**Alameda County Employees'
Retirement Association**

ACERA

INVESTMENT GUIDELINES, POLICIES AND PROCEDURES

AMENDED January 31, 2000

ACERA
INVESTMENT POLICY
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Investment Policy

MISSION AND PURPOSE

The Alameda County Employees' Retirement Association (ACERA) exists for the exclusive purpose of providing accurate, timely benefits to its members and their beneficiaries and defraying reasonable expenses of administration.

The Board of Retirement (the Board), having sole and exclusive authority and sole and exclusive fiduciary responsibility for the investment and administration of the Trust, establishes the following General Investment Policies and Guidelines (The Policy) for the investment of ACERA's assets. The Board reserves the right to amend, supplement or rescind this statement at any time.

The Board of Retirement is directed by law and given discretion to prudently invest the plan assets. The purpose of this statement of policy is to assist ACERA in effectively supervising said investments and to encourage effective communication between ACERA and its investment managers and consultants.

The Trust's goal is to operate at a level of performance in the upper quartile of comparable pension funds on a risk-adjusted basis and to be as fully funded as possible so that ACERA's benefit costs do not become a burden upon future generations of members and taxpayers.

CONSTITUTIONAL REQUIREMENTS

Notwithstanding any other provisions of law or the California State Constitution to the contrary, the Board shall have plenary authority and fiduciary responsibility for investment of monies and administration of the system.

A. The Board shall have the sole and exclusive fiduciary responsibility over the assets of the retirement system. The Board shall also have sole and exclusive responsibility to administer the system in a manner that will assure prompt delivery of benefits and related services to the participants and their beneficiaries. The assets of the retirement system are trust funds and shall be held for the exclusive purposes of providing benefits to participants in the retirement system and their beneficiaries and defraying reasonable expenses of administering the system.

B. The members of the Board shall discharge their duties with respect to the system solely in the interest of, and for the exclusive purposes of providing benefits to participants and their beneficiaries, minimizing employer contributions thereto, and defraying reasonable expenses of administering the system. The Board's duty to its participants and their beneficiaries shall take precedence over any other duty.

C. The members of the Board shall discharge their duties with respect to the system with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with these matters would use in the conduct of an enterprise of a like character and with like aims.

D. The Board shall diversify the investments of the system so as to minimize the risk of loss and to maximize the rate of return, unless under the circumstances it is clearly not prudent to do so.

E. The Board, consistent with the exclusive fiduciary responsibilities vested in it, shall have the sole and exclusive power to provide for actuarial services in order to assure the competency of the assets of the system.

ELIGIBLE ASSET CATEGORIES

A. The Trust shall hold assets in categories established by the Board. Any asset class may be held in direct form, in pooled form or in both. Each asset class shall be under the management of one or more "Qualified Investment Managers" (these are called Managed Accounts) and/or under the supervision of the County Treasurer (called the Treasurer's Account). Eligible asset categories are listed and defined below.

B. **CASH** shall consist of short term interest bearing investments (18 months or less) of high quality: U.S. Treasury issues, insured certificates of deposit of U.S. banks (fixed and/or variable), commercial paper rated A-1, P- 1 or both, or other instruments of equal or better quality, and includes money market funds available through the Custodian.

C. **U.S. EQUITY** shall consist of common stocks and other securities which are convertible into common stocks, and ADRs, , as well as cash (per "B" above) and fixed income (per "E" below) when used as temporary substitutes for common stocks.

D. **INTERNATIONAL EQUITY** shall consist of common stocks and other securities convertible into common stocks of companies domiciled outside of the U.S. and GDR's, as well as cash equivalents and fixed income, domestic or international, which are being used as temporary substitutes for common stock.

E. **FIXED INCOME** shall consist of investments in U.S. taxable bonds, debentures, notes and other evidences of debt generally rated BAA or better by Moody's Investor's Services or BBB by Standard and Poor's. Upon approval by the Board, fixed income may include such instruments rated B or better by Moody's Investor's Services or Standard and Poor's. Other eligible investments include cash equivalents per "B" above and convertible bonds. Upon approval by the Board, fixed income may include non-dollar denominated bonds of investment grade standard issued by corporations or governments domiciled outside of the United States of America as well as Brady Bonds.

F. **MEMBER MORTGAGES** (closed program) shall consist of first mortgages, secured by the primary residences of the borrowers, underwritten to GNMA/FNMA standards by a qualified third party expert underwriter retained by the Board for that purpose.

G. **REAL ESTATE** shall consist of investments in equity real estate through the use of commingled or direct investments. For more information about real estate investments, refer to ACERA's Real Estate policy which is maintained as a separate document.

H. **ALTERNATIVE INVESTMENTS** shall consist of private equities, venture capital, or other non-traditional asset classes.

INVESTMENT PHILOSOPHY

The Board believes that some segments of financial markets are more efficient than others and offer fewer opportunities for adding value through issue selection. For efficient market segments, it is prudent to attempt to capture market-like returns while minimizing costs and risk exposure. The Board also believes that diversification among asset classes will reduce risk and enhance returns of the overall investment portfolio.

INVESTMENT STRATEGY

A. Domestic Equity:

The U.S. equity portion of the portfolio will be structured to capture exposure to the broad U.S. equity market as represented by the Russell 3000 Index. Passively managed (index) portfolios will be used in markets that are reasonably efficient. These portfolios are intended to provide broadly diversified market exposure with controlled (market) risk and minimal cost.

Actively managed portfolios will be used in less efficient markets when the Board determines that a manager possesses special skills or abilities that enable that manager to capture excess returns relative to the market, adjusted for risk and fees; or to exploit specialty markets that provide enhanced return with acceptable risk.

The greater part of the Russell 3000, on a market value basis is comprised of large- and mid-cap stocks, which the Board believes are efficiently priced most of the time. Therefore, the Board has adopted a policy of obtaining overall exposure to these segments of the market via passively managed indexed products. Some active managers have been employed to enhance overall portfolio return in the large- and/or mid-cap sectors on a risk- and fee-adjusted basis. These managers comprise ACERA's "high alpha" program.

The remainder of the Russell 3000 index is comprised of small to mid - cap companies. Some opportunities for active management enhancement exist in these securities due to market inefficiencies. ACERA will attempt to capture these opportunities through a mix of managers who have the special skills required to identify smaller companies that may be undervalued or possess substantial growth potential.

The equity portion of the portfolio shall be allocated among the various investment styles and managers as indicated in Schedules I and IA.

B. International Equity:

International equities represent an opportunity to diversify risk and capture enhanced returns within markets generally less efficient than the U.S. domestic equity market. The international equity portion of the Fund will be invested in actively managed portfolios.

C. Fixed Income:

Fixed Income represents a means for reducing overall portfolio risk and capturing incremental returns. Due to inefficiencies in the pricing and trading of fixed income securities, opportunities exist to add value through active management. The fixed income portion of the portfolio will be invested in actively managed portfolios.

D. Real Estate:

Due to the low correlation of returns between real estate and financial assets, real estate will be used as a means of diversifying the portfolio and capturing additional returns. Due to the illiquid nature of real estate assets distinctions between active and passive management are not applicable. For more information regarding real estate investments, refer to ACERA's Real Estate Policy which is maintained as a separate document.

ASSET ALLOCATION AND REBALANCING

Asset allocation targets, a function of the returns and risks from various asset classes and the nature of the plan's liabilities, are set forth in Schedule I of this statement. A goal of asset allocation is balancing asset growth versus liability growth considering time horizons, liabilities and risk tolerance.

Rebalancing is the risk control process of returning an allocation back to the desired target level after having drifted away from its targeted position. Acceptable ranges around the asset allocation targets are set forth in Schedule IA of this statement. The objective of rebalancing is to enhance the risk-adjusted performance of the asset allocation structure.

Staff shall be responsible for maintaining the relative weights of asset classes and investment allocations within the acceptable rebalancing ranges indicated in Schedule IA – Asset Allocation and Portfolio Rebalancing of this Investment Policy. Should an asset class or allocation fall outside its target range, staff shall rebalance the asset class or allocation back to the target weights as specified in the asset allocation structure in Schedule I. Staff shall: (i) Monitor the portfolio and (ii) Determine whether or not any asset category is out of balance with its target asset allocation in excess of the specified tolerance range; and (iii) Determine whether or not any manager within each asset category is out of balance with their target allocation in the excess of the specified tolerance range; and if so (iv) either instruct the relevant managers to redirect cash income (interest coupon and dividends), in concert with an evaluation of other cash flows (employer and employee contributions) and pending commitments, in order to redirect cash to the category(s) or manager(s) necessary to bring the allocation(s) back to the adopted strategic target; or (v) instruct the relevant managers to liquidate or acquire the appropriate dollar value of securities to go to target and reallocate the cash thus generated or required to the other category(s) or manager(s) necessary.

Staff shall report to the Board on a regular basis the status of the trust fund with respect to how investment categories are tracking relative to their allowable ranges as well as any actions taken to rebalance the portfolio.

ASSET CATEGORIES OBJECTIVES

A. General: The general investment objective of the Trust is to preserve capital and earn a return from appreciation and income, as described herein.

B. The minimum return objective shall be the current actuarial interest assumption plus 100 basis points per year. Returns shall be calculated net of fees.

C. The minimum return objective over a market cycle (up to five years) is 400 basis points (4%) per year over the national Consumer Price Index, published by the U.S. Department of Commerce.

D. The objectives of the cash portion are:

(1) A rate of return in excess of 90-Day U.S. Treasury bills.

(2) A rate of return within the upper one half of a universe of like short term investment funds.

E. The objectives of the U.S. Equity portion are:

(1) A rate of return in excess of the U.S. equity market as measured by the Russell 3000 Index after adjustment for risk and fees.

(2) A rate of return within the upper half of the Wilshire Co-op or similar database of the performance of equity managers.

F. The objectives of the International Equity portion are:

(1) A rate of return in excess of the Morgan Stanley Capital International Europe Australia Far East Index (EAFE)'

(2) A rate of return within the upper half or the Wilshire Co-op or similar database of the performance of international equity managers.

G. The objectives of the U.S. Fixed Income portion are:

(1) A rate of return in excess of the Lehman Aggregate Bond Index published by Lehman Bros. Inc.;

(2) A rate of return within the upper half of the Wilshire Co-op or similar database of the performance of fixed income managers.

H. The objectives for the Member Mortgage portion are:

(1) A rate of return that compares favorably with the Salomon Mortgage Index

(2) A delinquency rate of less than 2% of loans outstanding;

I. The objective for the Real Estate portion is:

(1) over rolling 5 year periods a minimum total real rate of return (net of management fees) of 6.0% using a "Time Weighted Market Value" calculation. The real return expectation is after inflation (U.S.A. CPI-Urban).

J. Individual investment managers shall be subject to objectives that reflect the particular investment strategy or style used by the manager. Such objectives shall be outlined in an attachment to the Investment Manager's contract.

ALLOCATION OF CASH FLOW

Cash flow not needed for benefit payments or the cost of operating the Trust, shall be allocated to Managed Accounts in a ratio that best funds the overall asset allocation as shown in Schedules I and IA.

Should cash flow be insufficient for the payment of benefits and operation of the Trust, then Managed Accounts shall be debited in a ratio that best serves fulfillment of the target allocation shown in Schedules I and IA. Such debits, if necessary, will be carried out as needed, and with timely notice to Managers to facilitate effective funds transitions and performance measurement.

For planned investments which may not beimmediately available, a reserve may be budgeted and invested in appropriate index funds until such moneys are required. Alternatively, Managed Accounts within "overfunded" asset classes may be called upon to provide the required moneys. Funds intended for real estate investments but not yet invested shall be divided equally and held in the equity and fixed income index funds until called by the real estate manager.

PROHIBITED INVESTMENTS

A. Securities issued by the County of Alameda or any agency thereof.

B. Commodities.

C. Warrants, if purchased separately.

DIRECTED BROKERAGE

ACERA does not engage in either directed commission arrangements or "soft dollar" transactions.

DERIVATIVE INSTRUMENT USAGE POLICY

The purpose of the policy is to guide ACERA's asset managers in their use of derivative securities within assigned portfolios. Use of derivatives is limited to those described below which in the aggregate add to portfolio volatility. Exceptions, and policy exemption process, are described below. Managers' use of derivatives MUST be in the best interests of the members and beneficiaries. Presently there are no derivatives in any of the measurement standards used by ACERA.

Due to the rapid development of derivative instruments, it is expected this policy will be frequently reviewed and amended. Managers are expressly requested to keep ACERA informed of all new, or significantly modified, generic derivatives.

I. Allowable Media:

A. CMO, PAC
B. CMO, Sequential
Above are limited to 10% of the portfolio at cost.

If their duration is more than +/- 15 years, based on a 100 bp rate move, then the limit is 2% of the portfolio at cost.

II. Disallowed Media:

A. Futures,
B. Written Options,
C. Swaps,
D. Structured Notes,

III. Exceptions:

A. Exception authorization must be obtained from the Board in advance of use of disallowed, "exotic" or other instruments.

B. The domestic equity index fund manager may use exchange traded S&P 500 futures, limited to 90 days maturity, and synthetic futures (long call + short put) with the same maturity limit, to securitize idle funds.

C. The domestic fixed income index fund manager may use exchange traded interestrate futures and options and/or engage in index swap contracts wherein the index used is (is a component of the benchmark.)

IV. Reporting Requirements:

Managers using derivatives at any point during a calendar quarter shall report as follows at the end of the quarter:

Type of derivatives (PAC, Floater, etc.)

Face value amount (and cost price if different),
Current price,
% of portfolio at cost,
% of current portfolio value,
Duration at cost,
Duration, current
Brief description of risk (per type).

ETI INVESTMENT POLICY

I. DEFINITIONS.

A. Economically Targeted Investment
An economically targeted investment ("ETI") is an investment which provides a competitive, risk-adjusted market rate of return while producing corollary benefits.

B. Corollary Benefits
Corollary benefits are consequential benefits of an investment other than the financial return of the investment, such as economic growth, new jobs affordable housing or infrastructure projects.

II. POLICY REASONS FOR INVESTING IN ETIs.

Due to cuts in government spending and the general down turn in the economy, ETIs have become increasingly popular on both the state and national level. Similarly, both state and national leaders have been encouraging pension funds to invest in ETIs. The goal of ETIs is to provide a competitive rate of return for the Fund and to promote corollary benefits.

III. THE BOARD'S FIDUCIARY DUTIES.

The investments must remain at all times consistent with the Board's fiduciary responsibilities under the California Constitution and Government Code, the Internal Revenue Code and guidelines of the U.S. Department of Labor. These responsibilities require the Board to: (1) act solely in the interest of and for the exclusive purpose of providing benefits to participants and beneficiaries, minimize employer contributions and defray reasonable expenses of administering the system; (2) act with care, skill, prudence and diligence of a prudent person; and (3) diversify investments thereby reducing the risk of loss and maximizing return unless under the circumstances it is clearly prudent not to do so. The Board's duty to the participants and beneficiaries takes precedence over any other duty.

If compliance with the guidelines set for the below, the Board in its decision to invest in ETIs will be consistent with its fiduciary duties. At the same time, the investments will produce corollary benefits for the economy and certain targeted groups of people. Accordingly, assuming all things are economically equal, the Board may select an ETI with corollary benefits. However, the corollary benefits will remain at all times a secondary concern; the financial aspects of the investment will be the primary concern.

IV. GUIDELINES FOR INVESTING IN ETIs.

A. ETIs are a Goal, Not a Mandate. Investment in ETIs is not mandatory, but rather a desirable investment option if they meet the required economic criteria.

B. Duty of Prudence.

1. Policies and procedures for investing in ETIs.

The Board will follow established policies and procedures to ensure that it prudently identifies potential ETIs and evaluates potential ETIs. Pursuant to these policies and procedures, the Board will give appropriate consideration to those facts and circumstances that are relevant to the investment or the investment course of action, including the investment's role in the Fund's overall portfolio. "Appropriate consideration" includes evaluation of the following factors:

(a) The risk and return of the ETIs in light of the composition of the portfolio with regard to diversification;

(b) The liquidity, current and projected returns of the ETI relative to the anticipated cash flow requirement of the fund.

2. <u>Economic Return will not be Sacrificed for the Corollary Benefits.</u>

The Board will ensure that the ETIs yield market rates of return adjusted for risk and administrative costs and that they are consistent with the financial and liquidity needs of the Fund. The absolute level of risk to be undertaken will be analyzed and approved upon consideration of each investment. The ETIs shall be comparable financially to other investments available to the Fund. Under no circumstances will the Board accept a lower rate of performance from the ETI. When projecting or evaluating "return" on an ETI, the Board will consider only the financial return and associated risk, <u>i.e.,</u> the economic factors, not the social factors. The Board shall establish a benchmark for each ETI prior to the acquisition of the ETI.

3. <u>Ongoing Evaluations.</u>

The Board will perform regular and ongoing evaluations of ETI performances in order to ensure that it is prudent to retain such investments. For the purposes of the evaluation, the performance of an ETI will be compared to the performance of a similar (i.e.: by type, size, geography, maturity and leverage) investment that is not considered to be an ETI.

C. <u>Diversification.</u>

The Board will ensure that the ETIs are part of an overall fund strategy of geographical and asset Diversification. The board will ensure that the investments are not concentrated in a limited geographical area. Thus, the Board will not invest all or an unduly large portion of the Fund's assets in any locale, thereby avoiding the risk of large losses to the Fund.

D. <u>Duty of Loyalty.</u>

1. <u>The Best Interests of the Fund and Participants and Beneficiaries.</u>

The Board will at all times act for the exclusive purpose of providing benefits to the participants and beneficiaries. Thus, the purpose of the Fund's ETI investments will be to provide retirement income to the participants. The interests of the participants and beneficiaries will not be subordinated to unrelated goals, <u>i.e.,</u> a desire to stimulate the economy or advance the social welfare of the a particular group or region. However, the Board may select an investment course of action that reflects non-economic factors as long as the application of those factors follows primary consideration of a broad range of investment opportunities that are, economically, equally advantageous.

2. Defray Reasonable Administrative Costs and Protect Fund Assets.

The Board will defray reasonable administrative costs and protect the Fund's assets. Thus, when performing due diligence on ETIs, the Board will either follow the same policies and procedures as used for other investments or it will have a consultant or investment advisor who specializes in ETIs to evaluate and recommend ETIs in order to ensure that it does not incur extra review and research costs.

E. Corollary Benefits.

The Board does not warrant that the corollary benefits that the particular ETI is intended to develop will actually develop. The Board is only responsible to the Fund and the participants and beneficiaries for obtaining the best financial return possible, it is not responsible to the beneficiaries of an ETI for the achievement of the expected corollary benefits.

SELECTION OF INVESTMENT MANAGERS

The Investment Committee shall direct staff and/or consultant to initiate searches for investment managers. Staff and/or consultant shall screen qualified candidates and present a list of finalists to the Investment Committee for its approval. Upon approval of the list, the finalists shall be interviewed by staff and consultant in a publicly noticed meeting at which no less than three (3) Investment Committee members shall be present. Staff and consultant shall evaluate the interviews, rank the finalists, and make a recommendation to the Investment Committee to hire one or more firms attaining the highest rankings. It is possible that none of the firms will be recommended for hire.

THE AUTHORITY OF INVESTMENT MANAGER IN THE MANAGED ACCOUNTS

A. Subject to the laws of the United States and the state of California, and to the terms and conditions of this statement, Managers shall have full discretion to direct the purchase, exchange, sale and reinvestment of the assets of the Managed Accounts. The Board expects that Managers will recommend changes to this statement when any part of this statement appears to be at variance with overall market and economic conditions.

B. Managers shall place orders to buy and sell securities and, by notice to the custodian bank (Custodian), shall cause the Custodian to deliver and receive securities on behalf of the Trust. Managers shall upon Board inquiry report placement of ACERA brokerage such that the Board shall be assured commissions were placed for the sole and exclusive benefit of the trust.

C. Separate account managers shall not vote proxies. Proxies shall be voted by ACERA according to Board established policy and procedure.

D. Securities lending shall be performed by the Custodian Bank under the oversight of the Board.

INVESTMENT GUIDELINES FOR THE MANAGED ACCOUNTS

A. General:

(1) All investments shall comply with all applicable laws of the United States and the State of California governing the investment of pension trusts.

(2) All securities transactions shall be executed by reputable broker/dealers, banks, or the Custodian, and shall be at best-price and best execution basis, and shall be reported to ACERA as is called for elsewhere in this statement.

(4) Assets in a Managed Account not invested in equity securities shall be kept at interest in appropriate money market instruments, including any money market fund available through the Custodian.

(5) A Managed Account shall be subject to ACERA's policy on derivatives.

B. Equity Portion

Managers have full discretion to invest solely in readily marketable and diversified equity securities as defined above subject to the following:

(1) For Managed Accounts other than passive index funds and those designated as part of the high-alpha program, no more than 5% of the value (at cost) of the account shall be invested in the securities of a single issuer.

(2) A Managed Account shall not hold more than 5% of the equity securities of any issuer.

(3) Equity securities shall possess value and quality corroborated by generally accepted techniques and standards of fundamental securities analysis.

(6) All managers shall endeavor to be fully invested in stocks at all times unless they have received specific authorization to the contrary from the Board. Cash holdings, as defined in this Policy, shall generally not exceed 5% of the portfolio on a market value basis.

C. Fixed Income Portion:

This portion shall be invested in readily marketable and diversified securities including, but not limited to:

(1) obligations of the U.S. Treasury;

(2) obligations guaranteed by an agency of the United States;

(3) insured certificates of deposit and banker's acceptances of credit worthy banks;

(4) corporate and other evidences of debt rated BAA or better by Moody's Investor's Services or BBB or better by Standard & Poors, provided that those issues rated BAA or BBB do not exceed 20% of a Managed Account. Upon permission by the Board, such fixed income instruments rated B or better by

Moody's Investor's Services or Standard & Poor's may be used.

(5) commercial paper and banker's acceptances of issuers rated P-1 by Moody's Investor's Services or A-1 by Standard & Poors Corporation.

(6) Excepting direct obligations of the U.S. Government, and those explicitly guaranteed by the U.S. Government, no account shall hold more than 5%, at cost, of the obligations of any single issuer.

(7) Fixed income derivative investments shall be in accordance with ACERA's derivative policy.

SEPARATE ACCOUNT MANAGER SPECIFICATIONS

1. Managers must be registered as investment advisors under the Investment Advisor's Act of 1940, a bank (as defined in that act) or an insurance company qualified to perform investment management services under state law in more than one state, including California. In addition, by accepting appointment as an investment manager for ACERA, Managers shall acknowledge that they are "Qualified Investment Managers" as defined by ERISA and "Plan Fiduciaries."

2. Managers shall maintain fiduciary insurance in the amount of 10% of the total assets managed in the ACERA account.

3. Managers shall promptly notify ACERA of changes that occur in any of the following:
   a. the investment strategy used in managing the subject product;
   b. the personnel involved in managing ACERA's account;
   c. the ownership, key personnel, or organizational structure of the company;
   d. the company's financial condition;
   e. the number of clients invested in the subject product;
   f. the market value of the total assets managed in the subject product

4. Managers shall promptly notify ACERA if they are subject to censure or disciplinary action by a regulatory agency.

5. On a monthly basis, Managers shall report on the activities of the portfolios managed on behalf of ACERA. Monthly reports shall include descriptions of holdings along with cost and market values; summaries of purchases and sales; description of major changes to the portfolio; and a statement that the Manager believes that its investment decisions are in accord with the provisions of this Statement.

6. On a monthly basis, active Managers shall certify in writing that the portfolio market values, transactions and performance data are reconciled with ACERA's master custodian.

7. On a monthly basis, Managers shall furnish a report detailing the entities for whose services were paid using soft dollars; the total amount of soft dollars used for such services; descriptions of the services purchased with those soft dollars. Consultants and the Master custodian are also required to report on their soft dollar usage.

8. On a quarterly basis, Managers shall provide ACERA an invoice for payment of fees for services rendered. The fee shall be calculated using the rate established in the fee schedule of the Manager's contract with ACERA and using the market values determined by ACERA's master custodian.

9. Managers shall provide the most recent copy Form ADV, Part II on an ongoing basis.

10. Managers shall not make contributions, provide gifts, reimbursements of expenses or provide personal benefits exceeding $250 in the aggregate within any 12 month period to any Trustee, fiduciary, employee or consultant of ACERA. Donations of educational conferences and similar events and benefits, including travel, meals and accommodations will be made to ACERA and not directed to individuals. The Board will determine whether to accept any donations and will be solely responsible for selection of the Trustee, staff member, or other individual, who will attend or otherwise participate on behalf of ACERA.

MANAGER MONITORING POLICY

The ACERA Board has contracted with a number of external investment managers to invest ACERA assets in the public equity markets. As part of the Board's fiduciary duties to prudently select, monitor and supervise these managers, the Board has adopted this policy. The intent of this policy is to notify managers of the standards by which they will be judged and to establish a structure which the Investment Committee and the Board can use to make monitoring decisions.

Managers will be monitored to (1) evaluate how well they achieve their investment objectives; (2) ensure they adhere to their established investment approach/style and do not attempt to index returns to preserve stellar performance or take extraordinary risk to overcome poor performance; (3) identify issues or trends that have the potential to result in losses to the Fund; and (4) alert the Board when Managers are not performing to expectations and to take appropriate remedial action. Managers will be monitored and evaluated in terms of performance, style integrity, organization, compliance, and client service.

1. PERFORMANCE

On a monthly basis staff will monitor investment manager holdings, activity and performance.

On a quarterly basis staff and/or consultant will furnish the Investment Committee and/or Board an in-depth evaluation of each manager which will include a comparison of the manager to its contract benchmark and a peer universe of managers using a similar investment style. This report shall include an analysis of the sources of managers' returns (stock selection, industry selection, asset allocation, etc.) and shall identify which decisions enhanced or diminished performance.

On a quarterly basis, trading costs will be evaluated in terms of commissions paid and execution of trades. Staff and/or consultant shall furnish a report to the Investment Committee and/or Board regarding trading costs on an annual basis.

2. STYLE INTEGRITY

Each manager will be analyzed at least annually to ensure that the manager is continuing to invest the portfolio in the style for which they were originally hired. Style integrity is essential to maintaining the Board's asset allocation policy. Any significant deviation in style will result in the overall portfolio having a different characteristic, in some measure, than the broad market which is represented by the Russell 3000 index. Significant variations in the portfolio characteristics from the style anticipated in the management contract may indicate a change in investment style.

This review also provides the Investment Committee and/or Board an opportunity to evaluate the manager's continuing "fit" with the goals of the overall fund. By monitoring manager style the Investment Committee and/or Board can assure that its manager mix takes advantage of opportunities to increase diversification through lower correlation of returns among individual managers.

3. ORGANIZATION

Managers' organizations will be monitored to ensure continuity of the intellectual and philosophical processes that went into developing the particular investment approach contracted by ACERA. In addition, managers will be monitored for business risk, quality of staff and potential conflicts of interest.

It is ACERA's intent that its portfolio comprise no more than 40% of the manager's total assets under management. Therefore ACERA will monitor managers' assets under management firmwide as well as in the subject product.

4. COMPLIANCE

Managers will be monitored to ensure they are adhering to federal and state laws regarding securities and the management of investment portfolios, trading, and pension investments; ethical practices of the investment professions; the Contract governing their relationship with ACERA; and the policies and guidelines set forth in this policy statement and any other written directives issued by ACERA.

Each ACERA contract will specify which investment vehicles a manager is authorized to use, which markets the manager is authorized to transact business in and any limitations within a market (small or large capitalization, value or growth orientation). The assets in each manager's portfolio shall be reviewed monthly to ensure compliance with contract guidelines.

All required documents and reports must be submitted in a timely manner and in the format specified by ACERA.

Managers must provide prior notification and justification for failure to comply with rules, regulations, contracts, deadlines or other directives. Managers must provide a time frame for curing the deficiency. Staff shall evaluate each incident on a case-by-case basis and determine if an exception may be granted.

5. CLIENT SERVICE

Managers are required to comply with routine portfolio investment guidelines and reporting deadlines and are also expected to cooperate with special requests for information. ACERA will establish reasonable time frames for all requests and reporting and will provide feedback to all external equity managers regarding the perceived quality of their client service.

ACERA staff will endeavor to meet with each manager at least twice a year by telephone or in person to review performance and other issues.

CONTRACT REVIEW PROCESS

If during the course of regular monitoring, ACERA determines that a manager's performance, style, organization, compliance, or client service has declined to unacceptable levels, the manager shall be subject to ACERA's Contract Review Process. There are generally three levels in the formal Contract Review Process: Watchlist, Probation, and Termination. However, ACERA reserves the right to terminate an investment management contract upon 30 days notice for any reason.

The Contract Review process may result in one or more of the following consequences, or any other deemed appropriate by the Board:

a. Placement of a manager on watchlist or probation status
b. Movement of a manager from one status to another or removal from the contract review process
c. Reduction of assets under management
d. Revision of investment contract guidelines for that manager
e. Re-negotiation of fees
f. Termination of a manager's contract

The following criteria for Watchlist, Probation or Termination are general conditions that would initiate the formal Contract Review Process. Each situation is unique and will vary depending on the type of manager and the style/strategy involved.

INITIAL REVIEW

Prior to a manager being considered for Watchlist, Probation or Termination several steps should be taken:

1. Analysis

Staff will conduct more in-depth analyses of the perceived deficiency to verify that the deficiency exists, form an initial assessment of the severity of the deficiency, and make an initial determination of possible causes.

2. Discussion with the Manager

Staff will contact the manager to discuss the situation and the results of staff's analysis.

3. Consultant Input

The consultant shall be asked to provide additional assessment and advice regarding the situation, depending on the severity of the deficiency.

All phases of account compliance may be reviewed during this phase, in addition to the specific issue that originated the review process.

FORMAL ACTION

After completing the Initial Review, Staff may recommend to the Investment Committee and/or Board that the manager be either placed on Watchlist or Probation or, in certain cases, Terminated. (The specific criteria for determining which level of Contract Review to recommend is outlined later in this policy section and summarized in tabular form in Schedule II.) The Committee and/or Board will approve or reject the recommendation.

Upon approval of a Watchlist or Probation recommendation, staff will initiate the following actions:

1. Staff will notify the manager of the Board's decision and will provide the

manager with a statement of concerns which outlines the areas which need improvement.

2. The manager will be asked to respond in writing with an explanation of the issues and a proposed action plan to resolve the issues.

3. Staff, consultant and the manager will collectively draft a Plan of Action. The plan will identify 1) the specific steps to be taken to correct the problem, 2) the time frames for further review, and 3) what additional monitoring may be required.

At the end of the time period specified in the Plan of Action, the manager's success in resolving the issues identified in the Plan will be evaluated. Based on this evaluation, one of the following actions will be taken:

1. Removal from Contract Review: The manager will be removed from Watchlist or Probation after successfully resolving the issues in its Plan of Action and demonstrates continued success in all other areas of its relationship with ACERA.

2. Movement from Probation to Watchlist: If the Manager has satisfied all or most of the issues that caused it to be placed on Probation, yet staff continues to have less severe concerns about the manager, staff may change the manager's status from Probation to Watchlist. If circumstances warrant, a manager may also be moved from Watchlist to Probation at any time during the Contract Review process.

3. Extension of Contract Review: A Manager may be given additional time to satisfy the conditions of its Plan of Action if reasonable progress is being made but is not complete. Temporary extensions may also be granted if unfavorable market conditions or high costs make reallocation of assets inadvisable.

4. Termination: If the Manager has not satisfactorily resolved the issues in its Plan of Action, Staff may recommend terminating the relationship. Details of termination procedures are included at the end of the policy section. Termination may be recommended at any time during the Contract Review process if circumstances warrant.

WATCHLIST

Watchlisting indicates an increased level of concern, but does not indicate major deficiencies. The Watchlisting period is typically one year. The guidelines for placing a manager on Watchlist are as follows:

1. UNDERPERFORMANCE

- Index Managers

Index Managers are expected to closely track the specified benchmark within 5 basis points of the benchmark return on an annualized basis.

- Active Managers

The manager's cumulative returns on a three year rolling average or since inception, whichever is shorter, are below the contract benchmark (see Schedule III) by 50-150 basis points and remain so for two consecutive quarters; and/or

The manager's cumulative returns on a three-year (five-year, if high-alpha) rolling average or since inception, whichever is shorter, cause the manager's ranking amongst its peers in the Wilshire Co-Op database to fall below median in terms of performance for two consecutive quarters.

New managers will not be evaluated until the completion of 4 full quarters of performance.

2. STYLE DEVIATION

Managers are expected to adhere to the style of investment management for which ACERA originally hired them. Changes in portfolio characteristics or style drift may lead to a Watchlist recommendation.

3. ORGANIZATIONAL CHANGE

NEW OWNERSHIP
Relatively benign ownership changes, resulting in people key to ACERA's portfolio management remaining as a team and relatively autonomous may be cause for a Watchlist recommendation.

TURNOVER
Significant turnover in top management, portfolio managers, research or trading staff, or marketing personnel, which does not directly affect the team responsible for ACERA's account may warrant Watchlisting.

REORGANIZATION
Changes which signal management deterioration or hasty growth in the firm and have the potential to disrupt the investment team hired for management of the ACERA account may justify Watchlisting.

ASSETS UNDER MANAGEMENT
If the market value of ACERA's portfolio rises above 40% of the manager's total assets under management, Watchlist may be recommended.

4. COMPLIANCE

CONTRACTS AND OTHER AGREEMENTS
Managers are expected to comply with the investment management contract, investment guidelines, or other directives. Non- or partial compliance may result in a Watchlist recommendation.

UNAUTHORIZED INVESTMENT
A manager who purchases unauthorized investments or leverages the account must liquidate all such securities in accordance with guidelines established by the staff. Managers shall reimburse ACERA for any losses that may occur in the liquidation of an unauthorized security. Watchlisting is appropriate even if all guidelines for correction are complied with to ensure that no further unauthorized purchases take place.

REPORTING
Staff will contact managers to request past due reports. If the manager's reports are consistently delinquent, the payment of fees may be delayed. If a manager cannot comply with reporting deadlines, the Association should be given prior notification. If warranted, a variance may be allowed. Managers are expected to resolve reporting problems immediately upon notification by ACERA.

5. CLIENT SERVICE

If a manager is uncooperative and demonstrates a poor client service attitude, Watchlisting is appropriate. Managers are expected to resolve client service issues immediately upon notification by ACERA.

PROBATION

Probation indicates a level of serious deficiency and signals a need for closer contact with the firm. Probation necessitates a cautious, observant relationship with the manager.

Managers may be placed on Probation with or without first being placed on Watchlist.

The Probationary period is typically one year. The guidelines for recommending a Manager be placed on Probation are as follows:

1. UNDERPERFORMANCE

<u>INDEX MANAGERS</u>
4 consecutive quarters of tracking error in excess of 5 basis points from the benchmark, or two consecutive quarters with negative tracking error greater than 10 basis points from the benchmark.

<u>ACTIVE MANAGERS</u>

The manager's cumulative returns on a three year rolling average are below contract benchmark (see Schedule III) returns by more than 150 basis points, for two consecutive quarters; and/or

The manager's cumulative returns on a three-year (five-year, if high-alpha) rolling average or since inception, whichever is shorter, cause the manager's ranking amongst its peers in the Wilshire Co-Op database to fall below median in terms of performance for more than two consecutive quarters.

New managers will not be evaluated for Probation recommendations until the completion of 4 full quarters of performance.

2. STYLE DEVIATION

Probation may be recommended when a manager's portfolio characteristics are significantly different from its style. In general, a manager will be placed on Probation after 4 or more consecutive quarters of deviating from its style benchmark. In effect, if the manager is no longer the same manager that was retained for ACERA's account Probation and perhaps even termination is appropriate.

3. ORGANIZATIONAL CHANGE

Changes in ownership, organizational assignments or turnover that have the reasonable potential to seriously disrupt or destroy the investment management team that was hired to manage the ACERA account. When key personnel, such as top management, portfolio managers, research and trading staff are no longer available for use on the ACERA portfolio and do not appear to be replaced or replaceable, a Probation or termination recommendation is appropriate.

4. COMPLIANCE

If a manager does not comply with securities laws, industry regulations, standards of professional conduct or contractual agreements, a recommendation of Probation is appropriate. Certain circumstances may warrant termination.

5. CLIENT SERVICE

Failure to correct any issues that previously resulted in a Watchlist recommendation may result in Probation. Managers will generally be given one quarter to resolve client service issues.

TERMINATION

Upon determining that the manager has not made adequate improvement in the areas outlined in the Plan of Action, staff may recommend to the Investment Committee and/or Board that the manager be terminated. Prior to making the final decision to terminate the manager, the Investment Committee will invite the manager to make a presentation at the meeting in which the termination recommendation is to be discussed. Staff will have analyzed the liquidity of the manager's portfolio and will have a recommendation and plan for disposition of the assets.

Upon the Investment Committee's decision to terminate, staff will notify the accounting division as well as the Board's legal counsel of the action. All outstanding issues among the investment manager and ACERA's master custodian, brokers, consultant, or other parties shall be resolved prior to closing out the contract. The Manager Termination checklist is attached as Schedule IV.

SCHEDULE I

ASSET ALLOCATION SCHEDULE

	TARGET %
U.S. EQUITY PORTION	
Large Cap Growth (High alpha)	1.4
Large Cap Core Indexed	30.2
Large Cap Enhanced Core (High alpha)	1.4
Large Cap Value (High alpha)	1.4
Mid Cap	3.4
Small Cap Growth	2.1
Small Cap Value	2.1
Sub-total Equity Portion	42.0
INTERNATIONAL EQUITY PORTION	
Core Developed Markets	10.0
Emerging Markets	3.0
Sub-total International	13.0
U.S. FIXED INCOME PORTION	
Aggregate Bonds	22.0
Government/Corporate Bonds	9.0
Mortgages	2.0
Sub-total U.S. Fixed Portion	33.0
REAL ESTATE PORTION	
Total Real Estate	9.0
ALTERNATIVE INVESTMENTS	
Total Alternative Investments	2.0
CASH PORTION	
Total Cash Portion	1.0
Total Assets	100.0

SCHEDULE IA

ASSET ALLOCATION PORTFOLIO REBALANCING

The objective of rebalancing is to control and enhance the risk-adjusted return of the asset allocation strategy. For purposes of maintaining the characteristics of the asset allocation structure, the relative deviation of any liquid allocation away from its target weight (or liquidity-adjusted target weight) shall be no more than plus or minus 2.1 standard deviations of the allocation's expected volatility, relative to the other allocations in the asset mix.

Significant modifications to the asset allocation strategy shall be cause to review the appropriateness of maintaining this rebalancing parameter or revising it to a parameter more suitable to the revised asset allocation structure.

SCHEDULE II

Watchlist/Probation Criteria

Criterion	**Watchlist**	**Probation**
Performance	Index Fund: tracking error exceeds 5 basis points on an annualized basis. Active Managers: cumulative 3-year (5-year if high alpha) rolling returns (or since inception, whichever is shorter) is 50 to 150 basis points below the benchmark for two consecutive quarters and/or the manager's peer ranking falls below median for 2 consecutive quarters.	Index Fund: negative tracking error exceeds 5 basis points for 4 quarters; or negative tracking error exceeds 10 basis points for 2 quarters. Active Managers: cumulative 3-year (5-year if high alpha) rolling return is more than 150 basis points below the benchmark for 2 consecutive quarters and/or the manager's peer ranking falls below median for more than 2 consecutive quarters.
Style		Manager deviates from style for 4 or more quarters.
Organizational Change	Firm is under new ownership but the team responsible for ACERA's account remain intact and autonomous. Reorganization or turnover in top management, portfolio managers, research or trading staff that does not directly involve the ACERA portfolio team.	Changes in ownership, organizational assignments, or turnover in personnel that impacts the team responsible for ACERA's account.
Compliance	Violating investment guidelines or contractual agreements; purchasing unauthorized securities; leveraging the portfolio. Market Value of ACERA's account exceeds 40% of the manager's assets managed in the subject product. Failure to meet reporting requirements or deadlines. *Depending on circumstances and severity of the violation, higher level of contract review may be recommended.*	Violations of securities laws, industry regulations, standards of professional conduct, or contractual agreements. *Depending on circumstances and severity of the violation, termination may be recommended.*
Client Service	Uncooperative or unprofessional conduct.	Failure to correct client service issues within one quarter.

SCHEDULE III

Contract Benchmarks For ACERA Equity and Fixed Income Managers

DOMESTIC EQUITY

Bank of New York	S&P 500 and S&P MIDCAP 400 Indices
Brandywine	Russell 2000 Value Index
Nicholas-Applegate	Russell 2000 Growth Index plus 250 basis points before fees (or 150 basis points after fees)

HIGH-ALPHA PROGRAM

Pacific Financial Research	Russell 1000 Value Index plus 115 basis points after fees (or 175 basis points before fees)
TCW Asset Management	Russell 1000 Growth Index plus 190 basis points after fees (or 250 basis points before fees)
Salus Capital Management	S & P 500 Index plus fees and 190 basis points after fees (or 250 basis points before fees) over a rolling five-year time horizon.

FIXED INCOME

State Street Global Advisors	Lehman Aggregate Index
Loomis Sayles	Lehman Government/Corporate Index
AFL-CIO Housing InvestmentTrust	Salomon Mortgage Index

INTERNATIONAL EQUITY

Capital Guardian	MSCI EAFE
SSGA International Index	MSCI EAFE

SCHEDULE IV

MANAGER TERMINATION CHECK-LIST

This checklist is used to ensure that all details are covered when terminating investment management services.

1) Establish plan of action for reallocation of assets from terminated portfolio; transfer to other portfolios or prepare for liquidation.

2) Review department files and logs to identify any outstanding issues.

3) Notify ACERA Administration, Accounting Division, Legal Counsel, consultant, master custodian and any other vendors of the termination. Identify and resolve all outstanding issues with these parties.

4) Have manager and master custodian review and sign off on monthly market values and performance figures produced during the contract period.

5) Hold payment of last invoice until all issues are resolved.

6) Retain terminated manager files in the office for a minimum of one year , and send to archives.

7) Hold terminated manager files in archives for a minimum of 5 years.

SCHEDULE V

TABLE OF AMENDMENT DATES

AMENDING RESOLUTIONS

June	27,	1985	
Oct.	10,	1985	
Jan.	9,	1986	
Jan.	16,	1986	
Mar.	13,	1986	
May	22,	1986	
Sep.	11,	1986	
Oct.	9,	1986	
Nov.	20,	1986	
May	14,	1987	
Aug.	13,	1987	
Oct.	8,	1987	
Apr.	21,	1988	
July	28,	1988	
Jan.	29,	1989	(4)
Apr.	13,	1989	(5)
May	18,	1989	
July	13,	1989	
Aug.	10,	1989	
Nov.	16,	1989	(2)
July	11,	1991	
June	11,	1992	
June	10,	1993	
July	8,	1993	
Nov.	18,	1993	
May	14,	1994	
Aug.	18,	1994	
Nov.	20,	1994	
Feb.	16,	1995	
May	18,	1995	
Jan.	16,	1997	
Aug.	20,	1998	
May	20,	1999	
Jan.	31	2000	

Alameda County Employees'
Retirement Association

ACERA

INVESTMENT GUIDELINES, POLICIES AND PROCEDURES

AMENDED April, 2001

ACERA
INVESTMENT GUIDELINES, POLICIES AND PROCEDURES
2001

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ACERA
INVESTMENT GUIDELINES, POLICIES AND PROCEDURES

SECTION I: MISSION AND PURPOSE

The Alameda County Employees' Retirement Association (ACERA) exists for the purposes of providing accurate, timely benefits to its members and their beneficiaries and defraying reasonable expenses of administration.

The Board of Retirement (the Board), having exclusive authority and exclusive fiduciary responsibility for the investment and administration of the Trust Fund (the Fund), hereby establishes the following General Investment Policies and Guidelines (the Policy) for the investment of ACERA's assets. The Board reserves the right to amend, supplement or rescind this Policy at any time.

The Board of Retirement is directed by law and given discretion to prudently invest the plan assets. The purpose of this statement of policy is to assist ACERA in effectively supervising said investments and to encourage effective communication between ACERA and its managers and consultants.

[1] Prepared for ACERA by Cortex Consulting; adopted by the Board of Retirement on March 8, 2000 and revised May 2001.

ACERA's investment goal is to operate at a level of performance in the upper quartile of comparable pension funds on a risk-adjusted basis and to be as fully funded as possible so that ACERA's benefit costs do not become a burden upon future generations of members and taxpayers.

SECTION II: CONSTITUTIONAL REQUIREMENTS

Article 16 §17 of the California State Constitution provides in pertinent part as follows:

"Notwithstanding any other provisions of law or this Constitution to the contrary, the retirement board of a public pension or retirement system shall have plenary authority and fiduciary responsibility for investment of money and administration of the system, subject to the following:

a. The retirement board of a public pension or retirement system shall have the sole and exclusive fiduciary responsibility over the assets of the public pension or retirement system. The retirement board shall also have sole and exclusive responsibility to administer the system in a manner that will assure prompt delivery of benefits and related services to the participants and their beneficiaries. The assets of a public pension or retirement system are trust funds and shall be held for the exclusive purposes of providing benefits to participants in the pension or retirement system and their beneficiaries and defraying reasonable expenses of administering the system.

b. The members of the retirement board of a public pension or retirement system shall discharge their duties with respect to the system solely in the interest of, and for the exclusive purposes of providing benefits to participants and their beneficiaries, minimizing employer contributions thereto, and defraying reasonable expenses of administering the system. A retirement board's duty to its participants and their beneficiaries shall take precedence over any other duty.

c. The members of the retirement board of a public pension or retirement system shall discharge their duties with respect to the system with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with these matters would use in the conduct of an enterprise of a like character and with like aims.

d. The members of the retirement board of a public pension or retirement system shall diversify the investments of the system so as to minimize the risk of loss and to maximize the rate of return, unless under the circumstances it is clearly not prudent to do so.

e. The retirement board of a public pension or retirement system, consistent with the exclusive fiduciary responsibilities vested in it, shall have the sole and exclusive power to provide for actuarial services in order to assure the competency of the assets of the public pension or retirement system."

SECTION III: ELIGIBLE ASSET CATEGORIES

The Fund shall hold assets in categories established by the Board. Any asset category may be held in direct form, in pooled form or in both. Asset categories managed by one or more "Qualified Investment Managers" {Manager(s)} are called "Managed Accounts". Asset categories under the supervision of the County Treasurer are called the Treasurer's Accounts. Eligible asset categories are listed and defined below.

A. **CASH** shall consist of short term (12 months or less) interest bearing investments of high quality such as U.S. Treasury issues, insured certificates of deposit of U.S. banks (fixed and/or variable), commercial paper rated A-1, P-1 or both, or other instruments of equal or better quality, and includes money market funds available through the Custodian Bank (Custodian).

B. **U.S. EQUITY** shall consist of common stocks and other securities which are convertible into common stocks, and ADRs (American Depository Receipts) , as well as cash (per "A" above) and fixed income (per "D" below) when used as temporary substitutes for common stocks.

C. **INTERNATIONAL EQUITY** shall consist of common stocks and other securities convertible into common stocks of companies domiciled outside of the U.S., and GDR's (Global Depository Receipts), as well as cash equivalents and fixed income, domestic or international, which are being used as temporary substitutes for common stock.

D. **FIXED INCOME** shall consist of investments in U.S. taxable bonds, debentures, notes and other evidences of debt. Fixed income may include non-dollar denominated bonds issued by corporations or governments domiciled outside of the United States of America as well as Brady Bonds. Other eligible investments include cash equivalents per "A" above and convertible bonds and preferred stock.

E. **MEMBER MORTGAGES** (closed program) shall consist of first mortgages, secured by the primary residences of the borrowers, underwritten to GNMA/FNMA standards by a qualified third party expert underwriter retained by the Board for that purpose.

F. **REAL ESTATE** shall consist of investments in equity real estate through the use of commingled or direct investments. For more information about real estate investments, refer to ACERA's Real Estate policy which is maintained as a separate document.

SECTION IV:
INVESTMENT PHILOSOPHY

The following is a summary of ACERA's Investment Philosophy. For a complete statement, please refer to Schedule VI, "ACERA Investment Philosophy".

The Board believes that its investment policies, in aggregate, are the most important determinants of its investment success. Compliance with investment policies should therefore be monitored rigorously. The Board also believes that performance of the total portfolio, individual asset classes, and Managers should be monitored and compared to appropriate, predetermined benchmarks.

The Board believes that prudent management of risk is a central element of the investment function and that diversification among asset classes will reduce risk and enhance returns of the overall investment portfolio in the long term.

The Board believes that market efficiency and opportunities vary among asset classes and may change over extended periods of time; therefore ACERA believes that its portfolio management strategies should adapt over time to reflect the changing nature of capital markets.

The Board's primary goals in managing the Fund are:

1. To ensure that sufficient funds are available to pay vested benefits and maintain supplemental benefits;
2. To comply with all applicable fiduciary standards; and
3. To add marginal value that will help reduce the costs of the plan and/or to increase benefits for the beneficiaries.

The Board believes that in order to achieve its goals, ACERA must invest the necessary resources to build and maintain an appropriate organizational infrastructure.

SECTION V:
INVESTMENT STRATEGY

A. **U.S. EQUITY** will be structured to capture exposure to the broad U.S. equity market as represented by the Russell 3000 Index. Passively managed (index) portfolios will be used in markets that are reasonably efficient. These portfolios are intended to provide broadly diversified market exposure with controlled (market) risk and minimal cost.

Actively managed portfolios will be used in less efficient markets when the Board determines that a Manager possesses special skills or abilities that enable that Manager to capture excess returns relative to the market, adjusted for risk and fees; or to exploit specialty markets that provide enhanced return with acceptable risk.

A great part of the Russell 3000, on a market value basis, is comprised of large-cap stocks, which the Board believes are efficiently priced most of the time. Therefore, the Board has adopted a policy of obtaining overall exposure to this segment of the market via passively managed indexed products. Some active Managers have been employed to enhance overall portfolio return in the large- and/or mid-cap sectors on a risk- and fee-adjusted basis. These Managers manage ACERA's "Hi-Alpha" program.

The remainder of the Russell 3000 index is comprised of small to mid-cap companies. Some opportunities for active management enhancement exist in these securities due to market inefficiencies. ACERA will attempt to capture these opportunities through a mix of Managers who have the special skills required to identify smaller companies that may be undervalued or possess substantial growth potential.

The U.S. equity portion of the portfolio shall be allocated among the various styles and Managers as indicated in Schedules I and IA.

B. **INTERNATIONAL EQUITY** represents an opportunity to diversify risk and capture enhanced returns within markets generally less efficient than the U.S. domestic equity market. 100% of the international equity portion of the Fund will be invested in actively managed portfolios.

C. **FIXED INCOME** represents a means of reducing overall portfolio risk and capturing incremental returns. Inefficiencies in the pricing and trading of fixed income securities create opportunities to add value through active management. 100% of the fixed income portion of the portfolio will be invested in actively managed portfolios.

D. **REAL ESTATE** will be used as a means for diversifying the portfolio and capturing additional returns due to the low correlation between returns on real estate and financial assets. Due to the illiquid nature of real estate assets, distinctions between active and passive management are not applicable. For more information regarding real estate investments, refer to ACERA's Real Estate policy which is maintained as a separate document.

SECTION VI: ASSET ALLOCATION AND REBALANCING

Asset allocation targets, a function of the returns and risks from various asset classes and the nature of the plan's liabilities, are set forth in Schedule I. A goal of asset allocation is balancing asset growth versus liability growth considering time horizons, liabilities and risk tolerance.

Rebalancing is the risk control process of returning an allocation back to the desired target level after having drifted away from its targeted position. Acceptable ranges around the asset allocation targets are set forth in Schedule IA. The objective of rebalancing is to enhance the risk-adjusted performance of the asset allocation structure.

ACERA Staff ("Staff") shall be responsible for maintaining the relative weights of asset classes and allocations within the acceptable rebalancing ranges indicated in Schedule IA. Should an asset class or allocation fall outside its target range, Staff shall rebalance the asset class or allocation back to the target weights as specified in the asset allocation structure in Schedule I.

Staff shall:
1. Monitor the portfolio;
2. Determine whether or not any asset category is out of balance with its target asset allocation in excess of the specified tolerance range;
3. Determine whether or not any Manager within each asset category is out of balance with their target allocation in the excess of the specified tolerance range;
4. And, if so, either:

(a) instruct the relevant Managers to redirect cash income (interest coupon and dividends) in concert with an evaluation of pending commitments and other cash flows (employer and employee contributions), in order to bring the allocation(s) back to the adopted strategic target; or

(b) instruct the relevant Managers to liquidate or acquire the appropriate dollar value of securities to reach the target and reallocate the cash thus generated or required to the other category(s) or Manager(s) necessary.

Staff shall report to the Board on a regular basis the status of the Fund with respect to how categories are tracking relative to their allowable ranges, as well as any actions taken to rebalance the portfolio.

SECTION VII: ASSET CATEGORIES OBJECTIVES

The general objective of the Board is to preserve capital and earn a return from appreciation and income, as described herein.

The minimum return objective for the Fund shall be the current actuarial interest assumption rate plus 25 basis points per year over a market cycle. Returns shall be calculated net of fees.

The minimum return objective for the Fund over a market cycle (up to five years) shall also be 400 basis points (4%) per year over the national Consumer Price Index, published by the U.S. Department of Commerce.

The objectives of each asset category are:

A. CASH

1. A rate of return in excess of 90-Day U.S. Treasury bills.

2. A rate of return within the upper one half of a universe of like short-term funds.

B. U.S. EQUITY

1. A rate of return in excess of the U.S. equity market as measured by the Russell 3000 Index after adjustment for risk and fees.

2. A rate of return within the upper 33rd percentile of the Wilshire Co-op or similar database of the performance of diversified equity portfolios.

C. INTERNATIONAL EQUITY

1. A rate of return in excess of the Morgan Stanley Capital International All Country World Index Ex-U.S. Free (MSCI ACWI).

2. A rate of return within the top quartile of the Wilshire Co-op or similar database of the performance of diversified international equity portfolios.

D. U.S. FIXED INCOME

1. A rate of return in excess of the Lehman Aggregate Bond Index published by Lehman Bros. Inc..

2. A rate of return within the top quartile of the Wilshire Co-op or similar database of the performance of diversified fixed income portfolios.

E. MEMBER MORTGAGE (closed program)

1. A rate of return that compares favorably with the Salomon Mortgage Index.

2. A delinquency rate of less than 2% of loans outstanding;

F. REAL ESTATE

Total Return - over rolling 5 year periods a minimum total real rate of return (net of management fees) of 6.0% using a "Time Weighted Market Value" calculation. The real return expectation is after inflation (U.S.A. CPI-Urban).

