North Dakota State Investment Board

Friday, July 27, 2018, 8:30 a.m.
Bismarck State College
National Energy Center of Excellence
Energy Generation Conference Room #335
1500 Edwards Avenue Bismarck, ND

AGENDA

I. CALL TO ORDER AND ACCEPTANCE OF AGENDA

II. ACCEPTANCE OF MINUTES (May 25, 2018)

III. ELECTION OF OFFICERS AND APPOINTMENTS for 2018-19 *(10 minutes)*

A. Chair **(Board Action)**
B. Vice Chair **(Board Action)**
C. Parliamentarian **(Appointed by Chair)**
D. Audit Committee – Mr. Hunter **(Board Action)**
E. Securities Litigation Committee – Mr. Hunter **(Affirmation)**

IV. INVESTMENT GOVERNANCE *(20 minutes)*

A. PERS Job Service Investment Policy Statement - Mr. Hunter **Board Acceptance**
B. Code of Conduct Affirmation - Mr. Schmidt *Informational*
C. Private Equity Update - Mr. Hunter **Board Action**
D. Investment Consulting Contract Update – Mr. Hunter *Informational*

V. BOARD EDUCATION

A. Fundamental Investment Beliefs – Mr. Hunter *Informational* (5 mintues)
B. Callan - Performance Benchmarks – Mr. Erlendson & Mr. Browning *Informational (1 hour)*
C. Board Member Education Options – Mr. Hunter *Informational (10 minutes)*

========================= Suggested Break from 10:15 to 10:30 a.m. ===========================

D. Epoch Investments Market Update – Mr. Bill Priest and Mr. Jeff Ulness *Informational (1 hour)*

VI. OTHER *(15 minutes)*

A. RIO Update: Budget, VSIP and Investment Returns – Mr. Hunter *Informational*
B. RIO Strategy Review (Office of the Governor Presentation) – Mr. Hunter *Informational*

Next Meetings: Securities Litigation Committee - Aug. 23, 2018, 3:00pm, RIO, 3442 East Century Ave., Bismarck
SIB - Aug. 24, 2018, 8:30am - State Capitol, Peace Garden Room
Audit Committee - Sep. 27, 2018, 10:00am - RIO, 3442 East Century Ave., Bismarck

VII. ADJOURNMENT

Note: The meeting is scheduled to adjourn before Noon.

NORTH DAKOTA STATE INVESTMENT BOARD
MINUTES OF THE
MAY 25, 2018, BOARD MEETING

MEMBERS PRESENT: Rob Lech, TFFR Board, Vice Chair
Mike Burton, TFFR Board
Jon Godfread, Insurance Commissioner
Adam Miller, PERS Board
Mel Olson, TFFR Board
Kelly Schmidt, State Treasurer
Jodi Smith, Commissioner of Trust Lands
Yvonne Smith, PERS Board (TLCF)
Cindy Ternes, WSI Designee
Kim Wassim, PERS Board

MEMBERS ABSENT: Brent Sanford, Lt. Governor, Chair
Troy Seibel, PERS Board

STAFF PRESENT: Eric Chin, Senior Investment Officer
Connie Flanagan, Fiscal & Invt Ops Mgr
Bonnie Heit, Assist to the SIB
David Hunter, ED/CIO
Fay Kopp, Dep ED/CRA
Sara Sauter, Audit Svs Suprv
Cody Schmidt, Compliance Officer
Darren Schulz, Dep CIO
Susan Walcker, Invt Acct

OTHERS PRESENT: Brian Barrett, Apt., Inc.
Alex Browning, Callan Associates
Jack Dura, Bismarck Tribune
Paul Erlendson, Callan Associates
Bryan Klipfel, Workforce Safety & Insurance
Anders Odegaard, Attorney General's Office
Tim Porter, Bank of North Dakota
Bryan Reinhardt, PERS
Tom Stromme, Bismarck Tribune

CALL TO ORDER:

Mr. Rob Lech, Vice Chair, called the State Investment Board (SIB) regular meeting to order at 8:30 a.m. on Friday, May 25, 2018, at the State Capitol, Peace Garden Room, Bismarck, ND.

AGENDA:

IT WAS MOVED BY MR. OLSON AND SECONDED BY MS. TERNES AND CARRIED BY A VOICE VOTE TO ACCEPT THE AGENDA FOR THE MAY 25, 2018, MEETING.

AYES: COMMISSIONER SMITH, TREASURER SCHMIDT, MR. MILLER, COMMISSIONER GODFREAD, MR. OLSON, MS. TERNES, MR. BURTON, MS. WASSIM, MR. LECH, AND MS. SMITH

NAYS: NONE
MOTION CARRIED
ABSENT: LT. GOVERNOR SANFORD

MINUTES:

IT WAS MOVED BY COMMISSIONER SMITH AND SECONDED BY COMMISSIONER GODFREAD AND CARRIED BY A VOICE VOTE TO ACCEPT THE MINUTES OF THE APRIL 27, 2018, MEETING AS DISTRIBUTED.

AYES: MR. BURTON, COMMISSIONER SMITH, MS. SMITH, MS. TERNES, TREASURER SCHMIDT, MR. LECH, COMMISSIONER GODFREAD, MR. OLSON, MS. WASSIM, AND MR. MILLER

NAYS: NONE
MOTION CARRIED
ABSENT: LT. GOVERNOR SANFORD

INVESTMENTS:

Asset and Investment Performance – Mr. Hunter highlighted the SIB clients' assets currently under management for the quarter ending March 31, 2018.

SIB client investments exceeded $13.4 billion with the Pension Trust exceeding $5.6 billion, Legacy Fund approaching $5.4 billion, and the Insurance Trust nearing $2.1 billion.

The Pension Trust posted a net return of 12.3% in the last year. During the last 5-years, the Pension Trust generated a net annualized return of 8.3%, exceeding the performance benchmark of 7.3%. The Legacy Fund generated a net return of 10.2% last year, exceeding its policy benchmark. During the last 5-years, the Legacy Fund earned a net annualized return of 5.8%, exceeding the performance benchmark of 4.8%. The Insurance Trust generated a net return of 7.5% in the last year. During the last 5-years, the Insurance Trust posted a net annualized return of 5.0%, exceeding the performance benchmark of 3.7%.

RIO investment personnel estimates the SIB use of active management enhanced client returns by over $300 million since March 31, 2013. RIO's internal investment cost for administering the investment programs is less than 1 basis point or 0.01%.

Every Pension Trust client posted positive excess returns of at least 0.70% per annum over the last 5-years, while adhering to approved risk levels and generating at least 0.35% of positive risk adjusted excess return.

Every Non-Pension trust client generated positive excess returns of at least 0.65% per annum and positive risk adjusted excess returns for the 5-years ended March 31, 2018, with two exceptions for PERS Retiree Health Insurance Credit Fund (-0.08%) and PERS Group Insurance (-0.05%).

Risk as measured by standard deviation, was within approved levels for all SIB clients for the 5-years ended March 31, 2018.

Callan Performance Review – Callan representatives reviewed economic and market environments for the period ending March 31, 2018, as well as performance of the Pension Trust, Insurance Trust, and Legacy Fund for the same time period.

IT WAS MOVED BY TREASURER SCHMIDT AND SECONDED BY COMMISSIONER GODFREAD AND CARRID BY A ROLL CALL VOTE TO ACCEPT THE CALLAN PERFORMANCE EVALUATION REPORT FOR THE QUARTER ENDING MARCH 31, 2018.

AYES: MR. OLSON, MS. WASSIM, COMMISSIONER SMITH, MR. BURTON, COMMISSIONER GODFREAD, MS. SMITH, MR. MILLER, TREASURER SCHMIDT, MS. TERNES, AND MR. LECH
NAYS: NONE
MOTION CARRIED
ABSENT: LT. GOVERNOR SANFORD

Legacy Fund Asset Allocation and Spending Study – Callan representatives presented the results of the Legacy Fund asset allocation and spending study.

Callan Associates previously presented the results to the Legacy and Budget Stabilization Fund Advisory Board (LBSFAB) at their May 24, 2018, meeting. The LBSFAB accepted the results of the asset allocation and spending study and remained committed to the current allocation of 50% equity, 35% fixed income, and 15% real assets.

Callan Associates and RIO investment personnel recommended to also maintain the current asset allocation.

After the SIB review and discussion,

IT WAS MOVED BY TREASURER SCHMIDT AND SECONDED BY MR. OLSON AND CARRIED BY A ROLL CALL VOTE TO ACCEPT CALLAN ASSOCIATES, RIO INVESTMENT PERSONNEL, AND THE LBSFAB RECOMMENDATIONS TO MAINTAIN THE CURRENT ASSET ALLOCATION OF THE LEGACY FUND - 50% EQUITY, 35% FIXED INCOME, AND 15% REAL ASSETS.

AYES: TREASURER SCHMIDT, MR. BURTON, COMMISSIONER GODFREAD, MS. TERNES, COMMISSIONER SMITH, MS. SMITH, MR. LECH, MR. MILLER, MS. WASSIM, AND MR. OLSON
NAYS: NONE
MOTION CARRIED
ABSENT: LT. GOVERNOR SANFORD

The SIB recessed at 10:16 am and reconvened at 10:32 am

Bank of North Dakota (BND) Match Loan Programs – Mr. Hunter updated the SIB on the BND Matching and Infrastructure Loan Programs. BND requested increasing Legacy Fund investments in bank Certificates of Deposits (CDs) in order for the bank to increase funding available for the matching loan program and an infrastructure loan program. RIO investment personnel considered this request as the asset allocation study was being conducted by Callan. Callan recommended that RIO seek indicative pricing on BND CDs from its fixed income managers in order to determine the appropriate credit and liquidity spreads for the proposed program. RIO investment personnel reached out to three of the SIB's largest fixed income managers to obtain indicative pricing for BND CD's issued for terms of up to 10-years. Indicative pricing estimates widened at the 5-year term and ranged from a negative 0.08% to 1-year US Treasury yields to a positive 1.00% to 10-year US Treasury yields. Based on this indicative pricing analysis, RIO proposed spreads to BND representatives on May 18, 2018. Based on preliminary discussion, BND did not appear to be interested in aggressively pursuing the option at the indicative pricing levels. RIO investment personnel intend to meet with BND representatives to continue this discussion further noting that pricing levels, including credit and liquidity spreads, change over time.

Treasurer Schmidt and Mr. Lech commended RIO investment personnel for their excellent work in approaching this request which also assists the SIB in doing their job.

Infrastructure Benchmark – RIO requested Callan to review the current infrastructure benchmark and consider recommending a new benchmark which would better evaluate the contribution of the infrastructure investment within those SIB funds that utilize this asset class. Mr. Hunter requested the SIB approve Callan's recommendation to adopt a new custom benchmark for infrastructure.

IT WAS MOVED BY MR. OLSON AND SECONDED BY MR. MILLER AND CARRIED BY A ROLL CALL VOTE TO ACCEPT STAFF RECOMMENDATION AND APPROVE CALLAN'S RECOMMENDATION TO ADOPT A NEW CUSTOM BENCHMARK FOR INFRASTRATURE ON A PROSPECTIVE BASIS BEGINNING JULY 1, 2018.

AYES: MS. TERNES, MR. OLSON, COMMISSIONER GODFREAD, TREASURER SCHMIDT, COMMISSIONER SMITH, MR. LECH, MR. MILLER, AND MR. BURTON
NAYS: NONE

MOTION CARRIED
ABSENT: LT. GOVERNOR SANFORD, MS. SMITH, MS. WASSIM

Workforce Safety and Insurance Investment Policy Statement – Mr. Hunter presented a revised Investment Policy Statement for Workforce Safety and Insurance for the SIB's consideration. Callan conducted an asset allocation study during the first calendar quarter of 2018. The WSI Board approved Callan's recommended asset allocation changes on April 25, 2018.

IT WAS MOVED BY MS. TERNES AND SECONDED BY COMMISSIONER SMITH AND CARRIED BY A ROLL CALL VOTE TO ACCEPT THE REVISED INVESTMENT POLICY STATEMENT FOR THE WORKFORCE SAFETY AND INSURANCE FUND.

AYES: MS. TERNES, COMMISSIONER GODFREAD, MR. OLSON, MR. MILLER, TREASURER SCHMIDT, MR. BURTON, MS. SMITH, COMMISSIONER SMITH, AND MR. LECH
NAYS: NONE
MOTION CARRIED
ABSENT: LT. GOVERNOR SANFORD, MS. WASSIM

ADMINISTRATION:

Audit Committee – Ms. Sauter reported on the May 24, 2018 Audit Committee meeting. Mr. Thomas Rey, CliftonLarsonAllen (CLA), presented the audit scope and approach for the July 1, 2017 – June 30, 2018 fiscal year financial audit of RIO. Mr. Rey also reviewed the audit results for the GASB 68 schedules (schedules of employer allocations and pension amounts by employer) for the period ending June 30, 2017. An unmodified clean opinion was issued on the statements.

Ms. Sauter also presented on third quarter audit activities which included education on internal auditing.

Ms. Sauter presented a work plan for the Committee's consideration. The work plan was put on hold until Ms. Sauter conducts a formal risk assessment of RIO. A new work plan based on the results of the risk assessment will be presented to the Audit Committee at their September 27, 2018 meeting.

The TFFR Employer Audit Reporting process is being reviewed by the TFFR Board to include providing the final employer report to the School Board. Ms. Sauter will follow-up on this topic once the TFFR Board addresses it.

Membership on the Audit Committee will be reviewed by the SIB at their July 27, 2018 meeting. There is an opening for a TFFR representative.

Ms. Ternes commended Ms. Sauter for all of her work since coming on board January 1, 2018, especially towards the work plan. The Audit Committee is very pleased with the direction Ms. Sauter is taking the organization with the Internal Audit Program. Ms. Sauter has built a good rapport with her teammates and management.

IT WAS MOVED BY COMMISSIONER GODFREAD AND SECONDED BY MS. TERNES AND CARRIED BY A VOICE VOTE TO ACCEPT THE AUDIT COMMITTEE REPORT.

AYES: MR. LECH, TREASURER SCHMIDT, MR. OLSON, COMMISSIONER SMITH, MR. MILLER, COMMISSIONER GODFREAD, MR. BURTON, MS. SMITH, AND MS. TERNES
NAYS: NONE
MOTION CARRIED
ABSENT: LT. GOVERNOR SANFORD, MS. WASSIM

Securities Litigation Committee – Mr. Hunter updated the SIB on activities of the Securities Litigation Committee as of their May 10, 2018 meeting. The Committee reviewed the claims filing report from Financial Recovery Technologies (FRT). FRT took over on March 1, 2018 noting there were no unusual items or material concerns. The SIB was also provided the agenda/minutes from the May 10, 2018 meeting.

IT WAS MOVED BY TREASURER SCHMIDT AND SECONDED BY MR. OLSON AND CARRIED BY A VOICE VOTE TO ACCEPT THE SECURITIES LITIGATION REPORT.

AYES: COMMISSIONER GODFREAD, MS. TERNES, COMMISSIONER SMITH, MR. BURTON, MS. SMITH, MR. MILLER, MR. LECH, MR. OLSON, AND TREASURER SCHMIDT
NAYS: NONE
MOTION CARRIED
ABSENT: LT. GOVERNOR SANFORD, MS. WASSIM

Executive Review Committee – The Executive Review Committee presented the Executive Director's overall evaluation for calendar year 2017. Mr. Lech provided comments on the performance evaluation. The ED/CIO's composite score has continually improved over the past three years.

IT WAS MOVED BY MR. OLSON AND SECONDED BY MR. BURTON AND CARRIED BY A ROLL CALL VOTE TO ACCEPT THE EXECUTIVE DIRECTOR/CIO'S PERFORMANCE EVALUATION FOR CALENDAR YEAR 2017.

AYES: MR. BURTON, COMMISSIONER SMITH, MS. SMITH, TREASURER SCHMIDT, MR. LECH, COMMISSIONER GODFREAD, MR. OLSON, MR. MILLER, AND MS. TERNES
NAYS: NONE
MOTION CARRIED
ABSENT: LT. GOVERNOR SANFORD, MS. WASSIM

The Executive Review Committee recommended no increase in compensation given the current environment across the State. The Executive Review Committee did however suggest that the SIB work towards a benchmark for the ED/CIO position; one in which the SIB could strive towards which would be representative of the size of the fund and responsibilities.

Discussion followed on compensation options. After discussion,

IT WAS MOVED BY MS. TERNES AND SECONDED BY COMMISSIONER SMITH AND CARRIED BY A ROLL CALL VOTE TO ACCEPT THE RECOMMENDATION FROM THE EXECUTIVE REVIEW COMMITTEE REGARDING COMPENSATION FOR THE EXECUTIVE DIRECTOR/CIO.

AYES: MR. OLSON, MR. BURTON, MR. MILLER, MS. SMITH, MS. TERNES, COMMISSIONER GODFREAD, COMMISSIONER SMITH, MR. LECH, AND TREASURER SCHMIDT
NAYS: NONE
MOTION CARRIED
ABSENT: LT. GOVERNOR SANFORD, MS. WASSIM

RIO Budget – Mr. Hunter provided an update on RIO's budget planning for the 2019-21 biennium.

Discussion followed on budget planning strategies.

Board Member Education - Based on the SIB Self-Assessment Survey and Executive Review process, Mr. Hunter will work with Callan and each board member to develop a custom investment education program for consideration by each SIB member. Mr. Hunter will be reaching out to individual board members in June and July to gain insight into the types and format of investment education best suited for their needs. Callan will be consulted in the development of these investment education plans given their long-history of working with the SIB and the excellent educational courses and conferences the firm offers to a wide variety of board members with fiduciary responsibility. The plans will be presented to the SIB for their consideration at their July 27, 2018 meeting.

OTHER:

The next meeting of the SIB is scheduled for July 27, 2018, at 8:30 a.m. at the Bismarck State College Energy Center.

The next meeting of the Securities Litigation Committee meeting is scheduled for August 23, 2018, at 3:00 p.m. at the Retirement and Investment Office.

The next meeting of the SIB Audit Committee is scheduled for September 27, 2018, at 10:00 a.m. at the Retirement and Investment Office.

ADJOURNMENT:

With no further business to come before the SIB, Mr. Lech adjourned the meeting at 11:32 a.m.

____
Mr. Rob Lech, Vice Chair
State Investment Board

____
Bonnie Heit
Assistant to the Board

AGENDA ITEM III.

TO: State Investment Board (SIB)

FROM: Dave Hunter, ED/CIO

DATE: August 25, 2017

RE: Election of Officers – July 2018 to June 2019

In accordance with the SIB Governance Policy B-7 on "Annual Board Planning Cycle", the SIB will conduct an "Election of Officers" each July. The relevant By-Laws and Governance Policy of the SIB are highlighted immediately below for reference purposes.

CHAPTER 3 - OFFICERS AND DUTIES

Section 3-1. The officers of the SIB are a Chair and Vice Chair, one of which must be an appointed or elected member of the TFFR or PERS Board. The officers will be elected by the SIB to a one-year term at the first regularly scheduled meeting following July 1 of each year. Vacancies will be filled by the SIB at the first scheduled meeting following the vacancy.

Section 3-2. Chair. The Chair will preside at all meetings of the SIB.

Section 3-3. Vice Chair. In the absence of the Chair, the Vice Chair will perform the duties of the Chair.

Section 3-4. Executive Director. An Executive Director will be retained by the SIB. The Executive Director will serve at the SIB's pleasure, be responsible for keeping the records of the SIB and TFFR Board actions, and perform such duties as the SIB prescribes. The Executive Director will make out and give out all notices required to be given by law, procedures, or rules and regulations of the two boards.

Policy Implemented: June 23, 1995.

The chairperson's primary responsibility is to insure the integrity of the board's process. The chairperson is the only board member authorized to speak for the board other than in specifically authorized instances.

1. The duty of the chairperson is to see that the board operates consistent with state law, administrative rules, and its own policies.

   A. The board agenda will be the responsibility and be coordinated by the chairperson.
   B. Meeting discussion content will only be those issues which, according to board policy, clearly belong to the board and not the executive director, or in a board member's opinion, may deal with fiduciary responsibilities.
   C. Deliberation will be fair, open, and thorough, but also efficient, timely, orderly, and brief.
   D. The chairperson shall appoint a parliamentarian.

Board Action Requested

TO: STATE INVESTMENT BOARD

FROM: David Hunter, RIO ED/CIO and Sara Sauter, RIO Supervisor of Audit Services

DATE: **July 23, 2018**

RE: Audit Committee Appointments

As directed by SIB Policy B-6, Governance Process/Standing Committees, the Audit Committee shall consist of five members selected by the SIB. Three members of the Audit Committee represent the three groups on the SIB (TFFR board, PERS board, and the elected and appointed officials). The other two members will be selected from outside of the SIB and will be auditors with a Certified Public Accountant (CPA) or Certified Internal Auditor (CIA) designation or be responsible for oversight of the internal audit function at a significant business enterprise or other financial institution.

The SIB previously approved the following five Board representatives for the past year:

Rebecca Dorwart, CPA, CIA (former Chair)
Yvonne Smith, (former Vice Chair) representing PERS retirees
Joshua Wiens, CPA
Cindy Ternes (Workforce Safety & Insurance designee) representing elected and appointed officials
Michael Gessner, representing TFFR

Please note that Ms. Rebecca Dorwart no longer desires to serve, and Mr. Michael Gessner is no longer eligible to serve (due to retirement), on the Committee. We express our sincere appreciation and gratitude to both outstanding audit committee members noting they each served on the Committee for over ten years.

Background and Recommendation:

SIB Policy B-6 states the following: "An Audit Committee has been established as a standing committee of the SIB. The Audit Committee will assist the SIB in carrying out its oversight responsibilities as they relate to RIO's internal and external audit programs, including financial and other reporting practices, internal controls, and compliance with laws, regulations and ethics." **Based on the strong performance of the Audit Committee during the past year with regards to assisting the SIB in carrying out its oversight responsibilities, the Executive Director and Supervisor of Audit Services recommend the re-appointment of the three existing audit committee members including acting Audit Committee Chair Yvonne Smith (representing PERS), Cindy Ternes (WSI designee) and Mr. Joshua Wiens, CPA. RIO notes that TFFR will need to identify one new appointee to serve on the Committee (given the recent retirement of Mr. Gessner).**

In order to find a replacement for Ms. Dorwart, RIO reached out to various accounting and audit professionals in the State. The top two candidates which expressed a clear interest in pursuing this opportunity were interviewed by the Executive Director and Supervisor of Audit Services in July. Both candidates were deemed to be excellent choices to serve on the Committee. After significant consideration, we elected to recommend Mr. Jon Griffin to serve on the SIB Audit Committee for the upcoming year. Mr. Griffin's professional background is summarized on the next page.

Jon Griffin, MBA, BBA (Accounting & Financial Management)

Mr. Jon Griffin is currently Vice President of Risk Management at Capital Credit Union (CCU) reporting to the Ms. Deb Gallagher, CEO, and the CCU Policy Committee. Mr. Griffin effectively oversees and manages the overall risk of CCU noting he provides oversight and supervision of the entity's internal audit and enterprise risk management functions. Jon also acts as Compliance Officer and Security Officer, responsible for ensuring compliance with applicable federal and state laws and regulations. Mr. Griffin is also responsible for preparing and presenting all policy amendments to the Audit Policy Committee in addition to overseeing the Vendor Due Diligence program and being responsible for business continuity planning.

Mr. Jon Griffin graduated from the University of North Dakota in December of 2005 with a BBA and dual major in Accountancy and Financial Management. Jon also obtained an MBA from University of Mary in December of 2015. His certifications include the Credit Union Enterprise Risk Management Expert and Bank Secrecy Act Compliance Specialist designations.

Prior to serving as Vice President of Risk Management at CCU since 2011, Mr. Griffin was a Senior Associate at Brady Martz in Bismarck from 2006 to 2011 where he performed various auditing and tax services. Jon served as in-charge and associate on a wide variety of industries with an emphasis in not for profit, electric cooperatives and governmental areas. His resume is attached for further reference.

Joshua J. Wiens, CPA

Mr. Joshua Wiens currently serves as Chief Financial Officer of McDonalds of Bismarck-Mandan. Joshua manages the finances and accounting for six McDonalds stores in Bismarck and Mandan including all accounting and payroll related functions. He also manages the insurance and Affordable Care Act regulations and reporting for employees in addition to submitting monthly and annual financial statements to McDonalds Corporation. Joshua has served in this role since 2013 to date.

Mr. Wiens concurrently acts as Chief Financial Officer for Shiloh Christian School in Bismarck. Joshua effectively manages the business side of this private school which includes a $3.6 million budget and working with a bank and contractor on construction projects and financing along with handling numerous vendor relationships for the school.

Prior to serving as CFO for his two current employers, Joshua was a Senior Audit Manager for Eide Bailly, LLP in Bismarck. Mr. Wiens specialized in non-profit/government, financial institution, small business and construction contractor audits and consulting. Clients ranged in size from $100,000 to $5 billion in assets and total revenues of up to $100 million. Joshua's 15 years of professional auditing experience with Eide Bailly is ideal for serving as a member of the SIB Audit Committee. His resume is attached for further reference including his career accomplishments and professional education.

Suggested Language for Board Recommendation and Motion:

RIO recommends the re-appointment of three existing audit committee members including Ms. Cindy Ternes, Ms. Yvonne Smith and Mr. Joshua Wiens. RIO also recommends that Mr. Jon Griffin serve as the fourth (newly) appointed audit committee member.

Jon Griffin

EDUCATION

BBA with a Major in Accountancy and a **BBA with a Major in Financial Management**
University of North Dakota, Grand Forks, ND — December, 2005

Master of Business Administration
University of Mary, Bismarck, ND — February 2015

WORK EXPERIENCE

Vice President of Risk Management — 2011 - present
Capital Credit Union, Bismarck, ND

- Oversees and manage the overall risk of the Credit Union
- Leads the enterprise risk management program and business continuity plan
- Acts as Compliance Officer; responsible for administering the compliance function by ensuring compliance with applicable federal and state laws, regulations set forth by the NCUA and other regulatory agencies
- Acts as the Security Officer, responsible for the security of the Credit Union
- Monitor, analyze, and communicate to appropriate departments any changes or amendments to laws and regulations that affect the Credit Union
- Prepare and present policy amendments to the Policy Committee
- Responsible for the overall administration and coordination of the Vendor Due Diligence program
- Investigate and reviews loss related circumstances or incidents and provide guidance on how to mitigate risk and possible losses
- Responsible for training staff relating to compliance, security and risk management
- Conducts operational reviews and when appropriate; makes process improvement recommendations to improve the efficiency and overall effectiveness of various areas in the Credit Union
- Provide oversight and supervision for the internal audit, collection, compliance and electronic service staff
- Prepares and submits annual budget for department; regularly monitors and controls expenses
- Acts as the BSA Officer; responsible for compliance with the Bank Secrecy Act and Identity Theft Programs
- Acts as the main point of contact for the Credit Union's insurer

Senior Associate — 2006 to 2011
Brady, Martz and Associates, P.C., Bismarck, ND

- Performed Auditing, Tax, and other various accounting services
- Served as part of many different audit teams as in-charge and associate that worked in a wide variety of industries with an emphasis in not-for profit, electric cooperatives and governmental areas completing the planning, field work, and report aspect of the audit
- Worked on a variety of tax returns for *Corporations*, *Partnerships,* and *Individuals*
- Performed various accounting functions including the preparation of reports which entailed preparing balance sheets, income statements, statements of retained earnings, cash flow statements, and notes to the financials
- Completed *compilations* and *reviews* for various industries
- In charge of training new employees on various software and audit procedures
- Proficient in Excel, Word, IDEA, QuickBooks, and other accounting software packages

OUTSIDE ORGANIZATIONS

Partners Inc. - 2003-present

- Completed and filed all of the documents and forms with the IRS to establish a 501(c)(3)
- Ongoing financial and tax consulting services

Invest Twelve, LLC - 2014-present

- Prepare financial statements and tax returns; Ongoing management and consulting services

Light of Christ Finance Council *Bismarck Marathon* *Government Affairs Committee (GAC)*
Co-Cub Master and Co-Den Leader

CERTIFICATIONS

- Credit Union Enterprise Risk Management Expert (CU-ERME) designation
- Bank Secrecy Act Compliance Specialist (BSACS) designation

JOSHUA J. WIENS, CPA

EMPLOYMENT

Shiloh Christian School
2014-Present Chief Financial Officer

- Manage the business side of the school which includes a $3.6 million budget, proposing annual tuition and teacher's salaries to the Board, working with families on financial aid, working with a bank and contractor on construction projects and financing, working with vendors, etc.

McDonalds of Bismarck-Mandan
2013-Present Chief Financial Officer

- Manage the finances and accounting for the six stores in Bismarck-Mandan which include all accounting and payroll related functions.
- Manage the insurance and Affordable Care Act for our employees.
- Submit monthly and annual financial statements to McDonalds Corporation.

Eide Bailly LLP
1999-2013 Senior Manager

- Specialized in non-profit/government, financial institution, small business, and construction contractor audits and consulting. Clients ranged in size with $100,000 to $5 billion in assets and total revenues of up to $100 million.
- Reported audit plan, engagement status, issues, and results to client management and the Audit Committee of the Board of Directors.
- Managed relationships with current clients and their Board of Directors which includes presenting at their Board meetings
- Developed aptitude for working under strict deadlines and in high-pressure situations.
- Successfully monitored the budget and performance of the engagement team to ensure each audit jobs profitability.
- Performed risk assessment procedures, including inquiries with senior management, analytical procedures, and industry analysis, to effectively develop the audit plan and work program.

CAREER ACCOMPLISHMENTS

- Obtained Certified Public Accounting license
- Graduate of the Dakota School of Banking
- Graduate of Dale Carnegie
- Graduate of Eide Bailly's Leadership Training Program

EDUCATION

1999: B.S. in Accounting, North Dakota State University

COMMUNITY INVOLVEMENT

- Graduate of the Chambers' Leadership Bismarck Mandan program.
- Member of Stewardship Board for seven years at a local church; 4 years as the treasurer which involves preparing and presenting the $1 Million budget
- Treasurer of Child Evangelism Fellowship State Association.
- Created and ran Wild Game Feeds, Men's Sporting Clays Event, and other Men's events at a local church
- Started, organized, and periodically teach an adult Sunday School class with 15 to 40 participants;

Board Action Requested

TO: **STATE INVESTMENT BOARD**

FROM: David Hunter, ED/CIO

DATE: **July 20, 2018**

RE: Affirmation of Securities Litigation Committee Appointments

---

Background:

The Securities Litigation Committee is a standing committee of the North Dakota State Investment Board created to assist the SIB in fulfilling its fiduciary oversight responsibilities of monitoring the investment of assets entrusted to it by the various statutory and contracted funds, and to serve as a communications link for the SIB, RIO's management and staff, third party securities litigation firms, and others.

The SIB Securities Litigation Committee was initially established in early-2018 and currently consists of two members of the SIB appointed by the Chair, RIO's legal counsel, one member of RIO's fiscal or investment staff and RIO's executive director.

The following individuals were appointed and/or were confirmed to currently serve on the Securities Litigation Committee:

- **Chief Deputy Attorney General Troy Seibel (as Chair);**
- **State Treasurer Kelly Schmidt (as Vice Chair);**
- **Assistant Attorney General Anders Odegaard;**
- **RIO Fiscal and Investment Operations Manager Connie Flanagan; and**
- **RIO Executive Director Dave Hunter.**

As stated in the Securities Litigation Committee Charter, Committee membership will be for one year or termination of term on the SIB. Vacancies will be filled by the SIB Chair at the first scheduled meeting following the vacancy. There will be no limit to the number of terms served on the Committee.

Although less than one-year has passed since the initial appointment of the founding members of the Securities Litigation Committee, RIO would like to follow standing SIB governance policy which states that officer elections and committee memberships should be confirmed in July of each year.

As such, RIO respectfully requests the SIB to affirm the current members of the Securities Litigation Committee as noted above.

AGENDA ITEM IV.A.

BOARD ACCEPTANCE REQUESTED

TO: State Investment Board

FROM: Dave Hunter

DATE: July 20, 2018

SUBJECT: **PERS Job Service Investment Policy Statement Recommendation**

RIO requests the SIB accept investment policy statement changes recently approved by the NDPERS board which oversee the Job Service pension plan.

On June 21, 2018, the PERS board approved the recommendation of RIO, SEI and Gabriel Roeder Smith & Company (GRS) to de-risk the Job Service pension plan by reducing equities to 20% (from 30%) and increasing fixed income to 80% (from 70%). This recommendation was made by RIO and SEI due to the Job Service plan being closed with a funded ratio in excess of 130% assuming a discount rate of 4.7%. PERS staff was instrumental in moving this de-risking strategy forward noting that they engaged their actuarial consulting firm (GRS) to review the overall recommendation and impact on the plan's funded ratio. In a PERS investment sub-committee in early-2018, GRS confirmed the reasonableness of this proposed de-risking strategy. SEI was also instrumental in analyzing this change by proposing the specific asset allocation policy which was approved by the PERS board on June 21, 2018.

Job Service: Modeled portfolios

Asset Class	Current	Portfolio A	Portfolio B
US Managed Volatility Equity	18	9	6
Global Managed Volatility Equity	12	21	14
Total Equity	**30**	**30**	**20**
US High Yield	3	3	3
Emerging Markets Debt	3	3	3
Core Fixed Income	23	23	26
Limited Duration Fixed Income	22	22	26
Diversified Short Term Fixed Income	12	12	12
Short Term Corporate Fixed Income	7	7	10
Total Fixed Income	**70**	**70**	**80**
Portfolio Metric (Net of Fees)			
Expected Return (Short Term)	4.2	4.2	3.9
Expected Return (Equilibrium)	6.7	6.7	6.4
Standard Deviation	6.5	6.4	5.4
Risk of Loss (5th percentile-Short Term)	-5.9	-5.7	-4.6

Based on the above factors, RIO requests the SIB accept the NDPERS board approved investment policy statements changes as highlighted below:

1. **Job Service - Reduce equity to 20% (from 30%) and increase fixed income to 80% (from 70%) as detailed in SEI and RIO's staff recommendation.**

Please refer to the attached documentation which supports the above recommendation noting that RIO deems the NDPERS board action to be both practical and prudent. The Job Service pension plan is closed to new employees and adequately overfunded (130+%) using a conservative 4.7% discount rate. Given the strong funded status of the plan, NDPERS board decision to further de-risk the investment portfolio should be commended in order to reduce equity volatility and preserve the funded status of this mature, closed plan. It is noteworthy to acknowledge the clients professional actuarial firm (GRS) and consultant (SEI) supported this recommendation without exception.

North Dakota
Public Employees Retirement System
400 East Broadway, Suite 505 • Box 1657
Bismarck, North Dakota 58502-1657

Scott Miller
Executive Director
(701) 328-3900
1-800-803-7377

Fax: (701) 328-3920 Email ndpers-info@nd.gov Website https://ndpers.nd.gov

Memorandum

TO: NDPERS Board

FROM: **Bryan Reinhardt**

DATE: June 21, 2018

SUBJECT: Job Service Plan Asset Allocation

The Job Service retirement plan has about 200 retirees and only 8 active contributing members with total assets of $97.3 million at market value (July 2017). Market value of assets as of December 31, 2017 were $97.8 million. As this plan continues to mature, the NDPERS Board has worked to de-risk the asset allocation. SEI is the fund manager for the Job Service assets. Attachment 2 is a proposal to take the next step in de-risking the plan. The current asset allocation is a 70/30 stocks/fixed income ratio. The proposed portfolio B is an 80/20 allocation. This is projected to decrease the return by 0.3% points, but decrease the standard deviation (risk) by 1.1% points.

We had our consultant GRS analyze how this change would affect the plan. Their response is that the plan with the change would still be above 130% funded status (Attachment 1).

The NDPERS Investment Subcommittee reviewed this information and recommends the NDPERS Board approve Portfolio B to continue de-risking the Job Service plan. Attachment 3 is the updated JS Investment Policy.

Board Action Requested:
Approve the updated Job Service Investment Policy (Portfolio B 80/20 Asset Allocation).

Attachment 1

Mon 3/5/2018 1:07 PM

Lance.Weiss@grsconsulting.com

RE: SEI Presentation for 2/15 Meeting

To Reinhardt, Bryan T.

Cc Amy.Williams@grsconsulting.com; Schiermeister, Sharon L.; C3008@grsconsulting.com

You replied to this message on 3/21/2018 9:44 AM.

CAUTION: This email originated from an outside source. Do not click links or open attachments unless you know they are safe.

Hi Bryan.

Although it is not completely compatible, the GASB Report for Job Service as of June 30, 2017 (Page D-2) shows that a one percent reduction in the Single Discount Rate from 5.70% to 4.70% reduces the net pension asset from $33,635,942 to $27,182,597, which is equivalent to reducing the funded ratio from 152.86 to 138.79%.

Therefore for funding purposes, we think it is safe to say that, based on an investment return assumption of 4.75%, and the market value of assets, the funded ratio as of July 1, 2017 for the Retirement Plan for Employees of Job Service North Dakota will be above 130%.

Regards,

Lance

GRS

Lance J. Weiss, EA, MAAA, FCA
Senior Consultant/Team Leader
120 North LaSalle Street | Suite 1350 | Chicago, IL 60602-3495
Phone: 312.456.9800 | Direct: 312.368.6784 | Cell: 847.217.8454
lance.weiss@grsconsulting.com

Good afternoon Bryan.

In accordance with your request, we have modeled the revised asset Portfolio A (30% equity/70% fixed income) and asset Portfolio B (20% equity/80% fixed income) as described in the SEI Client Portfolio Management Fourth Quarter 2017 report) applicable to the Retirement Plan for Employees of Job Service North Dakota.

Based on our analysis, we recommend an investment return assumption of 5.0% in the event Portfolio A is chosen and an investment return assumption of 4.75% in the event Portfolio B is chosen.

Please note that the Retirement Plan for Employees of Job Service North Dakota was frozen to new members as of October 1, 1980. The plan, as of July 1, 2017, had a total of eight active members, 199 benefit recipients and one deferred vested participant entitled to a future benefit. All eight active members are eligible for retirement (normal, optional or early) as of July 1, 2017. Because of these demographics, we believe that more weight should be given to the shorter term expected returns rather than the equilibrium expected returns.

Based on the current investment return assumption of 5.70%, and the market value of assets, the funded ratio as of July 1, 2017 for the Retirement Plan for Employees of Job Service North Dakota was 152.4%. We estimate that, even with an investment return assumption of 4.75%, the Retirement Plan for Employees of Job Service North Dakota will still be well over 100% funded.

Please call us with any questions.

Regards,

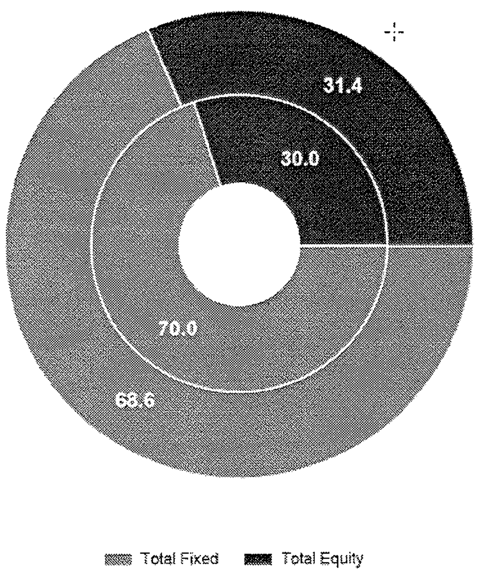
Lance

GRS

Lance J. Weiss, EA, MAAA, FCA
Senior Consultant/Team Leader
120 North LaSalle Street | Suite 1350 | Chicago, IL 60602-3495
Phone: 312.456.9800 | Direct: 312.368.6784 | Cell: 847.217.8454

Attachment 2

ND – Job Service Pension
Portfolio summary: December 31, 2017



Summary for periods ending 12/31/2017

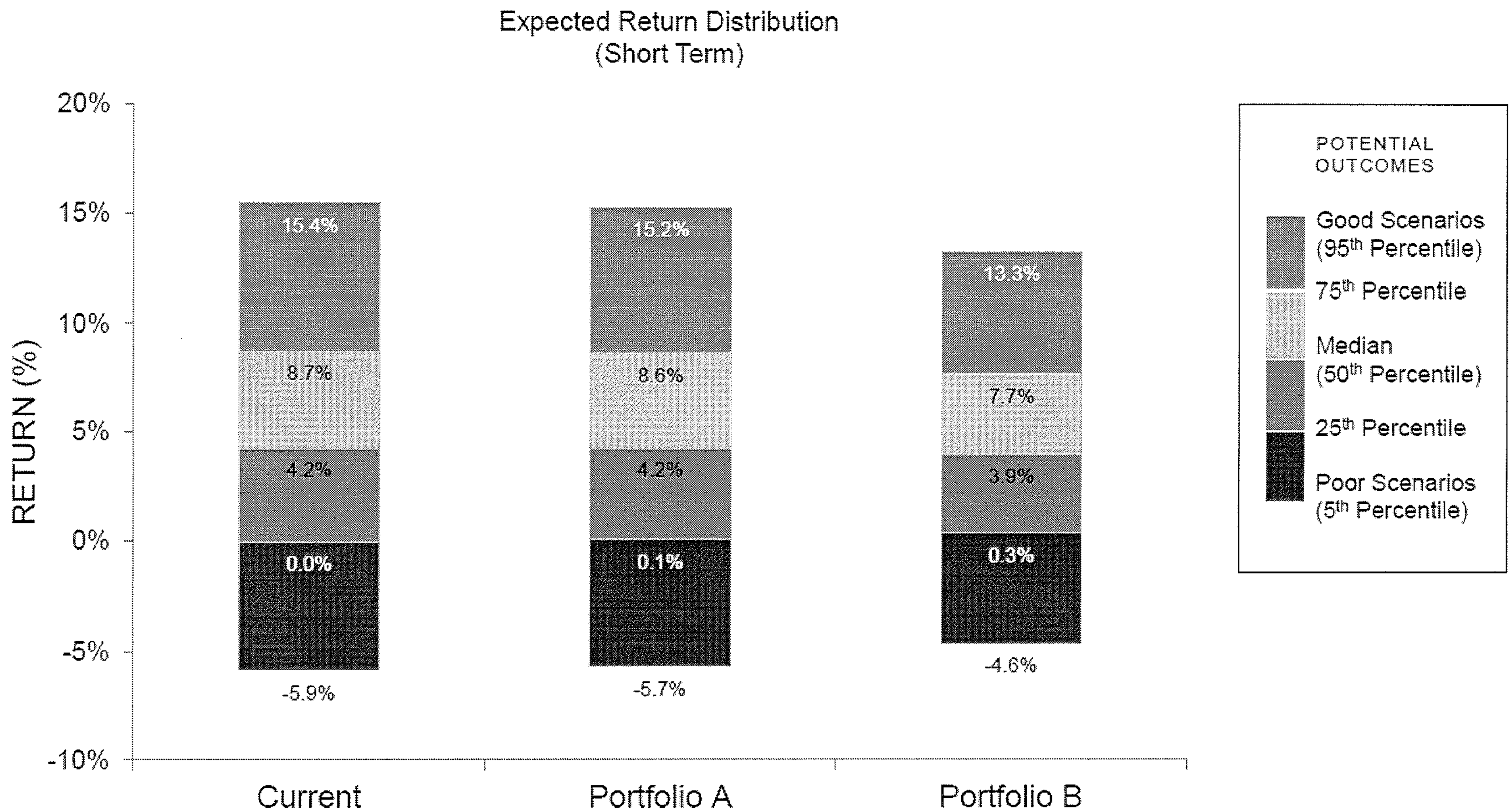
	One Month	Three Month	Year To Date
Portfolio Value	$97,904,168.43	$97,160,466.49	$95,295,462.45
Net Cash Flows	($500,000.00)	($1,300,000.00)	($4,925,000.00)
Realized Gains	($10,302.10)	($2,724.62)	$944,074.82
Unrealized Gains	($2,132,630.83)	($1,038,982.93)	$2,373,930.34
Interest	$0.00	$0.00	$0.00
Dividends	$2,542,784.94	$2,985,261.50	$4,115,552.83
Ending Portfolio Value	$97,804,020.44	$97,804,020.44	$97,804,020.44

Job Service: Modeled portfolios

Asset Class	Current	Portfolio A	Portfolio B
US Managed Volatility Equity	18	9	6
Global Managed Volatility Equity	12	21	14
Total Equity	**30**	**30**	**20**
US High Yield	3	3	3
Emerging Markets Debt	3	3	3
Core Fixed Income	23	23	26
Limited Duration Fixed Income	22	22	26
Diversified Short Term Fixed Income	12	12	12
Short Term Corporate Fixed Income	7	7	10
Total Fixed Income	**70**	**70**	**80**
Portfolio Metric (Net of Fees)			
Expected Return (Short Term)	4.2	4.2	3.9
Expected Return (Equilibrium)	6.7	6.7	6.4
Standard Deviation	6.5	6.4	5.4
Risk of Loss (5^{th} percentile-Short Term)	-5.9	-5.7	-4.6

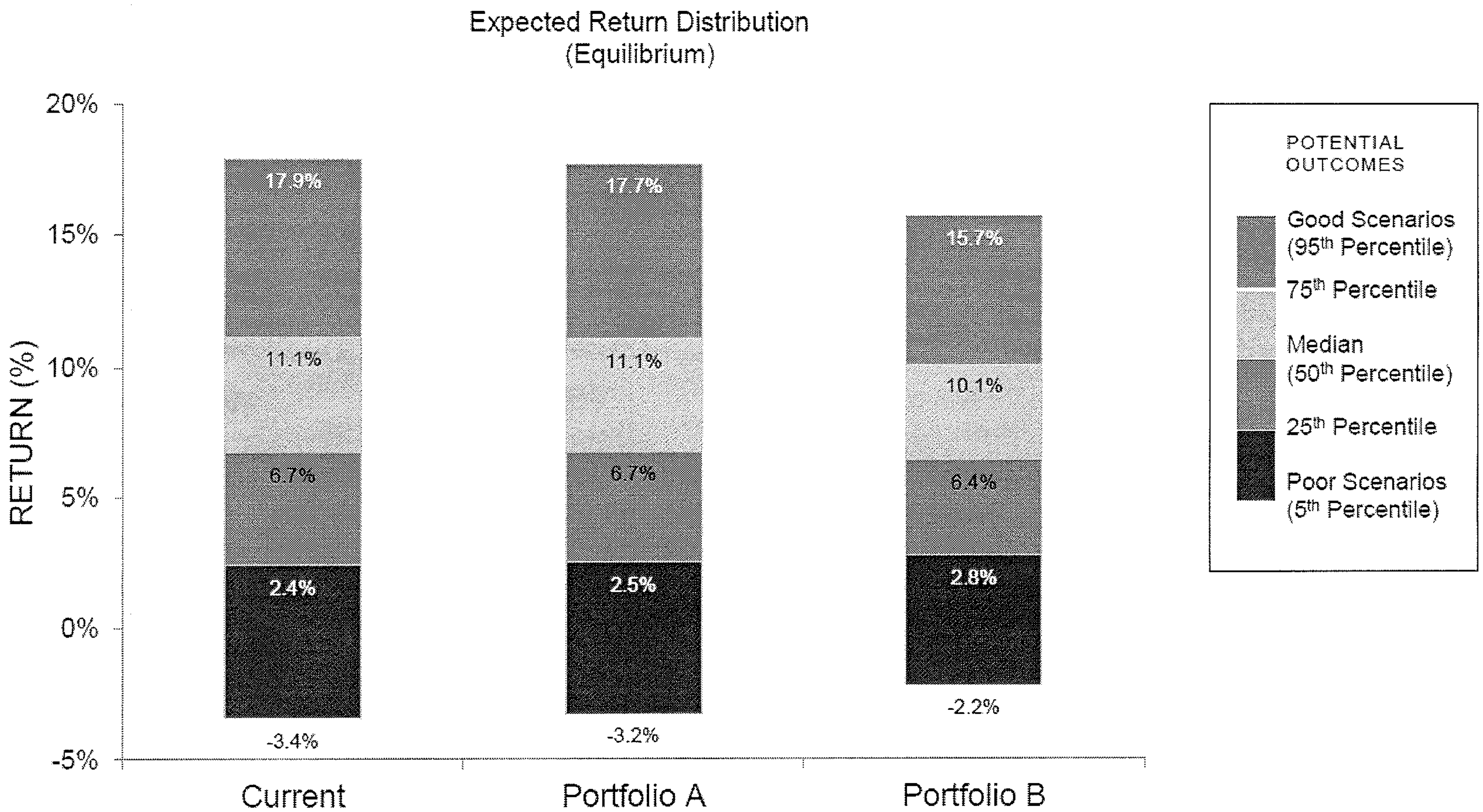
Source: SEI Capital Market Assumptions. Please see important disclosures at the beginning of this section and at the back of the presentation.

Job Service: Modeled portfolios



Source: SEI Capital Market Assumptions. Please see important disclosures at the beginning of this section and at the back of the presentation.

Job Service: Modeled portfolios



Source: SEI Capital Market Assumptions. Please see important disclosures at the beginning of this section and at the back of the presentation.

RETIREMENT PLAN FOR EMPLOYEES OF JOB SERVICE NORTH DAKOTA INVESTMENT POLICY STATEMENT

1. PLAN CHARACTERISTICS AND FUND CONSTRAINTS

The Retirement Plan for the Employees of Job Service North Dakota (Plan) is a defined benefit retirement plan for the eligible employees hired before October 1, 1980. There have been no new entrants to the plan since October 1, 1980. The plan provides retirement benefits, disability benefits and survivor benefits consistent with the written Plan document. Until October 1, 1993, annuities were purchased from the Travelers for retirees, since that date retiree benefits are paid from Plan assets. Annual cost of living adjustments for all Plan pensioners including annuitants with the Travelers are paid from Plan assets. The NDPERS Board (the Board) is the Plan Administrator and administers the Plan in accord with Chapter 52-11 of the North Dakota Century Code.

Job Service North Dakota as the employer contributes 4% of the active participant's salary as a contribution 'on behalf of the employee' and the active participants pay 3% of their salary into Plan assets.

Each year the Plan has an actuarial valuation performed. The current actuarial assumed rate of return on assets is ~~5.70~~4.75%.

2. RESPONSIBILITIES AND DISCRETION OF THE STATE INVESTMENT BOARD (SIB)

Aggregate plan contributions plus earnings, minus allowable expenses constitute the Fund. The Board is charged by NDCC chapters 54-52, 21-10-01, and 39-03.1 to establish policies for the investment goals and asset allocation of the Fund. The State Investment Board (SIB) is charged with implementing the asset allocation as promptly and prudently as possible in accordance with the Board's policies by investing the assets of the Fund in the manner provided in the prudent investor rule, which provides:

Fund fiduciaries shall exercise the judgment and care, under the circumstances then prevailing, that an institutional investor of ordinary prudence, discretion, and intelligence exercises in the management of large investments entrusted to it, not in regard to speculation but in regard to the permanent disposition of funds, considering probable safety of capital as well as probable income. The retirement funds belonging to the teachers' fund for retirement and the public employees retirement system must be invested exclusively for the benefit of their members and in accordance with the respective funds' investment goals and objectives. (NDCC 21-10-07)

The SIB may delegate investment responsibility of the Fund or any portion of the Fund to professional money managers. Where a money manager has been retained, the SIB's role in determining investment strategy is supervisory not advisory.

The SIB may at its discretion, pool the assets of the Fund with another fund or funds having similar investment objectives and time horizons in order to maximize returns and minimize costs. In pooling fund assets the SIB will establish asset class pools it deems necessary to achieve the specific quality, diversification, restrictions, and performance objectives subject to the prudent investor rule and the objectives of the funds participating in the pools.

The SIB is responsible for establishing the selection criteria, determining the performance measures, and retaining all fund money managers. SIB is also responsible for the selection and retention of any investment consultants that may be employed in the investment of the Fund assets.

3. DELEGATION OF AUTHORITY

Management responsibility for NDPERS funds not assigned to the North Dakota State Investment Board (SIB) in Chapter 21-10 of the North Dakota Century Code (NDCC) is hereby delegated to the SIB, which must establish written policies and procedures for the operation of the NDPERS funds, consistent with this investment policy.

Such procedures must provide for:

1. The definition and assignment of duties and responsibilities to advisory services and persons employed by the SIB pursuant to NDCC 21-10-02.1(1) (a).

2. Investment diversification, investment quality, qualification of money managers, and amounts to be invested by money managers pursuant to NDCC 21-10-02.1(1)(e). In developing these policies it is understood:

   a. Futures and options may be used to hedge or replicate underlying index exposure, but not for speculation.
   b. The use of derivatives will be monitored to ensure that undue risks are not taken by the money managers.
   c. All assets must be held in custody by the SIB's master custodian or such other custodians as are selected by the SIB.

3. Guidelines for the selection and redemption of investments will be in accordance with NDCC 21-10-02.1(1) (d).

4. The criteria for making decisions with respect to hiring, retention, and termination of money managers will be clearly defined. This also includes selecting performance measurement standards, consultants, report formats, and frequency of meetings with money managers.

All participants in the investment process must seek to act responsibly as custodians of the public trust.

4. INVESTMENT GOALS

The investment objectives of the Plan have been established by the Plan's Administrator upon consideration of its strategic objectives and a comprehensive review of current and projected financial requirements.

Objective #1: To maintain a level of surplus sufficient to eliminate the need for future contributions;

Objective #2: To achieve a rate of return which exceeds the rate of inflation, as measured by the Consumer Price index (CPI), by 3.0 or more percentage points per year (based on current actuarial assumptions of 5.7% return and 2.5% inflation), over a complete market cycle; and

Objective #3: As a secondary objective, to maximize the Plan's surplus to increase future benefit payments.

5. INVESTMENT PERFORMANCE OBJECTIVE

The NDPERS Board will seek to make investments that generate sufficient return to meet the goals outlined in this policy. The objectives established in this section are in accordance with the fiduciary requirement in federal and state law.

It is in the best interest of NDPERS and its beneficiaries that performance objectives be established for the total Fund. It is clearly understood these objectives are to be viewed over the long term and have been established after full consideration of all factors set forth in this Statement of Investment Goals, Objectives and Policies.

a) The funds rate of return, over the long term should equal that of the policy portfolio which is comprised of policy weights of appropriate asset class benchmarks as set by the SIB.
b) The annual standard deviation of total returns for the Fund should not materially exceed that of the policy portfolio by more than 15%.
c) Over 5-year and longer periods the fund should match or exceed the expected rate of return projected in the most recent asset/liability study without exceeding the expected risk for the period as measured by standard deviation by more than 15%.

6. ASSET ALLOCATION

The NDPERS Board as plan Administrator establishes the asset allocation of the Fund, with input from consultants and SIB staff. The current asset allocation is based upon the asset/liability study completed by SEI Consultants in 2017. That study provided an appraisal of current cash flow projections and estimates of the investment returns likely to be achieved by the various asset classes.

In recognition of the Plan's objectives, projected financial status, and capital market expectations, the following asset allocation options were deemed appropriate for the Fund:

Domestic Equity – ~~18~~6%
Global Equity - ~~12~~14%
U.S. High Yield Bonds - 3%
Emerging Markets Debt - 3%
Core Fixed Income - ~~23~~26%
Limited Duration Fixed Income - ~~22~~26%
Diversified Short Term Fixed Income - 12%
Short Term Corporate Fixed Income - ~~7~~10 %

Rebalancing of the Fund to this target allocation will be done in accordance with the SIB's rebalancing policy, but not less than annually.

7. RESTRICTIONS

While the SIB is responsible for establishing specific quality, diversification, restrictions, and performance objectives for the investment vehicles in which the Fund's assets will be invested, it is understood that:

a. Futures and options may be used to hedge or replicate underlying index exposure, but not for speculation.

b. Derivatives use will be monitored to ensure that undue risks are not taken by the money managers.

c. All assets will be held in custody by the SIB's master custodian or such other custodians as are acceptable to the SIB.

Social Investing is defined as *"The investment or commitment of public pension fund money for the purpose of obtaining an effect other than a maximized return to the intended beneficiaries."*

d. Social investing is prohibited unless it meets the Exclusive Benefit Rule and it can be substantiated that the investment must provide an equivalent or superior rate of return for a similar investment with a similar time horizon and similar risk.

Economically targeted investment is defined as an investment designed to produce a competitive rate of return commensurate with risk involved, as well as to create collateral economic benefits for a targeted geographic area, group of people, or sector of the economy.

e. Economically targeted investing is prohibited unless the investment meets the Exclusive Benefit Rule.

The Exclusive Benefit Rule is met if the following four conditions are satisfied:

(1) The cost does not exceed the fair market value at the time of investment.

(2) The investment provides the Fund with an equivalent or superior rate of return for a similar investment with a similar time horizon and similar risk.

(3) Sufficient liquidity is maintained in the Fund to permit distributions in accordance with the terms of the plan.

(4) The safeguards and diversity that a prudent investor would adhere to are present.

8. INTERNAL CONTROLS

The SIB must have a system of internal controls to prevent losses of public funds arising from fraud or employee error. The controls deemed most important are the separation of responsibilities for investment purchases from the recording of investment activity, custodial safekeeping, written confirmation of investment transactions, and established criteria for broker relationships. The annual financial audit must include a comprehensive review of the portfolio, accounting procedures for security transactions and compliance with the investment policy.

9. EVALUATION

Investment management of the Fund will be evaluated against the Fund's investment objectives and investment performance standards.

An annual performance report must be provided to the Board by the State Investment Officer at a regularly scheduled NDPERS Board meeting. The annual performance report must include asset returns and allocation data as well as information regarding all significant or material matters and changes pertaining to the investment of the Fund, including:

- Changes in asset class portfolio structures, tactical approaches and market values;
- All pertinent legal or legislative proceedings affecting the SIB.
- Compliance with these investment goals, objectives and policies.
- A general market overview and market expectations.
- A review of fund progress and its asset allocation strategy.

In addition, the State Investment Officer shall review with the Board the procedures and policies established by the SIB relating to this statement of investment goals, objectives, and policies.

~~Sharon Schiermeister~~Scott Miller **~~Interim~~ Plan Administrator and Trustee** **Retirement Plan for Employees of** **Job Service North Dakota**	**David Hunter** **Executive Director** **North Dakota Retirement and Investment Office**
Date:_______________	Date:_______________

Approved by the SIB:
Approved by the PERS Board:

3442 East Century Avenue | P.O. Box 7100 | Bismarck, ND 58507-7100
Telephone: 701-328-9885 | Toll Free: 800-952-2970| Fax: 701-328-9897|www.nd.gov/rio

To: **State Investment Board**

From: **RIO Compliance Officer**

Date: **July 18, 2018**

RE: **Annual Affirmation of Code of Conduct Policy**

Governance Process Policy B-8, *Board Members' Code of Conduct,* which is attached to this memorandum, details the Code of Ethical Responsibility for the SIB. Item #10 of this policy indicates that each Board Member is required to reaffirm their understanding of this policy annually and disclose any conflicts of interest. Therefore, please read and sign the statement below to comply with this requirement.

"I have read and understand SIB Governance Process Policy B-8 *Board Members' Code of Conduct*. I have disclosed any conflicts of interest as required by this policy."

Name (printed) ________________________________

Signature_____________________________________

Date____

Detail of any conflicts of interest (if any):

POLICY TYPE: GOVERNANCE PROCESS

POLICY TITLE: *BOARD MEMBERS' CODE OF CONDUCT*

The following will be the Code of Ethical Responsibility for the SIB:

1. SIB members owe a duty to conduct themselves so as to inspire the confidence, respect, and trust of the SIB members and to strive to avoid not only professional impropriety but also the appearance of impropriety.

2. SIB members should perform the duties of their offices impartially and diligently. SIB members are expected to fulfill their responsibilities in accord with the intent of all applicable laws and regulations and to refrain from any form of dishonest or unethical conduct. Board members should be unswayed by partisan interest, public sentiment, or fear of criticism.

3. Conflicts of interest and the appearance of impropriety shall be avoided by SIB members. Board members must not allow their family, social, professional, or other relationships to influence their judgment in discharging their responsibilities. Board members must refrain from financial and business dealings that tend to reflect adversely on their duties. If a conflict of interest unavoidably arises, the board member shall immediately disclose the conflict to the SIB. A board member must abstain in those situations where the board member is faced with taking some official action regarding property or a contract in which the board member has a personal interest. Conflicts of interest to be avoided include, but are not limited to: receiving consideration for advice given to a person concerning any matter over which the board member has any direct or indirect control, acting as an agent or attorney for a person in a transaction involving the board, and participation in any transaction involving for which the board member has acquire information unavailable to the general public, through participation on the board.

   "Conflict of Interest" means a situation in which a board member or staff member has a direct and substantial personal or financial interest in a matter which also involves the member's fiduciary responsibility.

4. The board should not unnecessarily retain consultants. The hiring of consultants shall be based on merit, avoiding nepotism and preference based upon considerations other than merit that may occur for any reason, including prior working relationships. The compensation of such consultants shall not exceed the fair value of services rendered.

5. Board members must abide by North Dakota Century code 21-10-09, which reads: "No member, officer, agent, or employee of the state investment board shall profit in any manner from transactions on behalf of the funds. Any person violating any of the provisions of this section shall be guilty of a Class A misdemeanor."

6. Board members shall perform their respective duties in a manner that satisfies their fiduciary responsibilities.

7. All activities and transactions performed on behalf of the public funds must be for the exclusive purpose of providing benefits to plan participants and defraying reasonable expenses of administering the plan.

8. Prohibited transactions. Prohibited transactions are those involving self-dealing. Self-dealing refers to the fiduciary's use of plan assets or material, non-public information for personal gain; engaging in transactions on behalf of parties whose interests are adverse to the plan; or receiving personal consideration in connection with any planned transaction.

9. Violation of these rules may result in an official reprimand from the SIB. No reprimand may be issued until the board member or employee has had the opportunity to be heard by the board.

