

State Board of Administration

**Investment Advisory Council and
Audit Committee Joint Meeting**

November 14, 2011



INVESTING FOR FLORIDA'S FUTURE

Call to Order/Opening Remarks

Ash Williams

SBA Investment Search, Selection and Monitoring Process Overview

Kevin SigRist

→ Presentation Outline

- Policy Background
- Search and Selection Processes
 - Public Markets
 - Private Market Funds
 - Direct-owned Real Estate
- Manager Monitoring

→ Policy Background on Advisor Search & Selection: Investment Policy Statement

- The Executive Director has investment responsibility for maintaining diversified portfolios, and maximizing returns with respect to the broad diversified market standards of individual asset classes, consistent with appropriate risk constraints. (Section IV)
- The Executive Director will develop policies and procedures to:
 - Identify, monitor and control/mitigate key investment and operational risks.
 - Maintain an appropriate and effective risk management and compliance program that identifies, evaluates and manages risks within business units and at the enterprise level.
 - Maintain an appropriate and effective control environment for SBA investment and operational responsibilities.
 - Approve risk allocations and limits, including total fund and asset class risk budgets. (Section IV)
- The Executive Director shall develop guidelines for the selection and retention of portfolios, and shall manage all external contractual relationships in accordance with the fiduciary responsibilities of the Board. (Section VIII)

FRS Pension Plan Active Risk Budget Monitoring Standards

	Active Risk		Active Share
TAA/ Asset Class	Monitoring Standard	Current Market Standard	
Tactical Asset Allocation	0.20%	0.40%	--
Global Equity	1.00%	1.50%	[40%, 60%]**
Fixed Income	0.75%	1.25%	[50%, 75%]
Real Estate	5.00%	8.00%	--
Private Equity (secondary benchmark)	6.00%	10.00%	--
Strategic Investments	4.00%	6.00%	--
Cash	0.10%	0.20%	--
Total Fund	1.00%	1.50%	

**Intra-Asset Class Ranges & Maximum Individual Portfolio Allocation as Percent of Asset Class for
FRS Pension Plan as of August 31, 2011**

	Actual Allocation	Intra-AC Ranges	Within Range	Max Individ. Portfolio	Within Range
Domestic Equities					
Traditional Active	7%	0% to 12%	Yes	5%	Yes
Enhanced Index	6%	0% to 18%	Yes	10%	Yes
Other	6%	0% to 10%	Yes	5%	Yes
Passive	80%	75% to 85%	Yes	85%	Yes
Foreign Equities					
Traditional Active	54%	20% to 60%	Yes		
<i>Developed</i>	26%	--	--	10%	Yes
<i>Developed Small Cap</i>	7%	--	--	2%	Yes
<i>Emerging Markets</i>	21%	--	--	6%	Yes
Enhanced Index	19%	15% to 40%	Yes		
<i>Developed</i>	14%	--	--	12%	Yes
<i>Developed Small Cap</i>	3%	--	--	5%	Yes
<i>Emerging Markets</i>	2%	--	--	8%	Yes
Other	2%	0% to 15%	Yes	8%	Yes
Passive	25%	10% to 40%	Yes	40%	Yes
Fixed Income					
Traditional Active	31%	10% to 30%	No	20%	Yes
<i>Active Core</i>	13%	--	--	15%	Yes
Enhanced Index	13%	10% to 25%	Yes	20%	Yes
Other	2%	0% to 5%	Yes	5%	Yes
Passive	54%	50% to 75%	Yes	75%	Yes

**Intra-Asset Class Ranges & Maximum Individual Portfolio Allocation as Percent of Asset Class for
FRS Pension Plan as of August 31, 2011**

	Actual Allocation	Intra-AC Ranges	Within Range	Max Individ. Portfolio	Within Range
Real Estate					
Public	12%	5% to 15%	Yes	10%	Yes
Private	88%	85% to 95%	Yes	35%/10%*	Yes
<i>Core (June 2011)</i>	85%	70% to 100%	Yes	--	--
<i>Non-Core (June 2011)</i>	15%	0% to 30%	Yes	--	--
Private Equity					
Leveraged Buyout	82%	50% to 80%	No	--	--
Venture Capital and Growth Capital	12%	5% to 20%	Yes	--	--
Special Situations	5%	10% to 30%	No	--	--
Strategic Investments					
Debt-Oriented	62%	10% to 60%	No	--	--
Hedge Fund and Related Vehicles	24%	30% to 70%	No	--	--
Real Assets	0%	0% to 15%	Yes	--	--
Other Opportun. & Special Situations	14%	0% to 15%	Yes	--	--

*35% for Separate Account Investment Advisors and 10% per fund.