1. Income Return – Income, which is defined as cash distributed to the Association, should comprise at least 2/3 of the total return over rolling five periods.

2. Minimum Going-in Yields – On individual separate account assets, the Manager's five year projection (net of fees) will exceed the consultant's five year projection for ten year treasuries by no less than 150 basis points.

In addition, objectives that reflect the particular investment strategy or style used by individual Managers shall be outlined in an attachment to the Manager's contract.

SECTION VIII: ALLOCATION OF CASH FLOW

Cash flow not needed for benefit payments or administrative expenses shall be allocated to Managed Accounts in a ratio that best funds the overall asset allocation as shown in Schedules I and IA.

If cash flow is insufficient for the payment of benefits or to cover administrative expenses, then Managed Accounts shall be debited in a ratio that best satisfies the target allocation shown in Schedules I and IA. Such debits, if necessary, will be carried out as needed, and with timely notice to Managers to facilitate effective funds transitions and performance measurement.

For planned investments which may not need to be funded immediately, a reserve may be budgeted and invested in appropriate index funds until such moneys are required. Alternatively, Managed Accounts within "overfunded" asset classes may be called upon to provide the required moneys. Funds intended for real estate investments but not yet invested shall be divided equally and held in the equity and fixed income index funds until called by the real estate Manager.

SECTION IX: PROHIBITED INVESTMENTS

Managers shall exercise prudent expert standards in defining prohibited investments. For example, prohibited investments include, but are not limited to, securities issued by the County of Alameda or any agency thereof.

SECTION X: DIRECTED BROKERAGE

ACERA does not engage in either directed commission arrangements or "soft dollar" transactions.

SECTION XI: DERIVATIVE INSTRUMENT USAGE POLICY

Exposure to risk by use of derivative instruments must be consistent with

ACERA's overall investment guidelines. Derivatives shall not be used to establish a leveraged position (i.e. offsetting Cash positions must be maintained against all delayed settlement transactions).

SECTION XII: SELECTION OF INVESTMENT MANAGERS

The Investment Committee shall direct Staff and/or a consultant to initiate searches for Managers. Staff and/or the consultant shall screen qualified candidates and present a list of finalists to the Investment Committee for its approval. Upon approval of the list, the finalists shall be interviewed by Staff and the consultant (if applicable) in a publicly noticed meeting at which no less than three (3) Investment Committee members shall be present. Staff and the consultant (if applicable) shall evaluate the interviews, rank the finalists, and make a recommendation to the Investment Committee to hire one or more firms attaining the highest rankings. It is possible that none of the firms will be recommended for hire**.**

These procedures are developed for the convenience and benefit of ACERA, and shall not bind ACERA or invalidate the selection of a Manager if different processes are used subsequent to the promulgation of this Policy.

SECTION XIII: AUTHORITY OF INVESTMENT MANAGERS

Subject to the laws of the United States and the State of California, and to the terms and conditions of this Policy, Managers shall have full discretion to direct the purchase, exchange, sale and reinvestment of the assets of the Managed Accounts. The Board expects that Managers will recommend changes to this Policy when any part of this Policy appears to be at variance with overall market and economic conditions.

Managers shall place orders to buy and sell securities and, by notice to the Custodian, shall cause the Custodian to deliver and receive securities on behalf of the Fund. Managers shall, upon Board inquiry, report placement of ACERA brokerage such that the Board shall be assured commissions were placed for the sole and exclusive benefit of the Fund.

Separate account Managers shall not vote proxies. Proxies shall be voted by ACERA according to Board-established policies and procedure.

Securities lending shall be performed by the Custodian Bank under the oversight of the Board.

SECTION XIV: INVESTMENT GUIDELINES FOR THE MANAGED ACCOUNTS

Individual Manager discretion shall be governed by the guidelines set out in the Investment Contract of each Manager.

A. GENERAL

1. All investments shall comply with all applicable laws of the United States and the State of California governing the investment of pension trusts.

2. All securities transactions shall be executed by reputable broker/dealers, banks, or the Custodian, and shall be on a best-price and best-execution basis, and shall be reported to ACERA as is called for elsewhere in this Policy.

3. All Managers shall refrain from investing in a tobacco producer investment opportunity when, in their expert opinion, an alternative non-tobacco producer investment opportunity is available that will satisfy the same ACERA portfolio guidelines, instructions and objectives for risk, return and diversification.

B. EQUITY

Managers have full discretion to invest solely in readily marketable and diversified equity securities as defined above subject to the following:

1. For Managed Accounts, no more than 10% of the value (at time of investment) of the account shall be invested in the securities of a single issuer.

2. ACERA shall not hold more than 10% of the equity securities of any issuer.

3. Equity securities shall possess value and quality corroborated by generally accepted techniques and standards of fundamental securities analysis.

4. Assets in a Managed Account not invested in equity securities shall be kept with interest in appropriate money market instruments, including any money market fund available through the Custodian.

5. A Managed Account shall be subject to ACERA's policy on derivatives.

6. All Managers shall endeavor to be fully invested in stocks at all times unless they have received specific authorization to the contrary from the Board. Cash holdings, as defined in this Policy, shall generally not exceed 5% of the portfolio on a market value basis.

C. FIXED INCOME

Managers have full discretion to invest solely in readily marketable and diversified securities including, but not limited to:

1. Obligations of the U.S. Treasury.

2. Obligations guaranteed by an agency of the United States.

3. Insured certificates of deposit and banker's acceptances of credit worthy banks.

4. Corporate and other evidences of debt. At least 80% of this debt must be rated by Moody's Investor's Services or by Standard & Poors.

5. Commercial paper and banker's acceptances of issuers rated P-1 by Moody's Investor's Service.

6. Or A-1 by Standard & Poors Corporation.

7. Excepting direct obligations of the U.S. Government, and those explicitly guaranteed by the U.S. Government, no account shall hold more than 5%, at cost, of the obligations of any single issuer.

8. Fixed income derivative investments shall be in accordance with ACERA's derivative policy.

SECTION XV: SEPARATE ACCOUNT MANAGER SPECIFICATIONS

A. Managers must be registered as investment advisors under the Investment

Advisor's Act of 1940, a bank (as defined in that act) or an insurance company qualified to perform investment management services under state law in more than one state, including California. In addition, by accepting appointment as an Manager for ACERA, Managers shall acknowledge that they are "Plan Fiduciaries" and "Qualified Investment Managers" as defined by the Employees' Retirement Income Security Act (ERISA) of 1974, see or reference United States Code Title 29 Section 1001 et. seq..

B. Managers shall maintain fiduciary insurance in the amount of 10% of the total assets managed in the ACERA account or $25 million, whichever is higher, unless the contract specifies otherwise.

C. Managers shall promptly notify ACERA of changes that occur in any of the following:

1. The investment strategy used in managing the subject product.
2. The personnel involved in managing ACERA's account.
3. The ownership, key personnel, or organizational structure of the Manager's company.
4. The Manager company's financial condition.
5. The number of clients invested in the subject product.
6. The market value of the total assets managed in the subject product.

D. Managers shall promptly notify ACERA if they are subject to censure or disciplinary action by a regulatory agency.

E. On a monthly basis, Managers shall report on the activities of the portfolios managed on behalf of ACERA. Monthly reports shall include descriptions of holdings along with cost and market values; summaries of purchases and sales; description of major changes to the portfolio; and a declaration by the Manager that its investment activities comply with the provisions of this Policy.

On a monthly basis, active Managers shall certify in writing that the portfolio market values, transactions and performance data are reconciled with ACERA's Custodian.

On a monthly basis, Managers shall furnish a report detailing the entities to whom services were paid for with soft dollars; the total amount of soft dollars used for such services; and descriptions of the services purchased with those soft dollars. Consultants and the Custodian are also required to report on their soft dollar usage, if applicable.

On a quarterly basis, Managers shall invoice ACERA for payment of fees for services rendered. The fee shall be calculated using the rate established in the fee schedule of the Manager's contract with ACERA and using the market values determined by ACERA's Custodian.

F. Managers shall provide ACERA with the most recent copy of Form ADV, Part II upon their receipt of the same, on an ongoing basis.

G. Managers shall not make contributions, provide gifts, reimbursements of expenses or provide personal benefits exceeding $250 in the aggregate within any 12-month period to any Trustee, fiduciary, employee or consultant of ACERA. Donations of educational conferences and similar events and benefits, including travel, meals and accommodations will be made to ACERA and not directed to individuals. The Board will determine whether to accept any donations and will be solely responsible for selection of the Trustee, staff member, or other individual, who will attend or otherwise participate on behalf of ACERA.

SECTION XVI: MANAGER MONITORING POLICY

The ACERA Board has contracted with a number of external Managers to invest ACERA assets in the public equity markets. As part of the Board's fiduciary duties to prudently select, monitor and supervise these Managers, the Board has adopted this Policy. The intent of this Policy is to notify Managers of the standards by which they will be judged and to establish a structure which the Investment Committee and the Board can use to monitor the performance of the Managers.

Managers will be monitored to:

1. Evaluate how well they achieve their investment objectives.
2. Ensure that they adhere to their established investment approach/style and do not attempt to index returns to preserve stellar performance or take extraordinary risk to overcome poor performance.
3. Identify issues or trends that have the potential to result in losses to the Fund.
4. Alert the Board when Managers are not performing to expectations so that appropriate remedial action can be taken.

Managers will be evaluated on the basis of the following: performance, style integrity, organizational stability, compliance, and client service described in greater detail below.

A. PERFORMANCE

On a monthly basis Staff will monitor Manager holdings, activity and performance. On a quarterly basis Staff and/or a consultant will furnish the Investment Committee and/or Board with an in-depth evaluation of each Manager which will include a comparison of the Manager to its contract benchmark and a peer universe of Managers using a similar investment style. This report shall include an analysis of the sources of Managers' returns (stock selection, industry selection, asset allocation, etc.) and shall identify which decisions enhanced or diminished performance.

On a quarterly basis, trading costs will be evaluated in terms of commissions paid and execution of trades. Staff and/or a consultant shall furnish a report to the Investment Committee and/or Board regarding trading costs on an annual basis.

B. STYLE INTEGRITY

Each Manager will be analyzed at least annually to ensure that the Manager is continuing to invest the portfolio in the style for which they were originally hired. Style integrity is essential to maintain the Board's asset allocation policy. Any significant deviation in style will result in the overall portfolio having a different characteristic, in some measure, from the broad market which is represented by the Russell 3000 index. Significant variations in the portfolio characteristics from the style anticipated in the management contract may indicate a change in its investment style.

This review also provides the Investment Committee and/or Board an opportunity to evaluate the Manager's continuing "fit" with the goals of the overall fund. By monitoring Manager style the Investment Committee and/or Board can assure that its Manager mix takes advantage of opportunities to increase diversification through lower correlation of returns among individual Managers.

C. ORGANIZATIONAL STABILITY

Managers' organizations will be monitored to ensure continuity of the intellectual and philosophical processes that went into developing the particular investment approach contracted for by ACERA. In addition, Managers will be monitored for business risk, quality of staff and potential conflicts of interest.

It is ACERA's intent that its portfolio comprises no more than 25% of the Manager's total assets under management. Therefore ACERA will monitor the Managers' assets, firm-wide, as well as in the subject product.

D. COMPLIANCE

Managers will be monitored to ensure they are adhering to Federal and state laws regarding securities and the management of investment portfolios, trading, and pension investments; ethical practices of the investment professions; the Contract governing their relationship with ACERA; and the policies and guidelines set forth in this Policy statement and any other written directives issued by ACERA.

Each ACERA contract will specify which investment vehicles a Manager is authorized to use, which markets the Manager is authorized to transact business in and any limitations within a market (small or large capitalization, value or growth orientation). The assets in each Manager's portfolio shall be reviewed monthly to ensure compliance with contract guidelines.

All required documents and reports, set forth in Schedule V, must be submitted in a timely manner and in the format specified by ACERA.

Managers must provide prior notification and justification for failure to comply with rules, regulations, contract provisions, deadlines or other directives. Managers must provide a time frame for curing any deficiencies. Staff shall evaluate each incident on a case-by-case basis and determine whether an exception may be granted.

E. CLIENT SERVICE

Managers are required to comply with routine portfolio investment guidelines and reporting deadlines and are also expected to cooperate with special requests for information. ACERA will establish reasonable time frames for all requests and reporting and will provide feedback to all external equity Managers regarding the perceived quality of their client service.

ACERA Staff will endeavor to meet with each Manager at least twice a year by telephone or in person to review performance and other issues.

SECTION XVII:

CONTRACT REVIEW PROCESS

If during the course of regular monitoring, ACERA determines that a Manager's performance, style, organizational stability, compliance, or client service has declined to unacceptable levels, ACERA may, at its discretion, subject the Manager to ACERA's Contract Review Process. As part of the Board's fiduciary duties to prudently select, monitor and supervise their Managers, the Board has approved this process. The purpose of this process is to ensure as little disruption as possible in the event that concerns or problems arise with respect to a

Manager's performance. The Board does not confer any additional rights or protections to its Managers by the promulgation of this Policy and/or this process.

There are generally three stages of review: Watchlist, Probation, and Termination. (described below). ACERA reserves the right to terminate an investment management contract at any time, upon 30 days notice, for any reason, and without resort to this Contract Review Process.

The Contract Review Process may result in one or more of the following:

1. Placement on Watchlist or Probation status.
2. Movement from one stage of review to another, or removal from the Contract Review Process.
3. Reduction of assets under management.
4. Revision of investment contract guidelines for that Manager.
5. Re-negotiation of fees.
6. Termination of a Manager's contract.
7. Or any other deemed appropriate by the Board

Each situation is unique and action by the Board will vary depending on the type of Manager and the style/strategy involved. The following describes the Contract Review Process:

A. INITIAL REVIEW

Prior to a Manager being considered for Watchlist, Probation or Termination, ACERA may take the following steps :

1. Analysis

Staff will conduct in-depth analyses of the perceived deficiency to verify that a deficiency exists, form an initial assessment of the severity of the deficiency, and make an initial determination of possible causes.

2. Discussion with the Manager

Staff will contact the Manager to discuss the situation and the results of Staff's analysis.

3. Consultant Input

ACERA may seek the services of a consultant to provide additional assessment and advice regarding the situation, depending on the severity of the deficiency.

All phases of account compliance may be reviewed during this step, in addition to the specific issue that originated the Review Process.

B. FORMAL ACTION

After completing the Initial Review, Staff may recommend to the Investment Committee and/or Board that the Manager be either placed on Watchlist or Probation or, in certain cases, Terminated. The specific criteria for determining which level of Contract Review to recommend is outlined later in this Policy section and summarized in tabular form in Schedule II. The Committee and/or Board will approve or reject the recommendation.

Upon approval of a Watchlist or Probation recommendation:

1. Staff will notify the Manager of the Board's decision and will provide the Manager with a statement of concerns which outlines the areas which need improvement.

2. The Manager will be asked to respond in writing with an explanation of the issues

and a proposed action plan to resolve the issues.

3. Staff, a consultant and the Manager will collectively draft a Plan of Action. The plan will identify: the specific steps to be taken to correct the problem; the time frames for further review; and what additional monitoring may be required.

   At the end of the time period specified in the Plan of Action, the Manager will be evaluated and one of the following actions may be taken:

   (a) Removal from Contract Review: If the successfully resolves the issues/deficiencies and demonstrates continued success in all other areas of its relationship with ACERA.

   (b) Movement from Probation to Watchlist: If the Manager has satisfied all or most of the issues/deficiencies that caused it to be placed on Probation, yet Staff continues to have concerns about the Manager. If circumstances warrant, a Manager may also be moved from Watchlist to Probation at any time during the Contract Review Process.

   (c) Extension of Contract Review: A Manager may be given additional time to satisfy the conditions of its Action Plan if reasonable progress is being made. Extensions may also be granted if unfavorable market conditions or high costs make reallocation of assets inadvisable.

   (d) Termination: If the Manager has not satisfactorily resolved the issues/deficiencies, Staff may recommend termination as described below. Termination may be recommended at any time during the Contract Review Process if circumstances warrant.

WATCHLIST

Watchlisting indicates an increased level of concern, but does not indicate major deficiencies. The Watchlisting period is typically one year. Any of the following may result in a Watchlist recommendation:

A. UNDERPERFORMANCE

Please refer to Schedule II for specific Watchlist criteria for each Manager.

B. STYLE DEVIATION

Managers are expected to adhere to the style of investment management for which ACERA originally hired them. Changes in portfolio characteristics or style drift may lead to a Watchlist recommendation.

C. ORGANIZATIONAL CHANGE

<u>NEW OWNERSHIP</u>
Even relatively benign ownership changes, which impact personnel key to ACERA's portfolio management may be cause for a Watchlist recommendation.

<u>TURNOVER</u>
Significant turnover in top management, portfolio Managers, research or trading staff, or marketing personnel, which does not directly affect the team responsible for ACERA's account may warrant Watchlisting.

<u>REORGANIZATION</u>
Changes which signal management deterioration or hasty /uncontrolled growth in the firm with potential to disrupt the investment team hired for

management of ACERA's account may justify Watchlisting.

ASSETS UNDER MANAGEMENT

If the market value of ACERA's portfolio rises above 25% of the Manager's total assets under management, Watchlist status may be recommended.

D. COMPLIANCE

CONTRACTS AND OTHER AGREEMENTS

Managers are expected to comply with the investment management contract, investment guidelines, or other directives. Non- or partial compliance may result in a Watchlist recommendation.

REPORTING

Staff will contact Managers to request past due reports. If the Manager's reports are consistently delinquent, the payment of fees may be delayed. If a Manager cannot comply with reporting deadlines, ACERA should be given prior notification. If warranted, a variance may be allowed. Managers are expected to resolve reporting problems immediately upon notification by ACERA. Repeated delinquency in reporting may result in a Watchlist recommendation.

E. CLIENT SERVICE

If a Manager is uncooperative and demonstrates a poor client service attitude, Watchlisting is appropriate. Managers are expected to resolve client service issues immediately upon notification by ACERA.

PROBATION

Probation indicates a level of serious deficiency and signals a need for closer contact with the firm. Probation necessitates a cautious, observant relationship with the Manager.

Managers may be placed on Probation with or without first being placed on Watchlist status. The Probation period is typically one year.

The following may result in Probation:

A. UNDERPERFORMANCE

Please refer to Schedule II for specific Probation criteria for each Manager.

B. STYLE DEVIATION

Probation may be recommended when a Manager's portfolio characteristics are significantly different from its style. In general, a Manager will be placed on Probation after four or more consecutive quarters of deviating from its style benchmark. In effect, if the Manager is no longer the same Manager that was retained for ACERA's account, Probation and perhaps even Termination is appropriate.

C. ORGANIZATIONAL CHANGE

Changes in ownership, organizational assignments or turnover that have the potential to seriously disrupt or destroy the investment management team that was hired to manage the ACERA account may result in Probation or Termination. When key personnel, such as top management, portfolio Managers, research and trading staff are no longer available for use on the ACERA portfolio and do not appear to be replaced or replaceable, a Probation or Termination recommendation is appropriate.

D. COMPLIANCE

If a Manager does not comply with securities laws, industry regulations, standards of professional conduct or contractual provisions, a recommendation of Probation is appropriate. Certain circumstances may warrant Termination.

E. CLIENT SERVICE

Failure to correct any issues that previously resulted in the Watchlist recommendation may result in Probation. Managers will generally be given one quarter to resolve client service issues.

TERMINATION

Upon determining that the Manager has not made adequate improvement in the areas outlined in the Plan of Action, Staff may recommend to the Investment Committee and/or Board that the Manager be terminated. Prior to making the final decision to terminate the Manager, the Investment Committee may invite the Manager to make a presentation at the meeting in which the Termination recommendation is to be discussed. Staff will have analyzed the liquidity of the Manager's portfolio and will have a recommendation and plan for disposition of the assets.

Upon the Investment Committee's decision to terminate, Staff will notify the accounting division as well as the Board's legal counsel of the action. All outstanding issues between the Manager and ACERA's master Custodian, brokers, consultant, or other parties shall be resolved prior to closing out the contract. The Manager Termination checklist is attached as Schedule IV.

The Contract Review Process described in this Policy does not provide any additional rights or protections to Managers, beyond what is provided in the contract. ACERA reserves the right to terminate an investment management contract without resort to the Contract Review Process, at any time, upon 30 days notice, for any reason.

SCHEDULE I

ASSET ALLOCATION AND MANAGER STRUCTURE TARGETS

ASSET ALLOCATION TARGETS

Asset Class	**Target Allocation**
U.S. Equity	35
International Equity	22
Total Equity	57
Fixed Income	34
Real Estate	9

MANAGER STRUCTURES TARGETS

Managers		**Target Allocation**
U.S. Equity		
Large Cap Core Index	BoNY S&P 500	61
Large Cap Growth (Hi-Alpha)	TCW	12
Large Cap Value (Hi-Alpha)	PFR	12
Large Cap Enhanced Core (Hi-Alpha)	Salus	4
Small Cap Growth	Nicholas Applegate	6
Small Cap Value	Brandywine	5
Non-U.S. Equity		
Core Developed Markets	Capital Guardian	65
Core Developed Markets	Putnam	35
Fixed Income		
Aggressive Core Plus	Loomis Sayles Boston	29
Global Bond	Brandywine	16
Enhanced Index	Baird	49
Mortgage	AFL-CIO	6

SCHEDULE IA

ASSET ALLOCATION PORTFOLIO REBALANCING

The objective of rebalancing is to control risk and enhance the risk-adjusted return of the asset allocation strategy. For purposes of enhancing the risk-adjusted return of the asset allocation structure, the relative deviation of any liquid sub asset class away from its target weight (or liquidity-adjusted target weight) shall be no more than plus or minus 1.7 standard deviation factors of each allocation's expected volatility, relative to the other allocations in the asset mix. This standard deviation factor shall be used to define the range of allowable deviation from Policy target asset allocations. If any sub asset class reaches its allowable deviation from its target allocation, all sub asset classes will be evaluated.

The actual reallocation will be at the discretion of ACERA's staff (with oversight by the rebalancing consultant) after reviewing: the relative magnitude of deviation from target for all other sub asset classes; the available cash liquidity of sub asset classes that could be used to fund rebalancing; pending cash flows (employer and employee contributions, or proceeds from a terminated manager's portfolio); pending liquidity windows with commingled investment pools; pending investment commitments (real estate transactions and/or new funding commitments; and, pending interest coupon and dividend cash flows.

Asset allocation and rebalancing status reports, and any rebalancing activity taken toward attaining the objective of the rebalancing program will be reported to the Board of Trustees on a monthly basis.

Significant modifications to the asset allocation strategy shall be cause to review the appropriateness of maintaining this rebalancing parameter or revising it to a parameter more suitable to the revised asset allocation structure.

SCHEDULE II

Watchlist/Probation Criteria for Performance

(Footnote: If Plan history with Manager is less than 5 years, use rolling 3 year period)

Watchlist Criteria	Probation Criteria
US Equity • Large Cap Core Index: negative tracking error exceeds 5 bps on an annualized basis in any 1 year period. • Large Cap Growth: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager’s peer ranking falls below median for 2 consecutive quarters. • Large Cap Value: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager’s peer ranking falls below median for 2 consecutive quarters. • Small Cap Growth: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager’s peer ranking falls below median for 2 consecutive quarters. • Small Cap Value: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager’s peer ranking falls below median for 2 consecutive quarters. • Large Cap Enhanced Core: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager’s peer ranking falls below median for 2 consecutive quarters.	**US Equity** • Large Cap Core Indexed: negative tracking error exceeds 5 bps in any 1 year period; or negative tracking error exceeds 10 bps for 2 quarters. • Large Cap Growth: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager’s peer ranking falls below median for more than 2 consecutive quarters. • Large Cap Value: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager’s peer ranking falls below median for more than 2 consecutive quarters. • Small Cap Growth: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager’s peer ranking falls below median for more than 2 consecutive quarters. • Small Cap Value: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager’s peer ranking falls below median for more than 2 consecutive quarters. • Large Cap Enhanced Core: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager’s peer ranking falls below median for more than 2 consecutive quarters.

International Equity • Concentrated Core: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters.	**International Equity** • Concentrated Core: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters.
Fixed Income • Aggressive Core Plus: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters. • Global Bond: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters. • Enhanced Index: cumulative 1 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters. • Mortgage: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters.	**Fixed Income** • Aggressive Core Plus: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters. • Global Bond: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters. • Enhanced Index: cumulative 1 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters. • Mortgage: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters.

SCHEDULE III

BENCHMARKS FOR ACERA ASSET CLASSES, EQUITY AND FIXED INCOME MANAGERS

BENCHMARKS FOR ASSET CLASSES

Asset Class	**Benchmark Index**
U.S. Equity	Russell 3000
International Equity	MSCI ACWI-Ex. U.S.
Total Equity	N/A
Fixed Income	Lehman Aggregate U.S./Salomon World Government Bond Ex U.S. /Lehman High Yield in the ratio of 75/15/10
Real Estate	NCREIF

BENCHMARKS FOR EQUITY AND FIXED INCOME MANAGERS
(Please refer to individual Manager's contract for expected annual premium)

Manager	**Benchmarks**
U.S. Equity	
BoNY S&P 500	S&P 500
TCW	Russell 1000 Growth
PFR	Russell 1000 Value
Salus	S&P 500
Nicholas Applegate	Russell 2000 Growth
Brandywine	Russell 2000 Value
Non-U.S. Equity	
Capital Guardian	MSCI ACWI-Ex. U.S.
Putnam	MSCI ACWI-Ex. U.S.
Fixed Income	
Loomis Sayles Boston	Lehman Brothers Baa Credit Index
Brandywine (Global Bond)	Salomon World Government Bond Index
Baird	Lehman Aggregate

AFL-CIO	Lehman Mortgage

SCHEDULE IV

MANAGER TERMINATION CHECK-LIST

This checklist is used to ensure that all details are covered when terminating investment management services.

1) Establish plan of action for reallocation of assets from terminated portfolio; transfer to other portfolios or prepare for liquidation.

2) Review department files and logs to identify any outstanding issues.

3) Notify ACERA Administration, Accounting Division, Legal Counsel, consultant, master Custodian and any other vendors of the Termination. Identify and resolve all outstanding issues with these parties.

4) Have Manager and master Custodian review and sign off on monthly market values and performance figures produced during the contract period.

5) Hold payment of last invoice until all issues are resolved.

6) Retain terminated Manager files in the ACERA office for a minimum of one year; then send to ACERA archives.

7) Hold terminated Manager files in ACERA archives for a minimum of 5 years.

SCHEDULE V

ACERA Compliance Schedule

REQUEST	**DUE DATE**
MONTHLY	
Soft Dollar Commission Report (If applicable) (Submit each month regardless of whether any commissions were directed – consultants and master Custodian are subject to this request)	By the 15th of the month following the reported month
Minority Broker Commission Report (Submit each month regardless of whether any commissions were directed)	By the 15th of the month following the reported month
Accounting Report / Portfolio Valuation (Please provide transaction data – buys/sells, a portfolio listing including cost & market values, and performance returns)	By the 20th of the month following the reported month
Derivative Report (If applicable) (Please check ACERA's Investment Policy for report guidelines.)	By the 20th of the month following the reported month
Confirmation that monthly reconciliation with Bank is performed. (Reconciliation should include market values, transactions and performance.)	By the 20th of the month following the reported month

QUARTERLY

Fee Billings (Provide all backup documentation/ reconciliation sign-offs/ DVBE Expenditure Report & backup invoices)	Within 30 days following the end of the quarter
Confirmation of compliance with limitations on investment vehicles and investment markets.	Within 30 days following the end of the quarter
Confirmation of compliance with % limitations on cash holdings (5%), on equity investment (5% of any issuer) and on fixed-income investment (20% of any rated issue).	Within 30 days following the end of the quarter
Confirmation that ACERA's assets under management did not exceed 40% of the total assets under management firm-wide.	Within 30 days following the end of the quarter

QUARTERLY – applicable to Real Estate Program

Operations Report	Due within 30 days of quarter close upon Staff's request

ANNUAL

Annual Performance Fee Billing (If Applicable) (Provide all backup documentation/ reconciliation sign-offs)	Within 30 days following the end of the performance fee period
Organization Chart	When available for the year
Fidelity Bond/ Errors & Omissions Insurance (Please send an original certificate)	When renewed each year

Audited Financial Statements	When available for the year
Form ADV, Parts I and II (If applicable)	When available for the year

<u>ANNUAL – applicable to Real Estate Program</u>

Tactical Plans	When available for the year
Asset Management Plan	Due 30 days prior to fiscal year end
Variance Report on Appraised Properties (if applicable)	Due within 30 days of final property appraisal

SCHEDULE VI

ACERA

INVESTMENT PHILOSOPHY (REVISED MAY 2001)

The following document describes the investment philosophy of the Alameda County Employees' Retirement Association (ACERA). Its purpose is to enunciate the basic principles and beliefs that will underlie ACERA's investment policy and impact the overall management of the pension fund. The Investment Philosophy is designed to complement rather than replace the specific investment policies of the Association. It is expected that the Association's approach to investments, as reflected in its policies and strategies, will be consistent with the philosophy over time. Though the philosophy allows significant flexibility, it also raises some constraints or implications. Where these were deemed to be significant, they have been explicitly identified and labeled as *Implications*.

Future boards may choose to amend the investment philosophy, as their experiences and circumstances will almost certainly differ. The initial document, and any subsequent changes will provide staff, advisors and future trustees with a frame of reference to help them understand how the investment program has evolved as well as the rationale behind its design. Future boards may modify the philosophy as their experiences and circumstances suggest is prudent.

The major sections of the philosophy are:

1. Mission
2. Risk Management
3. Diversification
4. Market Efficiency

5. Hi-Alpha Managers
6. Organizational Infrastructure and Communications
7. Performance Monitoring and Time Horizon

1. MISSION

a) The Board's primary goals in managing the Fund are:

i) To ensure that sufficient funds are available to pay vested benefits and maintain supplemental benefits;
ii) To comply with all applicable fiduciary standards; and,
iii) To create value added, where feasible, that will help reduce the costs of the plan, increase benefits, or both.

2. RISK MANAGEMENT

a) The Board believes that prudent management of risk is a central element of the investment function.

b) Though there are numerous risks involved in the management of a pension investment program, ACERA believes that the following warrant particular attention:

i) ***Funding-related Risk*** - The risk that the funds available in the Plan will be insufficient to pay the promised benefits, both vested and supplemental; or that contribution volatility will be unacceptably high. The primary methods for managing funding risk include regularly conducting integrated asset/liability studies, and establishing appropriate and prudent investment and funding policies.

0.1 In managing the relationship between assets and liabilities, the approved asset allocation of the Fund should provide a minimum of a 90% level of certainty of meeting the projected liabilities of the Plan over a 20 year time period, as determined by the actuary.

ii) ***Benchmark related Risk*** – The risk that the investment benchmarks adopted by the Fund are inappropriate, or that the aggregate of the individual manager benchmarks within an asset class do not adequately reflect the benchmark for the asset class as a whole. The latter risk is a specific risk generally referred to as *benchmark misfit risk (i.e. style risk).* Inappropriate benchmarks or excessive benchmark misfit risk could result in investment performance different than expected and could adversely impact decisions concerning the hiring or firing of investment managers.

0.1 The primary methods for effectively managing benchmark-related risk are:

(a) regular review of the Fund's benchmarks; and

(b) regular measurement and monitoring of misfit risk using proper methodologies.

iii) ***Manager Risk*** - The risk of aberrant performance on the part of individual investment managers, and the related active management risk for asset classes as a whole.

0.1 The primary methods for mitigating manager risk are:

(a) Prudent processes for selecting and monitoring investment managers;

(b) Competent internal investment staff;

(c) Effective investment consulting support; and,

(d) Clear communication to investment managers of ACERA's objectives, expectations, and investment time horizons.

0.2 The primary method for mitigating active management risk for asset classes include:

(a) Establishment of appropriate asset class benchmarks;

(b) Careful monitoring of asset class performance relative to the benchmarks; and

(c) Prudent use of passive management.

iv) ***Fortitude Risk*** - The risk that the board or staff will fail to exercise the patience, judgment, or fortitude required to support long-term policies and strategies for the investment and funding program.

0.1 The keys to managing fortitude risk are believed to include:

(a) Effective orientation and education with respect to institutional investing and actuarial science; and,

(b) A commitment to continually refining, confirming and communicating the investment philosophy and funding policy of the Association.

3. DIVERSIFICATION

a) ACERA acknowledges the basic tenets of modern portfolio theory, which suggest that diversification, or combining assets that are not perfectly correlated with each other, will reduce the long-term volatility of the overall portfolio.

b) It is generally desirable however to avoid overly complex asset structures, provided the allocation selected can reasonably be expected to meet the objectives of the Plan. ACERA believes that the benefits of diversification must be weighed against the costs involved, which may include fees, liquidity, complexity, communication, internal staff resources and expertise and trustee knowledge and effort.

c) The following asset classes are appropriate candidates for inclusion in its portfolio:

i) Domestic equity

ii) International equity (including emerging markets)

iii) Fixed income, including high yield fixed income and international fixed income

iv) Real estate

d) ACERA does not consider alternative investments to be an appropriate candidate for inclusion in its portfolio due to the substantial direct and indirect costs associated with it.

Implications

- A systematic methodology for re-balancing the investment portfolio is required to ensure proper implementation and adequate risk control concerning ACERA's asset allocation.
- Adding or deleting asset classes or investment managers should be considered in light of the impact such decisions are likely to have on the general complexity and cost structure of the portfolio, as well as ACERA's ability to prudently achieve its investment and funding goals over the long run.

4. MARKET EFFICIENCY

Except for specified high alpha assignments:

a) ACERA does not believe in the viability of active management strategies that rely on market timing.

b) ACERA does not believe in the viability of management strategies that call for over weighting or under weighting styles or sectors within an asset class; i.e. benchmark misfit risk will not generate long-term alpha. Accordingly, ACERA generally believes that it should maintain exposures within an asset class (such as style or capitalization weightings) that are consistent with the broad benchmark for the asset class as a whole.

c) ACERA does believe that market efficiency varies among asset classes, creating opportunities for successful active management strategies based on securities selection.

d) Asset classes that can be demonstrated to be efficient should be managed passively in order to reduce active management risk and lower the costs of managing the portfolio.

e) For inefficient asset classes, ACERA believes that it has the ability and a duty to prudently exploit such inefficiencies through active securities selection strategies.

Implications

- ACERA should be conscious of any subtle forms of market timing that may arise in the course of managing the fund, or that may be implicit in investment strategies presented to ACERA for inclusion in the investment program.

- ACERA must determine appropriate methodologies for determining whether an asset class is efficient or presents appropriate opportunities, thus providing insight to the Board on the use of particular strategies.

5. HIGH ALPHA MANAGERS

a) ACERA believes that the portfolio characteristics utilized to control risk in the broad portfolio, such as market capitalization, sector exposure, use of derivatives, leverage limitations, property type or deal structure may be modified for specific managers who control a limited portion of the portfolio and have demonstrated a proven capacity to consistently add value net of fees. Such strategies, which ACERA refers to as Hi-Alpha, may include the following elements:

i) The bulk of the asset class is passively managed or risk controlled; and,
ii) A small number of active managers are retained who employ somewhat more aggressive investment strategies, such as concentrated portfolios, leveraged purchases, developments, high-yield debt, etc.

b) The primary benefits of a Hi-Alpha approach are believed to include:
   i) Reduction in active management risk;
   ii) Lower average investment fees; and
   iii) Concentration on opportunities where the likelihood of adding value is greatest.

c) The market efficiency and opportunities in asset classes may change over extended periods of time; therefore ACERA believes that its portfolio management strategies should adapt over time to reflect the changing nature of capital markets.

6. ORGANIZATIONAL INFRASTRUCTURE AND COMMUNICATIONS

a) ACERA believes that in order for the investment program to achieve its goals, ACERA must invest the necessary resources to build and maintain an appropriate organizational infrastructure, key elements of which include:

   i) A competent, internal investment staff comprised of a sufficient number of investment professionals possessing appropriate leadership, technical and administrative skills.

      0.1 In attracting a competent staff, ACERA recognizes that it competes with the private sector. It must therefore continually strive to create a total work environment that is challenging, rewarding, and competitive.

   ii) A strong relationship with outside general investment consultant(s) who are able to provide ACERA with the following:

0.1 A high degree of investment expertise;
0.2 Innovative and proactive advise and counsel;
0.3 Strong research support; and
0.4 Strong reporting capabilities,

iii) A broad-based information gathering and reporting system to present well- researched, relevant and timely data in a manner that is easily understood, and that supports rigorous and consistent monitoring of critical investment activities.

iv) An open channel of communication between the Board, management, and the Association's external investment professionals.

b) By providing the Board with timely, accurate, and thorough information, the organizational infrastructure will give the Board the high level of comfort it needs to set policy, make investment decisions, oversee the performance of the investment program, and maintain the fortitude necessary to support its investment philosophy, policies and strategies.

Implications

- ACERA must determine what constitutes an appropriate internal investment staff structure, given the nature of the current investment program.

- ACERA must over time take concrete steps towards creating a work environment that will allow the Association to attract and retain needed staff.

- ACERA must recognize that developing the organizational infrastructure it needs – staffing, consulting support, information systems, and communication channels – cannot be achieved overnight, but rather will require an ongoing commitment of time and resources.

7. PERFORMANCE MONITORING & TIME HORIZON

a) ACERA holds the following basic beliefs concerning performance monitoring practices and methodologies:

i) The various investment policies of the Fund, in the aggregate, are the most important determinants of investment success; compliance with investment policies should therefore be monitored rigorously;

ii) The performance of the total portfolio, individual asset classes, and investment managers should be compared to appropriate, predetermined benchmarks;

iii) Peer comparisons are an additional valid tool in assessing individual manager performance (supplementing the use of benchmarks), given that ACERA aims to select superior managers within particular investment styles or mandates. Peer comparisons, or performance rankings, are also valid tools for measuring the performance of asset class portfolios.

iv) Peer group comparisons are not an appropriate means of assessing the performance of the total fund, given that sponsors have different objectives and risk tolerance levels, and therefore may have different asset allocation policies.

v) Benchmark misfit risk, or the risk that the aggregate of individual investment manager benchmarks in an asset class do not adequately reflect the benchmark for the asset class as a whole, should be explicitly measured on a regular basis.

vi) Investment managers are generally hired to fulfill a specific role in a portfolio. Accordingly, ACERA believes it is important that ACERA monitor the extent to which managers comply with their stated style and mandates.

b) ACERA believes that successful funding and investment decisions require a long-term perspective on the part of the Board and management:

i) It is the intention of the Retirement Board that commitments to asset classes and investment strategies should involve long time horizons that may include more than one business cycle (3-5 years each). Relatively illiquid asset classes may require even longer time horizons.

ii) The Board acknowledges that commitments to individual investment managers also require a long time horizon of at least one business cycle (3-5 years).

iii) ACERA believes that proper reporting and monitoring systems; and clear communication among consultants, management, investment managers and the board will enable the Board to maintain the necessary long term perspective on all investment decisions.

<u>Implications</u>

- Assessing the investment performance relative to appropriate, pre-determined, benchmarks is as applicable to the total portfolio and to individual asset classes as it is for individual investment managers, and therefore warrants a commensurate share of the Board's time and attention.

- The Board will spend relatively little time assessing the performance of the Fund relative to that of comparable pension funds.

- ACERA will need to either develop in-house capabilities to regularly measure benchmark-related risk, or it will need to purchase such capabilities from external investment consultants.

- ACERA will monitor all investment managers to ensure they are complying with their stated investment style, regardless of whether they are performing well or poorly. Strongly performing managers who are found to not be following their stated styles will be carefully scrutinized and may be subject to disciplinary action.

- ACERA will monitor all investment providers to ensure compliance with the Board's Investment Policies.

SCHEDULE VII

TABLE OF AMENDMENT DATES

AMENDING RESOLUTIONS

Jun	27,	1985
Oct.	10,	1985
Jan.	9,	1986
Jan.	16,	1986
Mar.	13,	1986
May	22,	1986
Sep.	11,	1986
Oct.	9,	1986
Nov.	20,	1986
May	14,	1987
Aug.	13,	1987
Oct.	8,	1987
Apr.	21,	1988
July	28,	1988
Jan.	29,	1989(4)
Apr.	13,	1989(5)
May	18,	1989
July	13,	1989
Aug.	10,	1989
Nov.	16,	1989(2)
July	11,	1991
June	11,	1992
June	10,	1993
July	8,	1993
Nov.	18,	1993
May	14,	1994
Aug.	18,	1994
Nov.	20,	1994
Feb.	16,	1995
May	18,	1995
Jan.	16,	1997
Aug.	20,	1998
May	20,	1999
Jan.	31,	2000
Apr.	19,	2001

**Alameda County Employees'
Retirement Association**

ACERA

INVESTMENT GUIDELINES, POLICIES AND PROCEDURES

AMENDED July 18, 2002

ACERA
INVESTMENT GUIDELINES, POLICIES AND PROCEDURES
2002

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INVESTMENT GUIDELINES, POLICIES AND PROCEDURES

SECTION I: MISSION AND PURPOSE

The Alameda County Employees' Retirement Association (ACERA) exists for the purposes of providing accurate, timely benefits to its members and their beneficiaries and defraying reasonable expenses of administration.

The Board of Retirement (the Board), having exclusive authority and exclusive fiduciary responsibility for the investment and administration of the Trust Fund (the Fund), hereby establishes the following General Investment Policies and Guidelines (the Policy) for the investment of ACERA's assets. The Board reserves the right to amend, supplement or rescind this Policy at any time.

The Board of Retirement is directed by law and given discretion to prudently invest the plan assets. The purpose of this statement of policy is to assist ACERA in effectively supervising said investments and to encourage effective communication between ACERA and its managers and consultants.

[1] Prepared for ACERA by Cortex Consulting; adopted by the Board of Retirement on March 8, 2000 and revised May 2001.

ACERA's investment goal is to operate at a level of performance in the upper quartile of comparable pension funds on a risk-adjusted basis and to be as fully funded as possible so that ACERA's benefit costs do not become a burden upon future generations of members and taxpayers.

SECTION II: CONSTITUTIONAL REQUIREMENTS

Article 16 §17 of the California State Constitution provides in pertinent part as follows:

"Notwithstanding any other provisions of law or this Constitution to the contrary, the retirement board of a public pension or retirement system shall have plenary authority and fiduciary responsibility for investment of money and administration of the system, subject to the following:

a. The retirement board of a public pension or retirement system shall have the sole and exclusive fiduciary responsibility over the assets of the public pension or retirement system. The retirement board shall also have sole and exclusive responsibility to administer the system in a manner that will assure prompt delivery of benefits and related services to the participants and their beneficiaries. The assets of a public pension or retirement system are trust funds and shall be held for the exclusive purposes of providing benefits to participants in the pension or retirement system and their beneficiaries and defraying reasonable expenses of administering the system.

b. The members of the retirement board of a public pension or retirement system shall discharge their duties with respect to the system solely in the interest of, and for the exclusive purposes of providing benefits to participants and their beneficiaries, minimizing employer contributions thereto, and defraying reasonable expenses of administering the system. A retirement board's duty to its participants and their beneficiaries shall take precedence over any other duty.

c. The members of the retirement board of a public pension or retirement system shall discharge their duties with respect to the system with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with these matters would use in the conduct of an enterprise of a like character and with like aims.

d. The members of the retirement board of a public pension or retirement system shall diversify the investments of the system so as to minimize the risk of loss and to maximize the rate of return, unless under the circumstances it is clearly not prudent to do so.

e. The retirement board of a public pension or retirement system, consistent with the exclusive fiduciary responsibilities vested in it, shall have the sole and exclusive power to provide for actuarial services in order to assure the competency of the assets of the public pension or retirement system."

SECTION III: ELIGIBLE ASSET CATEGORIES

The Fund shall hold assets in categories established by the Board. Any asset category may be held in direct form, in pooled form or in both. Asset categories managed by one or more "Qualified Investment Managers" {Manager(s)} are called "Managed Accounts". Asset categories under the supervision of the County Treasurer are called the Treasurer's Accounts. Eligible asset categories are listed and defined below.

A. **CASH** shall consist of short term (12 months or less) interest bearing investments of high quality such as U.S. Treasury issues, insured certificates of deposit of U.S. banks (fixed and/or variable), commercial paper rated A-1, P-1 or both, or other instruments of equal or better quality, and includes money market funds available through the Custodian Bank (Custodian).

B. **U.S. EQUITY** shall consist of common stocks and other securities which are convertible into common stocks, and ADRs (American Depository Receipts) , as well as cash (per "A" above) and fixed income (per "D" below) when used as temporary substitutes for common stocks.

C. **INTERNATIONAL EQUITY** shall consist of common stocks and other securities convertible into common stocks of companies domiciled outside of the U.S., and GDR's (Global Depository Receipts), as well as cash equivalents and fixed income, domestic or international, which are being used as temporary substitutes for common stock.

D. **FIXED INCOME** shall consist of investments in U.S. taxable bonds, debentures, notes and other evidences of debt. Fixed income may include non-dollar denominated bonds issued by corporations or governments domiciled outside of the United States of America as well as Brady Bonds. Other eligible investments include cash equivalents per "A" above and convertible bonds and preferred stock.

E. **MEMBER MORTGAGES** (closed program) shall consist of first mortgages, secured by the primary residences of the borrowers, underwritten to GNMA/FNMA standards by a qualified third party expert underwriter retained by the Board for that purpose.

F. **REAL ESTATE** shall consist of investments in equity real estate through the use of commingled or direct investments. For more information about real estate investments, refer to ACERA's Real Estate policy which is maintained as a separate document.

SECTION IV: INVESTMENT PHILOSOPHY

The following is a summary of ACERA's Investment Philosophy. For a complete statement, please refer to Schedule VI, "ACERA Investment Philosophy".

The Board believes that its investment policies, in aggregate, are the most important determinants of its investment success. Compliance with investment policies should therefore be monitored rigorously. The Board also believes that performance of the total portfolio, individual asset classes, and Managers should be monitored and compared to appropriate, predetermined benchmarks.

The Board believes that prudent management of risk is a central element of the investment function and that diversification among asset classes will reduce risk and enhance returns of the overall investment portfolio in the long term.

The Board believes that market efficiency and opportunities vary among asset classes and may change over extended periods of time; therefore ACERA believes that its portfolio management strategies should adapt over time to reflect the changing nature of capital markets.

The Board's primary goals in managing the Fund are:

1. To ensure that sufficient funds are available to pay vested benefits and maintain supplemental benefits;
2. To comply with all applicable fiduciary standards; and
3. To add marginal value that will help reduce the costs of the plan and/or to increase benefits for the beneficiaries.

The Board believes that in order to achieve its goals, ACERA must invest the necessary resources to build and maintain an appropriate organizational infrastructure.

SECTION V: INVESTMENT STRATEGY

A. **U.S. EQUITY** will be structured to capture exposure to the broad U.S. equity market as represented by the Russell 3000 Index. Passively managed (index) portfolios will be used in markets that are reasonably efficient. These portfolios are intended to provide broadly diversified market exposure with controlled (market) risk and minimal cost.

Actively managed portfolios will be used in less efficient markets when the Board determines that a Manager possesses special skills or abilities that enable that Manager to capture excess returns relative to the market, adjusted for risk and fees; or to exploit specialty markets that provide enhanced return with acceptable risk.

A great part of the Russell 3000, on a market value basis, is comprised of large-cap stocks, which the Board believes are efficiently priced most of the time. Therefore, the Board has adopted a policy of obtaining overall exposure to this segment of the market via passively managed indexed products. Some active Managers have been employed to enhance overall portfolio return in the large- and/or mid-cap sectors on a risk- and fee-adjusted basis. These Managers manage ACERA's "Hi-Alpha" program.

The remainder of the Russell 3000 index is comprised of small to mid-cap companies. Some opportunities for active management enhancement exist in these securities due to market inefficiencies. ACERA will attempt to capture these opportunities through a mix of Managers who have the special skills required to identify smaller companies that may be undervalued or possess substantial growth potential.

The U.S. equity portion of the portfolio shall be allocated among the various styles and Managers as indicated in Schedules I and IA.

B. **INTERNATIONAL EQUITY** represents an opportunity to diversify risk and capture enhanced returns within markets generally less efficient than the U.S. domestic equity market. 100% of the international equity portion of the Fund will be invested in actively managed portfolios.

C. **FIXED INCOME** represents a means of reducing overall portfolio risk and capturing incremental returns. Inefficiencies in the pricing and trading of fixed income securities create opportunities to add value through active management. 100% of the fixed income portion of the portfolio will be invested in actively managed portfolios.

D. **REAL ESTATE** will be used as a means for diversifying the portfolio and capturing additional returns due to the low correlation between returns on real estate and financial assets. Due to the illiquid nature of real estate assets, distinctions between active and passive management are not applicable. For more information regarding real estate investments, refer to ACERA's Real Estate policy which is maintained as a separate document.

SECTION VI: ASSET ALLOCATION AND REBALANCING

Asset allocation targets, a function of the returns and risks from various asset classes and the nature of the plan's liabilities, are set forth in Schedule I. A goal of asset allocation is balancing asset growth versus liability growth considering time horizons, liabilities and risk tolerance.

Rebalancing is the risk control process of returning an allocation back to the desired target level after having drifted away from its targeted position. Acceptable ranges around the asset allocation targets are set forth in Schedule IA. The objective of rebalancing is to enhance the risk-adjusted performance of the asset allocation structure.

ACERA Staff ("Staff") shall be responsible for maintaining the relative weights of asset classes and allocations within the acceptable rebalancing ranges indicated in Schedule IA. Should an asset class or allocation fall outside its target range, Staff shall rebalance the asset class or allocation back to the target weights as specified in the asset allocation structure in Schedule I.

Staff shall:

1. Monitor the portfolio;
2. Determine whether or not any asset category is out of balance with its target asset allocation in excess of the specified tolerance range;
3. Determine whether or not any Manager within each asset category is out of balance with their target allocation in the excess of the specified tolerance range;
4. And, if so, either:

(a) instruct the relevant Managers to redirect cash income (interest coupon and dividends) in concert with an evaluation of pending commitments and other cash flows (employer and employee contributions), in order to bring the allocation(s) back to the adopted strategic target; or
(b) instruct the relevant Managers to liquidate or acquire the appropriate dollar value of securities to reach the target and reallocate the cash thus generated or required to the other category(s) or Manager(s) necessary.

Staff shall report to the Board on a regular basis the status of the Fund with respect to how categories are tracking relative to their allowable ranges, as well as any actions taken to rebalance the portfolio.

SECTION VII: ASSET CATEGORIES OBJECTIVES

The general objective of the Board is to preserve capital and earn a return from appreciation and income, as described herein.

The minimum return objective for the Fund shall be the current actuarial interest assumption rate plus 25 basis points per year over a market cycle. Returns shall be calculated net of fees.

The minimum return objective for the Fund over a market cycle (up to five years) shall also be 400 basis points (4%) per year over the national Consumer Price Index, published by the U.S. Department of Commerce.

The objectives of each asset category are:

A. CASH

1. A rate of return in excess of 90-Day U.S. Treasury bills.

2. A rate of return within the upper one half of a universe of like short-term funds.

B. U.S. EQUITY

1. A rate of return in excess of the U.S. equity market as measured by the Russell 3000 Index after adjustment for risk and fees.

2. A rate of return within the upper 33rd percentile of the Wilshire Co-op or similar database of the performance of diversified equity portfolios.

C. INTERNATIONAL EQUITY

1. A rate of return in excess of the Morgan Stanley Capital International All Country World Index Ex-U.S. Free (MSCI ACWI).

2. A rate of return within the top quartile of the Wilshire Co-op or similar database of the performance of diversified international equity portfolios.

D. U.S. FIXED INCOME

1. A rate of return in excess of the Lehman Aggregate Bond Index published by Lehman Bros. Inc..

2. A rate of return within the top quartile of the Wilshire Co-op or similar database of the performance of diversified fixed income portfolios.

E. MEMBER MORTGAGE (closed program)

1. A rate of return that compares favorably with the Salomon Mortgage Index.

2. A delinquency rate of less than 2% of loans outstanding;

F. REAL ESTATE

Total Return - over rolling 5 year periods a minimum total real rate of return (net of management fees) of 6.0% using a "Time Weighted Market Value" calculation. The real return expectation is after inflation (U.S.A. CPI-Urban).

1. Income Return – Income, which is defined as cash distributed to the Association, should comprise at least 2/3 of the total return over rolling five periods.

2. Minimum Going-in Yields – On individual separate account assets, the Manager's five year projection (net of fees) will exceed the consultant's five year projection for ten year treasuries by no less than 150 basis points.

In addition, objectives that reflect the particular investment strategy or style used by individual Managers shall be outlined in an attachment to the Manager's contract.

SECTION VIII: ALLOCATION OF CASH FLOW

Cash flow not needed for benefit payments or administrative expenses shall be allocated to Managed Accounts in a ratio that best funds the overall asset allocation as shown in Schedules I and IA.

If cash flow is insufficient for the payment of benefits or to cover administrative expenses, then Managed Accounts shall be debited in a ratio that best satisfies the target allocation shown in Schedules I and IA. Such debits, if necessary, will be carried out as needed, and with timely notice to Managers to facilitate effective funds transitions and performance measurement.

For planned investments which may not need to be funded immediately, a reserve may be budgeted and invested in appropriate index funds until such moneys are required. Alternatively, Managed Accounts within "overfunded" asset classes may be called upon to provide the required moneys. Funds intended for real estate investments but not yet invested shall be divided equally and held in the equity and fixed income index funds until called by the real estate Manager.

SECTION IX: PROHIBITED INVESTMENTS

Managers shall exercise prudent expert standards in defining prohibited investments. For example, prohibited investments include, but are not limited to, securities issued by the County of Alameda or any agency thereof.

SECTION X: DIRECTED BROKERAGE

ACERA does not engage in either directed commission arrangements or "soft dollar" transactions.

SECTION XI: DERIVATIVE INSTRUMENT USAGE POLICY

Exposure to risk by use of derivative instruments must be consistent with

ACERA's overall investment guidelines. Derivatives shall not be used to establish a leveraged position (i.e. offsetting Cash positions must be maintained against all delayed settlement transactions).

SECTION XII: SELECTION OF INVESTMENT MANAGERS

The Investment Committee shall direct Staff and/or a consultant to initiate searches for Managers. Staff and/or the consultant shall screen qualified candidates and present a list of finalists to the Investment Committee for its approval. Upon approval of the list, the finalists shall be interviewed by Staff and the consultant (if applicable) in a publicly noticed meeting at which no less than three (3) Investment Committee members shall be present. Staff and the consultant (if applicable) shall evaluate the interviews, rank the finalists, and make a recommendation to the Investment Committee to hire one or more firms attaining the highest rankings. It is possible that none of the firms will be recommended for hire.