10. Board Members are required to affirm their understanding of this policy annually, in writing, and must disclose any conflicts of interest that may arise (See Exhibit B-I).

Policy Implemented: June 23, 1995.
Amended: January 22, 1999, February 25, 2011, January 27, 2012, February 27, 2015.

Private Equity Update

Board Approval Requested

July 24, 2018

Dave Hunter, Executive Director / CIO

Darren Schulz, Deputy Chief Investment Officer

ND Retirement & Investment Office (RIO)

State Investment Board (SIB)

Private Equity Background

1. The Pension Trust has maintained a target allocation to Private Equity (PE) for nearly three decades including initial commitments to Adams Street (and its predecessor, Brinson Partners) in 1989.
2. During the 1990's and early-2000's, the SIB diversified its PE portfolio away from Adams Street to include smaller, industry or geographically specific target strategies with firms such as Capital Group, Corsair, EIG Energy, Hearthstone, Lewis & Clark, Matlin Patterson and Quantum Energy.
3. Following a strategic review of our PE portfolio in 2014, the SIB approved RIO's recommendation to work towards engaging with one or two large, established investment firms to enhance our overall PE performance noting <u>the SIB has been successful in identifying key strategic relationships within other major private market sectors</u> (including JPMorgan and Invesco in real estate and JPMorgan and Grosvenor within infrastructure). In summary, the decision to align with two (or three) strategic partners in these private market segments was believed to ensure a greater alignment of interests, reduce fees, obtain more comprehensive sharing of best ideas, and improve overall performance.
4. After extensive RIO investment due diligence work in 2014 and 2015, the SIB approved RIO's recommendation to engage Callan to conduct a manager search to identify one new private equity firm to complement our existing strategic partnership with Adams Street. RIO and Callan identified 12 potential candidates and eventually recommended BlackRock Private Equity Partners for this new strategic relationship given the breadth and depth of the firms professional relationships and its ability to help RIO build a well diversified, non-industry, sector or geographic specific, private equity pool which would complement our existing program with Adams Street.
5. Since 2015, the SIB and RIO have continued to build out and diversify our PE portfolio within the Pension Trust by making $200 million of new commitments to BlackRock and $120 million of new commitments to Adams Street Global Funds (in 2015, 2016 and 2017).

Private Equity – Update and Recommendation

<u>Private Equity Update</u>:

1. **During the last six months, RIO has received a high volume of unsolicited offers to sell our non-core private equity holdings to firms which specialize in the "secondary" market.**
2. **Although RIO has generally been receptive to these reverse inquiries, the SIB has generally stated it is primarily interested in selling non-core private market holdings if the purchase price is close to par, if not above par.**
3. **Given that Corsair IV represents a concentrated investment in the financial services industry (100%) with significant geographic concentration risk (in the U.K. and U.S.), the opportunity to redeploy this $25 million private market investment into a more diversified strategy at this stage of the economic cycle should be strongly considered, if not approved.**
4. **The sale of Corsair IV would accelerate our ability to restructure our private equity portfolio noting that we contemplate recommending a follow-on commitment to Adams Street 2018 Global Equity Fund in the near future (with a target commitment size of up to $80 million).**
5. **RIO notes the Adams Street and BlackRock portfolios have historically been structured to be considerably more diversified from a geographic and industry perspective (than Corsair).**

<u>Recommendation</u>: In order to continue to diversify our PE portfolio away from smaller, industry or geographic specific investments, towards larger, more globally and industry diverse strategies, <u>RIO recommends the SIB approve the sale of non-core private equity commitment in Corsair IV at a purchase price which approximates the most recently reported quarter end value of $25 million.</u>

Callan's Quarterly Investment Reporting

Market Values and Allocation %'s - March 31, 2018 and December 31, 2017

	March 31, 2018				December 31, 2017	
	Market Value	Weight	Net New Inv.	Inv. Return	Market Value	Weight
Private Equity	**$181,873,860**	**3.21%**	**$(2,205,931)**	**$8,244,035**	**$175,835,756**	**3.10%**
Adams Street Direct Co-Invest Fd	1,337,757	0.02%	0	(123,445)	1,461,202	0.03%
Adams Street Direct Fund 2010	903,107	0.02%	(79,016)	24,817	957,306	0.02%
Adams Street 1998 Partnership	125,886	0.00%	0	579	125,307	0.00%
Adams Street 1999 Partnership	124,033	0.00%	(205,083)	4,107	325,009	0.01%
Adams Street 2000 Partnership	581,409	0.01%	0	20,512	560,897	0.01%
Adams Street 2001 Partnership	833,485	0.01%	(266,297)	57,049	1,042,733	0.02%
Adams Street 2002 Partnership	158,107	0.00%	0	(2,538)	160,645	0.00%
Adams Street 2003 Partnership	237,368	0.00%	0	6,373	230,995	0.00%
Adams Street 2010 Partnership	6,412,058	0.11%	(250,307)	371,298	6,291,067	0.11%
Adams Street 2008 Fund	7,591,595	0.13%	(561,952)	320,242	7,833,305	0.14%
Adams Street 1999 Non-US	71,376	0.00%	0	420	70,956	0.00%
Adams Street 2000 Non-US	435,643	0.01%	(130,538)	32,250	533,931	0.01%
Adams Street 2001 Non-US	171,139	0.00%	0	10,028	161,111	0.00%
Adams Street 2002 Non-US	89,239	0.00%	(179,907)	7,754	261,392	0.00%
Adams Street 2003 Non-US	206,989	0.00%	0	8,993	197,996	0.00%
Adams Street 2004 Non-US	257,629	0.00%	(39,986)	23,541	274,074	0.00%
Adams Street 2010 Non-US	3,162,967	0.06%	(54,533)	145,905	3,071,595	0.05%
Adams Street 2010 Non-US Emg	1,593,992	0.03%	(61,572)	108,894	1,546,670	0.03%
Adams Street 2015 Global Fd	11,649,256	0.21%	1,499,121	712,308	9,437,827	0.17%
Adams Street 2016 Global Fd	6,207,128	0.11%	405,000	389,866	5,412,262	0.10%
Adams Street 2017 Global Fd	2,666,685	0.05%	0	56,685	2,610,000	0.05%
Adams Street BVCF IV Fund	3,345,617	0.06%	0	2,763	3,342,854	0.06%
BlackRock	28,280,464	0.50%	7,835,818	0	20,444,646	0.36%
Capital International V	1,088,397	0.02%	27,252	(585,106)	1,646,251	0.03%
Capital International VI	27,070,109	0.48%	(218,002)	1,239,505	26,048,606	0.46%
CorsAir III	14,164,690	0.25%	(1,055,527)	1,510,906	13,709,311	0.24%
CorsAir IV	24,880,122	0.44%	(64,353)	429,481	24,514,994	0.43%
EIG Energy Fund XIV	5,560,655	0.10%	0	181,969	5,378,686	0.09%
Hearthstone Advisors MS II	1	0.00%	0	0	1	0.00%
Hearthstone Advisors MS III	2,365,900	0.04%	0	65,541	2,300,359	0.04%
Lewis & Clark, LP	1,638,301	0.03%	56,303	0	1,581,998	0.03%
Lewis & Clark II	6,619,916	0.12%	0	0	6,619,916	0.12%
Matlin Patterson II	1,152,793	0.02%	0	29,219	1,123,574	0.02%
Matlin Patterson III	17,082,516	0.30%	(8,862,351)	3,194,118	22,750,749	0.40%
Quantum Energy Partners	3,807,531	0.07%	0	0	3,807,531	0.07%

Callan

Investment Manager Returns

The table below details the rates of return for the Fund's investment managers over various time periods ended March 31, 2017. Negative returns are shown in red, positive returns in black. Returns for one year or greater are annualized. The first set of returns for each asset class represents the composite returns for all the fund's accounts for that asset class.

Returns for Periods Ended March 31, 2017

	Last Quarter	Last Year	Last 3 Years	Last 5 Years	Last 10 Years
Private Equity*					
Net	(1.19%)	3.29%	(3.06%)	1.37%	(0.65%)
Adams Street Direct Co-Invest Fd	(9.94%)	(1.66%)	12.38%	12.32%	5.44%
Adams Street Direct Fund 2010	(2.88%)	(3.48%)	10.21%	10.64%	-
Adams Street 1998 Partnership	(0.44%)	(0.83%)	1.22%	4.03%	(1.18%)
Adams Street 1999 Partnership	(2.15%)	(2.01%)	(3.13%)	2.68%	2.26%
Adams Street 2000 Partnership	(0.50%)	(3.39%)	(3.45%)	0.61%	3.16%
Adams Street 2001 Partnership	(3.53%)	(3.95%)	(0.13%)	5.32%	3.38%
Adams Street 2002 Partnership	0.04%	22.33%	2.62%	6.79%	3.71%
Adams Street 2003 Partnership	(1.10%)	1.34%	8.31%	10.64%	5.27%
Adams Street 2010 Partnership	1.70%	10.44%	13.45%	12.93%	-
Adams Street 2008 Fund	0.01%	6.32%	10.00%	10.67%	-
Adams Street 1999 Non-US	(2.30%)	(0.89%)	(1.17%)	3.12%	4.28%
Adams Street 2000 Non-US	4.25%	6.05%	(0.90%)	(0.74%)	1.91%
Adams Street 2001 Non-US	(0.88%)	(17.88%)	9.49%	14.00%	2.77%
Adams Street 2002 Non-US	(4.49%)	(6.83%)	5.42%	4.13%	1.80%
Adams Street 2003 Non-US	11.46%	25.79%	13.46%	17.68%	11.04%
Adams Street 2004 Non-US	(4.88%)	(2.88%)	2.39%	4.76%	3.49%
Adams Street 2010 Non-US	1.53%	11.10%	7.00%	8.08%	-
Adams Street 2010 Non-US Emg	0.60%	4.81%	12.72%	5.08%	-
Adams Street 2015 Global Fd	12.14%	36.84%	-	-	-
Adams Street 2016 Global Fd	41.27%	-	-	-	-
Adams Street BVCF IV Fund	(0.01%)	2.89%	16.30%	22.81%	30.23%
Capital International V	(8.92%)	(18.28%)	(20.20%)	(12.38%)	-
Capital International VI	(0.82%)	14.23%	(7.55%)	(8.40%)	-
CorsAir III	(2.61%)	2.69%	6.72%	2.66%	(4.34%)
CorsAir IV	2.94%	16.61%	16.18%	13.53%	-
EIG Energy Fund XIV	12.39%	(32.10%)	(37.98%)	(25.91%)	-
Lewis & Clark, LP	0.00%	(51.19%)	(35.55%)	(19.69%)	(7.95%)
Lewis & Clark II	2.64%	4.56%	(5.96%)	(5.07%)	-
Matlin Patterson II	(20.08%)	(25.86%)	0.23%	(11.14%)	(27.45%)
Matlin Patterson III	(0.93%)	5.02%	(3.81%)	10.15%	-
Quantum Energy Partners	0.00%	(5.58%)	(8.36%)	3.61%	3.20%

* Corsair III was taken out from the Private Equity Composite on July 1, 2009. It was then added back into the Private Equity Composite on October 1, 2011. At this time Corsair IV, Capital Intl and EIG were also added to this composite.

Private Equity - Appendix

Previously distributed SIB meeting materials

This slide was previously presented to the SIB on March 18, 2016 and August 25, 2017.

Callan Associates – Private Equity Overview

What is it?

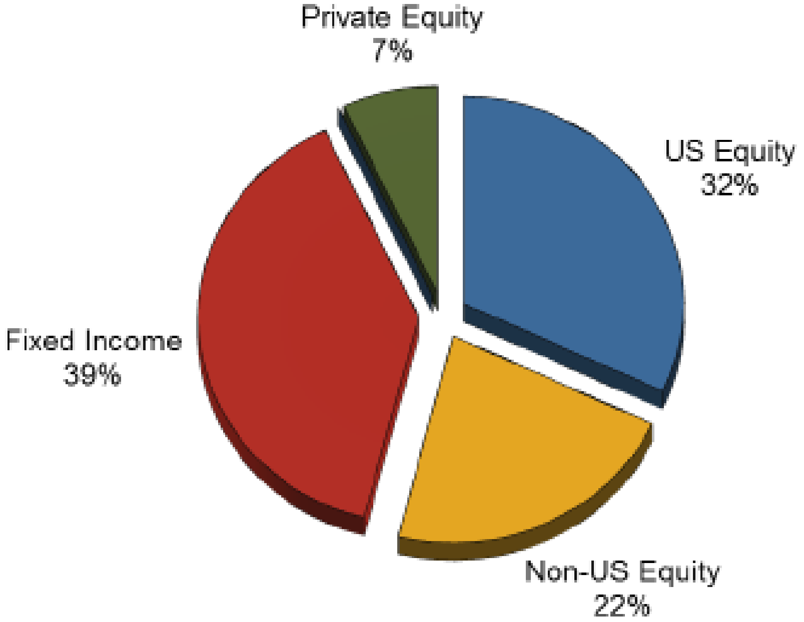
- Private equity is defined as private, unregistered investments in operating companies typically accessed through limited partnership companies.
- Partnership structure:
  - A general partner (GP) who manages the assets and who has unlimited liability for actions of the fund.
    - *The GP collects a fee for managing the fund, which typically takes the form of a management fee plus a percentage of profits.*
  - Limited partners (LPs) whose liabilities are limited to the capital commitments made and who have little participation in the partnership's management.
- Private equity investments are characterized by very long investment horizons.
- Private equity = private corporate finance investments.
- Five key strategies:
  - Venture capital
  - Buyouts
  - Special situations
  - Subordinated debt
  - Distressed debt
- Key benefit sought is high rate of return, other benefits such as diversification are secondary.
- The primary drawbacks are illiquidity and program complexity.
- Usage by institutional investors is becoming very common, especially among larger funds.

Callan Associates – Private Equity

Strategies and Benefits

- Generally invest in one or more of five types of strategies:
  - Venture capital
  - Buyouts
  - Special situations
  - Subordinated debt
  - Distressed debt
- Typically 5%-10% of portfolio.
- Returns above stocks and bonds.
  - Huge variation between best and worst-performing funds.
  - Huge variation between vintage years.
  - Median is typically not good enough to beat S&P 500.
- Moderate diversifier due to valuation based accounting.

Example Asset Allocation with Private Equity



This document was previously presented to the SIB on March 18, 2016 and August 25, 2017.

Callan's Capital Market Expectations

2015 Capital Market Expectations: Return and Risk

Summary of Callan's Long-Term Capital Market Projections (2015-2024)

		PROJECTED RETURN		PROJECTED RISK	
Asset Class	Index	1-Year Arithmetic	10-Year Geometric*	Standard Deviation	Projected Yield
Equities					
Broad Domestic Equity	Russell 3000	9.15%	7.60%	19.00%	2.00%
Large Cap	S&P 500	8.90%	7.50%	18.30%	2.20%
Small/Mid Cap	Russell 2500	10.15%	7.85%	22.95%	1.40%
International Equity	MSCI World ex USA	9.25%	7.50%	20.20%	3.00%
Emerging Markets Equity	MSCI Emerging Markets	11.45%	7.90%	27.95%	2.50%
Global ex-US Equity	MSCI ACWI ex USA	9.80%	7.80%	21.45%	2.90%
Fixed Income					
Defensive	Barclays Govt 1-3	2.75%	2.75%	2.25%	2.80%
Domestic Fixed	Barclays Aggregate	3.05%	3.00%	3.75%	4.00%
Long Duration	Barclays Long G/C	4.70%	4.10%	11.40%	5.50%
TIPS	Barclays TIPS	3.10%	3.00%	5.30%	4.00%
High Yield	Barclays High Yield	5.60%	5.05%	11.45%	7.00%
Non-US Fixed	Citi Non-USD World Govt	3.15%	2.75%	9.40%	3.80%
Emerging Market Debt	JMP EMBI Global Diversifiec	5.40%	4.90%	10.65%	6.40%
Other					
Real Estate	Callan Real Estate	7.35%	6.15%	16.50%	5.00%
Infrastructure	S&P Global Infrastructure	8.90%	7.35%	19.00%	3.00%
Private Equity	TR Post Venture Cap	13.55%	8.50%	33.05%	0.00%
Hedge Funds	Callan Hedge FoF	5.40%	5.10%	8.85%	0.00%
Commodities	DJ-UBS Commodity	4.65%	3.05%	18.25%	2.00%
Cash Equivalents	90-Day T-Bill	2.00%	2.00%	0.90%	2.00%
Inflation	CPI-U	2.25%	2.25%	1.50%	

*Geometric returns are derived from arithmetic returns and associated risk (standard deviation).

Private Equity offers the highest Projected Return (and Risk)

Callan's Key Considerations:

1. **Higher Fees and less liquid than public equity;**
2. **Implementation is a key risk and requires a long time horizon and continual investment; and**
3. **Requires greater oversight than most public investments and is more difficult to monitor and value.**

This document was previously presented to the SIB on March 18, 2016 and August 25, 2017.

Private Equity Performance Summary

Pension Trust Private Equity
As of September 30, 2015
($ in millions)

#	Adams Street Partnerships (ASP)	Vintage Year	Commitment	Unfunded Commitment	Net Asset Value	% Total Pension	Internal Rates of Return (IRR) – Net Returns: 1-year	3-years	5-years	10-years	Inception
1	1998 BPF Trust Subscription	1998	$ 23.7	$ 0.9	$ 2.1	0.0%	(5.9%)	2.9%	6.4%	10.6%	5.0%
2	1999 BPF Non-U.S. Trust Subscription	1999	$ 24.5	$ 0.6	$ 4.0	0.1%	9.7%	6.4%	6.7%	16.8%	12.0%
3	1999 BPF Trust Subscription	1999	$ 24.5	$ 1.1	$ 3.1	0.1%	(4.8%)	4.1%	7.4%	10.5%	6.0%
4	ASP 2008 Non-US Fund	2008	$ 10.0	$ 2.1	$ 7.7	0.2%	12.3%	13.7%	11.2%	-	9.3%
5	ASP 2010 Direct Fund	2010	$ 1.5	$ 0.1	$ 1.6	0.0%	14.4%	18.7%	16.6%	-	15.3%
6	ASP 2010 Emerging Markets Fund	2010	$ 1.5	$ 0.5	$ 1.2	0.0%	18.3%	14.6%	-	-	10.5%
7	ASP 2010 Non-US Developed Fund	2010	$ 4.5	$ 1.6	$ 2.5	0.1%	4.5%	6.9%	6.8%	-	6.4%
8	ASP 2010 US Fund	2010	$ 7.5	$ 2.8	$ 5.4	0.1%	18.6%	16.6%	15.7%	-	16.0%
9	Brinson Venture Partnership Fund III	1993	$ 3.0	$ -	$ -	0.0%	-	10.8%	21.9%	27.3%	29.6%
10	BVCF III	1993	$ 3.0	$ -	$ -	0.0%	-	-	(2.9%)	(7.4%)	40.4%
11	BVCF IV	1999	$ 25.0	$ -	$ 3.8	0.1%	2.7%	31.5%	39.1%	26.1%	7.7%
12	Direct Co-Investment	2006	$ 20.0	$ 0.9	$ 10.5	0.2%	13.1%	19.7%	14.5%	-	5.8%
13	Institutional Venture Capital Fund II	1989	$ 5.0	$ -	$ -	0.0%	-	-	(12.1%)	17.9%	21.3%
	Total ASP Private Equity		$ 153.7	$ 10.5	$ 41.9	0.9%	8.9%	14.5%	12.8%	13.6%	11.0%
	Non-ASP Primary Fund Partnerships										
11	Capital International Private Equity Fund V	2007	$ 35.0	$ 5.6	$ 11.9	0.3%	(31.1%)	(12.0%)	(0.4%)	-	0.8%
12	Capital International Private Equity Fund VI	2011	$ 35.0	$ 13.8	$ 13.8	0.3%	(26.2%)	(19.4%)	-	-	(19.3%)
13	Coral Momentum Fund	2002	$ 25.0	$ -	$ -	0.0%	(13.9%)	(41.6%)	(32.4%)	(19.6%)	(18.5%)
14	Coral Partners V	1998	$ 40.0	$ -	$ -	0.0%	-	-	5.8%	18.5%	(5.6%)
15	Coral Partners V - Supplemental	2001	$ 2.0	$ -	$ -	0.0%	-	-	(46.6%)	(13.9%)	(10.2%)
16	Corsair III	2007	$ 25.0	$ 2.7	$ 13.7	0.3%	(13.5%)	(5.2%)	(3.9%)	-	(4.6%)
17	Corsair III - ND Investors LLC	2008	$ 11.2	$ 0.3	$ 11.7	0.3%	1.2%	2.7%	2.0%	-	1.0%
18	Corsair IV	2010	$ 25.0	$ 12.5	$ 16.4	0.4%	18.1%	17.0%	8.8%	-	7.0%
19	EIG Energy Fund XIV	2007	$ 45.0	$ 3.1	$ 14.7	0.3%	(37.5%)	(15.3%)	(6.0%)	-	2.5%
20	Hearthstone MSII	1999	$ 3.5	$ 3.5	$ (0.1)	(0.0%)	18.6%	175.5%	(100.0%)	(18.8%)	27.5%
21	Hearthstone MSIII	2003	$ 35.0	$ 35.2	$ 0.1	0.0%	22.8%	-	-	85.3%	25.2%
22	InvestAmerica (Lewis and Clark Fund)	2002	$ 7.5	$ 0.8	$ 2.7	0.1%	(31.0%)	(10.1%)	0.0%	2.1%	2.2%
23	L&C II	2009	$ 15.0	$ 1.4	$ 9.5	0.2%	(14.1%)	(8.5%)	(7.7%)	-	(8.5%)
24	Matlin Patterson Global Opportunities	2002	$ 25.3	$ -	$ 0.0	0.0%	(0.0%)	(1.8%)	10.6%	12.3%	16.7%
25	Matlin Patterson Global Opportunities II	2004	$ 40.6	$ 0.0	$ 1.6	0.0%	26.6%	(1.4%)	(34.3%)	(24.1%)	(23.9%)
26	Matlin Patterson Global Opportunities III	2007	$ 40.0	$ 4.1	$ 26.9	0.6%	1.3%	3.2%	17.2%	-	4.9%
27	Quantum Energy Partners IV	2007	$ 15.0	$ 2.0	$ 6.4	0.1%	(36.5%)	4.4%	12.7%	-	7.1%
28	Quantum Resources	2006	$ 15.0	$ 1.4	$ 0.0	0.0%	(55.6%)	(15.3%)	16.0%	-	2.9%
	Total - Non-ASP Private Equity		$ 440.2	$ 86.4	$ 129.5	2.8%	(16.6%)	(5.5%)	(0.9%)	(0.4%)	(0.4%)
	Total - Private Equity		$ 593.9	$ 96.9	$ 171.4	3.8%	(10.7%)	(0.6%)	2.7%	4.0%	3.8%

Source: Adams Street

Returns are reviewed, but not audited.

Summary: The private equity portfolio within the Pension Trust can largely be divided into two groups:

1) the Adams Street Partnerships which have generally performed in line with expectations with a net IRR of 12.8% in the last 5-years and 11.0% since inception; and

2) the Non-ASP Partnerships which have generally performed below expectations with a net IRR of -0.9% in the last 5-years and -0.4% since inception (with a few positive exceptions).

Key Takeaway: Promote the development of ***strategic partnerships*** like ASP to leverage a "best ideas" approach while increasing pricing leverage.

AGENDA ITEM IV.D.

Informational

TO: State Investment Board

FROM: Dave Hunter

DATE: July 20, 2018

SUBJECT: **Investment Consulting Contract Update**

The North Dakota State Investment Board and its clients and constituents have benefitted from a long-term relationship with Callan Associates since 1989. Although RIO personnel have no significant concerns with this mutually beneficial and long standing relationship, and have occasionally engaged other third party consultants to obtain differing expert opinion on certain topics such as best practices in board governance or to conduct specialized due diligence in certain private market sectors, RIO looks forward to providing the SIB with an update on the growth and success of the leading investment consulting firms which compete with Callan in the institutional market place. RIO intends to reach out to the following firms to provide this market update in the upcoming months: Aon Hewitt, Callan, Cambridge, Mercer, NEPC, PCA, Russell, RVK, SIS and Towers Watson.

AGENDA ITEM V. A.

Informational

North Dakota State Investment Board
Fundamental Investment Beliefs

July 24, 2018

Dave Hunter, Executive Director / CIO
Darren Schulz, Deputy Chief Investment Officer
ND Retirement & Investment Office (RIO)
State Investment Board (SIB)

NDSIB - Fundamental Investment Beliefs

- ❑ **Asset allocation is the # 1 driver of investment returns.**
- ❑ **The prudent use of active management can improve investment returns and contribute towards ensuring our clients attain their stated investment objectives.** **(See example below.)**
  - **If SIB client assets started out the year at $12.3 billion and earned 8% in one-year, SIB assets would approximate $13.3 billion at year-end assuming no contributions or withdrawals (e.g. $12.3 billion x 8% = $1 billion + $12.3 billion to start = $13.3 billion at year-end).**
  - **RIO estimates that SIB clients earned $100 million of incremental income from the prudent use of active investment management for the fiscal year ended June 30, 2018 (see next slide for support).**
  - **If these estimates are accurate, "asset allocation" was responsible for $900 million (or 90%) of the net investment return, while "active management" was responsible for $100 million (or 10%) of the net investment return for the fiscal year ended June 30, 2018.**

The above amounts are preliminary estimates and subject to change.

State Investment Board
Statement of Net Position
As of 5/31/2018

	As of 5-31-18	As of 6-30-17
ASSETS:		
INVESTMENTS (AT FAIR VALUE)		
DOMESTIC EQUITIES	$ 3,388,322,832	$ 3,002,119,217
GLOBAL/INTERNATIONAL EQUITIES	3,129,298,584	2,867,654,261
DOMESTIC FIXED INCOME	4,602,991,559	3,799,348,243
INTERNATIONAL FIXED INCOME	2,786,478	261,313,883
REAL ASSETS	2,205,672,266	2,069,264,037
PRIVATE EQUITY	178,740,187	167,161,916
INVESTED CASH (NOTE 1)	154,606,643	84,608,146
TOTAL INVESTMENTS	13,662,418,549	12,251,469,703
RECEIVABLES		
DIVIDEND/INTEREST RECEIVABLE	46,129,322	42,601,062
MISCELLANEOUS RECEIVABLE	35,833	26,676
TOTAL RECEIVABLES	46,165,155	42,627,738
OTHER ASSETS		
INVESTED SECURITIES LENDING COLLATERAL (NOTE 2)	55,876,178	77,669,419
OPERATING CASH	224,341	347,866
TOTAL ASSETS	13,764,684,223	12,372,114,726
DEFERRED OUTFLOWS OF RESOURCES		
DEFERRED OUTFLOWS RELATED TO PENSIONS	258,598	314,494
LIABILITIES:		
SECURITIES LENDING COLLATERAL (NOTE 2)	55,876,178	77,669,419
ACCOUNTS PAYABLE	-	254,082
ACCRUED EXPENSES	770,993	826,254
INVESTMENT EXPENSE PAYABLE	6,775,082	6,765,881
TOTAL LIABILITIES	63,422,253	85,515,636
DEFERRED INFLOWS OF RESOURCES		
DEFERRED INFLOWS RELATED TO PENSIONS	41,447	41,447
NET POSITION:		
HELD IN TRUST	13,701,479,121	12,286,872,137
TOTAL NET POSITION	$ 13,701,479,121	$ 12,286,872,137

State Investment Board
Statement of Changes in Net Position
For the Month Ended 5/31/2018

	Month Ended 5-31-18	Year-to-Date
ADDITIONS:		
INVESTMENT INCOME		
GAIN ON SALE OF INVESTMENTS	$ 128,966,241	$ 1,433,269,482
LOSS ON SALE OF INVESTMENTS	85,119,909	1,016,528,056
NET GAINS (LOSSES) INVESTMENTS	43,846,332	416,741,426
NET APPREC (DEPREC) MARKET VALUE	27,356,100	328,369,156
NET CHANGE IN FAIR VALUE OF INVESTMENTS	71,202,432	745,110,582
INTEREST, DIVIDEND & OTHER INVESTMENT INCOME	34,453,387	266,740,150
	105,655,819	1,011,850,732
LESS INVESTMENT EXPENSES	3,093,514	28,579,110
NET INCOME FROM INVESTING ACTIVITIES	102,562,305	983,271,622
SECURITIES LENDING INCOME	130,807	1,338,848
SECURITIES LENDING EXPENSES	26,141	267,554
NET SECURITIES LENDING INCOME	104,666	1,071,294
NET INVESTMENT INCOME		984,342,916
PURCHASE OF UNITS ($1/UNI	146,153,557	907,100,295
TOTAL ADDITIONS	248,820,528	1,891,443,211
DEDUCTIONS:		
ADMINISTRATIVE EXPENSES	140,469	1,448,895
REDEMPTION OF UNITS ($1/U	47,616,248	475,387,332
TOTAL DEDUCTIONS	47,756,717	476,836,227
CHANGE IN NET POSITION	201,063,811	1,414,606,984
NET POSITION:		
BEGINNING OF PERIOD	13,500,415,310	12,286,872,137
END OF PERIOD	$ 13,701,479,121	$ 13,701,479,121

Net investment income exceeds $980 million for the 11 months ended May 31, 2018.

SIB assets exceed $13.7 billion as of May 31, 2018 versus $12.3 billion at June 30, 2017.

SIB Investment Ends – March 31, 2018

SIB clients should receive investment returns consistent with their written investment policies and market variables. This "End" is evaluated based on comparison of each client's (a) actual net investment return, (b) standard deviation and (c) risk adjusted excess return, to the client's policy benchmark over 5 years.

	1 Yr Ended 3/31/2018	3 Yrs Ended 3/31/2018	5 Yrs Ended 3/31/2018
Pension Trust - $5.7 billion	$5.5 billion	$5 billion	$5 billion
Total Fund Net Return	12.28%	7.23%	8.30%
Policy Benchmark Return	10.10%	6.30%	7.26%
Excess Return (over Policy Benchmark)	2.18%	0.93%	1.04%
Legacy Fund - $5.5 billion	$5 billion	$4 billion	$3 billion
Total Fund Net Return	10.23%	6.56%	5.82%
Policy Benchmark Return	8.27%	5.30%	4.84%
Excess Return (over Policy Benchmark)	1.96%	1.26%	0.98%
Insurance Trust - $2.3 billion	$2 billion	$2 billion	$2 billion
Total Fund Net Return	7.52%	4.95%	5.03%
Policy Benchmark Return	4.95%	3.37%	3.70%
Excess Return (over Policy Benchmark)	2.57%	1.58%	1.33%

Net returns for our SIB client portfolios consistently exceed their Policy Benchmark. The SIB use of active management has conservatively generated over $300 million of incremental income for our client portfolios over the past 5-years including over $100 million of excess return in fiscal 2018.

This slide was revised on July 23 to reflect the correct Insurance Trust returns as of March 31, 2018.

Legacy Fund – Policy Benchmark Return

For the 1-year ended March 31, 2018

Legacy Fund Benchmark - 1 Year Ended 3/31/2018		Target Allocation	Index Return	Weighted Return
Asset Class	**Benchmark Index**			
U.S. Large Cap Equity	Russell 1000 Index	22%	14.0%	10.3%
U.S. Small Cap Equity	Russell 2000 Index	8%	11.8%	3.1%
		30%	**13.4%**	8.0%
International Equity	MSCI World ex-U.S.	**20%**	**13.9%**	5.6%
Global Equity		**50%**	**13.6%**	**6.8%**
Fixed Income	Bloomberg Aggregate	**35%**	**1.2%**	**0.4%**
Global Inflation Linked	Bloomberg Global Linkers	7%	9.0%	6.3%
Infrastructure	CPI-W	3%	2.4%	0.7%
Diversified Real Assets		**10%**	**7.0%**	**0.7%**
Real Estate		**5%**	**7.1%**	**0.4%**
Legacy Fund Composite Benchmark >>>>>>>>>>>>>>>>>>>>>>>>>>>>>				**8.3%**

1) **The Legacy Fund has an overall target asset allocation of 50% Equity, 35% Fixed Income, and 15% Real Assets.**
2) **The 50% Equity allocation is segmented into 30% U.S. equities (Russell 1000 and 2000) and 20% International (MSCI World ex-U.S.), while Fixed Income is benchmarked using the Bloomberg Aggregate Index.**
3) **The 15% Real Asset allocation is benchmarked using 7% of the Bloomberg Global Inflation Linked Index, 5% for Real Estate (using the National Council of Real Estate Investment Fiduciaries) and 3% CPI-W for Infrastructure.**

The Bloomberg Aggregate Index is the most widely used broad based fixed income benchmark, while NCREIF is the most widely used broad based real estate index and Bloomberg's Global Linkers is the most widely used global inflation linked security index.

Preliminary Return Estimates – Fiscal 2018

- **Pension Trust +9%** **($500 million of net income - $5.7 billion AUM)**
  - Asset Allocation – 58% Equity, 23% Fixed Income, 18% Real Assets
  - Equities up 13%; Fixed Income up 3%; and Real Assets up 6%
- **Legacy Fund +7%** **($370 million of net income - $5.5 billion AUM)**
  - Asset Allocation – 50% Equity, 35% Fixed Income, 15% Real Assets
  - Equities up 13%; Fixed Income up 1%; and Real Assets up 5%
- **Insurance Trust +5%** **($110 million of net income - $2.3 billion AUM)**
  - Allocation – 23% Equity, 54% Fixed Income, 18% Real Assets, 5% Cash
  - Equities up 13%; Fixed Income up 1.5%; and Real Assets up 6%

AUM = Assets Under Management are as of May 31, 2018

Preliminary return estimates are unaudited and subject to change.

NDSIB - Fundamental Investment Beliefs

Committed to Continuing Board Education and Strong Board Governance

- **Maintain a persistent awareness to the importance of continuing board education.**
  - **Emphasize continuing board education at SIB meetings and promote the attendance of educationally focused industry conferences.**
  - **Given budget pressures, the SIB engaged our consultant offering "Callan College" in Bismarck in July 2017 in order improve accessibility for board members and clients while reducing costs.**

- **Reaffirm organizational commitment to strong board governance.**
  - **Annual board review of SIB governance manual (conducted every September) including investment and governance education meetings in July of 2015, 2016, 2017 and 2018.**
  - **Conducted first formal board self-assessment during the first half of 2018 and made a commitment to conduct continuing board self-assessments in future years.**

Annual Board Planning Cycle – Biennial Agenda

Board Approved on April 27,2018

Fiscal 2017-18	July 2017	August	September	October	November	December	January 2018	February	March	April	May
	Board Education (BSC Offsite) - Election of Officers, - Appoint Audit Comm. - Plan Annual Agenda	Annual Investment Performance Review - Establish Investment Work Plan - Add Invest. Education	Annual Review of Gov. Manual - New Board Member Orientation Complete	Annual Evaluation of RIO vs. *Ends* policies - Annual Board Evaluation	ED/CIO Report on Investment Work Plan Board Education Investments	No Meeting Scheduled	Board Education Governance Commence Board Self-Assessment	ED/CIO Report on Investment Work Plan - Executive Limitations Review	Conduct Board Self-Assessment	Review Biennial Agenda, Ends and Strategic Plan Accept Board Self-Assessment	ED/CIO Report on Investment Work Plan Review ED/CIO Review Budget Guidelines
Fiscal 2018-19	**July 2018**	**August**	**September**	**October**	**November**	**December**	**January 2019**	**February**	**March**	**April**	**May**
	Plan Board Education Offsite - Election of Officers, - Appoint Audit Comm. - Plan Annual Agenda	Annual Investment Performance Review - Establish Investment Work Plan - Add Invest. Education	Annual Review of Gov. Manual - New Board Member Orientation Complete	Annual Evaluation of RIO vs. *Ends* policies - Annual Board Evaluation	ED/CIO Report on Investment Work Plan Board Education Investments	Reserved for a potential SIB meeting in advance of Legislative Session (Preview RIO Budget)	Board Education Risk Management Commence Board Self-Assessment - Legislative Update	ED/CIO Report on Investment Work Plan - Executive Limitations Review - Legislative Update	Confirm Budget Guidelines Accept Board Self-Assessment - Legislative Update	Review Biennial Agenda, End Policies, Strategic Investment Plan and Budget Guidelines	ED/CIO Report on Investment Work Plan Review ED/CIO Review Investment Guidelines

1.) SIB Governance Policy B-7 on Governance Process states that "the Board will follow a biennial agenda which (a) completes a re-exploration of Ends policies annually (April) (which is also referred to as "RIO's Mission Statement") and (b) continually improves its performance through attention to board education and to enriched input and deliberation."

2.) "In the first three months of the new cycle, the Board will develop its agenda for the ensuing year. Scheduled monitoring will be used to evaluate and adjust the annual agenda as needed."

3.) "The Board will identify areas of education and input needed to increase the level of wisdom forethought it can give to subsequent choices. A board education plan will be developed during July and August of each year."

4.) Budget Guidelines: RIO will prepare & submit a biennial budget pursuant to OMB guidelines as established by the Governor that will not reduce the level of service provided by RIO. Expenditures for budget items will not exceed the appropriation without approval of the State Investment Board.

Date: April 20, 2018

RIO 2017-19 Strategic Investment Plan

Fundamental Investment Beliefs

Asset allocation decisions are the primary driver of investment returns, but the prudent use of active investment management is an important contributor towards ensuring our clients attain their stated investment objectives. All investment decisions are driven by our desire to maximize risk adjusted returns based on our clients stated risk appetite and liquidity profile. SIB clients generated over **$300 million** of incremental income via the prudent use of active management the last 5 years including over **$100 million** of incremental income in fiscal **2018**.

Strategic Investment Plan

1. Reaffirm our organizational commitment to the importance of **continuing board education and strong board governance**.
2. **Enhance understanding of our core goals and beliefs while enhancing overall transparency.**
   a. **Remain steadfast in our commitment to the prudent use of active investment management.**
   b. Expand awareness to downside risk management which is essential to achieving our long term investment goals.
   c. Given actual and projected growth of SIB client assets and the heightened public awareness of the Legacy Fund, align our investment platforms to promote greater clarity and efficiency in reporting and implementing client investment policies.
3. Expand RIO's influence and ability to create positive and sustainable change by building deeper relationships with existing clients, organizations and legislative leaders.
   a. Enhance community outreach to build upon public awareness and confidence.
   b. Develop concise presentations which highlight our overall risk, return and cost control framework including our progress towards attaining our long-term goals.
4. Heighten employee engagement by promoting an open and collaborative work environment while encouraging employee participation in staff meetings, offer team members more opportunities to impact RIO's change initiatives **and improve the office environment for staff and clients**.
   a. RIO's ability to continue to deliver strong results is dependent on the combined efforts of our highly valuable team members.
5. **Enhance our internal control environment by improving use of proven risk management solutions relating to fraud risk assessments, investment risk management and overall enterprise risk management.**
   a. **A robust risk management framework serves as a foundation to support a sound internal control environment and lessen downside risks.**
   b. **Broaden stakeholder awareness of the challenges faced in estimating Legacy Fund earnings for any given period.**
6. Evaluate and expand the efficient use of technology in our investment program activities including risk management, compliance monitoring, client satisfaction surveys, website design and communications in order to increase overall efficiency and effectiveness.

ND Legacy Fund
Summary of Deposits, Earnings and Net Position
As of May 31, 2018

	Deposits	Total Net Earnings	Net Increase/ (Decrease)	Ending Net Position	Earnings as defined in NDCC 21-10-12
FY2012	**396,585,658**	2,300,225	398,885,883	398,885,883	**2,571,475**
FY2013	**791,126,479**	4,216,026	795,342,505	1,194,228,388	**15,949,089**
FY2014	**907,214,971**	113,153,662	1,020,368,633	2,214,597,021	**50,033,655**
FY2015	**1,011,343,040**	99,895,650	1,111,238,690	3,325,835,711	**95,143,905**
FY2016	**434,853,950**	45,851,680	480,705,630	3,806,541,341	**65,326,673**
FY2017	**399,501,134**	479,595,256	879,096,390	4,685,637,731	**207,814,875**
Totals					**436,839,672**
					Transferable Earnings
FY2018 *	**471,022,591**	**372,506,509**	**843,529,100**	**5,529,166,831**	**222,661,258**
Life-to-date Totals	**4,411,647,823**	**1,117,519,008**	**5,529,166,831**	**5,529,166,831**	**659,500,930**

** FY2018 amounts are preliminary and unaudited.* **All earnings prior through 6/30/17 became part of principal.**

Legacy Fund exceeded $5.5 billion as of May 31, 2018. Net Investment Income exceeds $1.1 billion since inception and $372 million in Fiscal 2018 (with unrealized gains and losses). Earnings as defined by NDCC 21-10-12 exceeded $222 million for the 11 months ended May 31, 2018.

NDCC 21-10-12 defines "earnings" as net income in accordance with generally accepted accounting principles excluding any unrealized gains or losses.

Callan

July 27, 2018

Performance Benchmarks

North Dakota State Investment Board

Paul Erlendson
Senior Vice President

Alex Browning
Senior Vice President

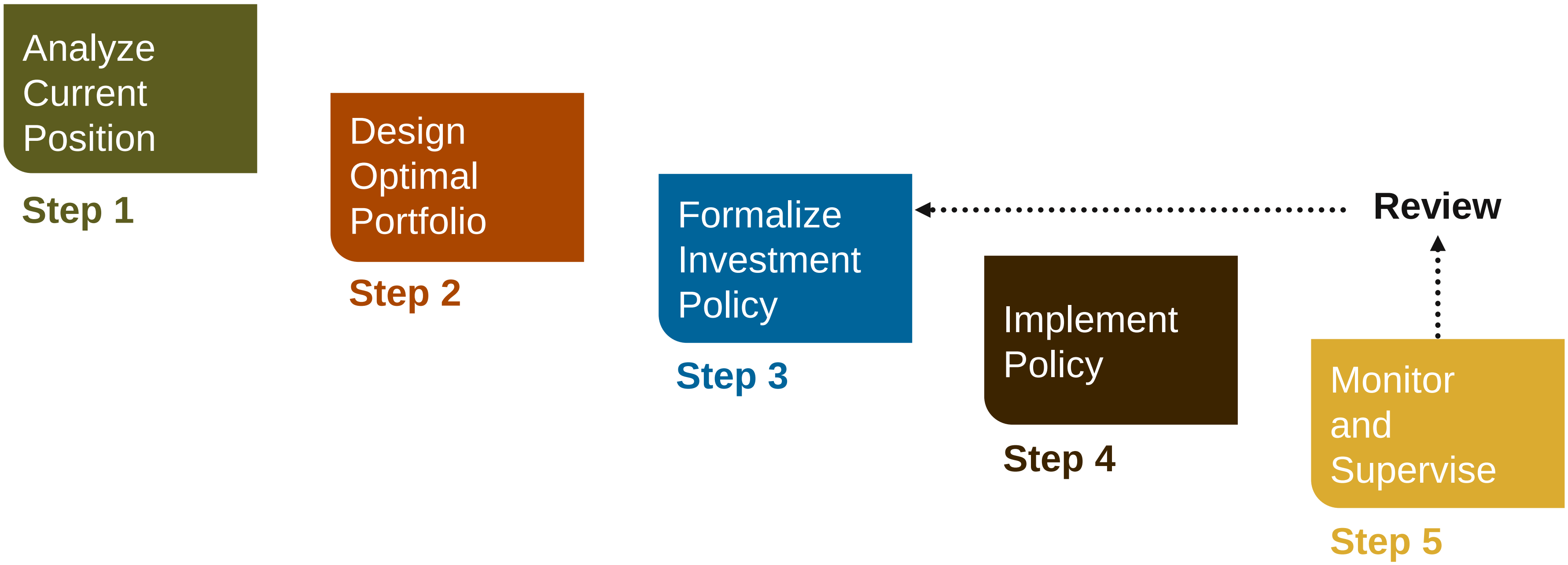
Benchmarking: An overview

- Definition of "benchmark": a standard of excellence, achievement, etc., against which similar things must be measured or judged[1]
- Benchmarking involves four (4) important issues:
  1. ***The object*** (the specific comparative index, group, or standard) that is the reference point of comparison;
  2. ***The subject*** (e.g.– Fund, asset class, manager) that is being evaluated:
  3. ***The characteristic***(s) or attribute(s) that are being measured or judged.
  4. ***The purpose*** of the measurement or judgement:
     – Is the exercise merely informative?
     – Is the comparison actionable (i.e.– will it lead to an adjustment or corrective action)?
- Utility relates to whether or not the comparison is actually useful – that it can lead to better outcomes – or is it merely being done as a matter of habit?
- Audience. For whose benefit is the comparison? *Policy makers* can change direction; *implementers* can adjust course; a *wider audience* might just want to know what's going on.
- Relevance. Comparisons should be carefully paired to the question at hand.
- Priority. There are limits to how much information can be absorbed by a Board. Prioritze!

[1] *http://www.dictionary.com/browse/benchmark?s=t*

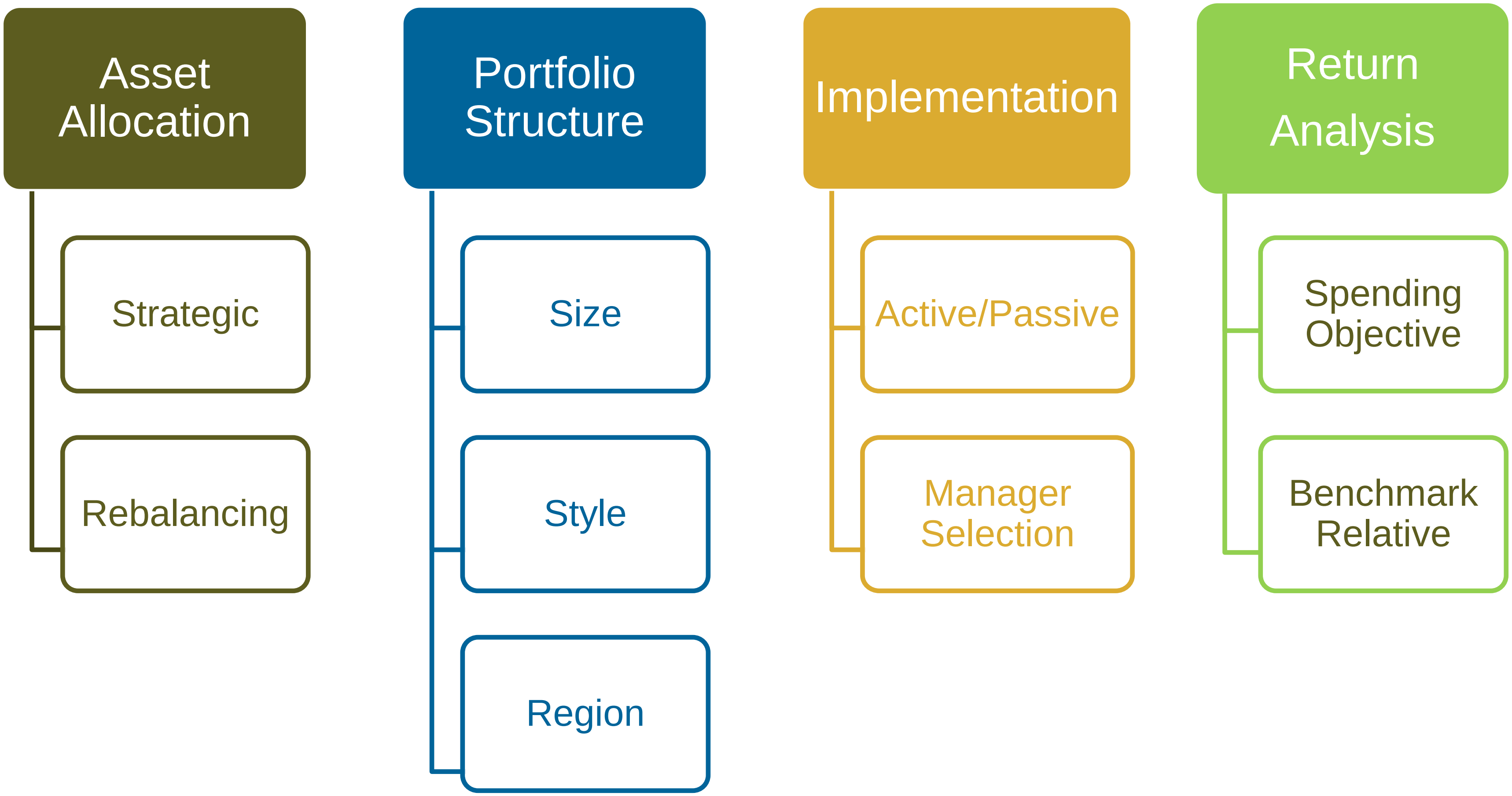
A backdrop: the fiduciary process

Benchmarking is used in all five steps of a prudently managed investment program



Decision-Making Levers

Which Decisions Are You Measuring?



- First Step: Define what is to be measured, how and why
  - "What" is often guided by the decisions that are under the Board's control
  - "How" involves the decision about the standard that will be measured and the object of comparison
  - "Why" is often answered by a belief that measurement and review can lead to better results

Strategic Asset Allocation Policy Target (Legacy Fund Example)

Asset Allocation

Strategic

Rebalancing

Asset Class	Policy Target	min	max	Optimal Mixes Mix 1	Mix 2	Mix 3	Mix 4	Mix 5
Broad US Equity	30%	0%	100%	18%	23%	29%	34%	40%
Broad Non-US Equity	20%	0%	100%	12%	16%	20%	24%	28%
Domestic Fixed Income	35%	0%	100%	55%	45%	35%	25%	15%
TIPS	5%	0%	100%	8%	7%	5%	4%	3%
Infrastructure	5%	0%	100%	2%	2%	3%	3%	3%
Real Estate	5%	0%	100%	5%	7%	8%	10%	11%
Total	**100%**			**100%**	**100%**	**100%**	**100%**	**100%**
Expected Return	**5.82%**			**4.88%**	**5.35%**	**5.79%**	**6.17%**	**6.52%**
Expected Real Return	**3.57%**			**2.63%**	**3.10%**	**3.54%**	**3.92%**	**4.27%**
Expected Standard Deviation	**10.75%**			**6.77%**	**8.63%**	**10.59%**	**12.59%**	**14.62%**
Projected Yield	**3.11%**			**3.27%**	**3.20%**	**3.12%**	**3.05%**	**2.97%**
Total Equity (%)	**50%**			**30%**	**39%**	**49%**	**58%**	**68%**
Total Fixed Income (%)	**40%**			**63%**	**52%**	**40%**	**29%**	**18%**
% Illiquid	**15%**			**12%**	**14%**	**16%**	**18%**	**19%**

- Assuming a spending policy of 3.75% and expected inflation of 2.25%, 6.00% is the nominal return benchmark to preserve real purchasing power and satisfy beneficiaries.
- The Strategic Asset Allocation (SAA) process, guided by the nominal return benchmark, examines which asset classes to invest in and their respective weights.
- The outcome is a Policy Target with an expected return (5.82%) and range of outcomes or standard deviation (10.75%). To achieve a higher return requires taking more risk.

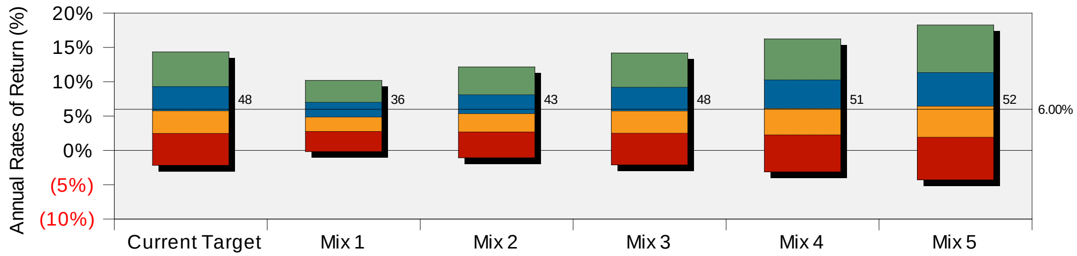
Alternative Asset Mixes & Projected 5 Yr. and 10 Yr. Returns

Asset Allocation

Strategic

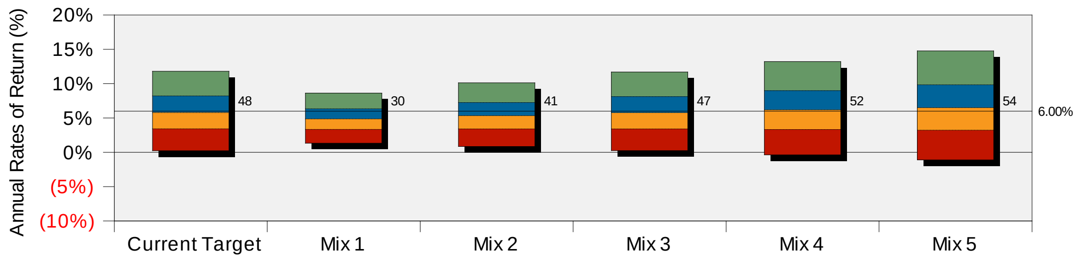
Rebalancing

Range of Projected Rates of Return
Projection Period: 5 Years



	Current Target	Mix 1	Mix 2	Mix 3	Mix 4	Mix 5
5th Percentile	14.4%	10.2%	12.2%	14.2%	16.2%	18.3%
25th Percentile	9.3%	7.0%	8.1%	9.2%	10.3%	11.3%
Median	5.8%	4.9%	5.4%	5.7%	6.1%	6.4%
75th Percentile	2.5%	2.8%	2.7%	2.5%	2.3%	1.9%
95th Percentile	(2.2%)	(0.2%)	(1.1%)	(2.1%)	(3.1%)	(4.3%)
Prob > 6.00%	48.4%	36.3%	43.3%	48.0%	50.6%	52.1%

Range of Projected Rates of Return
Projection Period: 10 Years



	Current Target	Mix 1	Mix 2	Mix 3	Mix 4	Mix 5
5th Percentile	11.8%	8.6%	10.1%	11.7%	13.2%	14.8%
25th Percentile	8.2%	6.4%	7.2%	8.1%	9.0%	9.8%
Median	5.8%	4.9%	5.3%	5.8%	6.2%	6.5%
75th Percentile	3.4%	3.3%	3.4%	3.4%	3.3%	3.2%
95th Percentile	0.2%	1.3%	0.9%	0.3%	(0.4%)	(1.1%)
Prob > 6.00%	47.6%	30.2%	40.9%	47.5%	51.5%	54.0%

- Range of returns narrows over longer time period. This is the benefit of “time diversification”, where extreme events offset one another producing less volatility.
- Negative returns are less likely over longer time period (roughly 1 in 20 chance).

Rebalancing Policy

Maintaining an expected level of risk

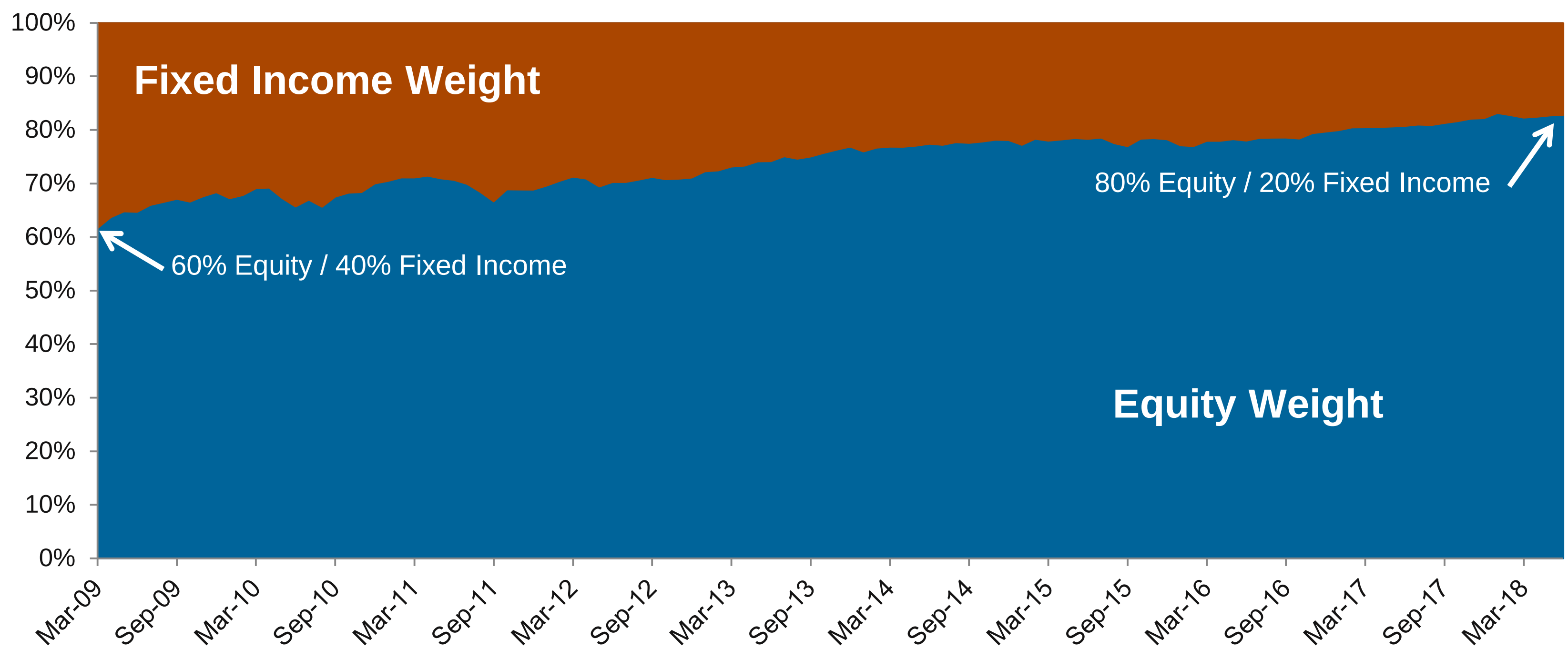
Asset Allocation

Strategic

Rebalancing

- Absent rebalancing, a portfolio of 60% equity and 40% fixed income beginning in March 2009 – after the Global Financial Crisis Market bottom – would have grown to over 80% equity and 20% fixed income by June 2018.
- This represents a large tactical shift away from the strategic asset allocation policy.
- For a Strategic Asset Allocation (SAA) policy to be relevant, it must be rebalanced.

Impact of "Buy and Hold" on a 60-40 Portfolio Over Time



Portfolio Structure

Legacy Fund Domestic Equity Composite vs. the Russell 3000 Index

Portfolio Structure
- Size
- Style
- Region

- Are there systematic pay-offs to Size and Style tilts vs. the benchmark?
- To what extent is it desirable and/or feasible to eliminate the existent Size and Style tilts?

Style Exposure Matrix for Holdings as of March 31, 2018
Top: Domestic Equity Composite
Bottom: Russell:3000 Index

	Value	Core	Growth	Total
Large	19.8% (110) 27.8% (110)	11.8% (86) 19.8% (87)	21.3% (92) 26.9% (96)	52.9% (288) 74.5% (293)
Mid	4.9% (117) 4.9% (168)	6.6% (148) 6.6% (214)	7.2% (143) 6.0% (204)	18.7% (408) 17.5% (586)
Small	7.8% (296) 2.1% (318)	10.7% (471) 2.8% (484)	6.2% (355) 2.3% (371)	24.7% (1122) 7.1% (1173)
Micro	1.6% (299) 0.3% (298)	1.5% (365) 0.4% (360)	0.7% (221) 0.2% (222)	3.7% (885) 0.9% (880)
Total	34.0% (822) 35.1% (894)	30.6% (1070) 29.6% (1145)	35.4% (811) 35.4% (893)	100.0% (2703) 100.0% (2932)

Portfolio Structure

Legacy Fund International Equity Composite

Portfolio Structure

Size

Style

Region

- Are there systematic pay-offs to Region and Style tilts vs. the benchmark?
- For example is there a high conviction in being overweight Europe & Pacific at the expense of Emerging?
- Is it desirable and/or feasible to eliminate the existent Region and Style tilts?

Style Exposure Matrix for Holdings as of March 31, 2018
Top: International Equity Composite
Bottom: MSCI:ACWI ex US

	Value	Core	Growth	Total
Europe	22.7% (369) 13.8% (124)	14.9% (347) 13.5% (129)	18.5% (251) 15.6% (201)	56.1% (967) 42.9% (454)
N. America	0.3% (68) 1.9% (32)	2.4% (62) 2.8% (28)	1.7% (26) 1.6% (31)	4.4% (156) 6.4% (91)
Pacific	11.3% (843) 9.0% (145)	8.7% (360) 6.4% (146)	11.8% (186) 9.3% (179)	31.8% (1389) 24.8% (470)
Emerging	1.4% (10) 8.0% (310)	1.5% (18) 7.9% (261)	4.8% (27) 10.0% (271)	7.7% (55) 26.0% (842)
Total	35.7% (1290) 32.7% (611)	27.5% (787) 30.7% (564)	36.8% (490) 36.6% (682)	100.0% (2567) 100.0% (1857)

Active/Passive and Efficient Markets

Allocating fees to active management

Implementation

Active/ Passive

Manager Selection

- Less efficient areas of the market, such as Non-U.S. Small Cap Equity, have tended to reward active management more than efficient areas such as U.S. Large Cap Equity.