** Global Equity intra-asset class allocations for Domestic Equities and Foreign Equities will be utilized pending Mercer Review.
See August 8, 2011 & September 13, 2011 SIG meeting materials and meeting minutes.

→ Catalysts for Search & Selection Activities

- Asset allocation policy changes
 - Revised long-term target policy allocations
 - New asset class
 - New performance benchmark
- Structural or business model changes to asset classes
- New or opportunistic initiatives: styles/strategies/vehicles
- Capacity requirements
- Manager terminations
- Annual private market work plans
 - Expected fund raising cycle by various general partners
 - Due diligence activities by staff and consultants with existing and potential new relationships
 - Portfolio construction considerations

→ SBA Public Market Search & Selection Process Overview

- Need determined by Senior Investment Officer
- Deputy Executive Director (DED) approves the Search Criteria
- SBA and Consultant develop a list of firms to receive a questionnaire, form of contract, SBA policies, etc.
- Finalist firms are interviewed by SBA and Consultant with recommendations to select provided through Risk Management & Compliance to DED for concurrence and Executive Director/CIO for approval
- Contracting staffed by General Counsel's Office, with participation from Risk Management & Compliance, and asset class

→ SBA Private Market Standard Search & Selection Process Overview

- Annual Work Plan sets out a forward calendar of targeted funds and other vehicles, plus unallocated amounts for funds TBD, based on:
- SBA and Consultants regularly interact to prioritize/screen general partners in market or expected to come to market so as to deploy due diligence resources
- SBA and Consultant independently conduct due diligence to support a recommendation to proceed to legal negotiations. Recommendations to contract communicated through Risk Management & Compliance to DED for concurrence and Executive Director/CIO for approval
- Contracting, including side-letter, conducted by external counsel, with oversight/input from General Counsel's Office, and participation from Risk Management & Compliance and asset class

→ SBA Private Market New/Specialized Initiatives Search & Selection Process Overview

- Annual Work Plan describes new and specialized initiatives in various stages of research and implementation, e.g.:
 - Corporate Governance/Activist Strategies
 - Infrastructure
 - Timberland
 - Hedge funds
- SBA selects a Specialist Consultant to advise on the opportunity set, portfolio construction and vehicle structuring, and assist in evaluating candidate managers/funds through questionnaires and interviews
- SBA and Consultant independently conduct due diligence to support a recommendation to proceed to legal negotiations. Recommendations to select communicated through Risk Management & Compliance to DED for concurrence and Executive Director/CIO for approval
- Contracting, including side-letter, conducted by external counsel, with oversight/input from General Counsel's Office, and participation from Risk Management & Compliance and asset class

→ SBA Real Estate Direct-Owned Search & Selection Process Overview

- Annual Work Plan describes expected allocation to Principal Investments Fund
- SBA regularly interacts with separate account Investment Advisors and periodically with consultants, brokers and operators to communicate desirable asset characteristics based on Work Plan, portfolio construction considerations and market conditions
- Investment Advisor typically identifies potential acquisition target and conducts initial pro forma analysis for review by SBA
- SBA and Investment Advisor independently conduct due diligence to support a recommendation to proceed to legal negotiations. Recommendations to acquire communicated through Risk Management & Compliance to DED for concurrence and Executive Director/CIO for approval
- Contracting, including side-letter, conducted by external counsel, with oversight/input from General Counsel's Office, and participation from Risk Management & Compliance and asset class

→ SBA Manager/Fund Monitoring Overview

- Public market investment managers (internal and external) are subject to quarterly monitoring by Consultant and SBA
 - Quantitative criteria focus on performance
 - Qualitative factors focus on organization, people, process, AUM, litigation, style drift, etc.
- Private market managers/funds/partners are subject to quarterly performance monitoring by Consultant and SBA and an annual review of qualitative factors