These procedures are developed for the convenience and benefit of ACERA, and shall not bind ACERA or invalidate the selection of a Manager if different processes are used subsequent to the promulgation of this Policy.

SECTION XIII: AUTHORITY OF INVESTMENT MANAGERS

Subject to the laws of the United States and the State of California, and to the terms and conditions of this Policy, Managers shall have full discretion to direct the purchase, exchange, sale and reinvestment of the assets of the Managed Accounts. The Board expects that Managers will recommend changes to this Policy when any part of this Policy appears to be at variance with overall market and economic conditions.

Managers shall place orders to buy and sell securities and, by notice to the Custodian, shall cause the Custodian to deliver and receive securities on behalf of the Fund. Managers shall, upon Board inquiry, report placement of ACERA brokerage such that the Board shall be assured commissions were placed for the sole and exclusive benefit of the Fund.

Separate account Managers shall not vote proxies. Proxies shall be voted by ACERA according to Board-established policies and procedure.

Securities lending shall be performed by the Custodian Bank under the oversight of the Board.

SECTION XIV: INVESTMENT GUIDELINES FOR THE MANAGED ACCOUNTS

Individual Manager discretion shall be governed by the guidelines set out in the Investment Contract of each Manager.

A. GENERAL

1. All investments shall comply with all applicable laws of the United States and the State of California governing the investment of pension trusts.

2. All securities transactions shall be executed by reputable broker/dealers, banks, or the Custodian, and shall be on a best-price and best-execution basis, and shall be reported to ACERA as is called for elsewhere in this Policy.

3. All Managers shall refrain from investing in a tobacco producer investment opportunity when, in their expert opinion, an alternative non-tobacco producer investment opportunity is available that will satisfy the same ACERA portfolio guidelines, instructions and objectives for risk, return and diversification.

B. EQUITY

Managers have full discretion to invest solely in readily marketable and diversified equity securities as defined above subject to the following:

1. For Managed Accounts, no more than 10% of the value (at time of investment) of the account shall be invested in the securities of a single issuer.

2. ACERA shall not hold more than 10% of the equity securities of any issuer.

3. Equity securities shall possess value and quality corroborated by generally accepted techniques and standards of fundamental securities analysis.

4. Assets in a Managed Account not invested in equity securities shall be kept with interest in appropriate money market instruments, including any money market fund available through the Custodian.

5. A Managed Account shall be subject to ACERA's policy on derivatives.

6. All Managers shall endeavor to be fully invested in stocks at all times unless they have received specific authorization to the contrary from the Board. Cash holdings, as defined in this Policy, shall generally not exceed 5% of the portfolio on a market value basis.

C. FIXED INCOME

Managers have full discretion to invest solely in readily marketable and diversified securities including, but not limited to:

1. Obligations of the U.S. Treasury.

2. Obligations guaranteed by an agency of the United States.

3. Insured certificates of deposit and banker's acceptances of credit worthy banks.

4. Corporate and other evidences of debt. At least 80% of this debt must be rated by Moody's Investor's Services or by Standard & Poors.

5. Commercial paper and banker's acceptances of issuers rated P-1 by Moody's Investor's Service.

6. Or A-1 by Standard & Poors Corporation.

7. Excepting direct obligations of the U.S. Government, and those explicitly guaranteed by the U.S. Government, no account shall hold more than 5%, at cost, of the obligations of any single issuer.

8. Fixed income derivative investments shall be in accordance with ACERA's derivative policy.

SECTION XV: SEPARATE ACCOUNT MANAGER SPECIFICATIONS

A. Managers must be registered as investment advisors under the Investment

Advisor's Act of 1940, a bank (as defined in that act) or an insurance company qualified to perform investment management services under state law in more than one state, including California. In addition, by accepting appointment as an Manager for ACERA, Managers shall acknowledge that they are "Plan Fiduciaries" and "Qualified Investment Managers" as defined by the Employees' Retirement Income Security Act (ERISA) of 1974, see or reference United States Code Title 29 Section 1001 et. seq..

B. Managers shall maintain fiduciary insurance in the amount of 10% of the total assets managed in the ACERA account or $25 million, whichever is higher, unless the contract specifies otherwise.

C. Managers shall promptly notify ACERA of changes that occur in any of the following:

1. The investment strategy used in managing the subject product.
2. The personnel involved in managing ACERA's account.
3. The ownership, key personnel, or organizational structure of the Manager's company.
4. The Manager company's financial condition.
5. The number of clients invested in the subject product.
6. The market value of the total assets managed in the subject product.

D. Managers shall promptly notify ACERA if they are subject to censure or disciplinary action by a regulatory agency.

E. On a monthly basis, Managers shall report on the activities of the portfolios managed on behalf of ACERA. Monthly reports shall include descriptions of holdings along with cost and market values; summaries of purchases and sales; description of major changes to the portfolio; and a declaration by the Manager that its investment activities comply with the provisions of this Policy.

On a monthly basis, active Managers shall certify in writing that the portfolio market values, transactions and performance data are reconciled with ACERA's Custodian.

On a monthly basis, Managers shall furnish a report detailing the entities to whom services were paid for with soft dollars; the total amount of soft dollars used for such services; and descriptions of the services purchased with those soft dollars. Consultants and the Custodian are also required to report on their soft dollar usage, if applicable.

On a quarterly basis, Managers shall invoice ACERA for payment of fees for services rendered. The fee shall be calculated using the rate established in the fee schedule of the Manager's contract with ACERA and using the market values determined by ACERA's Custodian.

F. Managers shall provide ACERA with the most recent copy of Form ADV, Part II upon their receipt of the same, on an ongoing basis.

G. Managers shall not make contributions, provide gifts, reimbursements of expenses or provide personal benefits exceeding $250 in the aggregate within any 12-month period to any Trustee, fiduciary, employee or consultant of ACERA. Donations of educational conferences and similar events and benefits, including travel, meals and accommodations will be made to ACERA and not directed to individuals. The Board will determine whether to accept any donations and will be solely responsible for selection of the Trustee, staff member, or other individual, who will attend or otherwise participate on behalf of ACERA.

SECTION XVI: MANAGER MONITORING POLICY

The ACERA Board has contracted with a number of external Managers to invest ACERA assets in the public equity markets. As part of the Board's fiduciary duties to prudently select, monitor and supervise these Managers, the Board has adopted this Policy. The intent of this Policy is to notify Managers of the standards by which they will be judged and to establish a structure which the Investment Committee and the Board can use to monitor the performance of the Managers.

Managers will be monitored to:

1. Evaluate how well they achieve their investment objectives.
2. Ensure that they adhere to their established investment approach/style and do not attempt to index returns to preserve stellar performance or take extraordinary risk to overcome poor performance.
3. Identify issues or trends that have the potential to result in losses to the Fund.
4. Alert the Board when Managers are not performing to expectations so that appropriate remedial action can be taken.

Managers will be evaluated on the basis of the following: performance, style integrity, organizational stability, compliance, and client service described in greater detail below.

A. PERFORMANCE

On a monthly basis Staff will monitor Manager holdings, activity and performance. On a quarterly basis Staff and/or a consultant will furnish the Investment Committee and/or Board with an in-depth evaluation of each Manager which will include a comparison of the Manager to its contract benchmark and a peer universe of Managers using a similar investment style. This report shall include an analysis of the sources of Managers' returns (stock selection, industry selection, asset allocation, etc.) and shall identify which decisions enhanced or diminished performance.

On a quarterly basis, trading costs will be evaluated in terms of commissions paid and execution of trades. Staff and/or a consultant shall furnish a report to the Investment Committee and/or Board regarding trading costs on an annual basis.

B. STYLE INTEGRITY

Each Manager will be analyzed at least annually to ensure that the Manager is continuing to invest the portfolio in the style for which they were originally hired. Style integrity is essential to maintain the Board's asset allocation policy. Any significant deviation in style will result in the overall portfolio having a different characteristic, in some measure, from the broad market which is represented by the Russell 3000 index. Significant variations in the portfolio characteristics from the style anticipated in the management contract may indicate a change in its investment style.

This review also provides the Investment Committee and/or Board an opportunity to evaluate the Manager's continuing "fit" with the goals of the overall fund. By monitoring Manager style the Investment Committee and/or Board can assure that its Manager mix takes advantage of opportunities to increase diversification through lower correlation of returns among individual Managers.

C. ORGANIZATIONAL STABILITY

Managers' organizations will be monitored to ensure continuity of the intellectual and philosophical processes that went into developing the particular investment approach contracted for by ACERA. In addition, Managers will be monitored for business risk, quality of staff**,** departures of key investment personnel, change in ownership or acquisition, and potential conflicts of interest.

It is ACERA's intent that its portfolio comprises no more than 25% of the Manager's total assets under management. Therefore ACERA will monitor the Managers' assets, firm-wide, as well as in the subject product.

D. COMPLIANCE

Managers will be monitored to ensure they are adhering to Federal and state laws regarding securities and the management of investment portfolios, trading, and pension investments; ethical practices of the investment professions; the Contract governing their relationship with ACERA; and the policies and guidelines set forth in this Policy statement and any other written directives issued by ACERA.

Each ACERA contract will specify which investment vehicles a Manager is authorized to use, which markets the Manager is authorized to transact business in and any limitations within a market (small or large capitalization, value or growth orientation). The assets in each Manager's portfolio shall be reviewed monthly to ensure compliance with contract guidelines.

All required documents and reports, set forth in Schedule V, must be submitted in a timely manner and in the format specified by ACERA.

Managers must provide prior notification and justification for failure to comply with rules, regulations, contract provisions, deadlines or other directives. Managers must provide a time frame for curing any deficiencies. Staff shall evaluate each incident on a case-by-case basis and determine whether an exception may be granted.

E. CLIENT SERVICE

Managers are required to comply with routine portfolio investment guidelines and reporting deadlines and are also expected to cooperate with special requests for information. ACERA will establish reasonable time frames for all requests and reporting and will provide feedback to all external equity Managers regarding the perceived quality of their client service.

ACERA Staff will endeavor to meet with each Manager at least twice a year by telephone or in person to review performance and other issues.

SECTION XVII:

CONTRACT REVIEW PROCESS

If during the course of regular monitoring, ACERA determines that a Manager's performance, style, organizational stability, compliance, or client service has declined to unacceptable levels, ACERA may, at its discretion, subject the Manager to ACERA's Contract Review Process. As part of the Board's fiduciary duties to prudently select, monitor and supervise their Managers, the Board has approved this process. The purpose of this process is to ensure as little disruption as possible in the event that concerns or problems arise with respect to a Manager's performance. The Board does not confer any additional rights or protections to its Managers by the promulgation of this Policy and/or this process.

There are generally three stages of review: Watchlist, Probation, and Termination. (described below). ACERA reserves the right to terminate an investment management contract at any time, upon 30 days notice, for any reason, and without resort to this Contract Review Process.

The Contract Review Process may result in one or more of the following:

1. Placement on Watchlist or Probation status.
2. Movement from one stage of review to another, or removal from the Contract Review Process.
3. Reduction of assets under management.
4. Revision of investment contract guidelines for that Manager.
5. Re-negotiation of fees.
6. Termination of a Manager's contract.
7. Or any other deemed appropriate by the Board

Each situation is unique and action by the Board will vary depending on the type of Manager and the style/strategy involved. The following describes the Contract Review Process:

A. INITIAL REVIEW

Prior to a Manager being considered for Watchlist, Probation or Termination, ACERA may take the following steps :

1. Analysis

Staff will conduct in-depth analyses of the perceived deficiency to verify that a deficiency exists, form an initial assessment of the severity of the deficiency, and make an initial determination of possible causes.

2. Discussion with the Manager

Staff will contact the Manager to discuss the situation and the results of Staff's analysis.

3. Consultant Input

ACERA may seek the services of a consultant to provide additional assessment and advice regarding the situation, depending on the severity of the deficiency.

All phases of account compliance may be reviewed during this step, in addition to the specific issue that originated the Review Process.

B. FORMAL ACTION

After completing the Initial Review, Staff may recommend to the Investment Committee and/or Board that the Manager be either placed on Watchlist or Probation or, in certain cases, Terminated. The specific criteria for determining which level of Contract Review to recommend is outlined later in this Policy section and summarized in tabular form in Schedule II. The Committee and/or Board will approve or reject the recommendation.

Upon approval of a Watchlist or Probation recommendation:

1. Staff will notify the Manager of the Board's decision and will provide the Manager with a statement of concerns which outlines the areas which need improvement.

2. The Manager will be asked to respond in writing with an explanation of the issues

and a proposed action plan to resolve the issues.

3. Staff, a consultant and the Manager will collectively draft a Plan of Action. The plan will identify: the specific steps to be taken to correct the problem; the time frames for further review; and what additional monitoring may be required.

   At the end of the time period specified in the Plan of Action, the Manager will be evaluated and one of the following actions may be taken:

   (a) Removal from Contract Review: If the successfully resolves the issues/deficiencies and demonstrates continued success in all other areas of its relationship with ACERA.

   (b) Movement from Probation to Watchlist: If the Manager has satisfied all or most of the issues/deficiencies that caused it to be placed on Probation, yet Staff continues to have concerns about the Manager. If circumstances warrant, a Manager may also be moved from Watchlist to Probation at any time during the Contract Review Process.

   (c) Extension of Contract Review: A Manager may be given additional time to satisfy the conditions of its Action Plan if reasonable progress is being made. Extensions may also be granted if unfavorable market conditions or high costs make reallocation of assets inadvisable.

   (d) Termination: If the Manager has not satisfactorily resolved the issues/deficiencies, Staff may recommend termination as described below. Termination may be recommended at any time during the Contract Review Process if circumstances warrant.

WATCHLIST

Watchlisting indicates an increased level of concern, but does not indicate major deficiencies. The Watchlisting period is typically one year. Any of the following may result in a Watchlist recommendation:

A. UNDERPERFORMANCE

Please refer to Schedule II for specific Watchlist criteria for each Manager.

B. STYLE DEVIATION

Managers are expected to adhere to the style of investment management for which ACERA originally hired them. Changes in portfolio characteristics or style drift may lead to a Watchlist recommendation.

C. ORGANIZATIONAL CHANGE

<u>NEW OWNERSHIP</u>
Even relatively benign ownership changes, which impact personnel key to ACERA's portfolio management may be cause for a Watchlist recommendation.

<u>TURNOVER</u>
Significant turnover in top management, portfolio Managers, research or trading staff, or marketing personnel, which does not directly affect the team responsible for ACERA's account may warrant Watchlisting.

<u>REORGANIZATION</u>
Changes which signal management deterioration**,** departures of key investment personnel, change in ownership that increases risk to

ACERA's investments, or hasty /uncontrolled growth in the firm with potential to disrupt the investment team hired for management of ACERA's account will mandate Watchlisting, without requiring prior approval of the Committee and/or Board.

<u>ASSETS UNDER MANAGEMENT</u>
If the market value of ACERA's portfolio rises above 25% of the Manager's total assets under management, Watchlist status may be recommended.

D. COMPLIANCE

<u>CONTRACTS AND OTHER AGREEMENTS</u>
Managers are expected to comply with the investment management contract, investment guidelines, or other directives. Non- or partial compliance may result in a Watchlist recommendation.

<u>REPORTING</u>
Staff will contact Managers to request past due reports. If the Manager's reports are consistently delinquent, the payment of fees may be delayed. If a Manager cannot comply with reporting deadlines, ACERA should be given prior notification. If warranted, a variance may be allowed. Managers are expected to resolve reporting problems immediately upon notification by ACERA. Repeated delinquency in reporting may result in a Watchlist recommendation.

E. CLIENT SERVICE

If a Manager is uncooperative and demonstrates a poor client service attitude, Watchlisting is appropriate. Managers are expected to resolve client service issues immediately upon notification by ACERA.

PROBATION

Probation indicates a level of serious deficiency and signals a need for closer contact with the firm. Probation necessitates a cautious, observant relationship with the Manager.

Managers may be placed on Probation with or without first being placed on Watchlist status. The Probation period is typically one year.

The following may result in Probation:

A. UNDERPERFORMANCE

Please refer to Schedule II for specific Probation criteria for each Manager.

B. STYLE DEVIATION

Probation may be recommended when a Manager's portfolio characteristics are significantly different from its style. In general, a Manager will be placed on Probation after four or more consecutive quarters of deviating from its style benchmark. In effect, if the Manager is no longer the same Manager that was retained for ACERA's account, Probation and perhaps even Termination is appropriate.

C. ORGANIZATIONAL CHANGE

Changes in ownership, organizational assignments**,** departures of key investment personnel, change in ownership that poses substantial risk to ACERA's investments, or turnover that have the potential to seriously disrupt or destroy the investment management team that was hired to manage the ACERA account may result in Probation or Termination. When key personnel, such as top management, portfolio Managers, research and trading staff are no longer available for use on the ACERA portfolio and do not appear to be replaced or replaceable, a Probation or Termination recommendation is appropriate. Managers may be placed on Probation without requiring prior approval of the Committee and/or Board.

D. COMPLIANCE

If a Manager does not comply with securities laws, industry regulations, standards of professional conduct or contractual provisions, a recommendation of Probation is appropriate. Certain circumstances may warrant Termination.

E. CLIENT SERVICE

Failure to correct any issues that previously resulted in the Watchlist recommendation may result in Probation. Managers will generally be given one quarter to resolve client service issues.

TERMINATION

Upon determining that the Manager has not made adequate improvement in the areas outlined in the Plan of Action, Staff may recommend to the Investment Committee and/or Board that the Manager be terminated. Prior to making the final decision to terminate the Manager, the Investment Committee may invite the Manager to make a presentation at the meeting in which the Termination recommendation is to be discussed. Staff will have analyzed the liquidity of the Manager's portfolio and will have a recommendation and plan for disposition of the assets.

Upon the Investment Committee's decision to terminate, Staff will notify the accounting division as well as the Board's legal counsel of the action. All outstanding issues between the Manager and ACERA's master Custodian, brokers, consultant, or other parties shall be resolved prior to closing out the contract. The Manager Termination checklist is attached as Schedule IV.

The Contract Review Process described in this Policy does not provide any additional rights or protections to Managers, beyond what is provided in the contract. ACERA reserves the right to terminate an investment management contract without resort to the Contract Review Process, at any time, upon 30 days notice, for any reason.

SCHEDULE I

ASSET ALLOCATION AND MANAGER STRUCTURE TARGETS

ASSET ALLOCATION TARGETS

Asset Class	Target Allocation
U.S. Equity	35
International Equity	22
Total Equity	57
Fixed Income	34
Real Estate	9

MANAGER STRUCTURES TARGETS

Managers		Target Allocation
U.S. Equity		
Large Cap Core Index	BoNY S&P 500	61
Large Cap Growth (Hi-Alpha)	TCW	12
Large Cap Value (Hi-Alpha)	PFR	12
Large Cap Enhanced Core (Hi-Alpha)	Salus	4
Small Cap Growth	Nicholas Applegate	6
Small Cap Value	Brandywine	5
Non-U.S. Equity		
Core Developed Markets	Capital Guardian	65
Core Developed Markets	Putnam	35
Fixed Income		
Aggressive Core Plus	Loomis Sayles Boston	29
Global Bond	Brandywine	16
Enhanced Index	Baird	49
Mortgage	AFL-CIO	6

SCHEDULE IA

ASSET ALLOCATION PORTFOLIO REBALANCING

The objective of rebalancing is to control risk and enhance the risk-adjusted return of the asset allocation strategy. For purposes of enhancing the risk-adjusted return of the asset allocation structure, the relative deviation of any liquid sub asset class away from its target weight (or liquidity-adjusted target weight) shall be no more than plus or minus 1.7 standard deviation factors of each allocation's expected volatility, relative to the other allocations in the asset mix. This standard deviation factor shall be used to define the range of allowable deviation from Policy target asset allocations. If any sub asset class reaches its allowable deviation from its target allocation, all sub asset classes will be evaluated.

The actual reallocation will be at the discretion of ACERA's staff (with oversight by the rebalancing consultant) after reviewing: the relative magnitude of deviation from target for all other sub asset classes; the available cash liquidity of sub asset classes that could be used to fund rebalancing; pending cash flows (employer and employee contributions, or proceeds from a terminated manager's portfolio); pending liquidity windows with commingled investment pools; pending investment commitments (real estate transactions and/or new funding commitments; and, pending interest coupon and dividend cash flows.

Asset allocation and rebalancing status reports, and any rebalancing activity taken toward attaining the objective of the rebalancing program will be reported to the Board of Trustees on a monthly basis.

Significant modifications to the asset allocation strategy shall be cause to review the appropriateness of maintaining this rebalancing parameter or revising it to a parameter more suitable to the revised asset allocation structure.

SCHEDULE II

Watchlist/Probation Criteria for Performance

(Footnote: If Plan history with Manager is less than 5 years, use rolling 3 year period)

Watchlist Criteria	Probation Criteria
US Equity • Large Cap Core Index: negative tracking error exceeds 5 bps on an annualized basis in any 1 year period. • Large Cap Growth: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters. • Large Cap Value: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters. • Small Cap Growth: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters. • Small Cap Value: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters. • Large Cap Enhanced Core: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters.	**US Equity** • Large Cap Core Indexed: negative tracking error exceeds 5 bps in any 1 year period; or negative tracking error exceeds 10 bps for 2 quarters. • Large Cap Growth: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters. • Large Cap Value: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters. • Small Cap Growth: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters. • Small Cap Value: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters. • Large Cap Enhanced Core: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters.

International Equity • Concentrated Core: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters.	**International Equity** • Concentrated Core: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters.
Fixed Income • Aggressive Core Plus: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters. • Global Bond: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters. • Enhanced Index: cumulative 1 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters. • Mortgage: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters.	**Fixed Income** • Aggressive Core Plus: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters. • Global Bond: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters. • Enhanced Index: cumulative 1 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters. • Mortgage: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters.

SCHEDULE III

BENCHMARKS FOR ACERA ASSET CLASSES, EQUITY AND FIXED INCOME MANAGERS

BENCHMARKS FOR ASSET CLASSES

Asset Class	**Benchmark Index**
U.S. Equity	Russell 3000
International Equity	MSCI ACWI-Ex. U.S.
Total Equity	N/A
Fixed Income	Lehman Aggregate U.S./Salomon World Government Bond Ex U.S. /Lehman High Yield in the ratio of 75/15/10
Real Estate	NCREIF

BENCHMARKS FOR EQUITY AND FIXED INCOME MANAGERS
(Please refer to individual Manager's contract for expected annual premium)

Manager	**Benchmarks**
U.S. Equity	
BoNY S&P 500	S&P 500
TCW	Russell 1000 Growth
PFR	Russell 1000 Value
Salus	S&P 500
Nicholas Applegate	Russell 2000 Growth
Brandywine	Russell 2000 Value
Non-U.S. Equity	
Capital Guardian	MSCI ACWI-Ex. U.S.
Putnam	MSCI ACWI-Ex. U.S.
Fixed Income	
Loomis Sayles Boston	Lehman Brothers Baa Credit Index
Brandywine (Global Bond)	Salomon World Government Bond Index
Baird	Lehman Aggregate
AFL-CIO	Lehman Mortgage

SCHEDULE IV

MANAGER TERMINATION CHECK-LIST

This checklist is used to ensure that all details are covered when terminating investment management services.

1) Establish plan of action for reallocation of assets from terminated portfolio; transfer to other portfolios or prepare for liquidation.

2) Review department files and logs to identify any outstanding issues.

3) Notify ACERA Administration, Accounting Division, Legal Counsel, consultant, master Custodian and any other vendors of the Termination. Identify and resolve all outstanding issues with these parties.

4) Have Manager and master Custodian review and sign off on monthly market values and performance figures produced during the contract period.

5) Hold payment of last invoice until all issues are resolved.

6) Retain terminated Manager files in the ACERA office for a minimum of one year; then send to ACERA archives.

7) Hold terminated Manager files in ACERA archives for a minimum of 5 years.

SCHEDULE V*

ACERA Compliance Schedule

REQUEST	**DUE DATE**
MONTHLY	
Soft Dollar Commission Report (If applicable) (Submit each month regardless of whether any commissions were directed – consultants and master Custodian are subject to this request)	By the 15th of the month following the reported month
Minority Broker Commission Report (Submit each month regardless of whether any commissions were directed)	By the 15th of the month following the reported month
Accounting Report / Portfolio Valuation (Please provide transaction data – buys/sells, a portfolio listing including cost & market values, and performance returns)	By the 20th of the month following the reported month
Derivative Report (If applicable) (Please check ACERA's Investment Policy for report guidelines.)	By the 20th of the month following the reported month
Confirmation that monthly reconciliation with Bank is performed. (Reconciliation should include market values, transactions and performance.)	By the 20th of the month following the reported month

* This Schedule is designed for all investment managers of ACERA. However, managers may be required to provide additional compliance reports based on their individual investment agreements with ACERA. Should there be any conflict between individual investment agreements with ACERA and ACERA investment guidelines, policies and procedures, the individual investment agreements should prevail.

QUARTERLY

Fee Billings (Provide all backup documentation/ reconciliation sign-offs/ DVBE Expenditure Report & backup invoices)	Within 30 days following the end of the quarter
Confirmation of compliance with limitations on investment vehicles and investment markets.*	Within 30 days following the end of the quarter
Confirmation of compliance with % limitations on cash holdings, on equity investment and on fixed-income investment. *	Within 30 days following the end of the quarter
Confirmation that ACERA's assets under management does not exceed 25% of the total assets under management firm-wide.	Within 30 days following the end of the quarter

QUARTERLY – applicable to Real Estate Program

Operations Report	Due within 30 days of quarter close upon Staff's request

ANNUAL

Annual Performance Fee Billing (If Applicable) (Provide all backup documentation/ reconciliation sign-offs)	Within 30 days following the end of the performance fee period
Organization Chart	When available for the year
Fidelity Bond/	When renewed each year

* Please refer to the Specific Investment Guidelines of each manager's investment contract for details.

Errors & Omissions Insurance (Please send an original certificate)	
Audited Financial Statements	When available for the year
Form ADV, Parts I and II (If applicable)	When available for the year

<u>ANNUAL – applicable to Real Estate Program</u>

Tactical Plans	When available for the year
Asset Management Plan	Due 30 days prior to fiscal year end
Variance Report on Appraised Properties (if applicable)	Due within 30 days of final property appraisal

SCHEDULE VI

ACERA

INVESTMENT PHILOSOPHY (REVISED MAY 2001)

The following document describes the investment philosophy of the Alameda County Employees' Retirement Association (ACERA). Its purpose is to enunciate the basic principles and beliefs that will underlie ACERA's investment policy and impact the overall management of the pension fund. The Investment Philosophy is designed to complement rather than replace the specific investment policies of the Association. It is expected that the Association's approach to investments, as reflected in its policies and strategies, will be consistent with the philosophy over time. Though the philosophy allows significant flexibility, it also raises some constraints or implications. Where these were deemed to be significant, they have been explicitly identified and labeled as *Implications*.

Future boards may choose to amend the investment philosophy, as their experiences and circumstances will almost certainly differ. The initial document, and any subsequent changes will provide staff, advisors and future trustees with a frame of reference to help them understand how the investment program has evolved as well as the rationale behind its design. Future boards may modify the philosophy as their experiences and circumstances suggest is prudent.

The major sections of the philosophy are:

1. Mission
2. Risk Management
3. Diversification
4. Market Efficiency

5. Hi-Alpha Managers
6. Organizational Infrastructure and Communications
7. Performance Monitoring and Time Horizon

1. MISSION

a) The Board's primary goals in managing the Fund are:

   i) To ensure that sufficient funds are available to pay vested benefits and maintain supplemental benefits;
   ii) To comply with all applicable fiduciary standards; and,
   iii) To create value added, where feasible, that will help reduce the costs of the plan, increase benefits, or both.

2. RISK MANAGEMENT

a) The Board believes that prudent management of risk is a central element of the investment function.

b) Though there are numerous risks involved in the management of a pension investment program, ACERA believes that the following warrant particular attention:

   i) ***Funding-related Risk*** - The risk that the funds available in the Plan will be insufficient to pay the promised benefits, both vested and supplemental; or that contribution volatility will be unacceptably high. The primary methods for managing funding risk include regularly conducting integrated asset/liability studies, and establishing appropriate and prudent investment and funding policies.

0.1 In managing the relationship between assets and liabilities, the approved asset allocation of the Fund should provide a minimum of a 90% level of certainty of meeting the projected liabilities of the Plan over a 20 year time period, as determined by the actuary.

ii) ***Benchmark related Risk*** – The risk that the investment benchmarks adopted by the Fund are inappropriate, or that the aggregate of the individual manager benchmarks within an asset class do not adequately reflect the benchmark for the asset class as a whole. The latter risk is a specific risk generally referred to as *benchmark misfit risk (i.e. style risk)*. Inappropriate benchmarks or excessive benchmark misfit risk could result in investment performance different than expected and could adversely impact decisions concerning the hiring or firing of investment managers.

0.1 The primary methods for effectively managing benchmark-related risk are:
   (a) regular review of the Fund's benchmarks; and
   (b) regular measurement and monitoring of misfit risk using proper methodologies.

iii) ***Manager Risk*** - The risk of aberrant performance on the part of individual investment managers, and the related active management risk for asset classes as a whole.

0.1 The primary methods for mitigating manager risk are:
   (a) Prudent processes for selecting and monitoring investment managers;
   (b) Competent internal investment staff;
   (c) Effective investment consulting support; and,
   (d) Clear communication to investment managers of ACERA's objectives, expectations, and investment time horizons.

0.2 The primary method for mitigating active management risk for asset classes include:
   (a) Establishment of appropriate asset class benchmarks;
   (b) Careful monitoring of asset class performance relative to the benchmarks; and

(c) Prudent use of passive management.

iv) ***Fortitude Risk*** - The risk that the board or staff will fail to exercise the patience, judgment, or fortitude required to support long-term policies and strategies for the investment and funding program.

0.1 The keys to managing fortitude risk are believed to include:

(a) Effective orientation and education with respect to institutional investing and actuarial science; and,

(b) A commitment to continually refining, confirming and communicating the investment philosophy and funding policy of the Association.

3. DIVERSIFICATION

a) ACERA acknowledges the basic tenets of modern portfolio theory, which suggest that diversification, or combining assets that are not perfectly correlated with each other, will reduce the long-term volatility of the overall portfolio.

b) It is generally desirable however to avoid overly complex asset structures, provided the allocation selected can reasonably be expected to meet the objectives of the Plan. ACERA believes that the benefits of diversification must be weighed against the costs involved, which may include fees, liquidity, complexity, communication, internal staff resources and expertise and trustee knowledge and effort.

c) The following asset classes are appropriate candidates for inclusion in its portfolio:

i) Domestic equity

ii) International equity (including emerging markets)

iii) Fixed income, including high yield fixed income and international fixed income

iv) Real estate

d) ACERA does not consider alternative investments to be an appropriate candidate for inclusion in its portfolio due to the substantial direct and indirect costs associated with it.

Implications

- A systematic methodology for re-balancing the investment portfolio is required to ensure proper implementation and adequate risk control concerning ACERA's asset allocation.
- Adding or deleting asset classes or investment managers should be considered in light of the impact such decisions are likely to have on the general complexity and cost structure of the portfolio, as well as ACERA's ability to prudently achieve its investment and funding goals over the long run.

4. Market Efficiency

Except for specified high alpha assignments:

a) ACERA does not believe in the viability of active management strategies that rely on market timing.

b) ACERA does not believe in the viability of management strategies that call for over weighting or under weighting styles or sectors within an asset class; i.e. benchmark misfit risk will not generate long-term alpha. Accordingly, ACERA generally believes that it should maintain exposures within an asset class (such as style or capitalization weightings) that are consistent with the broad benchmark for the asset class as a whole.

c) ACERA does believe that market efficiency varies among asset classes, creating opportunities for successful active management strategies based on securities selection.

d) Asset classes that can be demonstrated to be efficient should be managed passively in order to reduce active management risk and lower the costs of managing the portfolio.

e) For inefficient asset classes, ACERA believes that it has the ability and a duty to prudently exploit such inefficiencies through active securities selection strategies.

Implications

- ACERA should be conscious of any subtle forms of market timing that may arise in the course of managing the fund, or that may be implicit in investment strategies presented to ACERA for inclusion in the investment program.

- ACERA must determine appropriate methodologies for determining whether an asset class is efficient or presents appropriate opportunities, thus providing insight to the Board on the use of particular strategies.

5. HIGH ALPHA MANAGERS

a) ACERA believes that the portfolio characteristics utilized to control risk in the broad portfolio, such as market capitalization, sector exposure, use of derivatives, leverage limitations, property type or deal structure may be modified for specific managers who control a limited portion of the portfolio and have demonstrated a proven capacity to consistently add value net of fees. Such strategies, which ACERA refers to as Hi-Alpha, may include the following elements:

    i) The bulk of the asset class is passively managed or risk controlled; and,
    ii) A small number of active managers are retained who employ somewhat more aggressive investment strategies, such as concentrated portfolios, leveraged purchases, developments, high-yield debt, etc.

b) The primary benefits of a Hi-Alpha approach are believed to include:
   i) Reduction in active management risk;
   ii) Lower average investment fees; and
   iii) Concentration on opportunities where the likelihood of adding value is greatest.

c) The market efficiency and opportunities in asset classes may change over extended periods of time; therefore ACERA believes that its portfolio management strategies should adapt over time to reflect the changing nature of capital markets.

6. Organizational Infrastructure and Communications

a) ACERA believes that in order for the investment program to achieve its goals, ACERA must invest the necessary resources to build and maintain an appropriate organizational infrastructure, key elements of which include:

   i) A competent, internal investment staff comprised of a sufficient number of investment professionals possessing appropriate leadership, technical and administrative skills.

      0.1 In attracting a competent staff, ACERA recognizes that it competes with the private sector. It must therefore continually strive to create a total work environment that is challenging, rewarding, and competitive.

   ii) A strong relationship with outside general investment consultant(s) who are able to provide ACERA with the following:

0.1 A high degree of investment expertise;
0.2 Innovative and proactive advise and counsel;
0.3 Strong research support; and
0.4 Strong reporting capabilities,

iii) A broad-based information gathering and reporting system to present well- researched, relevant and timely data in a manner that is easily understood, and that supports rigorous and consistent monitoring of critical investment activities.

iv) An open channel of communication between the Board, management, and the Association's external investment professionals.

b) By providing the Board with timely, accurate, and thorough information, the organizational infrastructure will give the Board the high level of comfort it needs to set policy, make investment decisions, oversee the performance of the investment program, and maintain the fortitude necessary to support its investment philosophy, policies and strategies.

Implications

- ACERA must determine what constitutes an appropriate internal investment staff structure, given the nature of the current investment program.

- ACERA must over time take concrete steps towards creating a work environment that will allow the Association to attract and retain needed staff.

- ACERA must recognize that developing the organizational infrastructure it needs – staffing, consulting support, information systems, and communication channels – cannot be achieved overnight, but rather will require an ongoing commitment of time and resources.

7. Performance Monitoring & Time Horizon

a) ACERA holds the following basic beliefs concerning performance monitoring practices and methodologies:

i) The various investment policies of the Fund, in the aggregate, are the most important determinants of investment success; compliance with investment policies should therefore be monitored rigorously;

ii) The performance of the total portfolio, individual asset classes, and investment managers should be compared to appropriate, predetermined benchmarks;

iii) Peer comparisons are an additional valid tool in assessing individual manager performance (supplementing the use of benchmarks), given that ACERA aims to select superior managers within particular investment styles or mandates. Peer comparisons, or performance rankings, are also valid tools for measuring the performance of asset class portfolios.

iv) Peer group comparisons are not an appropriate means of assessing the performance of the total fund, given that sponsors have different objectives and risk tolerance levels, and therefore may have different asset allocation policies.

v) Benchmark misfit risk, or the risk that the aggregate of individual investment manager benchmarks in an asset class do not adequately reflect the benchmark for the asset class as a whole, should be explicitly measured on a regular basis.

vi) Investment managers are generally hired to fulfill a specific role in a portfolio. Accordingly, ACERA believes it is important that ACERA monitor the extent to which managers comply with their stated style and mandates.

b) ACERA believes that successful funding and investment decisions require a long-term perspective on the part of the Board and management:

i) It is the intention of the Retirement Board that commitments to asset classes and investment strategies should involve long time horizons that may include more than one business cycle (3-5 years each). Relatively illiquid asset classes may require even longer time horizons.

ii) The Board acknowledges that commitments to individual investment managers also require a long time horizon of at least one business cycle (3-5 years).

iii) ACERA believes that proper reporting and monitoring systems; and clear communication among consultants, management, investment managers and the board will enable the Board to maintain the necessary long term perspective on all investment decisions.

Implications

- Assessing the investment performance relative to appropriate, pre-determined, benchmarks is as applicable to the total portfolio and to individual asset classes as it is for individual investment managers, and therefore warrants a commensurate share of the Board's time and attention.

- The Board will spend relatively little time assessing the performance of the Fund relative to that of comparable pension funds.

- ACERA will need to either develop in-house capabilities to regularly measure benchmark-related risk, or it will need to purchase such capabilities from external investment consultants.

- ACERA will monitor all investment managers to ensure they are complying with their stated investment style, regardless of whether they are performing well or poorly. Strongly performing managers who are found to not be following their stated styles will be carefully scrutinized and may be subject to disciplinary action.

- ACERA will monitor all investment providers to ensure compliance with the Board's Investment Policies.

SCHEDULE VII

TABLE OF AMENDMENT DATES

AMENDING RESOLUTIONS

Jun	27,	1985
Oct.	10,	1985
Jan.	9,	1986
Jan.	16,	1986
Mar.	13,	1986
May	22,	1986
Sep.	11,	1986
Oct.	9,	1986
Nov.	20,	1986
May	14,	1987
Aug.	13,	1987
Oct.	8,	1987
Apr.	21,	1988
July	28,	1988
Jan.	29,	1989(4)
Apr.	13,	1989(5)
May	18,	1989
July	13,	1989
Aug.	10,	1989
Nov.	16,	1989(2)
July	11,	1991
June	11,	1992
June	10,	1993
July	8,	1993
Nov.	18,	1993
May	14,	1994
Aug.	18,	1994
Nov.	20,	1994
Feb.	16,	1995
May	18,	1995
Jan.	16,	1997
Aug.	20,	1998
May	20,	1999
Jan.	31,	2000
Apr.	19,	2001
Jul.	18,	2002

Alameda County Employees'
Retirement Association

ACERA

INVESTMENT GUIDELINES, POLICIES AND PROCEDURES

AMENDED February 21, 2003

ACERA
INVESTMENT GUIDELINES, POLICIES AND PROCEDURES 2003

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[1] Prepared for ACERA by Cortex Consulting; adopted by the Board of Retirement on March 8, 2000 and revised May 2001.

ACERA
INVESTMENT GUIDELINES, POLICIES AND PROCEDURES

SECTION I: MISSION AND PURPOSE

The Alameda County Employees' Retirement Association (ACERA) exists for the purposes of providing accurate, timely benefits to its members and their beneficiaries and defraying reasonable expenses of administration.

The Board of Retirement (the Board), having exclusive authority and exclusive fiduciary responsibility for the investment and administration of the Trust Fund (the Fund), hereby establishes the following General Investment Policies and Guidelines (the Policy) for the investment of ACERA's assets. The Board reserves the right to amend, supplement or rescind this Policy at any time.

The Board of Retirement is directed by law and given discretion to prudently invest the plan assets. The purpose of this statement of policy is to assist ACERA in effectively supervising said investments and to encourage effective communication between ACERA and its managers and consultants.

ACERA's investment goal is to operate at a level of performance in the upper quartile of comparable pension funds on a risk-adjusted basis and to be as fully funded as possible so that ACERA's benefit costs do not become a burden upon future generations of members and taxpayers.

SECTION II: CONSTITUTIONAL REQUIREMENTS

Article 16 §17 of the California State Constitution provides in pertinent part as follows:

"Notwithstanding any other provisions of law or this Constitution to the contrary, the retirement board of a public pension or retirement system shall have plenary authority and fiduciary responsibility for investment of money and administration of the system, subject to the following:

a. The retirement board of a public pension or retirement system shall have the sole and exclusive fiduciary responsibility over the assets of the public pension or retirement system. The retirement board shall also have sole and exclusive responsibility to administer the system in a manner that will assure prompt delivery of benefits and related services to the participants and their beneficiaries. The assets of a public pension or retirement system are trust funds and shall be held for the exclusive purposes of providing benefits to participants in the pension or retirement system and their beneficiaries and defraying reasonable expenses of administering the system.

b. The members of the retirement board of a public pension or retirement system shall discharge their duties with respect to the system solely in the interest of, and for the exclusive purposes of providing benefits to participants and their beneficiaries, minimizing employer contributions thereto, and defraying reasonable expenses of administering the system. A retirement board's duty to its participants and their beneficiaries shall take precedence over any other duty.

c. The members of the retirement board of a public pension or retirement system shall discharge their duties with respect to the system with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with these matters would use in the conduct of an enterprise of a like character and with like aims.

d. The members of the retirement board of a public pension or retirement system shall diversify the investments of the system so as to minimize the risk of loss and to maximize the rate of return, unless under the circumstances it is clearly not prudent to do so.

e. The retirement board of a public pension or retirement system, consistent with the exclusive fiduciary responsibilities vested in it, shall have the sole and exclusive power to provide for actuarial services in order to assure the competency of the assets of the public pension or retirement system."

SECTION III: ELIGIBLE ASSET CATEGORIES

The Fund shall hold assets in categories established by the Board. Any asset category may be held in direct form, in pooled form or in both. Asset categories managed by one or more "Qualified Investment Managers" {Manager(s)} are called "Managed Accounts". Asset categories under the supervision of the County Treasurer are called the Treasurer's Accounts. Eligible asset categories are listed and defined below.

A. **CASH** shall consist of short term (12 months or less) interest bearing investments of high quality such as U.S. Treasury issues, insured certificates of deposit of U.S. banks (fixed and/or variable), commercial paper rated A-1, P-1 or both, or other instruments of equal or better quality, and includes money market funds available through the Custodian Bank (Custodian).

B. **U.S. EQUITY** shall consist of common stocks and other securities which are convertible into common stocks, and ADRs (American Depository Receipts) , as well as cash (per "A" above) and fixed income (per "D" below) when used as temporary substitutes for common stocks.

C. **INTERNATIONAL EQUITY** shall consist of common stocks and other securities convertible into common stocks of companies domiciled outside of the U.S., and GDR's (Global Depository Receipts), as well as cash equivalents and fixed income, domestic or international, which are being used as temporary substitutes for common stock.

D. **FIXED INCOME** shall consist of investments in U.S. taxable bonds, debentures, notes and other evidences of debt. Fixed income may include non-dollar denominated bonds issued by corporations or governments domiciled outside of the United States of America as well as Brady Bonds. Other eligible investments include cash equivalents per "A" above and convertible bonds and preferred stock.

E. **MEMBER MORTGAGES** (closed program) shall consist of first mortgages, secured by the primary residences of the borrowers, underwritten to GNMA/FNMA standards by a qualified third party expert underwriter retained by the Board for that purpose.

F. **REAL ESTATE** shall consist of investments in equity real estate through the use of commingled or direct investments. For more information about real estate investments, refer to ACERA's Real Estate policy which is maintained as a separate document.

SECTION IV: INVESTMENT PHILOSOPHY

The following is a summary of ACERA's Investment Philosophy. For a complete statement, please refer to Schedule VI, "ACERA Investment Philosophy".

The Board believes that its investment policies, in aggregate, are the most important determinants of its investment success. Compliance with investment policies should therefore be monitored rigorously. The Board also believes that performance of the total portfolio, individual asset classes, and Managers should be monitored and compared to appropriate, predetermined benchmarks.

The Board believes that prudent management of risk is a central element of the investment function and that diversification among asset classes will reduce risk and enhance returns of the overall investment portfolio in the long term.

The Board believes that market efficiency and opportunities vary among asset classes and may change over extended periods of time; therefore ACERA believes that its portfolio management strategies should adapt over time to reflect the changing nature of capital markets.

The Board's primary goals in managing the Fund are:

1. To ensure that sufficient funds are available to pay vested benefits and maintain supplemental benefits;
2. To comply with all applicable fiduciary standards; and
3. To add marginal value that will help reduce the costs of the plan and/or to increase benefits for the beneficiaries.

The Board believes that in order to achieve its goals, ACERA must invest the necessary resources to build and maintain an appropriate organizational infrastructure.

SECTION V: INVESTMENT STRATEGY

A. **U.S. EQUITY** will be structured to capture exposure to the broad U.S. equity market as represented by the Russell 3000 Index. Passively managed (index) portfolios will be used in markets that are reasonably efficient. These portfolios are intended to provide broadly diversified market exposure with controlled (market) risk and minimal cost.

Actively managed portfolios will be used in less efficient markets when the Board determines that a Manager possesses special skills or abilities that enable that Manager to capture excess returns relative to the market, adjusted for risk and fees; or to exploit specialty markets that provide enhanced return with acceptable risk.

A great part of the Russell 3000, on a market value basis, is comprised of large-cap stocks, which the Board believes are efficiently priced most of the time. Therefore, the Board has adopted a policy of obtaining overall exposure to this segment of the market via passively managed indexed products. Some active Managers have been employed to enhance overall portfolio return in the large- and/or mid-cap sectors on a risk- and fee-adjusted basis. These Managers manage ACERA's "Hi-Alpha" program.

The remainder of the Russell 3000 index is comprised of small to mid-cap companies. Some opportunities for active management enhancement exist in these securities due to market inefficiencies. ACERA will attempt to capture these opportunities through a mix of Managers who have the special skills required to identify smaller companies that may be undervalued or possess substantial growth potential.

The U.S. equity portion of the portfolio shall be allocated among the various styles and Managers as indicated in Schedules I and IA.

B. **INTERNATIONAL EQUITY** represents an opportunity to diversify risk and capture enhanced returns within markets generally less efficient than the U.S. domestic equity market. 100% of the international equity portion of the Fund will be invested in actively managed portfolios.

C. **FIXED INCOME** represents a means of reducing overall portfolio risk and capturing incremental returns. Inefficiencies in the pricing and trading of fixed income securities create opportunities to add value through active management. 100% of the fixed income portion of the portfolio will be invested in actively managed portfolios.

D. **REAL ESTATE** will be used as a means for diversifying the portfolio and capturing additional returns due to the low correlation between returns on real estate and financial assets. Due to the illiquid nature of real estate assets, distinctions between active and passive management are not applicable. For more information regarding real estate investments, refer to ACERA's Real Estate policy which is maintained as a separate document.

SECTION VI: ASSET ALLOCATION AND REBALANCING

Asset allocation targets, a function of the returns and risks from various asset classes and the nature of the plan's liabilities, are set forth in Schedule I. A goal of asset allocation is balancing asset growth versus liability growth considering time horizons, liabilities and risk tolerance.

Rebalancing is the risk control process of returning an allocation back to the desired target level after having drifted away from its targeted position. Acceptable ranges around the asset allocation targets are set forth in Schedule IA. The objective of rebalancing is to enhance the risk-adjusted performance of the asset allocation structure.

ACERA Staff ("Staff") shall be responsible for maintaining the relative weights of asset classes and allocations within the acceptable rebalancing ranges indicated in Schedule IA. Should an asset class or allocation fall outside its target range, Staff shall rebalance the asset class or allocation back to the target weights as specified in the asset allocation structure in Schedule I.

Staff shall:

1. Monitor the portfolio;
2. Determine whether or not any asset category is out of balance with its target asset allocation in excess of the specified tolerance range;
3. Determine whether or not any Manager within each asset category is out of balance with their target

allocation in the excess of the specified tolerance range;

4. And, if so, either:

(a) instruct the relevant Managers to redirect cash income (interest coupon and dividends) in concert with an evaluation of pending commitments and other cash flows (employer and employee contributions), in order to bring the allocation(s) back to the adopted strategic target; or

(b) instruct the relevant Managers to liquidate or acquire the appropriate dollar value of securities to reach the target and reallocate the cash thus generated or required to the other category(s) or Manager(s) necessary.

Staff shall report to the Board on a regular basis the status of the Fund with respect to how categories are tracking relative to their allowable ranges, as well as any actions taken to rebalance the portfolio.

SECTION VII: ASSET CATEGORIES OBJECTIVES

The general objective of the Board is to preserve capital and earn a return from appreciation and income, as described herein.

The minimum return objective for the Fund shall be the current actuarial interest assumption rate plus 25 basis points per year over a market cycle. Returns shall be calculated net of fees.

The minimum return objective for the Fund over a market cycle (up to five years) shall also be 400 basis points (4%) per year over the national Consumer Price Index, published by the U.S. Department of Commerce.

The objectives of each asset category are:

A. CASH

1. A rate of return in excess of 90-Day U.S. Treasury bills.
2. A rate of return within the upper one half of a universe of like short-term funds.

B. U.S. EQUITY

1. A rate of return in excess of the U.S. equity market as measured by the Russell 3000 Index after adjustment for risk and fees.
2. A rate of return within the upper 33rd percentile of the Wilshire Co-op or similar database of the performance of diversified equity portfolios.

C. INTERNATIONAL EQUITY

1. A rate of return in excess of the Morgan Stanley Capital International All Country World Index Ex-U.S. Free (MSCI ACWI).
2. A rate of return within the top quartile of the Wilshire Co-op or similar database of the performance of diversified international equity portfolios.

D. U.S. FIXED INCOME

1. A rate of return in excess of the Lehman Aggregate Bond Index published by Lehman Bros. Inc..
2. A rate of return within the top quartile of the Wilshire Co-op or similar database of the performance of diversified fixed income portfolios.

E. MEMBER MORTGAGE (closed program)

1. A rate of return that compares favorably with the Salomon Mortgage Index.

2. A delinquency rate of less than 2% of loans outstanding;

F. REAL ESTATE

Total Return - over rolling 5 year periods a minimum total real rate of return (net of management fees) of 6.0% using a "Time Weighted Market Value" calculation. The real return expectation is after inflation (U.S.A. CPI-Urban).

1. Income Return – Income, which is defined as cash distributed to the Association, should comprise at least 2/3 of the total return over rolling five periods.

2. Minimum Going-in Yields – On individual separate account assets, the Manager's five year projection (net of fees) will exceed the consultant's five year projection for ten year treasuries by no less than 150 basis points.

In addition, objectives that reflect the particular investment strategy or style used by individual Managers shall be outlined in an attachment to the Manager's contract.

SECTION VIII: ALLOCATION OF CASH FLOW

Cash flow not needed for benefit payments or administrative expenses shall be allocated to Managed Accounts in a ratio that best funds the overall asset allocation as shown in Schedules I and IA.

If cash flow is insufficient for the payment of benefits or to cover administrative expenses, then Managed Accounts shall be debited in a ratio that best satisfies the target allocation shown in Schedules I and IA. Such debits, if necessary, will be carried out as needed, and with timely notice to Managers to facilitate effective funds transitions and performance measurement.

For planned investments which may not need to be funded immediately, a reserve may be budgeted and invested in appropriate index funds until such moneys are required. Alternatively, Managed Accounts within "overfunded" asset classes may be called upon to provide the required moneys. Funds intended for real estate investments but not yet invested shall be divided equally and held in the equity and fixed income index funds until called by the real estate Manager.

SECTION IX: PROHIBITED INVESTMENTS

Managers shall exercise prudent expert standards in defining prohibited investments. For example, prohibited investments include, but are not limited to, securities issued by the County of Alameda or any agency thereof.

SECTION X: DIRECTED BROKERAGE

ACERA does not engage in either directed commission arrangements or "soft dollar" transactions.

SECTION XI: DERIVATIVE INSTRUMENT USAGE POLICY

Exposure to risk by use of derivative instruments must be consistent with ACERA's overall investment guidelines. Derivatives shall not be used to establish a leveraged position (i.e. offsetting Cash positions must be maintained against all delayed settlement transactions).

SECTION XII: SELECTION OF INVESTMENT MANAGERS

The Investment Committee shall direct Staff and/or a consultant to initiate searches for Managers. Staff and/or the consultant shall screen qualified candidates and present a list of finalists to the Investment Committee for its approval. Upon approval of the list, the finalists shall be interviewed by Staff and the consultant (if applicable) in a publicly noticed meeting at which no less than three (3) Investment Committee members shall be present. Staff and the consultant (if applicable) shall evaluate the interviews, rank the finalists, and make a recommendation to the Investment Committee to hire one or more firms attaining the highest rankings. It is possible that none of the firms will be recommended for hire.

These procedures are developed for the convenience and benefit of ACERA, and shall not bind ACERA or invalidate the selection of a Manager if different processes are used subsequent to the promulgation of this Policy.

SECTION XIII: AUTHORITY OF INVESTMENT MANAGERS

Subject to the laws of the United States and the State of California, and to the terms and conditions of this Policy, Managers shall have full discretion to direct the purchase, exchange, sale and reinvestment of the assets of the Managed Accounts. The Board expects that Managers will recommend changes to this Policy when any part of this Policy appears to be at variance with overall market and economic conditions.

Managers shall place orders to buy and sell securities and, by notice to the Custodian, shall cause the Custodian to deliver and receive securities on behalf of the Fund. Managers shall, upon Board inquiry, report placement of ACERA brokerage such that the Board shall be assured commissions were placed for the sole and exclusive benefit of the Fund.

Separate account Managers shall not vote proxies. Proxies shall be voted by ACERA according to Board-established policies and procedure.

Securities lending shall be performed by the Custodian Bank under the oversight of the Board.

SECTION XIV: INVESTMENT GUIDELINES FOR THE MANAGED ACCOUNTS

Individual Manager discretion shall be governed by the guidelines set out in the Investment Contract of each Manager.

A. GENERAL

1. All investments shall comply with all applicable laws of the United States and the State of California governing the investment of pension trusts.

2. All securities transactions shall be executed by reputable broker/dealers, banks, or the Custodian, and shall be on a best-price and best-execution basis,

and shall be reported to ACERA as is called for elsewhere in this Policy.

3. All Managers shall refrain from investing in a tobacco producer investment opportunity when, in their expert opinion, an alternative non-tobacco producer investment opportunity is available that will satisfy the same ACERA portfolio guidelines, instructions and objectives for risk, return and diversification.

B. EQUITY

Managers have full discretion to invest solely in readily marketable and diversified equity securities as defined above subject to the following:

1. For Managed Accounts, no more than 10% of the value (at time of investment) of the account shall be invested in the securities of a single issuer.

