truong	Updated real estate consultant and real estate due diligence questionnaire names. Updated special note regarding sole source of consultants and managers. Added recommendations to #6 from SERS' Legal Team (Chris Houston and Jeff McCormick).

VIII. Steps

1. The Need to Hire an Investment Manager Has Been Identified

SERS' Strategic Investment Plan details the strategic direction and focus of the SERS investment program. The following are examples (not comprehensive) of various triggers that may prompt SERS' investment office staff and investment consultants to initiate an analysis of a current manager and/or begin a search for another investment manager:

- The replacement of who are performing poorly due to changes in personnel, organization, strategy, style drift, or other factors;
- The strategy of an existing investment manager no longer fits into the current asset allocation strategy;
- A need to fill new strategies and initiatives identified in the Strategic Investment Plan (e.g., allocating a portion of the Fund to new asset classes and liquidating or paring down other asset classes).
- Presentation or discovery of a new, opportunistic or emerging investment strategy; and
- Opportunity to participate in funds previously closed to new investors due to capacity or other constraints.

2. Search for Appropriate Managers

SERS' investment office staff and investment consultants search for managers capable of fulfilling the Board's investment program/policies. The staff and consultants use a database of the respective manager's universe (international, domestic, growth, cap weight, etc.) to generate a list of managers who are aligned to the specific needs of SERS' investment program. Staff may also recommend potential firms for consideration based on networking contacts, experience, and unsolicited contacts.

When screening the initial list of managers, the staff and consultants consider the manager's strategy, quality and experience of professional staff, ownership structure, investor level breakdown, assets under management, fund openness to new investments, availability of a measurable history for the product under consideration, and a comparison of performance history among peers and against an appropriate benchmark. Based on this analysis, staff and consultants determine which managers would be suitable candidates for further review.

3. Initial Identification

Candidates that successfully pass the first screening discussed above may be invited to come to SERS to discuss their product. Candidate teams will generally include the portfolio manager, co-portfolio manager or General Partner, a senior client service representative, and any integral members of the investment management company. The candidates will give a detailed presentation of the history of their organization, investment products, biographies of key team

players, assets under management, investment philosophy, portfolio construction, and risk management policies and procedures.

There is considerable dialogue between the managers and SERS staff and consultants regarding the philosophy, trading strategies, the impact of micro/macro events, whether the firm is “top down” or “bottom up,” whether they employ fundamental or quantitative analysis, use of models and development of assumptions, and other relevant matters. From those interviews, SERS staff and consultants work together to select a pool of potential candidates for the desired mandate that will be subjected to more intensive due diligence research and, potentially, recommended to the Board for an interview.

Because the consultants serve a diverse client group, extensive due diligence will have already been performed on managers that have passed the initial screening. That information is incorporated into the process of considering managers for a more detailed review.

4. Conduct Due Diligence

Manager due diligence is generally conducted on-site by SERS staff and/or consultants to gain a deeper understanding of the manager’s philosophy, products, performance history, research, buy/sell disciplines, staffing concerns, front and back office operations, and any other concerns of interest. The primary goals of conducting on-site due diligence are to gain an understanding of:

Investment Philosophy and Process:

- Whether the candidate has a clear, well-defined and cohesive process, from philosophy through implementation, and whether the firm’s resources are adequate to support the strategy;
- Whether the philosophy remains consistent over market cycles and environments and is supported by research, analysis, and results;
- Why the candidate believes their philosophy will produce sustainable, persistent results relative to an appropriate benchmark going forward; and
- The risk management policies and procedures employed by the Manager.

People and Organization:

- Whether there are any significant regulatory actions against the firm or any of its personnel;
- Whether the ownership structure is stable;
- Whether staffing is adequate and stable;
- Turnover of key personnel;
- The compensation structure of the firm;
- The manager’s ability to manage growth; and
- The commitment to research, enhancements, and/or improvements at the firm.