Evaluation of SBA Investment Search, Selection and Monitoring Policies

Mike Sebastian, Hewitt EnnisKnupp
Kristen Doyle, Hewitt EnnisKnupp



Review of Manager Monitoring Guidelines & Policies

November 2011

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Overview

- HEK reviewed the SBA's Executive Director and Deputy Executive Director manager search and selection policies

- Review also included the Investment Manager Monitoring Guidelines

- We conclude that the policies:
 - Appropriately establish clear roles and responsibilities;
 - Focus on critical aspects of manager evaluation;
 - Establish thorough processes and procedures;
 - Provide clear compliance procedures; and
 - Allow flexibility for staff to adapt to each unique circumstance

- Recommendations: Provided on slide 24

Key Criteria for External Manager Policies

- Clearly defined roles and responsibilities for the Executive Director/CIO and staff members
- Clearly defined process to be employed when conducting manager searches and making termination decisions
- A focus on evaluating managers on both qualitative and quantitative factors
- Procedures that specify ongoing monitoring of external managers
- Focus on longer-term performance and risk (5 years or longer) when evaluating quantitative factors

Recommendations

Investment Management Acquisition Policy

- Provide clarification as to what occurs or who makes the final decision should the Executive Director have a conflict of interest during the investment management acquisition process
- In the Compliance section, reference the Senior Investment Officer policies and procedures that are established

Investment Manager Monitoring Guidelines

- Clarify whether the qualitative factors guarantee inclusion on the Watch List or whether that is discretionary based on the evaluation by staff and the consultant – Currently, the Quantitative Factors note that the factor “may” result in inclusion and the Action Steps note to “Consider placing on Watch List”. Therefore, consider making Qualitative and Quantitative Factors consistent

Case Study: Ramius Search and Selection Process

Kevin SigRist, SBA

Trent Webster, SBA

Eileen Neill, Wilshire Associates

Review of Public Records Law and SBA Procedures

Maureen Hazen, SBA
Dennis MacKee, SBA

→ **Public Policy & Florida Constitution**

- Public policy of the State of Florida to have transparency in government affairs and in the conduct of the official business of the government
- The public's right to access records is recognized in Art. I, s. 24, Fla. Const., with exceptions only by law or the Constitution

→ Florida's Public Records Law

- The Public Records Law (Chapter 119, Fla. Stat.) provides a statutory right to access records in furtherance of the constitutional mandate
- Purpose of Chapter 119 is “to open public records to allow Florida’s citizens to discover the actions of their government.” [*Christy*, 698 So. 2d 1365 (Fla. 4th DCA 1997)].

→ Florida's Public Records Law

- The law provides: “[e]very person who has custody of a public record shall permit the record to be inspected and copied by any person desiring to do so, at any reasonable time, under reasonable conditions, and under supervision by the custodian of the public records.” (s. 119.07(1)(a), Fla. Stat.)

→ Florida's Public Records Law

- The law defines “Public Records” as “all documents, papers, letters, maps, books, tapes, photographs, films, sound recordings, data processing software, or other material, regardless of the physical form, characteristics, or means of transmission, made or received pursuant to law or ordinance or in connection with the transaction of official business by any agency (s. 119.011(12), Fla. Stat.)”

→ Exemptions to the Public Records Law

- Art. I, s. 24(c), Fla. Constit. authorizes the Legislature to enact laws creating exemptions to the FPRL provided such laws “shall state with specificity the public necessity justifying the exemption and shall be no broader than necessary to accomplish the stated purpose of the law.”

→ Exemptions to the Public Records Law

- The Public Records Act must be liberally construed in favor of open government , and exemptions from disclosure are to be narrowly construed. (*Krischer*, 674 So.2d 909 (Fla. 4th DCA 1996).)
- Exemptions in law will provide the records are either “exempt” or “confidential and exempt” from s. 119.07(1) and Art. I, s.24(a), Fla. Const.

→ Exemptions to the Public Records Law

- If Florida Statutes provide information is confidential and exempt, then the information is not subject to inspection by the public, and the agency may release only to those persons and entities designated by statute. [*WFTV, Inc.*, 892 So.2d 1015 (Fla. 2004)].