2. ACERA shall not hold more than 10% of the equity securities of any issuer.

3. Equity securities shall possess value and quality corroborated by generally accepted techniques and standards of fundamental securities analysis.

4. Assets in a Managed Account not invested in equity securities shall be kept with interest in appropriate money market instruments, including any money market fund available through the Custodian.

5. A Managed Account shall be subject to ACERA's policy on derivatives.

6. All Managers shall endeavor to be fully invested in stocks at all times unless they have received specific authorization to the contrary from the Board. Cash holdings, as defined in this Policy, shall generally not exceed 5% of the portfolio on a market value basis.

C. FIXED INCOME

Managers have full discretion to invest solely in readily marketable and diversified securities including, but not limited to:

1. Obligations of the U.S. Treasury.

2. Obligations guaranteed by an agency of the United States.

3. Insured certificates of deposit and banker's acceptances of credit worthy banks.

4. Corporate and other evidences of debt. At least 80% of this debt must be rated by Moody's Investor's Services or by Standard & Poors.

5. Commercial paper and banker's acceptances of issuers rated P-1 by Moody's Investor's Service.

6. Or A-1 by Standard & Poors Corporation.

7. Excepting direct obligations of the U.S. Government, and those explicitly guaranteed by the U.S. Government, no account shall hold more than 5%, at cost, of the obligations of any single issuer.

8. Fixed income derivative investments shall be in accordance with ACERA's derivative policy.

SECTION XV: SEPARATE ACCOUNT MANAGER SPECIFICATIONS

A. Managers must be registered as investment advisors under the Investment Advisor's Act of 1940, a bank (as defined in that act) or an insurance company qualified to perform investment management services under state law in more than one state, including California. In addition, by accepting appointment as an Manager for ACERA, Managers shall acknowledge that they are "Plan Fiduciaries" and "Qualified Investment Managers" as defined by the Employees' Retirement Income Security Act (ERISA) of 1974, see or reference United States Code Title 29 Section 1001 et. seq..

B. Managers shall maintain fiduciary insurance in the amount of 10% of the total assets managed in the ACERA account or $25 million, whichever is higher, unless the contract specifies otherwise.

C. Managers shall promptly notify ACERA of changes that occur in any of the following:

1. The investment strategy used in managing the subject product.
2. The personnel involved in managing ACERA's account.
3. The ownership, key personnel, or organizational structure of the Manager's company.
4. The Manager company's financial condition.
5. The number of clients invested in the subject product.
6. The market value of the total assets managed in the subject product.

D. Managers shall promptly notify ACERA if they are subject to censure or disciplinary action by a regulatory agency.

E. On a monthly basis, Managers shall report on the activities of the portfolios managed on behalf of ACERA. Monthly reports shall include descriptions of holdings along with cost and market values; summaries of purchases and sales; description of major changes to the portfolio; and a declaration by the Manager that its investment activities comply with the provisions of this Policy.

On a monthly basis, active Managers shall certify in writing that the portfolio market values, transactions and performance data are reconciled with ACERA's Custodian.

On a monthly basis, Managers shall furnish a report detailing the entities to whom services were paid for with soft dollars; the total amount of soft dollars used for such services; and descriptions of the services purchased with those soft dollars. Consultants and the Custodian are also required to report on their soft dollar usage, if applicable.

On a quarterly basis, Managers shall invoice ACERA for payment of fees for services rendered. The fee shall be calculated using the rate established in the fee schedule of the Manager's contract with ACERA and using the market values determined by ACERA's Custodian.

F. Managers shall provide ACERA with the most recent copy of Form ADV, Part II upon their receipt of the same, on an ongoing basis.

G. Managers shall not make contributions, provide gifts, reimbursements of expenses or provide personal benefits exceeding $250 in the aggregate within any 12-month period to any Trustee, fiduciary, employee or consultant of ACERA. Donations of educational conferences and similar events and benefits, including travel, meals and accommodations will be made to ACERA and not directed to individuals. The Board will determine whether to accept any donations and will be solely responsible for selection of the Trustee, staff member, or other individual, who will attend or otherwise participate on behalf of ACERA.

SECTION XVI: MANAGER MONITORING POLICY

The ACERA Board has contracted with a number of external Managers to invest ACERA assets in the public equity markets. As part of the Board's fiduciary duties to prudently select, monitor and supervise these Managers, the Board has adopted this Policy. The intent of this Policy is to notify Managers of the standards by which they will be judged and to establish a structure which the Investment Committee and the Board can use to monitor the performance of the Managers.

Managers will be monitored to:

1. Evaluate how well they achieve their investment objectives.
2. Ensure that they adhere to their established investment approach/style and do not attempt to index returns to preserve stellar performance or take extraordinary risk to overcome poor performance.
3. Identify issues or trends that have the potential to result in losses to the Fund.
4. Alert the Board when Managers are not performing to expectations so that appropriate remedial action can be taken.

Managers will be evaluated on the basis of the following: performance, style integrity, organizational stability, compliance, and client service described in greater detail below.

A. PERFORMANCE

On a monthly basis Staff will monitor Manager holdings, activity and performance.

On a quarterly basis Staff and/or a consultant will furnish the Investment Committee and/or Board with an in-depth evaluation of each Manager which will include a comparison of the Manager to its contract benchmark and a peer universe of Managers using a similar investment style. This report shall include an analysis of the sources of Managers' returns (stock selection, industry selection, asset allocation, etc.) and shall identify which decisions enhanced or diminished performance.

On a quarterly basis, trading costs will be evaluated in terms of commissions paid and execution of trades. Staff and/or a consultant shall furnish a report to the Investment Committee and/or Board regarding trading costs on an annual basis.

B. STYLE INTEGRITY

Each Manager will be analyzed at least annually to ensure that the Manager is continuing to invest the portfolio in the style for which they were originally hired. Style integrity is essential to maintain the Board's asset allocation policy. Any significant deviation in style will result in the overall portfolio having a different characteristic, in some measure, from the broad market which is represented by the Russell 3000 index. Significant variations in the portfolio characteristics from the style anticipated in the management contract may indicate a change in its investment style.

This review also provides the Investment Committee and/or Board an opportunity to evaluate the Manager's continuing "fit" with the goals of the overall fund. By monitoring Manager style the Investment Committee and/or Board can assure that its Manager mix takes advantage of opportunities to increase diversification through lower correlation of returns among individual Managers.

C. ORGANIZATIONAL STABILITY

Managers' organizations will be monitored to ensure continuity of the intellectual and philosophical processes that went into developing the particular investment approach contracted for by ACERA. In addition, Managers will be monitored for business risk, quality of staff**,** departures of key investment personnel, change in ownership or acquisition, and potential conflicts of interest.

It is ACERA's intent that its portfolio comprises no more than 25% of the Manager's total assets under management. Therefore ACERA will monitor the Managers' assets, firm-wide, as well as in the subject product.

D. COMPLIANCE

Managers will be monitored to ensure they are adhering to Federal and state laws regarding securities and the management of investment portfolios, trading, and pension investments; ethical practices of the investment professions; the Contract governing their relationship with ACERA; and the policies and guidelines set forth in this Policy statement and any other written directives issued by ACERA.

Each ACERA contract will specify which investment vehicles a Manager is authorized to use, which markets the Manager is authorized to transact business in and any limitations within a market (small or large capitalization, value or growth orientation). The assets in each Manager's portfolio shall be reviewed monthly to ensure compliance with contract guidelines.

All required documents and reports, set forth in Schedule V, must be submitted in a timely manner and in the format specified by ACERA.

Managers must provide prior notification and justification for failure to comply with rules, regulations, contract provisions, deadlines or other directives. Managers must provide a time frame for curing any deficiencies. Staff shall evaluate each incident on a case-by-case basis and determine whether an exception may be granted.

E. CLIENT SERVICE

Managers are required to comply with routine portfolio investment guidelines and reporting deadlines and are also expected to cooperate with special requests for information. ACERA will establish reasonable time frames for all requests and reporting and will provide feedback to all external equity Managers regarding the perceived quality of their client service.

ACERA Staff will endeavor to meet with each Manager at least twice a year by telephone or in person to review performance and other issues.

SECTION XVII:

CONTRACT REVIEW PROCESS

If during the course of regular monitoring, ACERA determines that a Manager's performance, style, organizational stability, compliance, or client service has declined to unacceptable levels, ACERA may, at its discretion, subject the Manager to ACERA's Contract Review Process. As part of the Board's fiduciary duties to prudently select, monitor and supervise their Managers, the Board has approved this process. The purpose of this process is to ensure as little disruption as possible in the event that concerns or problems arise with respect to a Manager's performance. The Board does not confer any additional rights or protections to its Managers by the promulgation of this Policy and/or this process.

There are generally three stages of review: Watchlist, Probation, and Termination. (described below). ACERA reserves the right to terminate an investment management contract at any time, upon 30 days notice, for any reason, and without resort to this Contract Review Process.

The Contract Review Process may result in one or more of the following:

1. Placement on Watchlist or Probation status.
2. Movement from one stage of review to another, or removal from the Contract Review Process.
3. Reduction of assets under management.
4. Revision of investment contract guidelines for that Manager.
5. Re-negotiation of fees.
6. Termination of a Manager's contract.
7. Or any other deemed appropriate by the Board

Each situation is unique and action by the Board will vary depending on the type of Manager and the style/strategy involved. The following describes the Contract Review Process:

A. INITIAL REVIEW

Prior to a Manager being considered for Watchlist, Probation or Termination, ACERA may take the following steps :

1. Analysis

Staff will conduct in-depth analyses of the perceived deficiency to verify that a deficiency exists, form an initial assessment of the severity of the deficiency, and make an initial determination of possible causes.

2. Discussion with the Manager

Staff will contact the Manager to discuss the situation and the results of Staff's analysis.

3. Consultant Input

ACERA may seek the services of a consultant to provide additional assessment and advice regarding the situation, depending on the severity of the deficiency.

All phases of account compliance may be reviewed during this step, in addition to the specific issue that originated the Review Process.

B. FORMAL ACTION

After completing the Initial Review, Staff may recommend to the Investment Committee and/or Board that the Manager be either placed on Watchlist or Probation or, in certain cases, Terminated. The specific criteria for determining which level of Contract Review to recommend is outlined later in this Policy section and summarized in tabular form in Schedule II. The Committee and/or Board will approve or reject the recommendation.

Upon approval of a Watchlist or Probation recommendation:

1. Staff will notify the Manager of the Board's decision and will provide the Manager with a statement of concerns

which outlines the areas which need improvement.

2. The Manager will be asked to respond in writing with an explanation of the issues and a proposed action plan to resolve the issues.

3. Staff, a consultant and the Manager will collectively draft a Plan of Action. The plan will identify: the specific steps to be taken to correct the problem; the time frames for further review; and what additional monitoring may be required.

   At the end of the time period specified in the Plan of Action, the Manager will be evaluated and one of the following actions may be taken:

   (a) Removal from Contract Review: If the successfully resolves the issues/deficiencies and demonstrates continued success in all other areas of its relationship with ACERA.

   (b) Movement from Probation to Watchlist: If the Manager has satisfied all or most of the issues/deficiencies that caused it to be placed on Probation, yet Staff continues to have concerns about the Manager. If circumstances warrant, a Manager may also be moved from Watchlist to Probation at any time during the Contract Review Process.

   (c) Extension of Contract Review: A Manager may be given additional time to satisfy the conditions of its Action Plan if reasonable progress is being made. Extensions may also be granted if unfavorable market conditions or high costs make reallocation of assets inadvisable.

   (d) Termination: If the Manager has not satisfactorily resolved the issues/deficiencies, Staff may recommend termination as described below. Termination may be recommended at any time during the Contract Review Process if circumstances warrant.

WATCHLIST

Watchlisting indicates an increased level of concern, but does not indicate major deficiencies. The Watchlisting period is typically one year. Any of the following may result in a Watchlist recommendation:

A. UNDERPERFORMANCE

Please refer to Schedule II for specific Watchlist criteria for each Manager.

B. STYLE DEVIATION

Managers are expected to adhere to the style of investment management for which ACERA originally hired them. Changes in portfolio characteristics or style drift may lead to a Watchlist recommendation.

C. ORGANIZATIONAL CHANGE

NEW OWNERSHIP
Even relatively benign ownership changes, which impact personnel key to ACERA's portfolio management may be cause for a Watchlist recommendation.

TURNOVER
Significant turnover in top management, portfolio Managers, research or trading staff, or marketing personnel, which does not directly affect the team responsible for ACERA's account may warrant Watchlisting.

REORGANIZATION
Changes which signal management deterioration**,** departures of key investment personnel, change in ownership that increases risk to ACERA's investments, or hasty /uncontrolled growth in the firm with potential to disrupt the investment team hired for management of ACERA's account will mandate Watchlisting, without requiring prior approval of the Committee and/or Board.

ASSETS UNDER MANAGEMENT
If the market value of ACERA's portfolio rises above 25% of the Manager's total assets under management, Watchlist status may be recommended.

D. COMPLIANCE

CONTRACTS AND OTHER AGREEMENTS
Managers are expected to comply with the investment management contract, investment guidelines, or other directives. Non- or partial compliance may result in a Watchlist recommendation.

REPORTING
Staff will contact Managers to request past due reports. If the Manager's reports are consistently delinquent, the payment of fees may be delayed. If a Manager cannot comply with reporting deadlines, ACERA should be given prior notification. If warranted, a variance may be allowed. Managers are expected to resolve reporting problems immediately upon notification by ACERA. Repeated delinquency in reporting may result in a Watchlist recommendation.

E. CLIENT SERVICE

If a Manager is uncooperative and demonstrates a poor client service attitude, Watchlisting is appropriate. Managers are expected to resolve client service issues immediately upon notification by ACERA.

PROBATION

Probation indicates a level of serious deficiency and signals a need for closer contact with the firm. Probation necessitates a cautious, observant relationship with the Manager.

Managers may be placed on Probation with or without first being placed on Watchlist status. The Probation period is typically one year.

The following may result in Probation:

A. UNDERPERFORMANCE

Please refer to Schedule II for specific Probation criteria for each Manager.

B. STYLE DEVIATION

Probation may be recommended when a Manager's portfolio characteristics are significantly different from its style. In general, a Manager will be placed on Probation after four or more consecutive quarters of deviating from its style benchmark. In effect, if the Manager is no longer the same Manager that was retained for ACERA's account, Probation and perhaps even Termination is appropriate.

C. ORGANIZATIONAL CHANGE

Changes in ownership, organizational assignments**,** departures of key investment personnel, change in ownership that poses substantial risk to ACERA's investments, or turnover that have the potential to seriously disrupt or destroy the investment management team that was hired to manage the ACERA account may result in Probation or Termination. When key personnel, such as top management, portfolio Managers, research and trading staff are no longer available for use on the ACERA portfolio and do not appear to be replaced or replaceable, a Probation or Termination recommendation is appropriate. Managers may be placed on Probation without requiring prior approval of the Committee and/or Board.

D. COMPLIANCE

If a Manager does not comply with securities laws, industry regulations, standards of professional conduct or contractual provisions, a recommendation of Probation is appropriate. Certain circumstances may warrant Termination.

E. CLIENT SERVICE

Failure to correct any issues that previously resulted in the Watchlist recommendation may result in Probation. Managers will generally be given one quarter to resolve client service issues.

TERMINATION

Upon determining that the Manager has not made adequate improvement in the areas outlined in the Plan of Action, Staff may recommend to the Investment Committee and/or Board that the Manager be terminated. Prior to making the final decision to terminate the Manager, the Investment Committee may invite the Manager to make a presentation at the meeting in which the Termination recommendation is to be discussed. Staff will have analyzed the liquidity of the Manager's portfolio and will have a recommendation and plan for disposition of the assets.

Upon the Investment Committee's decision to terminate, Staff will notify the accounting division as well as the Board's legal counsel of the action. All outstanding issues between the Manager and ACERA's master Custodian, brokers, consultant, or other parties shall be resolved prior to closing out the contract. The Manager Termination checklist is attached as Schedule IV.

The Contract Review Process described in this Policy does not provide any additional rights or protections to Managers, beyond what is provided in the contract. ACERA reserves the right to terminate an investment management contract without resort to the Contract Review Process, at any time, upon 30 days notice, for any reason.

SCHEDULE I

ASSET ALLOCATION AND MANAGER STRUCTURE TARGETS

ASSET ALLOCATION TARGETS

Asset Class	**Target Allocation**
U.S. Equity	39
International Equity	22
Total Equity	61
Fixed Income	30
Real Estate	9

MANAGER STRUCTURES TARGETS

Managers		**Target Allocation**
U.S. Equity		
Large Cap Core Index	BoNY S&P 500	50
Large Cap Growth (Hi-Alpha)	TCW	17.5
Large Cap Value (Hi-Alpha)	PFR	17.5
Large Cap Enhanced Core (Hi-Alpha)	Salus	5
Small Cap Growth	Next Century Growth	5
Small Cap Value	Brandywine	5
Non-U.S. Equity		
Core Developed Markets	Capital Guardian	65
Core Developed Markets	Delaware	35
Fixed Income		
Aggressive Core Plus	Loomis Sayles Boston	29
Global Bond	Brandywine	16
Enhanced Index	Baird	49
Mortgage	AFL-CIO	6

SCHEDULE IA

ASSET ALLOCATION PORTFOLIO REBALANCING

The objective of rebalancing is to control risk and enhance the risk-adjusted return of the asset allocation strategy. For purposes of enhancing the risk-adjusted return of the asset allocation structure, the relative deviation of any liquid sub asset class away from its target weight (or liquidity-adjusted target weight) shall be no more than plus or minus 1.7 standard deviation factors of each allocation's expected volatility, relative to the other allocations in the asset mix. This standard deviation factor shall be used to define the range of allowable deviation from Policy target asset allocations. If any sub asset class reaches its allowable deviation from its target allocation, all sub asset classes will be evaluated.

The actual reallocation will be at the discretion of ACERA's staff (with oversight by the rebalancing consultant) after reviewing: the relative magnitude of deviation from target for all other sub asset classes; the available cash liquidity of sub asset classes that could be used to fund rebalancing; pending cash flows (employer and employee contributions, or proceeds from a terminated manager's portfolio); pending liquidity windows with commingled investment pools; pending investment commitments (real estate transactions and/or new funding commitments); and, pending interest coupon and dividend cash flows.

Asset allocation and rebalancing status reports, and any rebalancing activity taken toward attaining the objective of the rebalancing program will be reported to the Board of Trustees on a monthly basis.

Significant modifications to the asset allocation strategy shall be cause to review the appropriateness of maintaining this rebalancing parameter or revising it to a parameter more suitable to the revised asset allocation structure.

SCHEDULE II

Watchlist/Probation Criteria for Performance

(Footnote: If Plan history with Manager is less than 5 years, use rolling 3 year period)

Watchlist Criteria	Probation Criteria
US Equity • Large Cap Core Index: negative tracking error exceeds 5 bps on an annualized basis in any 1 year period. • Large Cap Growth: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters. • Large Cap Value: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters. • Small Cap Growth: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters. • Small Cap Value: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters. • Large Cap Enhanced Core: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters.	**US Equity** • Large Cap Core Indexed: negative tracking error exceeds 5 bps in any 1 year period; or negative tracking error exceeds 10 bps for 2 quarters. • Large Cap Growth: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters. • Large Cap Value: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters. • Small Cap Growth: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters. • Small Cap Value: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters. • Large Cap Enhanced Core: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters.

International Equity • Concentrated Core: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters.	**International Equity** • Concentrated Core: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters.
Fixed Income • Aggressive Core Plus: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters. • Global Bond: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters. • Enhanced Index: cumulative 1 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters. • Mortgage: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters.	**Fixed Income** • Aggressive Core Plus: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters. • Global Bond: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters. • Enhanced Index: cumulative 1 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters. • Mortgage: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters.

SCHEDULE III

BENCHMARKS FOR ACERA ASSET CLASSES, EQUITY AND FIXED INCOME MANAGERS

BENCHMARKS FOR ASSET CLASSES

Asset Class	**Benchmark Index**
U.S. Equity	Russell 3000
International Equity	MSCI ACWI-Ex. U.S.
Total Equity	N/A
Fixed Income	Lehman Aggregate U.S./Salomon World Government Bond Ex U.S. /Lehman High Yield in the ratio of 75/15/10
Real Estate	NCREIF

BENCHMARKS FOR EQUITY AND FIXED INCOME MANAGERS
(Please refer to individual Manager's contract for expected annual premium)

Manager	**Benchmarks**
U.S. Equity	
BoNY S&P 500	S&P 500
TCW	Russell 1000 Growth
PFR	Russell 1000 Value
Salus	S&P 500
Nicholas Applegate	Russell 2000 Growth
Brandywine	Russell 2000 Value
Non-U.S. Equity	
Capital Guardian	MSCI ACWI-Ex. U.S.
Delaware	MSCI ACWI-Ex. U.S.
Fixed Income	
Loomis Sayles Boston	Lehman Brothers Baa Credit Index
Brandywine (Global Bond)	Salomon World Government Bond Index
Baird	Lehman Aggregate
AFL-CIO	Lehman Mortgage

SCHEDULE IV

MANAGER TERMINATION CHECK-LIST

This checklist is used to ensure that all details are covered when terminating investment management services.

1) Establish plan of action for reallocation of assets from terminated portfolio; transfer to other portfolios or prepare for liquidation.

2) Review department files and logs to identify any outstanding issues.

3) Notify ACERA Administration, Accounting Division, Legal Counsel, consultant, master Custodian and any other vendors of the Termination. Identify and resolve all outstanding issues with these parties.

4) Have Manager and master Custodian review and sign off on monthly market values and performance figures produced during the contract period.

5) Hold payment of last invoice until all issues are resolved.

6) Retain terminated Manager files in the ACERA office for a minimum of one year; then send to ACERA archives.

7) Hold terminated Manager files in ACERA archives for a minimum of 5 years.

SCHEDULE V*

ACERA Compliance Schedule

<u>REQUEST</u>	**<u>DUE DATE</u>**
<u>MONTHLY</u>	
Soft Dollar Commission Report (If applicable) (Submit each month regardless of whether any commissions were directed – consultants and master Custodian are subject to this request)	By the 15th of the month following the reported month
Minority Broker Commission Report (Submit each month regardless of whether any commissions were directed)	By the 15th of the month following the reported month
Accounting Report / Portfolio Valuation (Please provide transaction data – buys/sells, a portfolio listing including cost & market values, and performance returns)	By the 20th of the month following the reported month
Derivative Report (If applicable) (Please check ACERA's Investment Policy for report guidelines.)	By the 20th of the month following the reported month
Confirmation that monthly reconciliation with Bank is performed. (Reconciliation should include market values, transactions and performance.)	By the 20th of the month following the reported month

* This Schedule is designed for all investment managers of ACERA. However, managers may be required to provide additional compliance reports based on their individual investment agreements with ACERA. Should there be any conflict between individual investment agreements with ACERA and ACERA investment guidelines, policies and procedures, the individual investment agreements should prevail.

QUARTERLY

Fee Billings (Provide all backup documentation/ reconciliation sign-offs/ DVBE Expenditure Report & backup invoices)	Within 30 days following the end of the quarter
Confirmation of compliance with limitations on investment vehicles and investment markets.*	Within 30 days following the end of the quarter
Confirmation of compliance with % limitations on cash holdings, on equity investment and on fixed-income investment. *	Within 30 days following the end of the quarter
Confirmation that ACERA's assets under management does not exceed 25% of the total assets under management firm-wide.	Within 30 days following the end of the quarter

QUARTERLY – applicable to Real Estate Program

Operations Report	Due within 30 days of quarter close upon Staff's request

ANNUAL

Annual Performance Fee Billing (If Applicable) (Provide all backup documentation/ reconciliation sign-offs)	Within 30 days following the end of the performance fee period
Organization Chart	When available for the year
Fidelity Bond/	When renewed each year

* Please refer to the Specific Investment Guidelines of each manager's investment contract for details.

Errors & Omissions Insurance (Please send an original certificate)	
Audited Financial Statements	When available for the year
Form ADV, Parts I and II (If applicable)	When available for the year

ANNUAL – applicable to Real Estate Program

Tactical Plans	When available for the year
Asset Management Plan	Due 30 days prior to fiscal year end
Variance Report on Appraised Properties (if applicable)	Due within 30 days of final property appraisal

SCHEDULE VI

ACERA

INVESTMENT PHILOSOPHY (REVISED MAY 2001)

The following document describes the investment philosophy of the Alameda County Employees' Retirement Association (ACERA). Its purpose is to enunciate the basic principles and beliefs that will underlie ACERA's investment policy and impact the overall management of the pension fund. The Investment Philosophy is designed to complement rather than replace the specific investment policies of the Association. It is expected that the Association's approach to investments, as reflected in its policies and strategies, will be consistent with the philosophy over time. Though the philosophy allows significant flexibility, it also raises some constraints or implications. Where these were deemed to be significant, they have been explicitly identified and labeled as *Implications*.

Future boards may choose to amend the investment philosophy, as their experiences and circumstances will almost certainly differ. The initial document, and any subsequent changes will provide staff, advisors and future trustees with a frame of reference to help them understand how the investment program has evolved as well as the rationale behind its design. Future boards may modify the philosophy as their experiences and circumstances suggest is prudent.

The major sections of the philosophy are:

1. Mission
2. Risk Management
3. Diversification
4. Market Efficiency

5. Hi-Alpha Managers
6. Organizational Infrastructure and Communications
7. Performance Monitoring and Time Horizon

1. MISSION

a) The Board's primary goals in managing the Fund are:

i) To ensure that sufficient funds are available to pay vested benefits and maintain supplemental benefits;
ii) To comply with all applicable fiduciary standards; and,
iii) To create value added, where feasible, that will help reduce the costs of the plan, increase benefits, or both.

2. RISK MANAGEMENT

a) The Board believes that prudent management of risk is a central element of the investment function.

b) Though there are numerous risks involved in the management of a pension investment program, ACERA believes that the following warrant particular attention:

i) ***Funding-related Risk*** - The risk that the funds available in the Plan will be insufficient to pay the promised benefits, both vested and supplemental; or that contribution volatility will be unacceptably high. The primary methods for managing funding risk include regularly conducting integrated asset/liability studies, and establishing appropriate and prudent investment and funding policies.

0.1 In managing the relationship between assets and liabilities, the approved asset allocation of the Fund should provide a minimum of a 90% level of certainty of meeting the projected liabilities of the Plan over a 20 year time period, as determined by the actuary.

ii) ***Benchmark related Risk*** – The risk that the investment benchmarks adopted by the Fund are inappropriate, or that the aggregate of the individual manager benchmarks within an asset class do not adequately reflect the benchmark for the asset class as a whole. The latter risk is a specific risk generally referred to as *benchmark misfit risk (i.e. style risk)*. Inappropriate benchmarks or excessive benchmark misfit risk could result in investment performance different than expected and could adversely impact decisions concerning the hiring or firing of investment managers.

0.1 The primary methods for effectively managing benchmark-related risk are:

(a) regular review of the Fund's benchmarks; and

(b) regular measurement and monitoring of misfit risk using proper methodologies.

iii) ***Manager Risk*** - The risk of aberrant performance on the part of individual investment managers, and the related active management risk for asset classes as a whole.

0.1 The primary methods for mitigating manager risk are:

(a) Prudent processes for selecting and monitoring investment managers;

(b) Competent internal investment staff;

(c) Effective investment consulting support; and,

(d) Clear communication to investment managers of ACERA's objectives, expectations, and investment time horizons.

0.2 The primary method for mitigating active management risk for asset classes include:

(a) Establishment of appropriate asset class benchmarks;

(b) Careful monitoring of asset class performance relative to the benchmarks; and

(c) Prudent use of passive management.

iv) ***Fortitude Risk*** - The risk that the board or staff will fail to exercise the patience, judgment, or fortitude required to support long-term policies and strategies for the investment and funding program.

0.1 The keys to managing fortitude risk are believed to include:

(a) Effective orientation and education with respect to institutional investing and actuarial science; and,

(b) A commitment to continually refining, confirming and communicating the investment philosophy and funding policy of the Association.

3. DIVERSIFICATION

a) ACERA acknowledges the basic tenets of modern portfolio theory, which suggest that diversification, or combining assets that are not perfectly correlated with each other, will reduce the long-term volatility of the overall portfolio.

b) It is generally desirable however to avoid overly complex asset structures, provided the allocation selected can reasonably be expected to meet the objectives of the Plan. ACERA believes that the benefits of diversification must be weighed against the costs involved, which may include fees, liquidity, complexity, communication, internal staff resources and expertise and trustee knowledge and effort.

c) The following asset classes are appropriate candidates for inclusion in its portfolio:

i) Domestic equity

ii) International equity (including emerging markets)

iii) Fixed income, including high yield fixed income and international fixed income

iv) Real estate

d) ACERA does not consider alternative investments to be an appropriate candidate for inclusion in its portfolio due to the substantial direct and indirect costs associated with it.

Implications

- A systematic methodology for re-balancing the investment portfolio is required to ensure proper implementation and adequate risk control concerning ACERA's asset allocation.
- Adding or deleting asset classes or investment managers should be considered in light of the impact such decisions are likely to have on the general complexity and cost structure of the portfolio, as well as ACERA's ability to prudently achieve its investment and funding goals over the long run.

4. MARKET EFFICIENCY

Except for specified high alpha assignments:

a) ACERA does not believe in the viability of active management strategies that rely on market timing.

b) ACERA does not believe in the viability of management strategies that call for over weighting or under weighting styles or sectors within an asset class; i.e. benchmark misfit risk will not generate long-term alpha. Accordingly, ACERA generally believes that it should maintain exposures within an asset class (such as style or capitalization weightings) that are consistent with the broad benchmark for the asset class as a whole.

c) ACERA does believe that market efficiency varies among asset classes, creating opportunities for successful active management strategies based on securities selection.

d) Asset classes that can be demonstrated to be efficient should be managed passively in order to reduce active management risk and lower the costs of managing the portfolio.

e) For inefficient asset classes, ACERA believes that it has the ability and a duty to prudently exploit such inefficiencies through active securities selection strategies.

Implications

- ACERA should be conscious of any subtle forms of market timing that may arise in the course of managing the fund, or that may be implicit in investment strategies presented to ACERA for inclusion in the investment program.

- ACERA must determine appropriate methodologies for determining whether an asset class is efficient or presents appropriate opportunities, thus providing insight to the Board on the use of particular strategies.

5. HIGH ALPHA MANAGERS

a) ACERA believes that the portfolio characteristics utilized to control risk in the broad portfolio, such as market capitalization, sector exposure, use of derivatives, leverage limitations, property type or deal structure may be modified for specific managers who control a limited portion of the portfolio and have demonstrated a proven capacity to consistently add value net of fees. Such strategies, which ACERA refers to as Hi-Alpha, may include the following elements:

   i) The bulk of the asset class is passively managed or risk controlled; and,
   ii) A small number of active managers are retained who employ somewhat more aggressive investment strategies, such as concentrated portfolios, leveraged purchases, developments, high-yield debt, etc.

b) The primary benefits of a Hi-Alpha approach are believed to include:

   i) Reduction in active management risk;

   ii) Lower average investment fees; and

   iii) Concentration on opportunities where the likelihood of adding value is greatest.

c) The market efficiency and opportunities in asset classes may change over extended periods of time; therefore ACERA believes that its portfolio management strategies should adapt over time to reflect the changing nature of capital markets.

6. Organizational Infrastructure and Communications

a) ACERA believes that in order for the investment program to achieve its goals, ACERA must invest the necessary resources to build and maintain an appropriate organizational infrastructure, key elements of which include:

   i) A competent, internal investment staff comprised of a sufficient number of investment professionals possessing appropriate leadership, technical and administrative skills.

      0.1 In attracting a competent staff, ACERA recognizes that it competes with the private sector. It must therefore continually strive to create a total work environment that is challenging, rewarding, and competitive.

   ii) A strong relationship with outside general investment consultant(s) who are able to provide ACERA with the following:

0.1 A high degree of investment expertise;

0.2 Innovative and proactive advise and counsel;

0.3 Strong research support; and

0.4 Strong reporting capabilities,

iii) A broad-based information gathering and reporting system to present well- researched, relevant and timely data in a manner that is easily understood, and that supports rigorous and consistent monitoring of critical investment activities.

iv) An open channel of communication between the Board, management, and the Association's external investment professionals.

b) By providing the Board with timely, accurate, and thorough information, the organizational infrastructure will give the Board the high level of comfort it needs to set policy, make investment decisions, oversee the performance of the investment program, and maintain the fortitude necessary to support its investment philosophy, policies and strategies.

Implications

- ACERA must determine what constitutes an appropriate internal investment staff structure, given the nature of the current investment program.

- ACERA must over time take concrete steps towards creating a work environment that will allow the Association to attract and retain needed staff.

- ACERA must recognize that developing the organizational infrastructure it needs – staffing, consulting support, information systems, and communication channels – cannot be achieved overnight, but rather will require an ongoing commitment of time and resources.

7. Performance Monitoring & Time Horizon

a) ACERA holds the following basic beliefs concerning performance monitoring practices and methodologies:

i) The various investment policies of the Fund, in the aggregate, are the most important determinants of investment success; compliance with investment policies should therefore be monitored rigorously;

ii) The performance of the total portfolio, individual asset classes, and investment managers should be compared to appropriate, predetermined benchmarks;

iii) Peer comparisons are an additional valid tool in assessing individual manager performance (supplementing the use of benchmarks), given that ACERA aims to select superior managers within particular investment styles or mandates. Peer comparisons, or performance rankings, are also valid tools for measuring the performance of asset class portfolios.

iv) Peer group comparisons are not an appropriate means of assessing the performance of the total fund, given that sponsors have different objectives and risk tolerance levels, and therefore may have different asset allocation policies.

v) Benchmark misfit risk, or the risk that the aggregate of individual investment manager benchmarks in an asset class do not adequately reflect the benchmark for the asset class as a whole, should be explicitly measured on a regular basis.

vi) Investment managers are generally hired to fulfill a specific role in a portfolio. Accordingly, ACERA believes it is important that ACERA monitor the extent to which managers comply with their stated style and mandates.

b) ACERA believes that successful funding and investment decisions require a long-term perspective on the part of the Board and management:

i) It is the intention of the Retirement Board that commitments to asset classes and investment strategies should involve long time horizons that may include more than one business cycle (3-5 years each). Relatively illiquid asset classes may require even longer time horizons.

ii) The Board acknowledges that commitments to individual investment managers also require a long time horizon of at least one business cycle (3-5 years).

iii) ACERA believes that proper reporting and monitoring systems; and clear communication among consultants, management, investment managers and the board will enable the Board to maintain the necessary long term perspective on all investment decisions.

<u>Implications</u>

- Assessing the investment performance relative to appropriate, pre-determined, benchmarks is as applicable to the total portfolio and to individual asset classes as it is for individual investment managers, and therefore warrants a commensurate share of the Board's time and attention.

- The Board will spend relatively little time assessing the performance of the Fund relative to that of comparable pension funds.

- ACERA will need to either develop in-house capabilities to regularly measure benchmark-related risk, or it will need to purchase such capabilities from external investment consultants.

- ACERA will monitor all investment managers to ensure they are complying with their stated investment style, regardless of whether they are performing well or poorly. Strongly performing managers who are found to not be following their stated styles will be carefully scrutinized and may be subject to disciplinary action.

- ACERA will monitor all investment providers to ensure compliance with the Board's Investment Policies.

SCHEDULE VII

TABLE OF AMENDMENT DATES

AMENDING RESOLUTIONS

Jun	27,	1985
Oct.	10,	1985
Jan.	9,	1986
Jan.	16,	1986
Mar.	13,	1986
May	22,	1986
Sep.	11,	1986
Oct.	9,	1986
Nov.	20,	1986
May	14,	1987
Aug.	13,	1987
Oct.	8,	1987
Apr.	21,	1988
July	28,	1988
Jan.	29,	1989(4)
Apr.	13,	1989(5)
May	18,	1989
July	13,	1989
Aug.	10,	1989
Nov.	16,	1989(2)
July	11,	1991
June	11,	1992
June	10,	1993
July	8,	1993
Nov.	18,	1993
May	14,	1994
Aug.	18,	1994
Nov.	20,	1994
Feb.	16,	1995
May	18,	1995
Jan.	16,	1997
Aug.	20,	1998
May	20,	1999
Jan.	31,	2000
Apr.	19,	2001
Jul.	18,	2002
Feb.	21,	2003

Alameda County Employees'
Retirement Association

ACERA

INVESTMENT GUIDELINES, POLICIES AND PROCEDURES

AMENDED February 19, 2004

ACERA
INVESTMENT GUIDELINES, POLICIES AND PROCEDURES
2004

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[1] Prepared for ACERA by Cortex Consulting; adopted by the Board of Retirement on March 8, 2000 and revised May 2001.

ACERA
INVESTMENT GUIDELINES, POLICIES AND PROCEDURES

SECTION I: MISSION AND PURPOSE

The Alameda County Employees' Retirement Association (ACERA) exists for the purposes of providing accurate, timely benefits to its members and their beneficiaries and defraying reasonable expenses of administration.

The Board of Retirement (the Board), having exclusive authority and exclusive fiduciary responsibility for the investment and administration of the Trust Fund (the Fund), hereby establishes the following Investment Guidelines, Policies and Procedures (the Policy) for the investment of ACERA's assets. The Board reserves the right to amend, supplement or rescind this Policy at any time.

The Board of Retirement is directed by law and given discretion to prudently invest the plan assets. The purpose of this statement of policy is to assist ACERA in effectively supervising said investments and to encourage effective communication between ACERA and its managers and consultants.

ACERA's investment goal is to operate at a level of performance in the upper quartile of comparable pension funds on a risk-adjusted basis and to be as fully funded as possible so that ACERA's benefit costs do not become a burden upon future generations of members and taxpayers.

SECTION II: CONSTITUTIONAL REQUIREMENTS

Article 16 §17 of the California State Constitution provides in pertinent part as follows:

"Notwithstanding any other provisions of law or this Constitution to the contrary, the retirement board of a public pension or retirement system shall have plenary authority and fiduciary responsibility for investment of money and administration of the system, subject to the following:

a. The retirement board of a public pension or retirement system shall have the sole and exclusive fiduciary responsibility over the assets of the public pension or retirement system. The retirement board shall also have sole and exclusive responsibility to administer the system in a manner that will assure prompt delivery of benefits and related services to the participants and their beneficiaries. The assets of a public pension or retirement system are trust funds and shall be held for the exclusive purposes of providing benefits to participants in the pension or retirement system and their beneficiaries and defraying reasonable expenses of administering the system.

b. The members of the retirement board of a public pension or retirement system shall discharge their duties with respect to the system solely in the interest of, and for the exclusive purposes of providing benefits to participants and their beneficiaries, minimizing employer contributions thereto, and defraying reasonable expenses of administering the system. A retirement

board's duty to its participants and their beneficiaries shall take precedence over any other duty.

c. The members of the retirement board of a public pension or retirement system shall discharge their duties with respect to the system with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with these matters would use in the conduct of an enterprise of a like character and with like aims.

d. The members of the retirement board of a public pension or retirement system shall diversify the investments of the system so as to minimize the risk of loss and to maximize the rate of return, unless under the circumstances it is clearly not prudent to do so.

e. The retirement board of a public pension or retirement system, consistent with the exclusive fiduciary responsibilities vested in it, shall have the sole and exclusive power to provide for actuarial services in order to assure the competency of the assets of the public pension or retirement system.

f. With regard to the retirement board of a public pension or retirement system which includes in its composition elected employee members, the number, terms, and method of selection or removal of members of the retirement board which were required by law or otherwise in effect on July 1, 1991, shall not be changed, amended, or modified by the Legislature unless the change, amendment, or modification enacted by the legislature is ratified by a majority of the electors of the jurisdiction in which the participants of the system are or were, prior to retirement, employed.

g. The Legislature may by statute continue to prohibit certain investments by a retirement board where it is in the public interest to do so, and provided that the prohibition satisfies the standards of fiduciary care and loyalty required of a retirement board pursuant to this section.

h. As used in this section, the term "retirement board" shall mean the board of administration, board of trustees, board of directors, or other governing body or board of a public employees pension or retirement system; provided, however, that the term "retirement board" shall not be interpreted to mean or include a governing body or board created after July 1, 1991, which does not administer pension or retirement benefits, or the elected legislative body of a jurisdiction which employs participants in a public employees pension or retirement system."

SECTION III: ELIGIBLE ASSET CATEGORIES

The Fund shall hold assets in categories established by the Board. Any asset category may be held in direct form, in pooled form or in both. Asset categories managed by one or more "Qualified Investment Managers" {Manager(s)} are called "Managed Accounts". Asset categories under the supervision of the County Treasurer are called the Treasurer's Accounts. Eligible asset categories are listed and defined below.

A. **CASH** shall consist of short term (12 months or less) interest bearing investments of high quality such as U.S. Treasury issues, insured certificates of deposit of U.S. banks (fixed and/or variable), commercial paper rated A-1, P-1 or both, or other instruments of equal or better quality, and includes money market funds available through the Custodian Bank (Custodian).

B. **U.S. EQUITY** shall consist of common stocks and other securities which are convertible into common stocks, and ADRs (American Depository Receipts), as well as cash (per "A" above) and fixed income (per "D" below) when used as temporary substitutes for common stocks.

C. **INTERNATIONAL EQUITY** shall consist of common stocks and other securities convertible into common stocks of companies domiciled outside of the U.S., and GDR's (Global Depository Receipts), as well as cash equivalents and fixed income, domestic or international, which are being used as temporary substitutes for common stock.

D. **FIXED INCOME** shall consist of investments in U.S. taxable bonds, debentures, notes and other evidences of debt. Fixed income may also include non-dollar denominated bonds issued by corporations or governments domiciled outside of the United States of America as well as Brady Bonds. Other eligible investments include cash equivalents per "A" above and convertible bonds and preferred stock.

E. **MEMBER MORTGAGES** (closed program) shall consist of first mortgages, secured by the primary residences of the borrowers, underwritten to GNMA/FNMA standards by a qualified third party expert underwriter retained by the Board for that purpose.

F. **REAL ESTATE** shall consist of investments in equity real estate through the use of commingled or direct investments. For more information about real estate investments, refer to ACERA's Real Estate Policy which is maintained as a separate document.

SECTION IV: INVESTMENT PHILOSOPHY

The following is a summary of ACERA's Investment Philosophy. For a complete statement, please refer to Schedule VI, "ACERA Investment Philosophy".

The Board believes that its investment policies, in aggregate, are the most important determinants of its investment success. Compliance with investment policies should therefore be monitored rigorously. The Board also believes that performance of the total portfolio, individual asset classes, and Managers should be monitored and compared to appropriate, predetermined benchmarks.

The Board believes that prudent management of risk is a central element of the investment function and that diversification among asset classes will reduce risk and enhance returns of the overall investment portfolio in the long term.

The Board believes that market efficiency and opportunities vary among asset classes and may change over extended periods of time; therefore, the Board believes that ACERA's portfolio management strategies should adapt over time to reflect the changing nature of capital markets.

The Board's primary goals in managing the Fund are:

1. To ensure that sufficient funds are available to pay vested benefits and maintain supplemental benefits;
2. To comply with all applicable fiduciary standards; and

3. To add marginal value that will help reduce the costs of the plan and/or to increase benefits for the beneficiaries.

The Board believes that in order to achieve its goals, ACERA must invest the necessary resources to build and maintain an appropriate organizational infrastructure.

SECTION V: INVESTMENT STRATEGY

A. **U.S. EQUITY** will be structured to capture exposure to the broad U.S. equity market as represented by the Russell 3000 Index. Passively managed (index) portfolios will be used in markets that are reasonably efficient. These portfolios are intended to provide broadly diversified market exposure with controlled (market) risk and minimal cost.

Actively managed portfolios will be used in less efficient markets when the Board determines that a Manager possesses special skills or abilities that enable that Manager to capture excess returns relative to the market, adjusted for risk and fees; or to exploit specialty markets that provide enhanced return with acceptable risk.

A great part of the Russell 3000, on a market value basis, is comprised of large-cap stocks, which the Board believes are efficiently priced most of the time. Therefore, the Board has adopted a policy of obtaining overall exposure to this segment of the market via passively managed indexed products. Some active Managers have been employed to enhance overall portfolio return in the large- and/or mid-cap sectors on a risk- and fee-adjusted basis. These Managers manage ACERA's "Hi-Alpha" program.

The remainder of the Russell 3000 index is comprised of small to mid-cap companies. Some opportunities for active management enhancement exist in these securities due to market inefficiencies. ACERA will attempt to capture these opportunities through a mix of Managers who have the special skills required to identify smaller companies that may be undervalued or possess substantial growth potential.

The U.S. equity portion of the portfolio shall be allocated among the various styles and Managers as indicated in Schedules I and IA.

B. **INTERNATIONAL EQUITY** represents an opportunity to diversify risk and capture enhanced returns within markets generally less efficient than the U.S. domestic equity market. 100% of the international equity portion of the Fund will be invested in actively managed portfolios.

C. **FIXED INCOME** represents a means of reducing overall portfolio risk and capturing incremental returns either domestically or globally. Inefficiencies in the pricing and trading of fixed income securities create opportunities to add value through active management. 100% of the fixed income portion of the portfolio will be invested in actively managed portfolios.

D. **REAL ESTATE** will be used as a means for diversifying the portfolio and capturing additional returns due to the low correlation between returns on real estate and financial assets. Due to the illiquid nature of real estate assets, distinctions between active and passive management are not applicable. For more information regarding real estate investments, refer to ACERA's Real Estate Policy which is maintained as a separate document.

SECTION VI: ASSET ALLOCATION AND REBALANCING

Asset allocation targets, a function of the returns and risks from various asset classes and the nature of the plan's liabilities, are set forth in Schedule I. A goal of asset allocation is balancing asset growth versus liability growth considering time horizons, liabilities and risk tolerance.

Rebalancing is the risk control process of returning an allocation back to the desired target level after having drifted away from its targeted position. The standard deviation factors that shall be used to define the acceptable ranges around the asset allocation targets are set forth in Schedule IA. The objective of rebalancing is to enhance the risk-adjusted performance of the asset allocation structure.

ACERA Staff ("Staff") shall be responsible for maintaining the relative weights of asset classes and allocations within the acceptable rebalancing ranges as reflected in Schedule IA. Should an asset class or allocation fall outside its target range, Staff shall rebalance the asset class or allocation back to the target weights as specified in the asset allocation structure in Schedule I.

Staff shall:

1. Monitor the portfolio;
2. Determine whether or not any asset category is out of balance with its target asset allocation in excess of the specified tolerance range;
3. Determine whether or not any Manager within each asset category is out of balance with their target allocation in excess of the specified tolerance range;
4. And, if so, either:
   (a) instruct the relevant Managers to redirect cash income (interest coupon and dividends) in concert with an evaluation of pending commitments and other cash flows (employer and employee contributions), in order to bring the allocation(s) back to the adopted strategic target; or
   (b) instruct the relevant Managers to liquidate or acquire the appropriate dollar value of securities to reach the target and reallocate the cash thus generated or required to the other category(s) or Manager(s) as necessary.

Staff shall report to the Board on a regular basis the status of the Fund with respect to how categories are tracking relative to their allowable ranges, as well as any actions taken to rebalance the portfolio.

SECTION VII: ASSET CATEGORIES OBJECTIVES

The general objective of the Board is to preserve capital and earn a return from appreciation and income, as described herein:

To ensure the integrity of ACERA's actuarial funding plan, one minimum return objective for the Fund shall be the current actuarial interest assumption rate plus 25 basis points per year over a market cycle. Returns shall be calculated net of fees.

To ensure that ACERA's assets grow appropriately to match salary increases which directly impact benefit levels, an additional minimum return objective for the Fund over a market cycle (up to five years) shall also be 400 basis points (4%) per year over the national Consumer Price Index, published by the U.S. Department of Commerce.

To ensure that ACERA's external investment manager structure in aggregate is performing satisfactorily, an additional minimum return objective for the Fund over a market cycle (up to five years) shall also be equivalent to the Fund's Policy Index on a gross of fee basis.

The objectives of each asset category are:

A. CASH

1. A rate of return in excess of 90-Day U.S. Treasury bills.

2. A rate of return within the upper one half of a universe of like short-term funds.

B. U.S. EQUITY

1. A rate of return in excess of the U.S. equity market as measured by the Russell 3000 Index after adjustment for risk and fees.

2. A rate of return within the upper 33rd percentile of the Wilshire Co-op or similar database of the performance of diversified equity portfolios.

C. INTERNATIONAL EQUITY

1. A rate of return in excess of the Morgan Stanley Capital International All Country World Index Ex-U.S. Free (MSCI ACWI Ex-U.S.).

2. A rate of return within the top quartile of the Wilshire Co-op or similar database of the performance of diversified international equity portfolios.

D. FIXED INCOME

1. A rate of return in excess of the Lehman Aggregate Bond Index, Citigroup World Government Bond Ex. U.S. and Lehman High Yield in a ratio of 75/15/10.

2. A rate of return within the top quartile of the Wilshire Co-op or similar database of the performance of diversified fixed income portfolios.

E. MEMBER MORTGAGE (closed program)

1. A rate of return that compares favorably with the Salomon Mortgage Index.

2. A delinquency rate of less than 2% of loans outstanding;

F. REAL ESTATE

1. Total Return – a minimum total gross return equivalent to the National Council of Real Estate Investment Fiduciaries (NCREIF) Property Index over rolling five-year periods.

2. Income Return – Income, which is defined as cash distributed to the Association, should comprise at least 2/3 of the total expected return over rolling five-year periods for all Stable (as defined in ACERA's Real Estate Investment Policy) product.

In addition, objectives that reflect the particular investment strategy or style used by individual Managers shall be outlined in specific investment guidelines attached to the Manager's contract.

SECTION VIII: ALLOCATION OF CASH FLOW

Cash flow not needed for benefit payments or administrative expenses shall be allocated to Managed Accounts in a ratio that best funds the overall targeted asset allocation as reflected in Schedules I and IA.

If cash flow is insufficient for the payment of benefits or to cover administrative expenses, then Managed Accounts shall be debited in a ratio that best satisfies the target allocation shown in Schedules I and IA. Such debits, if necessary, will be carried out as needed, and with timely notice to Managers to facilitate effective funds transitions and performance measurement.

For all planned investments which may not need to be funded immediately, a reserve may be budgeted and invested in appropriate accounts in accordance with the asset allocation targets until such moneys are required. Alternatively, Managed Accounts within "overfunded" asset classes may be called upon to provide the required moneys.

SECTION IX: PROHIBITED INVESTMENTS

Managers shall exercise prudent expert standards in defining prohibited investments. For example, prohibited investments include, but are not limited to, securities issued by the County of Alameda or any agency thereof.

SECTION X: DIRECTED BROKERAGE

ACERA does not engage in either directed commission arrangements or "soft dollar" transactions.

SECTION XI: DERIVATIVE INSTRUMENT USAGE POLICY

Exposure to risk by use of derivative instruments must be consistent with ACERA's overall investment policy as well as an individual manager's specific investment guidelines. Derivatives shall not be used to establish a leveraged position (i.e. offsetting Cash positions must be maintained against all delayed settlement transactions).

SECTION XII: SELECTION OF INVESTMENT MANAGERS

The Investment Committee shall direct Staff and/or a consultant to initiate searches for Managers. Staff and/or the consultant shall research for qualified candidates and present a list of finalists to the Investment Committee for its approval. Upon approval of the list, the finalists shall be interviewed by Staff and the consultant (if applicable). Staff and the consultant (if applicable) shall evaluate the interviews, rank the finalists, and make a recommendation to the Investment Committee to hire one or more firms attaining the highest rankings in a publicly noticed meeting at which no less than five (5) Investment Committee members shall be present. It is possible that none of the firms will be recommended for hire.

These procedures are developed for the convenience and benefit of ACERA, and shall not bind ACERA or invalidate the selection of a Manager if different processes are used subsequent to the promulgation of this Policy.

SECTION XIII: AUTHORITY OF INVESTMENT MANAGERS

Subject to the laws of the United States and the State of California, and to the terms and conditions of this Policy, Managers shall have full discretion to direct the purchase, exchange, sale and reinvestment of the assets of the Managed Accounts. The Board expects that Managers will recommend changes to this Policy when any part of this Policy appears to be at variance with overall market and economic conditions.

Managers shall place orders to buy and sell securities and, by notice to the Custodian, shall cause the Custodian to deliver and receive securities on behalf of the Fund. Managers shall, upon Board inquiry, report placement of ACERA brokerage such that the Board shall be assured commissions were placed for the sole and exclusive benefit of the Fund.

Separate account Managers shall not vote proxies. Proxies shall be voted by ACERA, via a proxy voting service vendor, in accordance with Board-established policies and procedure.

Securities lending shall be performed under the oversight of Staff, in accordance with Board-established policies and procedure.

SECTION XIV: INVESTMENT GUIDELINES FOR THE MANAGED ACCOUNTS

Individual Manager discretion shall be governed by the investment guidelines for the managed accounts as well as the specific investment guidelines set out in the Investment Contract of each Manager. Should there be any conflict between the specific investment guidelines of an Individual Manager and the investment guidelines for the managed accounts, the specific investment guidelines shall prevail.

A. GENERAL

1. All investments shall comply with all applicable laws of the United States and the State of California governing the investment of pension trusts.

2. All securities transactions shall be executed by reputable broker/dealers, banks, or the Custodian, and shall be on a best-price and best-execution basis, and shall be reported to ACERA as is called for elsewhere in this Policy.

3. All Managers shall refrain from investing in a tobacco producer investment opportunity when, in their expert opinion, an alternative non-tobacco producer investment opportunity is available that will satisfy the same ACERA portfolio guidelines, instructions and objectives for risk, return and diversification.

B. EQUITY

Managers have full discretion to invest solely in readily marketable and diversified equity securities as defined above subject to the following:

1. For Managed Accounts, no more than 10% of the value (at time of investment) of the account shall be invested in the securities of a single issuer.

2. ACERA shall not hold more than 10% of the equity securities of any issuer.

3. Equity securities shall possess value and quality corroborated by generally accepted techniques and standards of fundamental securities analysis.

4. Assets in a Managed Account not invested in equity securities shall be kept with interest in appropriate money market instruments, including any money market fund available through the Custodian.

5. A Managed Account shall be subject to ACERA's policy on derivatives.

6. All Managers shall endeavor to be fully invested in stocks at all times unless they have received specific authorization to the contrary from the Board. Cash holdings, as defined in this Policy, shall generally not exceed 5% of the portfolio on a market value basis.