How Often Large Cap U.S. Equity Managers Beat the Russell 1000 Index by More Than Fee Hurdle in Rolling 3-Year Periods Over Last 20 Years

Fee Hurdle	0.25%	0.30%	0.35%	0.40%	0.45%	0.50%	0.55%	0.60%	0.65%	0.70%
Median	39%	38%	30%	30%	23%	15%	14%	14%	14%	10%
45th Percentile	51%	48%	48%	48%	46%	43%	40%	39%	38%	34%
40th Percentile	69%	69%	64%	61%	58%	53%	51%	49%	48%	46%
35th Percentile	81%	79%	79%	79%	76%	75%	70%	69%	69%	63%
30th Percentile	93%	91%	89%	86%	86%	86%	85%	84%	81%	80%
25th Percentile	99%	98%	95%	95%	94%	91%	90%	89%	88%	88%

Average Annualized 3-Year Excess Return (gross) – Median Manager: -0.18%

How Often Non-U.S. Small Cap Equity Managers Beat the MSCI EAFE Small Cap Index by More Than Fee Hurdle in Rolling 3-Year Periods Over Last 16 1/4 Years

Fee Hurdle	0.75%	0.80%	0.85%	0.90%	0.95%	1.00%	1.05%	1.10%	1.15%	1.20%
Median	65%	62%	62%	62%	60%	60%	58%	57%	57%	57%
45th Percentile	69%	68%	68%	66%	65%	65%	65%	63%	63%	63%
40th Percentile	83%	82%	80%	78%	74%	74%	72%	69%	69%	69%
35th Percentile	92%	91%	91%	91%	91%	91%	89%	89%	89%	88%
30th Percentile	100%	100%	100%	100%	100%	100%	100%	100%	98%	98%
25th Percentile	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%

Average Annualized 3-Year Excess Return (gross) – Median Manager: 1.54%

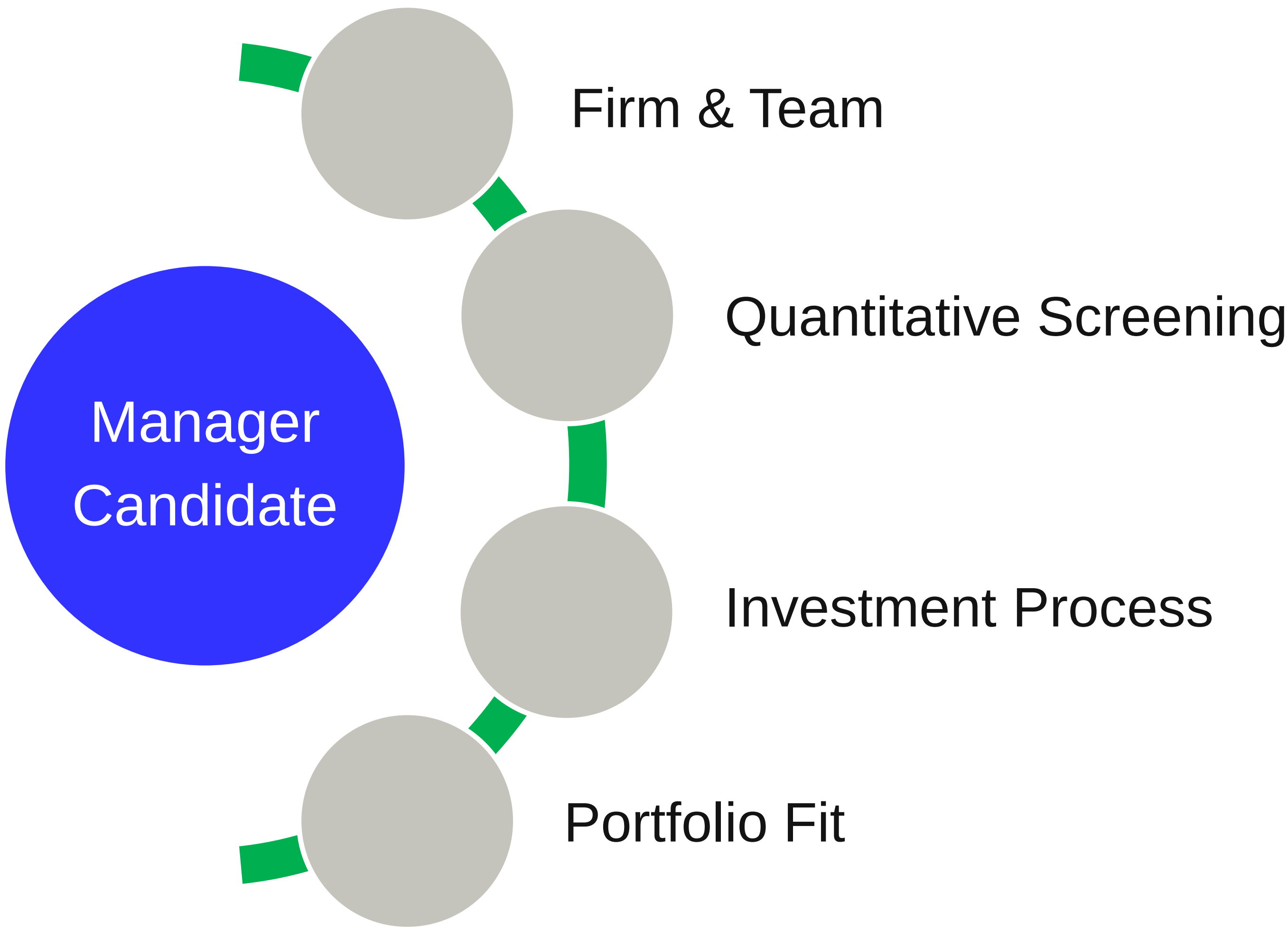
Manager Selection

Forecasting net of fee value add and fit within the existing portfolio

Implementation

Active/ Passive

Manager Selection



- First step: Define the prospective role of a manager and its strategy in the portfolio, then select a performance benchmark.

Measuring the Effectiveness of Process & Decisions[1]

Benchmark Criteria (In a perfect world)

1. **Specified in Advance:** The benchmark is specified prior to the start of the evaluation period.
2. **Relevant:** The benchmark reflects the objective, investment mandate, or strategy of the total fund.
3. **Measurable:** The benchmark's return is readily calculable on a reasonably frequent basis.
4. **Unambiguous:** The constituents of the investable universe can be clearly identified and priced.
5. **Representative of Current Investment Opinions:** In the case of a single strategy, the firm has current knowledge of the investable universe.
6. **Accountable:** The firm selects the benchmark and is accountable for any deviations from the benchmark.
7. **Investable:** The benchmark offers a passive alternative that is a realizable and alternative opportunity genuinely open to the investor.
8. **Complete:** The benchmark provides a broad representation of the market to which it pertains.

- Importantly, Private Markets and other illiquid asset classes fail criteria 3, 4, 7, and 8. In these cases additional analysis is required to create custom benchmarks.

[1] Modified from the CFA Institute Guidance Statement on Benchmarks; https://www.gipsstandards.org/standards/Documents/Guidance/exposure_draft_public_comment_benchmarks.pdf

Return Analysis

Forecasted Range of Returns

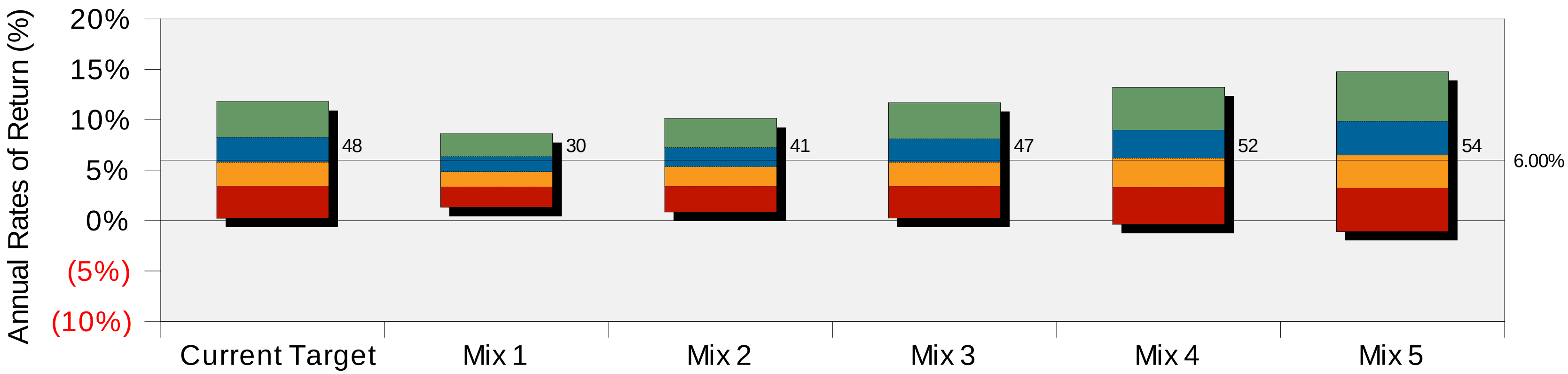
Returns

Spending Objective

Benchmark Relative

- The Strategic Asset Allocation forecasted an expected return of 5.82%.
- To achieve a 5.82% expected return, one must also accept an expected standard deviation of 10.75%.
- A portfolio standard deviation of 10.75% means that in any 10 year period, the portfolio could generate a return as low as 0.20% or as high as 11.8% with a near even chance of generating a 6.0% return.

Range of Projected Rates of Return
Projection Period: 10 Years



	Current Target	Mix 1	Mix 2	Mix 3	Mix 4	Mix 5
5th Percentile	11.8%	8.6%	10.1%	11.7%	13.2%	14.8%
25th Percentile	8.2%	6.4%	7.2%	8.1%	9.0%	9.8%
Median	5.8%	4.9%	5.3%	5.8%	6.2%	6.5%
75th Percentile	3.4%	3.3%	3.4%	3.4%	3.3%	3.2%
95th Percentile	0.2%	1.3%	0.9%	0.3%	(0.4%)	(1.1%)
Prob > 6.00%	47.6%	30.2%	40.9%	47.5%	51.5%	54.0%

Return Analysis

Historical Returns vs. Spending Objective

Returns

Spending Objective

Benchmark Relative

- The Strategic Asset Allocation (SAA) forecasted an expected return of 5.82%
- The Spending Objective is 6.00%
- Five different historical time periods – which one is relevant?

	Last Quarter	Last Year	Last 3 Years	Last 5 Years	Last 6-1/2 Years
Total Fund					
Gross	(0.49%)	10.45%	6.80%	6.04%	5.03%
Net	(0.54%)	10.23%	6.56%	5.82%	4.85%
Target*	(0.79%)	8.27%	5.30%	4.84%	3.81%

- *"The primary mission of the legacy fund is to preserve the real inflation-adjusted purchasing power of the money deposited into the fund while maximizing total return."*
- During the last three full years of performance, the fund has achieved its Spending Objective however at the expected risk of a near zero return over any 10 year period.
- Therefore while the Spending Objective guides the SAA, it does so with an expectation of periodic underperformance.
- Achieving a 6.00% return requires taking on the risk of under and out performance

3 Year Annualized Return Analysis

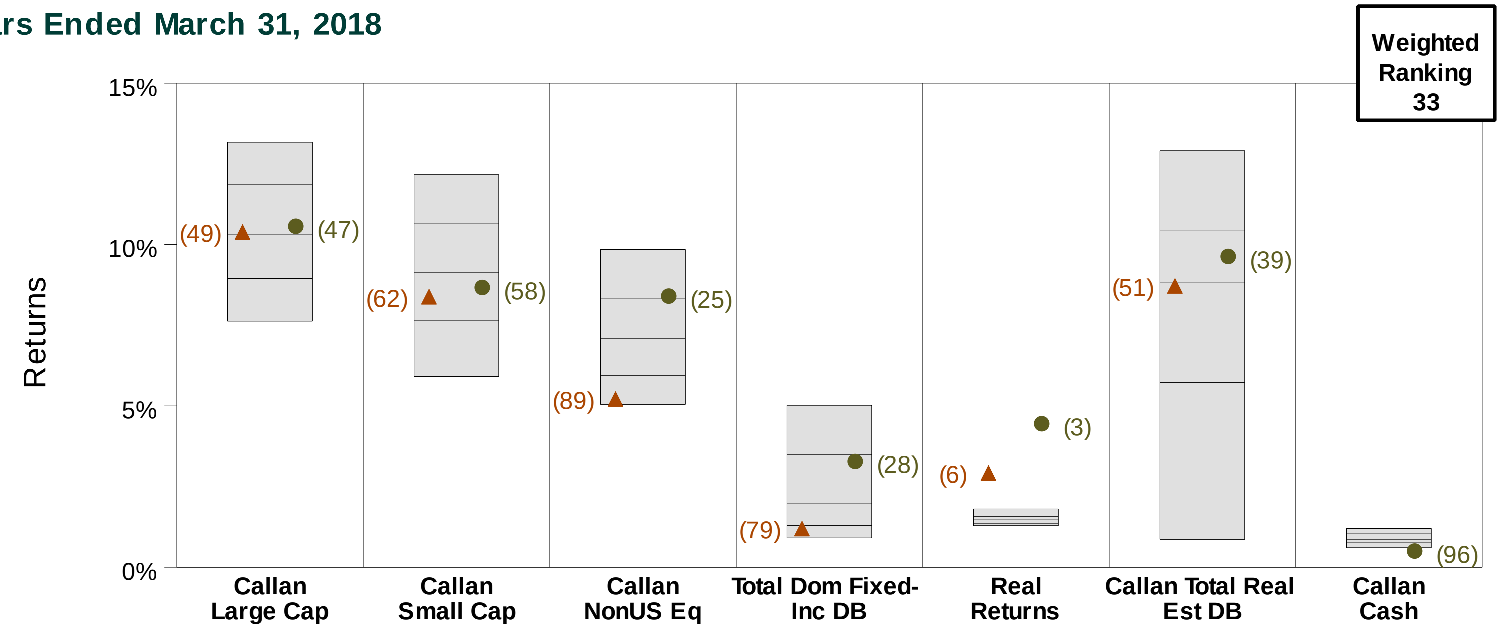
Historical Asset Class Returns vs. Asset Class Composite Benchmarks & Opportunity Sets

Returns

Spending Objective

Benchmark Relative

Total Asset Class Performance
Three Years Ended March 31, 2018



	Callan Large Cap	Callan Small Cap	Callan NonUS Eq	Total Dom Fixed-Inc DB	Real Returns	Callan Total Real Est DB	Callan Cash
10th Percentile	13.17	12.17	9.85	5.02	1.81	12.91	1.20
25th Percentile	11.86	10.66	8.34	3.50	1.58	10.43	1.04
Median	10.32	9.14	7.10	1.97	1.47	8.84	0.86
75th Percentile	8.95	7.64	5.95	1.29	1.37	5.73	0.76
90th Percentile	7.63	5.91	5.05	0.91	1.29	0.87	0.61
Asset Class Composite ●	10.52	8.61	8.35	3.23	4.40	9.57	0.45
Composite Benchmark ▲	10.39	8.39	5.22	1.20	2.92	8.72	-

- All asset classes, except cash, beat their respective benchmarks
- When weighted to the SAA, the total fund ranks in the 33rd percentile for implementation

3 Year Annualized Return Analysis

Historical Performance Decomposed

Returns

Spending Objective

Benchmark Relative

Three Year Annualized Relative Attribution Effects

Asset Class	Effective Actual Weight	Effective Target Weight	Actual Return		Target Return		Manager Effect		Asset Allocation	Total Relative Return
Large Cap Equity	22%	22%	10.52%		10.39%		0.02%		(0.02%)	(0.00%)
Small Cap Equity	8%	8%	8.61%		8.39%		0.01%		(0.01%)	0.01%
International Equity	20%	20%	8.35%		5.22%		0.62%		(0.03%)	0.59%
Domestic Fixed Income	35%	35%	3.23%		1.20%		0.71%		0.01%	0.72%
Diversified Real Assets	10%	10%	4.40%		2.92%		0.14%		0.02%	0.16%
Real Estate	6%	5%	9.57%		8.72%		0.05%		(0.00%)	0.04%
Short Term Fixed Income	0%	0%	-		-		0.00%		(0.00%)	(0.00%)
Cash & Equivalents	0%	0%	0.45%		0.45%		0.00%		(0.02%)	(0.02%)
Total			**6.80%**	**=**	**5.30%**	**+**	**1.56%**	**+**	**(0.05%)**	**1.50%**

- Total Fund annualized returns can be further decomposed into components of the process and decisions leading up to the implemented portfolio.
- **Target Return:** Represents the SAA return – are we expected to meet our Spending Objective given our risk tolerance?
- **Manager Effect:** Given the manager selection process, including intentional style, region, and size tilts, have we added value through active management and where?
- **Asset Allocation:** Given a Rebalancing Policy, how much did operating the portfolio add or detract from portfolio performance?
- **Actual Return:** Quantitatively summarizes decisions that are under the Board's control (Asset Allocation, Portfolio Structure, and Implementation) and their value added effects.

Performance Benchmarking

Conclusions

- First Step: Define what is to be measured, how and why
  - "What" is often guided by the decisions that are under the Board's control
  - "How" involves the decision about the standard that will be measured and the object of comparison
  - "Why" is often answered by a belief that measurement and review can lead to better results
- Determine the objective and – in the case of multiple objectives – their priority
- Decompose the total objective(s) into independent, measurable decisions
  - Identify what can't be measured
  - Develop an understanding of what can be measured and how it might be improved
- Determine the relevant time periods for analysis
- Marry the quantitative measurement process with the Fund's overarching mission

AGENDA ITEM V.C.

Informational

North Dakota State Investment Board
Board Member Education Options

July 24, 2017

Dave Hunter, Executive Director / CIO
Darren Schulz, Deputy Chief Investment Officer
ND Retirement & Investment Office (RIO)
State Investment Board (SIB)

Board Member Education Options - Background

- **Based on our Board Self-Assessment Survey and Executive Review process conducted earlier this year, SIB members expressed a willingness to engage in board education tailored to meet the varying needs and experience of individual board members.**

- **In order to address this need, RIO worked with Callan to create a brief survey distributed to each SIB member to develop a custom investment education options better suited to meet the individual needs of each board member.**

- **The results of the survey are summarized on the following slides noting that all responding SIB members indicated they were "comfortable" with the investment subjects that come before the SIB as evidenced by an average rating of 3.9 on a 5.0 scale.**
  - **On a scale of 1 (low) to 5 (high), how comfortable are you with the investment subjects that come before the SIB?**

Board Member Education – Survey Results

SIB member were asked to "Identify at least three of the following subjects as potential education topics in the order of interest":

1. **Performance Evaluation (including how to read the consultant's performance reports);**
2. **Manager Structure (number and types of strategies) within individual asset classes;**
3. **Best practices in investment program governance and fiduciary conduct;**
4. Asset allocation and liability valuations;
5. Trust and custody issues;
6. Manager selection process and considerations; and
7. Best practices in managing board, staff, and advisor relations.

Survey results indicated the # 1 education topic related to "Performance Evaluation". In response, RIO invited Callan to our July 27, 2018 SIB meeting to provide additional education on the performance benchmarks used to evaluate our overall performance (in addition to our monitoring of actual and target asset allocation levels to ensure they are materially consistent). RIO notes that recent meetings with OMB and Legacy Fund Advisory Board echoed this educational need.

The next two topics of interest relate to "# 2 Manager Structure" and "# 3 Best practices in investment program governance and fiduciary conduct" which RIO will look to address in the upcoming year. RIO notes that survey responses numbered 4 through 7 were identified by three or fewer respondents.

After this review of survey results, RIO will work with the SIB and Callan in the development of custom investment education plans for each SIB member noting that Callan has a long-history of offering excellent educational courses and conferences to our various board members.

Board Member Education – Survey Results

SIB member were asked "In order to participate in education, would your prefer":

1. **That topics be presented at specially scheduled SIB retreats;**
2. **To travel to third party sponsored conferences and/or training sessions;**
3. That topics be presented at regularly scheduled SIB meetings; and
4. To consume educational materials on your own time rather than in a group setting.

Survey results indicated SIB members clearly prefer to participate in education at "specially scheduled SIB retreats" like the ones we have scheduled in July in each of the last four years which have included world-renowned governance expert Dr. Keith Ambachtsheer, Aon Hewitt Fiduciary Services Practice Leader Jeanna Cullins JD, and Callan Executive Chairman and Chairman of the CFA Institute Asset Manager Code of Professional Conduct Advisory Committee Ron Peyton in addition to the four highly regarded investment professionals which are presenting to the SIB today!

"Travel to third party sponsored conferences and/or training sessions" was ranked # 2 followed by "topics presented at regularly scheduled SIB meetings at # 3.

<u>Given the above responses, I invite each SIB member to identify one professional investment and/or governance education conference each fiscal year going forward</u>. RIO will ensure that we continue to operate within our legislatively approved budget guidelines without exception. **The Office of the Attorney General has consistently emphasized the importance of RIO and SIB investment due diligence and professional continuing education for our staff and board members in order to adhere to our fiduciary standards and responsibilities in the oversight of SIB client investments which exceeded $13.7 billion as of May 31, 2018.**

Board Member Education – Survey Results

SIB member were asked "How much time are you willing to commit annually in pursuit of investment education". All respondents indicated "3 to 5 days" or "more than 5 days" (with no responses for "less than 3 days".

Based on this response, SIB members have stated a willingness to have at least 24 hours (or 3 days) of investment education annually, although the average response was closer to 32 to 40+ hours (or 4 or 5+ days) annually.

SIB member were also asked "Which of the following educational formats do you prefer"?

1. **Interactive sessions;**
2. **Conferences;**
3. **Lectures;** and
4. Readings (a distant fourth)

Based on the above responses, RIO will seek to schedule interactive sessions (such as today's SIB meeting) in addition to continuing to support professional continuing education "conferences" and "lectures" for all of our SIB members.

Summary:

RIO thanks the SIB members for participating in this educational survey while noting that educational needs and topics are dynamic and change over time. As such, RIO invites additional input and comments on enhancing our Board Education Options going forward.

NDSIB - Fundamental Investment Beliefs

Committed to Continuing Board Education and Strong Board Governance

- **Maintain a persistent awareness to the importance of continuing board education.**
  - **Emphasize continuing board education at SIB meetings and promote the attendance of educationally focused industry conferences.**
  - **Given budget pressures, the SIB engaged our consultant offering "Callan College" in Bismarck in July 2017 in order improve accessibility for board members and clients while reducing costs.**

- **Reaffirm organizational commitment to strong board governance.**
  - **Annual board review of SIB governance manual (conducted every September) including investment and governance education meetings in July of 2015, 2016, 2017 and 2018.**
  - **Conducted first formal board self-assessment during the first half of 2018 and made a commitment to conduct continuing board self-assessments in future years.**

Board Education – July 1, 2016 to June 30, 2018

SIB members have actively participated in numerous educational opportunities over the last year including the following sessions which occurred during our regularly scheduled board meetings:

- Capital Market Updates & Performance Review Education by Callan (6 hours)
- Investment Updates by JPMorgan, PIMCO, Western Asset Management, Invesco, Wells Fargo, Prudential, Adams Street & Financial Recovery Technologies (8 hours)
- Investment Performance Reviews by RIO Staff (6 hours)
- Governance Education by Aon Hewitt (5 hours)
- Investment, Litigation and Open Records Education by Attorney General Office (3 hours)
- Callan College and Governance Education by Callan (6 hours)
- New Manager Presentations by Ares, BlackRock, Cerberus and I-Squared (4 hours)
- Time spent by board members preparing for 10+ SIB meetings per year (10+ hours)

Several board members and RIO staff have obtained additional investment education by attending conferences sponsored by a wide variety of industry experts such as:

- Callan's Annual Conference and/or Callan College (two to three days)
- Public Pension Plan Roundtables, Forums & Conferences (two to three days)
- Great Plains (and/or Mountain States) Investor Forum (one to two days)
- National Association of State Retirement Officers (two to three days)
- National Association of State Investment Officers (two to three days)
- National Association of State Investment Professionals (two to three days)
- Various conferences sponsored by "Pensions and Investments" (one to three days)

Next Educational Opportunity: SIB Meeting on July 27, 2018

Annual SIB Meeting Schedule for 2018-19

July 27, 2018	**January 25, 2019**
August 24, 2018	**February 22, 2019**
September 28, 2018	**March 22, 2019**
October 26, 2018	**April 26, 2019**
November 16, 2018	**May 24, 2019**
Dec. 21, 2018 (Reserved)	June – No Meeting

The SIB approved the above meeting schedule on January 26, 2018.

Note: Most SIB meetings contain some type of board education on investments, governance, capital market trends, economic conditions or securities litigation.

Annual Board Planning Cycle – Biennial Agenda

Board Approved on April 27,2018

Fiscal 2017-18	July 2017	August	September	October	November	December	January 2018	February	March	April	May
	Board Education (BSC Offsite) - Election of Officers, - Appoint Audit Comm. - Plan Annual Agenda	**Annual Investment Performance Review** - Establish Investment Work Plan - Add Invest. Education	**Annual Review of Gov. Manual** - New Board Member Orientation Complete	**Annual Evaluation of RIO vs. *Ends* policies** - Annual Board Evaluation	**ED/CIO Report on Investment Work Plan** **Board Education Investments**	No Meeting Scheduled	**Board Education Governance** **Commence Board Self-Assessment**	**ED/CIO Report on Investment Work Plan** - Executive Limitations Review	**Conduct Board Self-Assessment**	**Review Biennial Agenda, Ends and Strategic Plan** **Accept Board Self-Assessment**	**ED/CIO Report on Investment Work Plan Review** **ED/CIO Review Budget Guidelines**

Fiscal 2018-19	July 2018	August	September	October	November	December	January 2019	February	March	April	May
	Plan Board Education Offsite - Election of Officers, - Appoint Audit Comm. - Plan Annual Agenda	**Annual Investment Performance Review** - Establish Investment Work Plan - Add Invest. Education	**Annual Review of Gov. Manual** - New Board Member Orientation Complete	**Annual Evaluation of RIO vs. *Ends* policies** - Annual Board Evaluation	**ED/CIO Report on Investment Work Plan** **Board Education Investments**	**Reserved for a potential SIB meeting in advance of Legislative Session (Preview RIO Budget)**	**Board Education Risk Management** **Commence Board Self-Assessment** - Legislative Update	**ED/CIO Report on Investment Work Plan** - Executive Limitations Review - Legislative Update	**Confirm Budget Guidelines** **Accept Board Self-Assessment** - Legislative Update	**Review Biennial Agenda, End Policies, Strategic Investment Plan and Budget Guidelines**	**ED/CIO Report on Investment Work Plan Review** **ED/CIO** Review Investment Guidelines

1.) SIB Governance Policy B-7 on Governance Process states that "the Board will follow a biennial agenda which (a) completes a re-exploration of Ends policies annually (April) (which is also referred to as "RIO's Mission Statement") and (b) continually improves its performance through attention to board education and to enriched input and deliberation."

2.) "In the first three months of the new cycle, the Board will develop its agenda for the ensuing year. Scheduled monitoring will be used to evaluate and adjust the annual agenda as needed."

3.) "The Board will identify areas of education and input needed to increase the level of wisdom forethought it can give to subsequent choices. A board education plan will be developed during July and August of each year."

4.) Budget Guidelines: RIO will prepare & submit a biennial budget pursuant to OMB guidelines as established by the Governor that will not reduce the level of service provided by RIO. Expenditures for budget items will not exceed the appropriation without approval of the State Investment Board.

Date: April 20, 2018

Agenda Item V.D.

Informational

TO: State Investment Board
FROM: Dave Hunter
DATE: July 20, 2018
SUBJECT: Epoch Investment Partners

Overview:

Epoch manages $414 million in global equities for the Pension Trust using a concentrated investment approach of 25 to 35 high conviction stocks. Epoch's "Global Choice" strategy severely underperformed the MSCI World index by over 8% in 2016 before outperforming its benchmark by nearly 9% in 2017. Epoch's investment performance as of June 30, 2018, is shown below:

	QTD	YTD	1 Year	3 Year	5 Year	Inception to Date (7/8/2007)
North Dakota State Investment Board (Gross)	3.6	1.0	14.7	8.3	10.2	7.0
MSCI World (Net)	1.7	0.4	11.1	8.5	9.9	4.4

	2017	2016	2015	2014	2013	2012	2011	2010	2009	2008	2007[1]
North Dakota State Investment Board (Gross)	31.2	-0.6	0.4	3.5	33.2	15.1	-1.3	7.5	37.5	-29.7	-1.8
MSCI World (Net)	22.4	7.5	-0.9	4.9	26.7	15.8	-5.5	11.8	30.0	-40.7	-1.9

Epoch has a 7% asset allocation within the Pension Trust and is paired with LSV in our Global Equity portfolio noting that Epoch and LSV returns have generally been negatively correlated over historical rolling 3-to-5 year periods.

	March 31, 2018 Market Value	Weight
GLOBAL EQUITY	**$3,269,439,660**	**57.61%**
Domestic Equity	**$1,252,298,768**	**22.07%**
Large Cap Domestic Equity	**$953,240,774**	**16.80%**
L.A. Capital	372,564,954	6.57%
LACM Enhanced Index	199,614,929	3.52%
Northern Trust AM Enh S&P 500	192,200,480	3.39%
Parametric Clifton Enh S&P 500	188,860,412	3.33%
Small Cap Domestic Equity	**$299,057,994**	**5.27%**
Atlanta Capital	152,021,780	2.68%
Parametric Clifton Enh Small Cap	147,036,214	2.59%
International Equity	**$916,187,276**	**16.15%**
Developed Int'l Equity	**$685,286,729**	**12.08%**
DFA Int'l Small Cap	90,579,085	1.60%
Northern Trust AM World Ex US	326,204,381	5.75%
Wellington Management Co.	90,339,739	1.59%
William Blair	178,163,524	3.14%
Emerging Markets Equity	**$230,900,547**	**4.07%**
Axiom	167,894,892	2.96%
DFA	63,005,655	1.11%
World Equity	**$919,079,756**	**16.20%**
EPOCH Investment Partners	400,400,325	7.06%
LSV Asset Management	518,679,431	9.14%

EPOCH

Epoch Investment Partners, Inc.

Global Choice

William W. Priest, CFA
CEO, Co-CIO & Portfolio Manager

Jeffrey M. Ulness
Managing Director, Sub-Advisory Relations

PRESENTATION TO:

North Dakota State Investment Board

JULY 27, 2018

Epoch's Aspiration Statement

To provide superior, risk-adjusted results using a transparent approach based on our free cash flow philosophy.

To serve investors who seek and value Epoch’s investment approach.

To continue as a thought leader and innovator in global investment management.

Agenda

- Our Firm
- Our Perspective
- Our Investment Process
- Account Review – Global Choice
- Capital Markets Outlook

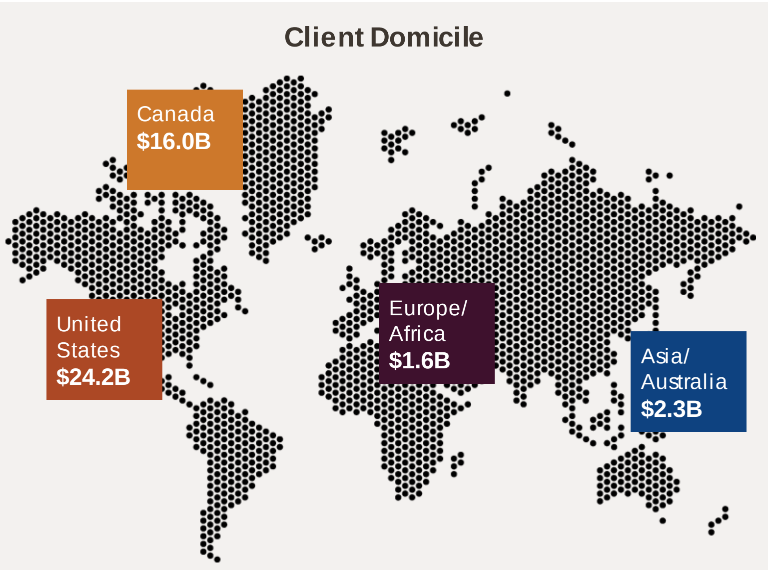
Epoch at a Glance

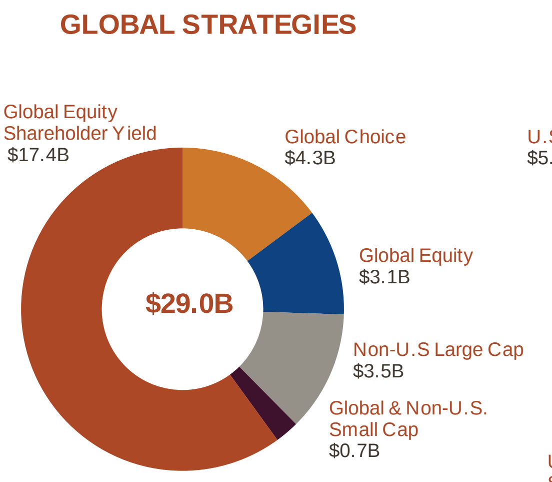
Global equity investors with a distinct perspective on the long-term drivers of shareholder return

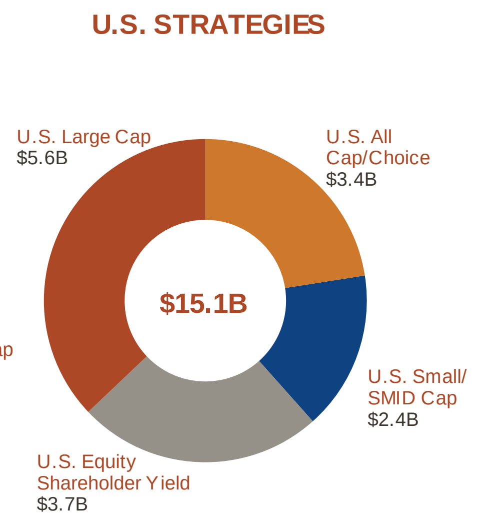
- Formed in 2004; an independently operated subsidiary of TD Bank since 2013
- Investment process focused on the generation and allocation of free cash flow
- Risk management integrated throughout the investment process
- A focused range of strategies managed for a diverse client base

Epoch at a Glance

AUM: $44.2 Billion[1]







Representative Client List[2]

CORPORATIONS

- ArcelorMittal USA
- DXC Technology
- Kellogg Company
- Nova Scotia Power Inc.
- Sentinel Retirement Fund
- StatePlus

NON-PROFIT & OTHER

- Bradley University
- Church of the Nazarene
- Masonic Homes of California
- Wespath Investment Management

GOVERNMENT

- CalPERS
- Florida State Board of Administration
- London CIV
- North Dakota State Investment Board
- Ohio Bureau of Workers' Compensation
- Oklahoma Teachers
- Public Employees' Retirement System of Mississippi

HEALTH SERVICES & INSURANCE

- Blue Cross and Blue Shield of Kansas
- Boston Medical Center
- Greater Baltimore Medical Center
- OhioHealth
- USAA

SUB-ADVISORY

- CI – Assante Funds
- Jackson National Asset Management
- John Hancock Funds
- New York Life – MainStay Funds
- Prudential Investments
- TD Bank Group

UNION

- CWA/ITU Negotiated Pension Plan
- Major League Baseball Players Association
- Theatrical State Employees, Local No. One, I.A.T.S.E.
- Steelworkers Pension Trust

[1]As of June 30, 2018; may not total due to rounding.
[2]The institutional clients shown were selected based on client type and client domicile across all strategies. It is not known whether the listed clients approve or disapprove of the advisory services provided.

Experienced Investment Team Supported by a Robust Infrastructure

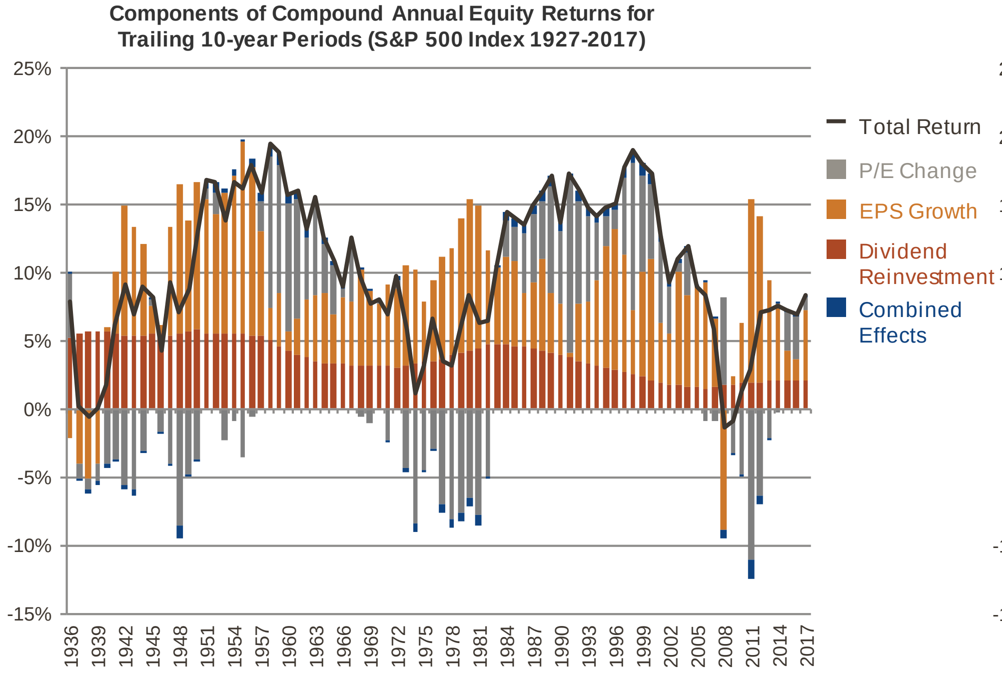
Investment Team
Portfolio Managers, Analysts, Risk Management, Traders, Client Portfolio Managers, Associates 50 Professionals
Average Industry Experience: 23 Years

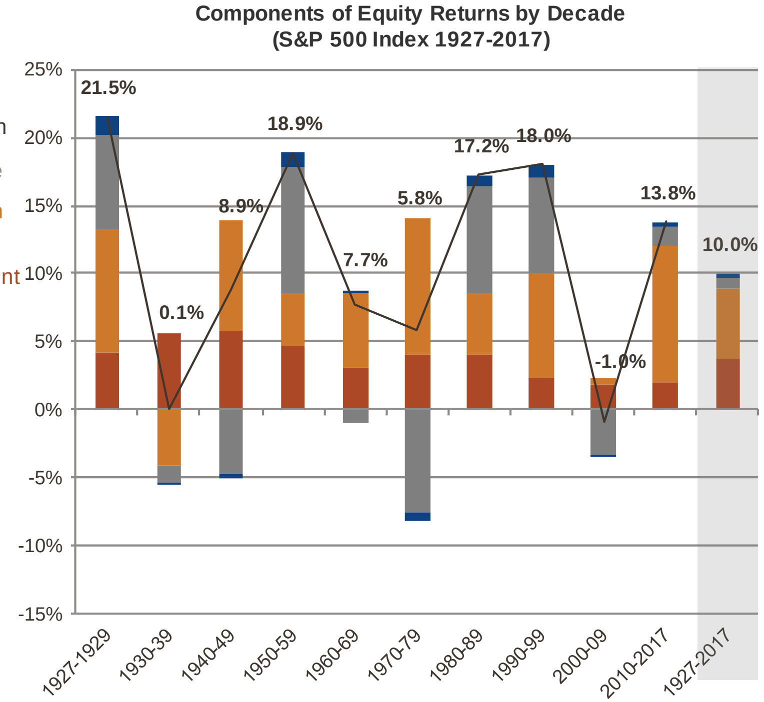
Infrastructure		
Compliance, Operations and IT 16 Professionals	**Client Relations / Marketing** 34 Professionals	**Finance and Administration** 16 Professionals
Average Industry Experience: 19 Years		

As of June 30, 2018

Agenda

The Components of Equity Returns





Long - Term History

1927 → 2017	
Earnings	5.1%
Dividends	3.8%
P/E	0.9%
Annualized Return[1]	10.0%

Looking Ahead

2018 →	
Earnings	3% - 5%
Dividends	2%
P/E	???
Expected Return	5% - 7%

Sources: Epoch Investment Partners, Inc.; Standard & Poor's.
[1] S&P 500 total return (USD)

Epoch's Distinct Approach to Investing

TRADITIONAL APPROACH	EPOCH'S APPROACH
Analysis driven by accounting metrics, primarily earnings and book value	**Analysis driven by financial metrics, primarily free cash flow**

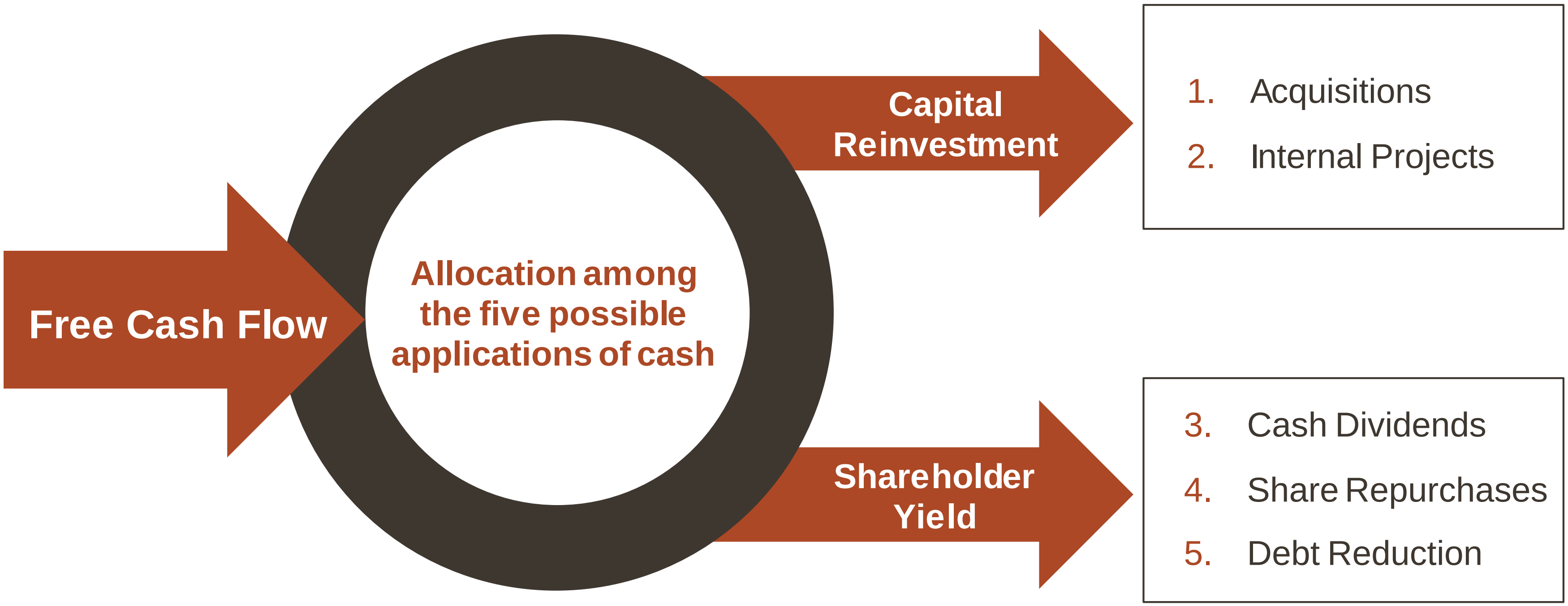
ACCOUNTING

- Distorted by accruals, easily manipulated
- No insight into skill at capital allocation
- Ignores the time value of money

FINANCE

- Free cash flow generation creates value
- Sound capital allocation drives growth in value
- Incorporates the time value of money

Companies Maximize Returns By Allocating Capital Well



Companies should reinvest capital if the expected return on invested capital is greater than the company's cost of capital. Remaining free cash flow should be returned to shareholders via shareholder yield.

Agenda

Our Firm

Our Perspective

Our Investment Process

Account Review – Global Choice

Capital Markets Outlook

Global Choice: Overview

Reporting Currency: USD

- Concentrated portfolio of 25-35 high conviction stocks
- Unconstrained approach to capture the benefits of globalization
- Managed by a team of Epoch's experienced global investors
- Attractive risk-adjusted returns
- Inception 2005

EPOCH Annualized Excess Return[1,2] *(As of June 30, 2018)*	
Excess return:	
vs. MSCI World Index (Net)	3.0%

Risk Return Metrics - Since Inception[1,2] *(As of June 30, 2018)*		
	EPOCH	**MSCI World Index (Net)**
Standard Deviation	14.1	15.0
Sharpe Ratio	0.59	0.35
		EPOCH vs. Index
Information Ratio		0.57
Alpha		3.63
Beta		0.88
R^2		0.87

1 *Excess Return is the difference between annualized return (Gross-of-Fees) since inception for Global Choice and the MSCI World Index (Net) . Inception date is September 30, 2005. Performance for the most recent quarter is preliminary and subject to change.*
2 *The risk statistics are shown as supplemental information only and supplement the Composite presentation which is located within the Disclosure section of the presentation.*

Global Choice: Investment Team

Research

Fundamental Analysis

Steven Bleiberg (34)	Glen Petraglia (18)
Bill Booth (22)	Nikolay Petrakov (19)
Michael Caputo (25)	Bill Priest (53)
Matthew Chan (19)	John Reddan (33)
Jeff Cino (18)	Stephen Rose (18)
Nigel Frankson (18)	Barney Rosen (21)
Kevin Hebner (23)	Stephen Salzone (14)
Justin Howell (15)	David Siino (20)
Wei Huang (17)	Tim Sledge (24)
Michael Jin (24)	Jeffrey Smith (27)
Josepha Kaufman (23)	Michael Takata (32)
Wayne Lin (17)	John Tobin (37)
Gary Low (19)	Jérôme Van Der Ghinst (15)
John Morgan (24)	Kera Van Valen (17)
Alex Orozco (19)	Tim Wengerd (10)
David Pearl (34)	Chris Wolters (28)

Client Portfolio Managers

Andrea Tasker Glogoff (23)	Rick Vandale (33)
Tamzin Manning (13)	Richard Watt (36)
John Miller (30)	Scott Weisenberger (35)

Quantitative Analysis & Risk Management

Mike Welhoelter (32)	Dave Pratter (13)
Harry Gregory (22)	Lilian Quah (15)
Lin Lin (14)	Jason Root (21)

Macro Analysis

Investment Policy Group

Bill Priest (53)	John Morgan (24)
David Pearl (34)	John Reddan (33)
Steven Bleiberg (34)	John Tobin (37)
Bill Booth (22)	Richard Watt (36)
Michael Caputo (25)	Mike Welhoelter (32)
Kevin Hebner (23)	

Trading

Mark Strauss (32)	Doug Van Gorp (20)

Global Choice Team

Bill Priest
Bill Booth
David Pearl
Mike Welhoelter
Josepha Kaufman
John Reddan
Michael Takata
Richard Watt

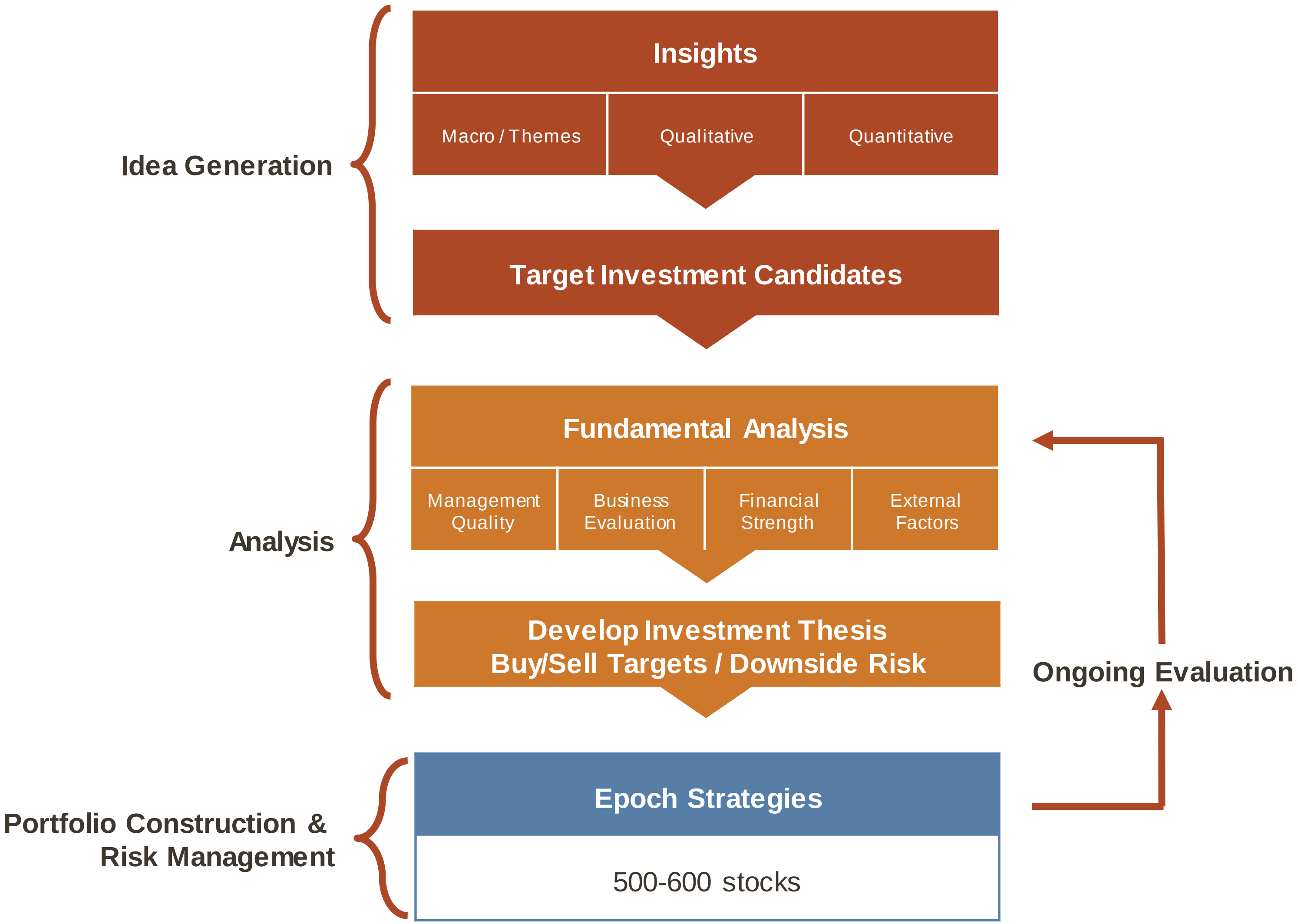
Portfolio Managers

Bill Priest
Bill Booth
David Pearl
Mike Welhoelter

As of June 30, 2018
Numbers in parentheses denote years of experience.

EPOCH

Epoch: Investment Process



Global Choice: Investment Process

Epoch Firm Wide Holdings

500 - 600 stocks

Liquidity Filters

150 – 200 stocks

Stock Ideas

Strategy Research Meetings	Investment Analyst Reviews

Investment Themes

Investment Policy Group

Global Choice Team

Weekly Global Choice Meetings

Investment Process: Fundamental Bottom-Up Analysis

Portfolio Holding Example: Safran

A global aerospace and defense company

Products

SAFRAN
AEROSPACE · DEFENCE · SECURITY

Engines

Landing Gear

Strong Revenue Generation

€18B in sales

- Propulsion (54%)
- Equipment (28%)
- Defense & Security (18%)

Sustainable Cash Flow

- **€2.8B** in operating cash flow
- Attractive business model with sustainable competitive advantages
  - Technology is a key barrier to entry
  - Supply agreements create natural monopolies and duopolies
  - Long-life annuity-like aftermarket business
- Secular growth trends in commercial aerospace
  - Developed market fleet renewal and upgrade
  - Emerging market travel and tourism

Disciplined Capital Allocation

Reinvest for Capital Growth

Current investment plan:

- Capital expenditures: €0.8B
  - Production capacity expansion
- Research & Development: €1.4B
  - New engine programs
  - More electrical aircraft

Return Capital to Shareholders

Policies for announced shareholder yield:

- Dividends: €0.5B
- Current focus is on investing in and executing on new engine programs to secure a strong position on the next generation of commercial aircraft

Source: Epoch Investment Partners, Inc., and Safran company reports; 2015. Information about specific companies or securities including whether they are profitable or not, is provided as a means of illustrating our investment thesis. Please see our disclosure located on the cover page of this presentation

Investment Process: Portfolio Construction and Risk Management

Portfolio Construction – Risk Control

- Position size and inverse risk weighting
- Risk models
  - Factor Exposures
  - Macro Exposures

Portfolio Holdings

Global Choice (25-35 stocks)

Ongoing Stock Evaluation

- Price target reached
- Change in investment thesis
- Portfolio rebalancing: aggregation and efficiency measures

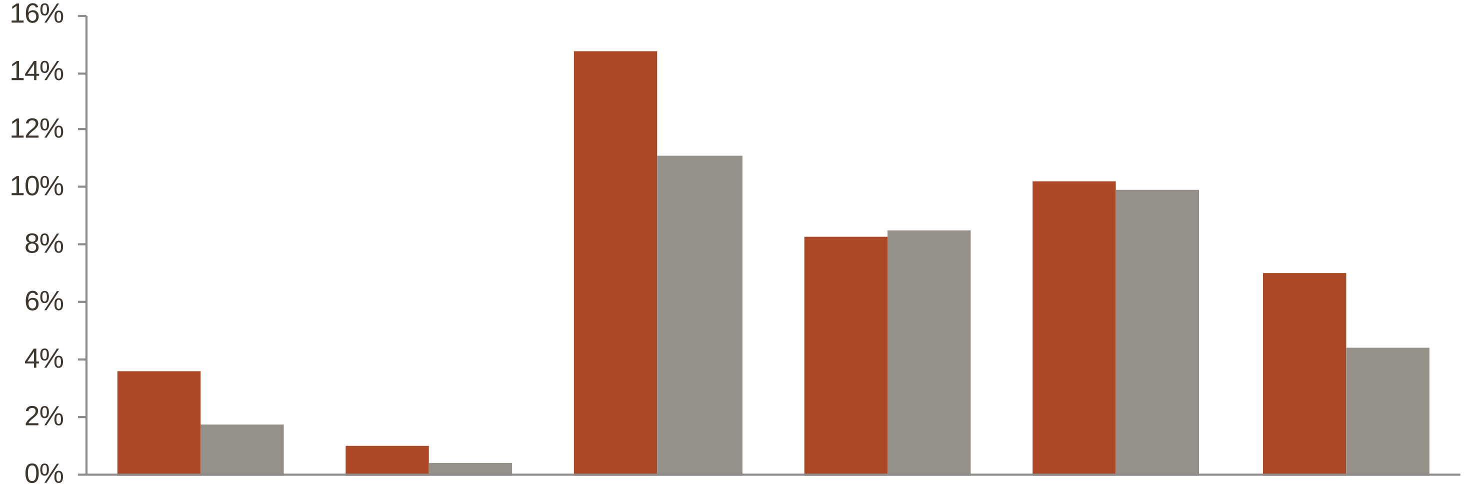
Page Intentionally Left Blank

Agenda

- Our Firm
- Our Perspective
- Our Investment Process
- Account Review – Global Choice
- Capital Markets Outlook

Performance: As of June 30, 2018

North Dakota State Investment Board
Market Value: $414,174,433



	QTD	YTD	1 Year	3 Year	5 Year	Inception to Date (7/8/2007)
North Dakota State Investment Board (Gross)	3.6	1.0	14.7	8.3	10.2	7.0
MSCI World (Net)	1.7	0.4	11.1	8.5	9.9	4.4

	2017	2016	2015	2014	2013	2012	2011	2010	2009	2008	2007[1]
North Dakota State Investment Board (Gross)	31.2	-0.6	0.4	3.5	33.2	15.1	-1.3	7.5	37.5	-29.7	-1.8
MSCI World (Net)	22.4	7.5	-0.9	4.9	26.7	15.8	-5.5	11.8	30.0	-40.7	-1.9

[1]Data represents a partial year from 7/08/07 – 12/31/07.
Performance for the most recent quarter is preliminary and subject to change. Returns are annualized for periods greater than one year. Periods less than one year are cumulative, unless otherwise noted. Additional information regarding policies for calculating and reporting returns is available upon request. Past performance is no guarantee of future results.

Performance Attribution: One Year Ending June 30, 2018

North Dakota State Investment Board

Sectors	Account Average Weight	Account Return (%)	MSCI World Average Weight	MSCI World Return (%)	Attribution Effects Allocation Effect	Attribution Effects Stock Selection	Attribution Effects Total Effect
Consumer Discretionary	6.5	5.4	12.4	17.9	(0.3)	(0.8)	(1.1)
Consumer Staples	5.1	15.3	8.8	(1.1)	0.4	0.3	0.7
Energy	6.5	36.4	6.2	23.9	0.2	1.1	1.3
Financials	19.9	6.5	17.9	4.5	(0.4)	0.3	(0.0)
Health Care	14.2	7.0	12.0	4.8	(0.1)	0.2	0.1
Industrials	12.2	16.8	11.4	6.7	0.1	1.0	1.1
Information Technology	27.0	28.0	17.1	28.5	1.5	0.5	1.9
Materials	4.8	(7.3)	5.0	14.2	(0.4)	(0.3)	(0.7)
Real Estate	--	--	3.1	5.5	0.2	--	0.2
Telecommunication Services	--	--	2.7	(3.5)	0.4	--	0.4
Utilities	1.2	13.1	3.0	3.1	0.1	0.2	0.3
[Cash]	2.6	0.8	--	--	(0.3)	--	(0.3)
[Unassigned]	--	--	0.3	11.4	(0.0)	--	(0.0)
Total					**1.3**	**2.5**	**3.7**

Source: FactSet Research Systems, Inc.; MSCI, Inc. Totals may not add due to rounding.

Performance Attribution: One Year Ending June 30, 2018

North Dakota State Investment Board

Country	Account Average Weight	Account Return (%)	MSCI World Average Weight	MSCI World Return (%)	Attribution Effects Allocation Effect (Local)	Attribution Effects Stock Selection (Local)	Attribution Effects Total Effect (Local)	Attribution Effects Total Currency Effect	Attribution Effects Total Effect
Australia	0.0	0.0	2.5	8.7	(0.0)	0.0	(0.0)	0.1	0.1
Austria	0.0	0.0	0.1	8.9	(0.0)	0.0	(0.0)	(0.0)	(0.0)
Belgium	1.6	5.1	0.4	1.7	(0.1)	(0.1)	(0.3)	0.1	(0.2)
Brazil	0.2	0.2	0.0	0.0	(0.1)	0.0	(0.1)	0.1	(0.0)
Canada	0.0	0.0	3.5	9.1	0.0	0.0	0.0	0.0	0.0
China	0.0	0.0	0.0	(22.5)	(0.0)	0.0	(0.0)	(0.0)	(0.0)
Denmark	0.0	0.0	0.7	0.9	0.1	0.0	0.1	(0.0)	0.1
Finland	0.0	0.0	0.4	10.4	0.0	0.0	0.0	(0.0)	(0.0)
France	8.1	19.5	4.0	9.8	(0.0)	0.7	0.7	(0.0)	0.7
Germany	2.7	(10.8)	3.6	2.5	0.1	(0.4)	(0.3)	(0.0)	(0.3)
Hong Kong	1.3	3.8	1.3	9.4	(0.1)	0.2	0.2	0.0	0.2
Ireland	0.0	0.0	0.2	5.3	0.0	0.0	0.0	(0.0)	0.0
Israel	0.0	0.0	0.2	(4.6)	0.0	0.0	0.0	0.0	0.0
Italy	0.0	0.0	0.9	8.4	0.0	0.0	0.0	(0.0)	0.0
Japan	1.1	13.0	8.9	10.5	0.2	0.1	0.3	(0.0)	0.3
Netherlands	0.0	0.0	1.3	9.2	0.0	0.0	0.0	(0.0)	0.0
New Zealand	0.0	0.0	0.1	1.7	(0.0)	0.0	(0.0)	0.0	0.0
Norway	0.0	0.0	0.3	27.1	(0.0)	0.0	(0.0)	(0.0)	(0.0)
Portugal	0.0	0.0	0.1	15.7	(0.0)	0.0	(0.0)	(0.0)	(0.0)
Singapore	0.0	0.0	0.5	7.9	0.0	0.0	0.0	(0.0)	0.0
Spain	0.0	0.0	1.2	(3.6)	0.2	0.0	0.2	(0.0)	0.2
Sweden	0.0	0.0	1.0	(4.6)	0.1	0.0	0.1	0.1	0.2
Switzerland	0.6	1.2	3.0	(3.4)	0.3	(0.1)	0.2	0.1	0.3
United Kingdom	3.0	(8.9)	6.5	10.0	0.3	(0.3)	(0.0)	(0.2)	(0.2)
United States	78.8	16.5	59.4	13.9	0.6	2.4	3.1	(0.2)	2.9
[Cash]	2.6	0.8	0.0	0.0	(0.3)	0.0	(0.3)	0.0	(0.3)
Total					**1.3**	**2.6**	**3.8**	**(0.1)**	**3.7**

Source: FactSet Research Systems, Inc.; MSCI, Inc. Totals may not add due to rounding.

Top Five Contributors and Bottom Five Detractors & Top Ten New and Closed Positions: One Year Ending June 30, 2018

North Dakota State Investment Board

Top Five Contributors	Contribution to Portfolio Return (%)
Microsoft Corporation	1.7
PTC Inc.	1.6
Visa Inc. Class A	1.4
Occidental Petroleum Corporation	1.2
AbbVie, Inc.	1.1

Bottom Five Detractors	Contribution to Portfolio Return (%)
Allergan plc	-1.3
Johnson Controls International plc	-0.6
Glencore plc	-0.5
Universal Display Corporation	-0.4
Liberty Global Plc Class A	-0.3

Top Ten New Positions
DowDuPont Inc.
Phillips 66
Martin Marietta Materials, Inc.
Airbus SE
Occidental Petroleum Corporation
Kroger Co.
CME Group Inc. Class A
Glencore plc
AIA Group Limited
Merck & Co., Inc.

Top Ten Closed Positions
Allergan plc
Johnson Controls International plc
Walt Disney Company
Anheuser-Busch InBev SA/NV
Apple Inc.
Coca-Cola European Partners Plc
NextEra Energy, Inc.
Unilever PLC
PayPal Holdings Inc
DENTSPLY SIRONA, Inc.

