

**NORTH CAROLINA DEPARTMENT OF STATE TREASURER
INVESTMENT MANAGEMENT DIVISION**

External Investment Manager and Vehicle Selection Policy

DST Reference:	IMD-POL-1001-IMD
Title:	External Investment Manager and Vehicle Selection Policy
Current Effective Date:	October 13, 2020
Version/Revision:	1.2
Original Effective Date:	June 5, 2013

I. Background

The Treasurer of the State of North Carolina (the “Treasurer”) maintains the investment programs for the North Carolina Retirement Systems (“NCRS”), Short-Term Investment Fund, Escheat Fund, and Other Ancillary Funds. The Treasurer and the North Carolina Supplemental Retirement Board of Trustees provide oversight for the investment programs of the North Carolina Supplemental Retirement Plans (“SRP”), the Supplemental Retirement Income Plan of North Carolina, North Carolina Public Employee Deferred Compensation Plan, and North Carolina Public School Teachers’ and Professional Educators’ Investment Plan. The Treasurer and the North Carolina ABLE Program Board of Trustees provide oversight for the investment programs of the North Carolina ABLE Program Trust.

The Investment Management Division (the “IMD”) is the primary operating division within the North Carolina Department of State Treasurer (“DST”) with responsibility for day-to-day oversight and management of various asset pools.

For a variety of reasons, IMD periodically recommends hiring external investment managers and adding to its portfolios new commitments to private market investment vehicles permitted by statute.¹ This policy sets forth the process that IMD will follow when hiring new external investment managers or making a new commitment to any of the aforementioned entities for the NCRS or another IMD managed fund. This policy does not apply to internally managed portfolios, individual co-investments periodically presented to staff, or managers, funds or other vehicles that receive allocations within a fund-of-fund vehicle.² On a case-by-case basis, the Chief Investment Officer may authorize procedures that deviate from this policy, but IMD shall note any material deviation from this policy in the investment recommendation memorandum provided to the Treasurer.

¹ The term “External Investment Manager” means any of the following: investment managers for separate or commingled accounts, investment advisors to private market vehicles (e.g., private equity, real estate, hedge funds, etc.), general partners or managing members of private market investments, or the funds, limited liability vehicles (separate or commingled), fund-of-funds, and other vehicles to which the IMD may commit capital. The term “External Investment Manager” also includes such organizations’ wholly-owned affiliates and any entities controlled by or under common control with the External Investment Manager.

² Staff directed rebalancing between direct fund investments or incremental funding to such vehicles will be evaluated on a case-by-case basis by the Chief Investment Officer to determine what updated due diligence and recommendation memorandum are required.

II. Policy Statement

The selection of a new portfolio commitment shall be carried out:

1. In accordance with investment objectives, fiduciary standards, and approved procedures and criteria as set out in the *Investment Policy Statement for NCRS, IMD-POL-1000-ALL*, and other applicable policies and statutes
2. With a predominant reliance on asset class Directors' and third-party experts' comparative evaluation of opportunities within a defined due diligence process
3. In a fair and consistent manner with a structured external communication protocol designed to facilitate transparency and efficiency of process for IMD and external parties

III. Identifying Investment Opportunities

IMD will typically utilize either a "Request for Information Search" or a "Work Plan and Opportunistic Search" to identify investment opportunities and ultimately recommend investment managers, advisors, fund-of-fund managers, separate account or commingled limited liability vehicles, and other investment vehicles permitted by statute. While IMD will be neutral regarding the sourcing or identification of investment opportunities, both approaches defined below are designed to focus scarce IMD resources on the highest potential value-added investment opportunities and relationships given IMD's evolving portfolio needs. To that end, every effort should be made to promptly refer investment opportunities to Directors for inclusion in one of the processes described below.

A. Request for Information Searches

It is the responsibility of the Director³ of the applicable asset class or individual mandate to develop and propose the:

1. Rationale for conducting a search
2. Role of staff and any consultant in that search
3. Search criteria that define broad parameters that ultimately determine the universe of eligible investment managers, funds, etc.

Once the foregoing three items are approved by the Chief Investment Officer, the Director will generally use the following process:

1. First-Level Screen. Consultant and third-party databases, peer information, and internal files will be screened to identify a universe of managers that meet the specific investment criteria. A short-form questionnaire may be sent. The purpose of these initial steps is to eliminate managers early in the process that would not be seriously considered due to size, experience, or focus, then prioritize attractive candidates. The Director will approve a list of managers to be sent Requests for Information (typically 3 or more managers).