Back Office:

- How the manager ensures best execution of trades;
- The soft dollar policy of the manager;
- Whether the manager's back office/trade operations support compliance efforts and portfolio management activities;
- Whether periodic reporting is adequate and timely;
- Whether information and communication systems are adequate to support philosophy and manage portfolio risk;
- The manager's Cybersecurity Plan and Business Recovery Plan and whether it has been tested;
- Whether the manager's insurance coverage complies with SERS investment office's insurance requirements;
- Whether a manager has an independent review of its internal control environment; and
- The financial position of the firm.

Fees:

- Management and performance fees relative to expected excess return and to other managers with similar mandates; and
- Whether SERS will receive "most favored nation" status.

Insurance:

Prospective managers are asked to provide evidence of their current types of insurance and levels of coverage.

Due Diligence Questionnaires:

Tailored comprehensive due diligence questionnaires exist for the different asset classes and are available as tools to assist staff in conducting their due diligence. The investment office staff and consultants work together to perform due diligence. SERS due diligence questionnaires may include questions regarding:

- Organization – Firm and People
- Strategy – People
- Strategy – Philosophy
- Strategy – Process
- Strategy – Characteristics
- Strategy – Progress/Review
- Performance
- Fee Discussion
- Trading
- Operational Controls and Compliance
- Valuation Policy
- Related Party Issues
- Marketing/Client Service
- Levels of Investment Manager Insurance

Private Equity (buyout, venture capital and special situations funds)

Note: All Private Equity funds with \$500 million or less in total commitments, or newer private equity managers raising their first, second, or third fund, should automatically be directed through SERS' Horizon Impact Fund for the General Partner's review at their sole discretion.

The Private Equity process is unique because the investments take the form of higher risk, less liquid limited partnerships.

The Private Equity consultant and staff conduct weekly calls to review the Private Equity program and investment opportunities. They also conduct in-depth annual strategy sessions to discuss the coming year's investments in Private Equity. This strategy contemplates the commitments needed to maintain the fund's exposure to the asset class as approved in the Strategic Investment Plan. In any particular year, the team considers existing managers in the portfolio, how many may offer follow-on funds, whether those follow-on funds are suitable for SERS' portfolio, and strategies to gain access to top-tier funds. Staff and consultant determine the needs of the SERS portfolio by analyzing what exposures are needed (private equity vs. venture capital, international, sector focused, etc.).

The Private Equity consultant has an extensive database to screen by type, stage, industry, geography, and by returns against peer Vintage Year and Internal Rates of Return in order to evaluate potential candidates. Other opportunities are evaluated based on received marketing materials, telephone and email contacts, networking, staff's firsthand experience, and other referrals.

In determining whether to commit to a "new" fund, or to participate in a "follow-on" fund with an existing manager, staff and consultant consider the following broad themes:

- Whether the strategy is still appropriate;
- Whether the team is stable and whether they carry out the strategy; and
- Whether the performance expectations are reasonable, realizable and consistent with risk/reward.

Potential candidates complete the Private Equity DDQ (SERS' Master DDQ, SERS Private Equity Questionnaire, consultant's DDQ or manager-provided DDQ) for evaluation by consultant and staff. The survey addresses the characteristics listed below.

The analysis of the responses is done independently and then compared and discussed by staff and consultant.

The questionnaire exists for use as a tool to discuss essential operational and background information about the candidates including:

Description of the fund	Ownership of the firm
Philosophy	Monitoring controls
Strategy	Valuation policies
Deal sourcing	References
Performance history	Background checks
Performance of previous funds and results	Litigation issues
Number of limited partners	Reporting financial conflicts of interests
Process and transactional controls	Management responsibilities and experience
Size of the fund	Management and transaction fees
GP commitments to fund	Advisory committees
Legal and capital structure of the fund	
Fees, carry and clawback provisions	

Much of the Private Equity fund due diligence is conducted by the consultants and SERS investment staff on-site. These items are discussed as well as an evaluation of the partnership's deal flow.

Interviews are also conducted by staff at the SERS home office and by Private Equity consultant at its offices. Both staff and consultant review the respective Private Placement Memorandums.

Approval for follow-on funds is generally less intensive at the staff level. All funds (new funds or follow-on funds) recommended to the Board must be interviewed by the Board.