Source: FactSet Research Systems, Inc. Top ten new and top ten closed positions are sorted in descending order from the largest position weight.

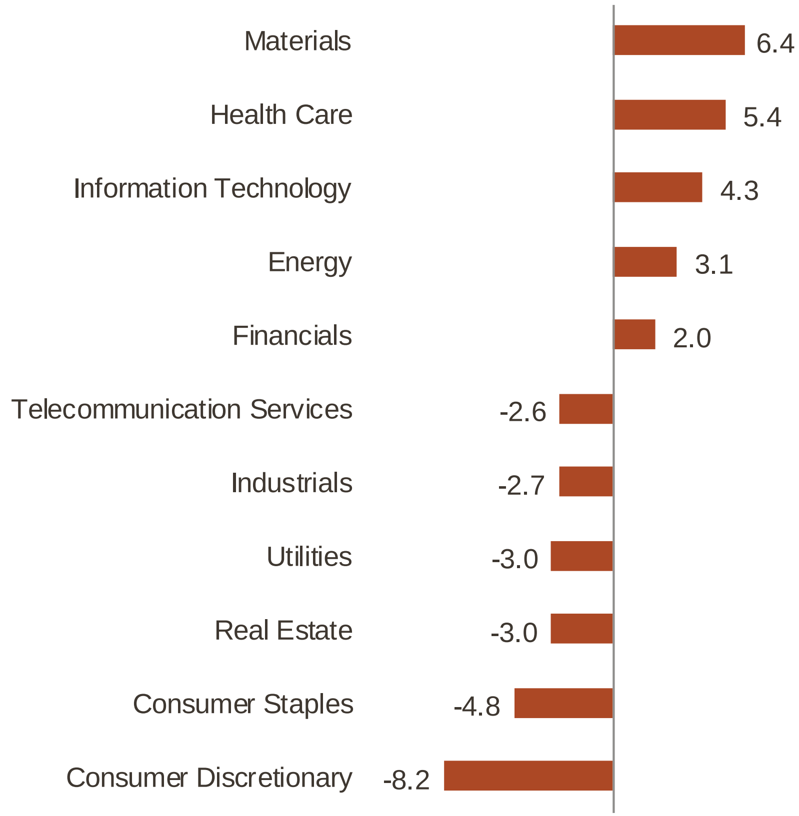
Sector Allocation & Characteristics: As of June 30, 2018

North Dakota State Investment Board

Sector	Portfolio Weight (%)	MSCI World Weight (%)
Consumer Discretionary	4.5	12.7
Consumer Staples	3.4	8.3
Energy	9.9	6.8
Financials	18.8	16.8
Health Care	17.5	12.1
Industrials	8.4	11.1
Information Technology	22.8	18.5
Materials	11.3	4.9
Real Estate	--	3.0
Telecommunication Services	--	2.6
Utilities	--	3.0
Cash	3.5	--

Characteristics	Portfolio	MSCI World
Dividend Yield (%)	1.8	2.4
Enterprise Value to EBITDA (x)	14.7	11.9
Weighted Average Market Cap ($M)	140,022	148,740
Weighted Median Market Cap ($M)	68,928	59,250
Predicted Beta	1.07	--
12 Month Turnover	78%	--
Number of Equity Positions	33	1,643

Sector Weights Relative to Benchmark



Source: FactSet Research Systems; MSCI, Inc. The data is unaudited and may change at any time. The data is shown for informational purposes only and is not indicative of future portfolio characteristics or returns. Totals may not add due to rounding and/or unassigned securities.

Top Ten Holdings & Countries: As of June 30, 2018

North Dakota State Investment Board

Top Ten Holdings	Portfolio Weight (%)
DowDuPont Inc.	4.8
Phillips 66	4.3
Visa Inc. Class A	4.1
Microsoft Corporation	4.0
UnitedHealth Group Incorporated	3.9
Martin Marietta Materials, Inc.	3.6
Airbus SE	3.6
Occidental Petroleum Corporation	3.6
JPMorgan Chase & Co.	3.6
Kroger Co.	3.4
Total	**39.0**

Top Ten Countries	Portfolio Weight (%)
United States	76.4
France	8.9
United Kingdom	5.5
Germany	2.9
Hong Kong	2.8
Total	**96.5**

Source: FactSet Research Systems, Inc. Totals may not add due to rounding.

Investment Process: Portfolio Themes

The global growth environment, while moderating from high levels, remains strong and widespread although increased trade tensions merit monitoring. We remain invested in more resilient developed markets and in industries underpinned by structural growth.

- Technology companies that provide productivity enhancing solutions for corporates and also benefit from the proliferation of smart devices
  - Applied Materials, Microsoft, Universal Display

- Synchronized global growth, improving capital discipline and company specific attributes underpin a more positive outlook for select companies in the energy and materials sectors
  - Occidental Petroleum, DowDuPont, Phillips 66

- Financial companies that have improved their capital position and, as a result, are better positioned to return a greater share of free cash flow to shareholders
  - Morgan Stanley, JPMorgan, CME Group

- Global Champions domiciled outside of the U.S.
  - Bayer, Safran, AstraZeneca

As of June 30, 2018

Global Choice Portfolio Positioning: As of June 30, 2018

Sector		Security	Domicile	Portfolio Weight (%)
Information Technology	**22.8%**	Visa Inc. Class A	United States	4.1
		Microsoft Corporation	United States	4.0
		Applied Materials, Inc.	United States	2.9
		Universal Display Corporation	United States	2.6
		Broadcom Inc.	United States	2.5
		PTC Inc.	United States	2.4
		Marvell Technology Group Ltd.	United States	2.2
		Alphabet Inc. Class C	United States	2.1
Financials	**18.7%**	JPMorgan Chase & Co.	United States	3.6
		Willis Towers Watson Public Limited Company	United States	3.0
		CME Group Inc. Class A	United States	2.9
		AIA Group Limited	Hong Kong	2.8
		Morgan Stanley	United States	2.6
		AXA SA	France	2.0
		Chubb Limited	United States	1.8
Health Care	**17.5%**	UnitedHealth Group Incorporated	United States	3.9
		Danaher Corporation	United States	3.4
		Bayer AG	Germany	2.9
		Merck & Co., Inc.	United States	2.7
		AstraZeneca PLC	United Kingdom	2.6
		Cerner Corporation	United States	2.0
Materials	**11.3%**	DowDuPont Inc.	United States	4.8
		Martin Marietta Materials, Inc.	United States	3.6
		Glencore plc	United Kingdom	2.9
Energy	**9.8%**	Phillips 66	United States	4.3
		Occidental Petroleum Corporation	United States	3.6
		Core Laboratories NV	United States	2.0
Industrials	**8.4%**	Airbus SE	France	3.6
		Safran S.A.	France	3.3
		United Technologies Corporation	United States	1.5
Consumer Discretionary	**4.4%**	Home Depot, Inc.	United States	2.7
		Mohawk Industries, Inc.	United States	1.8
Consumer Staples	**3.4%**	Kroger Co.	United States	3.4
		Cash		3.6
		Total		**100.0**

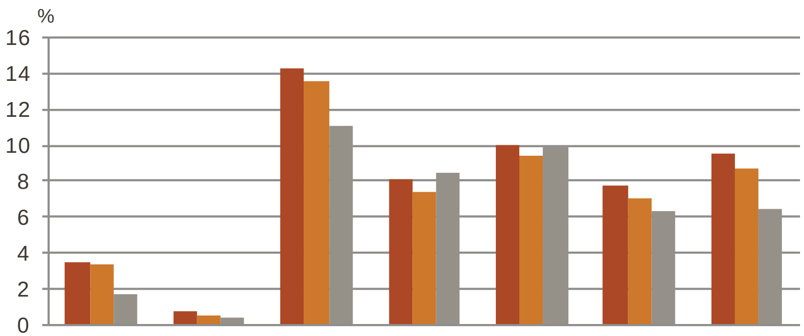
Source: Epoch Investment Partners, Inc. The data shown above is of a representative account and such data may vary for each client in the strategy due to market conditions, client guidelines and diversity of portfolio holdings. The data is unaudited and may change at any time. The data is supplemental to the composite presentation, is shown for informational purposes only, and is not indicative of future portfolio characteristics or returns.

Global Choice: Composite Results

As of June 30, 2018

Reporting Currency: USD

Returns



	QTR	YTD	1 Year	3 Year	5 Year	10 Year	Annualized Since Inception[1]
EPOCH (Gross)	3.5	0.8	14.3	8.1	10.0	7.7	9.5
EPOCH (Net)	3.4	0.5	13.6	7.4	9.4	7.0	8.7
MSCI World Index (Net)	1.7	0.4	11.1	8.5	9.9	6.3	6.4

Risk Return Metrics - Since Inception[1,2]

	EPOCH	MSCI World Index (Net)
Standard Deviation	14.1	15.0
Sharpe Ratio	0.59	0.35
		EPOCH vs. Index
Information Ratio		0.57
Alpha		3.63
Beta		0.88
R^2		0.87

	2017	2016	2015	2014	2013	2012	2011	2010	2009	2008	2007	2006	2005[3]
EPOCH Gross Return	30.8	-0.6	0.1	3.2	32.5	15.4	-0.1	6.8	37.4	-35.6	17.2	30.0	6.4
EPOCH Net Return	30.0	-1.1	-0.5	2.6	31.8	14.9	-0.6	6.3	36.2	-36.3	16.2	28.9	6.1
MSCI World Index (Net)	22.4	7.5	-0.9	4.9	26.7	15.8	-5.5	11.8	30.0	-40.7	9.0	20.1	3.1

1 *Inception date is September 30, 2005. Performance for the most recent quarter is preliminary and subject to change.*
2 *The risk statistics are shown as supplemental information only and supplement the Composite presentation which is located within the Disclosure section of the presentation.*
3 *Data represents a partial year from 9/30/05-12/31/05.*
Past performance is no guarantee of future results.

Agenda

Our Firm

Our Perspective

Our Investment Process

Account Review – Global Choice

Capital Markets Outlook

U.S.: Strengths, Weaknesses, Opportunities and Threats

STRENGTHS

- **Culture**: Commitment to innovation, free-market capitalism, allowing consumers to determine winners & losers.
- **Tech**: The U.S. is easily the world leader (except-FinTech and Robotics).
- **Economic cycle**: Turbo-charged by triple-whammy of: strong global recovery; fiscal stimulus (TCJA); and loose financial conditions (including negative real policy rates).
- **Earnings growth & buybacks**: 19% this year (7 ppts reflecting TCJA), with buybacks historical high of $800bn.
- **Deregulation**: A key focus of this administration (e.g., banking, energy), often under-the-radar.

WEAKNESSES

- **Fiscal deficit and other imbalances**: 2019's budget deficit is likely to be its largest ever (as % of GDP), outside of recessions and wartime. One reasons is that entitlement reform is challenging, the third rail of U.S. politics. Further, the trade balance is approaching its historical worse level, as is the personal savings rate.
- **Valuations**: Above historical averages.

OPPORTUNITIES

- **New Tech**: The pace of innovation is accelerating; the US should lead the march (vs most of China's 2025 ambitions), with a very positive impact on profitability.
- **Fast-growing emerging markets:** Opportunities for U.S. MNCs and exports of goods and services.

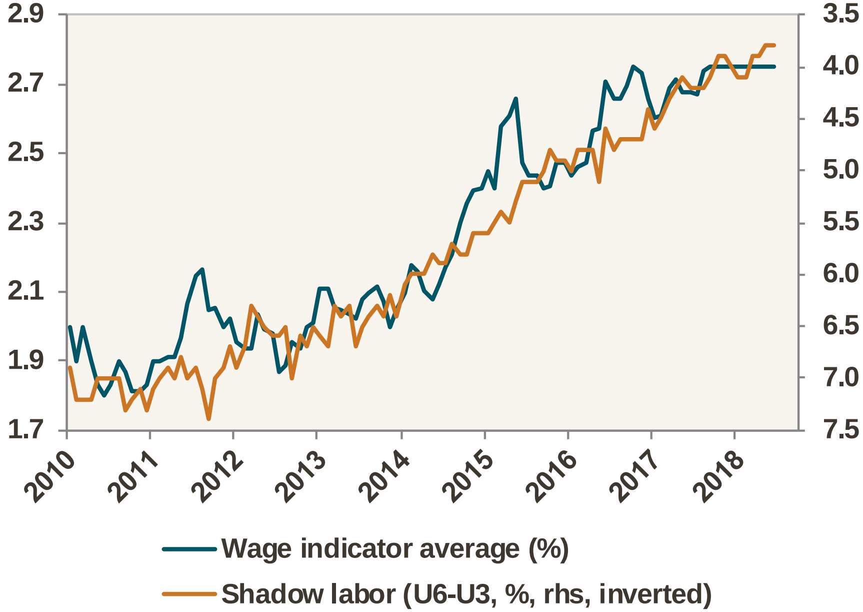
THREATS

- **Trump and Trade**: Key issues are market access, IP and China's state-driven economic model. China to retaliate.
- **President Xi and China 2025:** Aims to be a strategic competitor. China is challenging the U.S.'s lead in sectors such as AI, autonomous vehicles, electric vehicles & batteries, aviation, robotics, renewable energy, and bio-tech. Already leagues ahead in FinTech.
- **The risk of higher interest rates**: The looming trifecta of QT, soaring fiscal deficits and the wall of maturities.

Source: Epoch Investment Partners

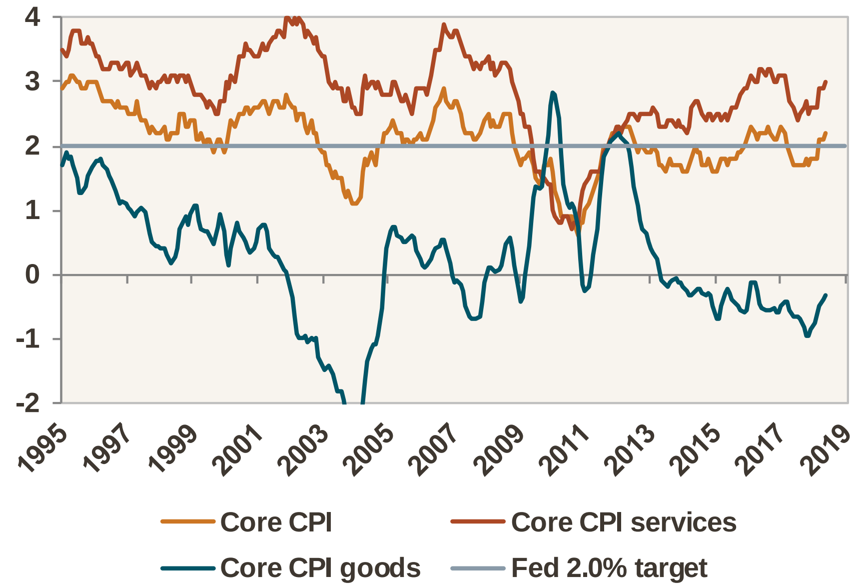
U.S. Employment is Now in its 8th Year of Solid Growth

Very tight labor market: Suggests higher wage growth



Source: Bloomberg, Epoch Investment Partners
As of May 31, 2018
Note: U6 includes U3 + those only marginally attached to labor force (not looking, but would if labor market improved) + those working part-time for economic reasons. The "Wage indicator average" is the mean of four series: Atlanta Fed, NY Fed Median, AHE, ECI.

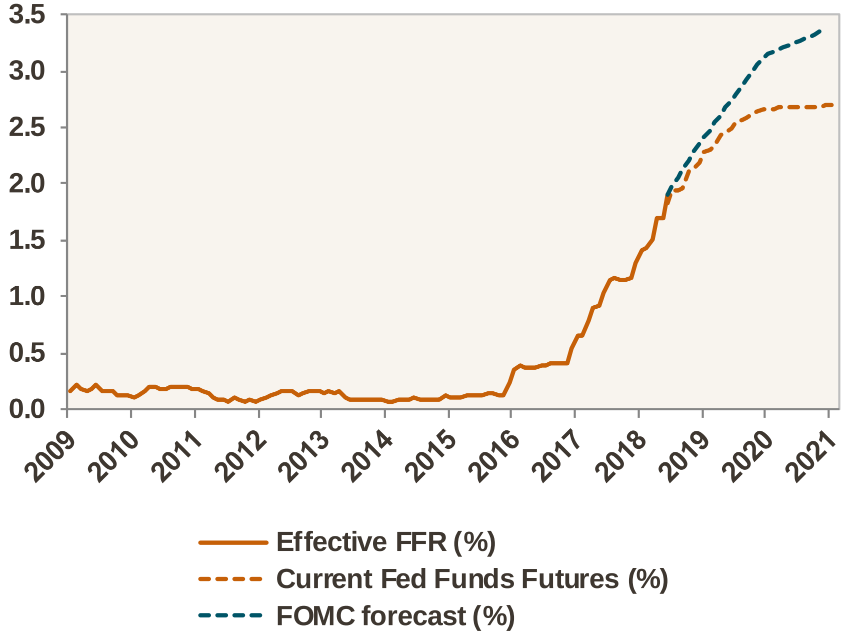
As output gap closes, inflation begins to tick up, typical of a late cycle



Source: Bloomberg, Epoch Investment Partners
As of May 31, 2018

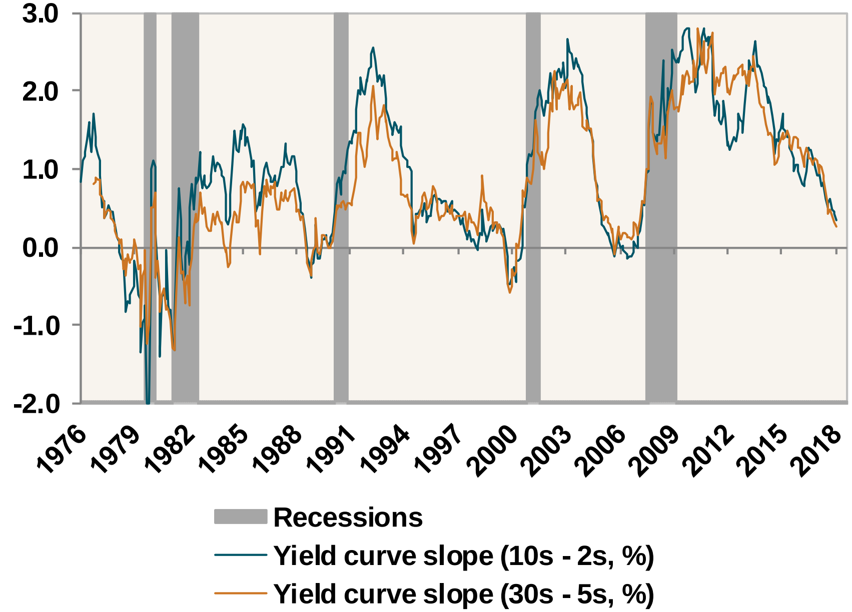
Tight Labor Means a Hawkish Fed: And an Inverted Yield Curve?

Fed projects five hikes by end-2019, with a few more to come in 2020



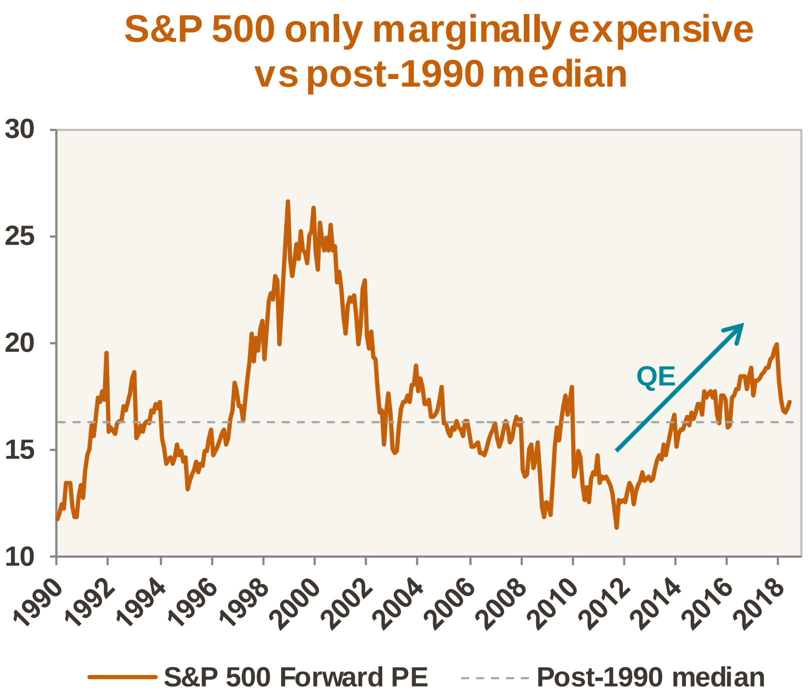
Source: FRB, Bloomberg, Epoch Investment Partners
As of May 31, 2018

This time is different? If the yield curve inverts, a recession inevitably follows

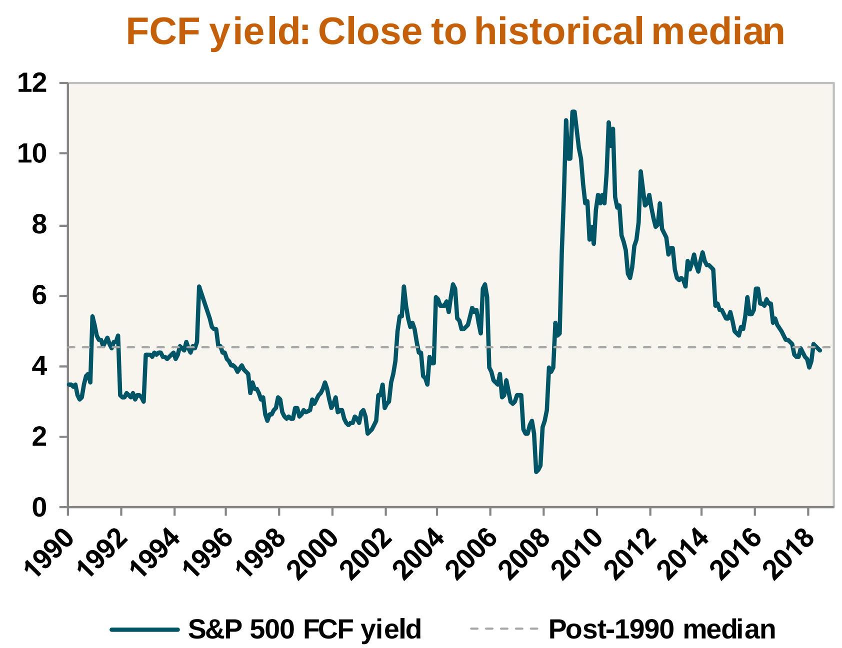


Source: Bloomberg, Epoch Investment Partners
As of May 31, 2018

U.S. Equity Multiples: Unlikely to Improve Given Transition to QT



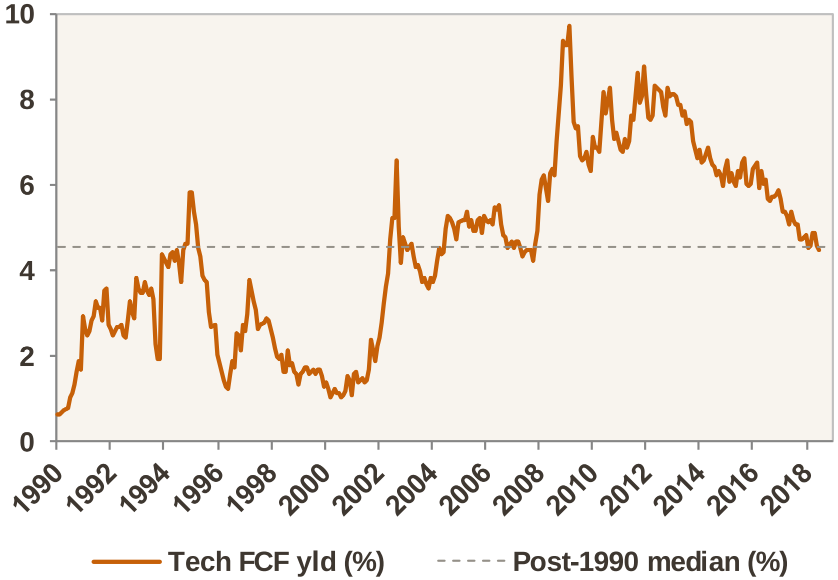
Source: Bloomberg, Epoch Investment Partners
As of May 31, 2018



Source: Bloomberg, Epoch Investment Partners
As of May 31, 2018

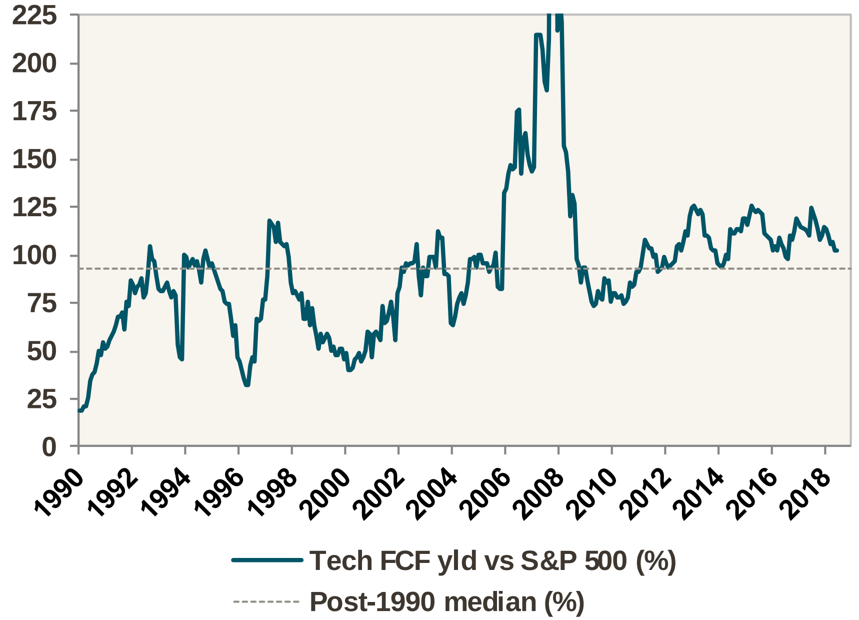
U.S. Tech: The Sector has Outperformed for Eons, but Valuation is In-line with Historical Norm as FCF Growth has Kept Pace

Tech isn't expensive vs. history; trading close to its post-1990 median FCF yield



Source: Bloomberg, Epoch Investment Partners
As of May 31, 2018

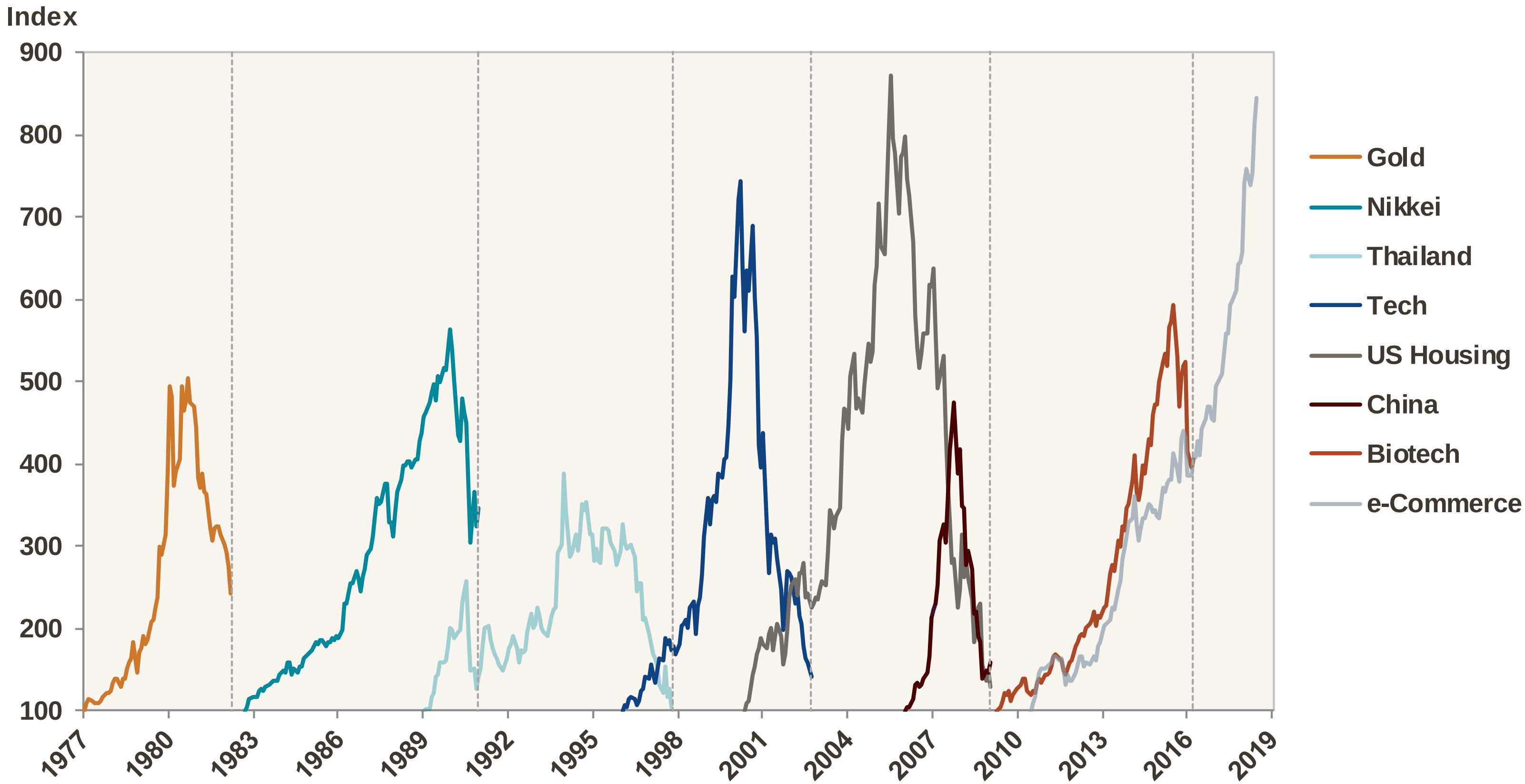
Tech FCF yield vs S&P 500: Trading just above its historical median



Source: Bloomberg, Epoch Investment Partners
As of May 31, 2018

E-Commerce is the 2nd Largest Bubble of the Last Four Decades

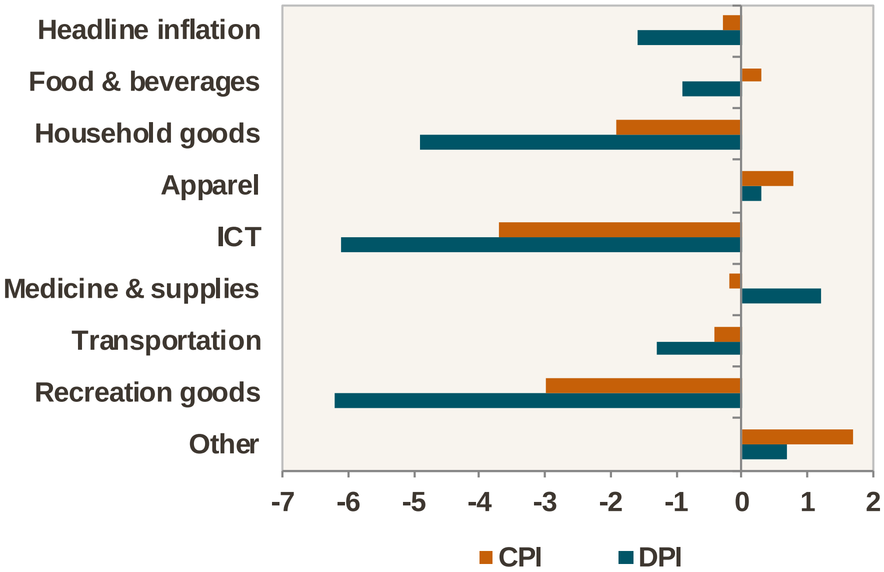
Facebook (25k employees) market cap > MSCI India (1.3 bn people)



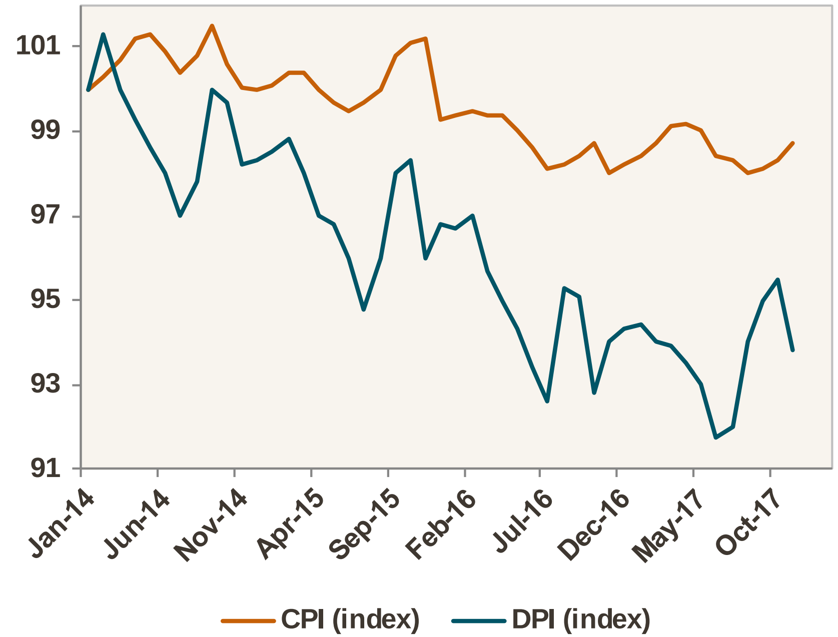
Source: Bloomberg, DoubleLine, Epoch Investment Partners
As of May 31, 2018

Tech is the New Macro: DPI vs CPI

Lower inflation online than in the CPI; by 1.3 ppts per year—for the same categories



The DPI is markedly lower than the CPI



- The entry of new products implies the CPI overstates true inflation by an additional 1.5 to 2.5 ppts per year.
- Combining the two effects suggests the DPI inflation rate is more than 3 ppts per year lower than the CPI inflation rate for the same categories from 2014–2017.

Source for both charts: "Internet Rising, Prices Falling: Measuring Inflation in a World of E-Commerce," American Economic Association
As of May 2018

Tech is the New Macro: Implications of a Capital-Light World

Return on Equity Components

$$\text{ROE} = \text{Profit Margin} \times \text{Asset Utilization} \times \text{Leverage}$$

$$\text{ROE} = \left[\frac{\textit{Profits}}{\textit{Sales}}\right] \times \left[\frac{\textit{Sales}}{\textit{Assets}}\right] \times \left[\frac{\textit{Assets}}{\textit{Equity}}\right]$$

$$\text{ROE} = \frac{\textit{Profits}}{\textit{Equity}}$$

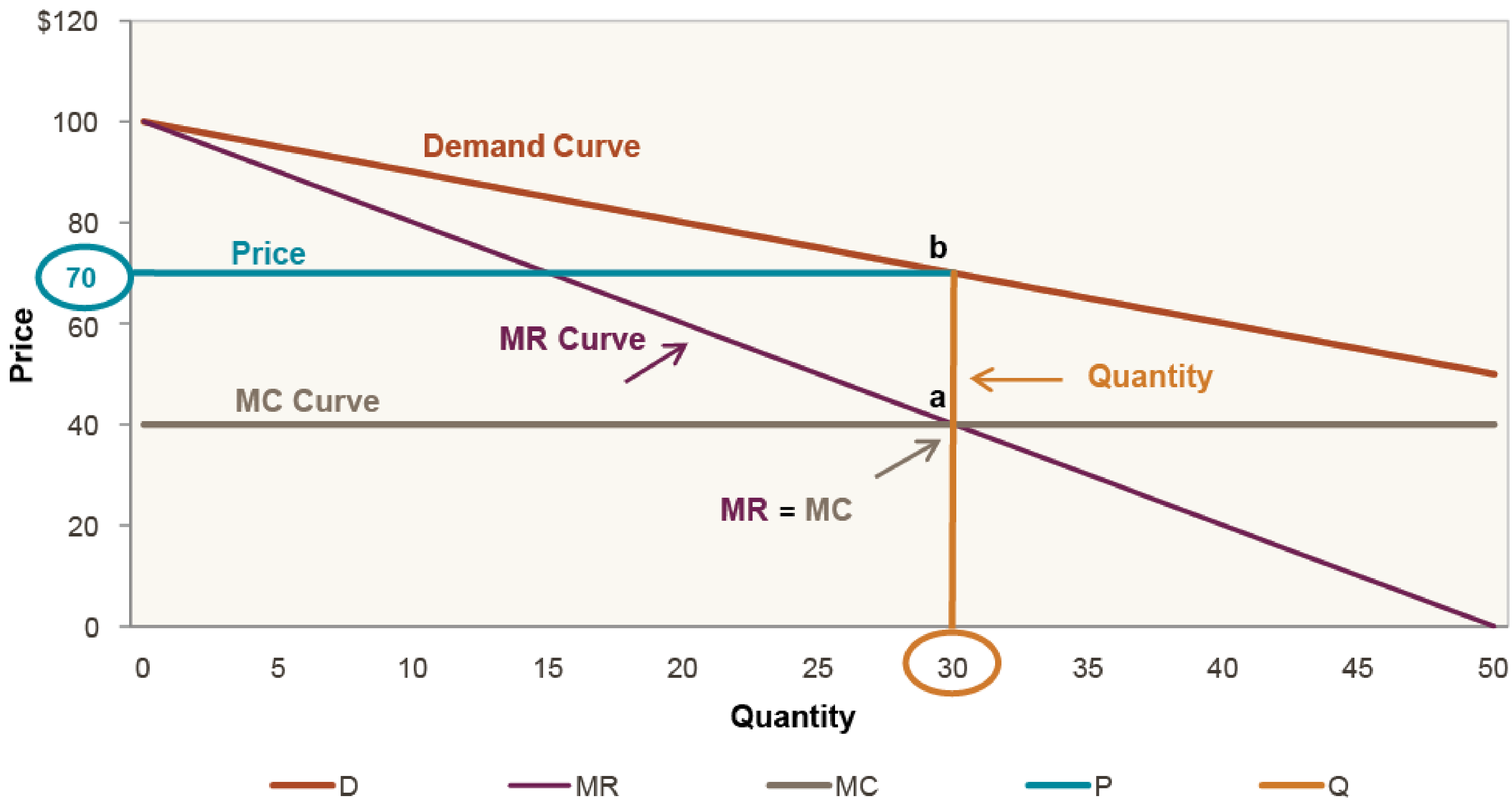
Payout ratios to rise with less need for equity to support decreasing asset base requirement

Technology will improve all three components

Source: Epoch Investment Partners

The Impact of Technology on Prices

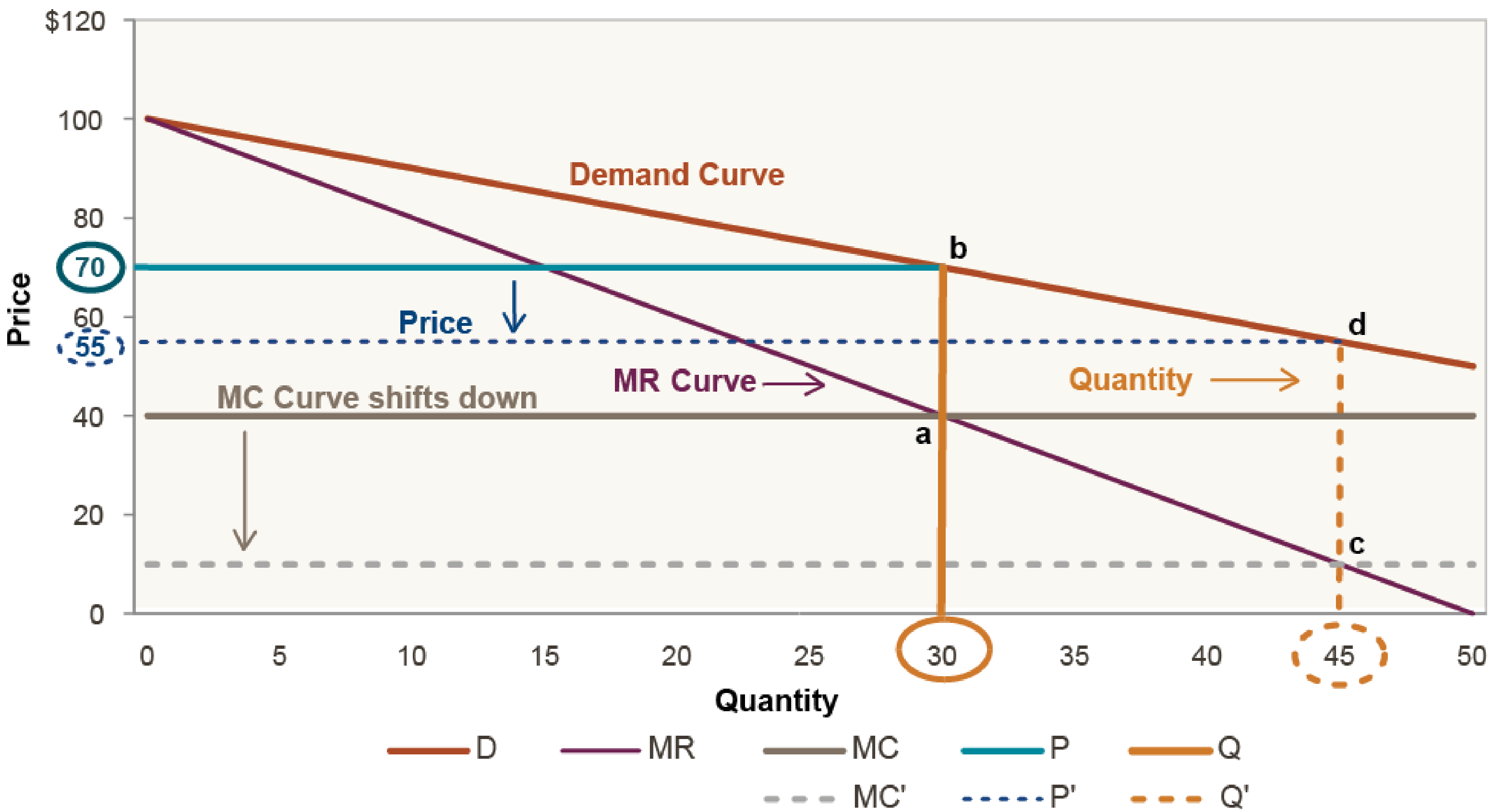
Firms set quantity where MR = MC (point "a") and then set price by moving vertically up to the Demand curve (point "b")



Source: Epoch Investment Partners

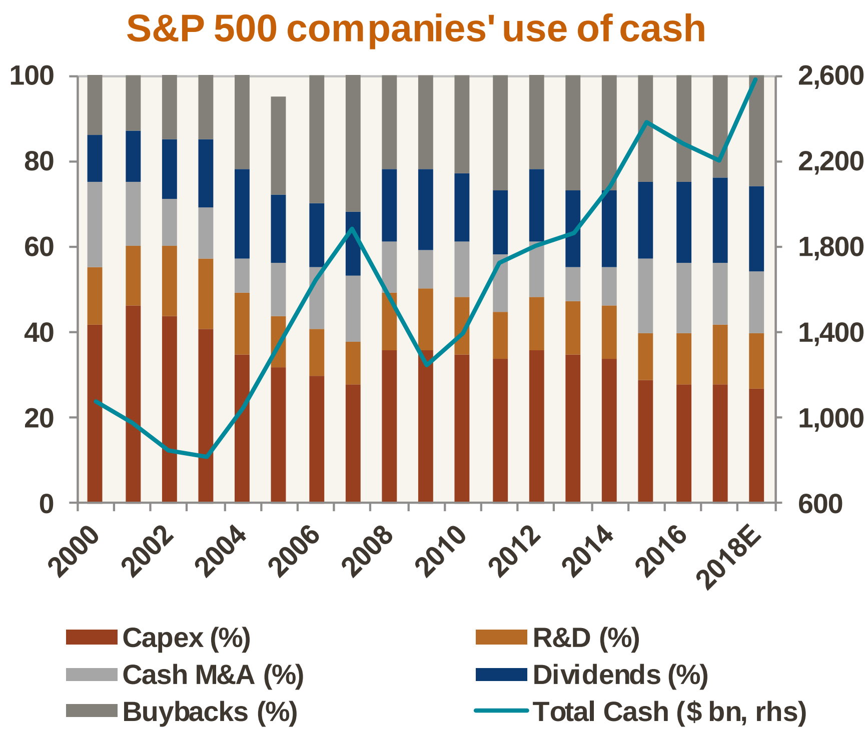
Technology Reduces Frictions, Pushing Marginal Costs Lower: This is Win-Win, Making Both Consumers and Firms Better Off

Tech lowers MC so that it now interests MR at point "c", which is where the firm sets quantity. The new price is set by moving vertically up to the Demand curve (point "d").



Source: Epoch Investment Partners

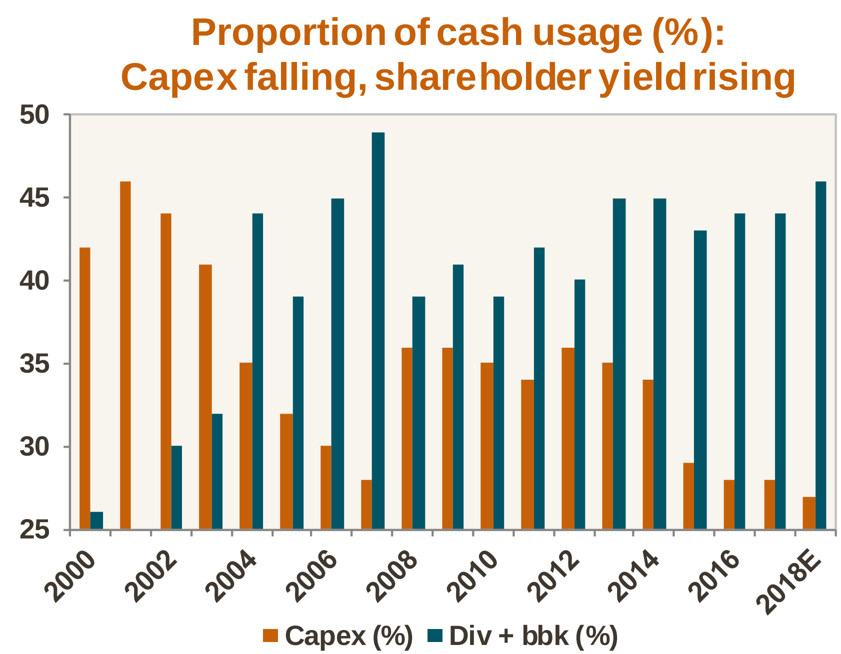
In a Capital-Light World, Companies Return a Higher Proportion of Cash to Shareholders: 2018 to be a Record Year for Buybacks



Source: Goldman Sachs

Dividends plus buybacks: Accounted for 26% of cash usage in 2000, surging to 46% in 2018.

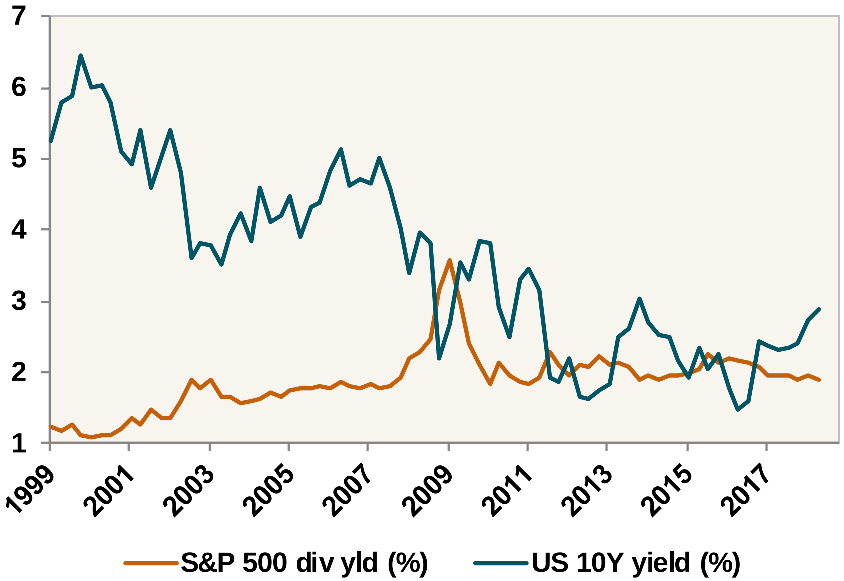
Capex: Represented 42 – 44% of cash usage in the early-2000s, vs. only 27 - 28% now.



Source: Goldman Sachs

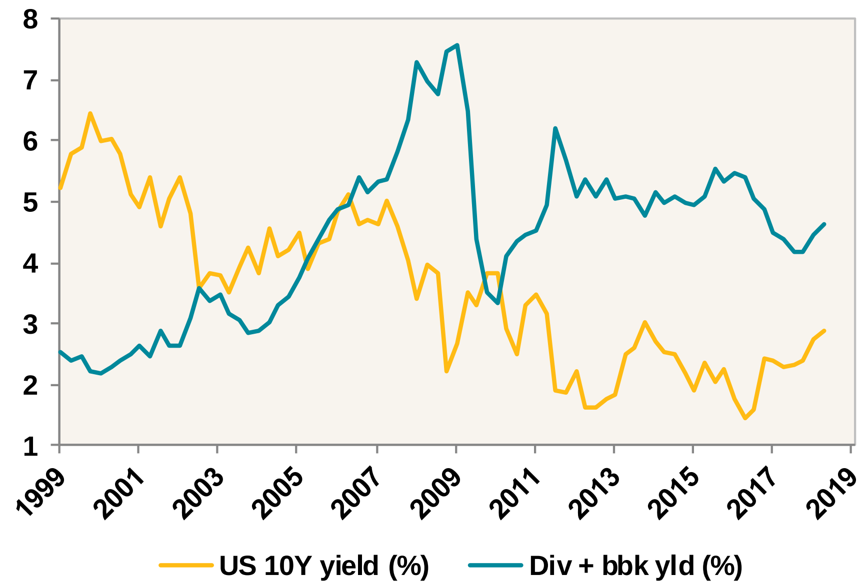
The Combined Cash Yield is Superior to that Available from Bonds

Dividend yield: Roughly 100bp less than the 10Y bond yield



Source: Bloomberg, Epoch Investment Partners
As of May 31, 2018

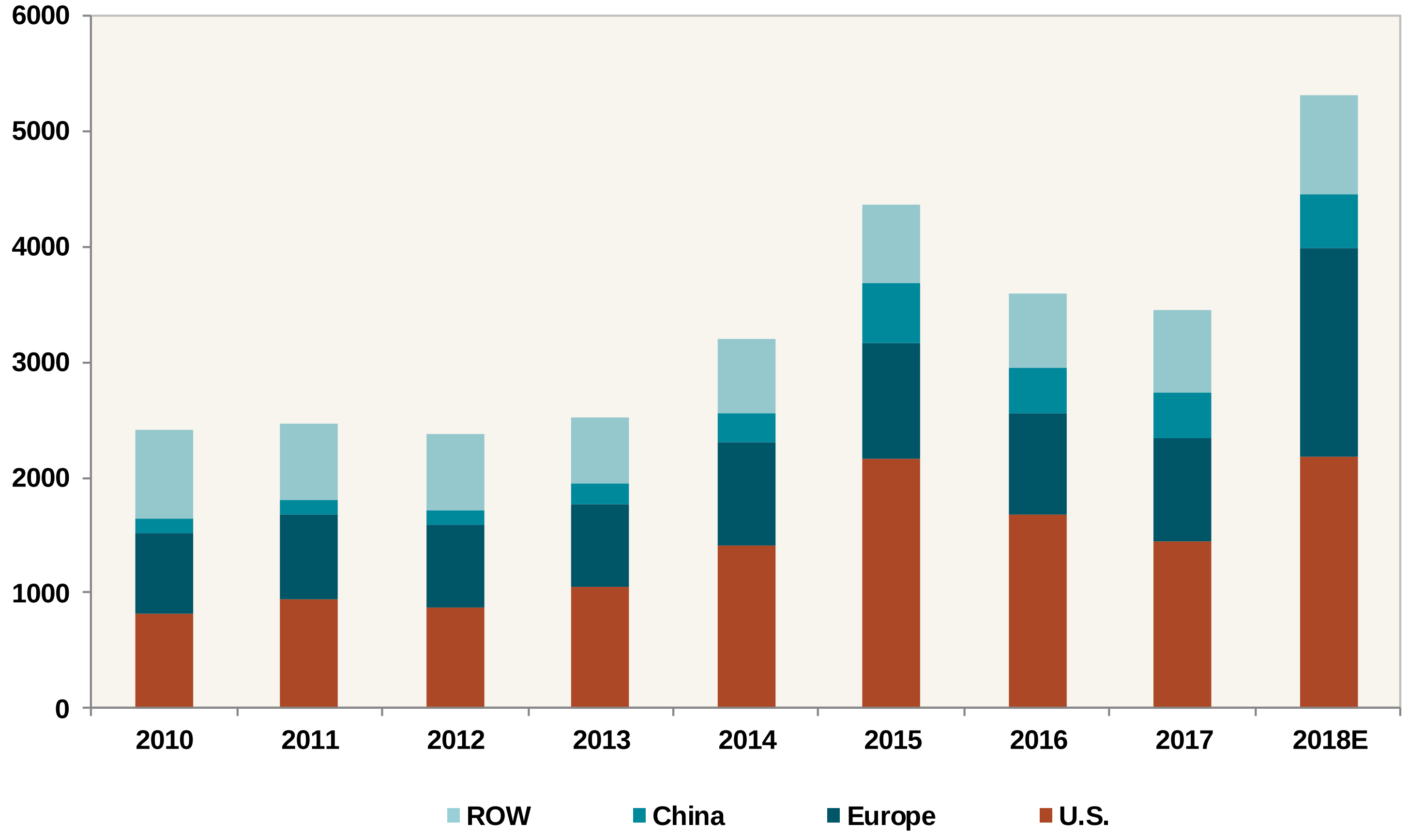
Dividend + buyback yield: 1.75 ppts above 10Y yield (reflecting record buybacks)



Source: Bloomberg, Standard and Poor's, Epoch Investment Partners
As of May 31, 2018

M&A: 2018 is Shaping Up as a Record Year for Global Deals

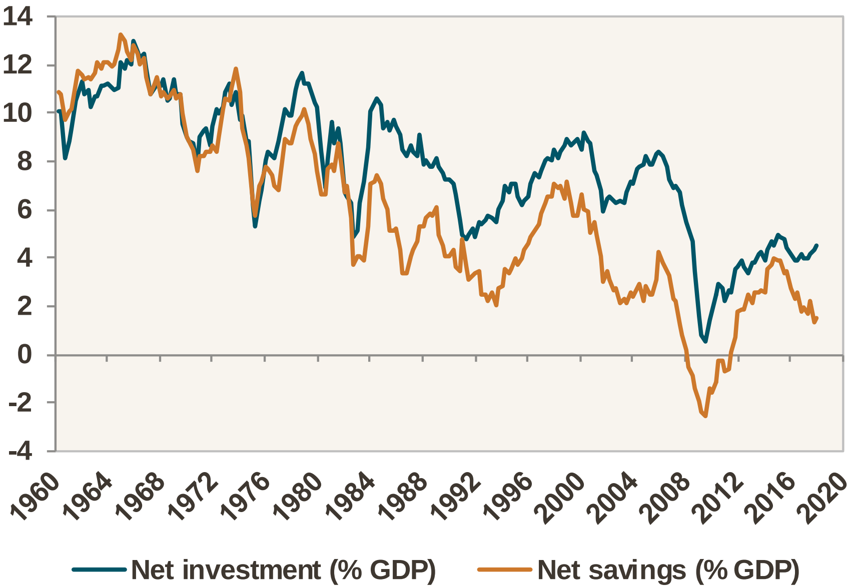
Announced global M&A volume (USD bn, deals worth more than $100 mn)



Source: Goldman Sachs

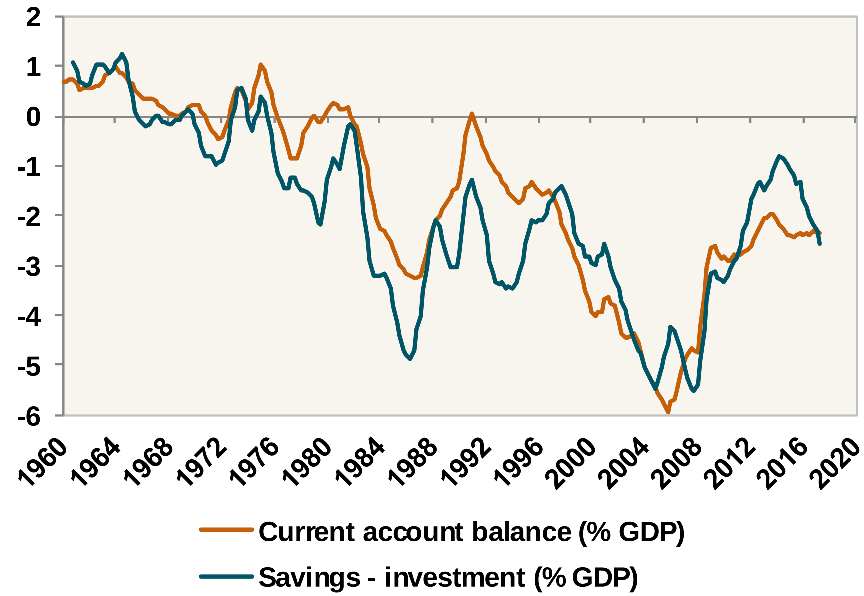
Trade Deficits are Driven by the Investment-Savings Balance

U.S. total net savings, as a % of GDP, has been on a declining trend since the early-1960s



Source: Federal Reserve, Bloomberg, Epoch Investment Partners
As of December 31, 2017

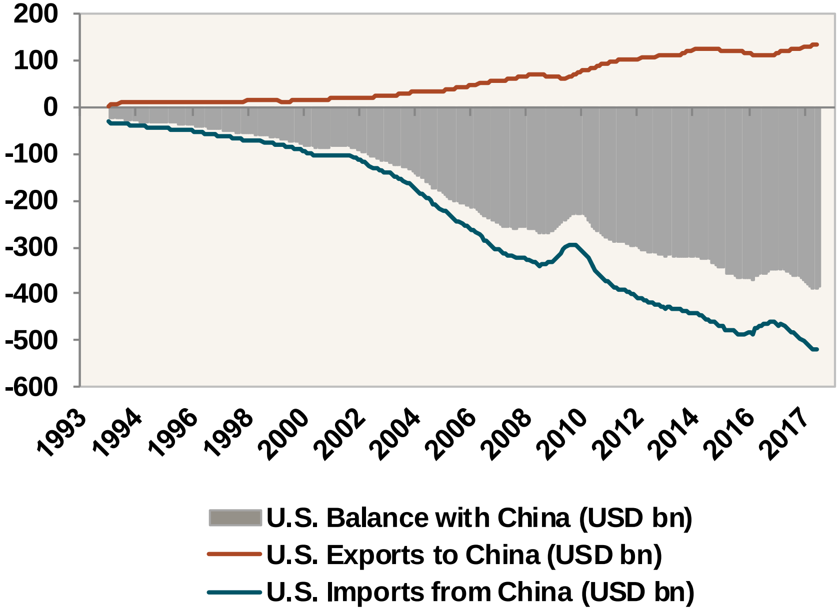
The U.S. current account is 88% correlated with the investment-savings gap



Source: Federal Reserve, Bloomberg, Epoch Investment Partners
As of December 31, 2017

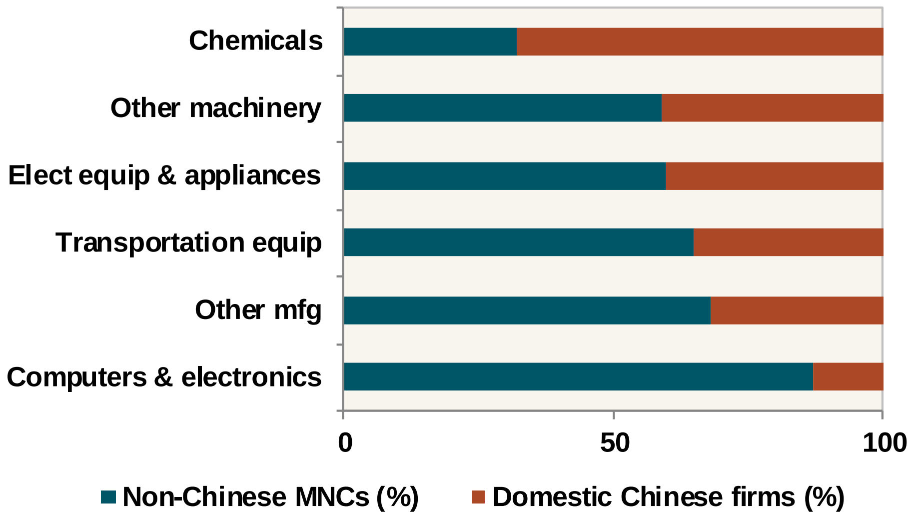
Trade Wars are Lose-Lose

Unbalanced: Solely due to comparative advantage? The trade gap has increased six-fold since 2001.