³ For convenience, the term "Director" is used to mean both the Director and all staff within their span of control. It is understood that the Directors' responsibilities described in this policy will be carried out with active participation of the asset class staff.

2. Requests for Information (RFI). Managers remaining under consideration will be requested to provide comprehensive information regarding performance, portfolio composition, personnel, organizational history and structure, proposed fees, and any other information deemed necessary to make an informed decision.
3. Additional Screen after Requests for Information. After receipt of the remaining managers' responses, the Director will evaluate risk-adjusted investment performance, investment processes and organizational issues to identify the target firms that will be interviewed for the assignment.
4. Preliminary Conference Call. The Director will coordinate with the target firms and IMD representatives to discuss preliminary issues involving the investment, including administrative details, operational concerns, risk and compliance issues, potential conflicts of interest, and manager's willingness to accept NCRS preferred terms. Informal reference calls to peers and industry contacts may be made. Additional managers may be eliminated as a result of these discussions.
5. Manager Interviews. The Director will develop and distribute interview materials and schedule interviews with the finalists. The Director should invite the Chief Investment Officer, IMD risk and operations personnel, and the Chief Risk and Operating Officer. Other DST personnel may also attend interviews. Additional cuts may be made as a result of these interviews.

The remainder of the investment manager diligence, recommendation, negotiation, and approval process is described starting in Section IV below.

B. Work Plan and Opportunistic Searches

The intent of Work Plan and Opportunistic Searches is to utilize a prudent process to maximize long-term access to attractive risk-adjusted investment opportunities through use of business partners.

Desirable characteristics of such business partners include:

1. Financial, operational, and investment expertise and resources
2. Alignment of interests
3. Transparency and repeatability of investment process
4. Controls on leverage

Work Plan and Opportunistic Searches are typically used for Private Equity, Opportunistic Fixed Income, Inflation Sensitive, Core and Non-Core Real Estate asset classes, and direct hedged equity. In each of these areas, the limited window of opportunity to commit capital in certain vehicles and strategies calls for a blend of proactive and opportunistic approaches. Non-marketable and marketable alternative strategies typically will be structured as limited partnerships with very specific offering periods that cycle on average every 4-6 years. Hedge funds may have periodic openings and closings to new investors. On the opportunistic front, strategies that intend to exploit capital market dislocations due to supply/demand imbalances, regulatory changes, or other events can be transitory in nature. Finally, IMD periodically approaches best-in-class managers to execute a targeted strategy customized to the NCRS portfolio structure.

Phase I - Annual Portfolio Evaluation

Each year, Directors will produce an Annual Investment Work Plan for each asset class. Portfolio and market analysis, cash flow forecasting, availabilities of various vehicles and targeted asset class allocation will be considered to determine the annual capital commitment pace and other cash flows for the asset class, although market opportunities will play an important role in determining interim allocations. The Annual Investment Work Plans will be submitted to the Chief Investment Officer for concurrence, then the Treasurer for approval.

Phase II - Fund Sourcing

Directors will proactively identify a broad universe of relevant offerings in the market from consultants, other investors, and direct outreach from general partners or their placement agents. Directors will proactively build strong relationships and communicate with market participants to access competitive/oversubscribed/soft-closed vehicles that may not be widely marketed or open for only limited periods of time.

In order to effectively track the various opportunities in the market, Directors will maintain a database of potential investment vehicles. This “Opportunity Database” will provide summary descriptive information about each investment opportunity and be used at regular internal asset class staff meetings as the basis for screening the various vehicles. The following procedures shall be used:

1. When staff identifies a viable investment opportunity, the contact and source of the contact will be logged into the Opportunity Database (e.g., Backstop).
2. As additional contacts are made concerning the investment opportunity, staff will log each such contact into the Opportunity Database entry for that potential investment.
3. The Opportunity Database should be updated as offering memoranda and other materials are received and reviewed by staff.

Phase III- Preliminary Fund Screen

Directors must choose from the potential opportunities in the Opportunity Database to identify the most attractive offerings and determining where due diligence resources will be deployed. Directors will choose based on various considerations, including but not limited to:

1. The fit within the Annual Investment Work Plan, overall portfolio construction, market opportunity, statutory classifications and limits, and competing offerings
2. IMD’s history with the firm
3. Prior funds or related investments performance, including co-investments and secondary investments
4. Research by consultants and other third parties on the offering
5. Professional judgment of IMD staff
6. Risk and operational considerations
7. Alignment and conflict of interest considerations
8. Willingness to accept NCRS preferred terms and ability to meet closing requirements

IV. Intensive Due Diligence

Upon selecting the most attractive investment opportunities under the processes identified in the Request for Information Searches (i.e., finalists) or Work Plan and Opportunistic Searches (i.e., opportunities from the Opportunity Database), Directors will conduct an intensive due diligence process for each investment opportunity, with the potential assistance of consultants and third-party research providers. The result of the process may be the recommendation to commit/invest capital in the offerings that are deemed most attractive by the Director.