→ SBA Records and Exemptions

- Most of the SBA's records do not contain any information that is confidential and exempt from disclosure
- However, there are a limited number of exemptions applicable to the SBA's records

→ SBA Records and Exemptions

Some examples:

- Social Security Numbers – F.S. 119.071(4), (5)
- SBA Account Numbers – F.S. 119.071(5)(b)
- Certain Security Systems records – F.S. 281.301, 282.318
- Attorney Work Product – F.S. 119.071(1)(d)
- SBA “in progress” investments – F.S. 215.4401(2)
- SBA alternative investments – F.S.215.4401(3)
- Trade Secrets – F.S. 812.045 by application of *Sepero*, 839 So.2d 781 (Fla. 1st DCA 2003)

→ Florida's Public Records Law - Costs

- Duplication - s. 119.07(4), Fla Stat., permits an agency to charge a fee of up to \$0.15 per one-sided copy (and no more than an additional \$.05 for each two-sided copy) for copies not more than 14 inches by 8 ½ inches and for all other copies, the actual cost of duplication

→ Florida's Public Records Law – Special Service Charge

- Special Service Charge - s. 119.07(4)(d) provides “[i]f the nature or volume of public records requested to be inspected or copied pursuant to this subsection is such as to require extensive use of information technology resources or extensive clerical or supervisory assistance by personnel of the agency involved, or both, the agency may charge, in addition to the actual cost of duplication, a special service charge, which shall be reasonable and shall be based on the cost incurred for such extensive use of information technology resources or the labor cost of the personnel providing the service that is actually incurred by the agency or attributable to the agency for the clerical and supervisory assistance required, or both.”

→ Florida's Public Records Law – Special Service Charge

- An agency may impose a special service charge if the volume of records and the number of potential exemptions make review and redaction of the records a time-consuming task. (*Florida Institutional Legal Services*, 579 So.2d 267 (Fla. 1st DCA 1991).)

→ SBA Process – PR Requests

- In addition to Florida Constitution, Florida Statutes and case law, SBA Policies 10-032 and 10-051 set forth general steps for handling of public records requests

→ SBA Process – PR Requests

- Steps

1. SBA staff/Director of Communications receives a public records request and forwards the request to the General Counsel's Office.
2. GC Office staff (generally the SBA's Paralegal – Public Records) reviews the request and determines the appropriate sources of records possibly responsive to the request.

→ SBA Process – PR Requests

3. The GC's Office contacts people that may have responsive records and evaluates and estimates the amount of staff time required to fulfill the request.
4. If the request does not involve duplication or special service charges, then the GC's Office begins gathering responsive documents.

→ SBA Process – PR Requests

5. If the request does involve duplication or special service charges, the GC's Office prepares a estimate and communicates estimated costs to the requestor.
6. If the requestor pays or agrees to pay the charges, the GC's Office gathers potentially responsive records and reviews the records for (A) responsiveness and (B) exemptions.

→ SBA Process – PR Requests

7. If the responsive records do not contain any information that may be confidential and exempt from disclosure, then the GC's Office contacts the requestor to determine delivery method (or delivers the records as previously directed by the requestor).

→ SBA Process – PR Requests

8. If the responsive records contain information that may be confidential and exempt that can be redacted by the SBA (e.g. social security and account numbers), then the GC's Office redacts that information.
9. If the responsive records contain information that may be confidential and exempt but can only be redacted by a third person proprietor (e.g. alternative investment and trade secret records), then the GC's Office contacts the proprietor.

→ SBA Process – PR Requests

10. If the third person proprietor claims certain information is confidential and exempt from disclosure by following the legal requirements, then the GC's Office receives and reviews the redacted records and any declaration and contacts the requestor to determine delivery method (or delivers as previously directed by the requestor).

→ SBA Process – PR Requests

11. If the third person proprietor does not claim any information is confidential and exempt, then the GC's Office contacts the requestor to determine delivery method (or delivers as previously directed by the requestor).

Council and Committee Discussion of Next Steps/Adjourn

Rob Gidel, Investment Advisory Council Chair
Judy Goodman, Audit Committee Chair