C. FIXED INCOME

Managers have full discretion to invest solely in readily marketable and diversified securities including, but not limited to:

1. Obligations of the U.S. and /or eligible foreign government's Treasuries.

2. Obligations guaranteed by agencies of the United States and /or eligible foreign governments.

3. Insured certificates of deposit and banker's acceptances of credit worthy banks.

4. Corporate and other evidences of debt. At least 80% of this debt must be rated by Moody's Investor's Services or by Standard & Poors.

5. Commercial paper and banker's acceptances of issuers rated P-1 by Moody's Investor's Service.

6. Or A-1 by Standard & Poors Corporation.

7. Excepting direct obligations of the U.S. and/or eligible foreign governments, and those explicitly guaranteed by the U.S. and/or eligible governments, no account shall hold more than 5%, at cost, of the obligations of any single issuer.

8. Fixed income derivative investments shall be in accordance with ACERA's derivative policy.

SECTION XV:
SEPARATE ACCOUNT MANAGER SPECIFICATIONS

A. Managers must be registered as investment advisers under the Investment Adviser's Act of 1940, a bank (as defined in that act) or an insurance company qualified to perform investment management services under state law in more than one state, including California. Unless an exception is granted by the Board, by accepting appointment as ACERA's Managers, Managers shall acknowledge that they are "Plan Fiduciaries" and "Qualified Investment Managers" as defined by the Employees' Retirement Income Security Act (ERISA) of 1974, (see or reference United States Code Title 29 Section 1001 et. seq..)

B. Managers shall maintain fiduciary insurance in the amount of 10% of the total assets managed in the ACERA account or $25 million, whichever is higher, unless the contract specifies otherwise.

C. Managers shall promptly notify ACERA of changes that occur in any of the following:

1. The investment strategy used in managing the subject product.
2. The key personnel involved in managing ACERA's account.
3. The ownership, key personnel, or organizational structure of the Manager's company.
4. The Manager company's financial condition.

5. The number of clients invested in the subject product.
6. The market value of the total assets managed in the subject product.

D. Managers shall promptly notify ACERA if they are subject to censure or disciplinary action by a regulatory agency.

E. Managers shall promptly provide to ACERA all of the required documents and reports as set forth in Schedule V – ACERA's Compliance Schedule.

F. Managers shall not make contributions, provide gifts, reimbursements of expenses or provide personal benefits exceeding $250 in the aggregate within any 12-month period to any Trustee, fiduciary, employee or consultant of ACERA. Donations of educational conferences and similar events and benefits, including travel, meals and accommodations will be made to ACERA and not directed to individuals. The Board will determine whether to accept any donations and will be solely responsible for selection of the Trustee, staff member, or other individual, who will attend or otherwise participate on behalf of ACERA.

SECTION XVI: MANAGER MONITORING POLICY

The ACERA Board has contracted with a number of external Managers to invest ACERA assets in the public equity markets. As part of the Board's fiduciary duties to prudently select, monitor and supervise these Managers, the Board has adopted this Policy. The intent of this Policy is to notify Managers of the standards by which they will be judged and to establish a structure which the Investment Committee and the Board can use to monitor the performance of the Managers.

Managers will be monitored to:

1. Evaluate how well they achieve their investment objectives.
2. Ensure that they adhere to their established investment approach/style and do not attempt to index returns to preserve stellar performance or take extraordinary risk to overcome poor performance.
3. Identify issues or trends that have the potential to result in losses to the Fund.
4. Alert the Board when Managers are not performing to expectations so that appropriate remedial action can be taken.

Managers will be evaluated on the basis of the following: performance, style integrity, organizational stability, compliance, and client service described in greater detail below.

A. PERFORMANCE

On a monthly basis Staff will monitor Manager holdings, activity and performance.

On a quarterly basis Staff and/or a consultant will furnish the Investment Committee and/or Board with an in-depth evaluation of each Manager which will include a comparison of the Manager to its contract benchmark and a peer universe of Managers using a similar investment style. This report shall include an analysis of the sources of Managers' returns (stock selection, industry selection, asset allocation, etc.) and shall identify which decisions enhanced or diminished performance.

On a quarterly basis, trading costs will be evaluated in terms of commissions paid and execution of trades. Staff and/or a consultant shall furnish a report to the

Investment Committee and/or Board regarding trading costs on an annual basis.

B. STYLE INTEGRITY

Each Manager will be analyzed at least annually to ensure that the Manager is continuing to invest the portfolio in the style for which they were originally hired. Style integrity is essential to maintain the Board's asset allocation policy. Any significant deviation in style will result in the overall portfolio having a different characteristic, in some measure, from the broad market which is represented by the Russell 3000 index. Significant variations in the portfolio characteristics from the style anticipated in the management contract may indicate a change in its investment style.

This review also provides the Investment Committee and/or Board an opportunity to evaluate the Manager's continuing "fit" with the goals of the overall fund. By monitoring Manager style the Investment Committee and/or Board can assure that its Manager mix takes advantage of opportunities to increase diversification through lower correlation of returns among individual Managers.

C. ORGANIZATIONAL STABILITY

Managers' organizations will be monitored to ensure continuity of the intellectual and philosophical processes that went into developing the particular investment approach contracted for by ACERA. In addition, Managers will be monitored for business risk, quality of staff**,** departures of key investment personnel, change in ownership or acquisition, and potential conflicts of interest.

It is ACERA's intent that its portfolio comprises no more than 25% of the Manager's total assets under management. Therefore ACERA will monitor the Managers' assets, firm-wide, as well as in the subject product.

D. COMPLIANCE

Managers will be monitored to ensure they are adhering to Federal and state laws regarding securities and the management of investment portfolios, trading, and pension investments; ethical practices of the investment professions; the Contract governing their relationship with ACERA; and the policies and guidelines set forth in this Policy statement and any other written directives issued by ACERA.

Each ACERA contract will specify which investment vehicles a Manager is authorized to use, which markets the Manager is authorized to transact business in and any limitations within a market (small or large capitalization, value or growth orientation). The assets in each Manager's portfolio shall be reviewed monthly to ensure compliance with contract guidelines.

All required documents and reports, set forth in Schedule V, must be submitted in a timely manner and in the format specified by ACERA.

Managers must provide prior notification and justification for failure to comply with rules, regulations, contract provisions, deadlines or other directives. Managers must provide a time frame for curing any deficiencies. Staff shall evaluate each incident on a case-by-case basis and determine whether an exception may be granted.

E. CLIENT SERVICE

Managers are required to comply with routine portfolio investment guidelines and reporting deadlines and are also expected to cooperate with special requests for information. ACERA will establish reasonable time frames for all requests and reporting and will provide feedback to all external equity Managers regarding the perceived quality of their client service.

ACERA Staff will endeavor to meet with each Manager at least twice a year by telephone or in person to review performance and other issues.

SECTION XVII: CONTRACT REVIEW PROCESS

If during the course of regular monitoring, ACERA determines that a Manager's performance, style integrity, organizational stability, compliance, or client service has declined to unacceptable levels, ACERA may, at its discretion, subject the Manager to ACERA's Contract Review Process. As part of the Board's fiduciary duties to prudently select, monitor and supervise their Managers, the Board has approved this process. The purpose of this process is to ensure as little disruption as possible in the event that concerns or problems arise with respect to a Manager's performance. The Board does not confer any additional rights or protections to its Managers by the promulgation of this Policy and/or this process.

There are generally three stages of review: Watchlist, Probation, and Termination. (described below). ACERA reserves the right to terminate an investment management contract at any time, with or without 30 days notice, for any reason, and without resort to this Contract Review Process.

The Contract Review Process may result in one or more of the following:

1. Placement on Watchlist or Probation status.
2. Movement from one stage of review to another, or removal from the Contract Review Process.
3. Reduction of assets under management.
4. Revision of investment contract guidelines for that Manager.
5. Re-negotiation of fees.
6. Termination of a Manager's contract.
7. Or any other deemed appropriate by the Board

Each situation is unique and action by the Board will vary depending on the type of Manager, the style/strategy and the deficiency involved. The following describes the Contract Review Process:

A. INITIAL REVIEW

Prior to a Manager being considered for Watchlist, Probation or Termination, ACERA may take the following steps :

1. Analysis

Staff will conduct in-depth analyses of the perceived deficiency to verify that a deficiency exists, form an initial assessment of the severity of the deficiency, and make an initial determination of possible causes.

2. Discussion with the Manager

Staff will contact the Manager to discuss the situation and the results of Staff's analysis.

3. Consultant Input

ACERA may seek the services of a consultant to provide additional assessment and advice regarding the situation, depending on the severity of the deficiency.

All phases of account compliance may be reviewed during this step, in addition to the specific issue that originated the Review Process.

B. FORMAL ACTION

After completing the Initial Review, Staff may recommend to the Investment Committee and/or Board that the Manager be either placed on Watchlist or Probation or, in certain cases, Terminated. The Committee and/or Board will approve or reject the recommendation. However, if a manager's deficiency satisfies the criteria as listed under Watchlist and Probation in this Review Process, Staff may place a manager on Watchlist or Probation without the Committee and/or Board's prior approval. In that case, Staff will be required to report to the Committee on the action taken in this Review Process as soon as possible. The specific criteria for determining which stage of Contract Review to recommend is outlined later in this Policy section and summarized in tabular form in Schedule II.

Upon approval of a Watchlist or Probation recommendation:

1. Staff will notify the Manager of the Board's decision and will provide the Manager with a statement of concerns which outlines the areas which need improvement.

2. The Manager will be asked to respond in writing with an explanation of the issues and a proposed action plan to resolve the issues within 30 days of receipt of the statement of concerns.

3. Staff, a consultant and the Manager will collectively draft a Plan of Action. The plan will identify: the specific steps to be taken to correct the problem; the time frames for further review; and what additional monitoring may be required.

   At the end of the time period specified in the Plan of Action, the Manager will be evaluated and one of the following actions may be taken:

   (a) Removal from Contract Review: If the manager successfully resolves the issues/deficiencies and demonstrates continued success in all other areas of its relationship with ACERA.

   (b) Movement from Probation to Watchlist: If the Manager has satisfied all or most of the issues/deficiencies that caused it to be placed on Probation, yet Staff continues to have concerns about the Manager. If circumstances warrant, a Manager may also be moved from Watchlist to Probation at any time during the Contract Review Process.

   (c) Extension of Contract Review: A Manager may be given additional time to satisfy the conditions of its Action Plan if reasonable progress is being made. Extensions may also be granted if unfavorable market conditions or high costs make reallocation of assets inadvisable.

   (d) Termination: If the Manager has not satisfactorily resolved the issues/deficiencies, Staff may recommend termination as described below. Termination may be recommended at any time during the

Contract Review Process if circumstances warrant.

WATCHLIST

Watchlisting indicates an increased level of concern, but does not indicate major deficiencies. The Watchlisting period is typically one year. Any of the following may result in a Watchlist status:

A. UNDERPERFORMANCE

Please refer to Schedule II for specific Watchlist criteria for each Manager.

B. STYLE DEVIATION

Managers are expected to adhere to the style of investment management for which ACERA originally hired them. Changes in portfolio characteristics or style drift may lead to a Watchlist status.

C. ORGANIZATIONAL CHANGE

NEW OWNERSHIP
Even relatively benign ownership changes, which impact personnel key to ACERA's portfolio management may be cause for a Watchlist status.

TURNOVER
Significant turnover in top management, portfolio Managers, research or trading staff, or marketing personnel, which does not directly affect the team responsible for ACERA's account may warrant Watchlisting.

REORGANIZATION
Changes which signal management deterioration**,** departures of key investment personnel, a change in ownership that increases risk to ACERA's investments, or hasty /uncontrolled growth in the firm with potential to disrupt the investment team hired for management of ACERA's account will mandate Watchlisting.

ASSETS UNDER MANAGEMENT
If the market value of ACERA's portfolio rises above 25% of the Manager's total assets under management, Watchlist status may be warranted.

D. COMPLIANCE

CONTRACTS AND OTHER AGREEMENTS
Managers are expected to comply with the investment management contract, investment guidelines, or other directives. Non- or partial compliance may result in a Watchlist status.

REPORTING
Staff will contact Managers to request past due reports. If the Manager's reports are consistently delinquent, the payment of fees may be delayed. If a Manager cannot comply with reporting deadlines, ACERA should be given prior notification. If warranted, a variance may be allowed. Managers are expected to resolve reporting problems immediately upon notification by ACERA. Repeated delinquency in reporting may result in a Watchlist status.

E. CLIENT SERVICE

If a Manager is uncooperative and demonstrates a poor client service attitude, Watchlisting is appropriate. Managers are expected to resolve client service issues immediately upon notification by ACERA.

PROBATION

Probation indicates a level of serious deficiency and signals a need for closer contact with the firm. Probation necessitates a cautious, observant relationship with the Manager.

Managers may be placed on Probation with or without first being placed on Watchlist status. The Probation period is typically one year.

The following may result in Probation:

A. UNDERPERFORMANCE

Please refer to Schedule II for specific Probation criteria for each Manager.

B. STYLE DEVIATION

Probation may be warranted when a Manager's portfolio characteristics are significantly different from its contractually specified style. In general, a Manager will be placed on Probation after four or more consecutive quarters of deviating from its style benchmark. In effect, if the Manager is no longer the same Manager that was retained for ACERA's account, Probation and perhaps even Termination is appropriate.

C. ORGANIZATIONAL CHANGE

Changes in ownership, organizational assignments**,** departures of key investment personnel, a change in ownership that poses substantial risk to ACERA's investments, or turnover that have the potential to seriously disrupt or destroy the investment management team that was hired to manage the ACERA account may result in Probation or Termination. When key personnel, such as top management, portfolio Managers, research and trading staff are no longer available for use on the ACERA portfolio and do not appear to be replaced or replaceable, Probation and perhaps even Termination is appropriate.

D. COMPLIANCE

If a Manager does not comply with securities laws, industry regulations, standards of professional conduct or contractual provisions, Probation is appropriate. Certain circumstances may warrant Termination.

E. CLIENT SERVICE

Failure to correct any issues that previously resulted in the Watchlist status may result in Probation. Managers will generally be given one quarter to resolve client service issues.

TERMINATION

Upon determining that the Manager has not made adequate improvement in the areas outlined in the Plan of Action, Staff may recommend to the Investment Committee and/or Board that the Manager be terminated. Prior to making the final decision to terminate the Manager, the Investment Committee may invite the Manager to make a presentation at the meeting in which the Termination recommendation is to be discussed. Staff will have analyzed the liquidity of the Manager's portfolio and will have a recommendation and plan for disposition of the assets.

Upon the Investment Committee's decision to terminate, Staff will notify the accounting division as well as the Board's legal counsel of the action. All outstanding issues between the Manager and ACERA's master Custodian, brokers, consultant, or other parties shall be resolved prior to closing out the contract. The Manager Termination checklist is attached as Schedule IV.

The Contract Review Process described in this Policy does not provide any additional rights or protections to Managers, beyond what is provided in the contract. ACERA reserves the right to terminate an investment management contract without resort to the Contract Review Process, at any time, with or without 30 days notice, for any reason.

SCHEDULE I

ACERA

ASSET ALLOCATION AND MANAGER STRUCTURE TARGETS

ASSET ALLOCATION TARGETS

Asset Class	**Target Allocation**
U.S. Equity	39
International Equity	22
Total Equity	61
Fixed Income	30
Real Estate	9

MANAGER STRUCTURES TARGETS

Managers		**Target Allocation**
U.S. Equity		
Large Cap Core Index	BoNY S&P 500	50
Large Cap Growth (Hi-Alpha)	TCW	17.5
Large Cap Value (Hi-Alpha)	PFR	17.5
Large Cap Enhanced Core (Hi-Alpha)	Salus	5
Small Cap Growth	Next Century Growth	5
Small Cap Value	Brandywine	5
Non-U.S. Equity		
Core Non-US Equity (growth)	Capital Guardian	60
Core Non-US Equity (value)	Delaware	40
Fixed Income		
Aggressive Core Plus	Loomis Sayles Boston	29
Global Bond	Brandywine	16
Enhanced Index	Baird	55

SCHEDULE IA

ACERA

ASSET ALLOCATION PORTFOLIO REBALANCING

The objective of rebalancing is to control risk and enhance the risk-adjusted return of the asset allocation strategy. For purposes of enhancing the risk-adjusted return of the asset allocation structure, the relative deviation of any liquid sub asset class away from its target weight (or liquidity-adjusted target weight) shall be no more than plus or minus 1.7 standard deviation factors of each allocation's expected volatility, relative to the other allocations in the asset mix. This standard deviation factor shall be used to define the range of allowable deviation from Policy target asset allocations. If any sub asset class reaches its allowable deviation from its target allocation, all sub asset classes will be evaluated.

The actual reallocation will be at the discretion of ACERA's staff (with oversight by the rebalancing consultant) after reviewing: the relative magnitude of deviation from target for all other sub asset classes; the available cash liquidity of sub asset classes that could be used to fund rebalancing; pending cash flows (employer and employee contributions, or proceeds from a terminated manager's portfolio); pending liquidity windows with commingled investment pools; pending investment commitments (real estate transactions and/or new funding commitments); and, pending interest coupon and dividend cash flows.

Asset allocation and rebalancing status reports, and any rebalancing activity taken toward attaining the objective of the rebalancing program will be reported to the Board of Trustees in a timely fashion or whenever a rebalancing transaction occurs.

Significant modifications to the asset allocation strategy shall be cause to review the appropriateness of maintaining this rebalancing parameter or revising it to a parameter more suitable to the revised asset allocation structure.

SCHEDULE II

ACERA

Watchlist/Probation Criteria for Performance

(Footnote: If Plan history with Manager is less than 5 years, use rolling 3 year period)

Watchlist Criteria	**Probation Criteria**
US Equity • Large Cap Core Index: negative tracking error exceeds 5 bps on an annualized basis in any 1 year period. • Large Cap Growth: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters. • Large Cap Value: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters. • Small Cap Growth: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters. • Small Cap Value: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters. • Large Cap Enhanced Core: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters.	**US Equity** • Large Cap Core Indexed: negative tracking error exceeds 5 bps in any 1 year period; or negative tracking error exceeds 10 bps for 2 quarters. • Large Cap Growth: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters. • Large Cap Value: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters. • Small Cap Growth: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters. • Small Cap Value: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters. • Large Cap Enhanced Core: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters.

Watchlist Criteria	Probation Criteria
International Equity • Core Non-US Equity (growth): cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters • Core Non-US Equity (value): cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters.	**International Equity** • Core Non-US Equity (growth): cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters. • Core Non-US Equity (value): cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters.
Fixed Income • Aggressive Core Plus: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters. • Global Bond: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters. • Enhanced Index: cumulative 1 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters.	**Fixed Income** • Aggressive Core Plus: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters. • Global Bond: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters. • Enhanced Index: cumulative 1 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters.

SCHEDULE III

ACERA

POLICY INDEX FOR TOTAL FUND AND
BENCHMARKS FOR ASSET CLASSES, EQUITY AND FIXED INCOME MANAGERS

POLICY INDEX FOR TOTAL FUND

39% Russell 3000 / 23% Lehman Aggregate / 4% Citigroup World Government Bond Ex. U.S. / 3% Lehman High Yield / 22% MSCI All Country World Index Ex. U.S. / 9% NCREIF Property Index

BENCHMARKS FOR ASSET CLASSES

Asset Class	**Benchmark Index**
U.S. Equity	Russell 3000
International Equity	MSCI ACWI-Ex. U.S.
Total Equity	N/A
Fixed Income	Lehman Aggregate U.S./Citigroup World Government Bond Ex U.S. /Lehman High Yield in the ratio of 75/15/10
Real Estate	NCREIF

BENCHMARKS FOR EQUITY AND FIXED INCOME MANAGERS
(Please refer to individual Manager's contract for expected annual premium)

Manager	**Benchmark**
U.S. Equity	
BoNY S&P 500	S&P 500
TCW	Russell 1000 Growth
PFR	Russell 1000 Value
Salus	S&P 500
Next Century Growth	Russell 2000 Growth
Brandywine	Russell 2000 Value
Non-U.S. Equity	
Capital Guardian	MSCI ACWI-Ex. U.S.
Delaware	MSCI ACWI-Ex. U.S.

Manager	**Benchmark**
Fixed Income	
Loomis Sayles Boston	Lehman Brothers Baa Credit Index
Brandywine (Global Bond)	Citigroup World Government Bond Index Ex U.S.
Baird	Lehman Aggregate

SCHEDULE IV

ACERA

MANAGER TERMINATION CHECK-LIST

This checklist is used to ensure that all details are covered when terminating investment management services.

1) Officially notify the manager in question of the Board's decision to terminate.

2) Establish plan of action for reallocation of assets from terminated portfolio; transfer to other portfolios or prepare for liquidation.

3) Review department files and logs to identify any outstanding issues.

4) Notify ACERA Administration, Accounting Division, Legal Counsel, consultant, master Custodian and any other vendors of the Termination. Identify and resolve all outstanding issues with these parties.

5) Have Manager and master Custodian review and sign off on monthly market values and performance figures produced during the contract period.

6) Hold payment of last invoice until all issues are resolved.

7) Retain terminated Manager files in the ACERA office for a minimum of one year; then send to ACERA archives.

8) Hold terminated Manager files in ACERA archives for a minimum of 5 years.

SCHEDULE V*

ACERA

Compliance Schedule

REQUEST	**DUE DATE**
MONTHLY	
Soft Dollar Commission Report (If applicable) (Submit each month regardless of whether any commissions were directed – consultants and master Custodian are subject to this request)	By the 20th of the month following the reported month
Minority Broker Commission Report (Submit each month regardless of whether any commissions were directed)	By the 20th of the month following the reported month
Accounting Report / Portfolio Valuation** (Please provide transaction data – buys/sells, a portfolio listing including cost & market values, and performance returns)	By the 20th of the month following the reported month
Derivative Report (If applicable) (Please check ACERA's Investment Policy for report guidelines.)	By the 20th of the month following the reported month
Confirmation that monthly reconciliation with Bank is performed. (Reconciliation should include market values, transactions and performance.)	By the 20th of the month following the reported month

* This Schedule is designed for all investment managers of ACERA. However, managers may be required to provide additional compliance reports based on their individual investment agreements with ACERA. Should there be any conflict between individual investment agreements with ACERA and ACERA investment guidelines, policies and procedures, the individual investment agreements should prevail.

** Please provide 20 copies of this report.

REQUEST	DUE DATE
QUARTERLY	
Fee Billings (Provide all backup documentation/ reconciliation sign-offs/ DVBE Expenditure Report & backup invoices)	Within 30 days following the end of the quarter
Confirmation of compliance with limitations on investment vehicles and investment markets.*	Within 30 days following the end of the quarter
Confirmation of compliance with % limitations on cash holdings, on equity investment and on fixed-income investment. *	Within 30 days following the end of the quarter
Confirmation that ACERA's assets under management does not exceed 25% of the total assets under management firm-wide.	Within 30 days following the end of the quarter
Market and Portfolio Analyses and Commentaries**	Within 30 days following the end of the quarter
QUARTERLY – applicable to Real Estate Program	
Operations Report** (Refer to Real Estate Policy for details)	Within 60 days following the end of the quarter
ANNUAL	
Annual Performance Fee Billing (If Applicable) (Provide all backup documentation/ reconciliation sign-offs)	Within 30 days following the end of the performance fee period

* Please refer to the Specific Investment Guidelines of each manager's investment contract for details.

** Please provide 20 copies of this report.

REQUEST	DUE DATE
Organization Chart	Within 30 days following the end of the year or as soon as updated, whichever is earlier
Fidelity Bond/ Errors & Omissions Insurance (Please send an original certificate)	Within 30 days of renewal
Audited Financial Statements	Within 90 days following the end of the year
Form ADV, Parts I and II (If applicable)	Within 30 days of filing
Statement or Summary of Code of Ethics	Within 30 days of any change
SEC Examination Reports	Within 30 days of receipt

ANNUAL – applicable to Real Estate Program

Tactical Plans***	Within 30 days of completion
Asset Management and Budget Plan***	Within 30 days prior to fiscal year end
Variance Report on Appraised Properties (if applicable) (Refer to Real Estate Policy for details)***	Within 30 days of final property appraisal
Audited Financial Statement for ACERA's Fund *** (Applicable to Individually Managed Account)	Within 90 days following the end of the year
Property Valuation for Each Asset*** (Applicable to Individually Managed Account)	Within 90 days following the anniversary date of asset acquisition

*** Please provide 5 copies of this report.

SCHEDULE VI

ACERA

INVESTMENT PHILOSOPHY (REVISED MAY 2001)

The following document describes the investment philosophy of the Alameda County Employees' Retirement Association (ACERA). Its purpose is to enunciate the basic principles and beliefs that will underlie ACERA's investment policy and impact the overall management of the pension fund. The Investment Philosophy is designed to complement rather than replace the specific investment policies of the Association. It is expected that the Association's approach to investments, as reflected in its policies and strategies, will be consistent with the philosophy over time. Though the philosophy allows significant flexibility, it also raises some constraints or implications. Where these were deemed to be significant, they have been explicitly identified and labeled as *Implications*.

Future boards may choose to amend the investment philosophy, as their experiences and circumstances will almost certainly differ. The initial document, and any subsequent changes will provide staff, advisors and future trustees with a frame of reference to help them understand how the investment program has evolved as well as the rationale behind its design. Future boards may modify the philosophy as their experiences and circumstances suggest is prudent.

The major sections of the philosophy are:

1. Mission
2. Risk Management
3. Diversification
4. Market Efficiency
5. Hi-Alpha Managers
6. Organizational Infrastructure and Communications

7. Performance Monitoring and Time Horizon

1. MISSION

a) The Board's primary goals in managing the Fund are:

   i) To ensure that sufficient funds are available to pay vested benefits and maintain supplemental benefits;
   ii) To comply with all applicable fiduciary standards; and,
   iii) To create value added, where feasible, that will help reduce the costs of the plan, increase benefits, or both.

2. RISK MANAGEMENT

a) The Board believes that prudent management of risk is a central element of the investment function.

b) Though there are numerous risks involved in the management of a pension investment program, ACERA believes that the following warrant particular attention:

   i) ***Funding-related Risk*** - The risk that the funds available in the Plan will be insufficient to pay the promised benefits, both vested and supplemental; or that contribution volatility will be unacceptably high. The primary methods for managing funding risk include regularly conducting integrated asset/liability studies, and establishing appropriate and prudent investment and funding policies.

      0.1 In managing the relationship between assets and liabilities, the approved asset allocation of the Fund should provide a minimum of a 90% level of certainty of meeting the projected liabilities of the Plan over a 20 year time period, as determined by the actuary.

ii) ***Benchmark related Risk*** – The risk that the investment benchmarks adopted by the Fund are inappropriate, or that the aggregate of the individual manager benchmarks within an asset class do not adequately reflect the benchmark for the asset class as a whole. The latter risk is a specific risk generally referred to as *benchmark misfit risk (i.e. style risk)*. Inappropriate benchmarks or excessive benchmark misfit risk could result in investment performance different than expected and could adversely impact decisions concerning the hiring or firing of investment managers.

0.1 The primary methods for effectively managing benchmark-related risk are:

(a) regular review of the Fund's benchmarks; and

(b) regular measurement and monitoring of misfit risk using proper methodologies.

iii) ***Manager Risk*** - The risk of aberrant performance on the part of individual investment managers, and the related active management risk for asset classes as a whole.

0.1 The primary methods for mitigating manager risk are:

(a) Prudent processes for selecting and monitoring investment managers;

(b) Competent internal investment staff;

(c) Effective investment consulting support; and,

(d) Clear communication to investment managers of ACERA's objectives, expectations, and investment time horizons.

0.2 The primary method for mitigating active management risk for asset classes include:

(a) Establishment of appropriate asset class benchmarks;

(b) Careful monitoring of asset class performance relative to the benchmarks; and

(c) Prudent use of passive management.

iv) ***Fortitude Risk*** - The risk that the board or staff will fail to exercise the patience, judgment, or fortitude required to support long-term policies and strategies for the investment and funding program.

0.1 The keys to managing fortitude risk are believed to include:

(a) Effective orientation and education with respect to institutional investing and actuarial science; and,

(b) A commitment to continually refining, confirming and communicating the investment philosophy and funding policy of the Association.

3. DIVERSIFICATION

a) ACERA acknowledges the basic tenets of modern portfolio theory, which suggest that diversification, or combining assets that are not perfectly correlated with each other, will reduce the long-term volatility of the overall portfolio.

b) It is generally desirable however to avoid overly complex asset structures, provided the allocation selected can reasonably be expected to meet the objectives of the Plan. ACERA believes that the benefits of diversification must be weighed against the costs involved, which may include fees, liquidity, complexity, communication, internal staff resources and expertise and trustee knowledge and effort.

c) The following asset classes are appropriate candidates for inclusion in its portfolio:

i) Domestic equity

ii) International equity (including emerging markets)

iii) Fixed income, including high yield fixed income and international fixed income

iv) Real estate

d) ACERA does not consider alternative investments to be an appropriate candidate for inclusion in its portfolio due to the substantial direct and indirect costs associated with it.

Implications

- A systematic methodology for re-balancing the investment portfolio is required to ensure proper implementation and adequate risk control concerning ACERA's asset allocation.
- Adding or deleting asset classes or investment managers should be considered in light of the impact such decisions are likely to have on the general complexity and cost structure of the portfolio, as well as ACERA's ability to prudently achieve its investment and funding goals over the long run.

4. Market Efficiency

Except for specified high alpha assignments:

a) ACERA does not believe in the viability of active management strategies that rely on market timing.

b) ACERA does not believe in the viability of management strategies that call for over weighting or under weighting styles or sectors within an asset class; i.e. benchmark misfit risk will not generate long-term alpha. Accordingly, ACERA generally believes that it should maintain exposures within an asset class (such as style or capitalization weightings) that are consistent with the broad benchmark for the asset class as a whole.

c) ACERA does believe that market efficiency varies among asset classes, creating opportunities for successful active management strategies based on securities selection.

d) Asset classes that can be demonstrated to be efficient should be managed passively in order to reduce active management risk and lower the costs of managing the portfolio.

e) For inefficient asset classes, ACERA believes that it has the ability and a duty to prudently exploit such inefficiencies through active securities selection strategies.

Implications

- ACERA should be conscious of any subtle forms of market timing that may arise in the course of managing the fund, or that may be implicit in investment strategies presented to ACERA for inclusion in the investment program.

- ACERA must determine appropriate methodologies for determining whether an asset class is efficient or presents appropriate opportunities, thus providing insight to the Board on the use of particular strategies.

5. HIGH ALPHA MANAGERS

a) ACERA believes that the portfolio characteristics utilized to control risk in the broad portfolio, such as market capitalization, sector exposure, use of derivatives, leverage limitations, property type or deal structure may be modified for specific managers who control a limited portion of the portfolio and have demonstrated a proven capacity to consistently add value net of fees. Such strategies, which ACERA refers to as Hi-Alpha, may include the following elements:

   i) The bulk of the asset class is passively managed or risk controlled; and,

ii) A small number of active managers are retained who employ somewhat more aggressive investment strategies, such as concentrated portfolios, leveraged purchases, developments, high-yield debt, etc.

b) The primary benefits of including a Hi-Alpha approach within the overall portfolio are:
   i) Reduction in active management risk;
   ii) Lower average investment fees; and
   iii) Concentration on opportunities where the likelihood of adding value is greatest.

c) The market efficiency and opportunities in asset classes may change over extended periods of time; therefore ACERA believes that its portfolio management strategies should adapt over time to reflect the changing nature of capital markets.

6. ORGANIZATIONAL INFRASTRUCTURE AND COMMUNICATIONS

a) ACERA believes that in order for the investment program to achieve its goals, ACERA must invest the necessary resources to build and maintain an appropriate organizational infrastructure, key elements of which include:

   i) A competent, internal investment staff comprised of a sufficient number of investment professionals possessing appropriate leadership, technical and administrative skills.

      0.1 In attracting a competent staff, ACERA recognizes that it competes with the private sector. It must therefore continually strive to create a total work environment that is challenging, rewarding, and competitive.

   ii) A strong relationship with outside general investment consultant(s) who are able to provide ACERA with the following:

0.1 A high degree of investment expertise;
0.2 Innovative and proactive advise and counsel;
0.3 Strong research support; and
0.4 Strong reporting capabilities,

iii) A broad-based information gathering and reporting system to present well- researched, relevant and timely data in a manner that is easily understood, and that supports rigorous and consistent monitoring of critical investment activities.

iv) An open channel of communication between the Board, management, and the Association's external investment professionals.

b) By providing the Board with timely, accurate, and thorough information, the organizational infrastructure will give the Board the high level of comfort it needs to set policy, make investment decisions, oversee the performance of the investment program, and maintain the fortitude necessary to support its investment philosophy, policies and strategies.

Implications

- ACERA must determine what constitutes an appropriate internal investment staff structure, given the nature of the current investment program.

- ACERA must over time take concrete steps towards creating a work environment that will allow the Association to attract and retain needed staff.

- ACERA must recognize that developing the organizational infrastructure it needs – staffing, consulting support, information systems, and communication channels – cannot be achieved overnight, but rather will require an ongoing commitment of time and resources.

7. Performance Monitoring & Time Horizon

a) ACERA holds the following basic beliefs concerning performance monitoring practices and methodologies:

i) The various investment policies of the Fund, in the aggregate, are the most important determinants of investment success; compliance with investment policies should therefore be monitored rigorously;

ii) The performance of the total portfolio, individual asset classes, and investment managers should be compared to appropriate, predetermined benchmarks;

iii) Peer comparisons are an additional valid tool in assessing individual manager performance (supplementing the use of benchmarks), given that ACERA aims to select superior managers within particular investment styles or mandates. Peer comparisons, or performance rankings, are also valid tools for measuring the performance of asset class portfolios.

iv) Peer group comparisons are not an appropriate means of assessing the performance of the total fund, given that sponsors have different objectives and risk tolerance levels, and therefore may have different asset allocation policies.

v) Benchmark misfit risk, or the risk that the aggregate of individual investment manager benchmarks in an asset class do not adequately reflect the benchmark for the asset class as a whole, should be explicitly measured on a regular basis.

vi) Investment managers are generally hired to fulfill a specific role in a portfolio. Accordingly, ACERA believes it is important that ACERA monitor the extent to which managers comply with their stated style and mandates.

b) ACERA believes that successful funding and investment decisions require a long-term perspective on the part of the Board and management:

i) It is the intention of the Retirement Board that commitments to asset classes and investment strategies should involve long time horizons that may include more than one business cycle (3-5 years each). Relatively illiquid asset classes may require even longer time horizons.

ii) The Board acknowledges that commitments to individual investment managers also require a long time horizon of at least one business cycle (3-5 years).

iii) ACERA believes that proper reporting and monitoring systems; and clear communication among consultants, management, investment managers and the board will enable the Board to maintain the necessary long term perspective on all investment decisions.

<u>Implications</u>

- Assessing the investment performance relative to appropriate, pre-determined, benchmarks is as applicable to the total portfolio and to individual asset classes as it is for individual investment managers, and therefore warrants a commensurate share of the Board's time and attention.

- The Board will spend relatively little time assessing the performance of the Fund relative to that of comparable pension funds.

- ACERA will need to either develop in-house capabilities to regularly measure benchmark-related risk, or it will need to purchase such capabilities from external investment consultants.

- ACERA will monitor all investment managers to ensure they are complying with their stated investment style, regardless of whether they are performing well or poorly. Strongly performing managers who are found to not be following their stated styles will be carefully scrutinized and may be subject to disciplinary action.

- ACERA will monitor all investment providers to ensure compliance with the Board's Investment Policies.

SCHEDULE VII

ACERA

TABLE OF AMENDMENT DATES

AMENDING RESOLUTIONS

Jun	27,	1985
Oct.	10,	1985
Jan.	9,	1986
Jan.	16,	1986
Mar.	13,	1986
May	22,	1986
Sep.	11,	1986
Oct.	9,	1986
Nov.	20,	1986
May	14,	1987
Aug.	13,	1987
Oct.	8,	1987
Apr.	21,	1988
July	28,	1988
Jan.	29,	1989(4)
Apr.	13,	1989(5)
May	18,	1989
July	13,	1989
Aug.	10,	1989
Nov.	16,	1989(2)
July	11,	1991
June	11,	1992
June	10,	1993
July	8,	1993
Nov.	18,	1993
May	14,	1994
Aug.	18,	1994
Nov.	20,	1994
Feb.	16,	1995
May	18,	1995
Jan.	16,	1997
Aug.	20,	1998
May	20,	1999
Jan.	31,	2000
Apr.	19,	2001
Jul.	18,	2002
Feb.	21,	2003
Feb.	19,	2004

Alameda County Employees'
Retirement Association

ACERA

GENERAL INVESTMENT GUIDELINES, POLICIES AND PROCEDURES

AMENDED February 17, 2005

ACERA
GENERAL INVESTMENT GUIDELINES, POLICIES AND PROCEDURES
2005

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SECTIONS	**PAGE**

[1] Prepared for ACERA by Cortex Consulting; Adopted by the Board of Retirement on March 8, 2000; Revised May 2001.

ACERA
GENERAL INVESTMENT GUIDELINES, POLICIES AND PROCEDURES

SECTION I: MISSION AND PURPOSE

The Alameda County Employees' Retirement Association (ACERA) exists for the purposes of providing accurate, timely benefits to its members and their beneficiaries and defraying reasonable expenses of administration.

The Board of Retirement (the Board), having exclusive authority and exclusive fiduciary responsibility for the investment and administration of the Trust Fund (the Fund), hereby establishes the following "General Investment Guidelines, Policies and Procedures" (the Policy) for the investment of ACERA's assets. The Board reserves the right to amend, supplement or rescind this Policy at any time.

The Board of Retirement is directed by law and given discretion to prudently invest the retirement plan assets. The purpose of this statement of policy is to assist ACERA in effectively supervising said investments and to encourage effective communication between ACERA and its managers and Consultants.

ACERA's investment goal is to operate at a level of performance in the upper quartile of comparable pension funds on a risk-adjusted basis and to be as fully funded as possible so that ACERA's benefit costs do not become a burden upon future generations of members and taxpayers.

SECTION II: CONSTITUTIONAL REQUIREMENTS

Article 16 §17 of the California State Constitution provides in pertinent part as follows:

"Notwithstanding any other provisions of law or this Constitution to the contrary, the retirement board of a public pension or retirement system shall have plenary authority and fiduciary responsibility for investment of money and administration of the system, subject to the following:

a. The retirement board of a public pension or retirement system shall have the sole and exclusive fiduciary responsibility over the assets of the public pension or retirement system. The retirement board shall also have sole and exclusive responsibility to administer the system in a manner that will assure prompt delivery of benefits and related services to the participants and their beneficiaries. The assets of a public pension or retirement system are trust funds and shall be held for the exclusive purposes of providing benefits to participants in the pension or retirement system and their beneficiaries and defraying reasonable expenses of administering the system.

b. The members of the retirement board of a public pension or retirement system shall discharge their duties with respect to the system solely in the interest of, and for the exclusive purposes of providing benefits to participants and their beneficiaries, minimizing employer contributions thereto, and defraying reasonable expenses of administering the system. A retirement

board's duty to its participants and their beneficiaries shall take precedence over any other duty.

c. The members of the retirement board of a public pension or retirement system shall discharge their duties with respect to the system with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with these matters would use in the conduct of an enterprise of a like character and with like aims.

d. The members of the retirement board of a public pension or retirement system shall diversify the investments of the system so as to minimize the risk of loss and to maximize the rate of return, unless under the circumstances it is clearly not prudent to do so.

e. The retirement board of a public pension or retirement system, consistent with the exclusive fiduciary responsibilities vested in it, shall have the sole and exclusive power to provide for actuarial services in order to assure the competency of the assets of the public pension or retirement system.

f. With regard to the retirement board of a public pension or retirement system which includes in its composition elected employee members, the number, terms, and method of selection or removal of members of the retirement board which were required by law or otherwise in effect on July 1, 1991, shall not be changed, amended, or modified by the Legislature unless the change, amendment, or modification enacted by the legislature is ratified by a majority of the electors of the jurisdiction in which the participants of the system are or were, prior to retirement, employed.

g. The Legislature may by statute continue to prohibit certain investments by a retirement board where it is in the public interest to do so, and provided that the prohibition satisfies the standards of fiduciary care and loyalty required of a retirement board pursuant to this section.

h. As used in this section, the term "retirement board" shall mean the board of administration, board of trustees, board of directors, or other governing body or board of a public employees pension or retirement system; provided, however, that the term "retirement board" shall not be interpreted to mean or include a governing body or board created after July 1, 1991, which does not administer pension or retirement benefits, or the elected legislative body of a jurisdiction which employs participants in a public employees pension or retirement system."

SECTION III:
ELIGIBLE ASSET CATEGORIES

The Fund shall hold assets in categories established by the Board. Any asset category may be held in direct form, in pooled form, or in both. Asset categories managed by one or more "Qualified Investment Managers" (Manager(s)) are called "Managed Accounts." Asset categories under the supervision of the County Treasurer are called the Treasurer's Accounts. Eligible asset categories are listed and defined below.

A. **CASH** shall consist of short term (12 months or less) interest bearing investments of high quality such as U.S. Treasury issues, insured certificates of deposit of U.S. banks (fixed and/or variable), commercial paper rated A-1, P-1 or both, or other instruments of equal or better quality, and includes money market funds available through the Custodian Bank (Custodian).

B. **U.S. EQUITY** shall consist of common stocks and other securities which are convertible into common stocks, and ADRs (American Depository Receipts), as well as cash (per "A" above) and fixed income (per "D" below) when used as temporary substitutes for common stocks.

C. **INTERNATIONAL EQUITY** shall consist of common stocks and other securities convertible into common stocks of companies domiciled outside of the U.S., and GDR's (Global Depository Receipts), as well as cash equivalents and fixed income, domestic or international, which are being used as temporary substitutes for common stock.

D. **FIXED INCOME** shall consist of investments in U.S. taxable bonds, debentures, notes and other evidences of debt. Fixed income may also include non-dollar denominated bonds issued by corporations or governments domiciled outside of the United States of America as well as Brady Bonds. Other eligible investments include cash equivalents per "A" above and convertible bonds and preferred stock.

E. **REAL ESTATE** shall consist of investments in U.S. real estate and equity real estate through the use of commingled or direct investments. For more information about real estate investments, refer to ACERA's "Real Estate Investment Policy," which is maintained as a separate document.

SECTION IV: INVESTMENT PHILOSOPHY

The following is a summary of ACERA's investment philosophy. For the complete statement, please refer to Schedule VI of this document, "ACERA Investment Philosophy."

The Board believes that its investment policies, in aggregate, are the most important determinants of its investment success. Compliance with investment policies should, therefore, be monitored rigorously. The Board also believes that performance of the total portfolio, individual asset classes, and Managers should be monitored and compared to appropriate, predetermined benchmarks.

The Board believes that prudent management of risk is a central element of the investment function and that diversification among asset classes will reduce risk and enhance returns of the overall investment portfolio in the long term.

The Board believes that market efficiency and opportunities vary among asset classes and may change over extended periods of time; therefore, the Board believes that ACERA's portfolio management strategies should adapt over time to reflect the changing nature of capital markets.

The Board's primary goals in managing the Fund are

1. To ensure that sufficient funds are available to pay vested benefits and maintain supplemental benefits;
2. To comply with all applicable fiduciary standards; and
3. To add marginal value that will help reduce the costs of the plan and/or to increase benefits for the beneficiaries.

The Board believes that in order to achieve its goals, ACERA must invest the necessary resources to build and maintain an appropriate organizational infrastructure.

SECTION V: INVESTMENT STRATEGY

A. **U.S. EQUITY** will be structured to capture exposure to the broad U.S. equity market as represented by the Russell 3000 Index. Passively managed (index) portfolios will be used in markets that are reasonably efficient. These portfolios are intended to provide broadly diversified market exposure with controlled (market) risk and minimal cost.

Actively managed portfolios will be used in less efficient markets when the Board determines that a Manager possesses special skills or abilities that enable that Manager to capture excess returns relative to the market, adjusted for risk and fees; or to exploit specialty markets that provide enhanced return with acceptable risk.

A great part of the Russell 3000, on a market value basis, is comprised of large-cap stocks, which the Board believes are efficiently priced most of the time. Therefore, the Board has adopted a policy of obtaining overall exposure to this segment of the market via passively managed indexed products. Some active Managers have been employed to enhance overall portfolio return in the large- and/or mid-cap sectors on a risk- and fee-adjusted basis. These Managers manage ACERA's "High-Alpha" program.

The remainder of the Russell 3000 index is comprised of small to mid-cap companies. Some opportunities for active management enhancement exist in these securities due to market inefficiencies. ACERA will attempt to capture these opportunities through a mix of Managers who have the special skills required to identify smaller companies that may be undervalued or possess substantial growth potential.

The U.S. equity portion of the portfolio shall be allocated among the various styles and Managers as indicated in Schedules I and IA.

B. **INTERNATIONAL EQUITY** represents an opportunity to diversify risk and capture enhanced returns within markets generally less efficient than the U.S. domestic equity market. 100% of the international equity portion of the Fund will be invested in actively managed portfolios.

C. **FIXED INCOME** represents a means of reducing overall portfolio risk and capturing incremental returns either domestically or globally. Inefficiencies in the pricing and trading of fixed income securities create opportunities to add value through active management. 100% of the fixed income portion of the portfolio will be invested in actively managed portfolios.

D. **REAL ESTATE** will be used as a means for diversifying the portfolio and capturing additional returns due to the low correlation between returns on real estate and financial assets. Due to the illiquid nature of real estate assets, distinctions between active and passive management are not applicable. For more information regarding real estate investments, refer to ACERA's "Real Estate Investment Policy," which is maintained as a separate document.

SECTION VI: ASSET ALLOCATION AND REBALANCING

Asset allocation targets, a function of the returns and risks from various asset classes and the nature of the plan's liabilities, are set forth in Schedule I. A goal of asset allocation is balancing asset growth versus liability growth considering time horizons, liabilities and risk tolerance.

Rebalancing is the risk control process of returning an allocation back to the desired target level after having drifted away from its targeted position. Equal probability bands, as defined by standard deviation factors that shall be used to define the acceptable ranges around the asset allocation targets are set forth in Schedule IA. The objective of rebalancing is to enhance the risk-adjusted performance of the asset allocation structure.

ACERA Staff (Staff) shall be responsible for maintaining the relative weights of asset classes and allocations within the acceptable rebalancing ranges as reflected in Schedule IA. Should an asset class or allocation fall outside its target range, Staff shall rebalance the asset class or allocation back to the target weights as specified in the asset allocation structure in Schedule I.

Staff shall

1. Monitor the portfolio;
2. Determine whether or not any asset category is out of balance with its target asset allocation in excess of the specified tolerance range;
3. Determine whether or not any Manager within each asset category is out of balance with their target allocation in excess of the specified tolerance range;
4. And, if this is determined, either
   (a) instruct the relevant Managers to redirect cash income (interest coupon and dividends) in concert with an evaluation of pending commitments and other cash flows (employer and employee contributions), in order to bring the allocation(s) back to the adopted strategic target; or
   (b) instruct the relevant Managers to liquidate or acquire the appropriate dollar value of securities to reach the target and reallocate the cash thus generated or required to the other category(s) or Manager(s), as necessary.

Staff shall report to the Board on a regular basis the status of the Fund with respect to how categories are tracking relative to their allowable ranges, as well as any actions taken to rebalance the portfolio.

SECTION VII:
ASSET CATEGORIES OBJECTIVES

The general objective of the Board is to preserve capital and to earn a return from appreciation and income, as described herein:

1. To ensure the integrity of ACERA's actuarial funding plan, one minimum return objective for the Fund shall be the current actuarial interest assumption rate plus 25 basis points per year over a market cycle. Returns shall be calculated net of fees.

2. To ensure that ACERA's assets grow appropriately to match salary increases which directly impact benefit levels, an additional minimum return objective for the Fund over a market cycle (up to five years) shall also be 400 basis points (4%) per year over the national Consumer Price Index, published by the U.S. Department of Commerce. Returns shall be calculated gross of fees.

3. To ensure that ACERA's external investment manager structure, in aggregate, is performing satisfactorily. An additional minimum return objective for the Fund over a market cycle (up to five years) shall also

be equivalent to the Fund's Policy Index on a gross of fee basis.

The objectives of each asset category are

A. CASH

1. A rate of return in excess of 90-Day U.S. Treasury bills.

2. A rate of return within the upper one half of a universe of like short-term funds.

B. U.S. EQUITY

1. A rate of return in excess of the U.S. equity market as measured by the Russell 3000 Index after adjustment for risk and fees.

2. A rate of return within the upper 33rd percentile of the Wilshire Co-op or similar database of the performance of diversified equity portfolios.

C. INTERNATIONAL EQUITY

1. A rate of return in excess of the Morgan Stanley Capital International All Country World Index Ex-U.S. Free (MSCI ACWI Ex-U.S.).

2. A rate of return within the top quartile of the Wilshire Co-op or similar database of the performance of diversified international equity portfolios.

D. FIXED INCOME

1. A rate of return in excess of the Lehman Aggregate Bond Index, Citigroup World Government Bond Ex. U.S. and Lehman High Yield in a ratio of 75/15/10.

2. A rate of return within the top quartile of the Wilshire Co-op or similar database of the performance of diversified fixed income portfolios.

E. REAL ESTATE

1. Total Return – a minimum total gross return equivalent to the National Council of Real Estate Investment Fiduciaries (NCREIF) Property Index (NPI) over rolling five-year periods.

2. Income Return – Income, which is defined as cash distributed to the Association, should comprise at least 2/3 of the total expected return over rolling five-year periods for all Stable (as defined in ACERA's "Real Estate Investment Policy") product.

In addition, objectives that reflect the particular investment strategy or style used by individual Managers shall be outlined in specific investment guidelines attached to the Manager's contract.

SECTION VIII: ALLOCATION OF CASH FLOW

Cash flow not needed for benefit payments or administrative expenses shall be allocated to Managed Accounts in a ratio that best funds the overall targeted asset allocation as reflected in Schedules I and IA.

If cash flow is insufficient for the payment of benefits or to cover administrative expenses, then Managed Accounts shall be debited in a ratio that best satisfies the target allocation shown in Schedules I and IA. Such debits, if necessary, will be carried out as needed and with timely notice to Managers to facilitate effective funds transitions and performance measurement.

For all planned investments which may not need to be funded immediately, a reserve may be budgeted and invested in appropriate accounts in accordance with the asset allocation targets until such moneys are required. Alternatively, Managed Accounts within "overfunded" asset classes may be called upon to provide the required moneys.

SECTION IX: PROHIBITED INVESTMENTS

Managers shall exercise prudent expert standards in defining prohibited investments. For example, prohibited investments include, but are not limited to, securities issued by the County of Alameda or any agency thereof.

SECTION X: DIRECTED BROKERAGE

ACERA does not engage in either directed commission arrangements or "soft dollar" transactions.

SECTION XI: DERIVATIVE INSTRUMENT USAGE POLICY

Exposure to risk by use of derivative instruments must be consistent with ACERA's overall investment policy as well as an individual Manager's specific investment guidelines. Derivatives shall not be used to establish a leveraged position (i.e., offsetting Cash positions must be maintained against all delayed settlement transactions).

SECTION XII: SELECTION OF INVESTMENT MANAGERS

The Investment Committee shall direct Staff and/or a Consultant to initiate searches for Managers. Staff and/or the Consultant shall research for qualified candidates and present a list of finalists to the Investment Committee for its approval. Upon approval of the list, the finalists shall be interviewed by Staff and the Consultant (if applicable). Staff and the Consultant (if applicable) shall evaluate the interviews, rank the finalists, and make a recommendation to the Investment Committee to hire one or more firms attaining the highest rankings in a publicly noticed meeting at which no less than five (5) Investment Committee members shall be present. It is possible that none of the firms will be recommended for hire.

These procedures are developed for the convenience and benefit of ACERA, and shall not bind ACERA or invalidate the selection of a Manager, if different processes are used subsequent to the promulgation of this Policy.

SECTION XIII: AUTHORITY OF INVESTMENT MANAGERS

Subject to the laws of the United States and the State of California, and to the terms and conditions of this Policy, Managers shall have full discretion to direct the purchase, exchange, sale and reinvestment of the assets of the Managed Accounts. The Board expects that Managers will recommend changes to this Policy when any part of this Policy appears to be at variance with overall market and economic conditions.

Managers shall place orders to buy and sell securities and, by notice to the Custodian, shall cause the Custodian to deliver and receive securities on behalf of the Fund. Managers shall, upon Board inquiry, report placement of ACERA brokerage such that the Board shall be assured commissions were placed for the sole and exclusive benefit of the Fund.

Separate account Managers shall not vote proxies. Proxies shall be voted by ACERA, via a proxy voting service vendor, in accordance with Board-established policies and procedure.

Securities lending shall be performed under the oversight of Staff, in accordance with Board-established policies and procedures.

SECTION XIV: INVESTMENT GUIDELINES FOR THE MANAGED ACCOUNTS

Individual Manager discretion shall be governed by the Investment Guidelines for the Managed Accounts as well as the "Specific Investment Guidelines" set out in the investment contract of each Manager. Should there be any conflict between the specific investment guidelines of an individual Manager and the Investment Guidelines for the Managed Accounts, the specific investment guidelines shall prevail.

A. GENERAL

1. All investments shall comply with all applicable laws of the United States and the State of California governing the investment of pension trusts.

2. All securities transactions shall be executed by reputable broker/dealers, banks, or the Custodian, and shall be on a best-price and best-execution basis, and shall be reported to ACERA as is called for elsewhere in this Policy.

3. All Managers shall refrain from investing in a tobacco producer investment opportunity when, in their expert opinion, an alternative non-tobacco producer investment opportunity is available that will satisfy the same ACERA portfolio guidelines, instructions and objectives for risk, return and diversification.

B. EQUITY

Managers have full discretion to invest solely in readily marketable and diversified equity securities as defined above subject to the following:

1. For Managed Accounts, no more than 10% of the value (at time of investment) of the account shall be invested in the securities of a single issuer.

2. ACERA shall not hold more than 10% of the equity securities of any issuer.

3. Equity securities shall possess value and quality corroborated by generally accepted techniques and standards of fundamental securities analysis.

4. Assets in a Managed Account not invested in equity securities shall be kept with interest in appropriate money market instruments, including any money market fund available through the Custodian.

5. A Managed Account shall be subject to ACERA's policy on derivatives.

6. All Managers shall endeavor to be fully invested in stocks at all times unless they have received specific authorization to the contrary from the Board. Cash holdings, as defined in this Policy, shall generally not exceed 5% of the portfolio on a market value basis.