The intensive due diligence process will include, but not be limited to:

1. Review of the Private Placement Memorandum and other related materials
2. Quantitative analysis of performance, fees, and incentives
3. Assessment of offering versus comparable or competing alternative offerings reasonably available in the market
4. Manager presentations to and/or onsite visit(s) to manager's office(s) by staff, Treasurer, and/or consultant
5. Reference checks with other investors, limited partners, consultants, and other industry contacts
6. Review of risk and operational considerations (identified by staff or consultant)
7. Review of alignment and conflict of interest considerations
8. Collection of the disclosure forms required by the Placement Agent Policy (To facilitate early collection of information and identification of potential issues, staff may ask investment managers and placement agents to submit these forms during the due diligence process as an unsigned draft. The final signed form will be due on the date specified in the Placement Agent Policy.)
9. Assessment of willingness to accept NCRS preferred terms and ability to meet closing requirements

At any point in the intensive due diligence process and during each of the following Sections, a Director, the Chief Investment Officer, or Treasurer may choose to reject the offering or table it for future consideration.

V. Forward Calendar and Coordination with Investment Committee

Directors are responsible for working proactively with the Director of Investment Operations and Risk to help maintain an updated, consolidated, and accurate "Forward Calendar" for purposes of the IMD Investment Committee's oversight of investment manager and vehicle selection. The Forward Calendar will contain the managers and/or vehicles that are deemed the most attractive by the Directors after screening available and potentially viable investment opportunities and, at a minimum, will include any that are the subject of Intensive Due Diligence.

Further, upon placing an entity on the Forward Calendar, Directors are responsible for closely and proactively coordinating with the Chief Risk and Operating Officer, legal counsel, and the Compliance Counsel, to manage obtaining materials and contacts at the entities in the event that an Investment Recommendation Memo is being drafted (see next section).

VI. Investment Recommendation Memorandum

Upon completing the intensive due diligence process, Directors shall prepare an Investment

Recommendation Memo to the Chief Investment Officer in order to pursue the commitment of capital or other investment. This recommendation will include:

1. A “SWOT” analysis (i.e., Strengths, Weaknesses, Opportunities, Threats)
2. Fit within portfolio construction
3. Statutory qualifications
4. Background on the general partner/investment firm
5. Historical returns
6. Investment merits and risks
7. Competitive analysis versus comparable or competing alternative offerings
8. Operational assessment
9. Liquidity provisions
10. Expected contract terms
11. Other relevant information

Consultants’ analysis and third-party research may be relied on to support the recommendation, if reasonable under the circumstances.

Documents to be requested prior to completion of the Investment Recommendation Memo include:

1. Disclosure forms required by Placement Agent Policy
2. Conflict of Interest Certification (*attached as Appendix 1*)
3. Code of Ethics
4. Compliance Manual Table of Contents
5. Organizational Chart
6. Valuation Policy
7. SSAE 16 Certification (if applicable)
8. Insurance Coverage
9. ADV Part I and II
10. Form 8 (Foreign) or Form 9 (U.S.)
11. Audited Financial Statements

The Investment Recommendation Memorandum will also include a statement by the Director, as required by the Placement Agent Policy, listing (1) the person or persons, if any, who initially suggested the investment opportunity to IMD and (2) any persons who appeared before IMD in the marketing or due diligence process on behalf of the proposed External Investment Manager and who were not employees of the proposed External Investment Manager or one of its affiliates. Investor and industry reference calls initiated by Directors may be described generically and without specific identifying information. The final draft of the Investment Recommendation Memo will be provided for the concurrence of the Chief Investment Officer, through the Chief Risk and Operating Officer and Compliance Counsel, and will be accompanied by:

1. All Disclosure forms required by the Placement Agent Policy
2. Compliance and conflict of interest certification forms signed by Treasurer, IMD staff,

consultant (as applicable), subject investment entity, and any related entities that participated in the process (as applicable)⁴