Source: Bloomberg, Epoch Investment Partners
As of May 31, 2018

Share of target U.S. imports from China: Chinese vs. non-Chinese firms, 2017



Source: Peterson Institute for International Economics
As of December 31, 2017

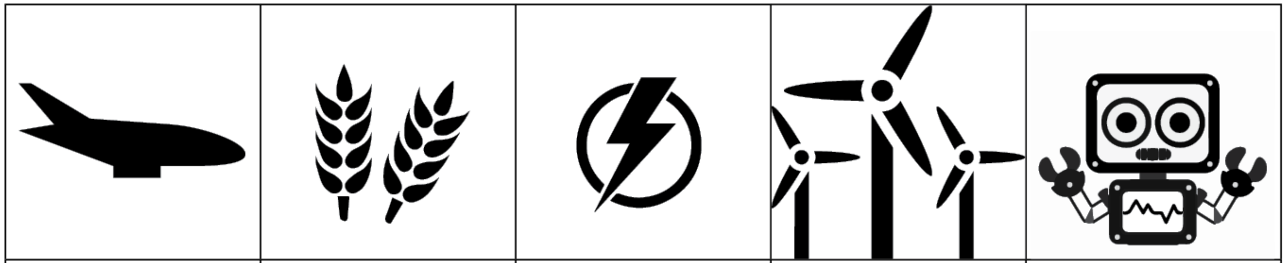
Complex global supply chains

- U.S. MNCs operating abroad have sales of $6tn, roughly 4x total U.S. exports

EPOCH

President Xi has Indicated that "Made in China 2025" is Non-Negotiable: Expect Trade Rhetoric to Remain in the Headlines

Increased state involvement in the Chinese economy, a web of opaque subsidies

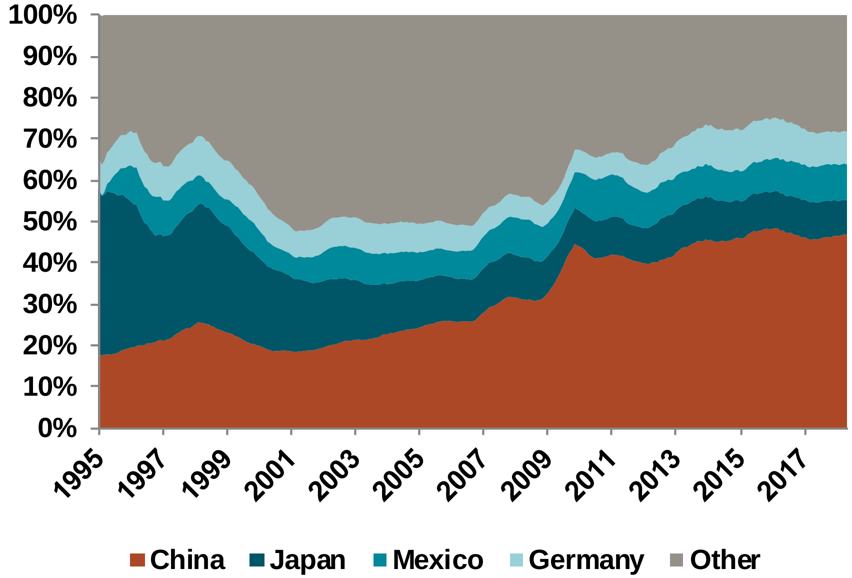


Aviation & Aerospace	Agriculture	Electrical Power	New Energy Automotive	High-End Robotics

Next Gen Information Technology	New Materials & Composites	Rail Transportation	Maritime Engineering	Biomedical & Advanced Medical Equipment

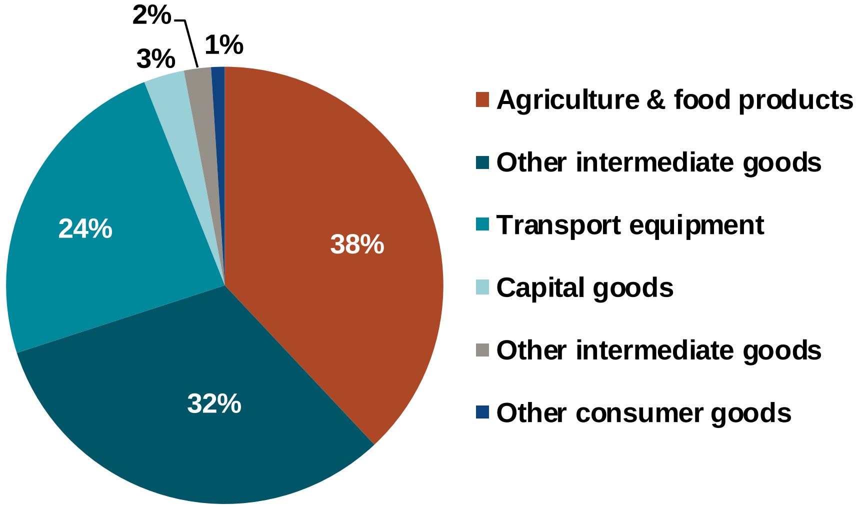
China is the Primary, but Not the Only, Target

U.S. trade deficit by country (proportion, %)



Source: Bloomberg, Epoch Investment Partners
As of May 31, 2018

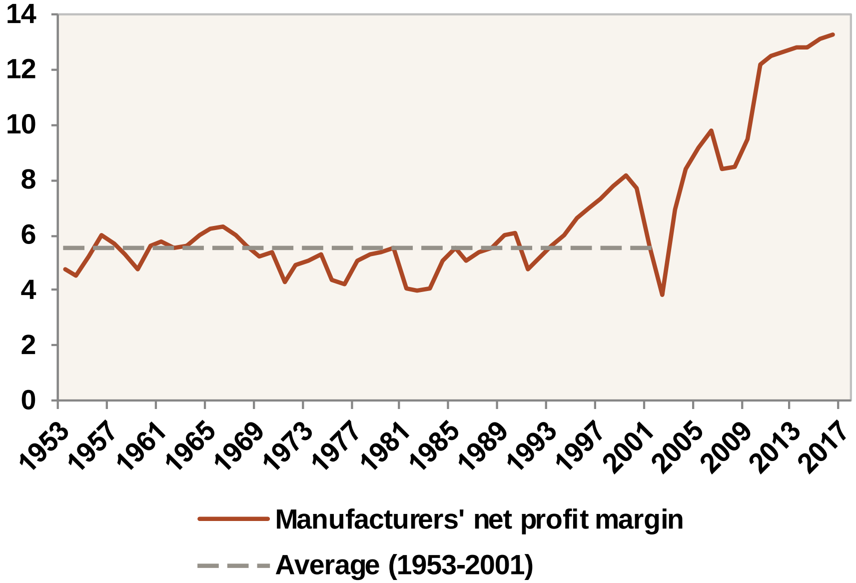
China's retaliation list (by product type, %)



Source: Peterson Institute for International Economics
As of May 31, 2018

Playing the Movie Backwards: Will Protectionism Shrink Manufacturers' Profit Margins?

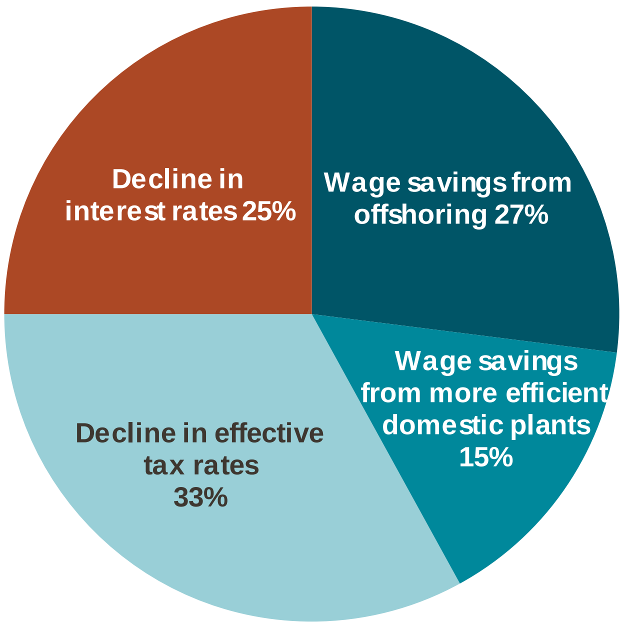
Manufacturers have propelled the S&P 500's margin gains during the Bretton-Woods II era



Source: Empirical Research Partners
Note: Net profit margins for S&P 500 companies, trailing 4 quarters, smoothed.
As of December 31, 2016

Even an escalation of the trade dispute to include $200bn of imports would only reduce US GDP growth by roughly 0.25% and increase inflation by about 0.15%. But the impact on the stock market could be much larger, and faster.

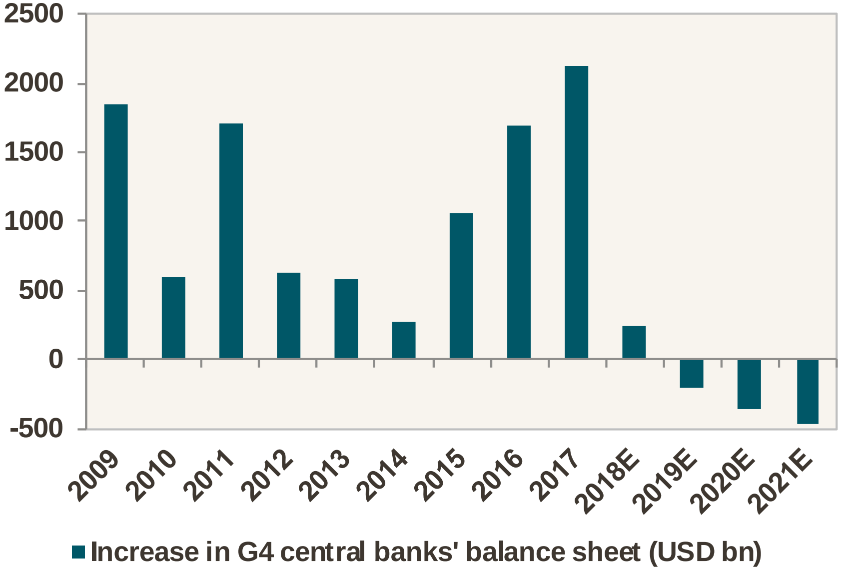
The margin expansion of S&P 500 manufacturers from 2000-2015 can be attributed to four key factors



Source: Empirical Research Partners
As of December 31, 2016

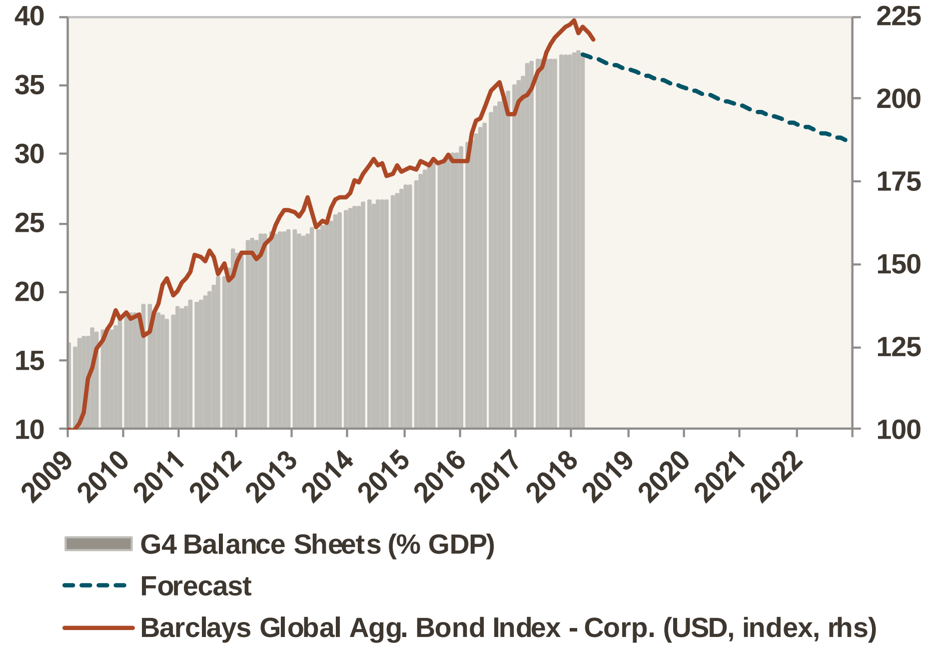
Unleashing Vol: The End of QE and the Return of Price Discovery

Combined G4 central bank balance sheet has increased inexorably for a decade. The yoy tightening impulse will be dramatic.



Source: FRB, ECB, BOJ, BOE, Bloomberg, Epoch Investment Partners
As of April 30, 2018

G4 QE suppressed interest rates and created a deluge in corporate bond issuance (96% correlation)

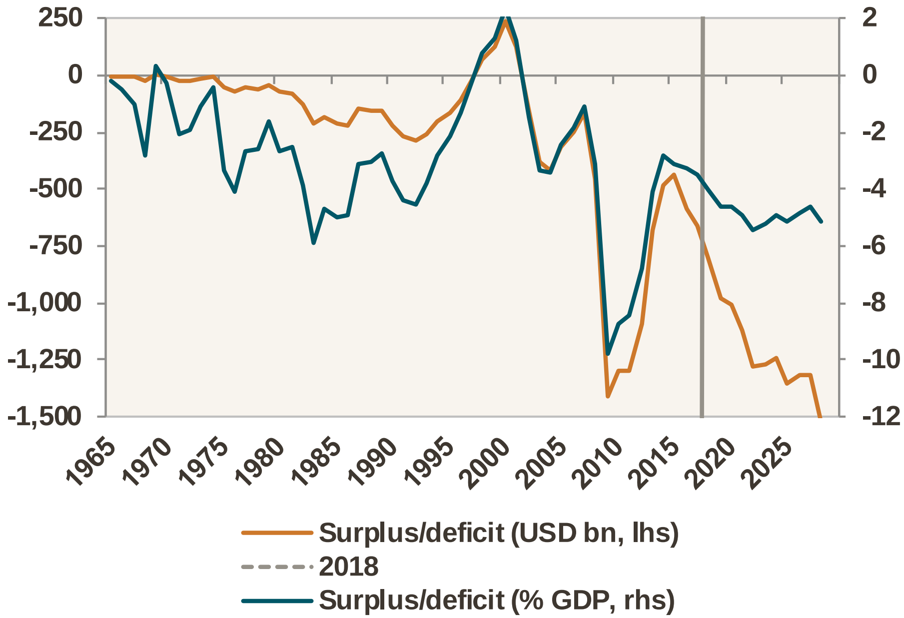


Source: FRB, ECB, BOJ, BOE, Bloomberg, Epoch Investment Partners
As of May 31, 2018

EPOCH

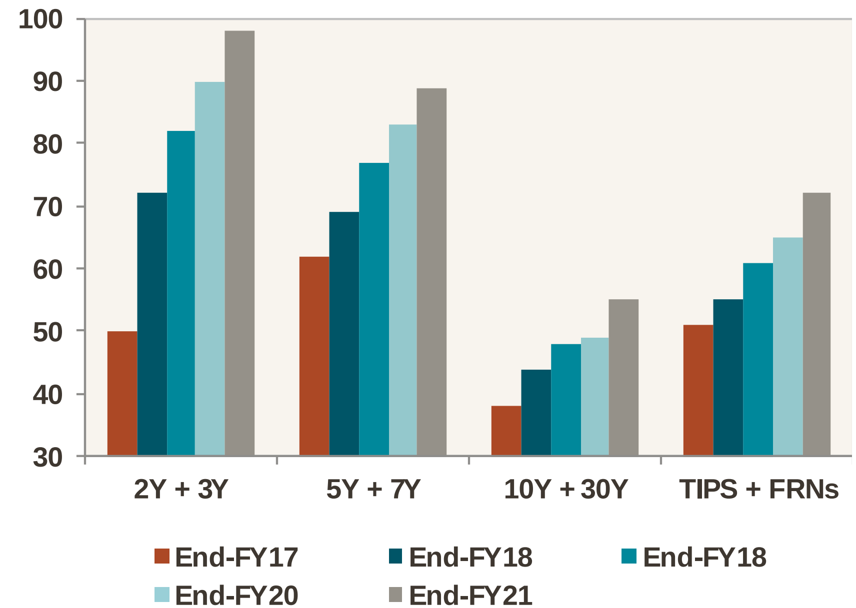
U.S. Fiscal Imbalances: To Infinity And Beyond

Trillion dollar federal budget deficits to be the norm from 2019, and is already the worse ever excluding wars and recessions.



Source: Congressional Budget Office, Bloomberg, Epoch Investment Partners
As of December 31, 2017

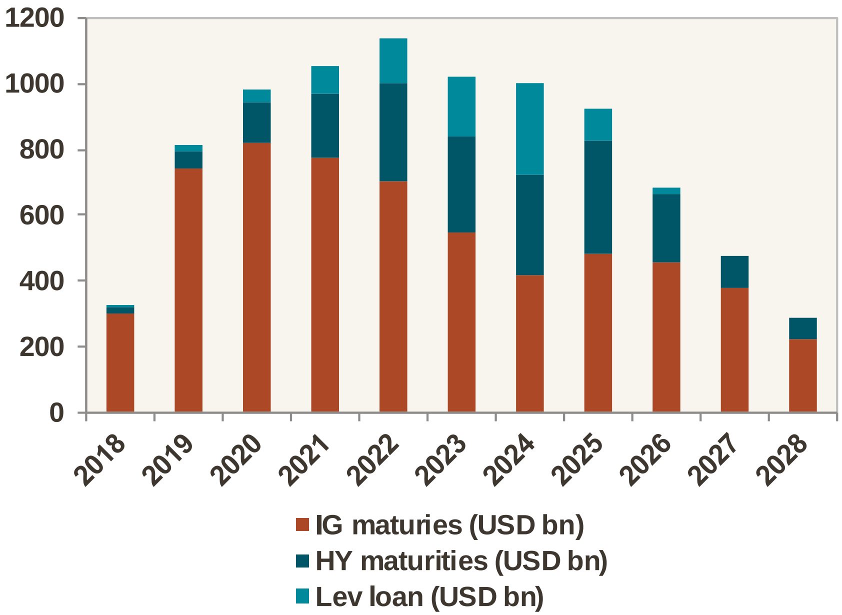
Rising U.S. deficit will likely be over $1 trillion in 2019. This and the Fed portfolio runoff, necessitates ever rising Treasury auctions.



Source: U.S. Treasury Department, Goldman Sachs, Epoch Investment Partners
As of May 9, 2018

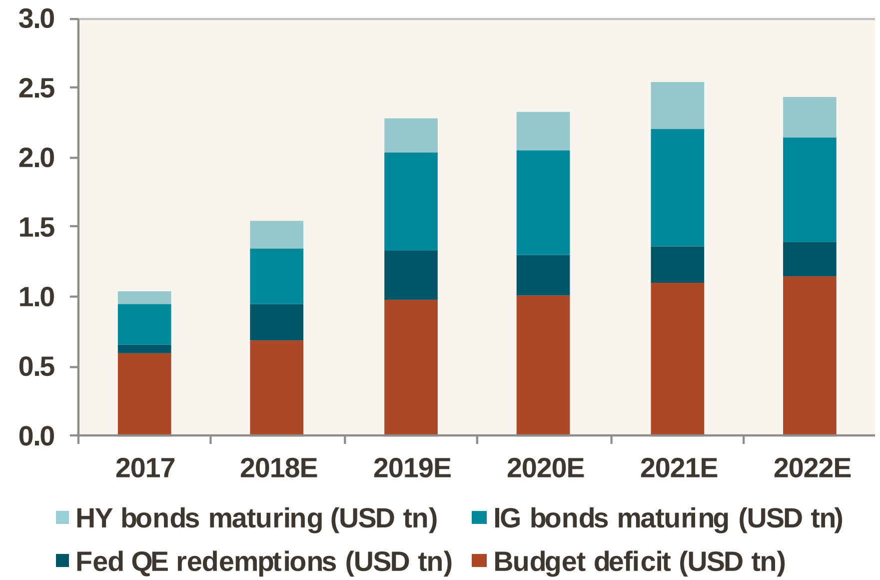
The Problem Next Time: Corporate Bonds At The Epicenter

Value of U.S. corporate bonds maturing is expected to be more than triple. Likely placing stress on the U.S. corporate debt market.



Source: Goldman Sachs, Epoch Investment Partners
As of May 31, 2018

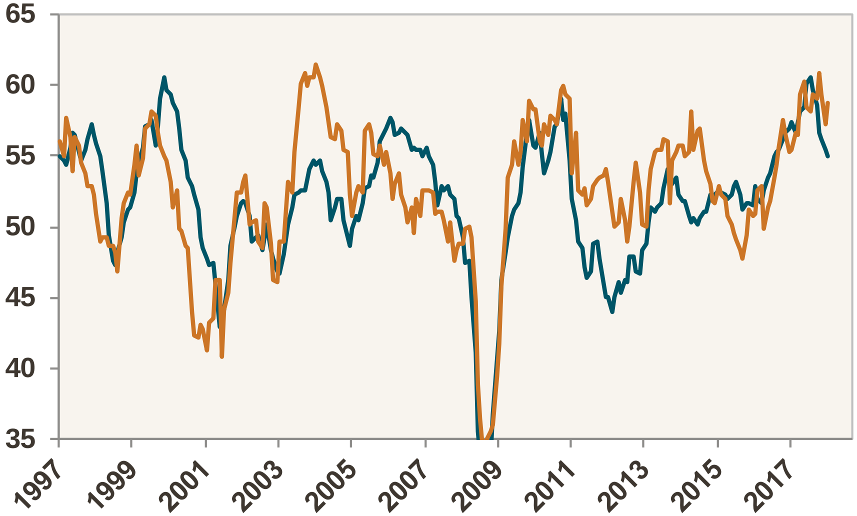
Rising U.S. budget deficit comes at the same time as Fed redemptions and soaring corporate bond maturities.



Source: Deutsche Bank, Epoch Investment Partners
As of April 27, 2018

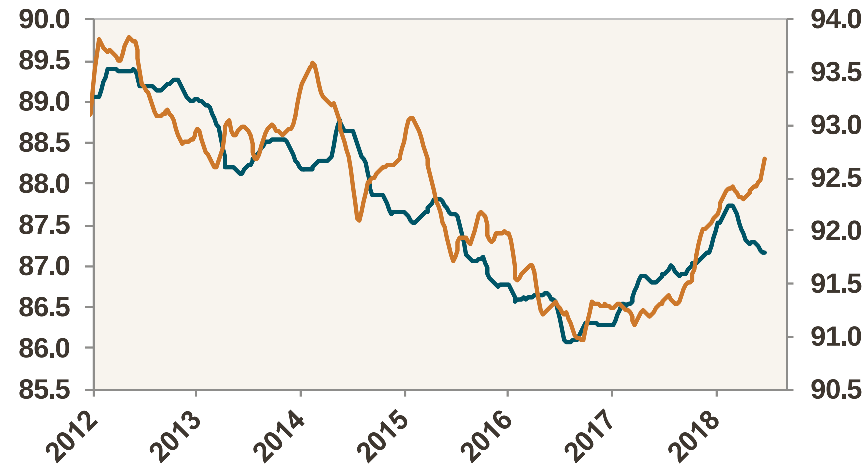
European Growth: Cresting, Not Collapsing

**Manufacturing PMIs:
Europe has rolled over, U.S. remains solid**



Source: Bloomberg
As of June 15, 2018

**GDP forecast revision indices:
Europe and the U.S. go their separate ways**

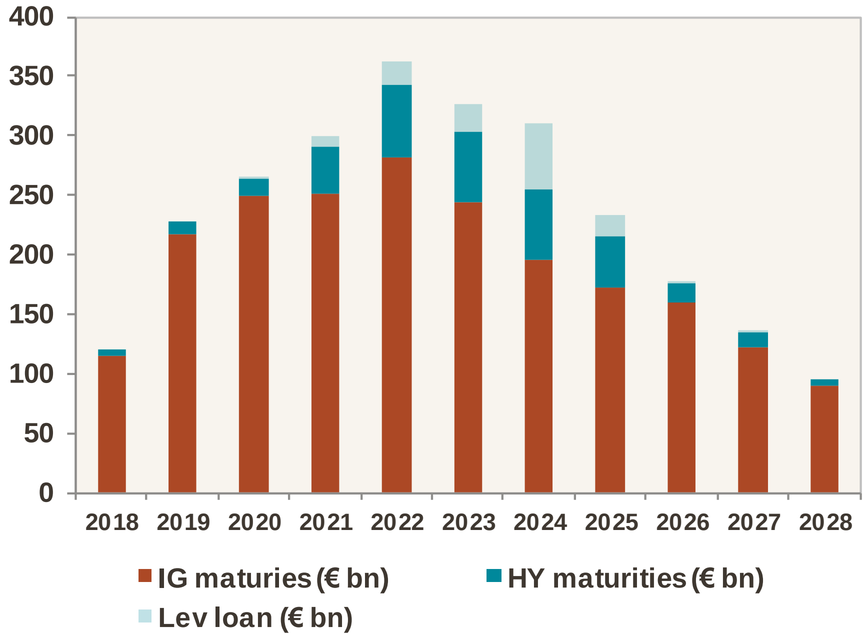


Source: Bloomberg
As of June 22, 2018

U.S. is still benefitting from the TCJA, while Europe gets roiled by political turmoil.

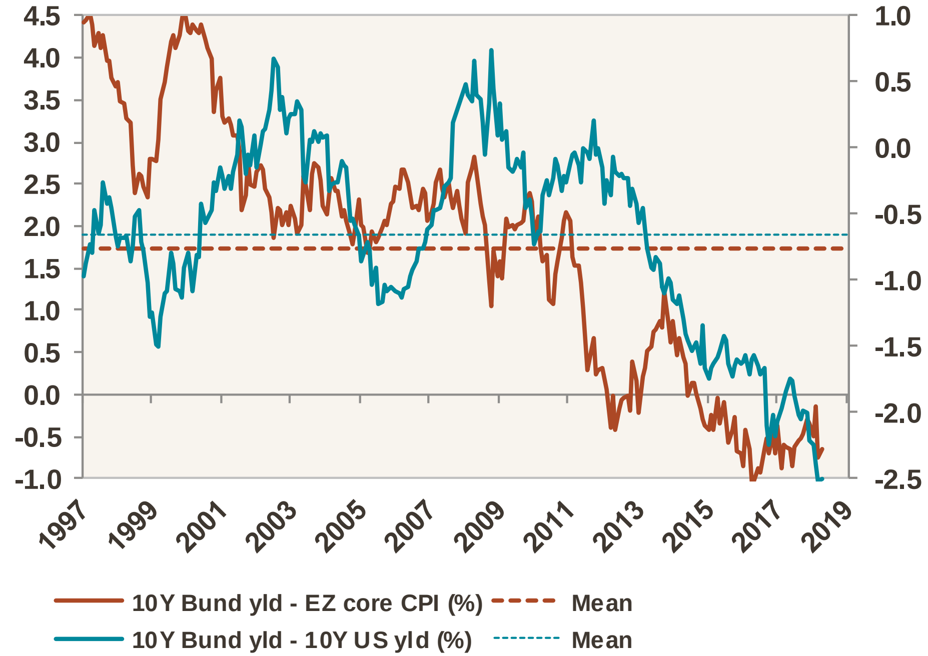
Europe's Double Whammy: The End of QE, Plus a Wall of Maturities

The value of European corporate bonds maturing is expected to triple, from €120 bn in 2018 to €362 bn in 2022 placing pressure on credit spreads.



Source: Goldman Sachs, Epoch Investment Partners
As of May 2, 2018

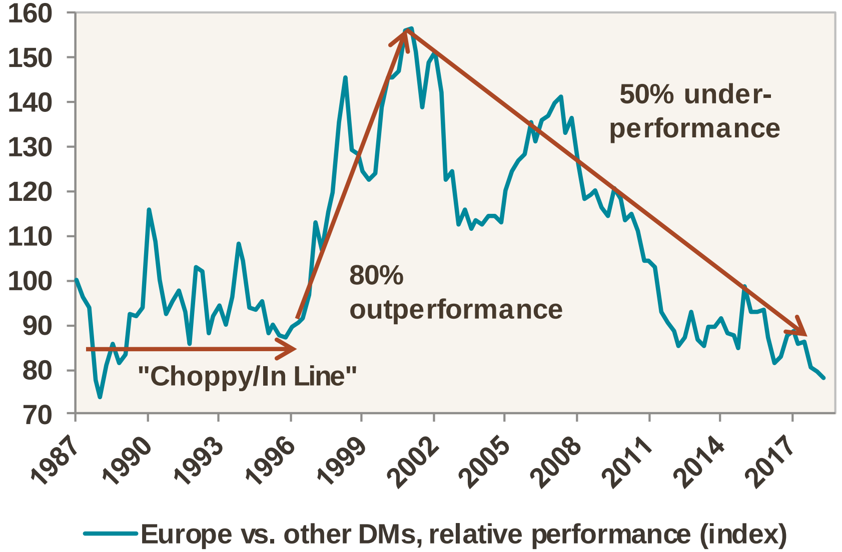
Unfettered by fundamentals – The 10Y bund yield is extraordinarily low relative to its own history, as well as Germany's strong fundamentals, domestic inflation and U.S. 10-year Treasury yields



Source: NBER, Bloomberg, Epoch Investment Partners
As of May 31, 2018

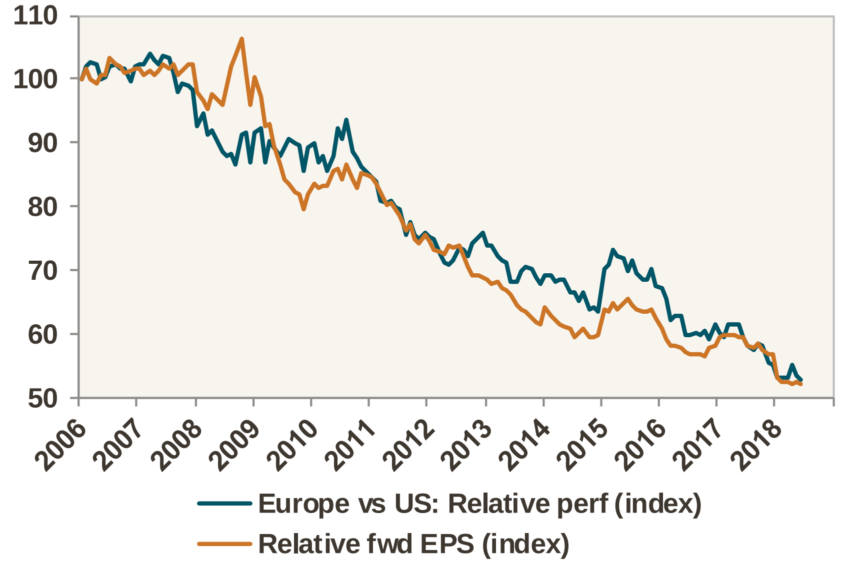
European Underperformance: Reflects Relative Earnings Growth

Long-term relative performance: This too shall pass, but not quite yet



Source: Bloomberg, Epoch Investment Partners
As of May 31, 2018

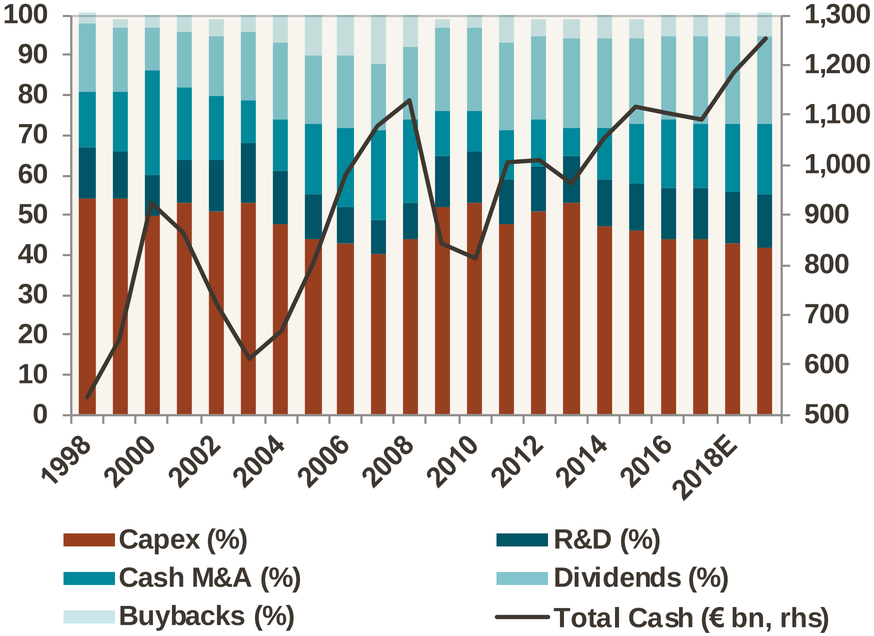
Weaker EPS growth reflects its sluggish macro performance and a dearth of tech



Source: Bloomberg, Epoch Investment Partners
As of May 31, 2018

Cash Flow has Grown Less Quickly in Europe than the U.S., With a Smaller Proportion Returned to Shareholders

STOXX European 600 (ex-fin): Companies' use of cash

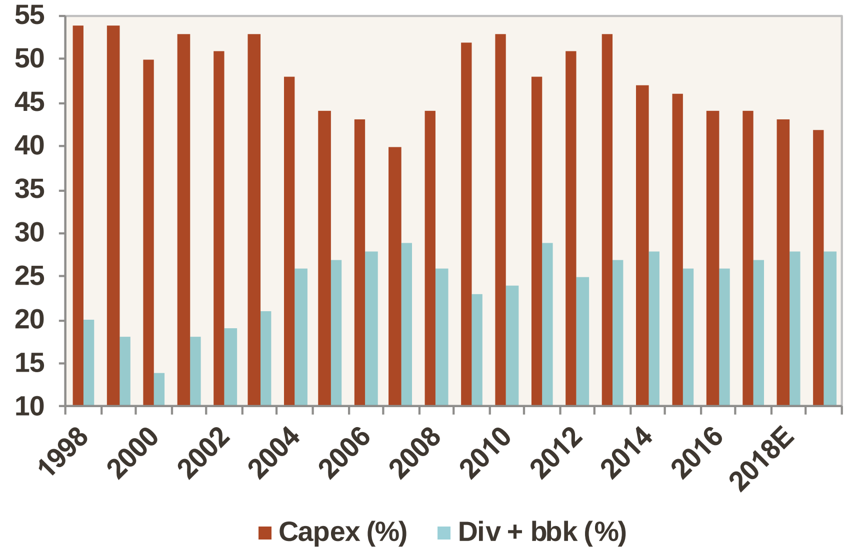


Source: Goldman Sachs

Dividends plus buybacks: Accounted for 18-20% of cash usage two decades ago, but has increased to 28% in 2018 (vs. 46% in U.S.).

Capex: Represented 50 – 54% of cash usage in the late-90s/early-2000s, compared to 42 - 44% now (vs. 27 - 28% in the U.S.).

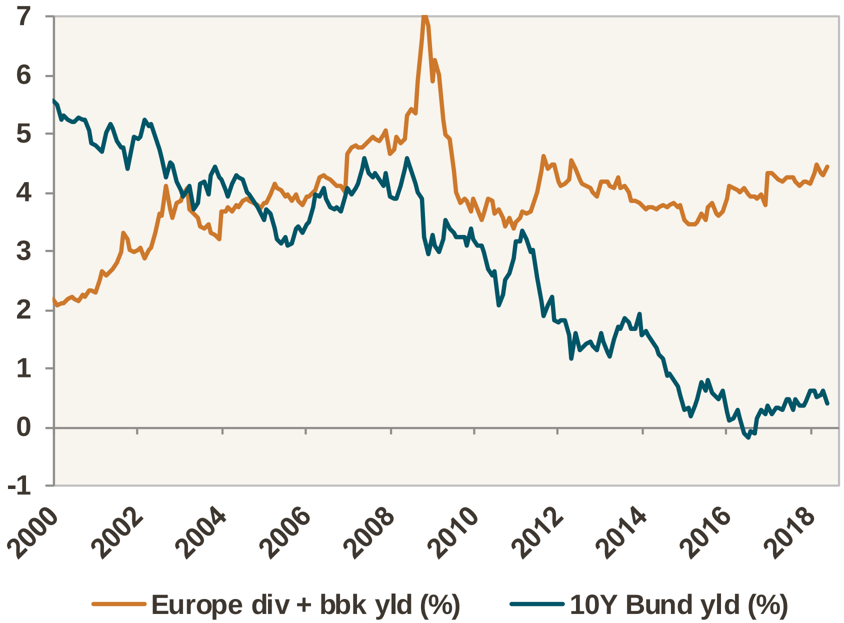
Cash usage (%) in Europe: Smaller proportion returned to shareholders than in the U.S.



Source: Goldman Sachs

Combined Cash Yield: Superior to that Available from Bunds. Eurozone Reform: Stalled.

Dividend + buyback yield:
400 bps above the 10Y bund yield



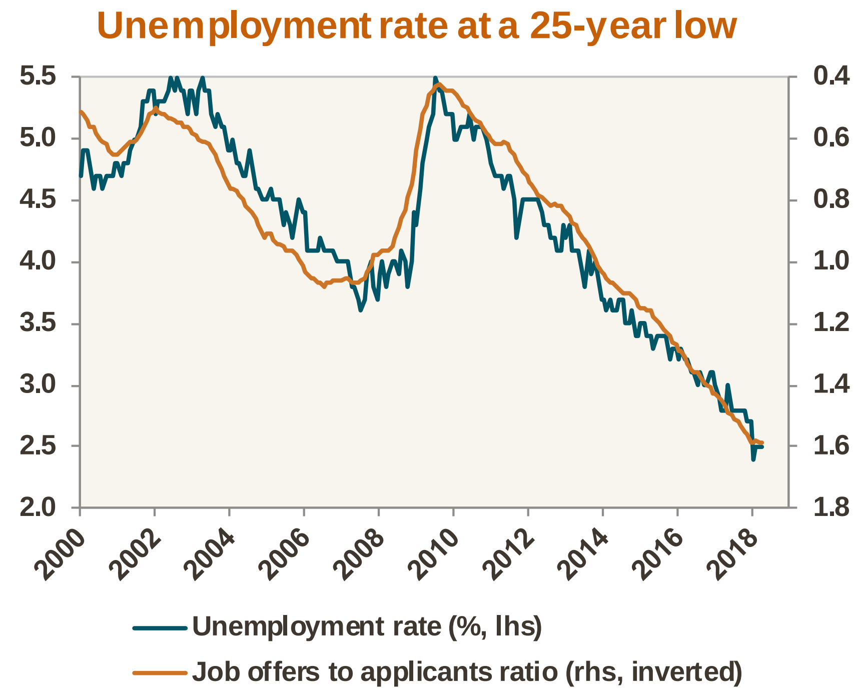
Source: Bloomberg, Epoch Investment Partners
As of May 31, 2018

The fundamental problems of the Eurozone have not been resolved

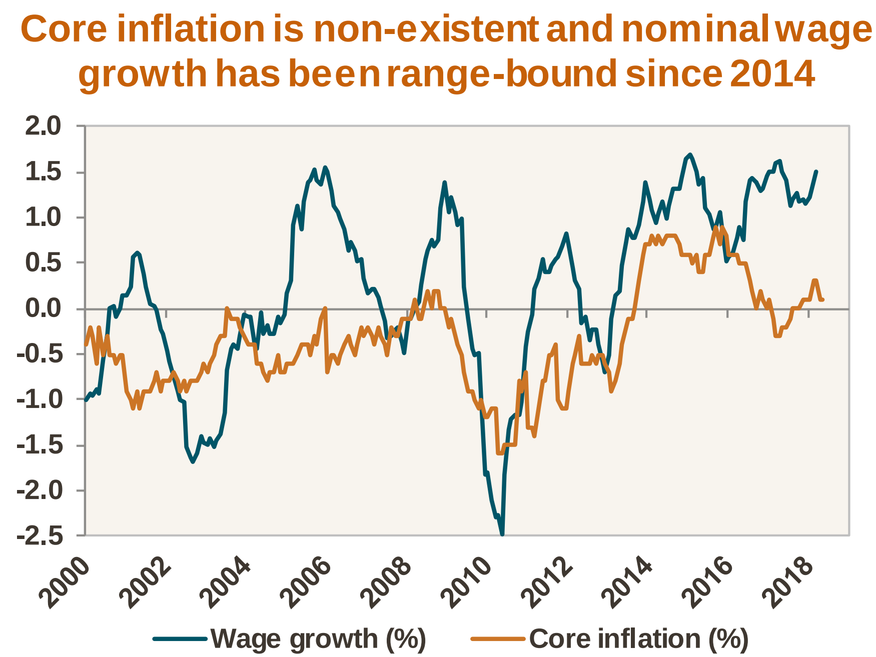
- Banking union: Progress seems to be reversing
- Fiscal union: The Growth and Stability Pact rules are increasingly broken.
- Political union: Not while populists are in the ascendancy.

Unlikely that 2018 will see any progress regarding the much needed reform agenda

Japan's Labor Market is Tight: But Why Aren't Wages Rising?



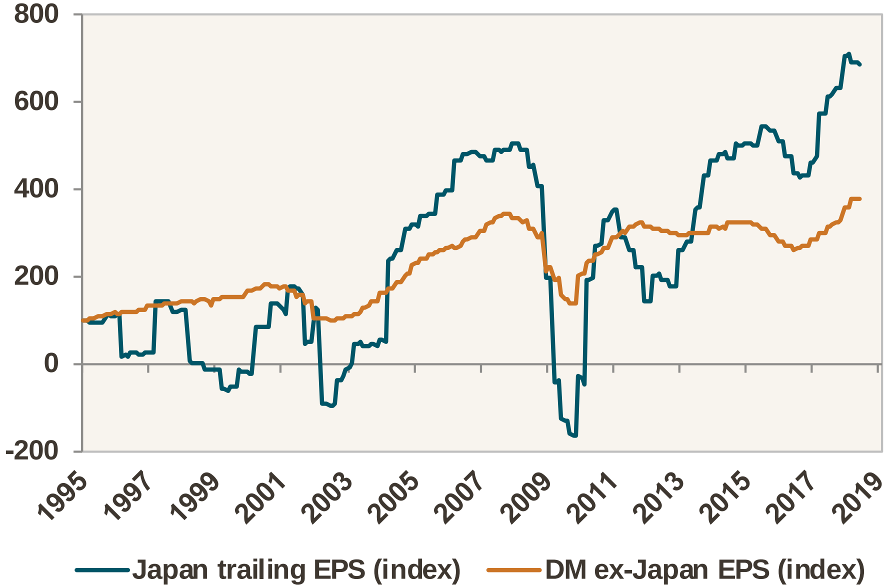
Source: Bloomberg, Epoch Investment Partners
As of April 30, 2018



Source: Bloomberg, Epoch Investment Partners
As of April 30, 2018

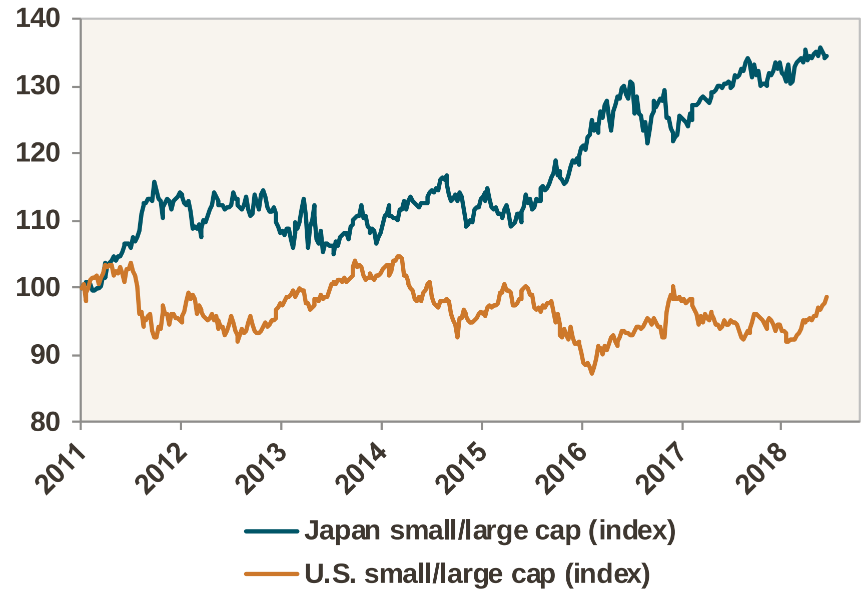
Why Isn't Japan Outperforming? Smaller Caps are Interesting.

Japan EPS growth has outperformed



Source: Bloomberg, Epoch Investment Partners
As of May 31, 2018

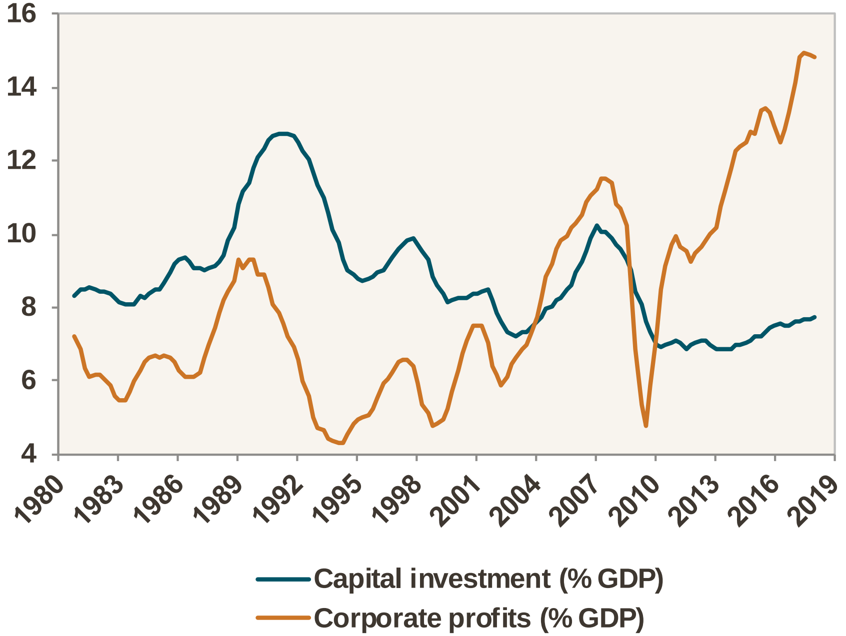
Japanese smaller companies outperform on improvements in the domestic environment



Source: Bloomberg, Epoch Investment Partners
As of June 22, 2018

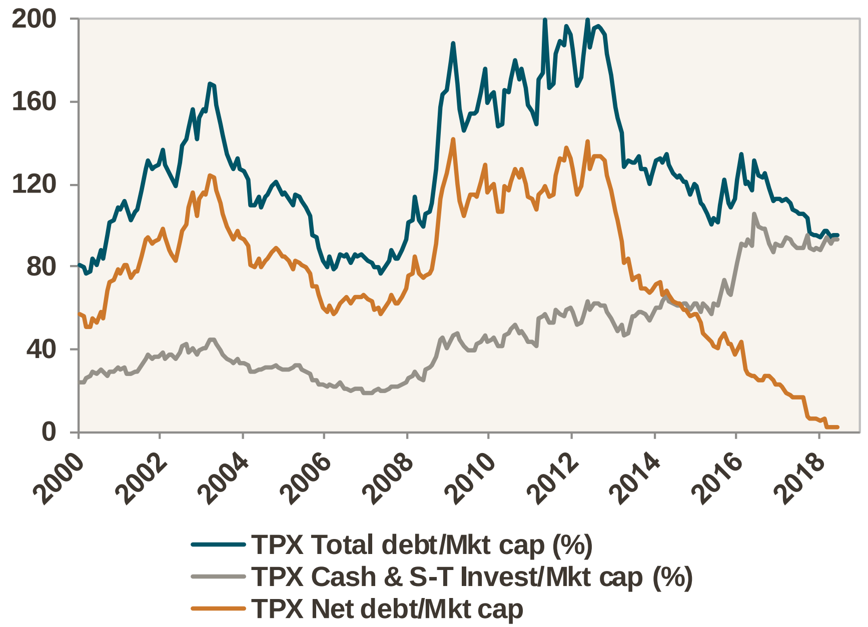
Japanese Profits Dramatically Outstripping Capex

Capital-lite Japan?



Source: Bloomberg, Epoch Investment Partners
As of March 31, 2018

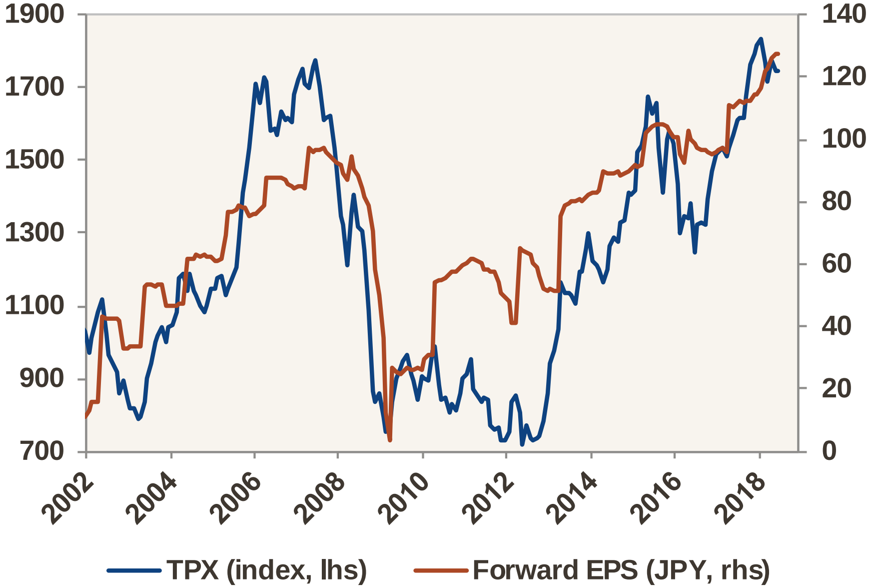
Topix: Approaching zero net debt



Source: Bloomberg, Epoch Investment Partners
As of May 31, 2018

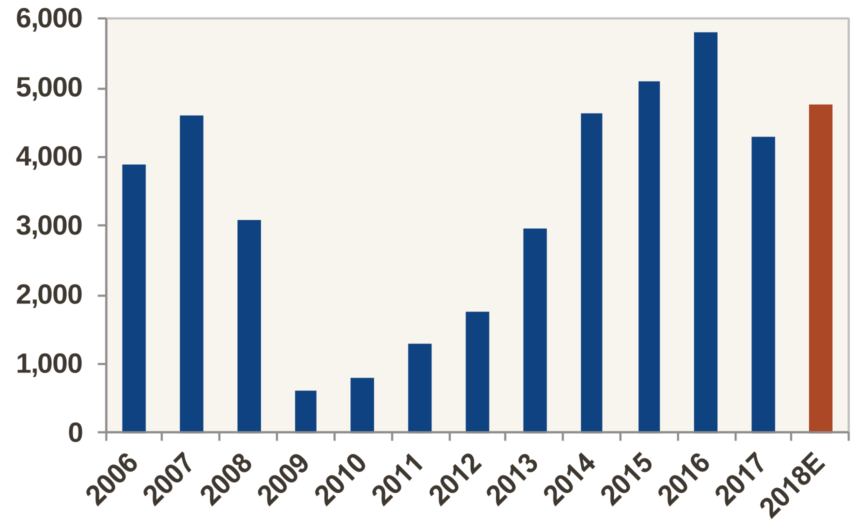
Outlook for Japan is More Constructive than Europe's

Solid earnings should drive the TPX higher



Source: Bloomberg, Epoch Investment Partners
As of May 31, 2018

Buybacks (JPY bn) expected to grow 10% yoy



Source: CLSA
As of May 31, 2018

EPOCH

Summary and Investment Implications

1. **Robust U.S. outlook:** The labor market is tight, domestic demand is solid and the production side of the economy has picked up markedly. This provides a robust backdrop for earnings growth in the coming quarters. Further, the Tax Cuts and Jobs Act (TCJA) is providing a short-term boost to growth (and adding roughly 7% to EPS).
2. **Wage and price inflation in the U.S.:** Increasing, but by less than in a typical cycle, likely due to technology. Still, the output gap has closed, so we expect moderate reflation and slightly higher bond yields.
3. **Equity multiples unlikely to increase further:** Multiples expanded on QE, but we are now transitioning into QT, and this is being combined with Fed hiking (the dot plot suggests 125 bps by end-2019). Consequently, equity return drivers have shifted from broad multiple expansion to earnings growth.
4. **Tech is the new macro:** Technology is positive for all three return on equity (ROE) components — profit margins, asset utilization, and leverage. Among other things, this implies corporate margins can remain high for a prolonged period and don't necessarily need to revert. Also suggests companies returning a higher proportion of cash to shareholders.
5. **Trade war rhetoric:** Key issues include asymmetric market access, alleged IP theft, forced IP transfers and China's 2025 policy. We expect trade tensions to remain a market theme, and a source of volatility, for years to come. However, an outright trade war, one that could cause a recession, is unlikely. We are more concerned about a bifurcation in global supply chains.
6. **The return of price discovery:** The looming trifecta of QT, soaring U.S. budget deficits and the upcoming wall of maturities (in Treasuries and corporate debt) could drive both interest rates and volatility markedly higher. Corporate debt is likely to be at the epicenter of upcoming market dislocations, as issuance has soared with QE and spreads remaining dangerously tight.
7. **Europe:** Growth is slowing, but is unlikely to collapse. Still, this is worrisome as Europe is likely to continue underperforming, as it grows EPS and CF less quickly than the U.S. (partially reflecting a lower weighting in Tech). Further, a smaller proportion of its CF is returned to shareholders. Finally, Eurozone's reform agenda has stalled, undermining medium-term growth prospects.
8. **Japan:** The outlook has improved and Japan now looks relatively cheap. Our main concern is that the pace of improvement, regarding how companies think in terms of shareholder yield and capital allocation, remains glacial. Progress in these areas would send the Topix markedly higher. Japanese smaller companies appear particularly interesting.
9. **Investment approach:** As a result of the above points, it is ever more important to favor companies with a demonstrated ability to produce FCF and allocate that cash flow wisely between return of capital options and reinvestment / acquisition opportunities.

Conclusion

A replay of our quarterly webinar is available on our website

www.eipny.com

RECENT PUBLICATIONS & WHITE PAPERS

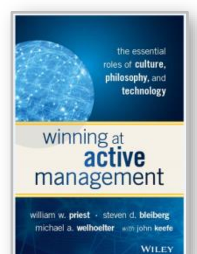
"The Limits of Theory"

"The Winds of Change: The Transition from QE to QT"

"When 'Bits' Meet 'Atoms'"

"What Do We Mean When We Talk About Value?"

"The Bull vs Bear Case for Emerging Markets"



Winning at Active Management

Page Intentionally Left Blank

Appendix

Biographies
Disclosures and Fees

Epoch Global Choice Team Biographies

William W. Priest, CFA – Chief Executive Officer, Co-Chief Investment Officer and Portfolio Manager

Bill is Chief Executive Officer and Co-Chief Investment Officer of Epoch Investment Partners. He is a portfolio manager for Epoch's global equity investment strategies and leads Epoch's Investment Policy Group, a forum for analyzing broader secular and cyclical trends that Epoch believes will influence investment opportunities. Prior to co-founding Epoch in 2004 with David Pearl, Tim Taussig and Phil Clark, Bill was a Co-Managing Partner and portfolio manager at Steinberg Priest & Sloane Capital Management, LLC for three years. Before joining Steinberg Priest, he was a member of the Global Executive Committee of Credit Suisse Asset Management (CSAM), Chairman and Chief Executive Officer of Credit Suisse Asset Management Americas and CEO and portfolio manager of its predecessor firm BEA Associates, which he co-founded in 1972. During his 30 year tenure at BEA and CSAM, he developed the firm into a well-recognized investment manager with over $100 billion under management. Bill is the author of several published articles and papers on investing and finance, including the books, The Financial Reality of Pension Funding Under ERISA, Free Cash Flow and Shareholder Yield: New Priorities for the Global Investor, and Winning at Active Management: The Essential Roles of Culture, Philosophy and Technology (with co-authors Steven Bleiberg and Michael Welhoelter). He holds the Chartered Financial Analyst designation, is a former CPA and a graduate of Duke University and the University of Pennsylvania Wharton Graduate School of Business. He is a member of the Council on Foreign Relations.

David N. Pearl – Executive Vice President, Co-Chief Investment Officer and Portfolio Manager

David is Executive Vice President and Co-Chief Investment Officer of Epoch Investment Partners. He is a portfolio manager for Epoch's U.S. investment strategies. Prior to co-founding Epoch in 2004 with Bill Priest, Tim Taussig and Phil Clark, David was a Managing Director and portfolio manager at Steinberg Priest & Sloane Capital Management, LLC where he was responsible for both institutional and private client assets. Previously, he held senior portfolio management positions at ING Furman Selz Asset Management and Citibank Global Asset Management where he managed mutual funds and institutional accounts. Prior to Citibank, David was an officer and senior analyst of BEA Associates, predecessor to Credit Suisse Asset Management – Americas. David holds a BS in Mechanical Engineering from the University of Pennsylvania and an MBA from The Stanford University Graduate School of Business.

William J. Booth, CFA – Managing Director, Co-Chief Investment Officer and Portfolio Manager

Bill is Co-Chief Investment Officer of Epoch Investment Partners. He is also a portfolio manager for global and non-U.S. equity strategies. Bill joined Epoch in 2009 from PioneerPath Capital, a long/short equity hedge fund where he was a consumer and retail analyst. Prior to PioneerPath, he was a senior analyst at Level Global focused on the consumer and industrial sectors. He also held an equity research position at Louis Dreyfus Commodities and was a credit analyst with Citigroup. Bill holds a BS in Chemical Engineering from Yale University and an MBA from New York University's Leonard N. Stern School of Business.

Michael A. Welhoelter, CFA – Managing Director, Co-Chief Investment Officer, Portfolio Manager and Head of Risk Management

Mike is Co-Chief Investment Officer of Epoch Investment Partners. He is also Chief Risk Officer. Mike is responsible for integrating risk management into the investment process. Prior to joining Epoch in 2005, he was a director and portfolio manager in the Quantitative Strategies Group at Columbia Management Group, Inc. Before that, Mike was at Credit Suisse Asset Management Group ("CSAM"), where he was a portfolio manager in the Structured Equity group. Before joining CSAM, he was a portfolio manager and quantitative research analyst at Chancellor/LGT Asset Management. Mike is an author (with co-authors Bill Priest and Steven Bleiberg) of Winning at Active Management: The Essential Roles of Culture, Philosophy and Technology. Mike holds a BA degree in Computer and Information Science from Colgate University. He is a member of the New York Society of Security Analysts and the Society of Quantitative Analysts.

Epoch Global Choice Team Biographies

Josepha Kaufman – Managing Director, Senior Research Analyst
Josepha is a senior equity research analyst. Prior to joining Epoch in 2010, Josepha was a senior analyst for six years for Michael Price at MFP Investors LLC. She worked as a global analyst covering primarily consumer, retail, industrials, special situations and conglomerates. Prior to MFP, she was an Associate for five years at Tanner & Co., Inc, a mergers and acquisitions boutique. Before Tanner, she was an investment banking analyst at Credit Lyonnais. Josepha received her BA from the University of Pennsylvania and MBA from Columbia University, Graduate School of Business.

John P. Reddan, CFA – Managing Director, Portfolio Manager and Senior Research Analyst
John is a portfolio manager for the U.S. Choice strategy and senior equity research analyst. Prior to joining Epoch in 2004, he was a senior equity analyst at Columbia Management Group responsible for research recommendations in the media/entertainment and online industries. Before Columbia Management, he was a senior investment analyst at Mark Partners for six years where he performed fundamental research on long and short investment ideas. Prior to joining Mark Partners, John held a similar position at Moran Asset Management where he provided both buy-side and sell-side research to investment policy committees, institutional brokerage clients, and the company's institutional sales force. He is a graduate of Siena College, and holds an MBA from Columbia University, Graduate School of Business.

Michael Takata – Director, Research Analyst
Michael is an equity research analyst. He joined Epoch in 2018 with over 30 years of experience covering a number of industries. His background includes portfolio management roles at Ulysses Management, Odyssey Partners and Soros Fund Management. Before that, Michael was a senior vice president and research analyst at BEA Associates, working with Bill Priest. He began his career as sell-side insurance research analyst. Michael has an AB in Pure Mathematics from the University of Chicago.

Richard Watt – Managing Director, Global Portfolio Management
Richard leads our client portfolio manager and product management group. Prior to joining Epoch in 2007, Richard spent four years as Executive Vice President of U.K.-based Schroders Investment Management where his responsibilities included consultant relations, client service and sales for domestic and international equity, fixed income and alternative products. Prior to Schroders, he worked at Credit Suisse Asset Management as Head of Emerging Markets and President of CSAM's closed-end investment funds responsible for managing a variety of investment products for clients located globally. Richard has held positions as a portfolio manager with Gartmore and Kleinwort Benson in London. He began his career in Edinburgh, Scotland in 1982. He holds an MA Joint Honors Degree in History and Politics from the University of Edinburgh.

Global Choice

Global Choice Composite Annual Performance Disclosures									
	Total Firm	Composite Assets		Annual Performance Results					
Year End	Assets (Millions)	USD (Millions)	Number of Accounts	Composite Gross	Composite Net **	MSCI World (Net)	Internal Dispersion	Composite 3-Yr St Dev	MSCI World (Net) 3-Yr St Dev
2017	49,482	5,097	18	30.82%	30.05%	22.40%	0.4%	11.01%	10.23%
2016	42,106	4,607	21	(0.56)%	(1.12)%	7.51%	0.2%	11.13%	10.92%
2015	41,918	4,847	23	0.07%	(0.52)%	(0.87)%	0.4%	10.79%	10.80%
2014	43,617	4,802	23	3.17%	2.61%	4.94%	0.4%	10.04%	10.23%
2013	38,439	3,987	23	32.52%	31.83%	26.68%	0.6%	12.10%	13.54%
2012	24,534	3,095	22	15.42%	14.86%	15.83%	0.8%	15.42%	16.74%
2011	19,217	1,918	18	(0.14)%	(0.61)%	(5.54)%	0.4%	16.43%	20.15%
2010	14,326	1,337	14	6.82%	6.27%	11.76%	0.7%	20.42%	23.72%
2009	11,354	943	11	37.40%	36.17%	29.99%	0.8%	18.47%	21.40%
2008	5,348	108	Five or fewer	(35.61)%	(36.30)%	(40.71)%	N.A	17.52%	17.02%
2007	6,682	67	Five or fewer	17.19%	16.20%	9.04%	N.A	N.P	N.P
2006	4,408	19	Five or fewer	29.95%	28.86%	20.07%	N.A	N.P	N.P
2005*	2,235	23	Five or fewer	6.35%	6.13%	3.06%	N.A	N.P	N.P

N.A. - Information is not statistically meaningful due to an insufficient number of portfolios in the composite for the entire year. *Results shown for the year 2005 represent partial period performance from October 1, 2005 through December 31, 2005. **Net performance reflects the gross-of-fees return reduced by the investment management fee incurred. Effective 1/2008, net performance is calculated by deducting the actual investment management fee incurred by each portfolio in the composite. Prior to 1/2008, net-of-fee returns reflect the deduction of the highest annual management fee, calculated on a monthly basis. N.P. – Information is not presented because 36 monthly returns are not available.

