

MEMORANDUM

March 2, 2012

TO: County Council

FROM: Robert H. Drummer, Senior Legislative Attorney 

SUBJECT: **Action:** Bill 2-12, Personnel – Retirement Trust Funds – Emerging Investment Managers

Government Operations and Fiscal Policy Committee recommendation (3-0): approve the Bill as introduced.

Bill 2-12, Personnel – Retirement Trust Funds – Emerging Investment Managers, sponsored by the Council President at the request of the County Executive, was introduced on January 17, 2012. A public hearing was held on February 14 and a Government Operations and Fiscal Policy Committee worksession was held on February 27.

Background

Bill 2-12 would require the Board of Investment Trustees and the Consolidated Retiree Health Benefits Trust Board of Trustees to make a good faith effort, consistent with their fiduciary duties, to hire qualified emerging investment managers. The Board of Investment Trustees (BIT) is responsible for managing the assets in the Employees' Retirement Trust Fund. The Consolidated Retiree Health Benefits Trust Board of Trustees is responsible for managing the assets in the Consolidated Retiree Health Benefits Trust Fund. Both Boards regularly hire professional investment managers to fulfill this responsibility.¹

Under the Bill, an “emerging investment manager” means an investment manager with assets or product assets below the 75th percentile of their respective peer group or a new or developing investment manager. The Bill would require each Board to adopt guidelines to identify and evaluate qualified emerging investment managers. Each Board would also be required to report annually to the Council and the Executive on or before September 1 for the prior fiscal year. The report must:

- (1) identify each emerging investment manager used during the fiscal year;
- (2) list the percentage and dollar value of the assets of the trust fund, by investment sector, managed by each emerging investment manager; and
- (3) describe the good faith effort made to include qualified emerging investment managers in the procurement process during the fiscal year.

¹ The Consolidated Retiree Health Benefits Trust Fund was recently established and is just beginning to retain active managers. The Board has adopted similar policies and will ultimately follow similar guidelines to hire managers and invest funds.

The fiduciary duties of the Trustees are codified in Section 33-61C for the Board of Investment Trustees and in Section 33-163 for the Consolidated Retiree Health Benefits Trust Board of Trustees. Section 33-61C states:

- A fiduciary must discharge the fiduciary's duties regarding the retirement systems:
- (a) only in the best interest of the participants and their beneficiaries;
 - (b) only to provide benefits to the participants and their beneficiaries, and defray reasonable expenses of administering the retirement systems;
 - (c) with the care, skill, prudence, and diligence under the circumstances that a prudent person acting in a similar capacity and familiar with the same matters would use to conduct a similar enterprise with similar purposes;
 - (d) by diversifying the investments of the retirement systems to minimize the risk of large losses, unless it is clearly not prudent to diversify under the circumstances;
 - (e) according to a good faith interpretation of the law governing the retirement systems;
 - (f) according to a good faith interpretation of the documents and instruments governing the retirement systems, if they comply with this Article.

Both Boards have currently established internal service provider procurement policies that require the inclusion of emerging investment managers in searches if the firms meet the search criteria. The Policies require that special efforts be made to identify possible eligible emerging investment managers and regular reporting on staff meetings with emerging investment managers. A copy of the BIT Service Provider Procurement Policy is at ©13-23. As of January 31, 2012, approximately 6% of the ERS assets were managed by firms that qualified as an emerging investment manager when first hired.

The Bill would codify the current emerging investment manager policies of the Boards.

Public Hearing

Assistant Chief Administrative Officer Kathleen Boucher, testifying on behalf of the Executive, (©24) and Linda Herman, Executive Director for both Boards, testifying on behalf of both Boards, (©25) supported the Bill at the February 14 public hearing.

February 27 Worksession

Kathleen Boucher, Assistant CAO, Linda Herman, Executive Director for the BIT, Marc Esen, BIT staff, and Amy Moskowitz, Associate County Attorney represented the Executive Branch at the Government Operations and Fiscal Policy Committee worksession on February 27. The Committee reviewed the Bill and the current BIT policy on hiring emerging investment managers with Executive staff. The Committee (3-0) recommended approval of the Bill as introduced.

Issues

1. Are there other emerging investment manager programs in the State?

The Maryland State Retirement and Pension System established an emerging manager program in April 2007. In September 2008, the program was expanded and renamed Terra Maria, the Maryland Developing Manager Program. A description of the Program is at ©26-29. The State hired 7 program managers to find and recommend emerging investment managers for possible retention by the Chief Investment Officer. There is no formal maximum size for an emerging investment manager and there is no graduation program. Once hired, an emerging investment manager is retained based upon performance against an appropriate benchmark. Emerging investment managers currently manage approximately 8.6% of the System's assets under the Terra Maria Program.

2. What is the universe of emerging investment managers?

Investment manager performance is often evaluated by comparing it to relevant benchmarks and the results achieved by other investment managers investing in similar types of securities. Retirement funds also measure success by comparing their results with appropriate benchmarks and the results achieved by similar retirement funds. The investment performance for the County Employees' Retirement System (MCERS) has been in the top quartile of the universe of similar retirement funds for the 1-year, 3-year, and 5-year periods ending on December 31, 2011. A chart showing the results compared to the universe of funds tracked by different organizations is at ©30-32. MCERS has achieved these results with an asset allocation that is more heavily weighted toward private equity and real estate than the average for other public funds. A chart comparing the asset allocation of MCERS with the average public retirement fund is at ©33.

The BIT must sort through a large universe of investment managers to select one. A chart showing the universe of emerging investment managers compared to the universe of all investment managers for different classes of investment securities is at ©34. The Bill defines an emerging investment manager as a firm with total assets under management less than 75% of the managers in the relevant universe. For example, there are 1246 different products² in the large cap equity universe. An emerging investment manager must have less than \$85 million under management. There are currently 312 products that meet this criterion. Under current policy, the BIT staff continually monitors emerging investment managers and includes those managers in manager searches, where appropriate. An outline of the steps used by the BIT in a manager search is at ©35-36.

3. Should the Bill be enacted?

Although each Board has already adopted an emerging investment manager policy, this Bill would ensure that these programs continue regardless of future changes in Board membership. The current emerging investment manager policy helps to keep the market open

² The BIT looks at products rather than firms because one firm may offer more than one product. For example, one firm may offer both a large cap equity management and a small cap equity management service.

for new and developing investment managers without conflicting with the trustees' fiduciary duties of care and loyalty. Opening the market for new and developing investment managers increases competition among service providers and can enhance investment performance. **Committee recommendation (3-0):** approve the Bill as introduced.

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Bill No. 2-12
 Concerning: Personnel – Retirement
Trust Funds – Emerging Investment
Managers
 Revised: December 22, 2011 Draft No.1
 Introduced: January 17, 2012
 Expires: July 17, 2013
 Enacted: _____
 Executive: _____
 Effective: _____
 Sunset Date: None
 Ch. _____, Laws of Mont. Co. _____

COUNTY COUNCIL
FOR MONTGOMERY COUNTY, MARYLAND

By: Council President at the request of the County Executive

AN ACT to:

- (1) require the Board of Investment Trustees and the Consolidated Retiree Health Benefits Trust Board of Trustees to make a good faith effort to hire qualified emerging investment managers; and
- (2) generally amend the laws governing the Employees’ Retirement System and the Consolidated Retiree Health Benefits Trust Fund.