VII. Independent Review by Compliance Counsel

The Compliance Counsel will make an independent review of the Placement Agent Policy disclosure form, the Investment Recommendation Memorandum, and the supporting documents to the Investment Recommendation Memorandum listed above. Directors should ensure that these documents are provided to the Compliance Counsel as soon as possible. Placement Agent Policy disclosure letters shall be provided to the Compliance Counsel at least one month before the anticipated closing of the transaction. Based on these documents, the Compliance Counsel will complete a signed Compliance Review Form that includes the following:

1. The Compliance Counsel's approval of the disclosure forms under the Placement Agent Policy with respect to responsiveness and completeness
2. The Compliance Counsel's report concerning any aspect of the transaction's recommendation, negotiation, or approval that, in the view of the Compliance Counsel, may reasonably violate any law, regulation, or Department policy
3. The Compliance Counsel's report concerning any aspect of the transaction's recommendation, negotiation, or approval that, in the view of the Compliance Counsel, raises significant reputational risk concerns related to conflicts of interest; i.e., whether circumstances in fact exist that create a material risk that professional judgment or actions regarding the transaction's recommendation, approval, or execution have been or will be unduly influenced by a direct or indirect personal interest⁵

Should the Compliance Counsel determine that the test stated by item (1) above is not met, he or she shall contact the External Investment Manager or Department staff to seek correction of the disclosure forms. Should the Compliance Counsel determine that the test stated by items (2) or (3) may not be met, the Compliance Counsel will promptly notify the Chief Investment Officer and General Counsel. The Chief Investment Officer has the authority to reject the offering or refer it to the Investment Committee to consider input from the Compliance Counsel and legal counsel on the materiality of the risk and recommended approaches to remediate the risk: recusal, third-party due diligence, etc.

The Compliance Counsel will forward the completed Compliance Review Form to the Chief Investment Officer.

If necessary, because of a condensed time frame for the transaction, the following steps may take place simultaneously with the review of the transaction by the Compliance Counsel. However, the transaction **may not** be submitted to the Treasurer for execution without an Investment Memorandum and its attachment reviewed by the Chief Investment Officer (or delegate), conflict of interest certifications, and a final, signed Compliance Review Form based on review of the complete and finalized record by the Compliance Counsel.

⁴ External counsel conflict checks, and any required waivers granted, will be coordinated by General Counsel's Office.

⁵ See Footnote 4.

VIII. Conditional Approval

The Chief Investment Officer is responsible for evaluating the Director's recommendation(s) including giving due consideration to input as received from the Investment Committee from time-to-time. The Chief Investment Officer may reject the recommendation, request changes or provide other feedback to the Director, or forward the recommendation to the Treasurer to receive conditional approval of the transaction. Unless otherwise expressly approved in writing by the Chief Investment Officer, conditional approval must be obtained before initiating the negotiation and contracting process described below. The Chief Investment Officer will regularly update the Treasurer on the Forward Calendar, including the status of pending and conditionally approved recommendations.

IX. Negotiations and Contracting

Upon conditional approval of the recommendation, the Director and external or DST internal legal counsel will negotiate contractual documents with the selected entity, with the Chief Investment Officer, and the Compliance Counsel involved to the extent necessary.

X. Final Approval

The Chief Investment Officer or General Counsel will provide to the Treasurer each of the following:

1. The final contractual documents, ready for execution
2. Memo from legal counsel concerning the final contractual documents, comparing actual terms to the NCRS preferred terms and addressing other items that were subject to material negotiations
3. The final Investment Recommendation Memorandum
4. The final Compliance Review Form signed by the Compliance Counsel
5. Compliance and conflict of interest certification forms (*attached as Appendix 1*) signed by the relevant Director, the Compliance Counsel, the Chief Investment Officer, and the Treasurer

The Treasurer shall then execute the documents or reject the transaction.

XI. External Communication Protocol

This portion of the policy specifically applies the principles of DST's *No Contact Policy* to communications between DST and investment managers concerning potential new commitments or new relationships. In the event of any perceived conflict between this policy and the *No Contact Policy*, the more detailed text in this policy will govern the issue.

Except where necessary, IMD staff, the Chief Investment Officer, and the Treasurer shall not use personal e-mail addresses to communicate with fund managers or placement agents regarding state business related to the investment of funds. Personal e-mail addresses may be used only in an emergency, and if the DST e-mail system is not functioning. All emails must be encrypted, regardless of email system used. Any DST documents sent using a personal e-mail account must be promptly copied by IMD staff onto the CRM system ("Backstop") or IMD shared drive.