1. Global Choice Composite contains fully discretionary portfolios managed by Epoch using an investment strategy that pursues long-term capital appreciation by investing in a concentrated portfolio of global businesses we believe have superior risk-reward profiles. Our bottom-up security selection and risk management process leads to a portfolio of 25-35 stocks. The portfolio reflects the highest-conviction ideas of our investment team as appropriate for a concentrated portfolio. Companies are selected based on their ability to generate free cash flow and allocate it intelligently to benefit shareholders. The minimum account size for this composite is $500 thousand.

2. For comparison purposes the composite is measured against the MSCI World (Net) Index [Net total return indices reinvest dividends after the deduction of withholding taxes, using (for international indices) a tax rate applicable to non-resident institutional investors who do not benefit from double taxation treaties]. Effective 1/2009, the benchmark was changed from the MSCI World (Gross) Index to the MSCI World (Net) Index because it is more representative of the firm's accounting methodology with regards to foreign withholding tax treatment. This change has been applied retroactively.

Global Choice

3. Epoch Investment Partners, Inc. claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS standards. Epoch Investment Partners, Inc. has been independently verified for the periods June 21, 2004 through March 31, 2018. Verification assesses whether (1) the firm has complied with all the composite construction requirements of the GIPS standards on a firm-wide basis and (2) the firm's policies and procedures are designed to calculate and present performance in compliance with the GIPS standards. The Global Choice composite has been examined for the periods October 1, 2005 through March 31, 2018. The verification and performance examination reports are available upon request.

4. Epoch Investment Partners, Inc. is a wholly owned subsidiary of The Toronto Dominion Bank. Epoch Investment Partners, Inc. ("Epoch") became a registered investment adviser under the Investment Advisers Act of 1940 in June 2004. Policies for valuing portfolios, calculating performance, and preparing compliant presentations are available upon request.

5. Results are based on fully discretionary accounts under management, including those accounts no longer with the firm.

6. Valuations are computed and performance is reported in U.S. dollars. Returns are presented gross and net of management fees and include the reinvestment of all income. Gross-of-fees returns are presented before management fees but after all trading expenses. Net performance reflects the gross-of-fees return reduced by the investment management fee and performance-based fee (where applicable) incurred. Effective 1/2008, net performance is calculated by deducting the actual investment management fee incurred by each portfolio in the composite. Prior to 1/2008, net-of-fee returns reflect the deduction of the highest annual management fee, calculated on a monthly basis. Returns include the effect of foreign currency exchange rates. Composite and benchmark (international indices) returns are presented net of non-reclaimable withholding taxes.

7. Internal dispersion is calculated using an asset-weighted standard deviation of annual gross returns of those accounts that were included in the composite for the entire year. Internal dispersion figures that are not meaningful due to the limited number of accounts in the composite are annotated by N/A. The three-year annualized standard deviation measures the variability of the composite and the benchmark returns over the preceding 36-month period.

8. The Global Choice Composite was created in October 2005. A complete list of composite descriptions is available upon request.

9. The investment management fee schedule is as follows:

Global Choice (Separate account minimum $50 million)	
ASSETS UNDER MANAGEMENT	**FEE**
First $50 million	0.85%
Next $50 million	0.75%
Over $100 million	Negotiable

Past performance is not indicative of future results. Actual investment advisory fees incurred by clients may vary. Minimum account sizes, fees and fee structure, and other conditions may be waived or modified in the future, and have been waived or modified in the past, at the discretion of Epoch.

Informational Purposes Only

RIO Update:

Budget, VSIP and Investment Returns

July 20, 2018

Dave Hunter, Executive Director / Chief Investment Officer
Fay Kopp, Deputy Executive Director / Chief Retirement Officer
Darren Schulz, Deputy Chief Investment Officer
Connie Flanagan, Fiscal and Investment Operations Manager
ND Retirement & Investment Office (RIO)
State Investment Board (SIB)

RIO Budget Background

On April 18, 2018, Governor Burgum released budget guidelines for 2019-2021. The Governor is requesting all agencies (including special fund agencies) to adopt the following guidelines:

1) Agencies with an appropriation less than $5 million should submit a base budget with a 5% reduction in ongoing expenditures;
2) Agencies with an appropriation of $5 million or more should submit a base budget with a 10% reduction in ongoing expenditures; and
3) Agencies with 20 or more FTE should submit a base budget with a 5% FTE reduction.

RIO currently has 19 authorized FTE and our appropriation for 2017-19 is $5.3 million. Given that RIO's budget is over $5 million, we will need to submit a base budget which includes a 10% reduction which will likely translate into 1-to-4 less FTE. The FTE reduction is assumed due to RIO's budget largely consisting of salaries and benefits (for $4.4 million or 83%) while operating expenses and contingencies have already been reduced to historically low levels. As evidence, RIO's operating expenses declined by 13% over the past 20 years (to less than $863,000 in 2017-19) due to our agency consistently being very cost conscious. RIO's contingency line has also been subject to extreme budget pressures and was reduced by over 36% in the last biennium (to $52,000).

	2017-19 Base Appropriation	Requested 10% Budget Cut	Governor's Base Budget
Salaries and Wages	$ 4,425,570	$ (572,066)	$ 3,853,504
Operating Expenses	$ 862,484	$ 38,061	$ 900,545
Contingencies	$ 52,000	$ -	$ 52,000
Total Special Funds	$ 5,340,054	$ (534,005)	$ 4,806,049
Full-time Equivalent	19.00	-3.00	16.00

RIO management believes our agency has operated in a fiscally conservative manner for many years, while maintaining favorable client satisfaction survey scores (for both TFFR and SIB) despite a 38% increase in TFFR membership (from 15,781 in 1998 to 21,853 in 2017) and 80% increase in assets under management (AUM) since 2013. During the last 20-years, RIO's FTE has only grown by 1 person including two new investment professionals in the last 6-years (which coincided with an 80% increase in AUM between 2013 and 2018). RIO's overall performance has generally been strong as evidenced by solid client survey scores while investment performance has generally met or exceeded expectations in recent years including above benchmark returns, favorable peer rankings, and a keen focus on optimizing risk adjusted returns. **SIB clients have benefitted from an excellent return on their investment over the last 5-years as evidenced by a 2-for-1 return on investment fees which conservatively translates into over $300 million of incremental client investment income since 2013.**

RIO Budget Submission – Agency Overview

	A	B	C	D	E	F
	2017-19 Approved Budget	2019-21 Base Budget Request	Option 1 - Reinstate 10% Cuts	Option 2 - TFFR Pension System	Option 3 - Investment Risk Officer	2019-21 Total Budget Request
SALARIES & BENEFITS	**4,425,570**	3,861,563	550,194	50,000	294,996	**4,756,753**
OPERATING	**862,484**	862,484	-	2,789,000	14,450	**3,665,934**
CONTINGENCY	**52,000**	82,000	-	-	-	**82,000**
CAPITAL ASSETS	**-**	-	-	6,300,000	-	**6,300,000**
TOTAL	**5,340,054**	4,806,047	550,194	9,139,000	309,446	**14,804,687**
% Change		-10.0%	10.3%	171.1%	5.8%	177.2%

Column A: RIO's **2017-19 Approved Budget** was for **$5.3 million** (including 19 FTE).

Column B: RIO's **Base Budget** submission of **$4.8 million** reflects a 10% cut in agency expenses as OMB requested.

Column C: **Option 1** - Given RIO's desire to maintain high quality service levels while noting that SIB investments and TFFR's client population are at all-time highs, RIO respectfully seeks to reinstate the 10% OMB budget cut request .

Column D: **Option 2** – Given TFFR's pension administration system is 13-years old and our desire to adopt recent IT system advances, efficiencies and cybersecurity protection levels, we respectfully made a 1-time request for **$9.1 million**.

Column E: **Option 3** – RIO also requests **$309,446** to enhance our investment risk management team, controls and processes by adding a new investment risk officer position to further improve our overall risk management environment.

Column F: RIO's **Total Budget Request for 2019-21** including three (3) optional packages exceeds **$14.8 million**.

RIO's Budget submission is classified at the SIB and TFFR board level on the following page.

RIO Budget Submission – July 20, 2018

TFFR and SIB Component Overview

	2017-19 Approved Budget			2019-21 Base Budget Request			Optional Package #1 Reinstate 10% Cuts		
	TFFR	SIB	RIO	TFFR	SIB	RIO	TFFR	SIB	RIO
SALARIES & BENEFITS	2,325,812	2,099,758	4,425,570	1,956,054	1,905,509	3,861,563	357,628	192,566	550,194
OPERATING	680,124	182,360	862,484	689,424	173,060	862,484	-	-	-
CONTINGENCY	26,000	26,000	52,000	41,000	41,000	82,000	-	-	-
CAPITAL ASSETS	-	-	-	-	-	-	-	-	-
TOTAL	3,031,936	2,308,118	5,340,054	2,686,478	2,119,569	4,806,047	357,628	192,566	550,194
% Change				-11.4%	-8.2%	-10.0%	11.8%	8.3%	10.3%

	Optional Package #2 TFFR Pension Administration			Optional Package #3 Additional FTE - Investment			2019-21 Total Budget Request		
	TFFR	SIB	RIO	TFFR	SIB	RIO	TFFR	SIB	RIO
SALARIES & BENEFITS	50,000	-	50,000	-	294,996	294,996	2,363,682	2,393,071	4,756,753
OPERATING	2,789,000	-	2,789,000	-	14,450	14,450	3,478,424	187,510	3,665,934
CONTINGENCY	-	-	-	-	-	-	41,000	41,000	82,000
CAPITAL ASSETS	6,300,000	-	6,300,000	-	-	-	6,300,000	-	6,300,000
TOTAL	9,139,000	-	9,139,000	-	309,446	309,446	12,183,106	2,621,581	14,804,687
% Change	301.4%	0.0%	171.1%	0.0%	13.4%	5.8%	301.8%	13.6%	177.2%

Optional Package # 2 is a one-time request. *Optional Package # 3 does not materially impact internal investment management costs (e.g. 0.001%).*

RIO Budget Update:

Detailed Narrative and Supporting Documentation

RIO Base Budget Narrative: 10% Cut

In order to meet the 10% overall base budget reduction, RIO carefully reviewed all expenditures to determine areas that could potentially be reduced. After that review, taking into consideration the 13% decrease in the operating line after the 2017 legislative session, it was determined that no additional cuts were possible within the operating line. There were recognized savings in some of the subcategories within operating that were used to reinstate some of the cuts from the previous biennium, but the overall change in the operating line is zero. Some of the larger adjustments were as follows:

IT Data Processing - a reduction of $22,000 or 12.1% from the previous biennium request was possible due mainly to the elimination of the necessity for a second web hosting site for the recently completed Member On-line site for TFFR members.

Postage and Printing - a reduction of nearly $22,000 or 30% from the previous biennium request was possible due to an internal change in the way semi-annual newsletters are delivered to active TFFR members. These newsletters are now delivered electronically, eliminating the need to print and mail them. Additional savings have been realized in this area through increased use of Central Services for printing and mailing of large batches of correspondence, such as 1099R tax statements and annual member statements.

Staff and Board Travel and Professional Development - the savings recognized in the previous subcategories within the operating line have been used to reinstate funds available for staff and board members to travel for out-of-state professional development opportunities. The SIB and TFFR boards place a high priority on ensuring board members are adequately trained in order to properly fulfill their fiduciary responsibilities to their clients and members. As equally important to the boards and management of RIO is the education and training of the RIO staff. This relatively small agency is fiduciarily responsible for a large amount of funds and it is of utmost importance that they keep abreast of all of the industry best practices and evolving regulations and requirements in both the pension and investment communities. Reinstating these funds for travel and professional development will enable these individuals to continue to provide a high level of services to the clients and members of these funds.

Contingency Line - For at least 20 years prior to the 2017 legislative session, RIO had $82,000 appropriated in the contingency line for use by the boards in instances where unforeseen events occurred that had a significant cost. Examples of some of the more recent events (in 2010 and 2013) were costs associated with a consultant hired to assist the SIB in hiring a new Executive Director/CIO for the agency. The cost of these services met or exceeded the amount in the contingency line. During the last legislative session, $30,000 was removed from the contingency line as part of the reductions across most state agencies. RIO is asking that the $30,000 be added back to the contingency line, to restore that line to its historical level.

Salaries & Benefits - In order to meet the requirement of a 10% cut in the base budget, RIO has chosen to submit that cut in the salaries and benefits line. As mentioned earlier, the previous 13% cut to the operating line has made it difficult to find any additional savings in that line. In addition to that fact, the 10% overall reduction, if taken from the operating line, would equate to a 62% cut to the operating line. RIO currently has no vacant positions and has no temporary salary dollars in the current biennium. Board member pay is included in the salaries and benefits line for the statutory $148 per meeting. No specific positions have been indicated for elimination at this point. Over a dozen combinations of position cuts and salary reductions have been considered and most scenarios require a minimum of three positions to be eliminated to reach the 10% unless high level executive positions are included. If ultimately required, RIO will make the decisions on which position(s) to eliminate.

RIO Budget: Option 1 Reinstate 10% Cut

- RIO is a Special Fund Agency; No General Fund dollars are appropriated.
  - Funding for administration of the TFFR Pension Plan comes from Member and Employer Contributions and Investment Earnings
  - Funding for administration of the Investment Program comes directly from Investment Clients' invested assets (both statutory and contracted).
- 83% of RIO's 2017-19 budget is Salaries & Benefits.
- Total FTE count has fluctuated between 17 and 19 over the past 26 years while assets under management have grown by over 200% in the past 10 years and TFFR membership has grown nearly 50% in the past 30 years.
- RIO's Operating line was cut by 13% for the 2017-19 biennium and is currently at $862,484 (0.006% of Assets Under Management)
  - That amount is also 13% lower than the RIO operating budget was 20 years ago.
- To meet the 10% budget reduction requirement, RIO needs to cut $534,005.
  - This equates to 62% of current Operating Line
- Although not required to cut FTE positions (RIO currently has 19 FTEs), in order to meet the 10% budget reduction requirement, the Salaries & Benefits line will need to be reduced.
  - RIO has no vacant positions currently.
  - RIO has no temporary positions in the current biennium budget.
  - Board member pay is included in the Salaries and Benefits Line ($148 per board member per meeting based on statute).
- Over a dozen combinations of position cuts and salary reductions have been considered.
  - Most require a minimum of 3 positions to be eliminated to reach 10% of total budget.
- With a reduction of over 15% or more (3+ FTEs) of RIO's current workforce, the agency's ability to maintain ongoing TFFR pension administration operations and SIB investment management functions would be severely compromised. This would result in:
  - TFFR Program
    - Critical retirement and audit programs, processes, and operations would need to be modified or eliminated. This would result in increased potential for inaccurate TFFR contribution and salary reporting, account maintenance, benefit payment processing, member and employer services and communications, compliance with statutes, and other essential functions.
    - Accuracy, timeliness and quality of benefit payments, communications, and customer service would be negatively impacted.
    - Initiatives intended to continue reinventing TFFR program administration processes would not be possible. For example, upgrading system software and transforming the manner in which members, employers, and staff conduct TFFR business would no longer be feasible, as it would require additional staff during the planning, implementation, and transition phases. This would limit our ability to reduce future costs and operate more efficiently.
  - SIB Program
    - Monitoring and due diligence on existing investments would be reduced and modifications and improvements to portfolios would be less timely, increasing the risk of underperformance due to investment manager issues and non-compliance with client policies.
  - RIO Agency
    - Overall financial and investment reporting would be impacted. Internal controls/segregation of duties would be reduced. Customers would not receive required reports in a timely manner, leading to lower client satisfaction scores. The potential for inaccurate reports and related audit findings would increase.
    - A 15% staff reduction would further negatively impact remaining RIO staff members. Staff retention, recruitment, and morale issues would worsen.

RIO Budget: Option 2 TFFR Pension Admin. System

The TFFR Pension Administration System (PAS) project is summarized in a separate memo given the estimated cost (of $9.1 million) and importance of this "one-time" expenditure.

RIO Budget: Option 3 - Add Investment Risk Officer

As an industry best practice, RIO is currently developing a more robust investment risk management oversight and reporting function within the SIB investment program. Investment risk management is the process of identifying the level of risk that an entity wants, measuring the level of risk that an entity currently has, taking actions that bring the actual level of risk to the desired level, and monitoring the new actual level of risk so that it continues to be aligned with the desired level of risk. The process is continuous and developing an effective framework requires measuring, monitoring, and managing exposure to both economic and fundamental drivers of risk and return across asset classes to avoid over-exposures to common risk factors.

The SIB's current strategic plan includes "enhancing our internal control environment by improving the use of proven risk management solutions" noting that "a robust risk management framework serves as the foundation to support a sound internal control environment and lessen downside risk."

Following an extensive review of leading investment risk management system vendors, RIO selected a solution in 2016 to implement a risk management system across the investment program. The state of the art multi-asset class risk management solution combines sophisticated risk analytics and subject matter expertise to help RIO better understand and manage risk, resulting in more informed investment decisions using the system's tools for portfolio risk, stress testing and scenario analysis; asset allocation analysis; performance and attribution; and compliance and oversight.

RIO continues to work with the vendor to develop a risk dashboard for monitoring downside risk under various historical and hypothetical stress scenarios. Additionally, RIO intends to enhance its investment risk monitoring reports to include an expanded list of key risk metrics. However, current staffing within the investment program is seriously limiting the amount of time available to make these enhancements.

This request is for an additional FTE for the SIB investment program and additional operating expenses related to that position. The tentative title for this new position is Senior Investment Risk Officer and it is anticipated that this position would have the following responsibilities:

- Assist in employing quantitative methods to assess attractiveness of investments
- Provide analysis in key areas including risk monitoring, risk management, and risk/return optimizations
- Provide monitoring and potential investment solutions to the assessment of absolute and/or relative risks
- Provide ex-ante and ex-post risk and return attribution analysis at various levels in the investment structure
- Work collaboratively across functional areas
- Analyze approaches to solving investment problems, quantifying results, and recommending practical implementation approaches
- Work with and understand external vendors' risk applications and methodologies
- Participate in the evaluation and implementation of fund-level, portfolio level, and asset-specific risk management systems such as value-at-risk measurement, aggregate exposure measurement, and credit concentration monitoring

This position would require high-level math skills and advanced analytical and quantitative skills as well as significant Excel and/or programming skills.

Significant highlights in the SIB investment program include the following; however RIO recognizes that our ability to continue achieving these results and reaching the goal of additional risk monitoring or any other enhancements to client services will be highly challenged without the additional FTE.

- SIB client investments have increased by $7.4 billion or 122% in the past 6 years while authorized FTEs assigned to the investment program have remained steady at 6.95.
- Investment returns for the Pension Trust (including PERS and TFFR) improved from the 71st percentile for the last 10-years to the 20th percentile the last 5-years and 13th percentile for the 3-years ended 3/31/2018.
- Legacy Fund investment earnings exceed $1 billion since inception including $373 million for the 11 months ended May 31, 2018. NDCC earnings (transferrable to the General Fund) were $222 million as of May 31.
- Customer satisfaction surveys have remained strong (averaging 3.6 on a 4.0 scale)

VSIP Update

RIO intends to offer its team members the opportunity to participate in the Voluntary Separation Incentive Program (VSIP) in the near future. RIO notes that Cabinet Level agencies rolled out this program on July 9, 2018 (with an end date of August 24, 2018). RIO employees will have 45-days from the offer date to submit a VSIP application for agency consideration.

SIB Client Investment Return Update

Preliminary Return Estimates – Fiscal 2018

- **Pension Trust +9% ($500 million of net income - $5.7 billion AUM)**
  - Asset Allocation – 58% Equity, 23% Fixed Income, 18% Real Assets
  - Equities up 13%; Fixed Income up 3%; and Real Assets up 6%
- **Legacy Fund +7% ($370 million of net income - $5.5 billion AUM)**
  - Asset Allocation – 50% Equity, 35% Fixed Income, 15% Real Assets
  - Equities up 13%; Fixed Income up 1%; and Real Assets up 5%
- **Insurance Trust +5% ($110 million of net income - $2.3 billion AUM)**
  - Allocation – 23% Equity, 54% Fixed Income, 18% Real Assets, 5% Cash
  - Equities up 13%; Fixed Income up 1.5%; and Real Assets up 6%

AUM = Assets Under Management are as of May 31, 2018

Preliminary return estimates are unaudited and subject to change.

State Investment Board
Statement of Net Position
As of 5/31/2018

	As of 5-31-18	As of 6-30-17
ASSETS:		
INVESTMENTS (AT FAIR VALUE)		
DOMESTIC EQUITIES	$ 3,388,322,832	$ 3,002,119,217
GLOBAL/INTERNATIONAL EQUITIES	3,129,298,584	2,867,654,261
DOMESTIC FIXED INCOME	4,602,991,559	3,799,348,243
INTERNATIONAL FIXED INCOME	2,786,478	261,313,883
REAL ASSETS	2,205,672,266	2,069,264,037
PRIVATE EQUITY	178,740,187	167,161,916
INVESTED CASH (NOTE 1)	154,606,643	84,608,146
TOTAL INVESTMENTS	13,662,418,549	12,251,469,703
RECEIVABLES		
DIVIDEND/INTEREST RECEIVABLE	46,129,322	42,601,062
MISCELLANEOUS RECEIVABLE	35,833	26,676
TOTAL RECEIVABLES	46,165,155	42,627,738
OTHER ASSETS		
INVESTED SECURITIES LENDING COLLATERAL (NOTE 2)	55,876,178	77,669,419
OPERATING CASH	224,341	347,866
TOTAL ASSETS	13,764,684,223	12,372,114,726
DEFERRED OUTFLOWS OF RESOURCES		
DEFERRED OUTFLOWS RELATED TO PENSIONS	258,598	314,494
LIABILITIES:		
SECURITIES LENDING COLLATERAL (NOTE 2)	55,876,178	77,669,419
ACCOUNTS PAYABLE	-	254,082
ACCRUED EXPENSES	770,993	826,254
INVESTMENT EXPENSE PAYABLE	6,775,082	6,765,881
TOTAL LIABILITIES	63,422,253	85,515,636
DEFERRED INFLOWS OF RESOURCES		
DEFERRED INFLOWS RELATED TO PENSIONS	41,447	41,447
NET POSITION:		
HELD IN TRUST	13,701,479,121	12,286,872,137
TOTAL NET POSITION	$ 13,701,479,121	$ 12,286,872,137

State Investment Board
Statement of Changes in Net Position
For the Month Ended 5/31/2018

	Month Ended 5-31-18	Year-to-Date
ADDITIONS:		
INVESTMENT INCOME		
GAIN ON SALE OF INVESTMENTS	$ 128,966,241	$ 1,433,269,482
LOSS ON SALE OF INVESTMENTS	85,119,909	1,016,528,056
NET GAINS (LOSSES) INVESTMENTS	43,846,332	416,741,426
NET APPREC (DEPREC) MARKET VALUE	27,356,100	328,369,156
NET CHANGE IN FAIR VALUE OF INVESTMENTS	71,202,432	745,110,582
INTEREST, DIVIDEND & OTHER INVESTMENT INCOME	34,453,387	266,740,150
	105,655,819	1,011,850,732
LESS INVESTMENT EXPENSES	3,093,514	28,579,110
NET INCOME FROM INVESTING ACTIVITIES	102,562,305	983,271,622
SECURITIES LENDING INCOME	130,807	1,338,848
SECURITIES LENDING EXPENSES	26,141	267,554
NET SECURITIES LENDING INCOME	104,666	1,071,294
NET INVESTMENT INCOME		984,342,916
PURCHASE OF UNITS ($1/UNI	146,153,557	907,100,295
TOTAL ADDITIONS	248,820,528	1,891,443,211
DEDUCTIONS:		
ADMINISTRATIVE EXPENSES	140,469	1,448,895
REDEMPTION OF UNITS ($1/U	47,616,248	475,387,332
TOTAL DEDUCTIONS	47,756,717	476,836,227
CHANGE IN NET POSITION	201,063,811	1,414,606,984
NET POSITION:		
BEGINNING OF PERIOD	13,500,415,310	12,286,872,137
END OF PERIOD	$ 13,701,479,121	$ 13,701,479,121

Net investment income exceeds $980 million for the 11 months ended May 31, 2018.

SIB assets exceed $13.7 billion as of May 31, 2018 (up $1.4 billion in fiscal 2018).

LEGACY FUND
Statement of Changes in Net Position
5/31/2018

		Year-to-Date
ADDITIONS:		
INVESTMENT INCOME		
GAIN ON SALE OF INVESTMENTS	$	615,086,366
LOSS ON SALE OF INVESTMENTS		485,687,485
NET GAINS (LOSSES) INVESTMENTS		129,398,881
NET APPREC (DEPREC) MARKET VALUE		149,845,251
NET CHANGE IN FAIR VALUE OF INVESTMENTS		279,244,132
INTEREST, DIVIDEND & OTHER INVESTMENT INCOME		103,578,774
		382,822,906
LESS INVESTMENT EXPENSES		10,310,977
NET INCOME FROM INVESTING ACTIVITIES		372,511,929
SECURITIES LENDING INCOME		703,862
SECURITIES LENDING EXPENSES		140,658
NET SECURITIES LENDING INCOME		563,204
NET INVESTMENT INCOME		373,075,133
PURCHASE OF UNITS ($1/UNIT) (NOTE 3)		471,022,591
TOTAL ADDITIONS		844,097,724
DEDUCTIONS:		
ADMINISTRATIVE EXPENSES		568,624
REDEMPTION OF UNITS ($1/UNIT) (NOTE 4)		-
TOTAL DEDUCTIONS		568,624
CHANGE IN NET POSITION		843,529,100
NET POSITION:		
BEGINNING OF PERIOD		4,685,637,731
END OF PERIOD	$	5,529,166,831

1) The Legacy Fund increased to over $5.5 billion as of May 31, 2018 (versus $4.7 billion as of June 30, 2017).

2) Legacy Funds "Net Investment Income" exceeded $373 million for the 11 months ended May 31, 2018.

3) NDCC 21-10-02 defines "earnings" as net income in accordance with generally accepted accounting principles excluding any unrealized gains or losses. These transferrable "earnings" approximated $222.6 million for the 11 months ended May 31, 2018.

EARNINGS AVAILABLE

Section 26 of Article X of the Constitution of North Dakota dictates that earnings of the Legacy Fund accruing after June 30, 2017, shall be transferred to the general fund at the end of each biennium. Earnings accrued prior to June 30, 2017, become part of the principal of the fund.

NDCC 21-10-12 defines "earnings" for the purposes of Section 26, Article X as "net income in accordance with generally accepted accounting principles, excluding any unrealized gains or losses."

As of the date of these financial statements, the principal balance of the Legacy Fund is $ 4,848,487,495

As of the date of these financial statements, earnings of the Legacy Fund eligible for transfer to General Fund at the end of the biennium is $ 222,661,258

RIO Strategy Review - Agenda VI.B.

Great State of North Dakota

Strategy Review

North Dakota Retirement & Investment Office
Teachers' Fund for Retirement
State Investment Board

David Hunter, Executive Director/CIO
Fay Kopp, Deputy Executive Director/CRO
Darren Schulz, Deputy CIO
Connie Flanagan, Fiscal & Investment Operations Manager


EMPOWER PEOPLE
IMPROVE LIVES
INSPIRE SUCCESS

5 STRATEGIC INITIATIVES

← CORE AGENCY MISSIONS →

5 CULTURAL ASPIRATIONS

Citizen Focused

Growth Mindset

Leadership Everywhere

Work As One

Make A Difference

Discussion Topics

- Current State
- Reinvention
- Future State

Current State - Agency

North Dakota Retirement & Investment Office
Teachers' Fund for Retirement
State Investment Board

Retirement and Investment Office (RIO)

The Retirement and Investment Office (RIO) was created by the 1989 Legislative Assembly to capture administrative and investment cost savings in the management of two important long-standing state programs - the retirement program of the Teachers' Fund for Retirement (TFFR) and the investment program of the State Investment Board (SIB).

TFFR is a qualified defined benefit public pension plan for over 20,000 active and retired North Dakota public school teachers and administrators.

The SIB is responsible for the investment of nearly $14 billion in client assets for the Legacy Fund, seven pension funds (including TFFR and PERS), WSI, the Budget Stabilization Fund and 15 other non-pension funds.

RIO exists in order that:

- SIB clients receive investment returns, consistent with their written investment policies and market variables, in a cost effective manner and under the Prudent Investor Rule.
- Potential SIB clients have access to information regarding the investment services provided by the SIB.
- TFFR benefit recipients receive their retirement benefits in a cost effective and timely manner.
- TFFR members have access to information which will allow them to become knowledgeable about the issues and process of retirement.
- SIB clients and TFFR benefit recipients receive satisfactory services from the boards and staff of the office.

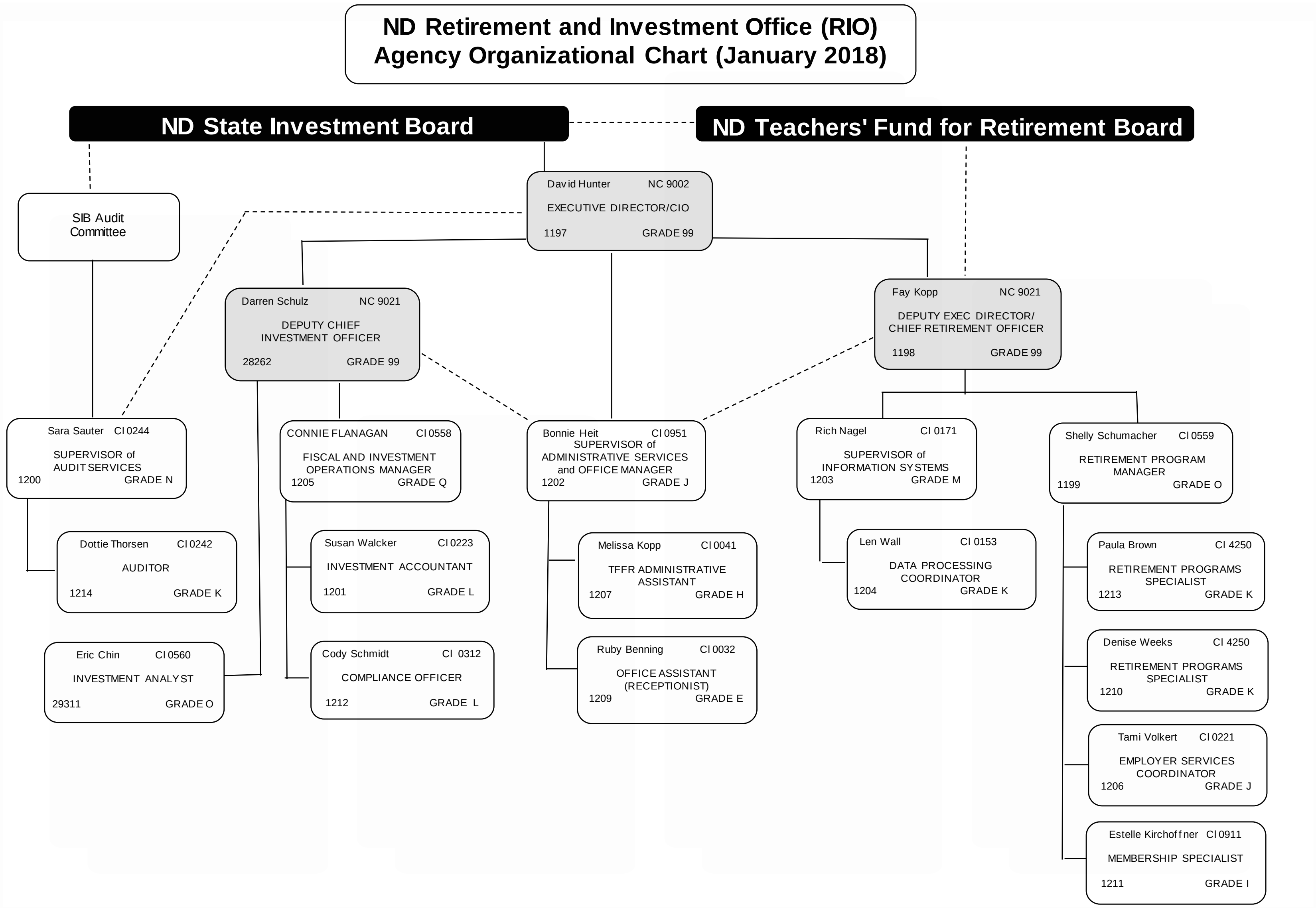
RIO Strategic Goals

- Deliver top tier retirement benefit services and investment management oversight at below market rates. (Example: SIB internal investment management costs approximate 0.01% per annum which compares favorably with most other comparable public pension plans which generally range from 0.01% to 0.02%.)
- Empower RIO team members to be leaders in their chosen field and reward this achievement by increasing compensation levels to median market rates at a minimum (for delivering top tier services at or below market rates).
- Engage with Legislative Leaders and the Executive Branch by working together to deliver effective and efficient solutions to meet, if not exceed, the needs and expectations of our citizens and constituents.

Current State – Agency

- RIO is a Special Fund Agency; No General Fund dollars are appropriated
  - Funding for administration of the **TFFR Pension Plan** comes from Member and Employer Contributions and Investment Earnings
    - Actual appropriated costs for the administration of the TFFR Pension Plan have averaged 8 basis points (0.08%) of fund investment value over the past 10 years. (10.1 basis points if administrative costs covered under continuing appropriation are included.)
    - The average cost of administration of other public pension plans polled was 8-15 basis points.
  - Funding for administration of the **Investment Program** comes directly from Investment Clients' invested assets (both statutory and contracted).
    - Actual costs are simply passed through to clients based on their pro-rata share of those expenses (based on AUM).
    - Actual appropriated costs for the administration of the SIB Investment Program have averaged 1 basis point (0.01%) of total assets under management (AUM) over the past 10 years. (1.2 basis points if administrative costs covered under continuing appropriation are included.)
    - The average cost of administration of other state investment programs polled was 1-2 basis points.

Current State – Agency



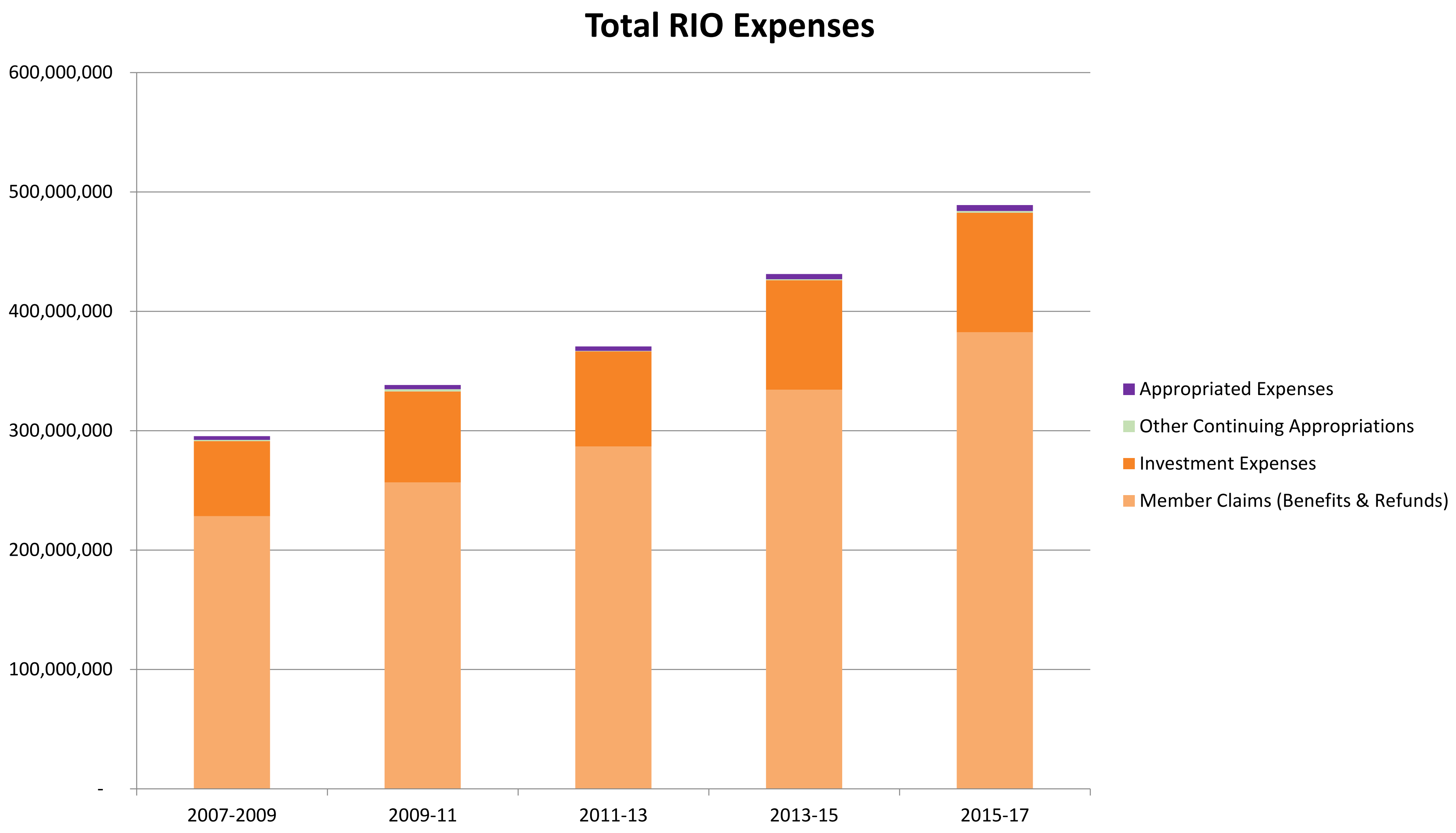
Current State – Agency

Appropriated expenses are only a small fraction of the total expenses of RIO. The following table shows actual total expenses paid in FY2017.

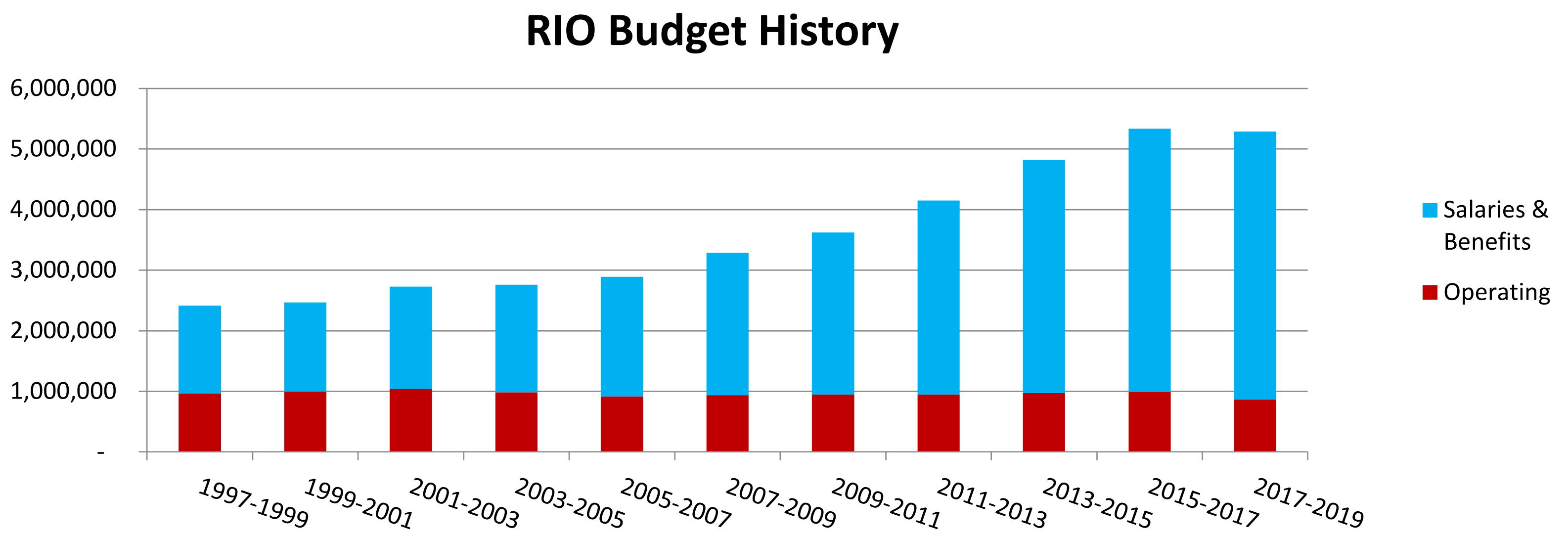
	TFFR		SIB		Total RIO	
	Actual Expenses	% of Total	Actual Expenses	% of Total	Actual Expenses	% of Total
CONTINUING APPROPRIATIONS						
INVESTMENT EXPENDITURES	$ 13,111,481	6.2%	$ 41,353,940	97.4%	$ 54,465,421	21.4%
MEMBER CLAIMS						
ANNUITY PAYMENTS	191,104,694		-		191,104,694	
REFUND PAYMENTS	5,411,850		-		5,411,850	
TOTAL MEMBER CLAIMS	196,516,544	92.8%	-	0.0%	196,516,544	77.3%
OTHER CONTINUING APPROPRIATIONS	415,576	0.2%	187,578	0.4%	603,154	0.2%
TOTAL CONTINUING APPROPRIATIONS	210,043,601	99.2%	41,541,518	97.8%	251,585,119	98.9%
APPROPRIATED EXPENDITURES						
SALARIES AND BENEFITS	1,135,689	0.5%	1,038,489	2.4%	2,174,178	0.9%
OPERATING EXPENSES	400,350	0.2%	101,981	0.2%	502,331	0.2%
CAPITAL ASSETS	8,999	0.0%	-	0.0%	-	0.0%
SIB EXPENSES ALLOCATED TO TFFR	221,816		(221,816)		-	
TOTAL APPROPRIATED EXPENDITURES	1,766,854	0.8%	918,654	2.2%	2,676,509	1.1%
TOTAL EXPENDITURES	$ 211,810,455		$ 42,460,171		$ 254,261,628	

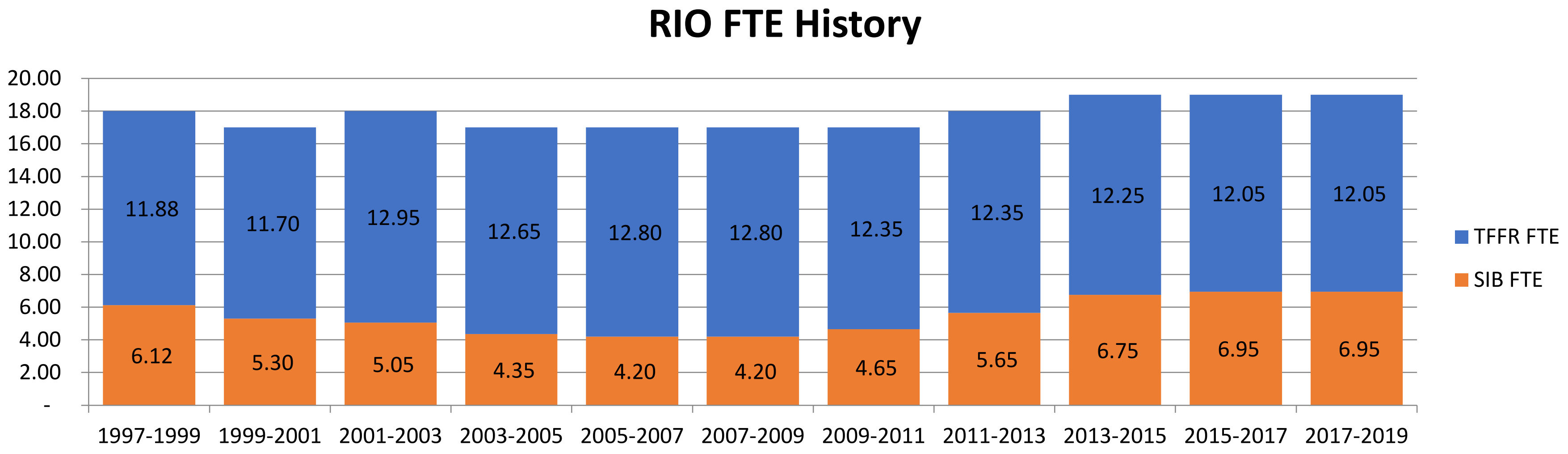
Other continuing appropriations per NDCC 21-10-06.2 and 15-39.1-05.2 include investment and fiduciary consulting services (actuary, audit, legal) as well as investment due diligence travel costs and other investment related expenses not directly attributable to investment managers.

Current State – Agency



Current State – Agency





North Dakota Retirement & Investment Office
Teachers' Fund for Retirement
State Investment Board

Current State – Agency

North Dakota Retirement & Investment Office
›Teachers' Fund for Retirement
›State Investment Board

Successes

- Operating Line of budget has decreased by 9.2% over the past 5 biennia and 13.1% over the past 10 biennia
- 83% of RIO budget is Salaries & Benefits
  - Average years of service of total RIO Staff is 17 years
  - Average years of service of RIO management staff is 17.6 years
  - Generally low overall staff turnover
- Annual Staff Survey
  - RIO has conducted an annual survey since 2014 to gauge staff satisfaction and morale.
  - Survey used in 2017 was the statewide survey developed for cabinet level agencies, modified for RIO.
  - Overall results have remained fairly consistent (between 2.7 and 2.9 on a 3.0 scale).
  - RIO results match the results of the statewide survey very closely, showing areas of most concern are communication and compensation.
- RIO has received the Certificate of Achievement in Financial Reporting from the Government Finance Officers' Association (GFOA) on its annual financial report for 20 consecutive years (as of 6/30/17 report)
- RIO has received unqualified/unmodified audit opinions on its annual financial statements since inception in FY1990.
- RIO has not had an audit finding/recommendation since FY2009.

Challenges

- Over 30% (6) of current staff will be retirement eligible by end of current biennium and another 10% (2) by 6/30/21.
  - 50% of those eligible to retire are in management positions
  - Potentially over 200 years of institutional knowledge will be lost over next 3-5 years.
- Succession planning
- Current budget reductions are limiting resources (funding and staffing) to make technology advances in areas such as website upgrades, disaster recovery and investment portfolio risk management.

Current State – Programs - SIB

State Investment Board (SIB)

Fundamental Investment Beliefs

Asset allocation decisions are the primary driver of investment returns, but the prudent use of active investment management is an important contributor towards ensuring our clients attain their stated investment objectives. All investment decisions are driven by our desire to maximize risk adjusted returns based on our clients stated risk appetite and liquidity profile.

- SIB clients generated over $300 million of incremental income via the prudent use of active management the last 5 years including over $120 million of incremental income in 2017.

Strategic Investment Plan

1. Reaffirm our organizational commitment to the importance of continuing board education and strong board governance.
2. Enhance understanding of our core goals and beliefs while enhancing overall transparency.
    a. Remain steadfast in our commitment to the prudent use of active investment management.
    b. Expand awareness to downside risk management which is essential to achieving our long term investment goals.
    c. Given actual and projected growth of SIB client assets and the heightened public awareness of the Legacy Fund, align our investment platforms to promote greater clarity and efficiency in reporting and implementing client investment policies.
3. Expand RIO's influence and ability to create positive and sustainable change by building deeper relationships with existing clients, organizations and legislative leaders.
    a. Enhance community outreach to build upon public awareness and confidence.
    b. Develop concise presentations which highlight our overall risk, return and cost control framework including our progress towards attaining our long-term goals.

Current State – Programs – SIB

North Dakota Retirement & Investment Office
Teachers' Fund for Retirement
State Investment Board

State Investment Board (SIB)

<u>Strategic Investment Plan (continued)</u>

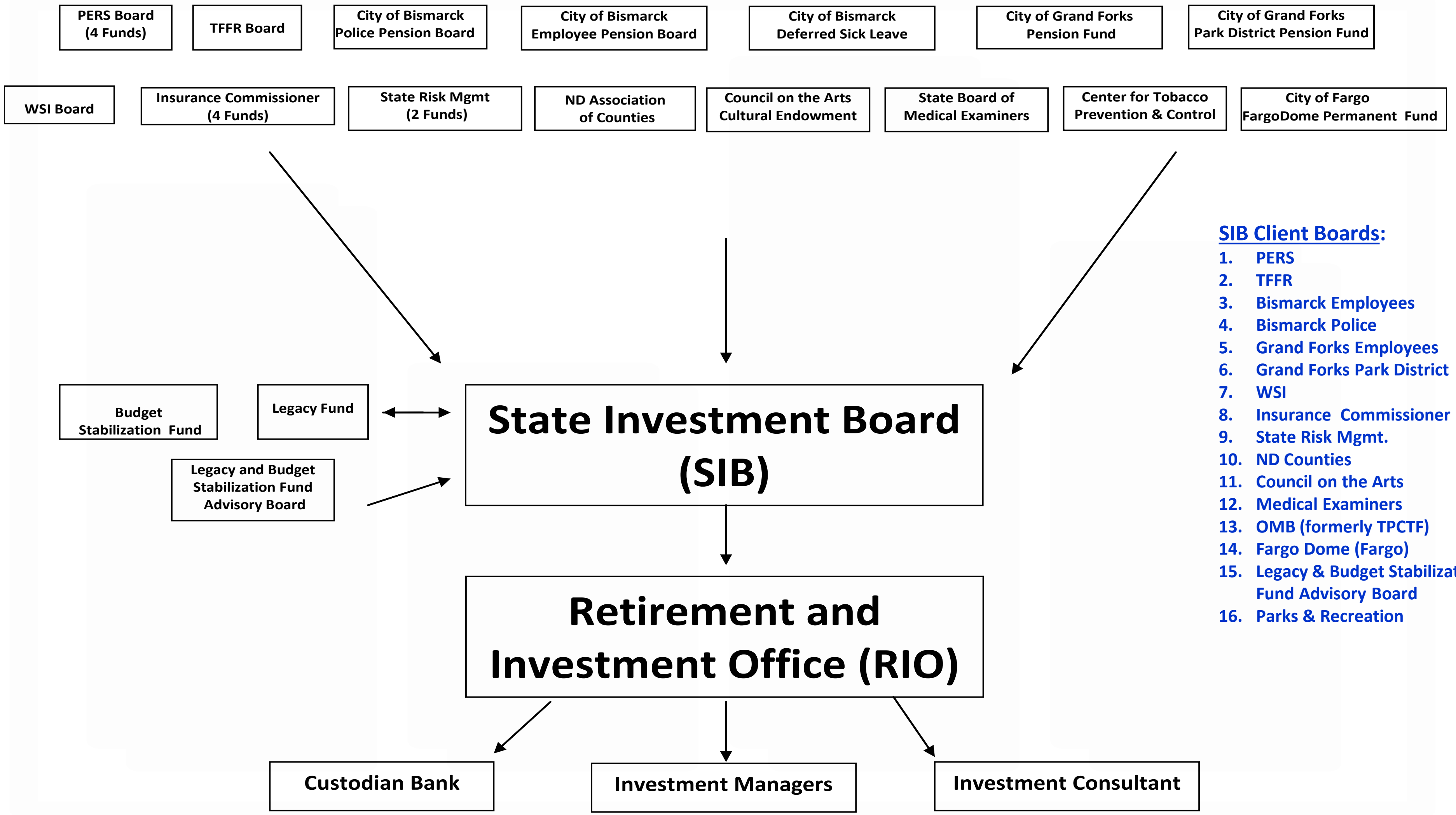
4. Heighten employee engagement by promoting an open and collaborative work environment while encouraging employee participation in staff meetings, offer team members more opportunities to impact RIO's change initiatives and improve the office environment for staff and clients.
    a. RIO's ability to continue to deliver strong results is dependent on the combined efforts of our highly valuable team members.
5. Enhance our internal control environment by improving use of proven risk management solutions relating to fraud risk assessments, investment risk management and overall enterprise risk management.
    a. A robust risk management framework serves as a foundation to support a sound internal control environment and lessen downside risks.
    b. Broaden stakeholder awareness of the challenges faced in estimating Legacy Fund earnings for any given period.
6. Evaluate and expand the efficient use of technology in our investment program activities including risk management, compliance monitoring, client satisfaction surveys, website design and communications in order to increase overall efficiency and effectiveness.

No legislative studies going on this biennium. Policy implementation relates to the Legacy Fund.

- 2017-19 biennium is first time Legacy Fund earnings will be transferred to General Fund.
- RIO investment staff have met with OMB and Treasurer's Office staff, as well as Legislative Council staff, to plan for the timing and methodology of this transfer. Legacy Fund earnings in the amount of $200 million were appropriated for use in this biennium but will not be transferred until the end of the biennium per State Constitution language. Actual amount of transfer will not be known until end of biennium.

Current State – Programs – SIB

North Dakota Retirement & Investment Office
›Teachers' Fund for Retirement
›State Investment Board



SIB Client Boards:

1. PERS
2. TFFR
3. Bismarck Employees
4. Bismarck Police
5. Grand Forks Employees
6. Grand Forks Park District
7. WSI
8. Insurance Commissioner
9. State Risk Mgmt.
10. ND Counties
11. Council on the Arts
12. Medical Examiners
13. OMB (formerly TPCTF)
14. Fargo Dome (Fargo)
15. Legacy & Budget Stabilization Fund Advisory Board
16. Parks & Recreation

Current State – Programs – SIB

North Dakota Retirement & Investment Office
›Teachers' Fund for Retirement
›State Investment Board

Client Responsibilities: (Per NDCC 21-10-02.1) The governing body of each fund shall establish policies on investment goals, objectives and asset allocation that must include:

- Acceptable rates of return, liquidity and levels of risk
- Long-range asset allocation goals

State Investment Board Responsibilities: (Per NDCC 21-10):

- Accept and implement client asset allocations
- Apply Prudent Investor Rule when investing for fund under its supervision
- Approve general types of securities for investment
- Set policies and procedures regulating securities transactions on behalf of clients
- Select custodian servicer, investment director and/or investment consultant
- Create investment pools

Retirement and Investment Office Staff Responsibilities (on behalf of SIB):

- Administer overall investment strategy
- Advise SIB on ways to maximize risk/return opportunities within each asset class
- Act as liaison between SIB and managers, consultant and custodian
- Monitor individual clients' investment guidelines and asset allocations
- Maintain separate accounting for client accounts

Current State – Programs – SIB

Investment Manager Responsibilities:

- Accept and implement specific mandates or "investment missions"
- Make buy/sell decisions based on investment guidelines
- Report to RIO Staff on regular basis
- Provide education to SIB

Custodian Bank Responsibilities:

- Safe-keep assets
- Settle trades
- Recordkeeper

Investment Consultant Responsibilities:

- Performance measurement of investment managers
- Manager search assistance
- Provide education to SIB including special projects

Others Experts:

- Legal Counsel
- Independent Actuaries and Auditors
- Specialists in custody and fee reviews and/or transaction cost analyses

Current State – Programs – SIB

North Dakota Retirement & Investment Office
›Teachers' Fund for Retirement
›State Investment Board

Highlights

- Investment returns for the Pension Trust (including PERS and TFFR) improved from the 71st percentile for the last 10-years to the 20th percentile the last 5-years and 13th percentile for the 3-years ended 3/31/2018.
- RIO conservatively estimates the SIB's use of active management has generated $300 million of incremental income for clients over the last 5-years (e.g. $10 billion x 0.60% x 5 years = $300 million) including $100 million for the 1-year ended March 31, 2018.
- The SIB's commitment to developing strategic partnerships with major institutional investment firms have paid significant dividends and reduced fees (as a % of investments) from 0.65% in 2013 to 0.46% in 2017. This 0.19% reduction translates into over $20 million of annual fee savings. The SIB earns more than a 2-for-1 return on every $1 spent on investment fees.
- Legacy Fund investment earnings exceed $1 billion since inception including $329 million for the 10 months ended April 30, 2018. NDCC earnings (transferrable to the General Fund) were $188 million as of April 30.
- Customer satisfaction surveys
    - SIB client satisfaction survey scores remain strong at 3.6 (on a 4.0 scale).
    - Client satisfaction surveys are sent out annually to all investment clients as part of the annual evaluation of the SIB "Ends" governance policies.
    - Rating factors include promptness and professionalism of staff, clarity and effectiveness of communications/reports, and knowledge of investment.
    - Additional feedback is requested regarding how service can be improved.

Lowlights

- Current budget reductions are limiting resources (funding and staffing) to make technology advances.

Current State - Programs – SIB

North Dakota Retirement & Investment Office
›Teachers' Fund for Retirement
›State Investment Board

State Investment Board – Client Assets Under Management

Fund Name	Market Values as of 3/31/18 (1)
Pension Trust Fund	
Teachers' Fund for Retirement (TFFR)	$ 2,466,427,925
Public Employees Retirement System (PERS)	2,999,335,828
City of Bismarck Employees Pension	98,280,546
City of Bismarck Police Pension	39,741,400
City of Grand Forks Employees Pension	64,240,952
Park District of the City of Grand Forks Pension	6,622,154
Subtotal Pension Trust Fund	5,674,648,805
Insurance Trust Fund	
Workforce Safety & Insurance (WSI)	1,925,297,355
State Fire and Tornado Fund	22,869,464
State Bonding Fund	3,411,679
Petroleum Tank Release Compensation Fund	6,466,968
Insurance Regulatory Trust Fund	1,924,358
State Risk Management Fund	5,244,793
State Risk Management Workers Comp Fund	5,278,321
Cultural Endowment Fund	454,379
Budget Stabilization Fund	38,323,931
ND Association of Counties (NDACo) Fund	5,871,740
Bismarck Deferred Sick Leave Account	726,168
City of Fargo FargoDome Permanent Fund	43,891,602
State Board of Medicine Fund	2,231,656
PERS Group Insurance Account	33,474,017
Lewis & Clark Interpretive Center Endowment	700,060
Subtotal Insurance Trust Fund	2,096,166,489
Legacy Trust Fund	5,375,052,531
Job Service of North Dakota Pension	96,405,170
Tobacco Control and Prevention Fund	54,065,143
PERS Retiree Health Insurance Credit Fund	125,145,623
Total Assets Under SIB Management	$ 13,421,483,761

(1) Market values are unaudited and subject to change.

- **SIB client investments exceeded $13.4 billion as of March 31, 2018,** with the Pension Trust exceeding $5.6 billion, Insurance Trust nearing $2.1 billion and Legacy Fund approaching $5.4 billion.
- **The Pension Trust posted a net return of 12.3% in the last year.** During the last 5-years, the Pension Trust generated a net annualized return of 8.3%, exceeding the performance benchmark of 7.3%.
- **The Insurance Trust generated a net return of 7.5% in the last year.** During the last 5-years, the Insurance Trust posted a net annualized return of 5.0%, exceeding the performance benchmark of 3.7%.
- **Legacy Fund generated a net return of 10.2% last year, exceeding its policy benchmark.** During the last 5-years, Legacy Fund earned a net annualized return of 5.8%, exceeding the performance benchmark of 4.8%.
- **RIO conservatively estimates the SIB use of active management enhanced client returns by over $300 million since March 31, 2013** (e.g. $10 billion x 0.60% = $60 million x 5 years = $300 million).
- **If SIB managers outperform their benchmark by 0.01% (or 1 basis point), after all fees & expenses, client returns improve by $1.3 million per year** (e.g. $13 billion x 0.01% = $1.3 million).
- **RIO's <u>internal</u> investment cost for administering the investment programs for our SIB clients is less than 1 basis point or 0.01% (i.e. less than 1/100th of 1%).**

Current State – Programs – SIB

North Dakota Retirement & Investment Office
›Teachers' Fund for Retirement
›State Investment Board

Investment performance vs benchmarks

- Per SIB Client Investment Policy, the total fund return, net of fees, should at least match the return of the policy benchmark over a minimum evaluation period of five years. The following table details the results for the five years ended March 31, 2018.

Fund Name	Total Fund Actual (Net)	Total Fund Benchmark
Pension Trust Fund		
Teachers' Fund for Retirement (TFFR)	8.33%	7.28%
Public Employees Retirement System (PERS)	8.34%	7.30%
City of Bismarck Employees Pension	7.52%	6.47%
City of Bismarck Police Pension	7.78%	6.78%
City of Grand Forks Employees Pension	8.24%	7.45%
Park District of the City of Grand Forks Pension	8.42%	7.52%
Insurance Trust Fund		
Workforce Safety & Insurance (WSI)	5.98%	4.43%
State Fire and Tornado Fund	6.33%	4.93%
State Bonding Fund	2.18%	1.17%
Petroleum Tank Release Compensation Fund	2.02%	1.09%
Insurance Regulatory Trust Fund	4.85%	3.99%
State Risk Management Fund	6.49%	5.07%
State Risk Management Workers Comp Fund	7.23%	5.87%
Cultural Endowment Fund	8.80%	7.64%
Budget Stabilization Fund	1.31%	0.62%
ND Association of Counties (NDACo) Fund	5.66%	4.32%
Bismarck Deferred Sick Leave Account	6.06%	4.46%
City of Fargo FargoDome Permanent Fund	7.75%	6.39%
State Board of Medicine Fund	*	*
PERS Group Insurance Account	0.36%	0.41%
Lewis & Clark Interpretive Center Endowment	*	*
Legacy Fund	5.82%	4.75%
Job Service of North Dakota Pension	6.00%	5.29%
Tobacco Control and Prevention Fund	*	*
PERS Retiree Health Insurance Credit Fund	7.56%	7.63%

* These funds do not have the specified periods of history under SIB management.