By adding

Montgomery County Code
 Chapter 33, Personnel and Human Resources
 Sections 33-60B and 33-162A

Boldface	<i>Heading or defined term.</i>
<u>Underlining</u>	<i>Added to existing law by original bill.</i>
[Single boldface brackets]	<i>Deleted from existing law by original bill.</i>
<u>Double underlining</u>	<i>Added by amendment.</i>
[[Double boldface brackets]]	<i>Deleted from existing law or the bill by amendment.</i>
* * *	<i>Existing law unaffected by bill.</i>

The County Council for Montgomery County, Maryland approves the following Act:

1 **Sec. 1. Sections 33-60B and 33-162A are added as follows:**

2 **33-60B. Emerging Investment Managers.**

3 (a) Legislative findings.

- 4 (1) Emerging investment managers, including businesses owned by
5 women, minorities and disabled individuals, should receive an
6 equal opportunity to provide investment management services
7 to the Board of Investment Trustees.
- 8 (2) The Board of Investment Trustees has adopted a policy
9 requiring its staff to identify qualified emerging investment
10 managers to participate in an investment manager search,
11 including regular monitoring of investment managers.
- 12 (3) Expanding opportunities for emerging investment managers
13 will increase competition.

14 (b) Definitions.

15 As used in this Section:

16 Assets means total client assets managed by an investment manager.

17 Emerging investment manager means:

- 18 (1) an investment manager with assets or product assets below the
19 75th percentile of their respective peer group; or
- 20 (2) a new or developing investment manager.

21 New or developing investment manager means an investment
22 manager:

- 23 (1) raising its first or second private institutional investment fund;
24 or
- 25 (2) creating its first institutional product.

26 Product Assets means client assets managed by an investment
27 manager in a single strategy.

- 28 (c) Consistent with the fiduciary duties established in Section 33-61C, the
 29 Board must make a good faith effort to remove any barriers that limit
 30 participation by qualified emerging investment managers to manage
 31 funds for the Employees' Retirement System.
- 32 (d) The Board must adopt guidelines to identify and evaluate qualified
 33 emerging investment managers. The guidelines must include
 34 procedures for:
- 35 (1) identifying possible firms;
 36 (2) reviewing, evaluating and interviewing emerging investment
 37 managers on an ongoing basis; and
 38 (3) maintaining research files on emerging investment managers.
- 39 (e) The Board must report annually to the Council and the Executive on
 40 compliance with this Section on or before September 1 for the prior
 41 fiscal year. The report must:
- 42 (1) identify each emerging investment manager used during the
 43 fiscal year;
 44 (2) list the percentage and dollar value of the assets of the trust
 45 fund, by investment sector, managed by each emerging
 46 investment manager; and
 47 (3) describe the good faith effort made to include qualified
 48 emerging investment managers in the procurement process
 49 during the fiscal year.

50 **33-162A. Emerging Investment Managers.**

51 (a) Legislative findings.

- 52 (1) Emerging investment managers, including businesses owned by
 53 women, minorities and disabled individuals, should receive an

54 equal opportunity to provide investment management services
55 to the Consolidated Retiree Health Benefits Trust Board.

56 (2) The Board has adopted a policy requiring its staff to identify
57 qualified emerging investment managers to participate in an
58 investment manager search, including regular monitoring of
59 investment managers.

60 (3) Expanding opportunities for emerging investment managers
61 will increase competition.

62 (b) Definitions.

63 As used in this Section:

64 Assets means total client assets managed by an investment manager.

65 Emerging investment manager means:

66 (1) an investment manager with assets or product assets below the
67 75th percentile of their respective peer group; or

68 (2) a new or developing investment manager.

69 New or developing investment manager means an investment
70 manager:

71 (1) raising its first or second private institutional investment fund;
72 or

73 (2) creating its first institutional product.

74 Product Assets means client assets managed by an investment
75 manager in a single strategy.

76 (c) Consistent with the fiduciary duties established in Section 33-163, the
77 Board must make a good faith effort to remove any barriers that limit
78 participation by qualified emerging investment managers to manage
79 funds for the Consolidated Retiree Health Benefits Trust Fund.

80 (d) The Board must adopt guidelines to identify and evaluate qualified
81 emerging investment managers. The guidelines must include
82 procedures for:

- 83 (i) identifying possible firms;
- 84 (ii) reviewing, evaluating and interviewing emerging
85 investment managers on an ongoing basis; and
- 86 (iii) maintaining research files on emerging investment
87 managers.

88 (e) The Board must report annually to the Council and the Executive on
89 compliance with this Section on or before September 1 for the prior
90 fiscal year. The report must:

- 91 (1) identify each emerging investment manager used during the
92 fiscal year;
- 93 (2) list the percentage and dollar value of the assets of the trust
94 fund, by investment sector, managed by each emerging
95 investment manager; and
- 96 (3) describe the good faith effort made to include qualified
97 emerging investment managers in the procurement process
98 during the fiscal year.

99 *Approved:*

100

101

Roger Berliner, President, County Council

Date

102 *Approved:*

103

Isiah Leggett, County Executive

Date

LEGISLATIVE REQUEST REPORT

Bill 2-12

Personnel – Retirement Trust Funds – Emerging Investment Managers

DESCRIPTION: This Bill would encourage the Board of Investment Trustees and the Consolidated Retiree Health Benefits Trust Board (Boards) to continue their current efforts to provide opportunities for emerging investment managers to manage some of the assets of the Employees' Retirement System Trust Fund and the Consolidated Retiree Health Benefits Trust Fund, consistent with their fiduciary duties.

PROBLEM: The Bill would codify the current procurement policies used by each Board which requires all investment managers who meet the stated criteria to be included in a search for a new investment manager. The Bill would also require the Boards to report annually to the Executive and the Council on the results of their good faith efforts to include emerging firms.

GOALS AND OBJECTIVES: The goal of this Bill is to provide opportunities for emerging investment managers to manage some of the assets of the Employees' Retirement System Trust Fund and the Consolidated Retiree Health Benefit Trust Fund.

COORDINATION: The Boards and the County Attorney's Office have reviewed this bill.

FISCAL IMPACT: See Fiscal and Economic Impact Statement.

ECONOMIC IMPACT: See Fiscal and Economic Impact Statement.

EVALUATION: N/A

EXPERIENCE ELSEWHERE: The State of Maryland, along with several other state and local pension systems, have recently enacted similar policies and laws requiring a pension system's governing body to make a good faith effort to use emerging managers.