C. FIXED INCOME

Managers have full discretion to invest solely in readily marketable and diversified securities including, but not limited to

1. Obligations of the U.S. and/or eligible foreign government's Treasuries.

2. Obligations guaranteed by agencies of the United States and/or eligible foreign governments.

3. Insured certificates of deposit and banker's acceptances of credit worthy banks.

4. Corporate and other evidences of debt. At least 80% of this debt must be rated by Moody's Investor's Services or by Standard & Poors.

5. Commercial paper and banker's acceptances of issuers rated P-1 by Moody's Investor's Service.

6. Or A-1 by Standard & Poors Corporation.

7. Excepting direct obligations of the U.S. and/or eligible foreign governments, and those explicitly guaranteed by the U.S. and/or eligible governments, no account shall hold more than 5%, at cost, of the obligations of any single issuer.

8. Fixed income derivative investments shall be in accordance with ACERA's derivative policy.

SECTION XV: SEPARATE ACCOUNT MANAGER SPECIFICATIONS

A. Managers must be registered as investment advisers under the Investment Adviser's Act of 1940, a bank (as defined in that Act) or an insurance company qualified to perform investment management services under state law in more than one state, including California. Unless an exception is granted by the Board, by accepting appointment as ACERA's Managers, Managers shall acknowledge that they are "Plan Fiduciaries" and "Qualified Investment Managers" as defined by the Employees' Retirement Income Security Act (ERISA) of 1974, (see or reference United States Code Title 29 Section 1001 et. seq..)

B. Managers shall maintain fiduciary insurance in the amount of 10% of the total assets managed in the ACERA account or $25 million, whichever is higher, unless the contract specifies otherwise.

C. Managers shall promptly notify ACERA of changes that occur in any of the following:

1. The investment strategy used in managing the subject product.
2. The key personnel involved in managing ACERA's account.
3. The ownership, key personnel, or organizational structure of the Manager's company.
4. The Manager company's financial condition.
5. The number of clients invested in the subject product.
6. The market value of the total assets managed in the subject product.

D. Managers shall promptly notify ACERAif they are subject to censure or disciplinary action by a regulatory agency.

E. Managers shall promptly provide to ACERA all required documents and reports as set forth in Schedule V – ACERA's Compliance Schedule.

F. Managers shall not make contributions, provide gifts, reimbursements of expenses or provide personal benefits exceeding $250 in the aggregate within any 12-month period to any Trustee, fiduciary, employee or Consultant of ACERA. Donations of educational conferences and similar events and benefits, including travel, meals and accommodations will be made to ACERA and not directed to individuals. The Board will determine whether to accept any donations and will be solely responsible for selection of the Trustee, Staff, or other individual, who will attend or otherwise participate on behalf of ACERA.

SECTION XVI: MANAGER MONITORING POLICY

The ACERA Board has contracted with a number of external Managers to invest ACERA assets in the capital markets. As part of the Board's fiduciary duties to prudently select, monitor and supervise these Managers, the Board has adopted this Policy. The intent of this Policy is to notify Managers of the standards by which they will be judged and to establish a structure which the Investment Committee and the Board can use to monitor the performance of the Managers.

Managers will be monitored to

1. Evaluate how well they achieve their investment objectives.
2. Ensure that they adhere to their established investment approach/style and do not attempt to index returns to preserve stellar performance or take extraordinary risk to overcome poor performance.
3. Identify issues or trends that have the potential to result in losses to the Fund.
4. Alert the Board when Managers are not performing to expectations so that appropriate remedial action can be taken.

Managers will be evaluated on the basis of the following: performance, style integrity, organizational stability, compliance, and client service described in greater detail below.

A. PERFORMANCE

On a monthly basis Staff will monitor Manager holdings, activity and performance.

On a quarterly basis Staff and/or a Consultant will furnish the Investment Committee and/or Board with an in-depth evaluation of each Manager which will include a comparison of the Manager to its contract benchmark and a peer universe of Managers using a similar investment style. This report shall include an analysis of the sources of Managers' returns (stock selection, industry selection, asset allocation, etc.) and shall identify which decisions enhanced or diminished performance.

On a quarterly basis, trading costs will be evaluated in terms of commissions paid and execution of trades. Staff and/or Consultants shall furnish a report to the Investment Committee and/or Board regarding trading costs on an annual basis.

B. STYLE INTEGRITY

Each Manager will be analyzed at least annually to ensure that the Manager is continuing to invest the portfolio in the style for which they were originally hired. Style integrity is essential to maintain the Board's asset allocation policy. Any significant deviation in style will result in the overall portfolio having a different characteristic, in some measure, from the broad market which is represented by the Russell 3000 index. Significant variations in the portfolio characteristics from the style anticipated in the management contract may indicate a change in its investment style.

This review also provides the Investment Committee and/or Board an opportunity to evaluate the Manager's continuing "fit" with the goals of the overall Fund. By monitoring Manager style the Investment Committee and/or Board can assure that its Manager mix takes advantage of opportunities to increase diversification through lower correlation of returns among individual Managers.

C. ORGANIZATIONAL STABILITY

Managers' organizations will be monitored to ensure continuity of the intellectual and philosophical processes that went into developing the particular investment approach contracted for by ACERA. In addition, Managers will be monitored for business risk, quality of staff, departures of key investment personnel, change in ownership or acquisition, and potential conflicts of interest.

It is ACERA's intent that its portfolio comprises no more than 25% of the Manager's total assets under management at any time. Therefore, ACERA will monitor the Managers' assets, firm-wide, as well as in the subject product.

D. COMPLIANCE

Managers will be monitored to ensure they are adhering to federal and state laws regarding securities and the management of investment portfolios, trading, and pension investments; ethical practices of the investment professions; the Contract governing their relationship with ACERA; and the policies and guidelines set forth in this Policy statement and any other written directives issued by ACERA.

Each ACERA contract will specify which investment vehicles a Manager is authorized to use, which markets the Manager is authorized to transact business in and any limitations within a market (small or large capitalization, value or growth orientation). The assets in each Manager's portfolio shall be reviewed monthly to ensure compliance with contract guidelines.

All required documents and reports, set forth in Schedule V, must be submitted in a timely manner and in the format specified by ACERA.

Managers must provide prior notification and justification for failure to comply with rules, regulations, contract provisions, deadlines or other directives. Managers must provide a time frame for curing any deficiencies. Staff shall evaluate each incident on a case-by-case basis and determine whether an exception may be granted.

E. CLIENT SERVICE

Managers are required to comply with routine portfolio investment guidelines and reporting deadlines and are also expected to cooperate with special requests for information. ACERA will establish reasonable time frames for all requests and reporting and will provide feedback to all external Managers regarding the perceived quality of their client service.

ACERA Staff will endeavor to meet with each Manager at least twice a year by telephone or in person to review performance and other issues.

SECTION XVII: CONTRACT REVIEW PROCESS

If during the course of regular monitoring, ACERA determines that a Manager's performance, style integrity, organizational stability, compliance, or client service has declined to unacceptable levels, ACERA may, at its discretion, subject the Manager to ACERA's Contract Review Process. As part of the Board's fiduciary duties to prudently select, monitor and supervise their Managers, the Board has approved this process. The purpose of this process is to ensure as little disruption as possible in the event that concerns or problems arise with respect to a Manager's performance. The Board does not confer any additional rights or protections to its Managers by the promulgation of this Policy and/or this process.

There are generally three stages of review: Watchlist, Probation, and Termination (described below). ACERA reserves the right to terminate an investment management contract at any time, with or without 30 days notice, for any reason, and without resort to this Contract Review Process.

The Contract Review Process may result in one or more of the following:

1. Placement on Watchlist or Probation status.
2. Movement from one stage of review to another, or removal from the Contract Review Process.
3. Reduction of assets under management.
4. Revision of investment contract guidelines for that Manager.
5. Re-negotiation of fees.
6. Termination of a Manager's contract.
7. Any other actions deemed appropriate by the Board

Each situation is unique. Action by the Board will vary depending on the type of Manager, the style/strategy, and the deficiency involved. The following describes the Contract Review Process:

A. INITIAL REVIEW

Prior to a Manager being considered for Watchlist, Probation or Termination, ACERA may take the following steps:

1. Analysis

Staff will conduct in-depth analyses of the perceived deficiency to verify that a deficiency exists, form an initial assessment of the severity of the deficiency, and make an initial determination of possible causes.

2. Discussion with the Manager

Staff will contact the Manager to discuss the situation and the results of Staff's analysis.

3. Consultant Input

ACERA may seek the services of a Consultant to provide additional assessment and advice regarding the situation, depending on the severity of the deficiency.

All phases of account compliance may be reviewed during this step, in addition to the specific issue that originated the Review Process.

B. FORMAL ACTION

After completing the Initial Review, Staff may recommend to the Investment Committee and/or Board that the Manager be either placed on Watchlist or Probation or, in certain cases, Terminated. The Committee and/or Board will approve or reject the recommendation. However, if a Manager's deficiency satisfies the criteria as listed under Watchlist and Probation in this Review Process, Staff may place a Manager on Watchlist or Probation without the Committee and/or Board's prior approval. In that case, Staff will be required to report to the Committee on the action taken in this Review Process as soon as possible. The specific criteria for determining which stage of Contract Review to recommend is outlined later in this Policy section and summarized in tabular form in Schedule II.

Upon approval of a Watchlist or Probation recommendation:

1. Staff will notify the Manager of the Board's decision and will provide the Manager with a statement of concerns which outlines the areas which need improvement.

2. The Manager will be asked to respond in writing with an explanation of the issues and a proposed action plan to resolve the issues within 30 days of receipt of the statement of concerns.

3. Staff, a Consultant and the Manager will collectively draft a Plan of Action. The plan will identify the specific steps to be taken to correct the problem; the time frames for further review; and what additional monitoring may be required.

   At the end of the time period specified in the Plan of Action, the Manager will be evaluated and one of the following actions may be taken:

   (a) Removal from Contract Review: if the Manager successfully resolves the issues/deficiencies and demonstrates continued success in all other areas of its relationship with ACERA.

   (b) Movement from Probation to Watchlist: if the Manager has satisfied all or most of the issues/deficiencies that caused it to be placed on Probation, yet Staff continues to have concerns about the Manager. If circumstances warrant, a Manager may also be moved from Watchlist to Probation at any time during the Contract Review Process.

   (c) Extension of Contract Review: a Manager may be given additional time to satisfy the conditions of its Action Plan if reasonable progress is being made. Extensions may also be granted if unfavorable market conditions or high costs make reallocation of assets inadvisable.

   (d) Termination: if the Manager has not satisfactorily resolved the issues/deficiencies, Staff may recommend termination as described below. Termination may be recommended at any time during the Contract Review Process if circumstances warrant.

WATCHLIST

Watchlisting indicates an increased level of concern, but does not indicate major deficiencies. The Watchlisting period is typically one year. Any of the following may result in a Watchlist status:

A. UNDERPERFORMANCE

Please refer to Schedule II for specific Watchlist criteria for each Manager.

B. STYLE DEVIATION

Managers are expected to adhere to the style of investment management for which ACERA originally hired them. Changes in portfolio characteristics or style drift may lead to a Watchlist status.

C. ORGANIZATIONAL CHANGE

NEW OWNERSHIP
Even relatively benign ownership changes, which impact personnel key to ACERA's portfolio management may be cause for a Watchlist status.

TURNOVER
Significant turnover in top management, portfolio Managers, research or trading staff, or marketing personnel, which does not directly affect the team responsible for ACERA's account may warrant Watchlisting.

REORGANIZATION
Changes which signal management deterioration, departures of key investment personnel, a change in ownership that increases risk to ACERA's investments, or hasty/ uncontrolled growth in the firm with potential to disrupt the investment team hired for management of ACERA's account will mandate Watchlisting.

ASSETS UNDER MANAGEMENT
If the market value of ACERA's portfolio rises above 25% of the Manager's total assets under management, Watchlist status may be warranted.

D. COMPLIANCE
CONTRACTS AND OTHER AGREEMENTS
Managers are expected to comply with the investment management contract, investment guidelines, or other directives. Non- or partial compliance may result in a Watchlist status.

REPORTING
Staff will contact Managers to request past due reports. If the Manager's reports are consistently delinquent, the payment of fees may be delayed. If a Manager cannot comply with reporting deadlines, ACERA should be given prior notification. If warranted, a variance may be allowed. Managers are expected to resolve reporting problems immediately upon notification by ACERA. Repeated delinquency in reporting may result in a Watchlist status.

E. CLIENT SERVICE

If a Manager is uncooperative and demonstrates a poor client service attitude, Watchlisting is appropriate. Managers are expected to resolve client service issues immediately upon notification by ACERA.

PROBATION

Probation indicates a level of serious deficiency and signals a need for closer contact with the firm. Probation necessitates a cautious, observant relationship with the Manager.

Managers may be placed on Probation with or without first being placed on Watchlist status. The Probation period is typically one year.

The following may result in Probation:

A. UNDERPERFORMANCE

Please refer to Schedule II for specific Probation criteria for each Manager.

B. STYLE DEVIATION

Probation may be warranted when a Manager's portfolio characteristics are significantly different from its contractually specified style. In general, a Manager will be placed on Probation after four or more consecutive quarters of deviating from its style benchmark. In effect, if the Manager is no longer the same Manager that was retained for ACERA's account, Probation and perhaps even Termination is appropriate.

C. ORGANIZATIONAL CHANGE

Changes in ownership, organizational assignments, departures of key investment personnel, a change in ownership that poses substantial risk to ACERA's investments, or turnover that have the potential to seriously disrupt or destroy the investment management team that was hired to manage the ACERA account may result in Probation or Termination. When key personnel, such as top management, portfolio Managers, research and trading staff are no longer available for use on the ACERA portfolio and do not appear to be replaced or replaceable, Probation and perhaps even Termination is appropriate.

D. COMPLIANCE

If a Manager does not comply with securities laws, industry regulations, standards of professional conduct or contractual provisions, Probation is appropriate. Certain circumstances may warrant Termination.

F. CLIENT SERVICE

Failure to correct any issues that previously resulted in the Watchlist status may result in Probation. Managers will generally be given one quarter to resolve client service issues.

TERMINATION

Upon determining that the Manager has not made adequate improvement in the areas outlined in the Plan of Action, Staff may recommend to the Investment Committee and/or Board that the Manager be terminated. Prior to making the final decision to terminate the Manager, the Investment Committee may invite the Manager to make a presentation at the meeting in which the Termination recommendation is to be discussed. Staff will have analyzed the liquidity of the Manager's portfolio and will have a recommendation and plan for disposition of the assets.

Upon the Investment Committee's decision to terminate, Staff will notify the accounting division as well as the Board's legal counsel of the action. All outstanding issues between the Manager and ACERA's Master Custodian, brokers, Consultant, or other parties shall be resolved prior to closing out the contract. The Manager Termination checklist is attached as Schedule IV.

The Contract Review Process described in this Policy does not provide any additional rights or protections to Managers, beyond what is provided in the contract. ACERA reserves the right to terminate an investment management contract without resort to the Contract Review Process, at any time, with or without 30 days notice, for any reason.

SCHEDULE I

ACERA

ASSET ALLOCATION AND MANAGER STRUCTURE TARGETS

ASSET ALLOCATION TARGETS

Asset Class	**Target Allocation %**
U.S. Equity	39
International Equity	22
Fixed Income	30
Real Estate*	9

MANAGER STRUCTURE TARGETS

Managers		**Target Allocation %**
U.S. Equity		
Large Cap Core Index	BoNY S&P 500	50
Large Cap Growth (Hi-Alpha)	TCW	17.5
Large Cap Value (Hi-Alpha)	PFR	17.5
Large Cap Enhanced Core (Hi-Alpha)	Salus	5
Small Cap Growth	Next Century Growth	5
Small Cap Value	Brandywine	5
International Equity		
Core Non-US Equity (growth)	Capital Guardian	60
Core Non-US Equity (value)	Mondrian	40
Fixed Income		
Aggressive Core Plus	Loomis Sayles Boston	29
Global Bond	Brandywine	16
Enhanced Index	Baird	55
Real Estate**		

* Does not include the allocation of $50 million to AFL-CIO Housing Investment Trust (HIT).

** Please refer to ACERA's "Real Estate Investment Policy" for ACERA's real estate manager structure targets.

SCHEDULE IA

ACERA

ASSET ALLOCATION PORTFOLIO REBALANCING

The objective of rebalancing is to control risk and enhance the risk-adjusted return of the asset allocation strategy. For purposes of enhancing the risk-adjusted return of the asset allocation structure, the relative deviation of any liquid sub asset class away from its target weight (or liquidity-adjusted target weight) shall be no more than plus or minus 1.85 standard deviation factors of each allocation's expected volatility, relative to the other allocations in the asset mix. This standard deviation factor shall be used to define the range of allowable deviation from Policy target asset allocations. If any sub asset class reaches its allowable deviation from its target allocation, all sub asset classes will be evaluated.

The actual reallocation will be at the discretion of ACERA's staff (with oversight by the rebalancing Consultant) after reviewing the following: the relative magnitude of deviation from target for all other sub asset classes; the available cash liquidity of sub asset classes that could be used to fund rebalancing; pending cash flows (employer and employee contributions, or proceeds from a terminated Manager's portfolio); pending liquidity windows with commingled investment pools; pending investment commitments (real estate transactions and/or new funding commitments); and pending interest coupon and dividend cash flows.

Asset allocation and rebalancing status reports, and any rebalancing activity taken toward attaining the objective of the rebalancing program will be reported to the Board of Trustees in a timely fashion or whenever a rebalancing transaction occurs.

Significant modifications to the asset allocation strategy shall be cause to review the appropriateness of maintaining this rebalancing parameter or revising it to a parameter more suitable to the revised asset allocation structure.

SCHEDULE II

ACERA

Watchlist/Probation Criteria for Performance*

Watchlist Criteria	Probation Criteria
US Equity • Large Cap Core Index: negative tracking error exceeds 5 bps on an annualized basis in any 1 year period. • Large Cap Growth: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters. • Large Cap Value: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters. • Small Cap Growth: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters. • Small Cap Value: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters. • Large Cap Enhanced Core: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters.	**US Equity** • Large Cap Core Index: negative tracking error exceeds 5 bps in any 1 year period; or negative tracking error exceeds 10 bps for 2 quarters. • Large Cap Growth: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters. • Large Cap Value: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters. • Small Cap Growth: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters. • Small Cap Value: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters. • Large Cap Enhanced Core: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters.

* If Plan history with Manager is less than 5 years, use rolling 3 year period.

Watchlist Criteria	Probation Criteria
International Equity • Core Non-US Equity (growth): cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters. • Core Non-US Equity (value): cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters.	**International Equity** • Core Non-US Equity (growth): cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters. • Core Non-US Equity (value): cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters.
Fixed Income • Aggressive Core Plus: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters. • Global Bond: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters. • Enhanced Index: cumulative 1 year rolling return is below the benchmark for two consecutive quarters, and/or the Manager's peer ranking falls below median for 2 consecutive quarters.	**Fixed Income** • Aggressive Core Plus: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters. • Global Bond: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters. • Enhanced Index: cumulative 1 year rolling return is below the benchmark for more than 2 consecutive quarters and/or the Manager's peer ranking falls below median for more than 2 consecutive quarters.

SCHEDULE III

ACERA

POLICY INDEX FOR TOTAL FUND AND BENCHMARKS FOR ASSET CLASSES, EQUITY AND FIXED INCOME MANAGERS

POLICY INDEX FOR TOTAL FUND

39% Russell 3000/ 23% Lehman Aggregate/ 4% Citigroup World Government Bond Ex. U.S./ 3% Lehman High Yield/ 22% MSCI All Country World Index Ex. U.S./ 9% NCREIF Property Index

BENCHMARKS FOR ASSET CLASSES

Asset Class	**Benchmark Index**
U.S. Equity	Russell 3000
International Equity	MSCI ACWI-Ex. U.S.
Fixed Income	Lehman Aggregate U.S./Citigroup World Government Bond Ex U.S./ Lehman High Yield in the ratio of 75/15/10
Real Estate	NPI

BENCHMARKS FOR EQUITY AND FIXED INCOME MANAGERS
(Please refer to individual Manager's contract for expected annual premium)

Manager	**Benchmark**
U.S. Equity	
BoNY S&P 500	S&P 500
TCW	Russell 1000 Growth
PFR	Russell 1000 Value
Salus	S&P 500
Next Century Growth	Russell 2000 Growth
Brandywine	Russell 2000 Value
International Equity	
Capital Guardian	MSCI ACWI-Ex. U.S.
Mondrian	MSCI ACWI-Ex. U.S.

Manager	Benchmark
Fixed Income	
Loomis Sayles Boston	Lehman Brothers Baa Credit Index
Brandywine (Global Bond)	Citigroup World Government Bond Index Ex U.S.
Baird	Lehman Aggregate
Real Estate*	

* Please refer to ACERA's "Real Estate Investment Policy" for benchmarks for real estate Managers.

SCHEDULE IV

ACERA

MANAGER TERMINATION CHECK-LIST

This checklist is used to ensure that all details are covered when terminating investment management services.

1) Officially notify the Manager in question of the Board's decision to terminate.

2) Establish a plan of action for reallocating assets from the terminated portfolio; transfer assets to other portfolios or prepare for liquidation.

3) Review department files and logs to identify any outstanding issues.

4) Notify ACERA Administration, Accounting Division, Legal Counsel, Consultant, Master Custodian and any other vendors of the termination. Identify and resolve all outstanding issues with these parties.

5) Have Manager and Master Custodian review and sign off on monthly market values and performance figures produced during the contract period.

6) Hold payment of last invoice until all issues are resolved.

7) Retain terminated Manager files in the ACERA office for a minimum of one year; then send to ACERA archives.

8) Hold terminated Manager files in ACERA archives for a minimum of 5 years.

SCHEDULE V*

ACERA

Compliance Schedule

REQUEST	**DUE DATE**
MONTHLY	
Soft Dollar Commission Report (if applicable) (Submit each month regardless of whether any commissions were directed – Consultants and Master Custodian are subject to this request.)	By the 20th of the month following the reported month
Minority Broker Commission Report (Submit each month regardless of whether any commissions were directed.)	By the 20th of the month following the reported month
Accounting Report/Portfolio Valuation** (Please provide transaction data – buys/sells, a portfolio listing including cost and market values, and performance returns.)	By the 20th of the month following the reported month
Derivative Report (if applicable) (Submit each month regardless of whether any derivative instruments were used.)	By the 20th of the month following the reported month
Confirmation that monthly reconciliation with Bank is performed. (Reconciliation should include market values, transactions and performance.)	By the 20th of the month following the reported month

* This Schedule is designed for all investment Managers of ACERA. However, Managers may be required to provide additional compliance reports based on their individual investment agreements with ACERA. Should there be any conflict between individual investment agreements with ACERA and ACERA's "General Investment Guidelines, Policies and Procedures," the individual investment agreements should prevail.

** 5 copies of this report shall be submitted to ACERA Staff.

REQUEST	**DUE DATE**
QUARTERLY	
Fee Billings (Provide all pertinent backup documentation for fee calculations.)	Within 30 days following the end of the quarter
Confirmation of compliance with limitations on investment vehicles and investment markets*	Within 30 days following the end of the quarter
Confirmation of compliance with % limitations on cash holdings, on equity investment and, on fixed-income investment*	Within 30 days following the end of the quarter
Confirmation that ACERA's assets under management does not exceed 25% of the total assets under management firm-wide	Within 30 days following the end of the quarter
Market and Portfolio Analyses and Commentaries**	Within 30 days following the end of the quarter
Additional requirements applicable to Real Estate Program***	
Operations Report/Financial Statements**	Within 60 days following the end of the quarter
Preliminary Investment Packages (applicable to Individually Managed Account)	Within 30 days following the completion of the report, if applicable
Valuation Adjustments Memo (applicable to Individually Managed Account)	Within 90 days following the anniversary date of asset acquisition

* Please refer to the "Specific Investment Guidelines" section of each Manager's investment contract for details.
**5 copies of this report shall be submitted to ACERA Staff.
***Please refer to ACERA's "Real Estate Investment Policy" for details

REQUEST	DUE DATE
Property Valuation Report (Applicable to Individually Managed Account)	Within 90 days following the anniversary date of asset acquisition

ANNUAL

REQUEST	DUE DATE
Annual Performance Fee Billing (if applicable) (Provide all backup documentation/ reconciliation sign-offs.)	Within 30 days following the end of the performance fee period
Organization Chart	Within 30 days following the end of the year or as soon as updated, whichever is earlier
Fidelity Bond/ Errors and Omissions Insurance (Please send an original certificate.)	Within 30 days of renewal
Audited Financial Statements	Within 90 days following the end of the year
Form ADV, Parts I and II (if applicable)	Within 30 days of filing
Statement or Summary of Code of Ethics	Within 30 days of any change
SEC Examination Reports	Within 30 days of receipt

Additional requirements applicable to Real Estate Program***

REQUEST	DUE DATE
Tactical Plans/Management Investment Plans**	Within 30 days of completion

** 5 copies of this report shall be submitted to ACERA Staff.
*** Please refer to ACERA's "real Estate Investment Policy" for details.

Asset Management and Budget Plan[**]	Within 30 days prior to fiscal year end
REQUEST	**DUE DATE**
Audited Financial Statement for ACERA's Fund[**] (applicable to Individually Managed Account)	Within 90 days following the end of the year

[**] 5 copies of this report shall be submitted to ACERA staff.

SCHEDULE VI

ACERA

INVESTMENT PHILOSOPHY (REVISED MAY 2001)

This document describes the investment philosophy of the Alameda County Employees' Retirement Association (ACERA). Its purpose is to enunciate the basic principles and beliefs that underlie ACERA's investment policy and impact the overall management of the pension Fund. The Investment Philosophy (Philosophy) is designed to complement rather than replace the specific investment policies of ACERA. It is expected that ACERA's approach to investments, as reflected in its policies and strategies, will be consistent with the Philosophy over time. Though the Philosophy allows significant flexibility, it also raises some constraints or implications. Where these were deemed to be significant, they have been explicitly identified and labeled as *Implications*.

Future Boards may choose to amend the investment philosophy, as their experiences and circumstances will almost certainly differ. The initial document, and any subsequent changes will provide staff, advisors and future trustees with a frame of reference to help them understand how the investment program has evolved as well as the rationale behind its design. Future Boards may modify the Philosophy as their experiences and circumstances suggest is prudent.

The major sections of the Philosophy are

1. Mission
2. Risk Management
3. Diversification
4. Market Efficiency
5. High-Alpha Managers
6. Organizational Infrastructure and Communications

7. Performance Monitoring and Time Horizon

1. MISSION

a) The Board's primary goals in managing the Fund are

i) To ensure that sufficient funds are available to pay vested benefits and maintain supplemental benefits;
ii) To comply with all applicable fiduciary standards; and
iii) To create value added, where feasible, that will help reduce the costs of the plan, increase benefits, or both.

2. RISK MANAGEMENT

a) The Board believes that prudent management of risk is a central element of the investment function.

b) Though there are numerous risks involved in the management of a pension investment program, ACERA believes that the following warrant particular attention:

i) ***Funding-related Risk*** - The risk that the funds available in the Plan will be insufficient to pay the promised benefits, both vested and supplemental, or that contribution volatility will be unacceptably high. The primary methods for managing funding risk include regularly conducting integrated asset/liability studies, and establishing appropriate and prudent investment and funding policies.

0.1 In managing the relationship between assets and liabilities, the approved asset allocation of the Fund should provide a minimum of a 90% level of certainty of meeting the projected liabilities of the Plan over a 20 year time period, as determined by the actuary.

ii) ***Benchmark-related Risk*** **–** The risk that the investment benchmarks adopted by the Fund are inappropriate, or that the aggregate of the individual Manager benchmarks within an asset class do not adequately reflect the benchmark for the asset class as a whole. The latter risk is a specific risk generally referred to as *benchmark misfit risk (i.e. style risk)*. Inappropriate benchmarks or excessive benchmark misfit risk could result in investment performance different than expected and could adversely impact decisions concerning the hiring or firing of investment managers.

0.1 The primary methods for effectively managing benchmark-related risk are

(a) regular review of the Fund's benchmarks; and

(b) regular measurement and monitoring of misfit risk using proper methodologies.

iii) ***Manager Risk*** - The risk of aberrant performance on the part of individual investment Managers, and the related active management risk for asset classes as a whole.

0.1 The primary methods for mitigating Manager risk are

(a) Prudent processes for selecting and monitoring investment Managers;

(b) Competent internal investment Staff;

(c) Effective investment consulting support; and

(d) Clear communication to investment Managers of ACERA's objectives, expectations, and investment time horizons.

0.2 The primary method for mitigating active management risk for asset classes include

(a) Establishment of appropriate asset class benchmarks;

(b) Careful monitoring of asset class performance relative to the benchmarks; and

(c) Prudent use of passive management.

iv) ***Fortitude Risk*** - The risk that the Board or Staff will fail to exercise the patience, judgment, or fortitude required to support long-term policies and strategies for the investment and funding program.

0.1 The keys to managing fortitude risk are believed to include

(a) Effective orientation and education with respect to institutional investing and actuarial science; and

(b) A commitment to continually refining, confirming, and communicating the investment philosophy and funding policy of the Association.

3. DIVERSIFICATION

a) ACERA acknowledges the basic tenets of modern portfolio theory, which suggest that diversification, or combining assets that are not perfectly correlated with each other, will reduce the long-term volatility of the overall portfolio.

b) It is generally desirable however to avoid overly complex asset structures, provided the allocation selected can reasonably be expected to meet the objectives of the Plan. ACERA believes that the benefits of diversification must be weighed against the costs involved, which may include fees, liquidity, complexity, communication, internal staff resources and expertise and trustee knowledge and effort.

c) The following asset classes are appropriate candidates for inclusion in its portfolio:

i) Domestic equity

ii) International equity (including emerging markets)

iii) Fixed income, including high yield fixed income and international fixed income

iv) Real estate

d) ACERA does not consider alternative investments to be an appropriate candidate for inclusion in its portfolio due to the substantial direct and indirect costs associated with it.

Implications

- A systematic methodology for re-balancing the investment portfolio is required to ensure proper implementation and adequate risk control concerning ACERA's asset allocation.
- Adding or deleting asset classes or investment Managers should be considered in light of the impact such decisions are likely to have on the general complexity and cost structure of the portfolio, as well as ACERA's ability to prudently achieve its investment and funding goals over the long run.

4. MARKET EFFICIENCY

Except for specified High-Alpha assignments:

a) ACERA does not believe in the viability of active management strategies that rely on market timing.

b) ACERA does not believe in the viability of management strategies that call for over weighting or under weighting styles or sectors within an asset class; i.e., benchmark misfit risk will not generate long-term alpha. Accordingly, ACERA generally believes that it should maintain exposures within an asset class (such as style or capitalization weightings) that are consistent with the broad benchmark for the asset class as a whole.

c) ACERA does believe that market efficiency varies among asset classes, creating opportunities for successful active management strategies based on securities selection.

d) Asset classes that can be demonstrated to be efficient should be managed passively in order to reduce active management risk and lower the costs of managing the portfolio.

e) For inefficient asset classes, ACERA believes that it has the ability and a duty to prudently exploit such inefficiencies through active securities selection strategies.

Implications

- ACERA should be conscious of any subtle forms of market timing that may arise in the course of managing the Fund, or that may be implicit in investment strategies presented to ACERA for inclusion in the investment program.

- ACERA must determine appropriate methodologies for determining whether an asset class is efficient or presents appropriate opportunities, thus providing insight to the Board on the use of particular strategies.

5. High-Alpha Managers

a) ACERA believes that the portfolio characteristics utilized to control risk in the broad portfolio, such as market capitalization, sector exposure, use of derivatives, leverage limitations, property type or deal structure may be modified for specific Managers who control a limited portion of the portfolio and have demonstrated a proven capacity to consistently add value net of fees. Such strategies, which ACERA refers to as High-Alpha, may include the following elements:

i) The bulk of the asset class is passively managed or risk controlled; and

ii) A small number of active managers are retained who employ somewhat more aggressive investment strategies, such as concentrated portfolios, leveraged purchases, developments, high-yield debt, etc.

b) The primary benefits of including a High-Alpha approach within the overall portfolio are
   i) Reduction in active management risk;
   ii) Lower average investment fees; and
   iii) Concentration on opportunities where the likelihood of adding value is greatest.

c) The market efficiency and opportunities in asset classes may change over extended periods of time; therefore ACERA believes that its portfolio management strategies should adapt over time to reflect the changing nature of capital markets.

6. Organizational Infrastructure and Communications

a) ACERA believes that in order for the investment program to achieve its goals, ACERA must invest the necessary resources to build and maintain an appropriate organizational infrastructure, key elements of which include

   i) A competent, internal investment staff comprised of a sufficient number of investment professionals possessing appropriate leadership, technical, and administrative skills.

      0.1 Attracting a competent staff. ACERA recognizes that it competes with the private sector. It must therefore continually strive to create a total work environment that is challenging, rewarding, and competitive.

   ii) A strong relationship with outside general investment Consultant(s) who are able to provide ACERA with the following:

0.1 A high degree of investment expertise;
0.2 Innovative and proactive advise and counsel;
0.3 Strong research support; and
0.4 Strong reporting capabilities.

iii) A broad-based information gathering and reporting system to present well- researched, relevant and timely data in a manner that is easily understood, and that supports rigorous and consistent monitoring of critical investment activities.

iv) An open channel of communication between the Board, management, and the ACERA's external investment professionals.

b) By providing the Board with timely, accurate, and thorough information, the organizational infrastructure will give the Board the high level of comfort it needs to set policy, make investment decisions, oversee the performance of the investment program, and maintain the fortitude necessary to support its investment philosophy, policies, and strategies.

Implications

- ACERA must determine what constitutes an appropriate internal investment staff structure, given the nature of the current investment program.

- ACERA must over time take concrete steps towards creating a work environment that will allow the Association to attract and retain needed staff.

- ACERA must recognize that developing its organizational infrastructure it needs – staffing, consulting support, information systems, and communication channels – cannot be achieved overnight, but rather will require an ongoing commitment of time and resources.

7. Performance Monitoring and Time Horizon

a) ACERA holds the following basic beliefs concerning performance monitoring practices and methodologies:

   i) The various investment policies of the Fund, in the aggregate, are the most important determinants of investment success; compliance with investment policies should, therefore, be monitored rigorously;

   ii) The performance of the total portfolio, individual asset classes, and investment Managers should be compared to appropriate, predetermined benchmarks;

   iii) Peer comparisons are an additional valid tool in assessing individual Manager performance (supplementing the use of benchmarks), given that ACERA aims to select superior Managers within particular investment styles or mandates. Peer comparisons, or performance rankings, are also valid tools for measuring the performance of asset class portfolios; and

   iv) Peer group comparisons are not an appropriate means of assessing the performance of the total Fund, given that sponsors have different objectives and risk tolerance levels, and therefore may have different asset allocation policies.

v) Benchmark misfit risk, or the risk that the aggregate of individual investment Manager benchmarks in an asset class do not adequately reflect the benchmark for the asset class as a whole, should be explicitly measured on a regular basis.

vi) Investment Managers are generally hired to fulfill a specific role in a portfolio. Accordingly, ACERA believes it is important that ACERA monitor the extent to which Managers comply with their stated style and mandates.

b) ACERA believes that successful funding and investment decisions require a long-term perspective on the part of the Board and management:

i) It is the intention of the Retirement Board that commitments to asset classes and investment strategies should involve long time horizons that may include more than one business cycle (3-5 years each). Relatively illiquid asset classes may require even longer time horizons.

ii) The Board acknowledges that commitments to individual investment Managers also require a long time horizon of at least one business cycle (3-5 years).

iii) ACERA believes that proper reporting and monitoring systems; and clear communication among Consultants, management, investment Managers and the Board will enable the Board to maintain the necessary long term perspective on all investment decisions.

<u>Implications</u>

- Assessing the investment performance relative to appropriate, pre-determined, benchmarks is as applicable to the total portfolio and to individual asset classes as it is for individual investment Managers, and therefore warrants a commensurate share of the Board's time and attention.

- The Board will spend relatively little time assessing the performance of the Fund relative to that of comparable pension funds.

- ACERA will need to either develop in-house capabilities to regularly measure benchmark-related risk, or it will need to purchase such capabilities from external investment Consultants.

- ACERA will monitor all investment Managers to ensure they are complying with their stated investment style, regardless of whether they are performing well or poorly. Strongly performing Managers who are found to not be following their stated styles will be carefully scrutinized and may be subject to disciplinary action.

- ACERA will monitor all investment providers to ensure compliance with ACERA's "General Investment Guidelines, Policies and Procedures."

SCHEDULE VII

ACERA

TABLE OF AMENDMENT DATES

AMENDING RESOLUTIONS

Jun	27,	1985
Oct.	10,	1985
Jan.	9,	1986
Jan.	16,	1986
Mar.	13,	1986
May	22,	1986
Sep.	11,	1986
Oct.	9,	1986
Nov.	20,	1986
May	14,	1987
Aug.	13,	1987
Oct.	8,	1987
Apr.	21,	1988
July	28,	1988
Jan.	29,	1989(4)
Apr.	13,	1989(5)
May	18,	1989
July	13,	1989
Aug.	10,	1989
Nov.	16,	1989(2)
July	11,	1991
June	11,	1992
June	10,	1993
July	8,	1993
Nov.	18,	1993
May	14,	1994
Aug.	18,	1994
Nov.	20,	1994
Feb.	16,	1995
May	18,	1995
Jan.	16,	1997
Aug.	20,	1998
May	20,	1999
Jan.	31,	2000
Apr.	19,	2001
Jul.	18,	2002
Feb.	21,	2003
Feb.	19,	2004
Feb.	17,	2005

Alameda County Employees' Retirement Association

ACERA

GENERAL INVESTMENT GUIDELINES, POLICIES AND PROCEDURES

AMENDED July 20, 2006

ACERA
GENERAL INVESTMENT GUIDELINES, POLICIES AND PROCEDURES
2006

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[1] Prepared for ACERA by Cortex Consulting; Adopted by the Board of Retirement on March 8, 2000; Revised May 2001.

ACERA
GENERAL INVESTMENT GUIDELINES, POLICIES AND PROCEDURES

SECTION I: MISSION AND PURPOSE

The Alameda County Employees' Retirement Association (ACERA) exists for the purposes of providing accurate, timely benefits to its members and their beneficiaries and defraying reasonable expenses of administration.

The Board of Retirement (the Board), having exclusive authority and exclusive fiduciary responsibility for the investment and administration of the Trust Fund (the Fund), hereby establishes the following "General Investment Guidelines, Policies and Procedures" (the Policy) for the investment of ACERA's assets. The Board reserves the right to amend, supplement or rescind this Policy at any time.

The Board of Retirement is directed by law and given discretion to prudently invest the retirement plan assets. The purpose of this statement of policy is to assist ACERA in effectively supervising said investments and to encourage effective communication between ACERA and its investment Managers and Consultants.

ACERA's investment goal is to operate at a level of performance in the upper quartile of comparable pension funds on a risk-adjusted basis and to be as fully funded as possible so that ACERA's benefit costs do not become a burden upon future generations of members and taxpayers.

SECTION II: CONSTITUTIONAL REQUIREMENTS

Article 16 §17 of the California State Constitution provides in pertinent part as follows:

"Notwithstanding any other provisions of law or this Constitution to the contrary, the retirement board of a public pension or retirement system shall have plenary authority and fiduciary responsibility for investment of money and administration of the system, subject to the following:

a. The retirement board of a public pension or retirement system shall have the sole and exclusive fiduciary responsibility over the assets of the public pension or retirement system. The retirement board shall also have sole and exclusive responsibility to administer the system in a manner that will assure prompt delivery of benefits and related services to the participants and their beneficiaries. The assets of a public pension or retirement system are trust funds and shall be held for the exclusive purposes of providing benefits to participants in the pension or retirement system and their beneficiaries and defraying reasonable expenses of administering the system.

b. The members of the retirement board of a public pension or retirement system shall discharge their duties with respect to the system solely in the interest of, and for the exclusive purposes of providing benefits to participants and their beneficiaries, minimizing employer contributions thereto, and defraying reasonable expenses of administering the system. A retirement

board's duty to its participants and their beneficiaries shall take precedence over any other duty.

c. The members of the retirement board of a public pension or retirement system shall discharge their duties with respect to the system with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with these matters would use in the conduct of an enterprise of a like character and with like aims.

d. The members of the retirement board of a public pension or retirement system shall diversify the investments of the system so as to minimize the risk of loss and to maximize the rate of return, unless under the circumstances it is clearly not prudent to do so.

e. The retirement board of a public pension or retirement system, consistent with the exclusive fiduciary responsibilities vested in it, shall have the sole and exclusive power to provide for actuarial services in order to assure the competency of the assets of the public pension or retirement system.

f. With regard to the retirement board of a public pension or retirement system which includes in its composition elected employee members, the number, terms, and method of selection or removal of members of the retirement board which were required by law or otherwise in effect on July 1, 1991, shall not be changed, amended, or modified by the Legislature unless the change, amendment, or modification enacted by the legislature is ratified by a majority of the electors of the jurisdiction in which the participants of the system are or were, prior to retirement, employed.

g. The Legislature may by statute continue to prohibit certain investments by a retirement board where it is in the public interest to do so, and provided that the prohibition satisfies the standards of fiduciary care and loyalty required of a retirement board pursuant to this section.

h. As used in this section, the term "retirement board" shall mean the board of administration, board of trustees, board of directors, or other governing body or board of a public employees pension or retirement system; provided, however, that the term "retirement board" shall not be interpreted to mean or include a governing body or board created after July 1, 1991, which does not administer pension or retirement benefits, or the elected legislative body of a jurisdiction which employs participants in a public employees pension or retirement system."

SECTION III: ROLES AND PRINCIPLE DUTIES

The Fund investments shall be prudently planned, implemented, managed, monitored and guarded. The Board, Investment Committee (the Committee), Investment Staff (Staff), General Investment Consultant (Consultant), Custodian Bank (Custodian), and Investment Managers (Manager(s)) shall coordinate this process. See the defined roles and principle duties of the above-mentioned parties below:

A. THE BOARD shall review and approve Committee recommendations. The Board also reviews, adopts and monitors all investment polices, guidelines and procedures required to prudently administer the Fund and to effectively mitigate risk to the Fund.

B. THE COMMITTEE shall identify issues pertinent to the effective investment and administration of the Fund and initiate analysis of such issues by Staff, Consultant or Managers. It also reviews Staff's and Consultant's recommendations regarding all investment policies and investment Fund management. The Committee provides recommendations to the Board for adoption, oversees implementation, and monitors the investment programs in accordance with all applicable laws and Board-established policies, guidelines and procedures. Refer to Schedule VII – Charter of ACERA's Investment Committee of the Board for detailed Committee responsibilities.

C. STAFF shall oversee the Fund's investment program activities, implement the Board/Committee's decisions, make recommendations to the Committee regarding Fund management, and recommend investment-related polices and procedures to the Committee. Additionally, Staff monitors the performance and compliance of Managers in accordance with all applicable laws, Board-established policies, guidelines and procedures, as well as "Specific Investment Guidelines" set out in the investment agreement between ACERA and each Manager (Agreement or Contract). Staff also facilitates Investment Committee meetings and completes activity as directed by the Board/Committee.

D. CONSULTANT shall review, analyze and evaluate the Fund's effectiveness and efficiency and make fund management related recommendations. Consultant assists Staff in implementing the Board/Committee's decisions and developing all investment-related policies. Consultant's responsibilities are detailed in the service agreement between ACERA and Consultant.

E. CUSTODIAN shall provide custody of ACERA's investment assets. Custodian's responsibilities are detailed in the service agreement between ACERA and Custodian.

F. MANAGER shall prudently manage its Managed Account (defined in Section IV – Eligible Asset Categories) in accordance with all applicable laws, Board-established policies, guidelines and procedures, as well as Specific Investment Guidelines. Manager's responsibilities are detailed in the investment agreement between ACERA and each Manager.

SECTION IV: ELIGIBLE ASSET CATEGORIES

The Fund shall hold assets in categories established by the Board. Any asset category may be held in direct form, in pooled form, or in both. Asset categories managed by one or more "Qualified Investment Managers" are called "Managed Accounts." Asset categories under the supervision of the County Treasurer are called the Treasurer's Accounts. Eligible asset categories are listed and defined below.

A. CASH shall consist of short term (12 months or less) interest bearing investments of high quality such as U.S. Treasury issues, insured certificates of deposit of U.S. banks (fixed and/or variable), commercial paper rated A-1, P-1 or both, or other instruments of equal or better quality, and includes money market funds available through the Custodian.

B. U.S. EQUITY shall consist of common stocks and other securities which are convertible into common stocks, and ADRs (American Depository Receipts), as well as cash (per "A" above) and fixed income (per "D" below) when used as temporary substitutes for common stocks.

C. INTERNATIONAL EQUITY shall consist of common stocks and other securities convertible into common stocks of companies domiciled outside of the U.S., and GDRs (Global Depository Receipts), as well as cash equivalents and fixed income, domestic or international, which are being used as temporary substitutes for common stock.

D. FIXED INCOME shall consist of investments in U.S. taxable bonds, debentures, notes and other evidences of debt. Fixed income may also include non-dollar denominated bonds issued by corporations or governments domiciled outside of the United States of America as well as Brady Bonds. Other eligible investments include cash equivalents per "A" above and convertible bonds and preferred stock.

E. REAL ESTATE shall consist of investments in real estate and equity real estate through the use of commingled or direct investments. Detailed information about real estate investments is included in ACERA's "Real Estate Investment Policy," which is maintained as a separate document.

SECTION V: INVESTMENT PHILOSOPHY

The following is a summary of ACERA's investment philosophy. For the complete statement, please refer to Schedule VI of this document, "ACERA Investment Philosophy."

The Board believes that its investment policies, in aggregate, are the most important determinants of its investment success. Compliance with investment policies should, therefore, be monitored rigorously. The Board also believes that performance of the total portfolio, individual asset class, and Managers should be monitored and compared to appropriate, predetermined benchmarks.

The Board believes that prudent management of risk is a central element of the investment function and that diversification among asset classes will reduce risk and enhance returns of the overall investment portfolio in the long term.

The Board believes that market efficiency and opportunities vary among asset classes and may change over extended periods of time; therefore, the Board believes that ACERA's portfolio management strategies should adapt over time to reflect the changing nature of capital markets.

The Board's primary goals in managing the Fund are

1. To ensure that sufficient funds are available to pay vested benefits and maintain supplemental benefits;

2. To comply with all applicable fiduciary standards; and

3. To add marginal value that will help reduce the costs of the plan and/or to increase benefits for the beneficiaries.

The Board believes that in order to achieve its goals, ACERA must invest the necessary resources to build and maintain an appropriate organizational infrastructure.

SECTION VI: INVESTMENT STRATEGY

A. U.S. EQUITY will be structured to capture exposure to the broad U.S. equity market as represented by the Russell 3000 Index. Passively managed (index) portfolios will be used in markets that are reasonably efficient. These portfolios are intended to provide broadly diversified market exposure with controlled (market) risk and minimal cost.

Actively managed portfolios will be used in less efficient markets when the Board determines that a Manager possesses special skills or abilities that enable that Manager to capture excess returns relative to the market, adjusted for risk and fees; or to exploit specialty markets that provide enhanced return with acceptable risk.

A great part of the Russell 3000, on a market value basis, is comprised of large-cap stocks, which the Board believes are efficiently priced most of the time. Therefore, the Board has adopted a policy of obtaining overall exposure to this segment of the market via passively managed indexed products. Some active Managers have been employed to enhance overall portfolio return in the large- and/or mid-cap sectors on a risk- and fee-adjusted basis. These Managers manage ACERA's "High-Alpha" program.

The remainder of the Russell 3000 index is comprised of small to mid-cap companies. Some opportunities for active management enhancement exist in these securities due to market inefficiencies. ACERA will attempt to capture these opportunities through a mix of Managers who have the special skills required to identify smaller companies that may be undervalued or possess substantial growth potential.

The U.S. equity portion of the portfolio shall be allocated among the various styles and Managers as indicated in Schedules I and IA.

B. INTERNATIONAL EQUITY represents an opportunity to diversify risk and capture enhanced returns within markets generally less efficient than the U.S. domestic equity market. 100% of the international equity portion of the Fund will be invested in actively managed portfolios.

C. FIXED INCOME represents a means of reducing overall portfolio risk and capturing incremental returns either domestically or globally. Inefficiencies in the pricing and trading of fixed income securities create opportunities to add value through active management. 100% of the fixed income portion of the portfolio will be invested in actively managed portfolios.

D. REAL ESTATE will be used as a means for diversifying the portfolio and capturing additional returns due to the low correlation between returns on real estate and financial assets. Due to the illiquid nature of real estate assets, distinctions between active and passive management are not applicable. Detailed information regarding real estate investments is included in ACERA's "Real Estate Investment Policy," which is maintained as a separate document.

SECTION VII: ASSET ALLOCATION AND REBALANCING

Asset allocation targets, a function of the returns and risks from various asset classes and the nature of the plan's liabilities, are set forth in Schedule I. A goal of asset allocation is balancing asset growth versus liability growth considering time horizons, liabilities and risk tolerance.

Rebalancing is the risk control process of returning an allocation back to the desired target level after having drifted away from its targeted position. Equal probability bands, as defined by standard deviation factors that shall be used to define the acceptable ranges around the asset allocation targets are set forth in Schedule IA. The objective of rebalancing is to enhance the risk-adjusted performance of the asset allocation structure.

Staff shall be responsible for maintaining the relative weights of asset classes and allocations within the acceptable rebalancing ranges as reflected in Schedule IA. Should an asset class or allocation fall outside its target range, Staff shall rebalance the asset class or allocation back to the target weights as specified in the asset allocation structure in Schedule I.

Staff shall

1. Monitor the portfolio;

2. Determine whether or not any asset category is out of balance with its target asset allocation in excess of the specified tolerance range;

3. Determine whether or not any Manager within each asset category is out of balance with their target allocation in excess of the specified tolerance range;

4. And, if this is determined, either

   (a) instruct the relevant Managers to redirect cash income (interest coupon and dividends) in concert with an evaluation of pending commitments and other cash flows (employer and employee contributions), in order to bring the allocation(s) back to the adopted strategic target; or

   (b) instruct the relevant Managers to liquidate or acquire the appropriate dollar value of securities to reach the target and reallocate the cash thus generated or required to the other category(s) or Manager(s), as necessary.

Staff shall report to the Board on a regular basis the status of the Fund with respect to how categories are tracking relative to their allowable ranges, as well as any actions taken to rebalance the portfolio.

SECTION VIII: ASSET CATEGORIES OBJECTIVES

The general objective of the Board is to preserve capital and to earn a return from appreciation and income, as described herein:

1. To ensure the integrity of ACERA's actuarial funding plan, one minimum return objective for the Fund shall be the current actuarial interest assumption rate plus 25 basis points per year over a market cycle. Returns shall be calculated net of all fees (both administrative and investment fees).

2. To ensure that ACERA's assets grow appropriately to match salary increases which directly impact benefit levels, an additional minimum return objective for the Fund over a market cycle (up to five years) shall also be 400 basis points (4%) per year over the national Consumer Price Index, published by the U.S. Department of Commerce. Returns shall be calculated gross of investment management fees.

3. To ensure that ACERA's external investment manager structure, in aggregate, is performing satisfactorily. An additional minimum return objective for the Fund over a market cycle (up to five years) shall also be equivalent to the Fund's Policy Index on a gross of investment management fee basis.

The objectives of each asset category are

A. CASH

1. A rate of return in excess of 90-Day U.S. Treasury bills, and

2. A rate of return within the upper one half of a universe of like short-term funds.

B. U.S. EQUITY

1. A rate of return in excess of the U.S. equity market as measured by the Russell 3000 Index after adjustment for risk and fees, and

2. A rate of return within the upper 33rd percentile of the Independent Consultants Cooperative (ICC)/State Street database or similar database of the performance of diversified equity portfolios.

C. INTERNATIONAL EQUITY

1. A rate of return in excess of the Morgan Stanley Capital International All Country World Index Ex-U.S. (MSCI ACWI Ex-U.S.), and

2. A rate of return within the top quartile of the ICC/State Street database or similar database of the performance of diversified international equity portfolios.

D. FIXED INCOME

1. A rate of return in excess of the Lehman Aggregate Bond Index, Citigroup World Government Bond Ex. U.S. and Lehman High Yield in a ratio of 75/15/10, and

2. A rate of return within the top quartile of the ICC/State Street database or similar database of the performance of diversified fixed income portfolios.

E. REAL ESTATE

1. Total Return – a minimum total gross return equivalent to the National Council of Real Estate Investment Fiduciaries (NCREIF) Property Index (NPI) over rolling five-year periods, and

2. Income Return – Income, which is defined as cash distributed to the Association, should comprise at least 2/3 of the total expected return over rolling five-year periods for all Stable (as defined in ACERA's "Real Estate Investment Policy") product.

In addition, objectives that reflect the particular investment strategy or style used by individual Manager shall be outlined in Specific Investment Guidelines attached to the Manager's Contract.

SECTION IX: ALLOCATION OF CASH FLOW

Cash flow not needed for benefit payments or administrative expenses shall be allocated to Managed Accounts in a ratio that best funds the overall targeted asset allocation as reflected in Schedules I and IA.

If cash flow is insufficient for the payment of benefits or to cover administrative expenses, then Managed Accounts shall be debited in a ratio that best satisfies the target allocation shown in Schedules I and IA. Such debits, if necessary, will be carried out as needed and with timely notice to Managers to facilitate effective funds transitions and performance measurement.

For all planned investments which may not need to be funded immediately, a reserve may be budgeted and invested in appropriate accounts in accordance with the asset allocation targets until such moneys are required. Alternatively, Managed Accounts within "overfunded" asset classes may be called upon to provide the required moneys.

SECTION X: PROHIBITED INVESTMENTS

Managers shall exercise prudent expert standards in defining prohibited investments. For example, prohibited investments include, but are not limited to, securities issued by the County of Alameda or any agency thereof.

SECTION XI: DIRECTED BROKERAGE

ACERA shall establish an open Directed Brokerage (DB) program designed to maximize the recapture of brokerage commissions by enforcement of the target percentages of direction. ACERA's DB program is governed by ACERA's DB Policy, which is maintained as a separate document.

The strategic objective of the DB program is to take advantage of the industry-accepted recapture of a portion of trade commissions paid to brokers. The primary goals of the DB program are to: 1) recapture 50% or more of commissions paid on a specific percentage of trades sent to correspondent brokers on a timely basis; 2) construct the percentage of trades subject to recapture so as to allow investment managers to have access to the research they need; 3) seek "Best Execution" through third-party administration and outside consultant monitoring; and 4) encourage local and emerging broker participation through the use of an open correspondent network program.