Once either an investment opportunity has been referred to a Director *and* the Director has provided notice of this fact to the investment manager, or a Request for Information Search has been announced, the following procedures apply:

1. The Director (or designee) will be the point of contact for all communication with representatives of the investment manager. Communication between the Director and the investment manager's employees or registered placement agent is not limited under DST policy.
2. Participation by various IMD staff and the Treasurer in investment managers' presentations scheduled by the applicable Director will occur in the normal course of the diligence activities described in this policy.
3. The investment manager and its placement agent should not contact other DST staff, the Treasurer, or Investment Advisory Committee members regarding the merits of the investment manager, regarding whether IMD should retain the manager, or regarding whether IMD should make the investment commitment. Any such contact may be cause for rejection in the sole discretion of the Treasurer.
4. The investment manager may continue to contact DST, as normal, concerning other funds and day-to-day business interaction. Interactions at social events also are not prohibited. In either case, the topic of the potential new investment should not be discussed.
5. In the event that the investment manager or any other external parties feel it is necessary to escalate concerns about the adequacy of the IMD evaluation process, they may contact the Chief Investment Officer or the Treasurer to raise those concerns. Every effort should be made to direct those external parties first to the Chief Investment Officer.

This Policy contemplates that numerous investment opportunities will be identified, evaluated, rejected, or tabled for future consideration. Directors will be proactive in promptly communicating with investment managers, placement agents, etc. that have actively engaged with IMD on diligence but that

have been eliminated under a Request For Information Search or do not survive an "Initial Fund Screen" or subsequent evaluation, negotiation or approval steps (as applicable).

XII. Revision History and Effective Date

This Policy is effective July 1, 2013.

Version/Revision	Date Approved	Description of Changes
1	June 5, 2013	Original Version
1.1	December 10, 2013	Changes to conform with revised Placement Agency Policy; clarifications to role of Compliance Counsel
1.1	September 21, 2016	Appendix 1 revised effective September 1, 2016. Policy otherwise unchanged
1.1	February 9, 2018	Policy reviewed, no changes made.
1.2	October 13, 2020	Clarifications and Technical Changes

SUBMISSION AND APPROVAL

Submitted:



Christopher Morris
Co-Chief Investment Officer

Date: 10-13-2020

Approved:



Dale R. Folwell, CPA
North Carolina State Treasurer

Date: 10-13-2020

NORTH CAROLINA DEPARTMENT OF STATE TREASURER
INVESTMENT MANAGEMENT DIVISION

External Investment Management Conflict of Interest Certification

When form is required. The Department of State Treasurer personnel listed below shall read, complete, and forward to the Compliance Counsel and the Director of Risk Management and Asset Allocation this form for each:

- A new commitment of funds, new investment management agreement, or any other "Investment Transaction" as defined in the *Placement Agent Policy*; or
- "Substantive Amendment" as defined in the *Placement Agent Policy*.

Definitions. For the purposes of this form:

- "External Investment Manager" shall have the meaning provided in the *External Investment Manager and Vehicle Selection Policy and Procedures*.
- "Conflict of interest" shall mean circumstances that create a material risk that professional judgment or actions regarding the transaction's recommendation, approval, or execution have been or will be unduly influenced by a direct or indirect personal interest.
- "Family" shall mean immediate family (mother, father, brother, sister, wife, husband, or child), either by birth, by marriage, by engagement to be married, or through a live-in domestic partnership that is similar to marriage; lineal ascendants (grandparents, etc.); and lineal descendants (grandchildren, etc.).

Name of External Investment Manager and Fund: _____

I understand and have adhered to the Department of State Treasurer, Investment Management Division's *Code of Ethics and Conduct* and other applicable policies in this recommendation, negotiation, and approval process and certify my participation in this process is not precluded, because to the best of my knowledge:

1. My Family and I have NO material financial interest in the External Investment Manager and will not receive a financial benefit derived from the compensation provided to the Manager.
2. My Family and I are NOT employees or directors of the External Investment Manager.
3. I have NOT been employed with the External Investment Manager within the past five (5) years.
4. I have NOT sought employment NOR discussed potential employment with the External Investment Manager.
5. I have NO Conflicts of Interest in the recommendation, negotiation, and/or approval of the External Investment Manager.
6. I voluntarily choose to disclose the following facts which I believe do not constitute a Conflict of Interest and do not preclude my unbiased participation in the recommendation, negotiation, and/or approval of the External Investment Manager. (If so, initial in the left margin and make any disclosure on attached sheets.)
7. I understand that I have an ongoing obligation to update any changes to this form prior to closing.

Portfolio Manager: _____

Date: ___

Director: _____

Date: ___

Chief Investment Officer: _____

Date: ___

General Counsel: _____

Date: ___

State Treasurer: _____

Date: ___