SOURCE OF INFORMATION: Linda Herman, Board of Investment Trustees
Amy Moskowitz, County Attorney's Office

APPLICATION WITHIN MUNICIPALITIES: N/A

PENALTIES: N/A



OFFICE OF THE COUNTY EXECUTIVE
ROCKVILLE, MARYLAND 20850

Isiah Leggett
County Executive

MEMORANDUM

December 19, 2011

TO: Roger Berliner, Council President

FROM: Isiah Leggett, County Executive 

SUBJECT: Bill ___ - Personnel - Retirement – Emerging Investment Managers

I am transmitting for introduction at Council a bill that would amend the County Code to require the Boards overseeing the investment programs for the Employees' Retirement System (ERS) and the Consolidated Retiree Health Benefits Trust (CRHBT) to continue their current efforts to include emerging investment managers in the procurement of services for the investment programs. I am also transmitting a Legislative Request Report and Fiscal and Economic Impact Statement for the bill.

The bill would require the Boards to make a good faith effort to use emerging investment managers defined as: (1) an investment manager with assets or product assets below the 75th percentile of their respective peer group; or (2) a new or developing investment manager.

The current Service Provider Procurement Policies (Policies) of the Boards require the Boards to include emerging investment managers in searches if the firms meet the search criteria. The Policies require special efforts be made by the Boards' staff and its consultants to ensure identification of possible eligible investment managers to participate in the search process, including regular monitoring of investment managers and maintenance of research files on such investment managers to assist efforts when searches begin. In addition, the Boards receive quarterly reports from Board staff on meetings conducted with emerging investment managers and their analysis of the firms.

As of November 30, 2011 the Board of Investment Trustees committed approximately 6% of ERS assets with firms that were emerging investment managers when hired.

I am proposing this legislation to codify the current procurement policies used by the Boards which require all service providers who meet the stated criteria to be included in searches conducted by the Boards. The primary purpose of the legislation is to ensure that all service providers are afforded the opportunity to participate in procurement searches conducted by the Boards, to provide full transparency of the procurement process, and to ensure that the

Roger Berliner, Council President
December 19, 2011
Page 2

intent and goals of the current procurement practices remain in place regardless of future changes in Board membership due to terms expiring, changes to Board policies, or changes in Board Staff. The legislation would also require an annual report on efforts made by the Board to include emerging service providers.

Thank you for your prompt consideration of this bill.

Attachments (3):

Proposed Legislation
Legislative Request Report
Fiscal and Economic Impact Statements



OFFICE OF MANAGEMENT AND BUDGET

Isiah Leggett
County Executive

Jennifer A. Hughes
Director

MEMORANDUM

December 9, 2011

TO: Roger Berliner, President, County Council

FROM: Jennifer A. Hughes, Director

SUBJECT: Council Bill XX-11 – Personnel – Retirement – Emerging Investment Managers

Attached please find the fiscal and economic impact statements for the above referenced legislation.

JAH:hv

Attachments

c: Kathleen Boucher, Assistant Chief Administrative Officer
Lisa Austin, Offices of the County Executive
Joy Nurmi, Special Assistant to the County Executive
Joseph F. Beach, Director, Department of Finance
Patrick Lacefield, Director, Public Information Office
Michael Coveyou, Department of Finance
Linda Herman, Executive Director, Board of Investment Trustees
Amy Moskowitz, Office of the County Attorney
Helen Vallone, Office of Management and Budget
Naeem Mia, Office of Management and Budget
Blaise DeFazio, Office of Management and Budget

Office of the Director

101 Monroe Street, 14th Floor • Rockville, Maryland 20850 • 240-777-2800
www.montgomerycountymd.gov



Fiscal Impact Statement
Council Bill XX-11 – Personnel – Retirement – Emerging Investment Managers

1. Legislative Summary

The bill would amend the County Code to encourage the Boards overseeing the investment programs for the Employees' Retirement System (ERS) and the Consolidated Retiree Health Benefits Trust (CRHBT) to continue their current efforts to include emerging investment managers in the procurement of services for the investment programs. The Bill would require the Boards to make a good faith effort to use emerging investment managers defined as:

- an investment manager with assets or product assets below the 75th percentile of their respective peer group; or
- a new or developing investment manager

The current Service Provider Procurement Policies (Policies) require the Boards to include emerging investment managers in searches if the firms meet the search criteria. The Policies require special efforts be made by the Boards' staff and its consultants to ensure identification of possible eligible investment managers to participate in the search process, including regular monitoring of investment managers and maintenance of research files on such investment managers to assist efforts when searches begin. In addition, the Boards receive quarterly reports from Board staff on meetings conducted with emerging investment managers and their analysis of the firms. The bill also requires annual reporting to the County Council on efforts made by the Boards to include emerging investment managers.

2. An estimate of changes in County revenues and expenditures regardless of whether the revenues or expenditures are assumed in the recommended or approved budget. Includes source of information, assumptions, and methodologies used.

This bill has no impact to revenues or expenditures.

3. Revenue and expenditure estimates covering at least the next 6 fiscal years.

This bill has no impact to revenues or expenditures.

4. An actuarial analysis through the entire amortization period for each bill that would affect retiree pension or group insurance costs.

Not Applicable

5. Later actions that may affect future revenue and expenditures if the bill authorizes future spending.

This change will not result in subsequent government action that will impact future revenues and expenditures.

6. An estimate of the staff time needed to implement the bill.

Not Applicable

7. An explanation of how the addition of new staff responsibilities would affect other duties.

No change in staff responsibilities.

8. An estimate of costs when an additional appropriation is needed.

Not Applicable

9. A description of any variable that could affect revenue and cost estimates.

Not Applicable

10. Ranges of revenue or expenditures that are uncertain or difficult to project.

Not Applicable

11. If a bill is likely to have no fiscal impact, why that is the case.

The bill codifies the current procurement policies used by the Boards which require all investment managers who meet the stated criteria to be included in searches conducted by the respective Boards.

12. Other fiscal impacts or comments.

Not Applicable

13. The following contributed to and concurred with this analysis:

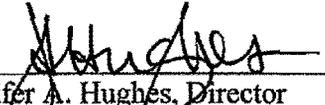
Linda Herman, Executive Director, Board of Investment Trustees and Consolidated Retiree Health Benefits Board

Amy Moskowitz, Counsel to the Boards, Office of the County Attorney

Helen Vallone, Office of Management and Budget

Naeem Mia, Office of Management and Budget

Blaise DeFazio, Office of Management and Budget



Jennifer A. Hughes, Director
Office of Management and Budget

12/19/11
Date

Economic Impact Statement
Council Bill XX-11, Qualified Emerging Investment Managers

Background:

This legislation requires the Boards overseeing the County's Retirement Plans and the Consolidated Retiree Health Benefits Trust to make a good faith effort to hire qualified emerging investment managers. A qualified emerging investment manager is defined as an investment manager with assets or product assets below the 75th percentile of their respective peer group; or a new investment manager who is raising its first or second private institutional investment fund; or creating its first institutional product. This legislation codifies current policy and practices of both Boards.

1. The sources of information, assumptions, and methodologies used.

Not Applicable. This legislation codifies current policy and practice, and its only requirement that is not currently in place is a requirement for an annual report, which the Boards state can be handled with existing resources.