The vast majority of SIB clients (98%) are surpassing agreed upon performance benchmarks for the 1, 3, 5 and 7 years ended March 31, 2018 (based on AUM).

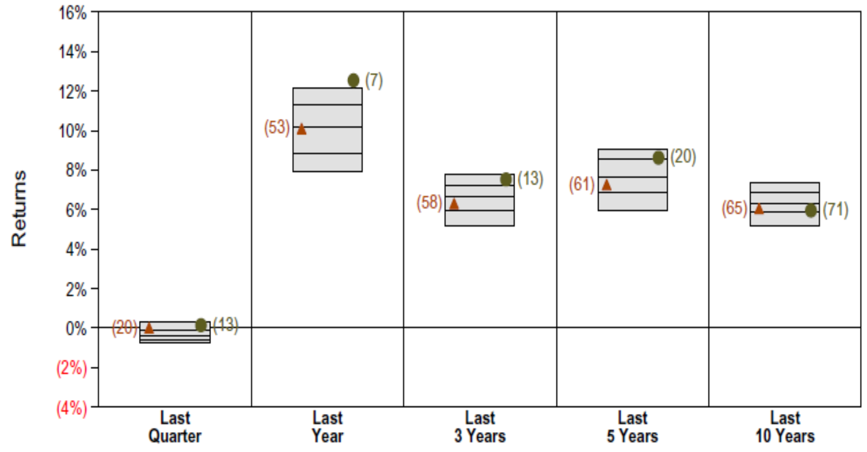
Current State - Programs – SIB

North Dakota Retirement & Investment Office
›Teachers' Fund for Retirement
›State Investment Board

ND Pension Trust Peer Rankings have improved from the 71st percentile in the Last 10 Years to the 20th Percentile for the Last 5 Years and 13th percentile in the Last 3 Years based on Callan's Public Fund Sponsor Database (left chart).

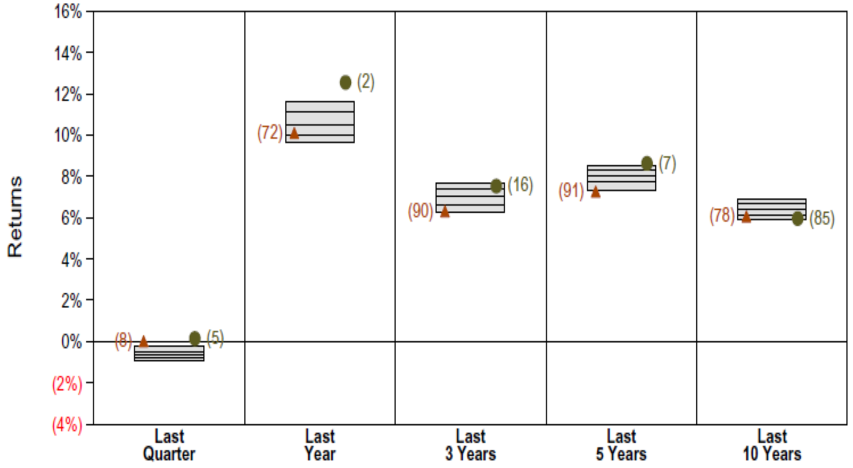
Total Fund Ranking – The following charts show the ranking of North Dakota's Pension Trust (including PERS and TFFR) performance relative to that of the Callan Public Fund Sponsor Database for the periods ended March 31, 2018. The left chart is a standard unadjusted ranking. In the right chart, each fund in the database is adjusted to have the same historical asset allocation of ND.

Callan Public Fund Sponsor Database



	Last Quarter	Last Year	Last 3 Years	Last 5 Years	Last 10 Years
10th Percentile	0.30	12.18	7.75	9.08	7.39
25th Percentile	(0.08)	11.29	7.21	8.55	6.85
Median	(0.39)	10.21	6.66	7.67	6.33
75th Percentile	(0.62)	8.84	5.96	6.86	5.87
90th Percentile	(0.75)	7.95	5.16	5.95	5.15
Total Fund ●	0.14	12.54	7.52	8.62	5.95
Policy Target ▲	0.01	10.10	6.30	7.26	6.05

Asset Allocation Adjusted Ranking



	Last Quarter	Last Year	Last 3 Years	Last 5 Years	Last 10 Years
10th Percentile	(0.21)	11.58	7.66	8.54	6.88
25th Percentile	(0.48)	11.15	7.35	8.30	6.67
Median	(0.67)	10.46	7.03	8.01	6.39
75th Percentile	(0.80)	10.02	6.60	7.71	6.09
90th Percentile	(0.92)	9.65	6.29	7.32	5.91
Total Fund ●	0.14	12.54	7.52	8.62	5.95
Policy Target ▲	0.01	10.10	6.30	7.26	6.05

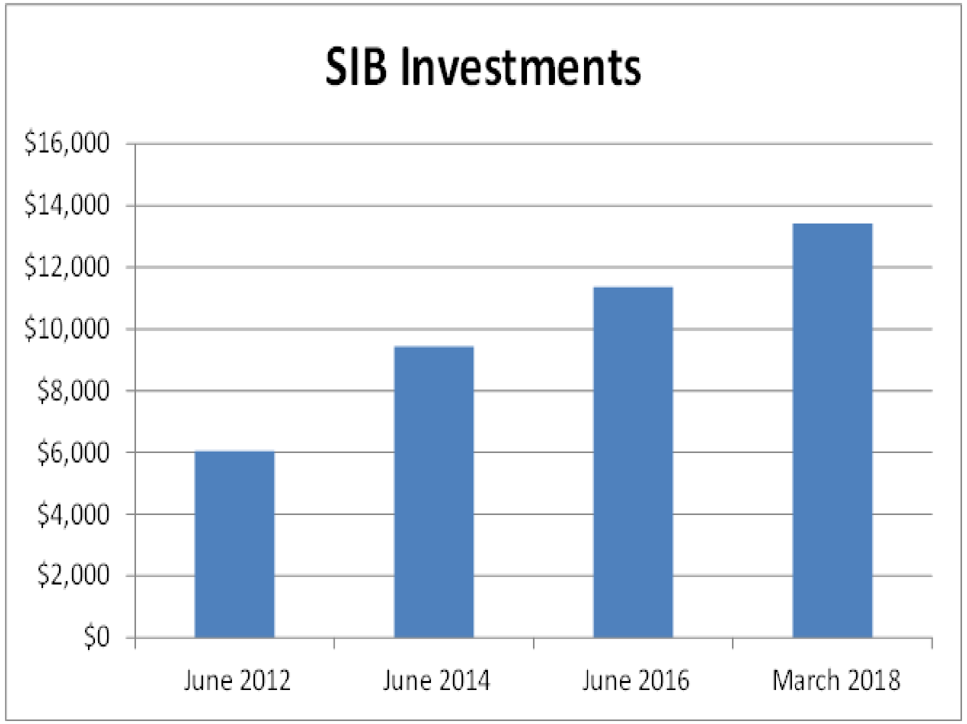
* Current Quarter Target = 16.3% Blmbg Aggregate, 16.1% Russell 1000 Index, 16.0% MSCI World, 11.2% MSCI World ex US, 10.5% NCREIF Total Index, 7.0% Blmbg HY 2% Iss Cap, 6.5% NDSIB PEN - Private Equity, 5.7% CPI-W, 4.9% Russell 2000 Index, 3.1% MSCI EM, 2.3% NCREIF Timberland Index and 0.4% 3-month Treasury Bill.

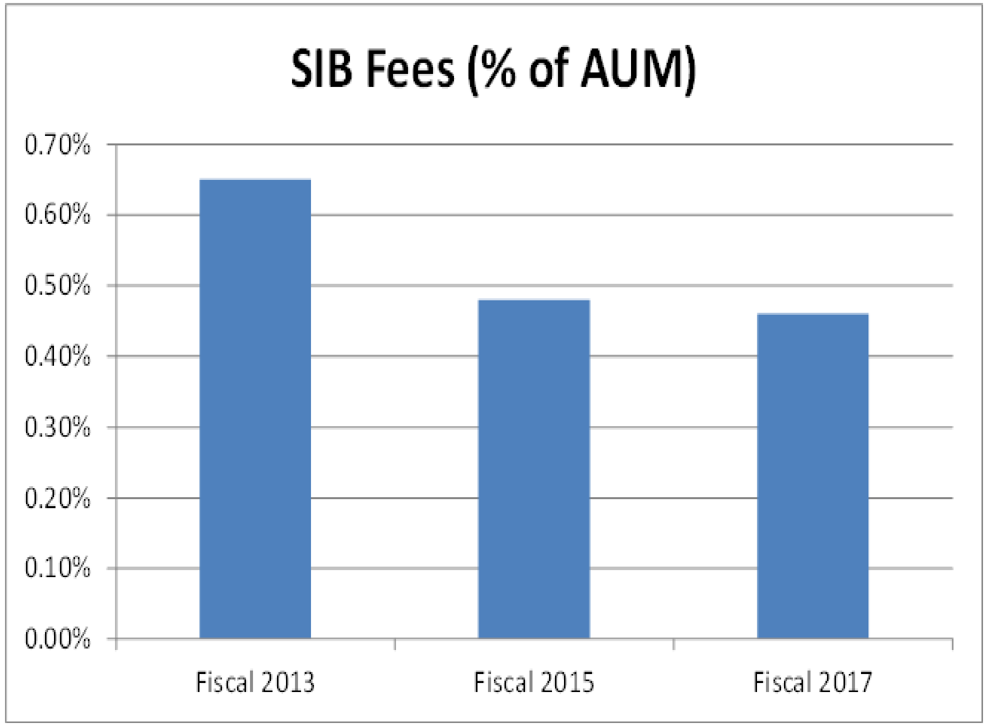
Current State - Programs – SIB

North Dakota Retirement & Investment Office
›Teachers' Fund for Retirement
›State Investment Board

SIB investments have increased by 120% from \$6 billion in 2012 to over \$13 billion in 2018. RIO's FTE budget has remained at 19 positions despite this significant asset growth, while SIB client satisfaction scores remain strong.

SIB Fees have declined by nearly 30% from 0.65% in Fiscal 2013 to 0.46% in Fiscal 2017. Based on \$13 billion of AUM, this 0.19% reduction translates into over \$24 million of annual fee savings (e.g. \$13 billion x 0.19% = \$24.7 million).

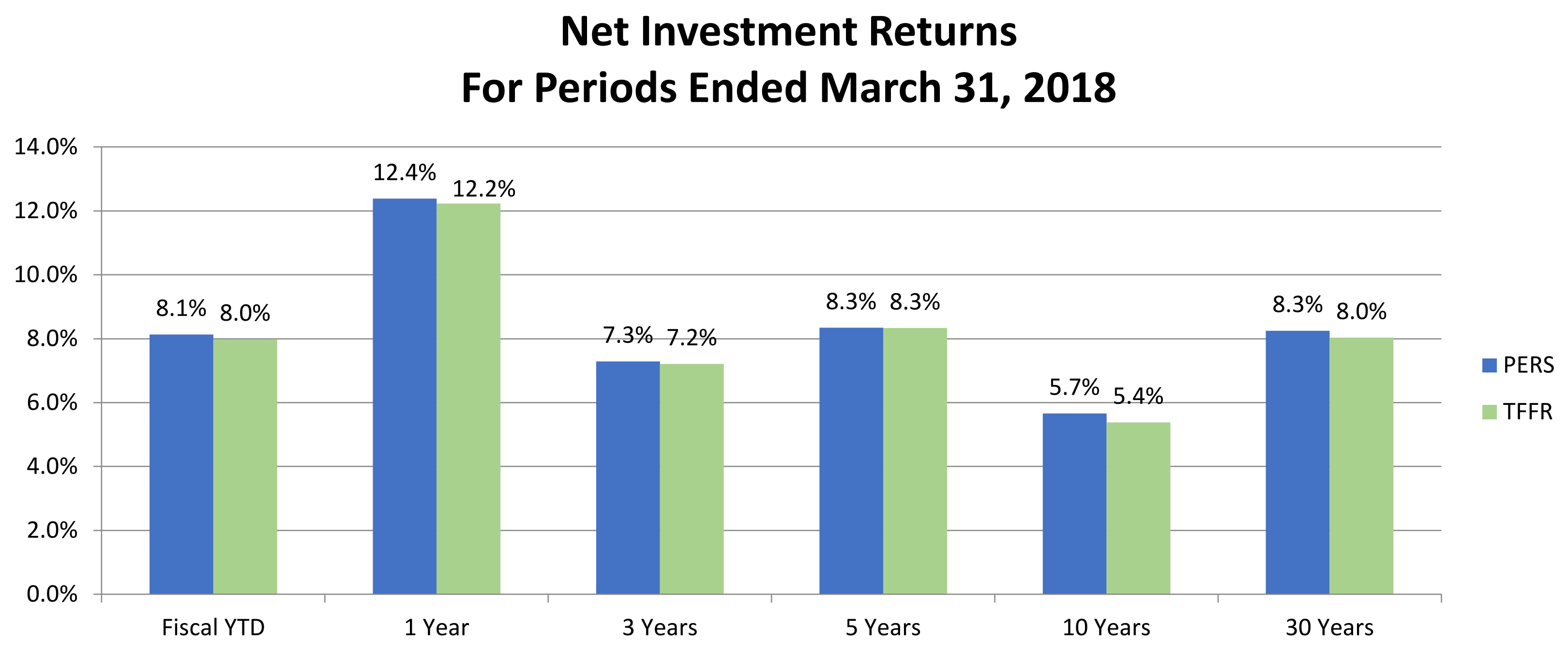




Current State - Programs – SIB

North Dakota Retirement & Investment Office
›Teachers' Fund for Retirement
›State Investment Board

TFFR and PERS – Net Investment Return Update



Interim Investment Update as of April 30, 2018:

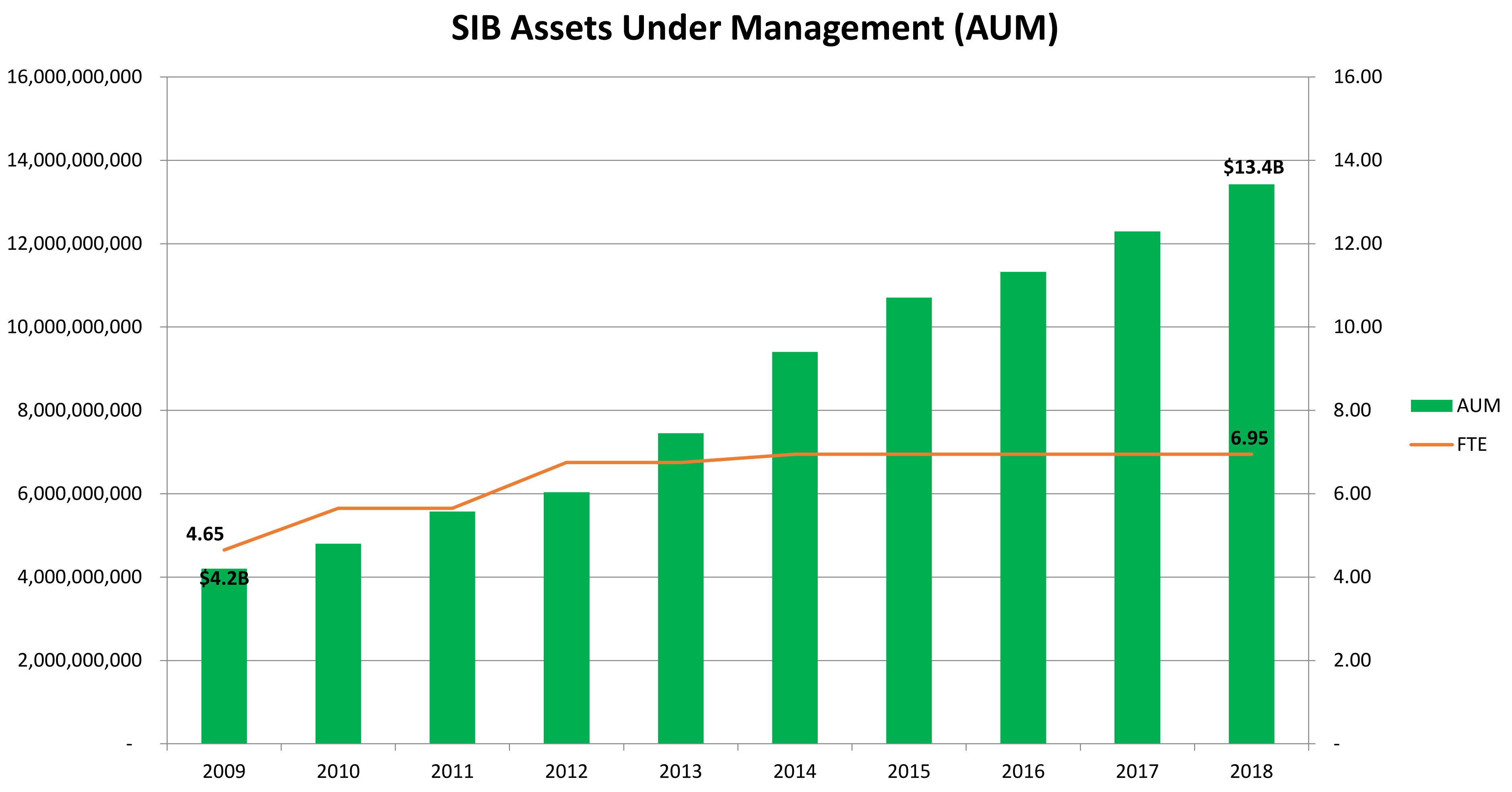
TFFR and PERS net investment returns are estimated to approximate 8% for the 10 months ended April 30, 2018.

These estimates are deemed to be materially accurate, but are unaudited and subject to change.

RIO estimates that actual net returns exceed their policy benchmarks by approximately 1% for the 10 months ended April 30, 2018.

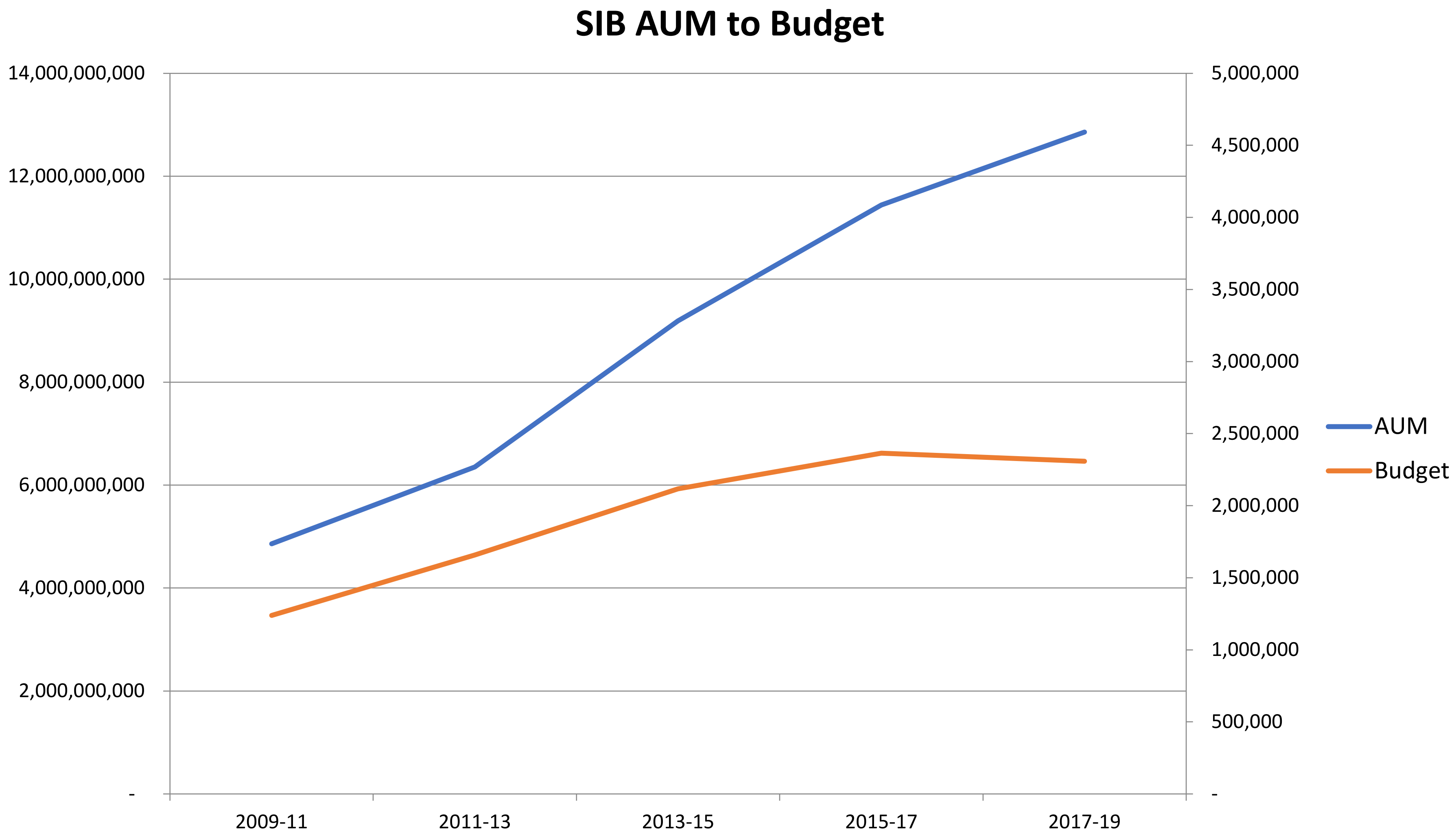
Current State – Programs – SIB

North Dakota Retirement & Investment Office
›Teachers' Fund for Retirement
›State Investment Board



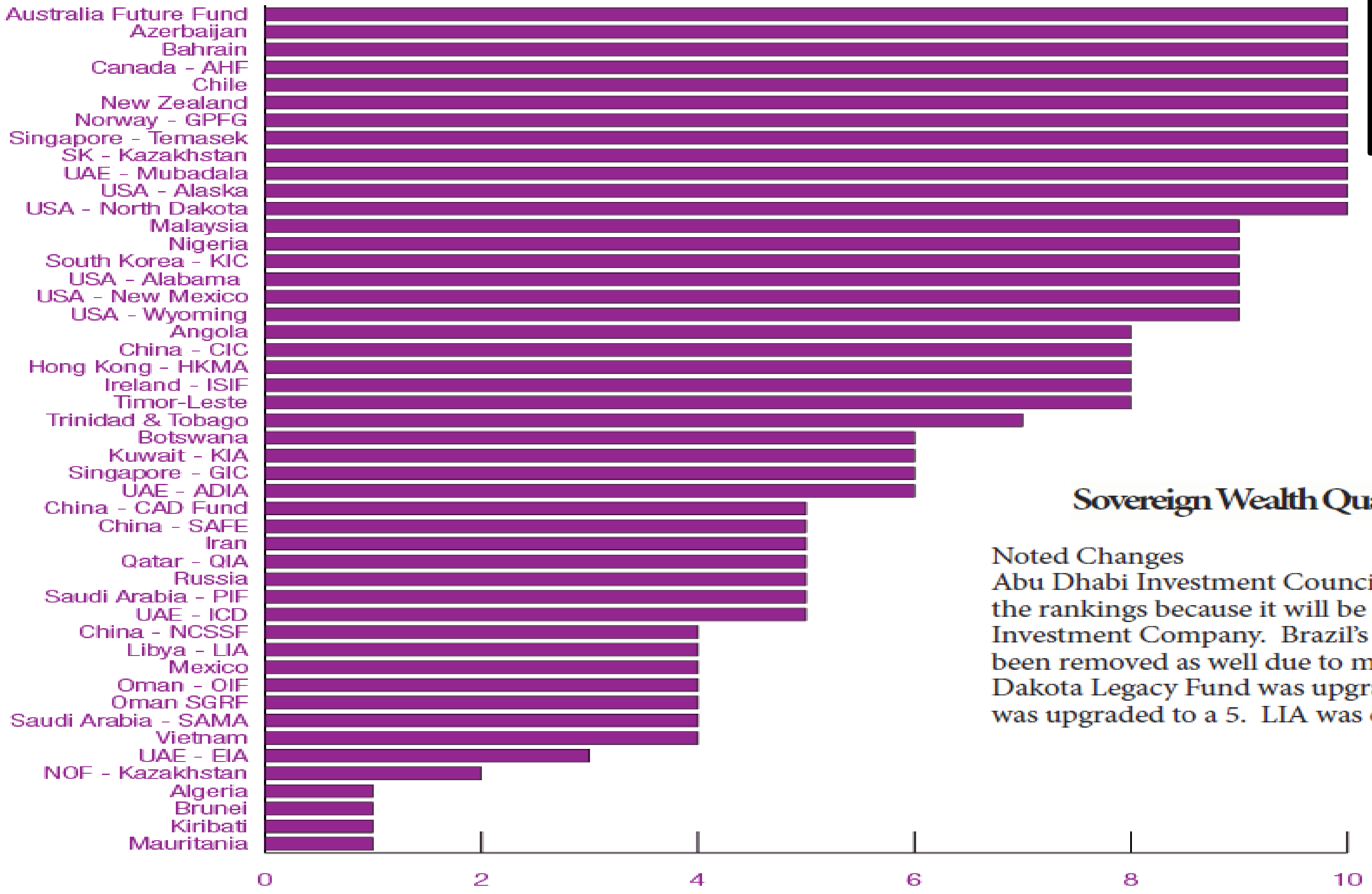
Current State – Programs – SIB

North Dakota
Retirement & Investment Office
Teachers' Fund for Retirement
State Investment Board



Current State - Programs – SIB

North Dakota
Retirement & Investment Office
›Teachers' Fund for Retirement
›State Investment Board



Alaska (Permanent Fund) and North Dakota (Legacy Fund) are rated 10 by the Sovereign Wealth Fund Institute using the Linaburg-Maduell Transparency Index.

Sovereign Wealth Quarterly | April 2018

Noted Changes
Abu Dhabi Investment Council has been removed from the rankings because it will be merged under Mubadala Investment Company. Brazil's sovereign wealth fund has been removed as well due to major asset shrinkage. North Dakota Legacy Fund was upgraded to a 10. Saudi Arabia PIF was upgraded to a 5. LIA was downgraded from 5 to 4.

Notes: The **Linaburg-Maduell Transparency Index** was developed at the Sovereign Wealth Fund Institute by Carl Linaburg and Michael Maduell. The Linaburg-Maduell transparency index is a method of rating transparency in respect to sovereign wealth funds. The transparency index was developed as a response to concerns of unethical agendas being carried out by government owned investment vehicles; calls have been made to the larger "opaque" or non-transparent funds to show their intentions.

Current State – Programs - TFFR

Teachers' Fund for Retirement (TFFR)

The mission of TFFR, a trust fund, is to advocate for, develop, and administer a comprehensive retirement program for all trust fund members within the resources available.

- TFFR plan is designed to provide lifetime retirement, disability, and death benefits for ND public school educators and certain state teachers. It provides ND educators with a financial foundation for the future that includes a secure and stable retirement. This is possible due to TFFR's plan design, professional plan management, strong investment performance, and outstanding customer service.
- The TFFR plan is an important feature in the recruitment and retention of high quality teachers and administrators.
- TFFR provides retirement benefits services to nearly 11,000 active teachers and administrators, 2,500 inactive members, and 8,500 retired educators. Licensed staff from 215 school districts or other employers participate in the plan.

TFFR investment and funding goals

- Improve the Plan's funding status to protect and sustain current and future benefits.
- Minimize the employee and employer contributions needed to fund the Plan over the long term.
- Avoid substantial volatility in required contribution rates and fluctuations in the Plan's funding status.

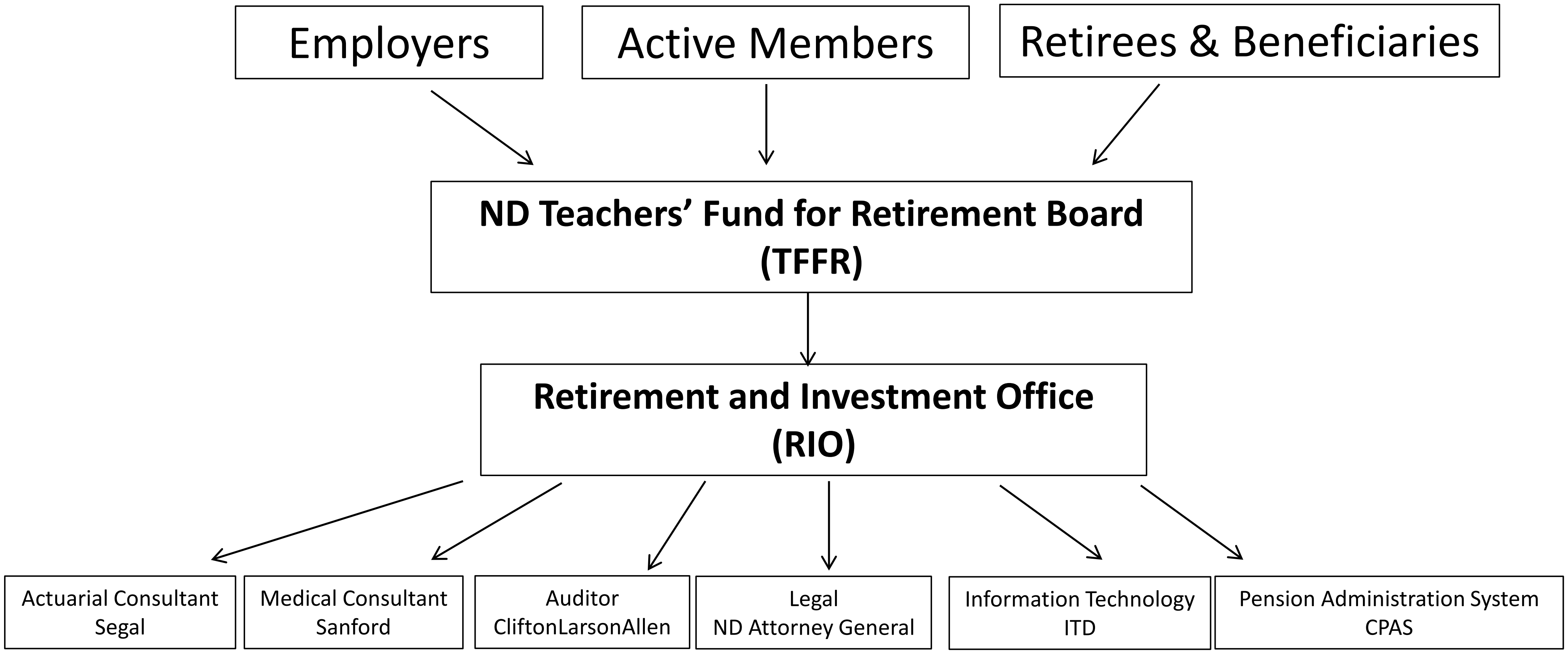
TFFR Service Goals

- Administer accurate, prompt, and efficient pension benefits program.
- Deliver high quality, friendly service to members and employers.
- Provide educational outreach programs including retirement education workshops and benefits counseling sessions.

No interim legislative studies or implementation of TFFR plan changes are occurring during the current biennium.

- Funding improvement legislation was approved in 2011, and implemented from 2011-14. This included member and employer contribution rate increases for all active and re-employed retired members, and benefit changes for nongrandfathered members (i.e. vesting, retirement eligibility, final average salary calculation period).
- Actuarial Valuation studies are conducted annually, Actuarial Experience Study was completed in 2015, followed by an Asset Liability Study in 2015-16, and an independent Actuarial Audit performed in 2016.

Current State – Programs - TFFR



Current State - Programs - TFFR

North Dakota Retirement & Investment Office
›Teachers' Fund for Retirement
›State Investment Board

Highlights

- TFFR customer satisfaction survey scores remain strong at 3.8 (on a 4.0 scale) despite a 38% increase in TFFR membership since 1998. Members are very supportive of the TFFR defined benefit plan and services provided by RIO staff.
- Processing and payment of TFFR member benefit claims including retirement, disability, death and refund benefits are accurate and timely. Processing of employer reports and collection of retirement contributions are accurate and timely.
- In FY 2017, $191 million in pension benefits was distributed to retirees and beneficiaries which positively impacts the state's economy.
- While the TFFR benefit plan is currently funded at 64%, long term funding projections are positive due to benefit and contribution changes approved by the Legislature in 2011.

Lowlights

- Current budget reductions are limiting resources (funding and staffing) to make technology advances.
- Current TFFR pension administration software has been in operation for 13 years and is at the end of its product release life cycle. The current system is a client-server based application that replaced the outdated mainframe system in 2005. In today's environment, a better and more common solution is a web based application. TFFR's current software should be upgraded or replaced with a modern web-based pension administration system which would provide significant functionality improvements for members, employers, and RIO staff.
- Due to funding improvement legislation supported by TFFR members and approved by the Legislature in 2011, the complexity of the TFFR program has increased - there are currently 3 tiers of members with different benefit provisions. Additionally, member and employer contribution rates were increased until TFFR's funding level reaches 100%, which is expected to be many years in the future.

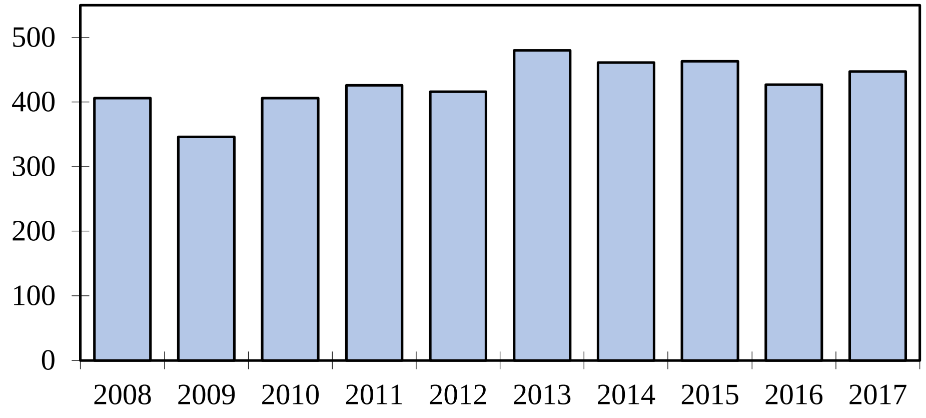
Current State – Programs - TFFR

North Dakota Retirement & Investment Office
Teachers' Fund for Retirement
State Investment Board

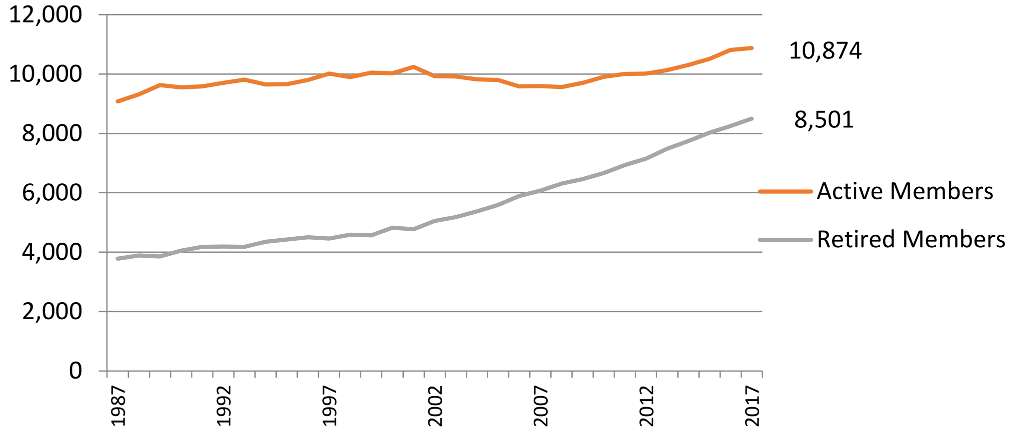
TFFR Participating Employers
As of June 30, 2017

Public School Districts	176
County Superintendents	6
Special Education Units	19
Vocational Education Units	5
Other	9
Total	215

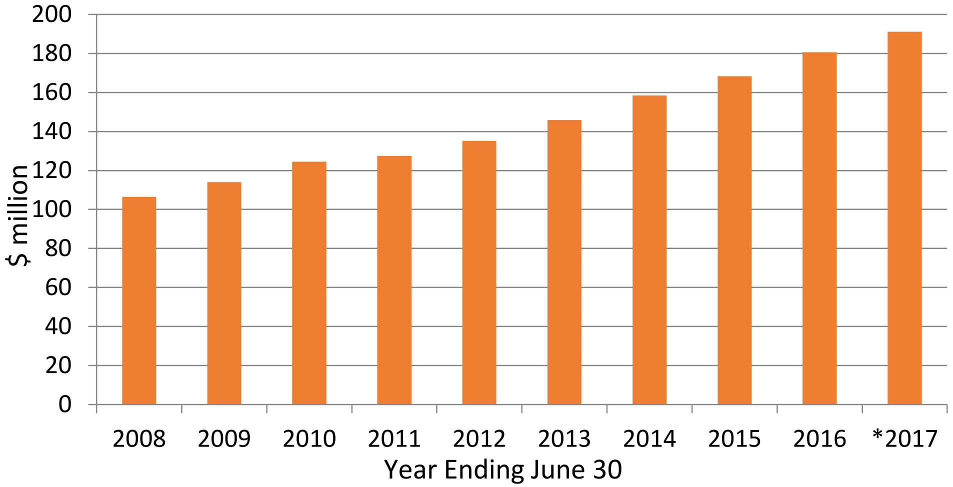
New Retirees by Fiscal Year



Active and Retired TFFR Members
1987 - 2017



Annual TFFR Pension Benefits Paid



Current State – Programs - TFFR

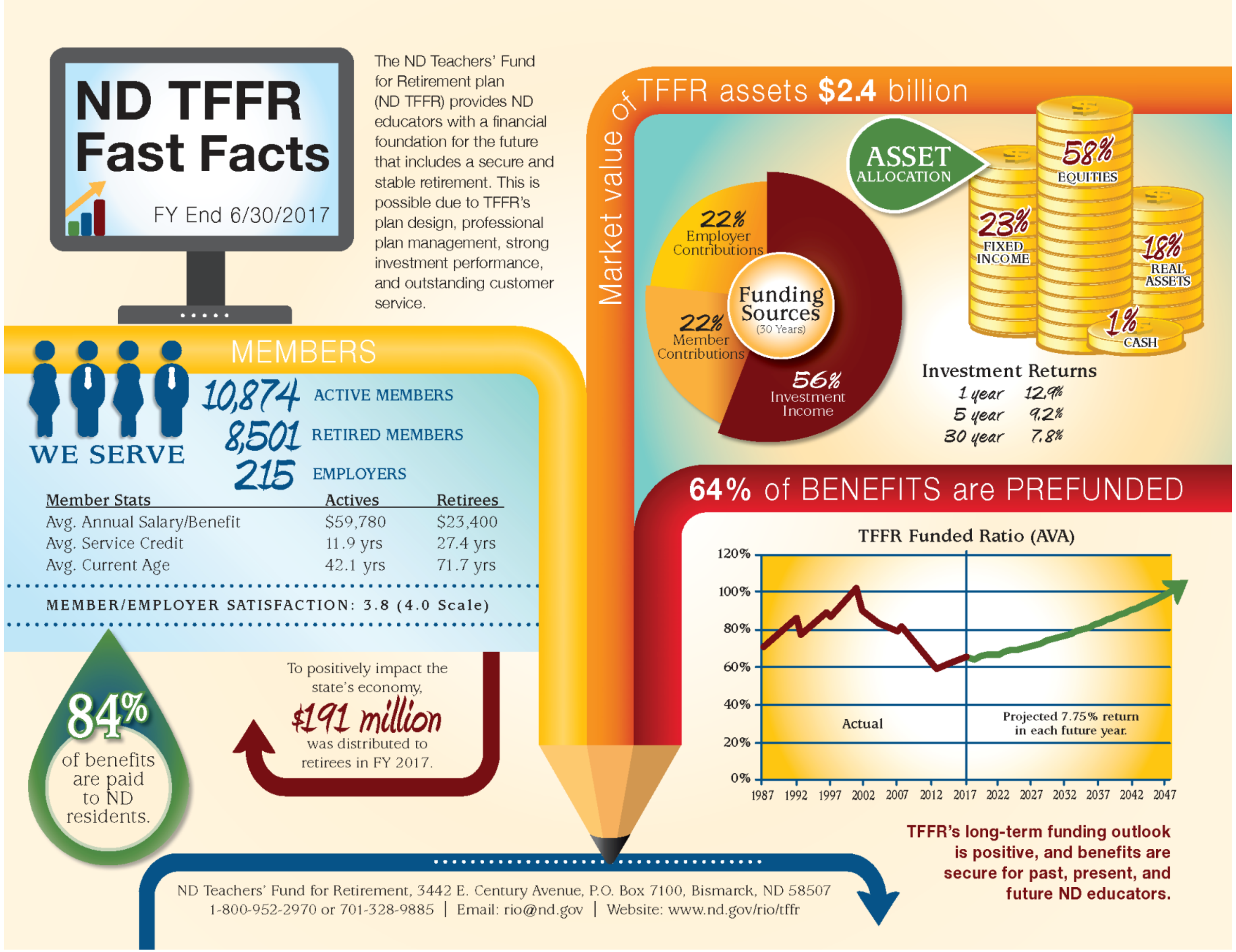
North Dakota Retirement & Investment Office
›Teachers' Fund for Retirement
›State Investment Board

Schedule of North Dakota Retirees by County
June 30, 2017

County	# Retirees	Avg Benefit	Total Benefits	County	# Retirees	Avg Benefit	Total Benefits
Adams	25	1,923	48,073	Mercer	106	2,000	212,037
Barnes	164	2,196	360,092	Morton	297	1,961	582,491
Benson	55	2,111	116,115	Mountrail	77	1,580	121,669
Billings	4	1,479	5,917	Nelson	61	1,827	111,455
Bottineau	129	1,696	218,817	Oliver	17	2,019	34,318
Bowman	44	1,896	83,445	Pembina	98	2,165	212,164
Burke	41	1,539	63,102	Pierce	66	1,817	119,895
Burleigh	860	2,123	1,825,552	Ramsey	140	1,857	259,956
Cass	1,109	2,225	2,467,351	Ransom	53	1,734	91,894
Cavalier	72	1,704	122,677	Renville	41	1,874	76,823
Dickey	72	1,921	138,330	Richland	143	2,191	313,334
Divide	33	1,903	62,812	Rolette	88	1,917	168,692
Dunn	40	2,108	84,317	Sargent	43	1,594	68,549
Eddy	41	1,987	81,476	Sheridan	16	1,620	25,926
Emmons	36	1,964	70,696	Sioux	6	902	5,413
Foster	48	2,271	109,017	Slope	4	1,190	4,760
Golden Valley	18	1,838	33,080	Stark	216	2,063	445,501
Grand Forks	610	2,200	1,342,275	Steele	20	1,766	35,329
Grant	31	1,434	44,446	Stutsman	224	2,026	453,780
Griggs	43	1,909	82,091	Towner	37	1,885	69,732
Hettinger	27	1,871	50,522	Traill	105	1,883	197,694
Kidder	38	1,802	68,463	Walsh	162	1,938	314,008
LaMoure	61	1,823	111,180	Ward	607	2,096	1,272,409
Logan	20	1,850	37,003	Wells	67	1,864	124,892
McHenry	75	1,950	146,248	Williams	182	2,102	382,534
McIntosh	39	1,734	67,609	**Totals**	**6,794**	**2,045**	**13,893,580**
McKenzie	59	2,024	119,442	Out of State	1,707	1,571	2,682,530
McLean	124	1,840	228,177	**Grand Totals**	**8,501**	**1,950**	**16,576,110**

Current State – Programs - TFFR

North Dakota
Retirement & Investment Office
›Teachers' Fund for Retirement
›State Investment Board



Current State – Programs - TFFR

North Dakota Retirement & Investment Office
›Teachers' Fund for Retirement
›State Investment Board

ND TFFR PLAN SUMMARY

	Tier 1 Grandfathered Member	Tier 1 Non-Grandfathered Member	Tier 2 Member
Employee Contribution Rates (active and re-employed retirees)			
7/1/10 – 6/30/12	7.75%	7.75%	7.75%
7/1/12 – 6/30/14	9.75%	9.75%	9.75%
*7/1/14 ongoing	11.75%	11.75%	11.75%
Employer Contribution Rates			
7/1/10 – 6/30/12	8.75%	8.75%	8.75%
7/1/12 – 6/30/14	10.75%	10.75%	10.75%
*7/1/14 ongoing	12.75%	12.75%	12.75%
Vesting Period	3 yrs	3 yrs	5 yrs
Unreduced Retirement Eligibility			
Minimum Age	No	60	60
AND Rule	Rule 85	Rule 90	Rule 90
OR Normal Retirement Age	65	65	65
Reduced Retirement Eligibility			
Minimum Age	55	55	55
Reduction Factor	6%	8%	8%
Retirement Formula Multiplier	2%	2%	2%
X Final Average Salary	3 yr FAS	3 yr FAS	5 yr FAS
X Service Credit	Total years	Total years	Total years
Disability Retirement	Yes	Yes	Yes
Retirement Formula Multiplier (2%) X Final Average Salary (FAS) X Total Service Credit			
Death/Survivor Benefits	Yes	Yes	Yes
Refund of account value or Life Annuity to survivor based on member's vesting status.			

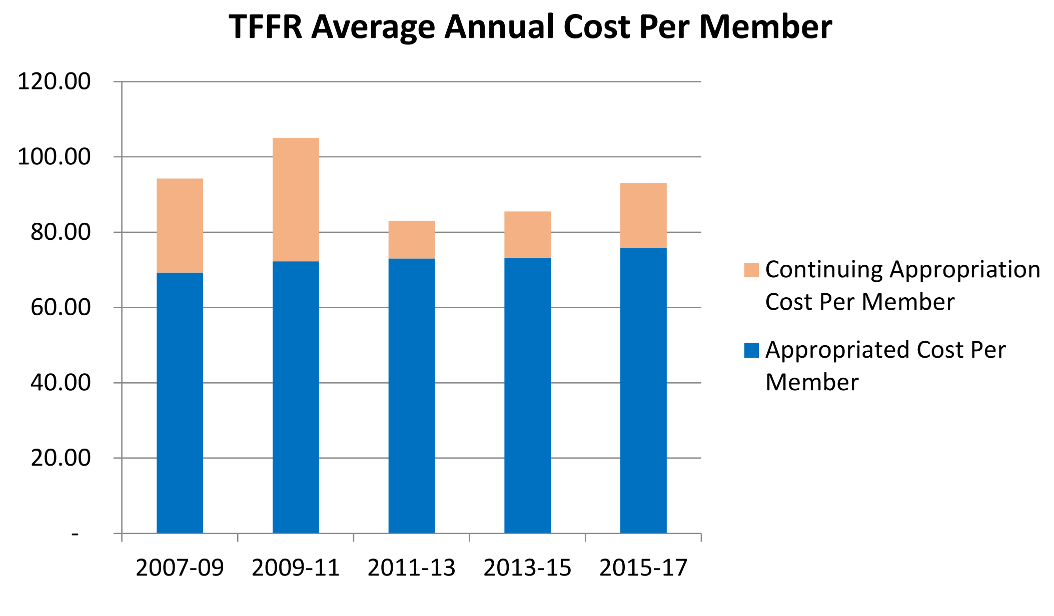
Tier 1 is a member who had service credit in the TFFR plan prior to 7/1/08.

- Tier 1 Grandfathered member was less than 10 years away from retirement eligibility as of 6/30/13. Grandfathered member was vested, and either age 55 or had a combined total of service credit and age equal to or greater than 65 on 6/30/13.
- Tier 1 Non-Grandfathered member was more than 10 years away from retirement eligibility as of 6/30/13. Non-grandfathered member was less than age 55 and had a combined total of service credit and age which was less than 65 on 6/30/13.

Tier 2 is a member who began participation in the TFFR plan on 7/1/08 or after.

**Contribution rates are in effect until TFFR reaches 100% funded level, then rates reduce to 7.75% each.*

Current State – Programs - TFFR



- Customer satisfaction surveys
  - TFFR customer satisfaction survey scores remain strong at 3.8 (on a 4.0 scale).
  - Customer comment cards or program evaluations are included in active and retired member correspondence, and distributed to participants in member and employer outreach programs, and to member and employer stakeholder group representatives.
  - While the survey rankings related to staff courtesy, promptness, and content/effectiveness of information are important (3.8), even more valuable are the numerous comments and suggestions from members and employers related to the benefits and services provided by RIO.
  - TFFR values the feedback from members and employers, and continually strives to update and improve services to our customers.

- TFFR has received the Public Pension Coordinating Council's Public Pension Standards award for the past 25 years.

- TFFR Actuarial Audit conducted in 2016 by independent actuary confirmed that actuarial assumptions, methods, and calculations done by plan actuary were accurate, reasonable, and performed in accordance with actuarial standards of practice. Audit results were positive, with only a few minor recommendations.

- TFFR received favorable determination letter from IRS in 2017 confirming the TFFR plan is in compliance with IRC requirements for qualified plans (conditioned on adoption of certain proposed technical amendments in 2019 legislative session).

Reinvention – Programs - TFFR

North Dakota Retirement & Investment Office
›Teachers' Fund for Retirement
›State Investment Board

- TFFR Pension administration software modernization project (exploring)
- TFFR Data analytics
  - School district master payroll files for audit (in progress)
  - Shared files with ESPB for teacher licensure (to be explored)
  - Shared files with PERS for dual membership (to be explored)
- TFFR Pension administration practices
  - Electronic payments to retirees (in progress – only 5 paper checks per month)
  - Electronic employer reporting (in progress – 98% of members currently reported electronically; system upgrade would offer other electronic options)
  - Electronic communications (in progress, limited – requires system upgrade)
  - Alternate delivery methods for member/employer information (in progress, limited – requires system upgrade)
  - Member and Employer self- service (requires system upgrade)
- RIO/TFFR and PERS executive staff are in the very early stages of exploring additional opportunities for future cost savings and/or administrative efficiencies. (Note: investment of PERS trust fund assets was transferred to the SIB in 1989 which provided significant investment cost savings.)

Reinvention – Programs - TFFR

North Dakota Retirement & Investment Office
›Teachers' Fund for Retirement
›State Investment Board

TFFR Pension Administration Software Modernization Project

- Current TFFR pension administration software has been in operation since 2005. The functionality and technical architecture of this client-server technology is 13 years old, and is at the end of its product release life cycle.
- In order to move towards a more technologically advanced, web based system which would provide significant self-service functionality for members and employers, RIO is exploring the potential benefits, risks and costs of upgrading or replacing our current application to improve and streamline TFFR pension administration processes, reporting capabilities, communications and services to members and employers.
- Most of the desired features needed to reinvent the way TFFR conducts business are standard functions of modern pension administration software, either out of the box, or implemented with configuration.
- An updated pension administration system will enable TFFR to adopt current best practices in self services for members and employers, and achieve greater efficiencies in daily administration.
- Employers will be enabled to take greater ownership of their data with the ability to securely upload contribution data, including optional electronic submission methods available to paper-based reporting employers, receive immediate validation results, and confirm contribution remittances.
- Members using self-service can access and update certain personal information, and run their own benefit estimates.
- Communications will be timelier with members being able to initiate requests online and receive statements and notifications securely through the web portal. Further, digital communication is direct and secure, saves on mailing costs, and reduces reliance on paper.
- As part of its study, RIO is also collaborating with other state agencies to review available options and identify potential synergies to enhance operational efficiencies and reduce costs.
- While a pension administration software modernization project will be costly and time consuming, we believe it is in the interests of TFFR members and employers to consider making this type of investment to take advantage of technology improvements that have been made in the years since the current software was implemented.

Reinvention – Programs - SIB

- SIB Risk Management oversight and reporting
- RIO/SIB and Land Board staff have historically shared information regarding common investment management firms and have realized fee savings from overlapping mandates. RIO welcomes additional discussion regarding the expansion of current collaborative efforts to explore new ways in which both agencies can work together to maintain strong investment performance and further reduce investment management fees & expenses.

Reinvention – Programs - SIB

North Dakota Retirement & Investment Office
›Teachers' Fund for Retirement
›State Investment Board

Investment Risk Management Oversight and Reporting

- The process of identifying the level of risk that an entity is comfortable with, measuring the level of risk that an entity currently has, taking actions that bring that actual level of risk to the desired level, and monitoring the new actual level of risk so that it continues to be aligned with the desired level.
  - Continuous process
  - Requires measuring, monitoring, and managing exposure to both economic and fundamental drivers of risk and return across asset classes
  - Avoidance of overexposures to common risk factors
- One of the six pillars of the SIB's 2017-19 Strategic Investment Plan - "Enhancing our internal control environment by improving the use of proven risk management solutions" noting that "a robust risk management framework serves as the foundation to support a sound internal control environment and lessen downside risk".
- BlackRock Aladdin risk management system
  - Chosen by RIO staff in 2016 after exhaustive review of leading investment risk management systems
  - State of the art multi-asset class risk management solution
    - Portfolio risk, stress testing & scenario analysis
    - Asset allocation analysis
    - Performance & attribution
    - Compliance & oversight
- Due to the expertise needed to effectively harness the full potential of this system, the time required to develop and continue to monitor the outputs, and the desire of RIO staff to provide the SIB with all of the data necessary to make informed decisions in the management of the multi-billion dollar investment portfolio, an additional FTE (Chief Risk Officer) is needed.
- If the SIB and RIO can improve investment returns by just 0.01% (by choosing investment managers that will outperform their benchmarks without taking excess risk) we increase our client investment income by $1.3 million (e.g. $13 billion x 0.01% = $1.3 million).

Reinvention – Agency

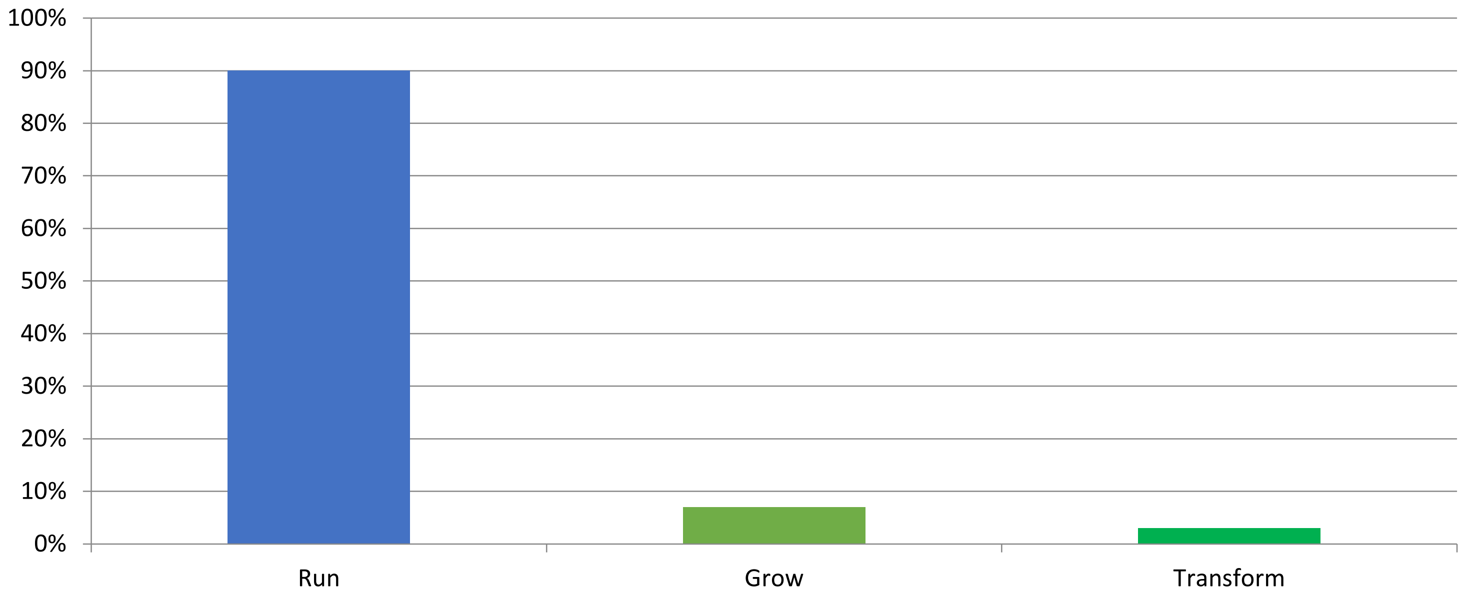
North Dakota Retirement & Investment Office
Teachers' Fund for Retirement
State Investment Board

- RIO Website Update project (in progress)
- RIO Shared Services (to be explored)
  - HR and payroll
  - Facilities
  - Marketing/Public Information/Communications
  - Procurement
  - Print/Mailing services

RIO Reinvention Barriers

- Budget limitations
- Staffing limitations
- Cost of shared services
- Statutory authority
- Board fiduciary responsibilities and governance issues
- Difficulty in communicating benefit information to TFFR members and employers who have no or limited use of technology.

Reinvention: Run – Grow - Transform



North Dakota Retirement & Investment Office
Teachers' Fund for Retirement
State Investment Board

Future State – Funding opportunities

North Dakota Retirement & Investment Office
›Teachers' Fund for Retirement
›State Investment Board

- RIO is a Special Fund Agency; **No General Fund dollars are appropriated.**
  - Funding for administration of the TFFR Pension Plan comes from Member and Employer Contributions and Investment Earnings
  - Funding for administration of the Investment Program comes directly from Investment Clients' invested assets (both statutory and contracted).
- 83% of RIO's current budget is Salaries and Benefits
- RIO's Operating Line was cut by **13%** for the current biennium and is currently at $862,484 (0.006% of AUM)
  - That amount is also 13% lower than the RIO operating budget was 20 years ago.
- To meet the 10% budget reduction requirement, RIO needs to cut $534,005.
  - This equates to 62% of current Operating Line
- Although not required to cut FTE positions (RIO currently has 19 FTE), in order to meet the 10% budget reduction requirement, the Salaries and Benefits Line will need to be reduced.
  - RIO has no vacant positions currently.
  - RIO has no temporary positions in the current biennium budget.
  - Board member pay is included in the Salaries and Benefits Line ($148 per board member per meeting based on statute).

Future State – Key Strategies – Budget/FTE

North Dakota Retirement & Investment Office
Teachers' Fund for Retirement
State Investment Board

Budget strategies

- Over a dozen combinations of position cuts and salary reductions have been considered.
- Most require a minimum of 3 positions to be eliminated to reach 10% of total budget (except if Executive Level positions are included)
- With a reduction of over 15% or more (3+) of RIO's current workforce, the agency's ability to maintain ongoing TFFR pension administration operations and SIB investment management functions would be severely compromised. This would result in:
  - TFFR Program
    - Critical retirement programs, processes, and operations would need to be modified or eliminated. This would result in increased potential for inaccurate TFFR contribution and salary reporting, account maintenance, benefit payment processing, member and employer services and communications, compliance with statutes, and other essential functions.
    - Accuracy, timeliness and quality of benefit payments, communications, and customer service would be negatively impacted.
    - Initiatives intended to continue reinventing TFFR program administration processes would not be possible. For example, upgrading system software and transforming the manner in which members, employers, and staff conduct TFFR business would no longer be feasible, as it would require additional staff during the planning, implementation, and transition phases. This would limit our ability to reduce future costs and operate more efficiently.

Budget strategies (continued)

- SIB Program
  - Monitoring and due diligence on existing investments would be reduced and modifications and improvements to portfolios would be less timely, increasing the risk of underperformance due to investment manager issues and non-compliance with client policies.
- RIO Agency
  - Overall financial and investment reporting would be impacted. Internal controls/segregation of duties would be reduced. Customers would not receive required reports in a timely manner, leading to lower client satisfaction scores. The potential for inaccurate reports and related audit findings would increase.
  - A 15% staff reduction would further negatively impact remaining RIO staff members. Staff retention, recruitment, and morale issues would worsen.

FTE Strategies

- RIO is not being requested to reduce FTE as the agency only has 19 positions.

Closing Themes

- RIO deems it critically important to maintain, if not grow, funding and professional resources for our agency given the continuing growth and increasing complexity of agency services, including our $13.5 billion client investment portfolio and TFFR member services. The rapid growth of the Legacy Fund also increases the need for additional funding to prudently manage escalating fiduciary responsibility for North Dakota’s intergenerational wealth fund which is forecasted to reach $13 billion to $16 billion over the next decade.

- RIO looks forward to collaborating with other state agencies to deliver top tier retirement benefit services and investment management oversight to our valued members, clients and boards over the next decade.

- RIO believes this goal is highly dependent upon improving the compensation levels of all of RIO team members when benchmarked against other public pension plans and emerging sovereign wealth funds to ensure we continue to attract and retain highly skilled professionals in all functions including accounting, administration, audit, IT, investments and retirement benefit services.

BOARD LEADERSHIP

INNOVATIVE APPROACHES TO GOVERNANCE

NUMBER 157, MAY–JUNE 2018

www.boardleadershipnewsletter.com

Create a Stellar Board

By Dr. Linda Henman

Dr. Linda Henman is the author of six books, including Tough Calls: How to Move Beyond Indecision and Good Intentions. *She has more than 35 years of experience working with executives and boards in Fortune 500 companies and small businesses to help them exceed their strategic objectives by maximizing talent. In this article, she walks readers through the five critical components of a successful, high-performing board of directors.*

In parts of Indonesia, Komodo dragons make unwelcome and unannounced visits to villages that border their habitat. Even though the giant lizards and humans lived in harmony for generations, contention exists now. Environmentalists have imposed new policies in a region where people once perceived a sacred duty for caring for the Komodo dragons. The relationship between lizard and human has not been the same since.