If an existing fund met return expectations, and continues to be a satisfactory investment for the fund, staff will evaluate the characteristics of the follow-on fund, review the Private Placement Memorandum and, in conjunction with the consultant, determine whether to proceed with a recommendation for the Board.

For candidates scheduled to appear before the Board, sizing issues are discussed.

Real Estate

Staff and the Board's independent real estate consultant evaluate portfolio needs on an annual basis. Portfolio needs are evaluated by determining whether to maintain, reduce or increase exposure to certain investment strategies, property types, or geographic areas. Once that has been determined, staff and consultant discuss how those needs can best be filled within the portfolio: separate accounts, funds or limited partnerships, or the Real Estate Investment Trust (REIT) portfolio. While each of these investment vehicles is different, the evaluation and hiring process of the managers is generally consistent.

When an investment opportunity is either presented or sought out, SERS obtains and reviews the Private Placement Memorandum (if applicable), marketing materials and other background information to determine if the opportunity merits further consideration. For opportunities that appear to be attractive, the consultant will be asked to begin its due diligence process and provide feedback on the opportunity.

The consultant will, if appropriate, review its database of historical returns of peer groups to validate the returns presented by the manager and identify how the manager compares relative to its peer and vintage group. The Real Estate Consultant also requires the manager to submit a written response to the Due Diligence Questionnaire that is used as a tool to evaluate managers. This questionnaire provides background and details on the following information:

Ownership structure	Hedging
Investment structures	Property types
Strategy	Qualifications and experience
Legal structure	Buy and sell decision making
Valuation policy	Valuation policies
Use of floating or fixed rate debt	Financial reporting
Regions	Diversification
Deal sourcing	Asset and property management services
Leverage	Advisory Committees
Management and incentive fees	
Research	
Asset management oversight	

The manager will be invited to SERS' offices for a formal presentation of the investment opportunity. During this meeting, the staff will discuss the manager's strategy, philosophy, history, development and expansion of the product and management team, and attempt to gain a more thorough understanding of the investment and the manager. Concerns will be raised if appropriate. Following this meeting, the manager will generally be invited to the Real Estate Consultant's offices for a similar meeting.

Staff and consultant will then convene to compare notes and determine if the opportunity merits further review. Based on that determination, either staff or consultant (or both) will visit the prospective manager at their offices and evaluate the fee structure, back office operations, deal flow, valuation and management techniques, and appraisal policies. Meetings with other key staff of the manager will be conducted to ascertain the depth of the management team. If the manager is a new relationship for SERS, reference contacts will be obtained and those will be checked.

All managers/funds (new or follow-ons) recommended to the Board must be interviewed by the Board. Assuming that staff and consultant are prepared to recommend the opportunity to the Board, a joint memorandum outlining the opportunity and its risks will be prepared for an upcoming Board meeting. This memorandum will recommend that the Board, at its upcoming meeting, consent to a formal interview of the manager at the subsequent Board meeting. Staff

and consultant present their recommendation to the Board and address any questions prior to the Board deciding whether to grant the interview.

The manager's formal presentation will be mailed to the Board a week prior to the Board interview to allow Board members time to review and evaluate. At the meeting, the manager will make its presentation and staff and consultant will make a final recommendation both in written form and orally, as well as discuss any final questions posed by the Board.

Hedge Funds

SERS obtains funds-of hedge funds (FoHFs) contacts through its general consultant. In order to reduce the list to the most attractive manager options, staff considers the experience of the investment team, references, extent of institutional experience, nature of other strategic relationships, and the capacity of the fund. To gain a better insight into these objectives, SERS and its general consultant developed a questionnaire to send to top candidates being considered for an investment mandate.

The questionnaire is designed to provide feedback on liquidity, sophistication of risk control and monitoring systems, the history of the fund and its management team, firm/fund capacity, performance, and whether the results are sustainable. Staff also performs statistical analysis on the competing funds' performance.