2. A description of any variable that could affect economic impact estimates.

Not Applicable

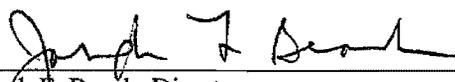
3. The bill's positive or negative effect, if any, on employment, spending, saving, investment, incomes, and property values in the County.

Not Applicable

4. If a bill is likely to have no economic impact, why that is the case.

This Bill codifies current policy and practice; therefore there is no economic impact.

5. The following contributed to and concurred with this analysis: David Platt, Finance; Mike Coveyou, Finance



Joseph J. Beach, Director
Department of Finance

12/5/11

Date

BOARD OF INVESTMENT TRUSTEES

MONTGOMERY COUNTY EMPLOYEE RETIREMENT PLANS



SERVICE PROVIDER PROCUREMENT POLICY

**BOARD OF INVESTMENT TRUSTEES
SERVICE PROVIDER PROCUREMENT POLICY
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**BOARD OF INVESTMENT TRUSTEES
SERVICE PROVIDER PROCUREMENT POLICY**

I. Purpose & Authorities

A. Purpose of Policy Statement/Board Requirements

The purpose of this statement is to define the policy of the Board of Investment Trustees (the "Board") regarding the procurement of external service providers. These services are required in the management of the investment programs for the Employee Retirement Plans (the "ERP") which include the Employees' Retirement System, Retirement Savings Plan and Deferred Compensation Plan. The policy statement is intended to foster competition and fairness while being flexible to meet the needs of a dynamic investment environment.

This policy does not cover procurement of Board office administrative services, which generally follows established County contracts and procedures (i.e., procurement of supplies, mini-contracts, etc.) and is set forth in the Board's Administrative Manual.

B. Statutory Board Responsibility and Authority to Contract for Services

Pursuant to Section 33-60 of the Montgomery County Code, the Board has the fiduciary responsibility for the governance of the ERP investment management programs and has exclusive authority to contract for services to meet this responsibility.

C. Board Exemption from County Procurement Regulations

Pursuant to Section 33-60 of the Montgomery County Code, the Board is exempt from the Montgomery County Government procurement regulations in the procurement of services for the management of ERP assets. However, as detailed in this policy, the Board adheres to a competitive procurement process in the procurement of service providers.

D. Communications Responsibilities

Official communications related to Board procurement processes and activities will be coordinated by Board Staff. Staff will report items of significance to the Board as appropriate.

II. Procurement of Service Providers - Procedures

A. Stage 1 – ERP Program requirements

- The Board will determine the services necessary to meet the goals of the program, including:
 - Hiring/Terminating of service providers
 - Number of service providers sought
 - Urgency/timeframe for search
 - Consultant support required

B. Stage 2 – Research Process

This stage involves determining search criteria and sources and the list of possible candidates that may meet Board needs as specified in Stage 1.

1. Criteria

Based on need, Staff will recommend a specific list of criteria for determining eligible vendors (“service providers”) for the ERP. The initial criteria will pertain to minimum requirements related to expertise in the service area being procured. The Board may add additional criteria to be used in a particular search.

2. Candidate sources

Although not limited to the sources listed below, Staff generally uses these sources to identify eligible candidates. Staff may also use sources identified by the Board’s consultant(s). The Board or Staff may recommend additional sources to be used in a particular search.

- Third-party databases including, consultant and other vendors
- Industry sources
- Marketing materials
- Institutional investor contacts
- Reports and sources used to identify emerging service providers
- Montgomery County resources and information

3. Emerging Service Provider and Minority Participation

The Board, Staff and consultants are committed to including emerging service providers, among prospective service provider candidates. Emerging service providers, including minority, female, and disabled owned firms, are broadly defined as:

- Firms with assets and/or product assets below the 75th percentile of their respective peer group
- New or developing firms (e.g. Funds I and II, or 1st institutional fund)

Special efforts will be made to ensure identification of possible eligible firms in the search process including:

- regular monitoring of above-referenced sources to identify possible candidates
- regular review of emerging service providers
- Staff interviews with emerging firms on an ongoing basis
- maintenance of research files on such firms to assist efforts when searches begin

4. Selection of Candidates

Based on criteria and sources noted above, Staff will prepare a list of possible candidates for a specific search. Staff, with the assistance of the investment consultant, generally will issue

a Request For Information (RFI) to the candidates selected. In special circumstances, with Board approval, Staff may not issue a RFI (e.g. using same service provider across County Plans).

Due to the nature of private market and non-marketable investment opportunities for the Employees' Retirement System Staff may not issue a RFI. Staff may identify opportunities based on criteria identified in Stage 2 and will evaluate the opportunity based on the criteria identified in Stage 3.

C. Stage 3 – Review and Verification Process

Stage 3 of the search process focuses on review and verification of information pertaining to the list of candidates identified in Stage 2. Completion of the Stage 3 process should result in the selection of a finalist.

1. Due diligence evaluations

Staff will complete a due diligence process to confirm findings identified in Stage 2. Those candidates deemed to be eligible will be interviewed by Staff, and the Board's consultant (if applicable), by phone or in person in the Board's office. Staff will prepare a summary of the candidate's evaluation which may include:

- Quantitative information resulting from Stage 2 criteria.
- Qualitative information related to candidate's experience, strategies and operations including:
 - organizational structure
 - experience and depth of personnel, including turnover
 - firm-specific operational philosophy
 - fees
 - references from Board consultant(s)
 - references from other sources
 - in the case of limited partnership arrangements such as private equity, real estate or hedge funds, fund-specific aspects including but not limited to liquidity and tax issues.
 - firm-specific legal/litigation issues

2. Selection of finalist(s)

Staff will usually conduct an onsite due diligence review of the finalist(s) which will include an interview, and prepare a report, along with a due diligence evaluation form, with input from the Board consultant resulting in a recommendation of a finalist(s) to the Board. The selection of the finalist(s) will be based on both quantitative and qualitative evaluations as well as interviews and results of reference checks.

3. Contracting

After Staff has selected any finalist(s), Staff, in conjunction with Board counsel, will evaluate the contract and governing documents to determine whether there are major issues with

the service provider's contract or governing documents that would prohibit the Board from entering into a contract.

D. Stage 4 – Board Selection of Finalist(s) and Contract Process

The Board will vote on Staff's recommendation of any service provider(s) at a meeting of the Board pursuant to Board bylaws. Staff, with assistance from the Board's counsel, will negotiate the terms of the contract or agreement.

1. Voting

The Board will vote based on all information made available by Staff, including information on the entire search process as summarized by Staff and the consultant, subsequent materials prepared for Board consideration, final interviews and due diligence meetings, as applicable. The Board will vote by formal resolution.

If the Board does not vote to accept Staff's recommendation, then the Board will determine at what stage to recommence the procurement process.

2. Contract process and negotiations

Staff will pursue contract negotiations, including terms related to fees, operational issues and guidelines, and will apprise the Board if needed.