SECTION XII: DERIVATIVE INSTRUMENT USAGE POLICY

Exposure to risk by use of derivative instruments must be consistent with ACERA's overall investment policy as well as an individual Manager's specific investment guidelines. Derivatives shall not be used to establish a leveraged position (i.e., offsetting Cash positions must be maintained against all delayed settlement transactions).

SECTION XIII: SELECTION OF INVESTMENT MANAGERS

The Investment Committee shall direct Staff and/or a Consultant to initiate searches for Managers. Staff and/or the Consultant shall research for qualified candidates and present a list of finalists to the Investment Committee for its approval. Upon approval of the list, the finalists shall be interviewed by Staff and the Consultant (if applicable). Staff and the Consultant (if applicable) shall evaluate the interviews, rank the finalists, and make a recommendation to the Investment Committee to hire one or more firms attaining the highest rankings in a publicly noticed meeting at which no less than five (5) Investment Committee members shall be present. It is possible that none of the firms will be recommended for hire.

These procedures are developed for the convenience and benefit of ACERA, and shall not bind ACERA or invalidate the selection of a Manager, if different processes are used subsequent to the promulgation of this Policy.

SECTION XIV: AUTHORITY OF INVESTMENT MANAGERS

Subject to the laws of the United States and the State of California, and to the terms and conditions of this Policy, Managers shall have full discretion to direct the purchase, exchange, sale and reinvestment of the assets of the Managed Accounts. The Board expects that Managers will recommend changes to this Policy when any part of this Policy appears to be at variance with overall market and economic conditions.

Managers shall place orders to buy and sell securities and, by notice to the Custodian, shall cause the Custodian to deliver and receive securities on behalf of the Fund. Managers shall, upon Board inquiry, report placement of ACERA brokerage such that the Board shall be assured commissions were placed for the sole and exclusive benefit of the Fund.

Separate account Managers shall not vote proxies. Proxies shall be voted by ACERA, via a proxy voting service vendor, in accordance with "ACERA Proxy Voting Guidelines and Procedures" which is maintained as a separate document.

Securities lending shall be performed under the oversight of Staff, in accordance with Board-established policies and procedures.

SECTION XV: INVESTMENT GUIDELINES FOR THE MANAGED ACCOUNTS

Individual Manager discretion shall be governed by the Investment Guidelines for the Managed Accounts as well as the Specific Investment Guidelines for each Manager. Should there be any conflict between the Specific Investment Guidelines of an individual Manager and the Investment Guidelines for the Managed Accounts, the Specific Investment Guidelines shall prevail.

A. GENERAL

1. All investments shall comply with all applicable laws of the United States and the State of California governing the investment of pension trusts.

2. All securities transactions shall be executed by reputable broker/dealers, banks, or the Custodian, and shall be on a best-price and best-execution basis, and shall be reported to ACERA as is called for elsewhere in this Policy.

3. All Managers shall refrain from investing in a tobacco producer investment opportunity when, in their expert opinion, an alternative non-tobacco producer investment opportunity is available that will satisfy the same ACERA portfolio guidelines, instructions and objectives for risk, return and diversification.

B. EQUITY

Managers have full discretion to invest solely in readily marketable and diversified equity securities as defined above subject to the following:

1. For Managed Accounts, no more than 10% of the value (at time of purchase) of the account shall be invested in the securities of a single issuer.

2. ACERA shall not hold more than 10% of the equity securities of any issuer.

3. Equity securities shall possess value and quality corroborated by generally

accepted techniques and standards of fundamental securities analysis.

4. Assets in a Managed Account not invested in equity securities shall be kept with interest in appropriate money market instruments, including any money market fund available through the Custodian.

5. A Managed Account shall be subject to ACERA's policy on derivatives.

6. All Managers shall endeavor to be fully invested in stocks at all times unless they have received specific authorization to the contrary from the Board. Cash holdings, as defined in this Policy, shall generally not exceed 5% of the portfolio on a market value basis.

C. FIXED INCOME

Managers have full discretion to invest solely in readily marketable and diversified securities including, but not limited to

1. Obligations of the U.S. and/or eligible foreign government's Treasuries.

2. Obligations guaranteed by agencies of the United States and/or eligible foreign governments.

3. Insured certificates of deposit and banker's acceptances of credit worthy banks.

4. Corporate and other evidences of debt. At least 80% of this debt must be rated by Moody's Investor's Services or by Standard & Poors.

5. Commercial paper and banker's acceptances of issuers rated P-1 by Moody's Investor's Service.

6. Or A-1 by Standard & Poors Corporation.

7. Excepting direct obligations of the U.S. and/or eligible foreign governments, and those explicitly guaranteed by the U.S. and/or eligible governments, no account shall hold more than 5%, at cost, of the obligations of any single issuer.

8. Excepting direct obligations of the U.S. and/or eligible foreign governments, and those explicitly guaranteed by the U.S. and/or eligible governments, no security shall comprise more than 5% of the account, as determined at the time of purchase.

9. Fixed income derivative investments shall be in accordance with ACERA's derivative policy.

SECTION XVI: SEPARATE ACCOUNT MANAGER SPECIFICATIONS

A. Managers must be registered as investment advisers under the Investment Adviser's Act of 1940, a bank (as defined in that Act) or an insurance company qualified to perform investment management services under state law in more than one state, including California. Unless an exception is granted by the Board, by accepting appointment as ACERA's Managers, Managers shall acknowledge that they are "Plan Fiduciaries" and "Qualified Investment Managers" as defined by the Employees' Retirement Income Security Act (ERISA) of 1974, (see or reference United States Code Title 29 Section 1001 et. seq..)

B. Managers shall maintain fiduciary insurance in the amount of 10% of the total assets managed in the ACERA account or

$25 million, whichever is higher, unless the contract specifies otherwise.

C. Managers shall promptly notify ACERA of changes that occur in any of the following:

1. The investment strategy used in managing the subject product.

2. The key personnel involved in managing ACERA's account.

3. The ownership, key personnel, or organizational structure of the Manager's company.

4. The Manager company's financial condition.

5. The number of clients invested in the subject product.

6. The market value of the total assets managed in the subject product.

D. Managers shall promptly notify ACERA if they are subject to censure or disciplinary action by a regulatory agency.

E. Managers shall provide to ACERA all required documents and reports as set forth in Schedule V – ACERA's Compliance Schedule.

F. Managers shall not make contributions, provide gifts, reimbursements of expenses or provide personal benefits exceeding $250 in the aggregate within any 12-month period to any Trustee, fiduciary, employee or Consultant of ACERA. Donations of educational conferences and similar events and benefits, including travel, meals and accommodations will be made to ACERA and not directed to individuals. The Board will determine whether to accept any donations and will be solely responsible for selection of the Trustee, Staff, or other individual, who will attend or otherwise participate on behalf of ACERA.

SECTION XVII: MANAGER MONITORING PROCEDURE

The ACERA Board has contracted with a number of external Managers to invest ACERA assets in the capital markets. As part of the Board's fiduciary duties to prudently select, monitor and supervise these Managers, the Board has adopted this Procedure. The intent of this Procedure is to notify Managers of the standards by which they will be judged and to establish a structure which the Investment Committee and the Board can use to monitor the performance of the Managers.

Managers will be monitored to

1. Evaluate how well they achieve their investment objectives.

2. Ensure that they adhere to their established investment approach/style and do not attempt to index returns to preserve stellar performance or take extraordinary risk to overcome poor performance.

3. Identify issues or trends that have the potential to result in losses to the Fund.

4. Alert the Board when Managers are not performing to expectations so that appropriate remedial action can be taken.

Managers will be evaluated on the basis of the following: performance, style integrity, organizational stability, compliance, and client service described in greater detail below.

A. PERFORMANCE

On a monthly basis Staff will monitor Manager holdings, activity and performance.

On a quarterly basis Staff and/or a Consultant will furnish the Investment Committee and/or Board with an in-depth evaluation of each Manager which will include a comparison of the Manager to its Contract benchmark and a peer universe of Managers using a similar investment style. This report shall include an analysis of the sources of Managers' returns (stock selection, industry selection, asset allocation, etc.) and shall identify which decisions enhanced or diminished performance.

On a quarterly basis, trading costs will be evaluated in terms of commissions paid and execution of trades. Staff and/or Consultants shall furnish a report to the Investment Committee and/or Board regarding trading costs on an annual basis.

B. STYLE INTEGRITY

Each Manager will be analyzed at least annually to ensure that the Manager is continuing to invest the portfolio in the style for which they were originally hired. Style integrity is essential to maintain the Board's asset allocation policy. Any significant deviation in style will result in the overall portfolio having a different characteristic, in some measure, from the broad market which is represented by the Russell 3000 index. Significant variations in the portfolio characteristics from the style anticipated in the management Contract may indicate a change in its investment style.

This review also provides the Investment Committee and/or Board an opportunity to evaluate the Manager's continuing "fit" with the goals of the overall Fund. By monitoring Manager style the Investment Committee and/or Board can assure that its Manager mix takes advantage of opportunities to increase diversification through lower correlation of returns among individual Managers.

C. ORGANIZATIONAL STABILITY

Managers' organizations will be monitored to ensure continuity of the intellectual and philosophical processes that went into developing the particular investment approach contracted for by ACERA. In addition, Managers will be monitored for business risk, quality of staff, departures of key investment personnel, change in ownership or acquisition, and potential conflicts of interest.

It is ACERA's intent that its portfolio comprises no more than 25% of the Manager's total assets under management at any time. Therefore, ACERA will monitor the Managers' assets, firm-wide, as well as in the subject product.

D. COMPLIANCE

Managers will be monitored to ensure they are adhering to federal and state laws regarding securities and the management of investment portfolios, trading, and pension investments; ethical practices of the investment professions; the Contract governing their relationship with ACERA; and the policies and guidelines set forth in this Policy statement and any other written directives issued by ACERA.

Each ACERA Contract will specify which investment vehicles a Manager is authorized to use, which markets the Manager is authorized to transact business in and any limitations within a market (small or large capitalization, value or growth orientation). The assets in each Manager's portfolio shall be reviewed monthly to ensure compliance with Contract guidelines.

All required documents and reports, set forth in Schedule V, must be submitted in a timely manner and in the format specified by ACERA.

Managers must provide prior notification and justification for failure to comply with rules, regulations, Contract provisions, deadlines or other directives. Managers must provide a time frame for curing any deficiencies. Staff shall evaluate each incident on a case-by-case basis and determine whether an exception may be granted.

E. CLIENT SERVICE

Managers are required to comply with routine portfolio investment guidelines and reporting deadlines and are also expected to cooperate with special requests for information. ACERA will establish reasonable time frames for all requests and reporting and will provide feedback to all external Managers regarding the perceived quality of their client service.

ACERA Staff will endeavor to meet with each Manager at least twice a year by telephone or in person to review performance and other issues.

SECTION XVIII: CONTRACT REVIEW PROCESS

If during the course of regular monitoring, ACERA determines that a Manager's performance, style integrity, organizational stability, compliance, or client service has declined to unacceptable levels, ACERA may, at its discretion, subject the Manager to ACERA's Contract Review Process. As part of the Board's fiduciary duties to prudently select, monitor and supervise their Managers, the Board has approved this process. The purpose of this process is to ensure as little disruption as possible in the event that concerns or problems arise with respect to a Manager's performance. The Board does not confer any additional rights or protections to its Managers by the promulgation of this Policy and/or this process.

There are generally three stages of review: Watchlist, Probation, and Termination (described below). ACERA reserves the right to terminate an investment management Contract at any time, with or without 30 days notice, for any reason, and without resort to this Contract Review Process.

The Contract Review Process may result in one or more of the following:

1. Placement on Watchlist or Probation status.
2. Movement from one stage of review to another, or removal from the Contract Review Process.
3. Reduction of assets under management.
4. Revision of investment Contract guidelines for that Manager.
5. Re-negotiation of fees.
6. Termination of a Manager's Contract.
7. Any other actions deemed appropriate by the Board

Each situation is unique. Action by the Board will vary depending on the type of

Manager, the style/strategy, and the deficiency involved. The following describes the Contract Review Process:

A. INITIAL REVIEW

Prior to a Manager being considered for Watchlist, Probation or Termination, ACERA may take the following steps:

1. Analysis

Staff will conduct in-depth analyses of the perceived deficiency to verify that a deficiency exists, form an initial assessment of the severity of the deficiency, and make an initial determination of possible causes.

2. Discussion with the Manager

Staff will contact the Manager to discuss the situation and the results of Staff's analysis.

3. Consultant Input

ACERA may seek the services of Consultant to provide additional assessment and advice regarding the situation, depending on the severity of the deficiency.

All phases of account compliance may be reviewed during this step, in addition to the specific issue that originated the Review Process.

B. FORMAL ACTION

After completing the Initial Review, Staff may recommend to the Investment Committee and/or Board that the Manager be either placed on Watchlist or Probation or, in certain cases, Terminated. The Committee and/or Board will approve or reject the recommendation. However, if a Manager's deficiency satisfies the criteria as listed under Watchlist and Probation in this Review Process, Staff may place a Manager on Watchlist or Probation without the Committee and/or Board's prior approval. In that case, Staff will be required to report to the Committee on the action taken in this Review Process as soon as possible. The specific criteria for determining which stage of Contract Review to recommend is outlined later in this Policy section and summarized in tabular form in Schedule II.

Upon approval of a Watchlist or Probation recommendation:

1. Staff will notify the Manager of the Board's decision and will provide the Manager with a statement of concerns which outlines the areas which need improvement.

2. The Manager will be asked to respond in writing with an explanation of the issues and a proposed action plan to resolve the issues within 30 days of receipt of the statement of concerns.

3. Staff, a Consultant and the Manager will collectively draft a Plan of Action. The plan will identify the specific steps to be taken to correct the problem; the time frames for further review; and what additional monitoring may be required.

   At the end of the time period specified in the Plan of Action, the Manager will be evaluated and one of the following actions may be taken:

   (a) Removal from Contract Review: if the Manager successfully resolves the issues/deficiencies and demonstrates continued success in all other areas of its relationship with ACERA.

(b) Movement from Probation to Watchlist: if the Manager has satisfied all or most of the issues/deficiencies that caused it to be placed on Probation, yet Staff continues to have concerns about the Manager. If circumstances warrant, a Manager may also be moved from Watchlist to Probation at any time during the Contract Review Process.

(c) Extension of Contract Review: a Manager may be given additional time to satisfy the conditions of its Action Plan if reasonable progress is being made. Extensions may also be granted if unfavorable market conditions or high costs make reallocation of assets inadvisable.

(d) Termination: if the Manager has not satisfactorily resolved the issues/deficiencies, Staff may recommend termination as described below. Termination may be recommended at any time during the Contract Review Process if circumstances warrant.

WATCHLIST

Watchlisting indicates an increased level of concern, but does not indicate major deficiencies. The Watchlisting period is typically one year. Staff shall conduct a comprehensive evaluation of the Manager at the end of the one-year Watchlisting period to determine whether the Manager may be removed from Watchlist status. Any of the following may result in a Watchlist status:

A. UNDERPERFORMANCE

Please refer to Schedule II for specific Watchlist criteria for each Manager.

B. STYLE DEVIATION

Managers are expected to adhere to the style of investment management for which ACERA originally hired them. Changes in portfolio characteristics or style drift may lead to a Watchlist status.

C. ORGANIZATIONAL CHANGE

1. New Ownership

Even relatively benign ownership changes, which impact personnel key to ACERA's portfolio management may be cause for a Watchlist status.

2. Turnover

Significant turnover in top management, portfolio Managers, research or trading staff, or marketing personnel, which does not directly affect the team responsible for ACERA's account may warrant Watchlisting.

3. Reorganization

Changes which signal management deterioration, departures of key investment personnel, a change in ownership that increases risk to ACERA's investments, or hasty/ uncontrolled growth in the firm with potential to disrupt the investment team hired for management of ACERA's account will mandate Watchlisting.

4. Assets under Management

If the market value of ACERA's portfolio rises above 25% of the Manager's total assets under management, Watchlist status may be warranted.

D. COMPLIANCE

1. Contracts and Other Agreements

Managers are expected to comply with the investment management Contract, investment guidelines, or other directives. Non- or partial compliance may result in a Watchlist status.

2. Reporting

Staff will contact Managers to request past due reports. If the Manager's reports are consistently delinquent, the payment of fees may be delayed. If a Manager cannot comply with reporting deadlines, ACERA should be given prior notification. If warranted, a variance may be allowed. Managers are expected to resolve reporting problems immediately upon notification by ACERA. Repeated delinquency in reporting may result in a Watchlist status.

E. CLIENT SERVICE

If a Manager is uncooperative and demonstrates a poor client service attitude, Watchlisting is appropriate. Managers are expected to resolve client service issues immediately upon notification by ACERA.

PROBATION

Probation indicates a level of serious deficiency and signals a need for closer contact with the firm. Probation necessitates a cautious, observant relationship with the Manager.

Managers may be placed on Probation with or without first being placed on Watchlist status. The Probation period is typically one year. Staff shall conduct a comprehensive evaluation of the Manager at the end of the one-year Probation period to determine whether the Manager may be removed from Probation status.

The following may result in Probation:

A. UNDERPERFORMANCE

Please refer to Schedule II for specific Probation criteria for each Manager.

B. STYLE DEVIATION

Probation may be warranted when a Manager's portfolio characteristics are significantly different from its contractually specified style. In general, a Manager will be placed on Probation after four or more consecutive quarters of deviating from its style benchmark. In effect, if the Manager is no longer the same Manager that was retained for ACERA's account, Probation and perhaps even Termination is appropriate.

C. ORGANIZATIONAL CHANGE

Changes in ownership, organizational assignments, departures of key investment personnel, a change in ownership that poses substantial risk to ACERA's investments, or turnover that have the potential to seriously disrupt or destroy the investment management team that was hired to manage the ACERA account may result in Probation or Termination. When key personnel, such as top management, portfolio Managers, research and trading staff are no longer available for use on the ACERA portfolio and do not appear to be replaced or replaceable, Probation and perhaps even Termination is appropriate.

D. COMPLIANCE

If a Manager does not comply with securities laws, industry regulations, standards of professional conduct or contractual provisions, Probation is appropriate. Certain circumstances may warrant Termination.

F. CLIENT SERVICE

Failure to correct any issues that previously resulted in the Watchlist status may result in Probation. Managers will generally be given one quarter to resolve client service issues.

TERMINATION

Upon determining that the Manager has not made adequate improvement in the areas outlined in the Plan of Action, Staff may recommend to the Investment Committee and/or Board that the Manager be terminated. Prior to making the final decision to terminate the Manager, the Investment Committee may invite the Manager to make a presentation at the meeting in which the Termination recommendation is to be discussed. Staff will have analyzed the liquidity of the Manager's portfolio and will have a recommendation and plan for disposition of the assets.

Upon the Investment Committee's decision to terminate, Staff will notify the accounting division as well as the Board's legal counsel of the action. All outstanding issues between the Manager and ACERA's Master Custodian, brokers, Consultant, or other parties shall be resolved prior to closing out the Contract. The Manager Termination checklist is attached as Schedule IV.

The Contract Review Process described in this Policy does not provide any additional rights or protections to Managers, beyond what is provided in the Contract. The Board reserves the right to terminate an investment management Contract without resort to the Contract Review Process, at any time, with or without 30 days notice, for any reason.

SCHEDULE I

ACERA

ASSET ALLOCATION AND MANAGER STRUCTURE TARGETS

ASSET ALLOCATION TARGETS

Asset Class	Target Allocation %
U.S. Equity	41
International Equity	22
Fixed Income	28
Real Estate*	9

MANAGER STRUCTURE TARGETS

Managers		Target Allocation %
U.S. Equity		
Large Cap Core Index	Bank of New York	43
Large Cap Growth (Hi-Alpha)	Trust Company of the West	17.5
Large Cap Value (Hi-Alpha)	Pzena	17.5
Large Cap Enhanced Core (Hi-Alpha)	Salus	5
Small Cap Growth	Next Century Growth	6
Small Cap Value	Brandywine	8.5
Micro Cap Growth	Next Century Growth	2.5
International Equity		
Core Non-US Equity (growth)	Capital Guardian	60
Core Non-US Equity (value)	Mondrian	40
Fixed Income		
Aggressive Core Plus	Loomis Sayles (Boston)	25
Global Bond	Brandywine	20
Enhanced Index	Baird	55
Real Estate**		

* Does not include the allocation of $50 million to AFL-CIO Housing Investment Trust (HIT).

** ACERA's real estate manager structure targets are specified in ACERA's "Real Estate Investment Policy."

SCHEDULE IA

ACERA

ASSET ALLOCATION PORTFOLIO REBALANCING

The objective of rebalancing is to control risk and enhance the risk-adjusted return of the asset allocation strategy. For purposes of enhancing the risk-adjusted return of the asset allocation structure, the relative deviation of any liquid sub asset class away from its target weight (or liquidity-adjusted target weight) shall be no more than plus or minus 1.80 standard deviation factors of each allocation's expected volatility, relative to the other allocations in the asset mix. This standard deviation factor shall be used to define the range of allowable deviation from Policy target asset allocations. If any sub asset class reaches its allowable deviation from its target allocation, all sub asset classes will be evaluated.

The actual reallocation will be at the discretion of ACERA's staff (with oversight by the rebalancing Consultant) after reviewing the following: the relative magnitude of deviation from target for all other sub asset classes; the available cash liquidity of sub asset classes that could be used to fund rebalancing; pending cash flows (employer and employee contributions, or proceeds from a terminated Manager's portfolio); pending liquidity windows with commingled investment pools; pending investment commitments (real estate transactions and/or new funding commitments); and pending interest coupon and dividend cash flows.

Asset allocation and rebalancing status reports, and any rebalancing activity taken toward attaining the objective of the rebalancing program will be reported to the Board of Trustees in a timely fashion or whenever a rebalancing transaction occurs.

Significant modifications to the asset allocation strategy shall be cause to review the appropriateness of maintaining this rebalancing parameter or revising it to a parameter more suitable to the revised asset allocation structure.

SCHEDULE II

ACERA

Watchlist/Probation Criteria for Performance*

Watchlist Criteria	Probation Criteria
US Equity • Large Cap Core Index: negative tracking error exceeds 5 bps on an annualized basis in any 1 year period. • Large Cap Growth: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, or the Manager's peer ranking falls below median for 2 consecutive quarters in a cumulative 5 year rolling period. • Large Cap Value: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, or the Manager's peer ranking falls below median for 2 consecutive quarters in a cumulative 5 year rolling period. • Small/Micro Cap Growth: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, or the Manager's peer ranking falls below median for 2 consecutive quarters in a cumulative 5 year rolling period. • Small Cap Value: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, or the Manager's peer ranking falls below median for 2 consecutive quarters in a cumulative 5 year rolling period. • Large Cap Enhanced Core: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, or the Manager's peer ranking falls below median for 2 consecutive quarters in a cumulative 5 year rolling period.	**US Equity** • Large Cap Core Index: negative tracking error exceeds 5 bps on an annualized basis in any period greater than 1 year, or negative tracking error exceeds 10 bps for any 2 consecutive quarters. • Large Cap Growth: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters, or the Manager's peer ranking falls below median for more than 2 consecutive quarters in a cumulative 5 year rolling period. • Large Cap Value: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters, or the Manager's peer ranking falls below median for more than 2 consecutive quarters in a cumulative 5 year rolling period. • Small/Micro Cap Growth: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters, or the Manager's peer ranking falls below median for more than 2 consecutive quarters in a cumulative 5 year rolling period. • Small Cap Value: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters, or the Manager's peer ranking falls below median for more than 2 consecutive quarters in a cumulative 5 year rolling period. • Large Cap Enhanced Core: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters, or the Manager's

* If Plan history with Manager is less than 5 years, use rolling 3 year period.

Watchlist Criteria	Probation Criteria
	peer ranking falls below median for more than 2 consecutive quarters in a cumulative 5 year rolling period.
International Equity • Core Non-US Equity (growth): cumulative 5 year rolling return is below the benchmark for two consecutive quarters, or the Manager's peer ranking falls below median for 2 consecutive quarters in a cumulative 5 year rolling period. • Core Non-US Equity (value): cumulative 5 year rolling return is below the benchmark for two consecutive quarters, or the Manager's peer ranking falls below median for 2 consecutive quarters in a cumulative 5 year rolling period.	**International Equity** • Core Non-US Equity (growth): cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters, or the Manager's peer ranking falls below median for more than 2 consecutive quarters in a cumulative 5 year rolling period. • Core Non-US Equity (value): cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters, or the Manager's peer ranking falls below median for more than 2 consecutive quarters in a cumulative 5 year rolling period.
Fixed Income • Aggressive Core Plus: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, or the Manager's peer ranking falls below median for 2 consecutive quarters in a cumulative 5 year rolling period. • Global Bond: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, or the Manager's peer ranking falls below median for 2 consecutive quarters in a cumulative 5 year rolling period. • Enhanced Index: cumulative 1 year rolling return is below the benchmark for two consecutive quarters, or the Manager's peer ranking falls below median for 2 consecutive quarters in a cumulative 5 year rolling period.	**Fixed Income** • Aggressive Core Plus: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters, or the Manager's peer ranking falls below median for more than 2 consecutive quarters in a cumulative 5 year rolling period. • Global Bond: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters, or the Manager's peer ranking falls below median for more than 2 consecutive quarters in a cumulative 5 year rolling period. • Enhanced Index: cumulative 1 year rolling return is below the benchmark for more than 2 consecutive quarters, or the Manager's peer ranking falls below median for more than 2 consecutive quarters in a cumulative 5 year rolling period.

SCHEDULE III

ACERA

POLICY INDEX FOR TOTAL FUND AND BENCHMARKS FOR ASSET CLASSES, EQUITY AND FIXED INCOME MANAGERS

POLICY INDEX FOR TOTAL FUND

41% Russell 3000/ 21% Lehman Aggregate/ 4% Citigroup World Government Bond Ex. U.S./ 3% Lehman High Yield/ 22% MSCI All Country World Index Ex. U.S./ 9% NCREIF Property Index

BENCHMARKS FOR ASSET CLASSES

Asset Class	**Benchmark**
U.S. Equity	Russell 3000
International Equity	MSCI ACWI-Ex. U.S.
Fixed Income	Lehman Aggregate U.S./Citigroup World Government Bond Ex U.S./ Lehman High Yield in the ratio of 75/15/10
Real Estate	NPI

BENCHMARKS FOR EQUITY AND FIXED INCOME MANAGERS[1]

Manager	**Benchmark**
U.S. Equity	
Bank of New York	S&P 500
Trust Company of the West	Russell 1000 Growth + 250 bps
Pzena	Russell 1000 Value + 200 bps
Salus	S&P 500 + 250 bps
Next Century Growth (small growth)	Russell 2000 Growth + 250 bps
Brandywine	Russell 2000 Value
Next Century Growth (micro growth)	Russell 2000 Growth + 250 bps
International Equity	
Capital Guardian	MSCI ACWI-Ex. U.S.
Mondrian	MSCI ACWI-Ex. U.S.
Fixed Income	
Loomis Sayles (Boston)	Lehman Brothers Baa Credit Index
Brandywine (Global Bond)	Citigroup World Government Bond Index
Baird	Lehman Aggregate
Real Estate[2]	

[1] Individual Manager's Contract contains more information about each Manager's benchmark.
[2] Benchmarks for real estate Managers are specified in ACERA's "Real Estate Investment Policy".

SCHEDULE IV

ACERA

MANAGER TERMINATION CHECK-LIST

This checklist is used to ensure that all details are covered when terminating investment management services.

1) Officially notify the Manager in question of the Board's decision to terminate.

2) Establish a plan of action for reallocating assets from the terminated portfolio; transfer assets to other portfolios or prepare for liquidation.

3) Review department files and logs to identify any outstanding issues.

4) Notify ACERA Administration, Accounting Division, Legal Counsel, Consultant, Custodian and any other vendors of the termination. Identify and resolve all outstanding issues with these parties.

5) Have Manager and Custodian review and sign off on monthly market values and performance figures produced during the Contract period.

6) Hold payment of last invoice until all issues are resolved.

7) Retain terminated Manager files in the ACERA office for a minimum of one year; then send to ACERA archives.

8) Hold terminated Manager files in ACERA archives for a minimum of 5 years.

SCHEDULE V*

ACERA

Compliance Schedule

REQUEST	DUE DATE
MONTHLY	
Soft Dollar Commission Report (if applicable) (Submit each month regardless of whether any commissions were directed.)	By the 20th of the month following the reported month
Minority Broker Commission Report (Submit each month regardless of whether any commissions were directed.)	By the 20th of the month following the reported month
Accounting Report/Portfolio Valuation** (Please provide transaction data – buys/sells, a portfolio listing including cost and market values, and performance returns.)	By the 20th of the month following the reported month
Derivative Report (if applicable) (Submit each month regardless of whether any derivative instruments were used.)	By the 20th of the month following the reported month
Confirmation that monthly reconciliation with Bank is performed. (Reconciliation should include market values, transactions and performance.)	By the 20th of the month following the reported month

* This Schedule is designed for all investment Managers of ACERA. However, Managers may be required to provide additional compliance reports based on their individual investment agreements with ACERA. Should there be any conflict between individual investment agreements with ACERA and ACERA's "General Investment Guidelines, Policies and Procedures," the individual investment agreements should prevail.

** 5 copies of this report shall be submitted to Staff.

REQUEST	DUE DATE
QUARTERLY	
Fee Billings (Provide all pertinent backup documentation for fee calculations.)	Within 30 days following the end of the quarter
Confirmation of compliance with limitations on investment vehicles and investment markets*	Within 30 days following the end of the quarter
Confirmation of compliance with % limitations on cash holdings, on equity investment and, on fixed-income investment*	Within 30 days following the end of the quarter
Confirmation that ACERA's assets under management does not exceed 25% of the total assets under management firm-wide	Within 30 days following the end of the quarter
Market and Portfolio Analyses and Commentaries**	Within 30 days following the end of the quarter
Additional requirements applicable to Real Estate Program***	
Operations Report/Financial Statements**	Within 60 days following the end of the quarter
Preliminary Investment Packages (applicable to Individually Managed Account)	Within 30 days following the completion of the report, if applicable
Valuation Adjustments Memo (applicable to Individually Managed Account)	Within 90 days following the anniversary date of asset acquisition
Property Valuation Report (Applicable to Individually Managed Account)	Within 90 days following the anniversary date of asset acquisition

* Detailed information can be found in "Specific Investment Guidelines" section of each Manager's investment Contract.
** 5 copies of this report shall be submitted to Staff.
*** Detailed information can be found in ACERA's "Real Estate Investment Policy."

REQUEST	**DUE DATE**
ANNUAL	
Annual Performance Fee Billing (if applicable) (Provide all backup documentation/ reconciliation sign-offs.)	Within 30 days following the end of the performance fee period
Organization Chart	Within 30 days following the end of the year or as soon as updated, whichever is earlier
Fidelity Bond/ Errors and Omissions Insurance (Please send a copy of the contractually required insurance policy and an original certificate.)	Within 30 days of renewal
Audited Financial Statements	Within 90 days following the end of the year
Form ADV, Parts I and II (if applicable)	Within 30 days of filing
Statement or Summary of Code of Ethics	Within 30 days of any change
SEC Examination Reports	Within 30 days of receipt

Additional requirements applicable to Real Estate Program***

Tactical Plans/Management Investment Plans**	Within 30 days of completion
Asset Management and Budget Plan**	Within 30 days prior to fiscal year end
Audited Financial Statement for ACERA's Fund** (applicable to Individually Managed Account)	Within 90 days following the end of the year

** 5 copies of this report shall be submitted to Staff.

*** Detailed information can be found in ACERA's "Real Estate Investment Policy."

SCHEDULE VI

ACERA

INVESTMENT PHILOSOPHY (REVISED MAY 2001)

This document describes the investment philosophy of the Alameda County Employees' Retirement Association (ACERA). Its purpose is to enunciate the basic principles and beliefs that underlie ACERA's investment policy and impact the overall management of the pension Fund. The Investment Philosophy (Philosophy) is designed to complement rather than replace the specific investment policies of ACERA. It is expected that ACERA's approach to investments, as reflected in its policies and strategies, will be consistent with the Philosophy over time. Though the Philosophy allows significant flexibility, it also raises some constraints or implications. Where these were deemed to be significant, they have been explicitly identified and labeled as *Implications*.

Future Boards may choose to amend the investment philosophy, as their experiences and circumstances will almost certainly differ. The initial document, and any subsequent changes will provide staff, advisors and future trustees with a frame of reference to help them understand how the investment program has evolved as well as the rationale behind its design. Future Boards may modify the Philosophy as their experiences and circumstances suggest is prudent.

The major sections of the Philosophy are

1. Mission
2. Risk Management
3. Diversification
4. Market Efficiency
5. High-Alpha Managers
6. Organizational Infrastructure and Communications
7. Performance Monitoring and Time Horizon

1. MISSION

a) The Board's primary goals in managing the Fund are

i) To ensure that sufficient funds are available to pay vested benefits and maintain supplemental benefits;
ii) To comply with all applicable fiduciary standards; and
iii) To create value added, where feasible, that will help reduce the costs of the plan, increase benefits, or both.

2. RISK MANAGEMENT

a) The Board believes that prudent management of risk is a central element of the investment function.

b) Though there are numerous risks involved in the management of a pension investment program, ACERA believes that the following warrant particular attention:

i) ***Funding-related Risk*** - The risk that the funds available in the Plan will be insufficient to pay the promised benefits, both vested and supplemental, or that contribution volatility will be unacceptably high. The primary methods for managing funding risk include regularly conducting integrated asset/liability studies, and establishing appropriate and prudent investment and funding policies.

0.1 In managing the relationship between assets and liabilities, the approved asset allocation of the Fund should provide an adequate level of certainty of meeting the projected liabilities of the Plan over a time period, as determined by the actuary.

ii) ***Benchmark-related Risk*** – The risk that the investment benchmarks adopted by the Fund are inappropriate, or that the aggregate of the individual Manager benchmarks within an asset class do not adequately reflect the benchmark for the asset class as a whole. The latter risk is a specific risk generally referred to as *benchmark misfit risk (i.e. style risk)*. Inappropriate benchmarks or excessive benchmark misfit risk could result in investment performance different than expected and could adversely impact decisions concerning the hiring or firing of investment managers.

0.1 The primary methods for effectively managing benchmark-related risk are
(a) regular review of the Fund's benchmarks; and
(b) regular measurement and monitoring of misfit risk using proper methodologies.

iii) ***Manager Risk*** - The risk of aberrant performance on the part of individual investment Managers, and the related active management risk for asset classes as a whole.

0.1 The primary methods for mitigating Manager risk are

(a) Prudent processes for selecting and monitoring investment Managers;

(b) Competent internal investment Staff;

(c) Effective investment consulting support; and

(d) Clear communication to investment Managers of ACERA's objectives, expectations, and investment time horizons.

0.2 The primary method for mitigating active management risk for asset classes include

(a) Establishment of appropriate asset class benchmarks;

(b) Careful monitoring of asset class performance relative to the benchmarks; and

(c) Prudent use of passive management.

iv) ***Fortitude Risk*** - The risk that the Board or Staff will fail to exercise the patience, judgment, or fortitude required to support long-term policies and strategies for the investment and funding program.

0.1 The keys to managing fortitude risk are believed to include

(a) Effective orientation and education with respect to institutional investing and actuarial science; and

(b) A commitment to continually refining, confirming, and communicating the investment philosophy and funding policy of the Association.

3. DIVERSIFICATION

a) ACERA acknowledges the basic tenets of modern portfolio theory, which suggest that diversification, or combining assets that are not perfectly correlated with each other, will reduce the long-term volatility of the overall portfolio.

b) It is generally desirable however to avoid overly complex asset structures, provided the allocation selected can reasonably be expected to meet the objectives of the Plan. ACERA believes that the benefits of diversification must be weighed against the costs involved, which may include fees, liquidity, complexity, communication, internal staff resources and expertise and trustee knowledge and effort.

c) The following asset classes are appropriate candidates for inclusion in its portfolio:
   i) Domestic equity
   ii) International equity (including emerging markets)
   iii) Fixed income, including high yield fixed income and international fixed income
   iv) Real estate

d) ACERA does not consider alternative investments to be an appropriate candidate for inclusion in its portfolio due to the substantial direct and indirect costs associated with it.

<u>Implications</u>

- A systematic methodology for re-balancing the investment portfolio is required to ensure proper implementation and adequate risk control concerning ACERA's asset allocation.
- Adding or deleting asset classes or investment Managers should be considered in light of the impact such decisions are likely to have on the general complexity and cost structure of the portfolio, as well as ACERA's ability to prudently achieve its investment and funding goals over the long run.

4. MARKET EFFICIENCY

Except for specified High-Alpha assignments:

a) ACERA does not believe in the viability of active management strategies that rely on market timing.

b) ACERA does not believe in the viability of management strategies that call for over weighting or under weighting styles or sectors within an asset class; i.e., benchmark misfit risk will not generate long-term alpha. Accordingly, ACERA generally believes that it should maintain exposures within an asset class (such as style or capitalization weightings) that are consistent with the broad benchmark for the asset class as a whole.

c) ACERA does believe that market efficiency varies among asset classes, creating opportunities for successful active management strategies based on securities selection.

d) Asset classes that can be demonstrated to be efficient should be managed passively in order to reduce active management risk and lower the costs of managing the portfolio.

e) For inefficient asset classes, ACERA believes that it has the ability and a duty to prudently exploit such inefficiencies through active securities selection strategies.

Implications

- ACERA should be conscious of any subtle forms of market timing that may arise in the course of managing the Fund, or that may be implicit in investment strategies presented to ACERA for inclusion in the investment program.

- ACERA must determine appropriate methodologies for determining whether an asset class is efficient or presents appropriate opportunities, thus providing insight to the Board on the use of particular strategies.

5. HIGH-ALPHA MANAGERS

a) ACERA believes that the portfolio characteristics utilized to control risk in the broad portfolio, such as market capitalization, sector exposure, use of derivatives, leverage limitations, property type or deal structure may be modified for specific Managers who control a limited portion of the portfolio and have demonstrated a proven capacity to consistently add value net of fees. Such strategies, which ACERA refers to as High-Alpha, may include the following elements:

   i) The bulk of the asset class is passively managed or risk controlled; and
   ii) A small number of active managers are retained who employ somewhat more aggressive investment strategies, such as concentrated portfolios, leveraged purchases, developments, high-yield debt, etc.

b) The primary benefits of including a High-Alpha approach within the overall portfolio are
   i) Reduction in active management risk;
   ii) Lower average investment fees; and
   iii) Concentration on opportunities where the likelihood of adding value is greatest.

c) The market efficiency and opportunities in asset classes may change over extended periods of time; therefore ACERA believes that its portfolio management strategies should adapt over time to reflect the changing nature of capital markets.

6. Organizational Infrastructure and Communications

a) ACERA believes that in order for the investment program to achieve its goals, ACERA must invest the necessary resources to build and maintain an appropriate organizational infrastructure, key elements of which include

i) A competent, internal investment staff comprised of a sufficient number of investment professionals possessing appropriate leadership, technical, and administrative skills.

0.1 Attracting a competent staff. ACERA recognizes that it competes with the private sector. It must therefore continually strive to create a total work environment that is challenging, rewarding, and competitive.

ii) A strong relationship with outside general investment Consultant(s) who are able to provide ACERA with the following:

0.1 A high degree of investment expertise;
0.2 Innovative and proactive advise and counsel;
0.3 Strong research support; and
0.4 Strong reporting capabilities.

iii) A broad-based information gathering and reporting system to present well-researched, relevant and timely data in a manner that is easily understood, and that supports rigorous and consistent monitoring of critical investment activities.

iv) An open channel of communication between the Board, management, and the ACERA's external investment professionals.

b) By providing the Board with timely, accurate, and thorough information, the organizational infrastructure will give the Board the high level of comfort it needs to set policy, make investment decisions, oversee the performance of the investment program, and maintain the fortitude necessary to support its investment philosophy, policies, and strategies.

Implications

- ACERA must determine what constitutes an appropriate internal investment staff structure, given the nature of the current investment program.

- ACERA must over time take concrete steps towards creating a work environment that will allow the Association to attract and retain needed staff.

- ACERA must recognize that developing its organizational infrastructure it needs – staffing, consulting support, information systems, and communication channels – cannot be achieved overnight, but rather will require an ongoing commitment of time and resources.

7. PERFORMANCE MONITORING AND TIME HORIZON

a) ACERA holds the following basic beliefs concerning performance monitoring practices and methodologies:

   i) The various investment policies of the Fund, in the aggregate, are the most important determinants of investment success; compliance with investment policies should, therefore, be monitored rigorously;

   ii) The performance of the total portfolio, individual asset classes, and investment Managers should be compared to appropriate, predetermined benchmarks;

   iii) Peer comparisons are an additional valid tool in assessing individual Manager performance (supplementing the use of benchmarks), given that ACERA aims to select superior Managers within particular investment styles or mandates. Peer comparisons, or performance rankings, are also valid tools for measuring the performance of asset class portfolios; and

iv) Peer group comparisons are not an appropriate means of assessing the performance of the total Fund, given that sponsors have different objectives and risk tolerance levels, and therefore may have different asset allocation policies.

v) Benchmark misfit risk, or the risk that the aggregate of individual investment Manager benchmarks in an asset class do not adequately reflect the benchmark for the asset class as a whole, should be explicitly measured on a regular basis.

vi) Investment Managers are generally hired to fulfill a specific role in a portfolio. Accordingly, ACERA believes it is important that ACERA monitor the extent to which Managers comply with their stated style and mandates.

b) ACERA believes that successful funding and investment decisions require a long-term perspective on the part of the Board and management:

i) It is the intention of the Retirement Board that commitments to asset classes and investment strategies should involve long time horizons that may include more than one business cycle (3-5 years each). Relatively illiquid asset classes may require even longer time horizons.

ii) The Board acknowledges that commitments to individual investment Managers also require a long time horizon of at least one business cycle (3-5 years).

iii) ACERA believes that proper reporting and monitoring systems; and clear communication among Consultants, management, investment Managers and the Board will enable the Board to maintain the necessary long term perspective on all investment decisions.

<u>Implications</u>

- Assessing the investment performance relative to appropriate, pre-determined, benchmarks is as applicable to the total portfolio and to individual asset classes as it is for individual investment Managers, and therefore warrants a commensurate share of the Board’s time and attention.

- The Board will spend relatively little time assessing the performance of the Fund relative to that of comparable pension funds.

- ACERA will need to either develop in-house capabilities to regularly measure benchmark-related risk, or it will need to purchase such capabilities from external investment Consultants.

- ACERA will monitor all investment Managers to ensure they are complying with their stated investment style, regardless of whether they are performing well or poorly. Strongly performing Managers who are found to not be following their stated styles will be carefully scrutinized and may be subject to disciplinary action.

- ACERA will monitor all investment providers to ensure compliance with ACERA's "General Investment Guidelines, Policies and Procedures."

SCHEDULE VII

CHARTER OF ACERA'S INVESTMENT COMMITTEE OF THE BOARD

To identify issues pertinent to the effective management of the investment portfolio, initiate analysis of such issues by management or consultants, review all policy recommendations by staff and consultants, provide recommendations to the Board for adoption, and oversee the implementation of the investment program. Specific responsibilities include:

1. The Investment Committee shall review recommendations of staff and consultants and in turn provide its own recommendations to the Board on all investment policies, including investment philosophy, requiring Board approval. Said policies shall normally be contained in, or appended to, the *ACERA Investment Guidelines, Policies and Procedures*.

2. The Investment Committee shall review and recommend additional policies for the Board's approval as requested by the Board and in accordance with the Policy Development Process.

3. The Investment Committee shall review recommendations of staff and consultants and in turn provide its own recommendation for Board approval on the following matters:
   a) Appointment of Investment Managers;
   b) Appointment of the Investment Consultants;
   c) Appointment of the Custodian Bank.

4. The Investment Committee shall monitor the investment program of ACERA in accordance with all relevant policies of the Board. In general, the Investment Committee shall monitor:
   a) Compliance with and continued appropriateness of all ACERA investment policies;
   b) Progress towards achievement of investment goals;
   c) Progress towards implementation of the ACERA budget and Business Plan with respect to investments; and
   d) Cost effectiveness of the ACERA investment program.

5. In accordance with the provisions of the Open Meeting Law, the Investment Committee shall allow adequate opportunity for input from the public and shall respond to such input in a manner that reflects the Committee members' fiduciary duties as trustees of the Plan.

Frequency of Meetings

The Investment Committee shall generally meet monthly on the second Wednesday of the month, but may meet more or less frequently as required.

Committee Composition

The Investment Committee shall be composed of all Board members, one of whom shall serve as Committee Chair. Alternate members shall serve on the Investment Committee as provided by law.

Staff Contact

The Chief Executive Officer shall appoint a staff person to serve as a staff contact to the Investment Committee

SCHEDULE VIII

ACERA

TABLE OF AMENDMENT DATES

AMENDING RESOLUTIONS

Jun	27,	1985
Oct.	10,	1985
Jan.	9,	1986
Jan.	16,	1986
Mar.	13,	1986
May	22,	1986
Sep.	11,	1986
Oct.	9,	1986
Nov.	20,	1986
May	14,	1987
Aug.	13,	1987
Oct.	8,	1987
Apr.	21,	1988
July	28,	1988
Jan.	29,	1989(4)
Apr.	13,	1989(5)
May	18,	1989
July	13,	1989
Aug.	10,	1989
Nov.	16,	1989(2)
July	11,	1991
June	11,	1992
June	10,	1993
July	8,	1993
Nov.	18,	1993
May	14,	1994
Aug.	18,	1994
Nov.	20,	1994
Feb.	16,	1995
May	18,	1995
Jan.	16,	1997
Aug.	20,	1998
May	20,	1999
Jan.	31,	2000
Apr.	19,	2001
Jul.	18,	2002
Feb.	21,	2003
Feb.	19,	2004
Feb.	17,	2005
Jul.	20,	2006

Alameda County Employees' Retirement Association

ACERA

GENERAL INVESTMENT GUIDELINES, POLICIES AND PROCEDURES

AMENDED June 21, 2007

ACERA
GENERAL INVESTMENT GUIDELINES, POLICIES AND PROCEDURES
2007

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ACERA
GENERAL INVESTMENT GUIDELINES, POLICIES AND PROCEDURES

[1] Prepared for ACERA by Cortex Consulting; Adopted by the Board of Retirement on March 8, 2000; Revised May 2001.

SECTION I: MISSION AND PURPOSE

The Alameda County Employees' Retirement Association (ACERA) exists for the purposes of providing accurate, timely benefits to its members and their beneficiaries and defraying reasonable expenses of administration.

The Board of Retirement (the Board), having exclusive authority and exclusive fiduciary responsibility for the investment and administration of the Trust Fund (the Fund), hereby establishes the following "General Investment Guidelines, Policies and Procedures" (the Policy) for the investment of ACERA's assets. The Board reserves the right to amend, supplement or rescind this Policy at any time.

The Board of Retirement is directed by law and given discretion to prudently invest the retirement plan assets. The purpose of this statement of policy is to assist ACERA in effectively supervising said investments and to encourage effective communication between ACERA and its investment Managers and Consultants.

ACERA's investment goal is to operate at a level of performance in the upper quartile of comparable pension funds on a risk-adjusted basis and to be as fully funded as possible so that ACERA's benefit costs do not become a burden upon future generations of members and taxpayers.

SECTION II: CONSTITUTIONAL REQUIREMENTS

Article 16 §17 of the California State Constitution provides in pertinent part as follows:

"Notwithstanding any other provisions of law or this Constitution to the contrary, the retirement board of a public pension or retirement system shall have plenary authority and fiduciary responsibility for investment of money and administration of the system, subject to the following:

a. The retirement board of a public pension or retirement system shall have the sole and exclusive fiduciary responsibility over the assets of the public pension or retirement system. The retirement board shall also have sole and exclusive responsibility to administer the system in a manner that will assure prompt delivery of benefits and related services to the participants and their beneficiaries. The assets of a public pension or retirement system are trust funds and shall be held for the exclusive purposes of providing benefits to participants in the pension or retirement system and their beneficiaries and defraying reasonable expenses of administering the system.

b. The members of the retirement board of a public pension or retirement system shall discharge their duties with respect to the system solely in the interest of, and for the exclusive purposes of providing benefits to participants and their beneficiaries, minimizing employer contributions thereto, and defraying reasonable expenses of administering the system. A retirement board's duty to its participants and their beneficiaries shall take precedence over any other duty.

c. The members of the retirement board of a public pension or retirement system shall discharge their duties with respect to the system with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with these matters would use in the conduct of an enterprise of a like character and with like aims.

d. The members of the retirement board of a public pension or retirement system shall diversify the investments of the system so as to minimize the risk of loss and to maximize the rate of return, unless under the circumstances it is clearly not prudent to do so.

e. The retirement board of a public pension or retirement system, consistent with the exclusive fiduciary responsibilities vested in it, shall have the sole and exclusive power to provide for actuarial services in order to assure the competency of the assets of the public pension or retirement system.

f. With regard to the retirement board of a public pension or retirement system which includes in its composition elected employee members, the number, terms, and method of selection or removal of members of the retirement board which were required by law or otherwise in effect on July 1, 1991, shall not be changed, amended, or modified by the Legislature unless the change, amendment, or modification enacted by the legislature is ratified by a majority of the electors of the jurisdiction in which the participants of the system are or were, prior to retirement, employed.

g. The Legislature may by statute continue to prohibit certain investments by a retirement board where it is in the public interest to do so, and provided that the prohibition satisfies the standards of fiduciary care and loyalty required of a retirement board pursuant to this section.

h. As used in this section, the term "retirement board" shall mean the board of administration, board of trustees, board of directors, or other governing body or board of a public employees pension or retirement system; provided, however, that the term "retirement board" shall not be interpreted to mean or include a governing body or board created after July 1, 1991, which does not administer pension or retirement benefits, or the elected legislative body of a jurisdiction which employs participants in a public employees pension or retirement system."

SECTION III: ROLES AND PRINCIPAL DUTIES

The Fund investments shall be prudently planned, implemented, managed, monitored and guarded. The Board, Investment Committee (the Committee), Investment Staff (Staff), General Investment Consultant (Consultant), Custodian Bank (Custodian), and Investment Managers (Manager(s)) shall coordinate this process. See the defined roles and principal duties of the above-mentioned parties below:

A. THE BOARD shall review and approve Committee recommendations. The Board also reviews, adopts and monitors all investment polices, guidelines and procedures required to prudently administer the Fund and to effectively mitigate risk to the Fund.

B. THE COMMITTEE shall identify issues pertinent to the effective investment and administration of the Fund and initiate analysis of such issues by Staff, Consultant or Managers. It also reviews Staff's and Consultant's recommendations regarding all investment policies and investment Fund management. The Committee provides recommendations to the Board for adoption, oversees implementation, and monitors the investment programs in accordance with all applicable laws and Board-established policies, guidelines and procedures. Refer to Schedule VII – Charter of ACERA's Investment Committee of the Board for detailed Committee responsibilities.

C. STAFF shall oversee the Fund's investment program activities, implement the Board/Committee's decisions, make recommendations to the Committee regarding Fund management, and recommend investment-related polices and procedures to the Committee. Additionally, Staff monitors the performance and compliance of Managers in accordance with all applicable laws, Board-established policies, guidelines and procedures, as well as "Specific Investment Guidelines" set out in the investment agreement between ACERA and each Manager (Agreement or Contract). Staff also facilitates Investment Committee meetings and completes activity as directed by the Board/Committee.

D. CONSULTANT shall review, analyze and evaluate the Fund's effectiveness and efficiency and make fund management related recommendations. Consultant assists Staff in implementing the Board/Committee's decisions and developing all investment-related policies. Consultant's responsibilities are detailed in the service agreement between ACERA and Consultant.

E. CUSTODIAN shall provide custody of ACERA's investment assets. Custodian's responsibilities are detailed in the service agreement between ACERA and Custodian.

F. MANAGER shall prudently manage its Managed Account (defined in Section VII – Eligible Asset Categories) in accordance with all applicable laws, Board-established policies, guidelines and procedures, as well as Specific Investment Guidelines. Manager's responsibilities are detailed in the Agreement.

SECTION IV: INVESTMENT PHILOSOPHY

The following is a summary of ACERA's investment philosophy. For the complete statement, please refer to Schedule VI of this document, "ACERA Investment Philosophy."

The Board believes that its investment policies, in aggregate, are the most important determinants of its investment success. Compliance with investment policies should, therefore, be monitored rigorously. The Board also believes that performance of the total portfolio, individual asset class, and Managers should be monitored and compared to appropriate, predetermined benchmarks.

The Board believes that prudent management of risk is a central element of the investment function and that diversification among asset classes will reduce risk and enhance returns of the overall investment portfolio in the long term.

The Board believes that market efficiency and opportunities vary among asset classes and may change over extended periods of time; therefore, the Board believes that ACERA's portfolio management strategies should adapt over time to reflect the changing nature of capital markets.

The Board's primary goals in managing the Fund are

1. To ensure that sufficient funds are available to pay vested benefits and maintain supplemental benefits;
2. To comply with all applicable fiduciary standards; and
3. To add marginal value that will help reduce the costs of the plan and/or to increase benefits for the beneficiaries.

The Board believes that in order to achieve its goals, ACERA must invest the necessary resources to build and maintain an appropriate organizational infrastructure.

SECTION V: ASSET ALLOCATION AND REBALANCING

Asset allocation targets, a function of the returns and risks from various asset classes and the nature of the plan's liabilities, are set forth in Schedule I. A goal of asset allocation is balancing asset growth versus liability growth considering time horizons, liabilities and risk tolerance.

Rebalancing is the risk control process of returning an allocation back to the desired target level after having drifted away from its targeted position. Equal probability bands, as defined by standard deviation factors that shall be used to define the acceptable ranges around the asset allocation targets are set forth in Schedule IA. The objective of rebalancing is to enhance the risk-adjusted performance of the asset allocation structure.

Staff shall be responsible for maintaining the relative weights of asset classes and allocations within the acceptable rebalancing ranges as reflected in Schedule IA. Should an asset class or allocation fall outside its target range, Staff shall rebalance the asset class or allocation back to the target weights as specified in the asset allocation structure in Schedule I.

Staff shall

1. Monitor the portfolio;
2. Determine whether or not any asset category is out of balance with its target asset allocation in excess of the specified tolerance range;
3. Determine whether or not any Manager within each asset category is out of balance with their target allocation in excess of the specified tolerance range;
4. And, if this is determined, either
   (a) instruct the relevant Managers to redirect cash income (interest coupon and dividends) in concert with an evaluation of pending commitments and other cash flows (employer and employee contributions), in order to bring the allocation(s) back to the adopted strategic target; and/or
   (b) instruct the relevant Managers to liquidate or acquire the appropriate dollar value of securities to reach the target and reallocate the cash thus generated or required to the other category(s) or Manager(s), as necessary.