The Due Diligence Questionnaire is used as a tool to discuss essential operational and background information about the candidates including:

Company overview	Hedge fund management
Organizational structure	Reporting quantitative data
Staff experience	Leverage
Co-Investment Levels	Legal issues
Performance measurement	Fees and costs
Diversification of strategies	Risk and monitoring controls
Due diligence efforts	Capacity
Portfolio construction and decision making	Other

Based on the evaluation of the responses and results of analysis, if the candidate is attractive, staff determine whether to conduct on-site visits to gain better perspective on risk monitoring, review the reports used by management for monitoring the funds, review the adequacy of back office operations and monitoring procedures, meet with all levels of the management team and gain a better understanding of the manager's edge in their market, and how the manager can build a portfolio to meets SERS' needs.

Results of surveys, analyses, and site visits are discussed with consultants and an analysis is prepared for the Board.

4.1 If qualified candidates are identified in public markets or hedge funds, potentially two to five managers are presented to the Board for its review and consideration.

4.2 Investment Recommendations Standards

GOAL: Standardize and improve the process for reviewing and recommending investment opportunities for SERS to ensure that all suitable opportunities are thoroughly investigated and approved by SERS' investment staff, SERS' independent external consultants, and SERS' Chief Investment Officer.

PROCESS: Prior to presenting any investment opportunity to the SERS' Board for its consideration, SERS' investment staff and the appropriate Asset Class Managing Director, together with the designated external independent consultant, must complete most of its due diligence and review the investment opportunity with the Chief Investment Officer.

The Asset Class Managing Director will discuss the following items with the Chief Investment Officer regarding the investment opportunity:

- How the investment fits into the Strategic Investment Plan;
- Proposed manager's investment strategy;
- Background on the management entity;
- Any issues that were uncovered during the due diligence process by either staff or consultant;
- Proposed investment terms;
- How the investment will be funded;
- Proposed amount for investment and rationale for the amount; and
- Track record.

The Chief Investment Officer will have the final decision on whether the investment should be brought forward for the Board's consideration.

After the Chief Investment Officer decides to bring an opportunity forward for the Board's consideration, SERS' investment staff and the designated independent external consultant will prepare a Recommendation for Interview memo, addressed to the Board, for the Chief Investment Officer to review two weeks prior to the 1st Board Meeting (as defined below).

5. Provide Recommendations to Board ("1st Board Meeting")

Staff and consultant provide a joint Recommendation for Interview memo and an Executive Summary (collectively, the "Executive Summary") to the Board in advance of the 1st Board Meeting, and then summarize their combined due diligence, and ultimate recommendation, in a presentation to the Board during the 1st Board Meeting. The recommendation includes a

discussion of the managers being requested for Board interviews, summary information from the due diligence, and any related questions or concerns of the Board.

Public Equity and Fixed Income Managers:

The Executive Summary is presented by SERS Investment Office Staff and the General Investment Consultant. Information provided in the Executive Summary includes:

Background	Performance history
Mandates	Investment
Investment manager agreements	Style
Amount of commitment	Other
Sourcing of funds	

Chart comparison of candidates may include:

Investment style	Portfolio construction
Tracking error	Investment objective
Fees	Risk/Return ratios
Investment team	Inception date
Assets under management	Research method
Analysis on new companies	Holdings in team products
Company characteristics	Annual portfolio turnover

Facts Sheet for each candidate may contain:

Inception date	Total firm assets
Breakdown of assets	Ownership
Office locations	Firm history
Investment Style	Portfolio advisor
Inception of strategy	Assets in strategy
Investment philosophy	Investment process
Performance history	Weaknesses
Strengths	Consultant's rating

Private Equity:

The Executive Summary is presented by SERS' Investment Office Staff and the Private Equity Consultant. Information provided in the Executive Summary generally includes:

Size of fund	Recommended commitment level
Overview of the fund	Investment strategy
SERS' investment thesis	Geographic/Industry focus
Average investment size	Key personnel
Performance history	Summary of Key Terms

Real Estate Managers:

The Executive Summary is presented by SERS' Investment Office Staff and the Real Estate Consultant. Information provided in the Executive Summary includes a discussion of the impact the proposed investment will have on the portfolio, as well as:

Portfolio construction	Key Personnel
Investment process and strategy	Background
Diversification of strategies	Investment experience
A summary of terms and conditions	Recommendations
Performance in up and down markets	Organizational structure

Hedge Funds:

The Executive Summary is presented by SERS Investment Office Staff and the General Investment Consultant. Information provided in the Executive Summary includes:

- A chart providing a comparison and indication of the strategies and allocations in which the proposed candidates may invest.
- A chart providing a comparison of the candidates' assets under management, number of strategies and absolute return managers, and an indication of their respective targeted return, volatility, and beta relative to the S&P 500 or Lehman Aggregate Bond Index (depending on the respective underlying strategy).

Strategies	Objective of the strategies
Approach of the strategies	Search process
Evaluation of the candidates	Recommendations

- A summary for candidates recommended, which includes:

Strategy	Capacity
Underlying advisor selection	Portfolio construction
Risk controls	Monitoring system
Reporting methods	Operations
Experience	Strategic partnerships

The Board engages in discussion with Investment Office staff and consultants posing questions and concerns regarding the respective candidates, and then makes a decision whether to interview any recommended managers at the 2nd Board Meeting (as defined below).

6. Board Interviews and Evaluates Proposed Manager (“2nd Board Meeting”)

The staff's Recommendation for Approval Memo (recommending approval for funding or a commitment) will be updated to reflect any new information or changes that may have occurred after the staff's Recommendation for Interview Memo submitted to the Board in advance of the

1st Board Meeting. The managers prepare and send a report and/or presentation to SERS and the Board prior to the 2nd Board Meeting.

The relevant asset class consultant provides to SERS' investment office staff and Board an Investment Recommendation update to the Executive Summary provided to the Board in advance of the 1st Board Meeting. This report provides a more detailed discussion of fund strategy, portfolio construction, and investment performance as supporting data to make investment decisions.

The Board discusses the recommendations with the consultants and investment office staff prior to interviewing the managers.

The managers' prepared written presentation is mailed to the Board a week prior to the 2nd Board Meeting for the Board's review and analysis. The managers then appear at the 2nd Board Meeting and present themselves and the investment opportunity to the Board.

The Board requests feedback from the Investment Office Staff, the subject matter consultant, and the manager candidates before, during, and/or after the manager's interview, which may include the following:

- Company Overview;
- Personnel;
- Portfolio Strategy;
- Market Outlooks;
- Performance Related Issues;
- Pending Legal Matters; and
- Fees.

The Board generally votes on whether or not to hire a manager or combination of managers following the manager interviews. If Board members have a conflict and/or connection to the manager of some kind that could potentially affect the objectivity of their vote, they must file the appropriate forms notifying the Board of same in advance of the 2nd Board Meeting, and then go on record recusing themselves from the vote during such meeting's public session. Applicable policies are:

- SERS Ethical Conduct Policy and Ethics & Fiduciary Requirements Affecting Board Members
- Recusal Policy

Board approval is subject to successful completion of contract negotiations.

Once the Board approves an allocation, SERS Legal Office negotiates contracts that include, without limitation, investment guidelines/restrictions that establish strategy, style, diversification, turnover, appropriate benchmarks, prohibited transactions, portfolio construction and

characteristics, and other matters. Negotiated contracts are subject to approval for form and legality by the Office of Attorney General (OAG) and the Office of General Counsel (OGC) which, by law, may take up to 30 days. Contract documents of follow-on investment vehicles, and amendments to existing management agreements, may be reviewed and approved by SERS Legal Office (with authority delegated by OAG/OGC) where the legal terms are materially similar to, or more favorable to SERS than, those contained in the contract documents/agreements that OAG/OGC had previously reviewed and approved.

7. Provide Candidates with Appropriate/Applicable Policies and Guidelines

- Main Statement of Investment Policy
- Private Equity Statement of Investment Policy
- Real Estate Statement of Investment Policy
- Strategic Investment Plan
- Policy Regarding Investment Managers Insurance
- SERS Derivatives Investment Policy Statement