A. Agreements may follow a format approved by the Board and generally will include provisions for:

- establishment of the account and assignment of management and fiduciary responsibility if required
- directions pertaining to the operations of the account
- directions pertaining to Board and Staff authorities and communications
- professional liability insurance for errors and omissions
- fee and terms of invoicing and payment
- contract termination upon notice by either Board or service provider
- Board required disclosures
- addenda related to Board policies and procedures, and operational guidelines

B. All service provider agreements will be reviewed by Staff and the Board's counsel to confirm conformance with Board policies and applicable law.

3. Contract execution

All agreements and contracts will be approved and executed in accordance with Board Bylaws.

III. Monitoring of Service Providers

A. Review process

Staff regularly conducts contract compliance reviews, including reviews of service provider performance, conformance to guidelines, organizational structure and any other performance requirements as specified in the service provider's contract. Service provider related matters other than performance and contract compliance matters will be reported to the Compliance and Audit Committee when deemed significant by Staff, i.e. if the matter(s) have a possible effect on the service provider's ability to perform as expected. Staff will apprise the Board of performance issues and make recommendations to the Board as necessary. The Compliance and Audit Committee will assess compliance issues and make recommendations to the Board as necessary.

Generally Staff conducts reviews of all aspects of the service provider's contract on an annual basis. The review may include a due diligence review in the service provider's office or the Board's office when necessary. Matters to be reviewed include but are not limited to the quantitative and qualitative factors which served as the basis for selection as a service provider.

Annually the Compliance and Audit Committee will review and report compliance by Board service providers with contract disclosure requirements

B. Contract modifications

With the exception of minor guideline or contract changes, Staff will advise the Board of any suggested modifications to the contract terms, whether requested by the service provider or by Staff. Staff, with the assistance of Counsel, will determine the appropriate method of modification, i.e. contract amendment or letter agreement. Staff will recommend an approval method and background information required by the Board to consider any such modification. Staff will prepare an annual report to the Board reflecting recommendations of modifications to service provider contracts.

With the exception of minor guideline and contract changes, the Board approves contract modifications through Board resolution. For all minor guideline and contract changes, Staff, in conjunction with Board counsel, has the authority to recommend that the Board Chair approve the contract modification.

For all private market and non-marketable investments, Staff, in conjunction with Board counsel, will have the authority to recommend approval/disapproval to the Board Chair of all amendments to the governing documents proposed by the fund manager.

IV. Termination of Service Providers

A. Basis for termination

With the exception of private market investments, the Board may terminate a service provider at any time and contract terms must provide for immediate termination upon written notice by the Board. Private market investments may not be easily liquidated and therefore immediate termination may not be possible. The Board may terminate service providers for any reason, including but not limited to one or more of the following reasons:

- ERP program changes
- Changes in the following:
 - people and organization of the firm
 - philosophy and process of investment strategy
 - resources dedicated to the investment strategy
 - performance of the product that is being reviewed

- Service providers -specific issues related to lack of adherence to contract terms or guidelines or any other changes in the service provider's business strategies.

B. Procedures

Staff provides background information regarding any basis for termination of a service provider to the Board. Action to terminate a service provider must be made by Board resolution. Staff determines and implements the appropriate account transfer/liquidation procedures, informing the Board as necessary.

V. Records Retention

Staff will maintain service provider records in the Board office. Service provider records will include search-related materials presented to the Board at the time of selection as well as legal and correspondence files. Records will be retained in accordance with Board office procedures. After the service provider relationship has ended, Staff will archive records in accordance with the Board office's records retention policy.

VI. Ethics

The Board, and as applicable, Staff, will at all times conform to Standard of Professional and Ethical Conduct adopted by the Board and County ethics laws. In addition, individual Board and Staff members will disclose to the Board any inherent, potential, or perceived conflicts of interest in dealing with specific service providers prior to taking any official action concerning any service provider.

Any violation of County or Board ethics rules by any Board or Staff member will be handled in accordance with County Government procedures.

VI. Policy Review

Staff and/or the Board will review and recommend amendments to this policy as necessary.

Amended:
July 22, 2011
May 21, 2010
January 11, 2008
December 7, 2007

(A) Due Diligence Evaluation – Liquid Investment Managers

Liquid managers will be evaluated using the following broad categories:

- People
 - Ownership/incentives
 - Quality of key professionals/team
- Organization
 - Assets under management
 - Commitment to improvement
 - Firm evaluation
- Philosophy/Process
 - Alpha – Idea generation
 - Portfolio construction
- Resources/Systems/Administration
 - Research resources
 - Information/compliance systems
 - Administration/back-office
 - Trading
- Performance
- Fees

(B) Due Diligence Evaluation – Illiquid Investment Managers

Illiquid managers will be evaluated using the following broad categories:

- People
 - Ownership/incentives
 - Quality of key professionals/team
- Organization
 - Assets under management
 - Commitment to improvement
 - Firm evaluation
 - Boards/committees/decision-making bodies
- Philosophy/Process
 - Investment process
 - Portfolio construction
- Resources/Systems/Administration
 - Research resources
 - Information systems
 - Administration/back-office
- Performance
- Fees

(C) Due Diligence Evaluation – Other Service Providers

Non-manager vendors will be evaluated using the following broad categories:

- People
 - Ownership/incentives
 - Quality of key professionals/team
- Organization
 - Assets under management/advisement
 - Commitment to improvement
 - Firm evaluation
- Philosophy/Process (may be non-applicable to certain vendors)
 - Idea generation
 - Portfolio construction
- Resources/Systems/Administration
 - Research resources
 - Information/compliance systems
 - Administration/back-office
- Other categories deemed critical for the search

Bill 2-12 - Personnel - Retirement – Emerging Investment Managers

Public Hearing

February 14, 2012

My name is Kathleen Boucher and I am an Assistant Chief Administrative Officer with the County Executive's Office. I am here to testify in support of Bill 2-12 on behalf of the County Executive.

This bill would amend County law to require the Boards overseeing the investment programs for the Employees' Retirement System (ERS) and the Consolidated Retiree Health Benefits Trust (CRHBT) to continue their current efforts to include emerging investment managers in the procurement of services for the investment programs.

The bill would require the Boards to make a good faith effort to use emerging investment managers defined as: (1) an investment manager with assets or product assets below the 75th percentile of their respective peer group; or (2) a new or developing investment manager.

The current Service Provider Procurement Policies (Policies) of the Boards require the Boards to include emerging investment managers in procurement searches if the firms meet the search criteria. The Policies require the Board's staff and consultants to make special efforts to ensure identification of possible eligible investment managers to participate in the search process, including regular monitoring of investment managers and maintenance of research files on such investment managers to assist efforts when searches begin.

In addition, the Boards receive quarterly reports from Board staff on meetings conducted with emerging investment managers and their analysis of the firms. As of November 30, 2011 the Board of Investment Trustees committed approximately 6% of ERS assets with firms that were emerging investment managers when hired.