Executives and boards of directors have experienced a similar loss of symbiosis. Policies and procedures that worked for decades don't always work when the economy, regulations, or other significant factors change. Now more than ever, directors are taking their responsibilities seriously, speaking up, and striving for results; but in many cases, the evolving relationship between the company's executives and the board has not found the right symmetry. As we're realizing, the real challenge for directors and executives isn't regulatory compliance—it's high performance. To achieve it, directors and executives need to systematically examine the five constructs of a successful Stellar Board.

Leadership

Thought leaders do not agree about the best way to lead a board. Some steadfastly hold to the notion that the CEO and board chair should be the same person. Others think the board should split the roles.

Shareholder activists strongly support the idea that the chair and CEO roles should remain separate. In their estimation, both directors and the CEO can be more effective when the roles and duties of the chair differ from those of the chief executive. Also, when different people hold these roles, the chair can act as a lubricant between directors and executives, especially when inevitable conflict occurs. However, although shareholder activists maintain this position, in large corporations, this happens less than 50 percent of the time.

Executives who interact with the board have the leadership responsibility to keep the group focused on the right issues. To do this, they need to

(continued on page 2)

ALSO IN THIS ISSUE

NEWS

Study delves into corporate secretaries' view of directors

The Conference Board's Governance Center has released a report detailing the role and expectations of corporate directors from the perspective of corporate secretaries. Among the findings, the center said, is that many corporate secretaries are not convinced that publicly disclosing formal board skill matrices—a request some investors are increasingly demanding—will improve board composition and functioning.

Other insights from the Just What Is the Corporate Director's Job? report include:

- The most important facet of directors' interaction with management is the information they receive, analyze, and respond to as they carry out their oversight responsibilities. Corporate secretaries who participated voiced their concern over asymmetric information risk regarding management's communications with directors and ways to mitigate this inherent risk, the report said.
- "Ruffling feathers" can have its benefits, but directors must do so with respect. Per the report, corporate secretaries have a unique position to assess whether a board is too collegial with directors, who often fear

(continued on page 7)

Stellar

(continued from front page)

keep things succinct and, whenever possible, to present information in a summary or bullet format.

Too often, directors assume the role of sponges who simply absorb that which they see in front of them. Part of CEOs' leadership duties requires the preparation of questions that will stimulate dialogue.

Leadership duties of the chair and other directors involve moving the discussion to consensus. The discussion should uncover all kinds of differing points of view, but ultimately board members need to ask, "So what?" What will directors support, if the decision is theirs? And how will executives use the insights they have gained from the debate to influence the decisions they will make?

Rapport with the CEO

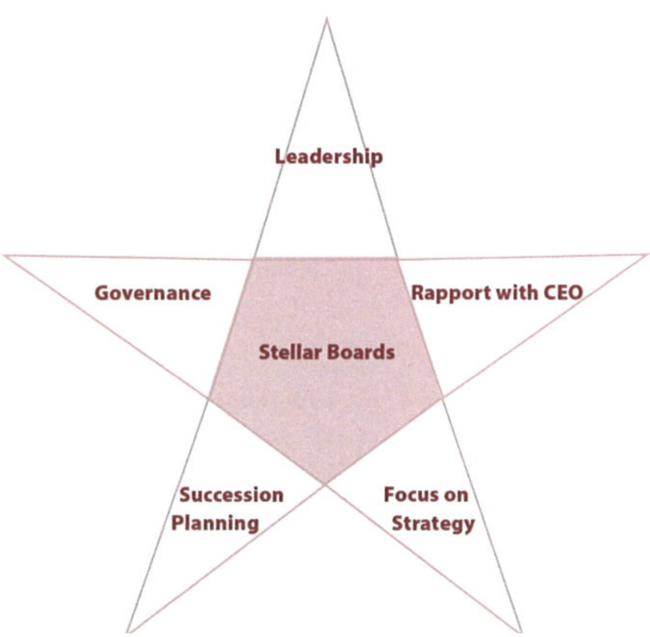
Board success starts with the relationships between the directors and the CEO. The CEO should regularly disagree with the board, and robust debate should occur, but never at the expense of good rapport. All should embrace tension and move beyond the outdated thinking that the board is a necessary evil. Members of Stellar Boards realize that a certain degree of tension is both healthy and desirable. Contention, however, won't prove productive.

The CEO should ask questions and question answers, but all in a climate of candor and responsiveness. Trust, respect, and open communication form the foundation of any strong relationships; board relationships are no exception.

When building rapport with the board, the CEO should keep top of mind the importance of predictability, excellence, and honesty. Directors need to trust executives to do what they say they will do, to uphold the values of the organization always, and to conduct their personal and private lives with the utmost integrity. Gone are the days of CEOs expecting directors to trust them in business decisions when they have clearly not represented the highest ethical standards in their private lives—here to stay are days of scrutiny and accountability.

Open communication holds the keys to the kingdom of good rapport. Executives and directors of Stellar Boards need to be on the same page about the company's vision, mission, values, and strategy. But they'll need to go beyond that. Does everyone agree about what success will look like? Can they routinely bring the conversation around to priorities?

Stellar Boards



Executives tend to worry too much about what they will say in a meeting instead of concentrating on how much they listen. If CEOs don't find the directors in the room worth listening to, they have the wrong people on their board. A meeting presents a chance for executives to hear what directors have to say and to benefit from their collective knowledge and expertise.

Focus on Strategy

Too often, directors don't understand when and how they should be involved in strategy. When earnings decline, a competitor makes a sudden move, or a merger or acquisition looms, they come to life. But often it's too late. By not getting involved earlier in the game, directors deny executives, and the company in general, the value of their input.

Stellar Boards do better. They don't formulate strategy, but they maintain a clear focus on it. They assess and critique it. Like the princess in "The Princess and the Pea," directors need to detect flaws deep in the strategy—not to execute, but to perceive and report. The challenge for executives, therefore, is to make sure directors have all the necessary information to do their jobs.

Sounds simple. Why then does strategy create so much angst? Too often, boards and executives don't take a systematic approach to how they will interact with regard to strategy. The board discusses strategy piecemeal over a period, often in relation to something else. Or, when executives present the strategy as a finished product, directors sit idly and contribute little.

Contrast these practices to the process the Stellar Board uses, not only to reach full agreement on the strategy, but also to shape it. Executives articulate the strategic direction and clarify the measurements, criteria, timelines, and standards for evaluating it. Then, directors ask questions and offer opinions. This list offers a starting point for this discussion:

- Does this strategy support our mission?
- Does the company have the resources, financial and human, to execute?
- Have they considered the full range of external factors?
- Have they sufficiently examined risk?
- Are the assumptions valid?

- What is the company's competitive advantage?
- How does this strategy leverage it?
- Will customers benefit?
- How will we make money with this strategy?

When directors ask these questions, they ensure that executives have not made a major market entry or other strategic decision based simply on instinct, historical experience, or guesswork. Executives should anticipate these questions and prepare answers for them. If directors don't ask them, they should put them on the table themselves.

Succession Planning

Years ago, I worked with the board of a large publicly traded manufacturing company to help them formulate a succession plan for all key positions in the company, especially the CEO's. In the one-on-one interviews with directors, I found that universally they thought the company was most vulnerable to the sudden loss of Jim, the CEO.

In this company, the CEO engaged in many of the day-to-day duties normally assigned to others, and he was the only one who knew how to perform specific functions that were critical to the success of the company.

I offered my recommendations for a long-range succession plan for each key position and a step-by-step development plan for each executive. As part of it, I suggested Jim start teaching his heir apparent to take over some of the duties he had been doing. Jim refused.

He knew that if he held his cards tightly enough, he had all the control. He understood the board couldn't fire him without putting the company at risk, at least in the short run. The board accepted this grim reality, even after I brought it to their attention.

Stellar Boards expect more loyalty from their CEOs. They know that the biggest favor executives can do the company is to help directors select both emergency and long-range replacements for key positions—especially their own. These stellar CEOs also openly discuss their plans for retirement. This isn't an easy topic for directors to broach, so the best CEOs take the lead. Unlike Jim, they realize the real power comes from both exceptional performance today and a plan for tomorrow.

They map out the specific role they will play in finding and preparing their eventual replacement. They keep a future orientation and think about what will be required of executive positions in the future, not what anyone else has done in the past.

When they find themselves two years away from retiring, they identify an internal replacement, or oversee the recruitment of one. They also identify high-potential candidates for each executive position 10 to 15 years before any one of them will reach the executive level. Then, they let the board know them and interact with them.

Finally, these executives work with the board to define the stages of transition. They create a list of likely candidates for each executive position. Then, they place each in a series of expanding roles that give candidates the opportunity to learn and the board the chance to assess them.

Governance

"Governance" is one of those all-encompassing words people use but that few can explain in concrete terms. When used for corporations, it usually means general board oversight.

Governance underpins the board's ability to do all the aspects of its job. While strategy and succession planning address specific "What?" questions, governance deals with the "How?" It includes but is not limited to decisions about the board's size, frequency of meetings, director selection, shareholder relations, and social responsibility. When a board has a governance committee, those directors initiate action plans with specific timelines for implementation of recommendations. This committee should have the authority to shape and recommend policy and structure.

The existence of a governance committee doesn't let the CEO or other executives off the hook. To be part of a Stellar Board, executives need to play an active role in how things happen. Have strategy drive the agenda. Regulatory issues will control a considerable portion of each meeting, but executives and directors can collaborate to control the rest.

Of course, an agenda will guide the actual meeting, but the CEO can do a great deal to streamline governance. For instance, when the board meets, tackle important, difficult, and unpleasant issues immediately. When this doesn't happen, by the time the committee discusses the thorny issues, everyone will be tired and impatient.

Most boards hold executive session meetings following the board meeting. However, if this meeting occurs late in the day, people will be spent. Boards can benefit, therefore, from what I call an "executive session sandwich." In other words, meet before the general meeting to address critical issues and then use the low-energy time after the session to tie up loose ends.

The board book presents another energy zapper. Use the board book to inform, not persuade. If the book includes mountains of data with little salient information, directors will overlook key issues. Lead with a summary page, the questions members need to discuss, and the topics that merit debate. In short, discuss, don't present the book.

Whenever possible, enrich committee reports too. Typically, these reports include a detailed description that lacks relevant information or that rehashes an entire committee meeting or topic. Directors are busy people. Aggregate the critical information; present it in summary form; and offer analysis, not just information.

Another key to good governance lies in better leveraging directors' contributions. All members of the board should encourage directors to communicate regularly about their experience and expertise. This will allow everyone to apply this information when they

(continued on page 8)

Governance Systems and Municipal Governing—One City's Experience

By Rob Lewis

Rob Lewis currently serves as program coordinator with the City of Red Deer, Alberta, Canada. He has a diploma in theology from Vanguard College, Edmonton, Alberta, and is certified in Policy Governance proficiency. In this article, he looks at the unique challenges and solutions related to implementing Policy Governance in a municipal council environment in Red Deer. It gives the history of the city's municipal governance and talks about why it looked to do something different, why it landed on Policy Governance, and the results the city has seen thus far.

Almost a decade ago, Red Deer's City Council, always looking for better, more effective ways to govern in a manner truly representative of Red Deer's citizens, endeavored to address two pressing and yet fundamental leadership questions: "What does the City Council need in order to govern well?" and "What role does the administration play in the council's governance success?"

In 2010, the City of Red Deer embarked on a journey that would cause a profound shift in its decision-making and governance mindset and processes. Traditionally, city councils have a very hands-on approach to providing direction to the administrative side of the organization. There are many reasons for this, not the least of which is the thought that, in order to truly represent its citizens, the council needs to be part of the administrative processes used to address the issues the council brings to the administration. While this is a reality the council needs to own, the underlying question is: Where is the most effective point at which the council should intersect with the administration to be part of the process, while not hindering that very process at the same time? This was one of the many considerations the City Council wrestled with when deciding to review the way Red Deer was governed.

FOOD FOR THOUGHT

"Management is doing things right; leadership is doing the right things."

Peter Drucker

The Search for a Model

Municipal governance doesn't happen in isolation. Therefore, the council's search for a more effective governance model needed to consider several critical contributing factors. The council operates in a broader context, with several levels of government above them as well as horizontal relationships with other municipalities. Various pieces of legislation and regulations govern what a municipal council is solely responsible for (that which cannot be delegated to the administration) and specific parameters in which it needs to operate. Add to this the very public nature of the council's work and the need to ensure the decisions made are truly reflective of the values of the community, and Red Deer's council was facing a formidable task in looking to adopt a new governance model.

Change is never easy, and this undertaking was no exception. The Red Deer City Council had used essentially the same typical method of governing for decades. In order to help ensure success in this significant change in direction, the council moved forward guided by solid, predetermined criteria. Strong governance would need to define role clarity by articulating what decisions are to be made and by whom. It should rely on reporting outcome attainment as opposed to methodological detail. And finally, it would have to consider decisions through the lens of how they reflect and uphold the values of those who own the organization—the citizens. The city reviewed an abundance of literature related to governance models, including the works of George Cuff and John Carver. In the end, the council moved forward with a "hybrid model" that follows Carver's Policy Governance structure, influenced by Cuff's work.

Implementation Challenges

The implementation of the Policy Governance model was not without its challenges. Time itself would prove to be an adversary during its implementation and the first few years of use. In order to avoid governing under two models—the "old" model they had governed under to this point and the "new Policy Governance model" with potentially conflicting ideologies and operational methodologies—the council wanted to make sure its primary set of policies was established and any key "old" policies were migrated to the Policy Governance model as quickly as possible. That said, it also had to be certain Policy Governance was implemented correctly and in such a fashion to promote the longevity of the model. To do this, administrative personnel were trained in Policy Governance at the Policy Governance Academy, creating "in-house" expertise. External consultants were also employed to ensure a necessary breadth of experience and understanding in the implementation process. The first and most important phase of the implementation process was completed over the course of about three years, wherein the council and administration worked to develop the council's core set of policies. This core set of policies continues to evolve, with new policies being added to it as required.

The other time-related challenge the council faces on a perpetual basis is the fact that every four years the make-up of the City Council changes due to the

Alberta municipal election cycle. This is healthy for both the council and its governance model, in that it brings new members to the council table and gives the council the opportunity to assess and affirm ownership of its policy set. It, however, also poses some potential challenges regarding the consistency of model use and application. With the introduction of new council members comes a sense of "starting over from scratch" that needs to be acknowledged and managed. In all likelihood, the incoming council members will not have the same understanding of the model the incumbents do. Even if they are familiar with Policy Governance, as already mentioned, the particular application and implementation of the model in a municipal government setting is unique. If the incumbents (particularly the chief governance officer) aren't strong advocates of the model, there is the possibility it may lose momentum and be set aside. This could, in turn, lead the council to either revert to the previous governance structure or investigate alternative governance options. Only when the members of the council have seen and experienced the value of the model, as it allows them to better hold themselves to the articulated values of the citizens, will they be able to advocate for its permanency as the governance model for the city.

Reasons for Caution

Since the model was introduced, Red Deer has gone through two election cycles and the model has been retained. While all indications point to the model's continuation as a core component of governance for Red Deer, this should never be assumed or taken for granted. The fact that the model continues to be engrained in Red Deer's governance environment is in no small part due to the council's acknowledgment of the value it offers as a governance model and to the hard work of the administration in championing the model. Through ongoing professional training, the administration ensures there are resident experts on staff to continually educate and support the council in its proficient use of the model. The goal is that this, along with other new and innovative initiatives, will help to ensure the longevity of the model as a central part of the council's governance structure.

Looking forward, the integration of Policy Governance in the governance structure of Red Deer's City Council looks favorable. There may be, however, the tendency on the part of the council to allow itself to "creep" into the administration's work, just as there may be the tendency for the administration to want to take on governance roles. The line needs to be held firm if governance is to enjoy the success it should. As soon as the council steps outside of the Policy Governance parameters that clarify the distinct roles of the council and administration, the strength of the model begins to dissipate. The council needs to remain focused on the ends as they relate to the attainment of outcomes congruent with the values of the citizens, allowing the administration to focus on mechanisms needed to see the council's outcomes come to fruition. The administration, through the city manager (the council's one employee), can support the council in this by stressing the importance of the council holding itself accountable to properly and effectively using Policy Governance. The council's role is to link to the citizens as owners in order to provide leadership to the organization based on what values and priorities the owners have expressed.

To help ensure the council's governance success, the administration then needs to respectfully work within the direction and limitations of Council as conveyed through the city manager. If the council is diligent, and the administration steadfast, the results will continually substantiate the value of effective governance. When the model is properly used, the owners become the focal point and all decisions are made in light of the values the owners have verbalized. When that alone is the priority of the council, it becomes much easier to

(continued on page 7)

WHEN WE SAY...

Board Leadership's mission is "to discover, explain and discuss innovative approaches to board governance with the goal of helping organizations achieve effective, meaningful and successful leadership to fulfill their missions."

Board Leadership aims to fulfill this mission by engaging its readers in a lively and illuminating inquiry into how board governance can be made more effective. This inquiry is based on three key assumptions:

- Boards exist to lead organizations, not merely monitor them.
- Effective board governance is not about either systems, structures, processes, theories, practices, culture, or behaviors—it is about all of them.
- Significant improvements are likely to come only through challenging the status quo and trying out new ideas in theory and in practice.

Uniquely among regular publications on board governance, *Board Leadership* primarily focuses on the job of board leadership as a whole, rather than on individual elements of practice within the overall job.

Over time, *Board Leadership* will provide a repository of different approaches to governance created through its regular "One Way to Govern" feature.

Here's what a few of the key terms we use mean to us:

- **Innovative:** Creating significant positive change
- **Approaches:** Principles, theories, ideas, methodologies and practices.
- **Board governance:** The job of governing whole organizations. ❑

CALENDAR OF EVENTS

June 7–8, 2018

Annual Leadership Development Conference

—Hyatt Regency San Francisco, 5 Embarcadero Center, San Francisco, CA 94111 USA

Learn how practitioners take steps to address critical leadership challenges at all levels of their enterprises. Having direct access to speakers and panelists enables attendees to customize their experience at the conference to solve problems, brainstorm ideas, and strengthen their leadership pipelines and the performance of their leaders at all levels of the organization.

For more information, visit conference-board.org.

June 15, 2018 9:30 A.M.–3:00 P.M.

ICSA Charity Governance Conference

—ICSA, Saffron House, 6-10 Kirby St., London, England EC1N 8TS UK

This full-day conference will focus on themes relevant to charities and not-for-profit organizations. It will provide attendees with an insight into the latest thinking and offer a unique opportunity to share ideas and gain valuable knowledge on some of the challenges faced by governance professionals in the sector.

For more information, visit icsa.org.uk.

June 20–22, 2018

Certificate of Nonprofit Board Consulting

—Hyatt House Denver/Lakewood at Belmar, 7310 W. Alaska Dr., Lakewood, CO 80226 USA

To better meet the ongoing need for governance training among nonprofit organizations throughout the country, BoardSource has created the Certificate of Nonprofit Board Consulting. This three-day course is designed to heighten the skills and abilities of those who currently, or would like to, consult and train nonprofit boards of directors on governance issues.

For more information, visit boardsource.org.

June 20–23, 2018

Society for Corporate Governance National Conference

—Renaissance Downtown, 999 9th Street NW, Washington, DC 20001 USA

The Society for Corporate Governance is dedicated to shaping corporate governance through education, collaboration, and advocacy. This year's theme is "Building Our Governance Capital."

For more information, visit societycorpgov.org.

June 21–23, 2018

2018 International Policy Governance Association Annual Conference

—Hilton Savannah DeSoto Hotel, 15 East Liberty St., Savannah, GA 31401 USA

This is the annual conference for boards, CEOs, and administrators using the Policy Governance® system, and young governance professionals and others exploring good governance. This year's event focuses on exploring governance excellence.

For more information, visit policygovernanceassociation.org.

June 25–28, 2018

International Corporate Governance Network Annual Conference

—Unicredit, Head Office, Piazza, Gae Aulenti 3, 20154 Milan, Italy

For more information, visit icgn.org.

July 9–10, 2018

International Conference on Corporate Governance

—Hotel Ambassador - Zlatá Husa, Václavské nám. 5 - 7111 24 Prague, Czech Republic

This event aims to bring together leading academic scientists, researchers and research scholars to exchange and share their experiences and research results on all aspects of corporate governance. It also provides a premier interdisciplinary platform for researchers, practitioners, and educators to present and discuss the most recent innovations, trends, and concerns, as well as practical challenges encountered and solutions adopted in the fields of corporate governance.

July 10–11, 2018

ICSA Annual Conference: The New Age for Governance

—ExCeL, Royal Victoria Dock, 1 Western Gateway, London, England E16 1XL UK

This year's program will explore the implications of the revised U.K. Corporate Governance Code and what it will mean for boards. It will also examine how business can prepare for Brexit, alongside a wealth of quality opportunities for professional and personal development.

For more information, visit icsa.org.uk.

Governance

(continued from page 5)

relinquish control over "how it's done" in favor of the fact that outcomes are being attained. In this environment of owner-centric decision-making, the Council can comfortably set its ends, effectively govern and delegate the means to the administration, and truly empower them to accomplish what they have been hired to do. The leaders can lead, the experts can fully utilize their expertise, and the citizens can enjoy increased benefit!

Results and Impact

The City of Red Deer is seeing the return on its investment in moving to the Policy Governance model. Administrative processes are being streamlined as the council's focus turns more and more toward the ownership linkage and moves away from the mechanics of operations. This shift in mentality is also starting to produce residual impacts that continue to build momentum. For example, because the council is focusing more on linking with its ownership and developing its policy set to reinforce this, there is less time to spend "digging into" operational details. This, in turn, empowers and charges the city manager with the responsibility to implement the mechanisms needed to accomplish council purposes. This further frees the administration to exercise its subject-matter expertise, which increases their buy-in to the process and, in the end, produces better services for the citizens. The more the council uses the model as it is intended to be used, the more this positive cycle will be perpetuated.

Conclusion

The City of Red Deer and its City Council made a brave and wise decision to move to a Policy Governance–centered model. The implementation of Policy Governance may have come with its challenges due to the aforementioned uniquely legislative and fundamentally public forum in which municipal governing exists. That said, working through such obstacles has helped the city reach a greater degree of commitment and success in relation to serving its citizens. The Red Deer City Council's decision to focus on the citizens as the true benefactors of the services the city provides—and learning to rely on a system of governance that allows for this focus—has truly sent the organization as a whole down a path that will continue to ensure citizens retain their rightful ownership of the direction the city takes now and in the future. ❑

CALENDAR OF EVENTS (continued)

SEPTEMBER 23–26, 2018

September Governance Institute Leadership Conference

—Encore at Wynn Las Vegas, 3131 Las Vegas Blvd. South, Las Vegas, NV 89109 USA

The Governance Institute offers current information, interactive sessions, expert speakers, and the opportunity to meet others with a similar commitment to improving governance and achieving optimal board performance.

For more information, visit GovernanceInstitute.com.

OCTOBER 7–10, 2018

October Governance Institute Leadership Conference

—The Broadmoor, 1 Lake Ave., Colorado Springs, CO 80906 USA

The Governance Institute offers current information, interactive sessions, expert speakers, and the opportunity to meet others with a similar commitment to improving governance and achieving optimal board performance.

For more information, visit GovernanceInstitute.com.

OCTOBER 14–16, 2018

Executive Retreat 2018: Coming Together to Discover, Collaborate, and Learn

—Loews Coronado Bay, 4000 Coronado Bay Rd., Coronado, CA 92118 USA

During this collaborative three-day program, you will have the opportunity to meet and connect with other nonprofit executives from throughout the United States and the sector who understand exactly what you're experiencing as your organization's chief staff leader. Together with a nationally respected faculty, you'll discuss what it takes to strengthen the leadership partnership between you and your board, as well as have the opportunity to have open and honest conversations with your peers about the unique challenges of your role. The course will encourage self-reflection and provide a "safe" place for sharing and learning.

For more information, visit boardsource.org.

News

(continued from page 1)

upsetting the chair and CEO. Corporate secretaries said that having directors with a tendency to "ruffle feathers" can have value as long as all directors maintain an appropriate level of respect for one another.

- How to carry out effective oversight of company strategy remains up for debate. According to the report, some corporate secretaries encourage specific strategy-focused sessions or retreats in addition to regular board meetings, but others stressed that strategy should be consciously integrated into every board meeting, not limited to an annual strategy meeting or retreat with management.

To access the report in full, visit https://www.conference-board.org.

Stellar

(continued from page 3)

need it, but if they have never formally gathered this kind of information, it won't exist in a time of emergency or decision-making.

Constantly evaluate whether the directors' skills, talents, and experience support the current strategy. In general, you will want directors who exhibit integrity, good judgment, strategic skills, financial literacy, confidence, and high-performance standards. But occasionally the board might also need an industry authority, an international expert, a turnaround specialist, or a government procurement professional.

Stellar Boards also encourage regular evaluations of directors and have a clear, agreed-upon purpose for conducting the evaluation. Do they want to improve overall performance? Individual performance? Drive shareholder value? Or eliminate someone from the board? Clarify how information will be collected, who will have access to it, and how it will be presented to the directors collectively and individually.

When doing board evaluations or committee evaluations, both interviews and surveys work. However, all records should be "paper and pencil" so they can be shredded to protect confidentiality. The minutes will represent a summary of the process, forms, action steps, and ratings, but only in general terms. Any papers distributed at meetings should be collected and destroyed.

Include an assessment of committees in a board evaluation. What is the quality of their reports? Are they transparent? Does the committee drive shareholder value? Make evaluations complete, thorough, and efficient. Asking each director to complete an exhaustive survey—or even worse, an exhaustive survey on each peer—requires an enormous use of time, and many of the directors either will not do them or will not do them in a timely fashion. When using a survey for the entire board or committees, customize it to the board's needs. Measure only those categories that are directly applicable.

Routinely evaluate the composition of the board, not just the performance of the directors. As the direction and strategy of the organization shift, so should the skills and experiences of the directors. Present the balanced findings to the board, encourage discussion, identify ways to leverage strengths, spotlight areas where adjustments need to occur, and formulate an action plan and timeline for moving forward.

In a confidential format, have directors evaluate their peers based on observable behavior that highlights how this person can add more value. Then, provide one-on-one, private feedback to each director, preferably delivered by a third party.

Ask the board to conduct separate evaluations of key executives at least once a year but seek timely feedback in executive sessions or private conversations. Above all, don't create materials that can be subpoenaed. Doing these things won't guarantee you'll have a well-run board, but you will have taken significant steps in the direction of goodness.

Conclusion

Corporate governance is on the move. Meltdowns and regulations cause change, but some things remain the same. We have come to demand more of our executives and directors. No longer can either group languish in a role and expect to keep it for life—not even in privately held companies. A volatile economy has shown us not to rest on our laurels too long, or we won't have any glory to rest on. Active, compliant directors and executives no longer offer organizations enough. Companies need and demand stellar governance from both individual contributors and the board as a whole. ❑

Thinking of publishing in Board Leadership? Contact Samara Kuehne for criteria at skuehne@wiley.com

BOARD LEADERSHIP

INNOVATIVE APPROACHES TO GOVERNANCE

BOARD LEADERSHIP: INNOVATIVE APPROACHES TO GOVERNANCE (Print ISSN: 1061-4249; Online ISSN: 1542-7862) is published bimonthly by Wiley Subscription Services, Inc., a Wiley Company, 111 River St., Hoboken, NJ 07030-5774.

Postmaster: Send all address changes to BOARD LEADERSHIP, John Wiley & Sons Inc., c/o The Sheridan Press, PO Box 465, Hanover, PA 17331.

Information for subscribers: *Board Leadership* is published in 6 issues per year. Subscription prices for 2018 are: **Personal Print Only:** \$181 (USA, Canada, and Mexico), £112 (UK), €141 (Europe), \$219 (rest of world). **Personal Print & Online:** \$198 (USA, Canada, and Mexico), £121 (UK), €153 (Europe), \$236 (rest of world). **Personal Online Only:** \$134 (all locations). **Institutional Print Only:** \$888 (USA), \$960 (Canada and Mexico), £524 (UK), €663 (Europe), \$1020 (rest of world). **Institutional Print & Online:** \$1110 (USA), \$1200 (Canada and Mexico), £655 (UK), €829 (Europe), \$1275 (rest of world). **Institutional Online Only:** \$888 (USA, Canada, and Mexico), £456 (UK), €576 (Europe), \$888 (rest of world). Prices are exclusive of tax. Asia-Pacific GST, Canadian GST/HST and European VAT will be applied at the appropriate rates. For more information on current tax rates, please go to www.wileyonlinelibrary.com/tax-vat. The price includes online access to the current and all online back files to January 1st, 2014, where available. For other pricing options, including access information and terms and conditions, please visit www.wileyonlinelibrary.com/access.

Delivery Terms and Legal Title: Where the subscription price includes print issues and delivery is to the recipient's address, delivery terms are **Delivered at Place (DAP)**; the recipient is responsible for paying any import duty or taxes. Title to all issues transfers Free of Board (FOB) our shipping point, freight prepaid. We will endeavour to fulfil claims for missing or damaged copies within six months of publication, within our reasonable discretion and subject to availability.

Customer Service: For ordering information, claims, and any enquiry concerning your journal subscription, please go to www.wileycustomerhelp.com/ask or contact your nearest office. **Americas:** Email: cs-journals@wiley.com; Tel: +1 781 388 8598 or +1 800 835 6770 (toll free in the USA and Canada). **Europe, Middle East, and Africa:** Email: cs-journals@wiley.com; Tel: +44 (0) 1865 778315. **Asia Pacific:** Email: cs-journals@wiley.com; Tel: +65 6511 8000. **Japan:** For Japanese-speaking support, Email: cs-japan@wiley.com. **Visit our Online Customer Help** available in 7 languages at www.wileycustomerhelp.com/ask

Wiley's Corporate Citizenship initiative seeks to address the environmental, social, economic, and ethical challenges faced in our business and which are important to our diverse stakeholder groups. Since launching the initiative, we have focused on sharing our content with those in need, enhancing community philanthropy, reducing our carbon impact, creating global guidelines and best practices for paper use, establishing a vendor code of ethics, and engaging our colleagues and other stakeholders in our efforts. Follow our progress at www.wiley.com/go/citizenship

View this journal online at wileyonlinelibrary.com/journal/BL

Publishing Editor: Samara Kuehne. **Editor:** Nicholas King. **Production Editor:** Mary Jean Jones. **Editorial Correspondence:** Samara Kuehne, Email: skuehne@wiley.com.

For submission instructions, subscription and all other information visit: wileyonlinelibrary.com/journal/bl

Printed in the USA by The Allied Group

Policy Governance is a registered service mark of John Carver.

JOSSEY-BASS™

A Wiley Brand

BOARD LEADERSHIP
INNOVATIVE APPROACHES TO GOVERNANCE

NUMBER 158, JULY–AUG. 2018

www.boardleadershipnewsletter.com

Can Shareholders Hold Directors Liable for Failing to Address Social Issues?

By Stephanie Resnick, Esq., and John C. Fuller, Esq.

Stephanie Resnick is office managing partner of Fox Rothschild LLP's Philadelphia office and chair of the Directors' & Officers' Liability & Corporate Governance Practice Group. John C. Fuller is an attorney with Fox Rothschild's Directors' & Officers' Liability & Corporate Governance Practice Group. In this article, they discuss the liabilities that boards and their leaders face if they fail to adequately address marquee social issues impacting their organizations.

Directors and officers face mounting pressure from shareholders to ensure that social issues are reflected in how their companies do business. The equal and proper treatment of women, maintaining data privacy, addressing the company's environmental impact, and promoting diversity are among the pressing social concerns shareholders are raising with directors and officers.

As companies consider how to address these important social issues, they must also consider potential legal liability for their failure to do so. As shareholder pressure increases and theories of liability and corporate injury continue to evolve rapidly, the stakes for corporations and their directors and officers have never been higher.

ALSO IN THIS ISSUE

Changing Corporate Culture: Address Harassment and Discrimination

Sexual harassment in the workplace is, unfortunately, not a new phenomenon. However, the rise of, among other things, the #MeToo movement has made the eradication of sexual discrimination and harassment a key concern for shareholders. Historically, companies have faced liability for the failure to properly address allegations of sexual harassment or sexual misconduct. In more recent cases, the allegations depict toxic work environments and willful blindness by directors. The trend should give directors and officers pause and prompt them to re-evaluate the integrity of their anti-harassment policies and the potential liability if the policies are not meaningfully enforced at all levels.

For instance, in the wake of allegations of pervasive sexual misconduct, gaming magnate Steve Wynn stepped down from his position as chairman of Wynn Resorts, Ltd. and shareholder derivative actions have followed. They focused not only on the alleged

(continued on page 2)

NEWS

Study links diversity, increased board engagement

Data collected on over 1,600 nonprofit boards show that American charities continue to struggle with the quest for diversity—and are missing out on some key advantages a diverse board offers in the way of internal and external engagement.

According to research conducted by the Lilly Family School of Philanthropy at Indiana University, nonprofit boards don't yet match up, proportionally, with the demographic breakdown of the general public in terms of age and race/ethnicity. The typical board has far fewer African-Americans, Hispanics and Asians than their actual population statistics would warrant—7.5 percent vs. 13.3 percent for African-Americans, 4.2 percent vs. 17.8 percent for Hispanics and 2.6 percent vs. 5.7 percent for Asians—and tend to skew quite a bit older as well. Women make up about 47 percent of nonprofit boards, pretty close to the 50.8 percent women make up of the American public overall.

According to Dr. Una Osili, associate dean for research and international programs at IU, the report confirms the advantages a diverse board offers, in three key areas:

- **Board member engagement**—the level at which board members participate in community building and outreach and are engaged

(continued on page 8)

Stellar

(continued from front page)

failures of the board to address purportedly known incidents of sexual misconduct or combat a corporate culture that condoned such behavior, but emphatically "connected the dots" from those alleged failures to address the conduct to resulting monetary damages stemming from the failure to do so.

The complaints against Wynn Resorts, Ltd. and its board cite the dramatic (10%) drop in share prices following the revelation of misconduct, as well as the company's downgrade in investment rating as bases of damages. The complaints also allege the creation of a separate entity used to pay a $7.5 million settlement to an alleged victim and the exposure of additional lawsuits. The complaints, however, also include allegations of loss in value based on prior statements by the company regarding a "Wynn premium" in reference to the value the company enjoyed from its association with Steve Wynn and his track record of success that has been lost as a result of his alleged actions and subsequent resignation. In addition, the complaints raise the possible loss of the company's gaming licenses in Nevada and other jurisdictions, where the relevant regulations contain prohibitions on associating with criminal or "unsavory" actors.

This case, among others making headlines, signals a fundamental shift in what constitutes an appropriate response to sexual harassment and abuse in the workplace. Implementing an anti-harassment policy and reacting to violations of the policy with settlement payments can no longer be considered a sufficient response. Directors and officers must reflect on whether their anti-harassment policies and reporting systems truly address and repair the corporate cultures that allow harassment, discrimination, and abuse to continue.

A successful anti-harassment policy must be enforced at all levels. It must be clear and direct with respect to what constitutes appropriate conduct. Regular trainings of employees, management, and the board should include specific examples of proper and improper conduct and should be tailored for the type of work environment and the nature of the interactions that occur between employees.

Trainings should also include clear instructions for making a report of harassment or discrimination. Moreover, employees should be provided with a list of individuals in the company who have been identified to receive and investigate complaints appropriately. Employees should be assured that all reports are confidential and that retaliation against a reporting employee will not occur. Management training regarding the processes for complaint investigation and escalation is also essential. Promptly addressing complaints and reporting them to upper management and the board for corrective action is critical. Indeed, if improper conduct is widely perceived and employee reports are received—but management fails to act—the system has utterly failed.

Moreover, if complaints, particularly those regarding high-level personnel, such as C-suite officers and business generators, are susceptible to being downplayed or disregarded, liability and substantial monetary damages will result, and criminal charges are also possible. For anti-harassment programs to remain effective, it may be necessary to ensure that reporting structures eliminate managerial discretion from escalating complaints and automatically generate reports to the board no matter how egregious.

Boards must take steps to ensure that robust anti-harassment policies are in place and—most significantly—that they are seriously considered and enforced at all levels of the company.

Ensuring Sufficient Safeguards for Digital Information

Individual privacy and the security of digital data have become social issues of their own. The technological safeguards and procedures for responding to cyberattacks are complex and often involve sophisticated technologies. Nevertheless, officers and directors must understand the steps their company is taking to protect its digital assets.

Despite some early unsuccessful attempts by consumers and shareholders to hold directors and officers liable for failures to address cyberthreats, recent litigation involving the catastrophic Equifax data breach may have created a new focus of liability for directors and officers when a data breach occurs.

In September 2017, credit monitoring and reporting firm Equifax announced a cyber "incident" that may have affected as many as 143 million U.S. customers. The misappropriated information included names, Social Security numbers, birth dates, addresses, and, in some cases, driver's license and/or credit card numbers.

One securities class action complaint filed in the wake of the breach asserted a direct nexus between oft-pled allegations that the company failed to maintain adequate measures to protect its data systems and the precipitous decline in Equifax's stock price following the announcement of the data breach. This connection between a data breach and a decline in stock price creates a tangible injury, which prior actions against directors and officers lacked. Equifax may have experienced a particularly conspicuous decrease in its stock price because its business is largely dependent on its ability to protect confidential consumer information. However, the theory that a decrease in stock price may create sufficient damage to support claims that a company or its directors and officers failed to adequately safeguard digital information may lead to increased litigation.

With data breaches of increased size and sensitivity continually in the headlines, directors and officers cannot merely rely on technology officers and employees to safeguard corporate data. Instead, they must be in a position to genuinely participate in the decisions made to protect the company's technological assets. To discharge their duties in evaluating threats and assessing whether their protections are adequate, directors and officers must personally understand how their company's technologies work and how the selected safeguards are designed to react to potential threats.

Part of developing appropriate security measures is responding—in some fashion—to every digital security incident. Because the reasonableness of cyberprotections is measured, in part, by the known and potential threats to specific industry or company, the failure to evaluate, learn, and upgrade security in response to smaller incidents could create liability if a catastrophic breach occurs. Indeed, otherwise mundane irregularities and innocuous anomalies may be preliminary attempts by cybercriminals to probe for weaknesses in a company's security.

Finally, the weakest link in digital security policies is often the human users. Regular trainings should help management and employees understand data-breach protocols and make them aware of email phishing and other scams cybercriminals use to gain access to corporate networks.

Ultimately, to implement effective data security, directors and officers must genuinely understand the threats their company faces, as well as the policies, technologies, and trainings they are deploying to meet those threats.

Staying Vigilant as Social Issues Emerge as Potential Sources of Liability

Directors and officers must continually evaluate and prepare to address social issues, such as environmental concerns, for which damages have long been difficult to demonstrate, but for which liability may be on the horizon.

For example, it has long been difficult for a shareholder-plaintiff to demonstrate how the failure of directors and officers to adopt environmentally conscious policies has adversely affected the company's earnings. In fact, in many cases, "green" policies decrease profits because they internalize environmental costs for which a company may not otherwise be financially responsible. However, recent analyses from firms such as Vanguard and BlackRock are beginning to examine how environmental concerns and sustainability should be factored into long-term corporate growth plans. As these analyses continue to gain mainstream acceptance, they may eventually be used by shareholders to demonstrate that a board's failure to plan for environmental costs has stifled long-term growth.

In addition, with increased pressure to bring environmentally conscious products to market, managers, directors, and officers face substantial liability if they fail to comply with strict environmental regulations. Volkswagen, for example, faced consumer and shareholder class actions in 2015 based on the declines in vehicle values and the company's stock after it was revealed that Volkswagen had programmed its diesel vehicles to produce acceptable emissions only during laboratory testing. Volkswagen was in the news again in January 2018, when its director of government relations stepped down amid allegations that he was aware of emissions testing on animals but did not inform the company's then-CEO.

The takeaway is that directors and officers must be vigilant in staying informed of emerging reports about the environment, as well as their company's practices for complying with regulatory and market pressures to create environmentally conscious products.

Encouraging Diversity Through Board Refreshment

Increased diversity in race, religion, gender, age, and other demographics of officers and directors is another social issue about which shareholders are demanding action. In many cases, increased diversity will create a board that is better equipped to deal with all of the social, political, and economic pressures companies face.

To attract and retain motivated directors and officers with diverse perspectives, a company must first examine the composition of its current board. One widely used mechanism to encourage refreshment and promote transparency in the board appointment process is evaluations of current directors and officers. Such evaluations help determine the skill sets and performance of individual officers and directors, and the board as a whole. Evaluations can help the company avoid liability by creating comparable data that directors and officers can rely on when identifying, addressing concerns with, and/or removing underperforming board members. In addition, having historical performance data can be particularly valuable where the prevailing board culture may have permitted underperforming directors and officers to remain.

Removing underperforming directors and officers, however, is only part of responsible board refreshment. Recruitment efforts must be under-

(continued on page 7)

FOOD FOR THOUGHT

"Consensus: The process of abandoning all beliefs, principles, values, and policies in search of something in which no one believes, but to which no one objects; the process of avoiding the very issues that have to be solved, merely because you cannot get agreement on the way ahead. What great cause would have been fought and won under the banner: 'I stand for consensus?"

Margaret Thatcher

The Hard and Critical Work of School Board Governance

By Cindy Elsbernd

Cindy Elsbernd is the vice chair of the Des Moines Public Schools board of directors in Des Moines, Iowa; a member of the second cohort of the IPGA Policy Governance Proficiency Program; founder and director of Iowa Kidstrong Inc.; the program manager for the United Way of Central Iowa's Well Kids Coalition; and an independent contractor with the Iowa Association of School Boards' Board Development Cadre. In this article, she discusses the application of Policy Governance principles in a school board setting.

I have served on the Des Moines Public Schools board of directors for a little over six-and-a-half years now. I've been a governing board member for about four of those. A perpetual process of reflection tells me that in those early years, I neither knew what it was I was supposed to be doing, nor did I understand the gravity of my ignorance. I certainly wasn't (and still am not) a bad person, nor did I have ill intent. I, like many, many others who find themselves sitting on a publicly elected school board, simply didn't know what the job was. I thought there was something else I was supposed to be doing—serving as a management advisory or coming up with the next great breakthrough school reform idea (because, hey, I had kids in the system and had also started and managed a small but successful nonprofit to support youth and liked to think of myself as a creative problem-solver). Maybe it was even a little bit about thinking my role was to provide servant leadership on what might equate to the most important and powerful of PTAs. Now—and I'm still not claiming to be perfect or to not have moments of regression—through development; experience; and a lot of reading, listening, and learning, I understand how even the best intent when focused in the wrong places can be damaging to achievement of the organizational mission and, more pointedly, harmful to students.

Seeing the Big Picture

Perhaps you have an even better and more seasoned vantage point than I do to see the big picture in school board governance. If not, let's take a look together at where boards of education (and sometimes superintendents too) get stuck, how that is harmful, and how a framework of principled governance that includes a robust monitoring plan and process affords boards the ability to direct management's job and rigorously evaluate its accomplishment without interfering. This in turn allows boards to be focused on the bigger picture and do the critical work of visioning for the future in account to their organizational ownership and for the benefit of the students they are trusted to serve.

I sometimes feel that what seems like the no-brainer stuff is often the hardest. Or maybe it's just the least fun. Or both. Regardless, school boards should take a significant amount of time to decide what it is they exist to do, how they are going to interact with each other and get their work done, how they are going to interact with their superintendent and delegate the authority bestowed upon them by those to which they are accountable, and how they are going to ensure the mission and organizational goals are accomplished in a prudent, ethical, and effective manner. Using Policy Governance® principles, this translates to determining organizational ends, the governance process, delegation to management, and management limitations. This requires a lot of dialogue, value for and consideration of diverse perspectives, and discipline … in perpetuity. It's not a one-and-done scenario or a "check it off the list and call it good" thing. That's because context changes over time, values change over time relationally with context, things advance, and things regress, and, therefore, the agility to respond becomes increasingly important. But what cannot be lost here is that the response needs to be intentional and done explicitly through policy—write it down and then expect it and only it (because someone—the ownership—expects it of you) until there comes a point where feedback tells you something different or new needs to be written down and expected. In the meantime, boards and board members need to stay in their lane while it's being worked out by the expert hired by the board and trusted to hire other experts, and so on, and so on throughout the organization.

Purposeful Monitoring

But if we don't insert ourselves in the mix, where it's all happening, how will we know? Boards know because they monitor. Easy enough, right? Apparently not though, because it often either doesn't happen or is mistaken for receipt of piles and piles of data and information that may or may not be accompanied by discussion that is not focused toward specified and meaningful indicators or is so hyper-focused and localized to actually be nothing about outcomes achievement, tending more toward a means and/or program and/or people focus. Various forms of data sifting and hyper-focus may be critical to management decisions, but not so much to the governance job—specifically to the type of performance monitoring that requires looking in the rearview mirror and understanding the trends exhibited and their meaning in having made progress toward and anticipating further progress toward a set of high-level priorities so that concentrated effort toward forward-looking adjustments and decisions can be made.

Does this mean outcomes-focused governance boards and board members care about words and data more than people? That they are cold-blooded and uncompassionate? Of course not. A board cares about employees and it cares about students and families; however, a board's expression of compassion and its use of capital toward ensuring their well-being is best demonstrated at the policy level—where systems-level movement and change can be fostered and vulnerabilities understood and mitigated.

Does it mean that these boards have given up authority to administration without any oversight but for the board's wielding of the infamous rubber stamp? Not at all. Boards who have done their scope of work in advance in accounting for the desired outcomes and defining bounds within which the superintendent must work through set and proscriptive management limitations, have iterated a tight values framework that acknowledges the board's prior approval and support for the superintendent to make operational decisions. It is a framework rooted in trust, but not absent of oversight. It's just that oversight is not defined by board interjection into individual management issues, as that is an arbitrary practice and risks under- or unvisited operational policy territory as well as low-level mitigation that could result in what may be systemic issues remaining unresolved. This might also prolong or propagate harm or risk to the organization and, more importantly, to the students it serves.

This also does not mean the absence of the board's capability to adjust expectations and boundaries when the board deems it necessary, but the board has to be having the right discussions based on evidence to know when that needs to happen. Time and again, school boards can quickly subscribe to the busy-ness of getting involved with operational issues or diving into rabbit holes based on single-case or nonrepresentative scenarios, embarking on a host of non-complementary tasks and directions without prioritization. This work is certainly easier and may even have the optic of being productive, but it isn't the right work, and though seemingly counterintuitive, this is often where oversight is lost. In sum, when you're constantly leaving the press box to run out onto the middle of the field to block and tackle, it's likely pretty fair to say that your eyes are most certainly not on the scoreboard, nor could you possibly be thinking about the season ahead, not to mention you may have missed penalties occurring throughout the whole game.

This is where monitoring, the seemingly (and maybe even understandably) much-maligned principle of governance, is so key. There's a lot for both boards and superintendents to get comfortable with in this process. Boards may wonder, if we're not receiving all data about all things, then what is it we're monitoring and how could that possibly be sufficient? What they're monitoring is every ends (organizational goals, outcomes, expectations) and management limitation policy, or, more precisely, the superintendent's interpretation of those policies and measure of compliance with them. And they're doing so according to a set calendar and methodology—again practicing intentionality so that there is no question of what needs to be prepared and by when to assure the best potential for quality information and to leave as little question as possible to the effectiveness of oversight and fiduciary stewardship.

Policy Interpretation and Application

There is a lot to unpack here, but assuming familiarity with what ends and management limitations policies are and that the board has thoughtfully constructed them, let's spend some time with the idea of interpretation. In Policy Governance, the inter-

(continued on page 6)

WHEN WE SAY…

Board Leadership's mission is "to discover, explain and discuss innovative approaches to board governance with the goal of helping organizations achieve effective, meaningful and successful leadership to fulfill their missions."

Board Leadership aims to fulfill this mission by engaging its readers in a lively and illuminating inquiry into how board governance can be made more effective. This inquiry is based on three key assumptions:

- Boards exist to lead organizations, not merely monitor them.
- Effective board governance is not about either systems, structures, processes, theories, practices, culture, or behaviors—it is about all of them.
- Significant improvements are likely to come only through challenging the status quo and trying out new ideas in theory and in practice.

Uniquely among regular publications on board governance, *Board Leadership* primarily focuses on the job of board leadership as a whole, rather than on individual elements of practice within the overall job.

Over time, *Board Leadership* will provide a repository of different approaches to governance created through its regular "One Way to Govern" feature.

Here's what a few of the key terms we use mean to us:

- **Innovative:** Creating significant positive change
- **Approaches:** Principles, theories, ideas, methodologies and practices.
- **Board governance:** The job of governing whole organizations. ❑

Governance

(continued from page 5)

pretation of the policy, including each policy level, must pass the "any reasonable person" test. In other words, could a reasonable person interpret or define the policy in the same way? And is there adequate data provided as evidence to determine targeted movement toward accomplishment of that outcome or avoidance of that limitation? These key questions can be tough for boards, as an interpretation that is reasonable may not fulfill the intent of the board. Additionally, individual board members, often depending on their level of discipline with their own compliance with the board governance process, may not distinguish personal opinion from majority board will—which in reality constitutes a whole different article, but for now will be addressed by advising adherence to the principle of Unity of Control, in that it is the voice of the board and not individual board members that constitutes board will and direction. Also with data, there can be the assumption that more is better, when in actuality quality is more significant and more is simply more, especially when it doesn't lend itself to providing assurance of accomplishment and when data fatigue has the potential to either confuse or stifle a board and the decision-making process.

So what's the remedy? There is no magic pill or drag-and-drop one-time answer here. It goes back to the idea of dialogue, diversity of perspectives, and discipline that happens repeatedly when the board is served a monitoring report through concurrent reflection on the policy itself and whether or not it is fulfilling the board's intent regardless of the story the data tells or if something was missed in policy design that needs to be addressed. It is important to note here, however, that a board's intended and therefore future expectation is not what they get to evaluate the superintendent on; rather, only the current policy and interpretation is fair game, as this is the board's shortcoming, not the superintendent's (and shortcomings can happen as a matter of course—it's just best to recognize, fix, and move on). The superintendent does, however, have the highly significant and consequential responsibility in providing a clear and clearly defensible rationale for their interpretation and to provide such in writing. This too takes work and discipline, but can go a long way in assurance of reasonableness and accomplishment of expectations or of transparency of accountability in missing the mark, because not only was it reasoned via narrative, but a level of the measure to be achieved was included—just like in math class, work was shown. And if the superintendent didn't do their job, the board has choices it can make, ranging from kicking the report back for additional work to resubmit at a subsequent meeting to accepting it with recognition of noncompliance to not accepting and issuing consequences of the board's determination.

It's important to remember that the board has other options outside of internal reports from their superintendent. The board can and should include external monitoring as part of its robust plan where auditors or other third-party means are accessed by the board to answer specific questions relative to policy and policy interpretation. The board may also apply direct inspection as a form of monitoring by which implementation or maintenance of a policy is examined through site visits with predetermined criteria compliance.

I'd also be remiss not to mention that monitoring isn't only reserved for superintendent performance. Boards should also include regular and disciplined monitoring of themselves against their governance process policies. Boards must also practice with integrity and transparency to their agreed-upon processes to assure coherent and functional governance on behalf of a broad ownership. They must also be forthcoming with the public regarding what their role is and, maybe even more importantly, what it isn't.

Choosing to Govern

At the end of the day, governance—real, true, solid governance—takes work and tending to and a focus on what is in the board's purview. The job is what it is, regardless of what the individual or constituent believes it should be (and the board should be exercising its power to inform that opinion, by the way).

Going back to the football metaphor used earlier, yes, playing often looks way more fun and the pace much more attractive than what can feel like overseeing the slow-as-molasses-on-a-cold-day progress toward meaningful change from a mile high in the press box. No one blames you if you want to play, but if that's the case, you need to reconsider your position and instead try out for the team. If you want to represent the players, become an agent. And if you want to call the plays, apply to be the coach. If you don't want to do that and at the same time don't want to let down either the players or the fans, then it's your job to let them know how your role is different from that of a player, player agent, or coach and then do the job you're supposed to, not theirs, by monitoring performance against predetermined goals and standards of fair play and planning for future results. And don't take it personally—it's a universal governance concept, and when everyone understands the rules of the game and where they fit, forward progress can be made with less chance of anyone getting hurt—even when the foul was unintentional—and the best part is, students gain the best potential to emerge the winners. ❑

Stellar

(continued from page 3)

taken not merely to fill vacant director and office positions or address shortcomings in diversity among directors and officers. Instead, directors and officers must critically assess the strengths and weaknesses of the collective board and determine the skills and attributes that should be prioritized among new directors and officers. Inviting shareholder input into a transparent process of determining these priorities may also aid shareholder relations and provide the directors and officers with a clearer understanding of shareholders' most pressing social concerns.

Ultimately, while diversity is often held out as a lofty corporate aspiration, developing a board with diverse qualifications and perspectives will enhance the board's effectiveness. Further, ongoing and transparent refreshment will ensure that the board reflects changing demographics and shareholders' increasing demand for socially responsible corporate governance.

Conclusion

As shareholders demand that companies' business practices are in line with prevailing social issues, claims that directors and officers have failed to properly address these concerns is a near certainty. The steps boards take today to stay genuinely informed about these issues, understand the sources of potential liability, and help evolve their corporate culture may be the only way to avoid substantial liability in the years to come. ❑

CALENDAR OF EVENTS

July 9–10, 2018

International Conference on Corporate Governance

—Hotel Ambassador - Zlatá Husa, Václavské nám. 5 - 7111 24 Prague, Czech Republic

This event aims to bring together leading academic scientists, researchers and research scholars to exchange and share their experiences and research results on all aspects of corporate governance. It also provides a premier interdisciplinary platform for researchers, practitioners, and educators to present and discuss the most recent innovations, trends, and concerns, as well as practical challenges encountered and solutions adopted in the fields of corporate governance.

July 10–11, 2018

ICSA Annual Conference: The New Age for Governance

—ExCeL, Royal Victoria Dock, 1 Western Gateway, London, England E16 1XL UK

This year's program will explore the implications of the revised U.K. Corporate Governance Code and what it will mean for boards. It will also examine how business can prepare for Brexit, alongside a wealth of quality opportunities for professional and personal development.

For more information, visit icsa.org.uk.

September 23–26, 2018

September Governance Institute Leadership Conference

—Encore at Wynn Las Vegas, 3131 Las Vegas Blvd South, Las Vegas, NV 89109 USA

The Governance Institute offers current information, interactive sessions, expert speakers and the opportunity to meet others with a similar commitment to improving governance and achieving optimal board performance

For more information, visit GovernanceInstitute.com.

October 7–10, 2018

October Governance Institute Leadership Conference

—The Broadmoor, 1 Lake Ave., Colorado Springs, CO 80906 USA

The Governance Institute offers current information, interactive sessions, expert speakers and the opportunity to meet others with a similar commitment to improving governance and achieving optimal board performance.

For more information, visit GovernanceInstitute.com.

October 14–16, 2018

Executive Retreat 2018: Coming Together to Discover, Collaborate, and Learn

—Loews Coronado Bay, 4000 Coronado Bay Rd., Coronado, CA 92118 USA

During this collaborative three-day program, you will have the opportunity to meet and connect with other nonprofit executives from throughout the United States and the sector who understand exactly what you're experiencing as your organization's chief staff leader. Together with a nationally respected faculty, you'll discuss what it takes to strengthen the leadership partnership between you and your board, as well as have the opportunity to have open and honest conversations with your peers about the unique challenges of your role. The course will encourage self-reflection and provide a "safe" place for sharing and learning.

For more information, visit boardsource.org. ❑

News

(continued from page 1)

in oversight and governing of the organization, and whether they stay on the board for the maximum time allowed.

- **Fundraising engagement**—as determined by whether board members meet with potential donors, whether they ask others for money, whether they personally contribute to the organization and whether they attend the organization's fundraising events.
- **Advocacy engagement**—the level at which board members engage with policymakers, monitor the impact of government policy and educate policymakers on their issues/program areas.

Per IU's research, female board members rated higher in all three categories, while younger board members also rated high in fundraising and board member engagement. Certain ethnic groups also correlated with increased engagement—most notably, Asians were highly rated in terms of fundraising effectiveness.

To access the study in full, visit https://bit.ly/2ELESH2.

Successful transitions often involve keeping founders involved, study shows

Many nonprofits struggle with succession planning, especially when it's the organization's founder that is moving on and being replaced with another leader. But while conventional wisdom has held that a "clean break" is often best in these cases—allowing the new executive to operate without the stress of the founder looking over his or her shoulders—that may not be the case after all.

In "Making Founder Successions Work," published recently in the *Stanford Social Innovation Review*, researchers from the Bridgespan Group reveal some interesting conclusions from an in-depth study of nonprofit founder transitions. Among the key findings:

- More nonprofit boards work out a continuing role for founders (45 percent) than pursue an amicable clean break (31 percent).
- Transitions that paired a founder and successor from inside the organization proved to be the most successful of all transition models.
- Involuntary breaks (24 percent), where founders are ousted by the board, tend to be the least successful.

"Bridgespan's research indicates that an extended founder role, when done right, can be the best path to maintain funder, board and staff loyalty, while allowing the new leader to benefit from the founder's capabilities and knowledge," said Jari Tuomala, coauthor of the study, along with Donald Yeh and Katie Smith Milway.

"Everyone wins, including the organizations and, most importantly, their beneficiaries," Tuomala said.

The study identified several practices used by interviewees to manage leadership transitions in their organizations, including starting early in planning for the transition; investing in developing internal successors; establishing frequent interaction between successors and board chairs; and maintaining active board engagement in the process.

In addition, the researchers put forth several recommendations that directly address the challenges that can arise when retaining an ongoing role for a founder, including:

- Engaging in regular coaching to help navigate operational and emotional aspects of the transition.
- Anticipating conflict and agreeing to a process to mitigate it.
- Transitioning board, funder and staff loyalty in logical order, so that they are shepherded to new leadership.
- Creating some initial separation, with a low profile for the founder, to allow the successor to settle in, particularly if the founder's new role is substantial or long-term.

For more information, visit http://www.bridgespan.org. ❑

BOARD LEADERSHIP
INNOVATIVE APPROACHES TO GOVERNANCE

BOARD LEADERSHIP: INNOVATIVE APPROACHES TO GOVERNANCE (Print ISSN: 1061-4249; Online ISSN: 1542-7862) is published bimonthly by Wiley Subscription Services, Inc., a Wiley Company, 111 River St., Hoboken, NJ 07030-5774.

Postmaster: Send all address changes to BOARD LEADERSHIP, John Wiley & Sons Inc., c/o The Sheridan Press, PO Box 465, Hanover, PA 17331.

Information for subscribers: *Board Leadership* is published in 6 issues per year. Subscription prices for 2018 are: **Personal Print Only:** \$181 (USA, Canada, and Mexico), £112 (UK), €141 (Europe), \$219 (rest of world). **Personal Print & Online:** \$198 (USA, Canada, and Mexico), £121 (UK), €153 (Europe), \$236 (rest of world). **Personal Online Only:** \$134 (all locations). **Institutional Print Only:** \$888 (USA), \$960 (Canada and Mexico), £524 (UK), €663 (Europe), \$1020 (rest of world). **Institutional Print & Online:** \$1110 (USA), \$1200 (Canada and Mexico), £655 (UK), €829 (Europe), \$1275 (rest of world). **Institutional Online Only:** \$888 (USA, Canada, and Mexico), £456 (UK), €576 (Europe), \$888 (rest of world). Prices are exclusive of tax. Asia-Pacific GST, Canadian GST/HST and European VAT will be applied at the appropriate rates. For more information on current tax rates, please go to www.wileyonlinelibrary.com/tax-vat. The price includes online access to the current and all online back files to January 1st, 2014, where available. For other pricing options, including access information and terms and conditions, please visit www.wileyonlinelibrary.com/access.

Delivery Terms and Legal Title: Where the subscription price includes print issues and delivery is to the recipient's address, delivery terms are **Delivered at Place (DAP)**; the recipient is responsible for paying any import duty or taxes. Title to all issues transfers Free of Board (FOB) our shipping point, freight prepaid. We will endeavour to fulfil claims for missing or damaged copies within six months of publication, within our reasonable discretion and subject to availability.

Customer Service: For ordering information, claims, and any enquiry concerning your journal subscription, please go to www.wileycustomerhelp.com/ask or contact your nearest office. **Americas:** Email: cs-journals@wiley.com; Tel: +1 781 388 8598 or +1 800 835 6770 (toll free in the USA and Canada). **Europe, Middle East, and Africa:** Email: cs-journals@wiley.com; Tel: +44 (0) 1865 778315. **Asia Pacific:** Email: cs-journals@wiley.com; Tel: +65 6511 8000. **Japan:** For Japanese-speaking support, Email: cs-japan@wiley.com. **Visit our Online Customer Help** available in 7 languages at www.wileycustomerhelp.com/ask

Wiley's Corporate Citizenship initiative seeks to address the environmental, social, economic, and ethical challenges faced in our business and which are important to our diverse stakeholder groups. Since launching the initiative, we have focused on sharing our content with those in need, enhancing community philanthropy, reducing our carbon impact, creating global guidelines and best practices for paper use, establishing a vendor code of ethics, and engaging our colleagues and other stakeholders in our efforts. Follow our progress at www.wiley.com/go/citizenship

View this journal online at wileyonlinelibrary.com/journal/BL

Publishing Editor: Samara Kuehne. **Editor:** Nicholas King. **Production Editor:** Mary Jean Jones. **Editorial Correspondence:** Samara Kuehne, Email: skuehne@wiley.com.

For submission instructions, subscription and all other information visit: wileyonlinelibrary.com/journal/bl

Printed in the USA by The Allied Group

Policy Governance is a registered service mark of John Carver.

JOSSEY-BASS™
A Wiley Brand