The County Executive proposed Bill 2-12 for the purpose of codifying the current procurement policies used by the Boards and increasing transparency and accountability to those policies by establishing an annual reporting requirement. Under the bill, the Boards must submit a report to the County Executive and Council on or before September 1 which includes the following information:

1. identifies each emerging investment manager used during the fiscal year;
2. lists the percentage and dollar value of the assets of the trust fund, by investment sector, managed by each emerging investment manager; and
3. describes the good faith effort made to include qualified emerging investment managers in the procurement process during the fiscal year.

The primary purpose of the legislation is to ensure that all service providers are afforded the opportunity to participate in procurement searches conducted by the Boards, to provide full transparency of the procurement process, and to ensure that the intent and goals of the current procurement practices remain in place regardless of future changes in Board membership due to terms expiring, changes to Board policies, or changes in Board Staff.

Thank you for your consideration of this bill. I look forward to working with the Council as it reviews this bill.

**TESTIMONY FOR EXPEDITED BILL 2-12, PERSONNEL
RETIREMENT TRUST FUNDS**

Good morning, for the record, I am Linda Herman, Executive Director for the Board of Investment Trustees, which oversees the assets of the County’s three retirement plans, and the Board of Trustees, which oversees the assets of the Consolidated Retiree Health Benefits Trust. I am here today on behalf of the Boards to testify in support of Bill 2-12, Personnel – Retirement Trust Funds.

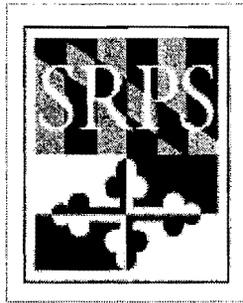
The proposed Bill would amend the County Code to require the Boards overseeing the investment programs for the Employees’ Retirement System (ERS) and the Consolidated Retiree Health Benefits Trust (CRHBT) to continue their current efforts to include emerging investment managers in the procurement of services for the investment programs. The Bill would require the Boards to make a good faith effort to use emerging investment managers defined as:

- investment managers with assets or product assets below the 75th percentile of their respective peer group; or
- new or developing investment managers

The Service Provider Procurement Policies (Policies) established by the Boards require the Boards to include emerging investment managers in searches if the firms meet the search criteria. The Policies require that special efforts be made by the Boards’ staff and its consultants to ensure identification of possible eligible investment managers to participate in the search process, including regular monitoring of investment managers and maintenance of research files on such investment managers to assist efforts when searches begin. In addition, the Boards require quarterly reports from their staff on meetings conducted with emerging investment managers and their analysis of the firms.

The Boards are committed to ensuring that all investment managers, meeting the search criteria, are afforded the opportunity to participate in procurement searches conducted and to providing full transparency of the procurement process. As of January 31, 2012 the Board of Investment Trustees has committed nearly 6% of ERS assets to firms that were emerging investment managers when hired.

We look forward to working with the Council in its deliberations on this legislation.



Maryland State Retirement and Pension System

Terra Maria: Developing Manager Program

In Public Markets and Private Equity

Updated February 2011

Terra Maria

The Maryland Developing Manager Program

Program Structure Outline

The Maryland State Retirement and Pension System (the "System") formed an emerging manager program in April 2007. In September 2008, the System revised, expanded and transformed the program into Terra Maria, the Maryland developing manager program. The initial Terra Maria program consisted of seven Program Managers in the public markets. Recently, the program was expanded to include private equity fund managers as described in Section II below.

I. Public Markets

The focus of the Terra Maria Program (the "Program") is on investment performance with an alignment of interests. An investment manager's product may only be represented once in the program, however, investment managers may have more than one product in the Program, if each product is recommended by a Program Manager.

The Program Managers are under contract with the System and recommend investment managers based on their ability to generate alpha relative to their assigned benchmarks. The Program Managers essentially represent an extension of the Investment Division Staff by providing due diligence, recommendations and ongoing monitoring of the underlying investment managers. The investment manager's accounts are maintained with the System's custodian bank.

Following are some key facets of the Program:

The primary focus of the Program is alpha generation, or performance. Program Managers and investment managers are evaluated primarily on performance relative to benchmarks. The Program Managers are instructed to focus on smaller investment managers. While the Program Managers apply no absolute maximum in terms of assets under management for purposes of recommending investment managers to the Chief Investment Officer (the "CIO"), the Program Managers are aware of the spirit of the program.

There is no formal "graduation" policy for this initiative. Investment managers that perform on a consistent basis may become eligible for larger allocations of funds, regardless of whether they are monitored by a Program Manager or staff.

The Program Managers are responsible for sourcing investment managers, performing due diligence, monitoring the retained investment managers, and presenting manager hire and termination recommendations to the CIO. All investment manager selections must be approved by the CIO.

The investment managers are part of the System's total portfolio and evaluated the same as any other investment manager in the portfolio. While investment managers may have been introduced to the System via a Program Manager, this has been done so primarily for administrative purposes. Once an investment manager has been "hired" by the CIO, they are part of the System's portfolio. Unlike the more traditional manager-of-manager programs, the CIO is ultimately responsible for the managers in the Maryland program, not the manager-of-managers.

Each Program Manager's benchmark is the weighted average of the benchmarks of the underlying investment managers selected by the Program. Investment manager benchmarks will be representative of the manager's investment style and aligned with the System's benchmark(s) within the manager's designated asset class. Benchmarks must be approved by the CIO.

Program Managers will make recommendations to the CIO regarding the initial allocation of funds to investment managers. In making recommendations, the Program Managers consider factors such as total assets under management by the investment manager on both a firm-wide and a product specific basis and also the total funding allocation to the Program Manager. In addition to portfolio asset allocation decisions, continued investment manager funding will be subject to the review of the investment manager's performance and an evaluation of the investment manager's business growth and organizational stability since the investment manager was initially funded by the System. The investment manager's performance will be evaluated on a continuous basis, although the Program Manager will have a formal review of the manager at least annually. Final decisions regarding funding and rebalancing decisions will be made by the CIO and Investment Division Staff.

If there are questions about the Terra Maria program in public markets, contact the Investment Division at 410-625-5621 or the individual Program Managers found in the attached Program Manager list.

II. Private Equity

The Terra Maria program has recently been expanded to include private equity investment managers. The System's private equity consultant reviews private equity funds and investment managers for potential inclusion in the System's Terra Maria program. The program is designed to include smaller managers, typically fund managers with less than \$2 billion in assets under management that are raising a private equity fund of up to \$500 million

whose funds otherwise satisfy the due diligence and investment case analysis performed by the private equity consultant and SRPS staff.

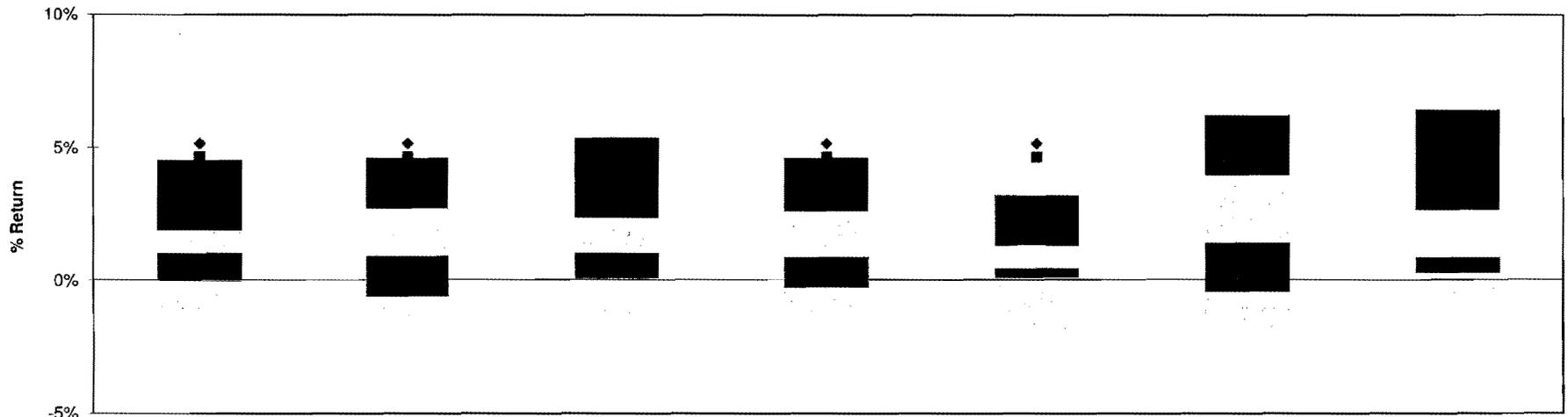
The portfolio will potentially include small and mid-sized buyout and early to late stage venture capital and debt funds.

The System will invest directly into the Terra Maria private equity funds. The System's consultant will provide reporting on the Terra Maria private equity funds as it does with other private equity investments made by SRPS.

If there are questions about the Terra Maria program in private equity, please contact the Investment Division at 410-625-5621 or the System's private equity consultant, Altius Associates, at 804-282-9000 or emergingmanagerinfo@altius-associates.com.

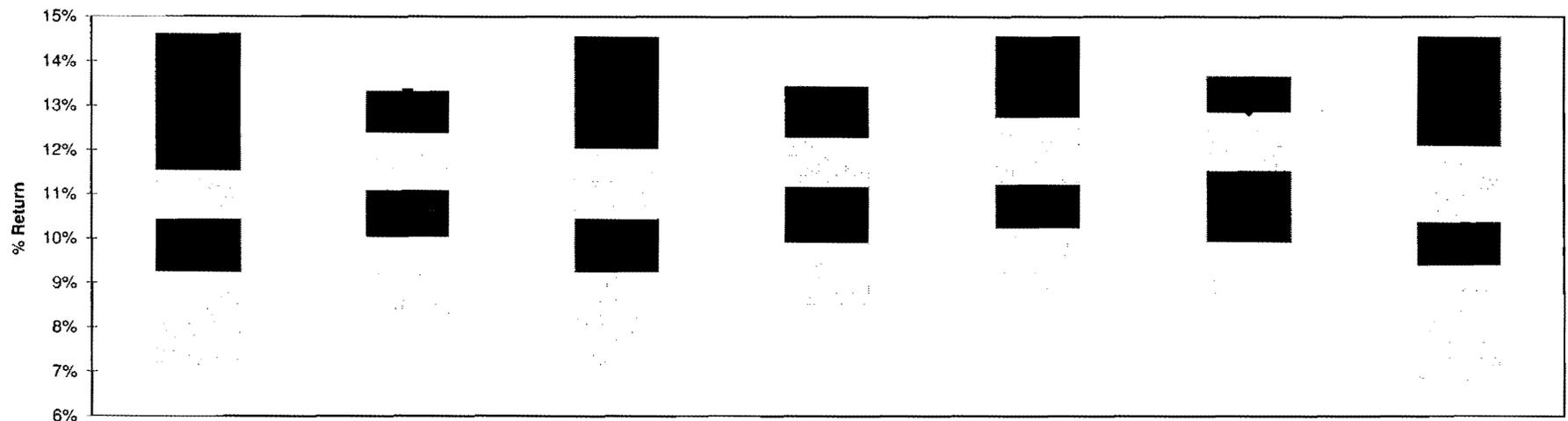
Attachment: Program Manager List

1 Year Performance by Quartiles - December 31, 2011



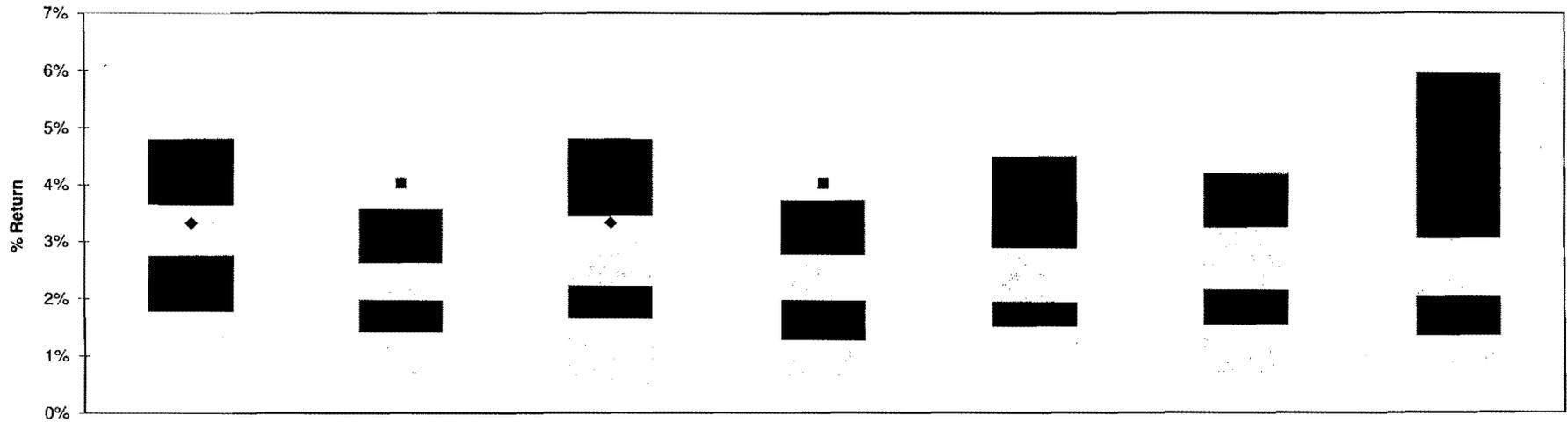
	Wilshire	Northern (All Public)	TUCS	Russell	Wilshire >\$1B	Northern >\$1B	TUCS >\$1B
■ MCERS	4.7%	4.7%	4.7%	4.7%	4.7%	4.7%	4.7%
◆ MCERS Policy	5.2%	5.2%	5.2%	5.2%	5.2%	5.2%	5.2%
1st Quartile	1.9%	2.7%	2.3%	2.6%	1.3%	4.0%	2.7%
Median	1.0%	0.9%	1.0%	0.9%	0.5%	1.4%	0.9%
3rd Quartile	-0.0%	-0.6%	0.1%	-0.3%	0.1%	-0.4%	0.3%
Number of Observations	136	40	137	111	37	133	62

3 Year Performance by Quartiles - December 31, 2011



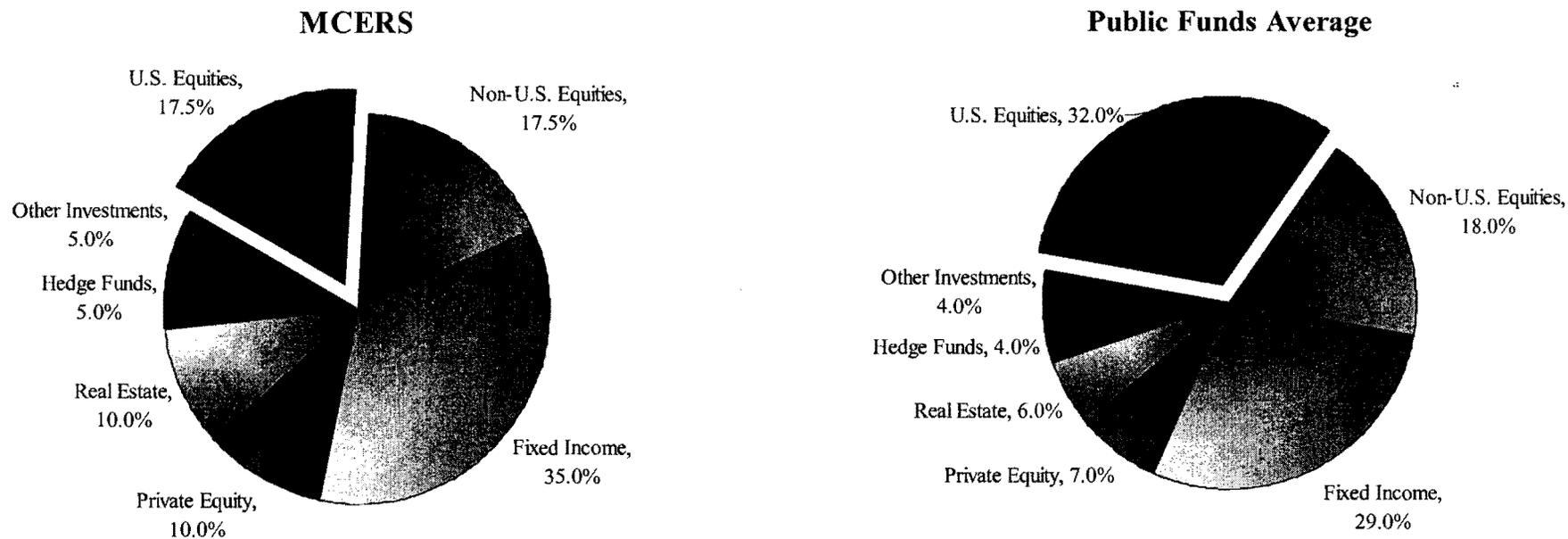
	Wilshire	Northern (All Public)	TUCS	Russell	Wilshire >\$1B	Northern >\$1B	TUCS >\$1B
■ MCERS	13.3%	13.3%	13.3%	13.3%	13.3%	13.3%	13.3%
◆ MCERS Policy	12.9%	12.9%	12.9%	12.9%	12.9%	12.9%	12.9%
1st Quartile	11.5%	12.4%	12.0%	12.3%	12.7%	12.9%	12.1%
Median	10.4%	11.1%	10.4%	11.2%	11.2%	11.5%	10.4%
3rd Quartile	9.2%	10.0%	9.2%	9.9%	10.2%	9.9%	9.4%
Number of Observations	132	38	133	101	37	104	59

5 Year Performance by Quartiles - December 31, 2011



	Wilshire	Northern (All Public)	TUCS	Russell	Wilshire >\$1B	Northern >\$1B	TUCS >\$1B
■ MCERS	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%
◆ MCERS Policy	3.3%	3.3%	3.3%	3.3%	3.3%	3.3%	3.3%
1st Quartile	3.6%	2.6%	3.4%	2.8%	2.9%	3.2%	3.0%
Median	2.8%	2.0%	2.2%	2.0%	1.9%	2.2%	2.0%
3rd Quartile	1.8%	1.4%	1.7%	1.3%	1.5%	1.5%	1.3%
Number of Observations	125	28	131	96	37	88	59

Asset Allocation – MCERS vs. Public Fund Peers



Historically, most emerging manager programs are focused in U.S. equities and core fixed income. MCERS has shifted \$400m from U.S. equities to other asset classes over the past 3 years and will be moving another \$300m in the next 2 years. A recent survey of public plans noted that 40% of pension funds stated they plan to shift assets from U.S. equities in the next 12 months.

Wilshire Database

Emerging Firms and/or Emerging Products by Asset Class

As of December 19, 2011

Emerging Managers and/or Emerging Products (bottom 25 percentile of product AUM)			
Asset Class	# of Total Products	Under 25% AUM	
		Limit (Million)	# of Products
U.S. Large Cap	1,246	\$85	312
U.S. Mid Cap	757	35	189
U.S. Small Cap	660	44	165
International/Global	1,831	78	458
U.S. Fixed Income	1,478	225	370
International Fixed Income	469	142	117
Total	6,441		1,611

Search Process – Public Market Investments

- **Database:** Staff utilizes Wilshire’s Compass, an industry leading database and analytics tool, to screen products/firms. Managers that contact Staff are encouraged to provide their information (returns, holdings information, etc.) to Wilshire. In addition, Wilshire maintains a robust database of emerging managers. There is no cost to be included in the database.
 - **Screening Managers:** RFI candidates are determined through a rigorous quantitative screening process. Risk adjusted returns and consistency of returns are some of the criteria being used for identifying RFI candidates. The data for each search is saved, with every step being documented in a MS Excel format.
 - **RFI Process:** RFI responses are summarized by Staff and discussed with the Consultant to determine semifinalists. Discussion notes and reason for inclusion/elimination are documented.
 - **Due Diligence:** Due diligence calls and meetings are conducted to obtain qualitative information on the firm, the investment team, the investment process, etc. Finalists are scored by category (per the Service Provider Procurement Policy) by Staff and further discussed with the Consultant.
 - **Investment Committee (IC):** Candidates which score highly, both quantitatively and qualitatively, are discussed at the IC Meeting. The IC members debate the merits of the recommendation and the Portfolio Manager provides additional information as necessary.
 - **Final Decision:** Board receives a presentation from the manager being recommended by Staff, and the consultant, and makes the final decision whether or not to hire the manager.
-

Staff Investment Committee – Operational Process

- Executive Director (*Linda Herman*)
- Senior Portfolio Manager – Fixed Income and Opportunistic (*Stuart Potter*)

- Senior Portfolio Manager – Private Markets (*Brad Stelzer*)
- Portfolio Manager – Public Equities and Commodities (*Marc Esen*)