Staff shall report to the Board on a regular basis the status of the Fund with respect to how categories are tracking relative to their allowable ranges, as well as any actions taken to rebalance the portfolio.

SECTION VI: INVESTMENT STRATEGY AND MANAGER STRUCTURE

A. U.S. EQUITY will be structured to capture exposure to the broad U.S. equity market as represented by the Russell 3000 Index. Passively managed (index) portfolios will be used in portions of the markets that are reasonably efficient. These portfolios are intended to provide broadly diversified market exposure with controlled (market) risk and minimal cost.

   Actively managed portfolios will be used when the Board determines that a Manager possesses special skills or abilities that enable that Manager to capture excess returns relative to the market, adjusted for risk and fees; or to exploit specialty markets that provide enhanced return with acceptable risk.

   A great part of the Russell 3000, on a market value basis, is comprised of large-cap stocks, which the Board believes are efficiently priced most of the time. Therefore, the Board has adopted a policy of obtaining overall exposure to this segment of the market via passively managed indexed products. Some active Managers have been employed to enhance overall portfolio return on a risk- and fee-adjusted basis. These Managers manage ACERA's "High-Alpha" program.

   The remainder of the Russell 3000 index is comprised of small to mid-cap companies. Some opportunities for active management enhancement exist in these securities due to market inefficiencies. ACERA will attempt to capture these opportunities through a mix of Managers who have the special skills required to identify smaller companies that may be undervalued or possess substantial growth potential.

The U.S. equity portfolio shall be allocated among the various styles and Managers. The U.S. equity manager structure is outlined in Schedule I.

B. INTERNATIONAL EQUITY represents an opportunity to diversify risk and capture enhanced returns within markets generally less efficient than the U.S. domestic equity market. 100% of the international equity portion of the Fund will be invested in actively managed portfolios.

The international equity portfolio shall be allocated among the various styles and Managers. The international equity manager structure is outlined in Schedule I.

C. FIXED INCOME represents a means of reducing overall portfolio risk and capturing incremental returns either domestically or globally. Inefficiencies in the pricing and trading of fixed income securities create opportunities to add value through active management. 100% of the fixed income portion of the portfolio will be invested in actively managed portfolios.

The fixed income portfolio shall be allocated among the various styles and Managers. The fixed income manager structure is outlined in Schedule I.

D. REAL ESTATE will be used as a means for diversifying the portfolio and capturing additional returns due to the low correlation between returns on real estate and financial assets. Due to the illiquid nature of real estate assets, distinctions between active and passive management are not applicable. Detailed information regarding real estate investments is included in ACERA's "Real Estate Strategic Plan," which is maintained as a separate document.

SECTION VII: ELIGIBLE ASSET CATEGORIES

The Fund shall hold assets in categories established by the Board. Any asset category may be held in direct form, in pooled form, or in both. Asset categories managed by one or more "Qualified Investment Managers" are called "Managed Accounts." Asset categories under the supervision of the County Treasurer are called the Treasurer's Accounts. Eligible asset categories are listed and defined below.

A. CASH shall consist of cash, short term (12 months or less) interest bearing investments of high quality such as U.S. Treasury issues, insured certificates of deposit of U.S. banks (fixed and/or variable), commercial paper rated A-1, P-1 or both, or other instruments of equal or better quality, and includes money market funds available through the Custodian.

B. U.S. EQUITY shall consist of common stocks and other securities which are convertible into common stocks, and ADRs (American Depository Receipts), as well as cash (per "A" above) and fixed income (per "D" below) when used as temporary substitutes for common stocks.

C. INTERNATIONAL EQUITY shall consist of common stocks and other securities convertible into common stocks of companies domiciled outside of the U.S., and GDRs

(Global Depository Receipts), as well as cash/cash equivalents (per "A" above) and fixed income (per "D" below), domestic or international, which are being used as temporary substitutes for common stock.

D. FIXED INCOME shall consist of investments in U.S. taxable bonds, debentures, notes and other evidences of debt. Fixed income may also include non-dollar denominated bonds issued by corporations or governments domiciled outside of the United States of America as well as Brady Bonds. Other eligible investments include cash/cash equivalents (per "A" above) and convertible bonds and preferred stock.

E. REAL ESTATE shall consist of investments in real estate and equity real estate through the use of commingled or direct investments. Detailed information about real estate investments is included in ACERA's "Real Estate Strategic Plan," which is maintained as a separate document.

SECTION VIII: ASSET CATEGORIES OBJECTIVES

The general objective of the Board is to preserve capital and to earn a return from appreciation and income, as described herein:

1. To ensure the integrity of ACERA's actuarial funding plan, one minimum return objective for the Fund shall be the current actuarial interest assumption rate plus 25 basis points per year over a market cycle. Returns shall be calculated net of all fees (both administrative and investment fees).
2. To ensure that ACERA's assets grow appropriately to match salary increases which directly impact benefit levels, an additional minimum return objective for the Fund over a market cycle (up to five years) shall also be 400 basis points (4%) per year over the national Consumer Price Index, published by the U.S. Department of Commerce. Returns shall be calculated gross of investment management fees.
3. To ensure that ACERA's external investment manager structure, in aggregate, is performing satisfactorily. An additional minimum return objective for the Fund over a market cycle (up to five years) shall also be equivalent to the Fund's Policy Index on a gross of investment management fee basis.

The objectives of each asset category are

A. CASH

1. A rate of return in excess of 90-Day U.S. Treasury bills, and
2. A rate of return within the upper one half of a universe of like short-term funds.

B. U.S. EQUITY

1. A rate of return in excess of the U.S. equity market as measured by the Russell 3000 Index, and

2. A rate of return within the upper 33rd percentile of the Independent Consultants Cooperative (ICC)/State Street database or similar database of the performance of diversified equity portfolios.

C. INTERNATIONAL EQUITY

1. A rate of return in excess of the Morgan Stanley Capital International All Country World Index Ex U.S. (MSCI ACWI Ex U.S.), and
2. A rate of return within the top quartile of the ICC/State Street database or similar database of the performance of diversified international equity portfolios.

D. FIXED INCOME

1. A rate of return in excess of the Lehman Aggregate Bond Index, Citigroup World Government Bond Ex. U.S. and Lehman High Yield in a ratio of 75/15/10, and
2. A rate of return within the top quartile of the ICC/State Street database or similar database of the performance of diversified fixed income portfolios.

E. REAL ESTATE

1. Total Return – a minimum total gross return equivalent to the National Council of Real Estate Investment Fiduciaries (NCREIF) Property Index (NPI) over rolling five-year periods, and
2. Income Return – Income, which is defined as cash distributed to the Association, should comprise at least 2/3 of the total expected return over rolling five-year periods for all Stable (as defined in ACERA's "Real Estate Strategic Plan") product.

In addition, objectives that reflect a particular investment strategy or style employed by an individual Manager shall be outlined in Specific Investment Guidelines attached to the Manager's Contract.

SECTION IX: ALLOCATION OF CASH FLOW

Cash flow not needed for benefit payments or administrative expenses shall be allocated to Managed Accounts in a ratio that best funds the overall targeted asset allocation as reflected in Schedules I and IA.

If cash flow is insufficient for the payment of benefits or to cover administrative expenses, then Managed Accounts shall be debited in a ratio that best satisfies the target allocation shown in Schedules I and IA. Such debits, if necessary, will be carried out as needed and with timely notice to Managers to facilitate effective funds transitions and performance measurement.

For all planned investments which may not need to be funded immediately, a reserve may be budgeted and invested in appropriate accounts in accordance with the asset allocation targets until such moneys are required. Alternatively, Managed Accounts within "overfunded" asset classes may be called upon to provide the required moneys.

SECTION X: PROHIBITED INVESTMENTS

Managers shall exercise prudent expert standards in defining prohibited investments. For example, prohibited investments include, but are not limited to, securities issued by the County of Alameda or any agency thereof.

SECTION XI: DIRECTED BROKERAGE

ACERA shall establish an open Directed Brokerage (DB) program designed to maximize the recapture of brokerage commissions by enforcement of the target percentages of direction. ACERA's DB program is governed by ACERA's DB Policy, which is maintained as a separate document.

The strategic objective of the DB program is to take advantage of the industry-accepted recapture of a portion of trade commissions paid to brokers. The primary goals of the DB program are to: 1) recapture 50% or more of commissions paid on a specific percentage of trades sent to correspondent brokers on a timely basis; 2) construct the percentage of trades subject to recapture so as to allow investment managers to have access to the research they need; 3) seek "Best Execution" through third-party administration and outside consultant monitoring; and 4) encourage local and emerging broker participation through the use of an open correspondent network program.

SECTION XII: DERIVATIVE INSTRUMENT USAGE POLICY

Exposure to risk by use of derivative instruments must be consistent with ACERA's overall investment policy as well as an individual Manager's specific investment guidelines. In general, Derivatives shall not be used to establish a leveraged position (i.e., offsetting Cash positions must be maintained against all delayed settlement transactions). Should there be any conflict between an individual Manager's Specific Investment Guidelines and the Derivative Instrument Usage Policy, the Specific Investment Guidelines shall prevail.

SECTION XIII: SELECTION OF INVESTMENT MANAGERS

The Investment Committee shall direct Staff and/or a Consultant to initiate searches for Managers. Staff and/or the Consultant shall research for qualified candidates and present a list of finalists to the Investment Committee for its approval. Upon approval of the list, the finalists shall be interviewed by Staff and the Consultant (if applicable). Staff and the Consultant (if applicable) shall evaluate the interviews, rank the finalists, and make a recommendation to the Investment Committee to hire one or more firms attaining the highest rankings in a publicly noticed meeting at which no less than five (5) Investment Committee members shall be present. It is possible that none of the firms will be recommended for hire**.**

These procedures are developed for the convenience and benefit of ACERA, and shall not bind ACERA or invalidate the selection of a Manager, if different processes are used subsequent to the promulgation of this Policy.

SECTION XIV: EMERGING INVESTMENT MANAGERS

The Board has established the ACERA Emerging Investment Manager Policy ("EM Policy"), which is maintained as a separate document. The purpose of the EM Policy is to establish a framework for the development and administration of ACERA's Emerging Investment Manager Program ("EM Program"), consistent with the Board's fiduciary responsibilities in the investment of the Fund.

The strategic objective of the EM Program is to add incremental value to the Fund through the hiring of the most talented Emerging Investment Managers (EMs) to manage ACERA's assets.

The primary goals of the EM Program are to 1) identify and gain early access to the most talented investment managers in their early business stages; 2) generate superior Fund return performance through the EM Program; 3) identify superior EMs and/or investment opportunities in California and Alameda County that are equal to or superior to comparable available investments; and 4) further diversify the Fund's overall investment program, so as to enhance risk-adjusted returns of the Fund.

SECTION XV: AUTHORITY OF INVESTMENT MANAGERS

Subject to the laws of the United States and the State of California, and to the terms and conditions of this Policy, Managers shall have full discretion to direct the purchase, exchange, sale and reinvestment of the assets of the Managed Accounts. The Board expects that Managers will recommend changes to this Policy when any part of this Policy appears to be at variance with overall market and economic conditions.

Managers shall place orders to buy and sell securities and, by notice to the Custodian, shall cause the Custodian to deliver and receive securities on behalf of the Fund. Managers shall, upon Board inquiry, report placement of ACERA brokerage such that the Board shall be assured commissions were placed for the sole and exclusive benefit of the Fund.

Separate account Managers shall not vote proxies. Proxies shall be voted by ACERA, via a proxy voting service vendor, in accordance with "ACERA Proxy Voting Guidelines and Procedures" which is maintained as a separate document.

Securities lending shall be performed under the oversight of Staff, in accordance with Board-established policies and procedures.

SECTION XVI: INVESTMENT GUIDELINES FOR THE MANAGED ACCOUNTS

Individual Manager discretion shall be governed by the Investment Guidelines for the Managed Accounts as well as the Specific Investment Guidelines for each Manager. Should there be any conflict between the Specific Investment Guidelines of an individual Manager and the Investment Guidelines for the Managed Accounts, the Specific Investment Guidelines shall prevail.

A. GENERAL

1. All investments shall comply with all applicable laws of the United States and the State of California governing the investment of pension trusts.
2. All securities transactions shall be executed by reputable broker/dealers, banks, or the Custodian, and shall be on a best-price and best-execution basis, and shall be reported to ACERA as is called for elsewhere in this Policy.
3. All Managers shall refrain from investing in a tobacco producer investment opportunity when, in their expert opinion, an alternative non-tobacco producer investment opportunity is available that will satisfy the same ACERA portfolio guidelines, instructions and objectives for risk, return and diversification.

B. EQUITY

Managers have full discretion to invest solely in readily marketable and diversified equity securities subject to the following:

1. For Managed Accounts, no more than 10% of the value (at time of purchase) of the account shall be invested in the securities of a single issuer.
2. ACERA shall not hold more than 10% of the equity securities of any issuer.
3. Equity securities shall possess value and quality corroborated by generally accepted techniques and standards of fundamental securities analysis.
4. Assets in a Managed Account not invested in equity securities shall be kept with interest in appropriate money market instruments, including any money market fund available through the Custodian.
5. A Managed Account shall be subject to ACERA's policy on derivatives.
6. All Managers shall endeavor to be fully invested in stocks at all times unless they have received specific authorization to the contrary from the Board. Cash holdings, as defined in this Policy, shall generally not exceed 5% of the portfolio on a market value basis.

C. FIXED INCOME

Managers have full discretion to invest solely in readily marketable and diversified securities including, but not limited to

1. Obligations of the U.S. and/or eligible foreign government's Treasuries.
2. Obligations guaranteed by agencies of the United States and/or eligible foreign governments.
3. Insured certificates of deposit and banker's acceptances of credit worthy banks.
4. Corporate and other evidences of debt. At least 80% of this debt must be rated by Moody's Investor's Services or by Standard & Poors.
5. Commercial paper and banker's acceptances of issuers rated P-1 by Moody's Investor's Service.
6. Or A-1 by Standard & Poors Corporation.

7. Excepting direct obligations of the U.S. and/or eligible foreign governments, and those explicitly guaranteed by the U.S. and/or eligible governments, no account shall hold more than 5%, at cost, of the obligations of any single issuer.
8. Excepting direct obligations of the U.S. and/or eligible foreign governments, and those explicitly guaranteed by the U.S. and/or eligible governments, no security shall comprise more than 5% of the account, as determined at the time of purchase.
9. Fixed income derivative investments shall be in accordance with ACERA's derivative policy.

SECTION XVII: INVESTMENT MANAGER SPECIFICATIONS

A. Managers must be registered as investment advisers under the Investment Adviser's Act of 1940, a bank (as defined in that Act) or an insurance company qualified to perform investment management services under state law in more than one state, including California. Unless an exception is granted by the Board, by accepting appointment as ACERA's Managers, Managers shall acknowledge that they are "Plan Fiduciaries" and "Qualified Investment Managers" as defined by the Employees' Retirement Income Security Act (ERISA) of 1974, (see or reference United States Code Title 29 Section 1001 et. seq.)

B. Managers shall maintain fiduciary insurance in the amount of 10% of the total assets managed in the ACERA account or $25 million, whichever is higher, unless the Contract specifies otherwise.

C. Managers shall promptly notify ACERA of changes that occur in any of the following:

    1. The investment strategy used in managing the subject product.
    2. The key personnel involved in managing ACERA's account.
    3. The ownership, key personnel, or organizational structure of the Manager's company.
    4. The Manager company's financial condition.
    5. The number of clients invested in the subject product and firm wide.
    6. The market value of the total assets managed in the subject product and firm wide.

D. Managers shall promptly notify ACERA if they are subject to censure or disciplinary action by a regulatory agency.

E. Managers shall provide to ACERA all required documents and reports as set forth in Schedule V – ACERA's Compliance Schedule.

F. Managers shall not make contributions, provide gifts, reimbursements of expenses or provide personal benefits exceeding $250 in the aggregate within any 12-month period to any Trustee, fiduciary, employee or Consultant of ACERA. Donations of educational conferences and similar events and benefits, including travel, meals and accommodations will be made to ACERA and not directed to individuals. The Board will determine whether to accept any donations and will be solely responsible for selection of the Trustee, Staff, or other individual, who will attend or otherwise participate on behalf of ACERA.

SECTION XVIII: MANAGER MONITORING PROCEDURE

The Board has contracted with a number of external Managers to invest ACERA assets in the capital markets. As part of the Board's fiduciary duties to prudently select, monitor and supervise these Managers, the Board has adopted this Procedure. The intent of this Procedure is to notify Managers of the standards by which they will be evaluated and to establish a structure which the Investment Committee and the Board can use to monitor the performance of the Managers.

Managers will be monitored to

1. Evaluate how well they achieve their investment objectives.
2. Ensure that they adhere to their established investment approach/style and do not attempt to index returns to preserve stellar performance or take extraordinary risk to overcome poor performance.
3. Identify issues or trends that have the potential to result in losses to the Fund.
4. Alert the Board when Managers are not performing to expectations so that appropriate remedial action can be taken.

Managers will be evaluated on the basis of the following: performance, style integrity, organizational stability, compliance, client service, and fees described in greater detail below.

A. PERFORMANCE

On a monthly basis Staff will monitor Manager holdings, activity, and performance.

On a quarterly basis Staff and/or a Consultant will furnish the Investment Committee and/or Board with an in-depth evaluation of each Manager which will include a comparison of the Manager to its Contract benchmark and a peer universe of Managers using a similar investment style. This report shall include an analysis of the sources of Managers' returns (stock selection, industry selection, asset allocation, etc.) and shall identify which decisions enhanced or diminished performance.

On a quarterly basis, trading costs will be evaluated in terms of commissions paid and execution of trades. Staff and/or Consultants shall furnish a report to the Investment Committee and/or Board regarding trading costs on an annual basis.

B. STYLE INTEGRITY

Each Manager will be analyzed at least annually to ensure that the Manager is continuing to invest the portfolio in the style for which they were originally hired. Style integrity is essential to maintain the Board's asset allocation policy. Any significant deviation in style will result in the overall portfolio having a different characteristic, in some measure, from the broad market which is represented by the Russell 3000 index. Significant variations in the portfolio characteristics from the style anticipated in the management Contract may indicate a change in its investment style.

This review also provides the Investment Committee and/or Board an opportunity to evaluate the Manager's continuing "fit" with the goals of the overall Fund. By monitoring the Manager style integrity, the Investment Committee and/or Board can assure that its Manager mix takes advantage of opportunities to increase diversification through lower correlation of returns among individual Managers.

C. ORGANIZATIONAL STABILITY

Managers' organizations will be monitored to ensure continuity of the intellectual and philosophical processes that went into developing the particular investment approach contracted for by ACERA. In addition, Managers will be monitored for business risk, quality of staff, departures of key investment personnel, change in ownership or acquisition, and potential conflicts of interest.

It is ACERA's intent that its portfolio comprises no more than 25% of the Manager's total assets under management (AUM)[2] at any time. Therefore, ACERA will monitor the Managers' assets, firm-wide, as well as in the subject product.

D. COMPLIANCE

Managers will be monitored to ensure they are adhering to federal and state laws regarding securities and the management of investment portfolios, trading, and pension investments; ethical practices of the investment professions; the Contract governing their relationship with ACERA; this Policy; and any other written directives issued by ACERA.

Each ACERA Contract will specify which investment vehicles a Manager is authorized to use, which markets the Manager is authorized to transact business in and any limitations within a market (small or large capitalization, value or growth orientation). The assets in each Manager's portfolio shall be reviewed monthly to ensure compliance with Contract guidelines.

All required documents and reports, set forth in Schedule V, must be submitted in a timely manner and in the format specified by ACERA.

Managers must provide prior notification and justification for failure to comply with rules, regulations, Contract provisions, deadlines or other directives. Managers must provide a time frame for curing any deficiencies. Staff shall evaluate each incident on a case-by-case basis and determine whether an exception may be granted.

E. CLIENT SERVICE

Managers are required to comply with routine portfolio investment guidelines and reporting deadlines and are also expected to cooperate with special requests for information. ACERA will establish reasonable time frames for all requests and reporting and will provide feedback to all external Managers regarding the perceived quality of their client service.

[2] ACERA defines total AUM as the total market value of assets a Manager manages on behalf of investors under discretionary management where the client delegates responsibility to the Manager.

F. FEES

Managers are expected to charge ACERA investment management fees no greater than the fees charged for other clients with a similar investment style, investment objective, and account type, size and services. Should a Manager enter into a more favorable fee schedule with a similar client, the manager is expected to modify ACERA's fee schedule to reflect the more favorable terms.

ACERA Staff will endeavor to meet with each Manager at least twice a year by telephone or in person to review performance and other issues.

SECTION XIX: CONTRACT REVIEW PROCESS

If during the course of regular monitoring, ACERA determines that a Manager's performance, style integrity, organizational stability, compliance, client service, and/or fees have reached to unacceptable levels, ACERA may, at its discretion, subject the Manager to ACERA's Contract Review Process. As part of the Board's fiduciary duties to prudently select, monitor and supervise their Managers, the Board has approved this process. The purpose of this process is to ensure as little disruption as possible in the event that concerns or problems arise with respect to a Manager's performance. The Board does not confer any additional rights or protections to its Managers by the promulgation of this Policy and/or this process.

There are generally three stages of review: Watchlist, Probation, and Termination (described below). ACERA reserves the right to terminate an investment management Contract at any time, with or without 30 days notice, for any reason, and without resort to this Contract Review Process.

The Contract Review Process may result in one or more of the following:

1. Placement on Watchlist or Probation status.
2. Movement from one stage of review to another, or removal from the Contract Review Process.
3. Reduction of assets under management.
4. Revision of investment Contract guidelines for that Manager.
5. Re-negotiation of fees.
6. Termination of a Manager's Contract.
7. Any other actions deemed appropriate by the Board

Each situation is unique. Action by the Board will vary depending on the type of Manager, the style/strategy, and the deficiency involved. The following describes the Contract Review Process:

A. INITIAL REVIEW

Prior to a Manager being considered for Watchlist, Probation or Termination, ACERA may take the following steps:

1. Analysis

   Staff will conduct in-depth analyses of the perceived deficiency to verify that a deficiency exists, form an initial assessment of the severity of the deficiency, and make an initial determination of possible causes.

2. Discussion with the Manager

   Staff will contact the Manager to discuss the situation and the results of Staff's analysis.

3. Consultant Input

   ACERA may seek the services of Consultant to provide additional assessment and advice regarding the situation, depending on the severity of the deficiency.

All phases of account compliance may be reviewed during this step, in addition to the specific issue that originated the Review Process.

B. FORMAL ACTION

After completing the Initial Review, Staff may recommend to the Investment Committee and/or Board that the Manager be either placed on Watchlist or Probation or, in certain cases, Terminated. The Committee and/or Board will approve or reject the recommendation. However, if a Manager's deficiency satisfies the criteria as listed under Watchlist and Probation in this Review Process, Staff may place a Manager on Watchlist or Probation without the Committee and/or Board's prior approval. In that case, Staff will be required to report to the Committee on the action taken in this Review Process as soon as possible. The specific criteria for determining which stage of Contract Review to recommend is outlined later in this Policy section and summarized in tabular form in Schedule II.

Upon approval of a Watchlist or Probation recommendation:

1. Staff will notify the Manager of the Board's decision and will provide the Manager with a statement of concerns which outlines the areas which need improvement.
2. The Manager will be asked to respond in writing with an explanation of the issues and a proposed action plan to resolve the issues within 30 days of receipt of the statement of concerns.
3. Staff, a Consultant and the Manager will collectively draft a Plan of Action. The plan will identify the specific steps to be taken to correct the problem; the time frames for further review; and what additional monitoring may be required.

At the end of the time period specified in the Plan of Action, the Manager will be evaluated and one of the following actions may be taken:

(a) Removal from Contract Review: if the Manager successfully resolves the issues/deficiencies and demonstrates continued success in all other areas of its relationship with ACERA.
(b) Movement from Probation to Watchlist: if the Manager has satisfied all or most of the issues/deficiencies that caused it to be placed on Probation, yet Staff continues to have concerns about the Manager. If circumstances warrant, a Manager may also be moved from Watchlist to Probation at any time during the Contract Review Process.
(c) Extension of Contract Review: a Manager may be given additional time to satisfy the conditions of its Action Plan if reasonable progress is being made. Extensions may also be granted if unfavorable market conditions or high costs make reallocation of assets inadvisable.
(d) Termination: if the Manager has not satisfactorily resolved the issues/deficiencies, Staff may recommend termination as described below. Termination may be recommended at any time during the Contract Review Process if circumstances warrant.

WATCHLIST

Watchlisting indicates an increased level of concern, but does not indicate major deficiencies. The Watchlisting period is typically one year. Staff shall conduct a comprehensive evaluation of the Manager at the end of the one-year Watchlisting period to determine whether the Manager may be removed from Watchlist status. Any of the following may result in a Watchlist status:

A. UNDERPERFORMANCE

Please refer to Schedule II for specific Watchlist criteria for each Manager.

B. STYLE DEVIATION

Managers are expected to adhere to the style of investment management for which ACERA originally hired them. Changes in portfolio characteristics or style drift may lead to a Watchlist status.

C. ORGANIZATIONAL CHANGE

1. New Ownership

   Even relatively benign ownership changes, which impact personnel key to ACERA's portfolio management may be cause for a Watchlist status.

2. Turnover

   Significant turnover or reassignment in top management, portfolio Managers, research or trading staff, or marketing personnel may warrant Watchlisting.

3. Reorganization

   Changes which signal management deterioration, departures or reassignment of key investment personnel, a change in ownership that increases risk to ACERA's investments, or hasty, uncontrolled growth in the firm with potential to disrupt the investment team hired for management of ACERA's account will mandate Watchlisting.

4. Assets Under Management

   If the market value of ACERA's portfolio rises above 25% of the Manager's total AUM, Watchlist status may be warranted.

D. NONCOMPLIANCE

1. Contracts and Other Agreements

   Managers are expected to comply with the investment management Contract, investment guidelines, or other directives. Non- or partial compliance may result in a Watchlist status.

2. Reporting

   Staff will contact Managers to request past due reports. If the Manager's reports are consistently delinquent, the payment of fees may be delayed. If a Manager cannot comply with reporting deadlines, ACERA should be given prior notification. If warranted, a variance may be allowed. Managers are expected to resolve reporting problems immediately upon notification by ACERA. Repeated delinquency in reporting may result in a Watchlist status.

E. POOR CLIENT SERVICE

If a Manager is uncooperative and demonstrates a poor client service attitude, Watchlisting is appropriate. Managers are expected to resolve client service issues immediately upon notification by ACERA.

F. HIGH FEES

Watchlisting may be appropriate if a Manager

1. charges ACERA unreasonably high fees relative to what it charges its other clients with a similar investment style, investment objective, and account type, size and service, and/or
2. charges ACERA unreasonably high fees relative to the current market fee rate.

PROBATION

Probation indicates a level of serious deficiency and signals a need for closer contact with the firm. Probation necessitates a cautious, observant relationship with the Manager.

Managers may be placed on Probation with or without first being placed on Watchlist status. The Probation period is typically one year. Staff shall conduct a comprehensive evaluation of the Manager at the end of the one-year Probation period to determine whether the Manager may be removed from Probation status.

The following may result in Probation:

A. UNDERPERFORMANCE

Please refer to Schedule II for specific Probation criteria for each Manager.

B. STYLE DEVIATION

Probation may be warranted when a Manager's portfolio characteristics are significantly different from its contractually specified style. In general, a Manager will be placed on Probation after four or more consecutive quarters of deviating from its style benchmark. In effect, if the Manager is no longer the same Manager that was retained for ACERA's account, Probation and perhaps even Termination is appropriate.

C. ORGANIZATIONAL CHANGE

Changes in ownership, organizational assignments, departures of key investment personnel, a change in ownership that poses substantial risk to ACERA's investments, or turnover that have the potential to seriously disrupt or destroy the investment management team that was hired to manage the ACERA account may result in Probation or Termination. When key personnel, such as top management, portfolio Managers, research and trading staff are no longer available for use on the ACERA portfolio and do not appear to be replaced or replaceable, Probation and perhaps even Termination is appropriate.

D. NONCOMPLIANCE

If a Manager does not comply with securities laws, industry regulations, standards of professional conduct or contractual provisions, Probation is appropriate. Certain circumstances may warrant Termination.

E. POOR CLIENT SERVICE

Failure to correct any issues that previously resulted in the Watchlist status shall result in Probation. Managers will generally be given one quarter to resolve client service issues.

F. HIGH FEES

Failure to reduce unreasonably high investment management fees shall result in Probation.

TERMINATION

Upon determining that the Manager has not made adequate improvement in the areas outlined in the Plan of Action, Staff may recommend to the Investment Committee and/or Board that the Manager be terminated. Prior to making the final decision to terminate the Manager, the Investment Committee may invite the Manager to make a presentation at the meeting in which the Termination recommendation is to be discussed. Staff will have analyzed the liquidity of the Manager's portfolio and will have a recommendation and plan for disposition of the assets.

Upon the Investment Committee's decision to terminate, Staff will notify the accounting division as well as the Board's legal counsel of the action. All outstanding issues between the Manager and ACERA's Master Custodian, brokers, Consultant, or other parties shall be resolved prior to closing out the Contract. The Manager Termination checklist is attached as Schedule IV.

The Contract Review Process described in this Policy does not provide any additional rights or protections to Managers, beyond what is provided in the Contract. The Board reserves the right to terminate an investment management Contract without resort to the Contract Review Process, at any time, with or without 30 days notice, for any reason.

SCHEDULE I

ACERA

ASSET ALLOCATION AND MANAGER STRUCTURE TARGETS

ASSET ALLOCATION TARGETS

Asset Class	Target Allocation %	
U.S. Equities	41	
U.S. Large Cap		34
U.S. Small Cap		7
International Equities	22	
Fixed Income	28	
Real Estate	9	

MANAGER STRUCTURE TARGETS

Managers		Target Allocation % Within Asset Class	Target Allocation % Within Total Fund
U.S. Equity			
Large Cap Core Index	Bank of New York	43	17.6
Large Cap Growth (Hi-Alpha)	Trust Company of the West	17.5	7.2
Large Cap Value (Hi-Alpha)	Pzena	17.5	7.2
Large Cap Enhanced Core (Hi-Alpha)	Salus	5	2.0
Small Cap Growth	Next Century Growth	6	2.5
Micro Cap Growth	Next Century Growth	2.5	1.0
Small Cap Value	Brandywine	8.5	3.5
International Equity			
Core Non-US Equity (growth)	Capital Guardian	45	9.9
Core Non-US Equity (value)	Mondrian	35	7.7
Core Non-US Equity (quantitative)	TBD	20	4.4
Fixed Income			
Enhanced Index	Baird	55	15.4
Aggressive Core Plus	Loomis Sayles	25	7
Global Bond	Brandywine	20	5.6

Real Estate[3]

[3] ACERA's real estate manager structure targets are specified in ACERA's "Real Estate Strategic Plan."

SCHEDULE IA

ACERA

ASSET ALLOCATION PORTFOLIO REBALANCING

The objective of rebalancing is to control risk and enhance the risk-adjusted return of the asset allocation strategy. For purposes of enhancing the risk-adjusted return of the asset allocation structure, the relative deviation of any liquid sub asset class away from its target weight (or liquidity-adjusted target weight) shall be no more than plus or minus 1.80 standard deviation factors of each allocation's expected volatility, relative to the other allocations in the asset mix. This standard deviation factor shall be used to define the range of allowable deviation from Policy target asset allocations. If any sub asset class reaches its allowable deviation from its target allocation, all sub asset classes will be evaluated.

The actual reallocation will be at the discretion of Staff (with oversight by the rebalancing Consultant) after reviewing the following: the relative magnitude of deviation from target for all other sub asset classes; the available cash liquidity of sub asset classes that could be used to fund rebalancing; pending cash flows (employer and employee contributions, or proceeds from a terminated Manager's portfolio); pending liquidity windows with commingled investment pools; pending investment commitments (real estate transactions and/or new funding commitments); and pending interest coupon and dividend cash flows.

Asset allocation and rebalancing status reports, and any rebalancing activity taken toward attaining the objective of the rebalancing program will be reported to the Board of Trustees in a timely fashion or whenever a rebalancing transaction occurs.

Significant modifications to the asset allocation strategy shall be cause to review the appropriateness of maintaining this rebalancing parameter or revising it to a parameter more suitable to the revised asset allocation structure.

SCHEDULE II

ACERA

Watchlist/Probation Criteria for Performance [4]

Watchlist Criteria	**Probation Criteria**
US Equity • Large Cap Core Index: negative tracking error exceeds 5 bps on an annualized basis in any 1 year period. • Large Cap Growth: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, or the Manager's peer ranking falls below median for 2 consecutive quarters in a cumulative 5 year rolling period. • Large Cap Value: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, or the Manager's peer ranking falls below median for 2 consecutive quarters in a cumulative 5 year rolling period. • Small/Micro Cap Growth: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, or the Manager's peer ranking falls below median for 2 consecutive quarters in a cumulative 5 year rolling period. • Small Cap Value: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, or the Manager's peer ranking falls below median for 2 consecutive quarters in a cumulative 5 year rolling period. • Large Cap Enhanced Core: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, or the Manager's peer ranking falls below median for 2 consecutive quarters in a cumulative 5 year rolling period.	**US Equity** • Large Cap Core Index: negative tracking error exceeds 5 bps on an annualized basis in any period greater than 1 year, or negative tracking error exceeds 10 bps for any 2 consecutive quarters. • Large Cap Growth: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters, or the Manager's peer ranking falls below median for more than 2 consecutive quarters in a cumulative 5 year rolling period. • Large Cap Value: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters, or the Manager's peer ranking falls below median for more than 2 consecutive quarters in a cumulative 5 year rolling period. • Small/Micro Cap Growth: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters, or the Manager's peer ranking falls below median for more than 2 consecutive quarters in a cumulative 5 year rolling period. • Small Cap Value: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters, or the Manager's peer ranking falls below median for more than 2 consecutive quarters in a cumulative 5 year rolling period. • Large Cap Enhanced Core: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters, or the Manager's

[4] If the Fund history with Manager is less than 5 years, use rolling 3 year period.

Watchlist Criteria	Probation Criteria
	peer ranking falls below median for more than 2 consecutive quarters in a cumulative 5 year rolling period.
International Equity • Core Non-US Equity (growth): cumulative 5 year rolling return is below the benchmark for two consecutive quarters, or the Manager's peer ranking falls below median for 2 consecutive quarters in a cumulative 5 year rolling period. • Core Non-US Equity (value): cumulative 5 year rolling return is below the benchmark for two consecutive quarters, or the Manager's peer ranking falls below median for 2 consecutive quarters in a cumulative 5 year rolling period.	**International Equity** • Core Non-US Equity (growth): cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters, or the Manager's peer ranking falls below median for more than 2 consecutive quarters in a cumulative 5 year rolling period. • Core Non-US Equity (value): cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters, or the Manager's peer ranking falls below median for more than 2 consecutive quarters in a cumulative 5 year rolling period.
Fixed Income • Aggressive Core Plus: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, or the Manager's peer ranking falls below median for 2 consecutive quarters in a cumulative 5 year rolling period. • Global Bond: cumulative 5 year rolling return is below the benchmark for two consecutive quarters, or the Manager's peer ranking falls below median for 2 consecutive quarters in a cumulative 5 year rolling period. • Enhanced Index: cumulative 1 year rolling return is below the benchmark for two consecutive quarters, or the Manager's peer ranking falls below median for 2 consecutive quarters in a cumulative 5 year rolling period.	**Fixed Income** • Aggressive Core Plus: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters, or the Manager's peer ranking falls below median for more than 2 consecutive quarters in a cumulative 5 year rolling period. • Global Bond: cumulative 5 year rolling return is below the benchmark for more than 2 consecutive quarters, or the Manager's peer ranking falls below median for more than 2 consecutive quarters in a cumulative 5 year rolling period. • Enhanced Index: cumulative 1 year rolling return is below the benchmark for more than 2 consecutive quarters, or the Manager's peer ranking falls below median for more than 2 consecutive quarters in a cumulative 5 year rolling period.

SCHEDULE III

ACERA

POLICY INDEX FOR TOTAL FUND AND BENCHMARKS FOR ASSET CLASSES, EQUITY AND FIXED INCOME MANAGERS

POLICY INDEX FOR TOTAL FUND

41% Russell 3000/ 21% Lehman Aggregate/ 4% Citigroup World Government Bond Ex. U.S./ 3% Lehman High Yield/ 22% MSCI All Country World Index Ex U.S./ 9% NCREIF Property Index

BENCHMARKS FOR ASSET CLASSES

Asset Class	Benchmark
U.S. Equity	Russell 3000
International Equity	MSCI ACWI Ex. U.S.
Fixed Income	Lehman Aggregate U.S./Citigroup World Government Bond Ex U.S./ Lehman High Yield in the ratio of 75/15/10
Real Estate	NPI

BENCHMARKS FOR EQUITY AND FIXED INCOME MANAGER[5]

Manager	Benchmark
U.S. Equity	
Bank of New York	S&P 500
Trust Company of the West	Russell 1000 Growth + 250 bps
Pzena	Russell 1000 Value + 200 bps
Salus	S&P 500 + 250 bps
Next Century Growth (small growth)	Russell 2000 Growth + 250 bps
Next Century Growth (micro growth)	Russell 2000 Growth + 250 bps
Brandywine	Russell 2000 Value
International Equity	
Capital Guardian	MSCI ACWI Ex U.S.
Mondrian	MSCI ACWI Ex U.S.
TBD	MSCI ACWI Ex U.S.
Fixed Income	
Loomis Sayles (Boston)	Lehman Brothers Baa Credit Index
Brandywine (Global Bond)	Citigroup World Government Bond Index
Baird	Lehman Aggregate
Real Estate[6]	

[5] Individual Manager’s Contract contains more information about each Manager’s benchmark.
[6] Benchmarks for real estate Managers are specified in ACERA’s “Real Estate Strategic Plan.”

SCHEDULE IV

ACERA

MANAGER TERMINATION CHECK-LIST

This checklist is used to ensure that all details are covered when terminating investment management services.

1) Officially notify the Manager in question of the Board's decision to terminate.

2) Establish a plan of action for reallocating assets from the terminated portfolio; transfer assets to other portfolios or prepare for liquidation.

3) Review department files and logs to identify any outstanding issues.

4) Notify ACERA Administration, Accounting Division, Legal Counsel, Consultant, Custodian and any other vendors of the termination. Identify and resolve all outstanding issues with these parties.

5) Have Manager and Custodian review and sign off on monthly market values and performance figures produced during the Contract period.

6) Hold payment of last invoice until all issues are resolved.

7) Retain terminated Manager files in the ACERA office for a minimum of one year; then send to ACERA archives.

8) Hold terminated Manager files in ACERA archives for a minimum of 5 years.

SCHEDULE V[7]

ACERA

Compliance Schedule

REQUEST	**DUE DATE**
MONTHLY	
Soft Dollar Commission Report (if applicable) (Submit each month regardless of activity.)	By the 20th of the month following the reported month
Minority Broker Commission Report (Submit each month regardless of activity.)	By the 20th of the month following the reported month
Accounting Report/Portfolio Valuation (Please provide transaction data – buys/sells, a portfolio listing including cost and market values, and performance returns.)	By the 20th of the month following the reported month
Derivative Report (if applicable) (Submit each month regardless of whether any derivative instruments were used.)	By the 20th of the month following the reported month
Confirmation that monthly reconciliation with Bank is performed. (Reconciliation should include market values, transactions and performance.)	By the 20th of the month following the reported month
Overall compliance checklist	By the 20th of the month following the reported month

[7] This Schedule is designed for all investment Managers of ACERA. However, Managers may be required to provide additional compliance reports based on their individual investment agreements with ACERA. Should there be any conflict between individual investment Agreements with ACERA and ACERA's "General Investment Guidelines, Policies and Procedures," the individual investment Agreements shall prevail.

REQUEST	DUE DATE
QUARTERLY	
Fee Billings (Provide all pertinent backup documentation for fee calculations.)	Within 30 days following the end of the quarter
Confirmation of compliance with limitations on investment vehicles and investment markets[8]	Within 30 days following the end of the quarter
Confirmation of compliance with % limitations on cash holdings, on equity investment and, on fixed-income Investment[8]	Within 30 days following the end of the quarter
Confirmation that ACERA's assets under management does not exceed 25% of the total assets under management firm-wide	Within 30 days following the end of the quarter
Market and Portfolio Analyses and Commentaries	Within 30 days following the end of the quarter

Additional requirements applicable to Real Estate Program[9]

Operations Report/Financial Statements	Within 60 days following the end of the quarter
Preliminary Investment Packages (applicable to Individually Managed Account)	Within 30 days following the completion of the report, if applicable
Valuation Adjustments Memo (applicable to Individually Managed Account)	Within 90 days following the anniversary date of asset acquisition
Property Valuation Report (Applicable to Individually Managed Account)	Within 90 days following the anniversary date of asset acquisition

[8] Detailed information can be found in "Specific Investment Guidelines" section of each Manager's investment Contract.
[9] Detailed information can be found in ACERA's "Real Estate Strategic Plan."

REQUEST	DUE DATE
ANNUAL	
Annual Performance Fee Billing (if applicable) (Provide all backup documentation/ reconciliation sign-offs.)	Within 30 days following the end of the performance fee period
Organization Chart	Within 30 days following the end of the year or as soon as updated, whichever is earlier
Fidelity Bond/ Errors and Omissions Insurance (Please send an original certificate.)	Within 30 days of renewal
Audited Financial Statements	Within 90 days following the end of the year
Form ADV, Parts I and II (if applicable)	Within 30 days of filing
Statement or Summary of Code of Ethics	Within 30 days of any change
SEC Examination Reports	Within 30 days of receipt

Additional requirements applicable to Real Estate Program[10]

Tactical Plans/Management Investment Plans[11] (applicable to Individually Managed Account)	Within 30 days of completion
Asset Management and Budget Plan[11] (applicable to Individually Managed Account)	Within 30 days prior to fiscal year end
Audited Financial Statement for ACERA's Fund (applicable to Individually Managed Account)	Within 90 days following the end of the year

[10] Detailed information can be found in ACERA's "Real Estate Strategic Plan."
[11] 7 copies of this report shall be submitted to Staff.

SCHEDULE VI

ACERA

INVESTMENT PHILOSOPHY (REVISED MAY 2001)

This document describes the investment philosophy of the Alameda County Employees' Retirement Association (ACERA). Its purpose is to enunciate the basic principles and beliefs that underlie ACERA's investment policy and impact the overall management of the pension Fund. The Investment Philosophy (Philosophy) is designed to complement rather than replace the specific investment policies of ACERA. It is expected that ACERA's approach to investments, as reflected in its policies and strategies, will be consistent with the Philosophy over time. Though the Philosophy allows significant flexibility, it also raises some constraints or implications. Where these were deemed to be significant, they have been explicitly identified and labeled as *Implications*.

Future Boards may choose to amend the investment philosophy, as their experiences and circumstances will almost certainly differ. The initial document and any subsequent changes will provide staff, advisors and future trustees with a frame of reference to help them understand how the investment program has evolved as well as the rationale behind its design. Future Boards may modify the Philosophy as their experiences and circumstances suggest is prudent.

The major sections of the Philosophy are

1. Mission
2. Risk Management
3. Diversification
4. Market Efficiency
5. High-Alpha Managers
6. Organizational Infrastructure and Communications
7. Performance Monitoring and Time Horizon

1. MISSION

a) The Board's primary goals in managing the Fund are

i) To ensure that sufficient funds are available to pay vested benefits and maintain supplemental benefits;
ii) To comply with all applicable fiduciary standards; and
iii) To create value added, where feasible, that will help reduce the costs of the plan, increase benefits, or both.

2. RISK MANAGEMENT

a) The Board believes that prudent management of risk is a central element of the investment function.

b) Though there are numerous risks involved in the management of a pension investment program, ACERA believes that the following warrant particular attention:

i) ***Funding-related Risk*** - The risk that the funds available in the Plan will be insufficient to pay the promised benefits, both vested and supplemental, or that contribution volatility will be unacceptably high. The primary methods for managing funding risk include regularly conducting integrated asset/liability studies, and establishing appropriate and prudent investment and funding policies.

0.1 In managing the relationship between assets and liabilities, the approved asset allocation of the Fund should provide an adequate level of certainty of meeting the projected liabilities of the Plan over a time period, as determined by the actuary.

ii) ***Benchmark-related Risk*** – The risk that the investment benchmarks adopted by the Fund are inappropriate, or that the aggregate of the individual Manager benchmarks within an asset class do not adequately reflect the benchmark for the asset class as a whole. The latter risk is a specific risk generally referred to as *benchmark misfit risk (i.e. style risk)*. Inappropriate benchmarks or excessive benchmark misfit risk could result in investment performance different than expected and could adversely impact decisions concerning the hiring or firing of investment managers.

0.1 The primary methods for effectively managing benchmark-related risk are
(a) regular review of the Fund's benchmarks; and
(b) regular measurement and monitoring of misfit risk using proper methodologies.

iii) ***Manager Risk*** - The risk of aberrant performance on the part of individual investment Managers, and the related active management risk for asset classes as a whole.

0.1 The primary methods for mitigating Manager risk are

(a) Prudent processes for selecting and monitoring investment Managers;
(b) Competent internal investment Staff;
(c) Effective investment consulting support; and
(d) Clear communication to investment Managers of ACERA's objectives, expectations, and investment time horizons.

0.2 The primary method for mitigating active management risk for asset classes include

(a) Establishment of appropriate asset class benchmarks;
(b) Careful monitoring of asset class performance relative to the benchmarks; and
(c) Prudent use of passive management.

iv) ***Fortitude Risk*** - The risk that the Board or Staff will fail to exercise the patience, judgment, or fortitude required to support long-term policies and strategies for the investment and funding program.

0.1 The keys to managing fortitude risk are believed to include

(a) Effective orientation and education with respect to institutional investing and actuarial science; and
(b) A commitment to continually refining, confirming, and communicating the investment philosophy and funding policy of the Association.

3. DIVERSIFICATION

a) ACERA acknowledges the basic tenets of modern portfolio theory, which suggest that diversification, or combining assets that are not perfectly correlated with each other, will reduce the long-term volatility of the overall portfolio.

b) It is generally desirable however to avoid overly complex asset structures, provided the allocation selected can reasonably be expected to meet the objectives of the Plan. ACERA believes that the benefits of diversification must be weighed against the costs

involved, which may include fees, liquidity, complexity, communication, internal staff resources and expertise and trustee knowledge and effort.

c) The following asset classes are appropriate candidates for inclusion in its portfolio:
   i) Domestic equity
   ii) International equity (including emerging markets)
   iii) Fixed income, including high yield fixed income and international fixed income
   iv) Real estate

d) ACERA does not consider alternative investments to be an appropriate candidate for inclusion in its portfolio due to the substantial direct and indirect costs associated with it.

<u>Implications</u>

- A systematic methodology for re-balancing the investment portfolio is required to ensure proper implementation and adequate risk control concerning ACERA's asset allocation.
- Adding or deleting asset classes or investment Managers should be considered in light of the impact such decisions are likely to have on the general complexity and cost structure of the portfolio, as well as ACERA's ability to prudently achieve its investment and funding goals over the long run.

4. MARKET EFFICIENCY

Except for specified High-Alpha assignments:

a) ACERA does not believe in the viability of active management strategies that rely on market timing.

b) ACERA does not believe in the viability of management strategies that call for over weighting or under weighting styles or sectors within an asset class; i.e., benchmark misfit risk will not generate long-term alpha. Accordingly, ACERA generally believes that it should maintain exposures within an asset class (such as style or capitalization weightings) that are consistent with the broad benchmark for the asset class as a whole.

c) ACERA does believe that market efficiency varies among asset classes, creating opportunities for successful active management strategies based on securities selection.

d) Asset classes that can be demonstrated to be efficient should be managed passively in order to reduce active management risk and lower the costs of managing the portfolio.

e) For inefficient asset classes, ACERA believes that it has the ability and a duty to prudently exploit such inefficiencies through active securities selection strategies.

Implications

- ACERA should be conscious of any subtle forms of market timing that may arise in the course of managing the Fund, or that may be implicit in investment strategies presented to ACERA for inclusion in the investment program.

- ACERA must determine appropriate methodologies for determining whether an asset class is efficient or presents appropriate opportunities, thus providing insight to the Board on the use of particular strategies.

5. HIGH-ALPHA MANAGERS

a) ACERA believes that the portfolio characteristics utilized to control risk in the broad portfolio, such as market capitalization, sector exposure, use of derivatives, leverage limitations, property type or deal structure may be modified for specific Managers who control a limited portion of the portfolio and have demonstrated a proven capacity to consistently add value net of fees. Such strategies, which ACERA refers to as High-Alpha, may include the following elements:

   i) The bulk of the asset class is passively managed or risk controlled; and
   ii) A small number of active managers are retained who employ somewhat more aggressive investment strategies, such as concentrated portfolios, leveraged purchases, developments, high-yield debt, etc.

b) The primary benefits of including a High-Alpha approach within the overall portfolio are
   i) Reduction in active management risk;
   ii) Lower average investment fees; and
   iii) Concentration on opportunities where the likelihood of adding value is greatest.

c) The market efficiency and opportunities in asset classes may change over extended periods of time; therefore ACERA believes that its portfolio management strategies should adapt over time to reflect the changing nature of capital markets.

6. ORGANIZATIONAL INFRASTRUCTURE AND COMMUNICATIONS

a) ACERA believes that in order for the investment program to achieve its goals, ACERA must invest the necessary resources to build and maintain an appropriate organizational infrastructure, key elements of which include

i) A competent, internal investment staff comprised of a sufficient number of investment professionals possessing appropriate leadership, technical, and administrative skills.

0.1 Attracting a competent staff. ACERA recognizes that it competes with the private sector. It must therefore continually strive to create a total work environment that is challenging, rewarding, and competitive.

ii) A strong relationship with outside general investment Consultant(s) who are able to provide ACERA with the following:

0.1 A high degree of investment expertise;
0.2 Innovative and proactive advise and counsel;
0.3 Strong research support; and
0.4 Strong reporting capabilities.

iii) A broad-based information gathering and reporting system to present well-researched, relevant and timely data in a manner that is easily understood, and that supports rigorous and consistent monitoring of critical investment activities.

iv) An open channel of communication between the Board, management, and the ACERA's external investment professionals.

b) By providing the Board with timely, accurate, and thorough information, the organizational infrastructure will give the Board the high level of comfort it needs to set policy, make investment decisions, oversee the performance of the investment program, and maintain the fortitude necessary to support its investment philosophy, policies, and strategies.

Implications

- ACERA must determine what constitutes an appropriate internal investment staff structure, given the nature of the current investment program.

- ACERA must over time take concrete steps towards creating a work environment that will allow the Association to attract and retain needed staff.

- ACERA must recognize that developing its organizational infrastructure it needs – staffing, consulting support, information systems, and communication channels – cannot be achieved overnight, but rather will require an ongoing commitment of time and resources.

7. PERFORMANCE MONITORING AND TIME HORIZON

a) ACERA holds the following basic beliefs concerning performance monitoring practices and methodologies:

i) The various investment policies of the Fund, in the aggregate, are the most important determinants of investment success; compliance with investment policies should, therefore, be monitored rigorously;

ii) The performance of the total portfolio, individual asset classes, and investment Managers should be compared to appropriate, predetermined benchmarks;

iii) Peer comparisons are an additional valid tool in assessing individual Manager performance (supplementing the use of benchmarks), given that ACERA aims to select superior Managers within particular investment styles or mandates. Peer comparisons, or performance rankings, are also valid tools for measuring the performance of asset class portfolios; and

iv) Peer group comparisons are not an appropriate means of assessing the performance of the total Fund, given that sponsors have different objectives and risk tolerance levels, and therefore may have different asset allocation policies.

v) Benchmark misfit risk, or the risk that the aggregate of individual investment Manager benchmarks in an asset class do not adequately reflect the benchmark for the asset class as a whole, should be explicitly measured on a regular basis.

vi) Investment Managers are generally hired to fulfill a specific role in a portfolio. Accordingly, ACERA believes it is important that ACERA monitor the extent to which Managers comply with their stated style and mandates.

b) ACERA believes that successful funding and investment decisions require a long-term perspective on the part of the Board and management:

i) It is the intention of the Retirement Board that commitments to asset classes and investment strategies should involve long time horizons that may include more than one business cycle (3-5 years each). Relatively illiquid asset classes may require even longer time horizons.

ii) The Board acknowledges that commitments to individual investment Managers also require a long time horizon of at least one business cycle (3-5 years).

iii) ACERA believes that proper reporting and monitoring systems; and clear communication among Consultants, management, investment Managers and the Board will enable the Board to maintain the necessary long term perspective on all investment decisions.

Implications

- Assessing the investment performance relative to appropriate, pre-determined, benchmarks is as applicable to the total portfolio and to individual asset classes as it is for individual investment Managers, and therefore warrants a commensurate share of the Board's time and attention.

- The Board will spend relatively little time assessing the performance of the Fund relative to that of comparable pension funds.

- ACERA will need to either develop in-house capabilities to regularly measure benchmark-related risk, or it will need to purchase such capabilities from external investment Consultants.

- ACERA will monitor all investment Managers to ensure they are complying with their stated investment style, regardless of whether they are performing well or poorly. Strongly performing Managers who are found to not be following their stated styles will be carefully scrutinized and may be subject to disciplinary action.

- ACERA will monitor all investment providers to ensure compliance with ACERA's "General Investment Guidelines, Policies and Procedures."

SCHEDULE VII

CHARTER OF ACERA'S INVESTMENT COMMITTEE OF THE BOARD

To identify issues pertinent to the effective management of the investment portfolio, initiate analysis of such issues by management or consultants, review all policy recommendations by staff and consultants, provide recommendations to the Board for adoption, and oversee the implementation of the investment program. Specific responsibilities include:

1. The Investment Committee shall review recommendations of staff and consultants and in turn provide its own recommendations to the Board on all investment policies, including investment philosophy, requiring Board approval. Said policies shall normally be contained in, or appended to, the *ACERA General Investment Guidelines, Policies and Procedures*.

2. The Investment Committee shall review and recommend additional policies for the Board's approval as requested by the Board and in accordance with the Policy Development Process.

3. The Investment Committee shall review recommendations of staff and consultants and in turn provide its own recommendation for Board approval on the following matters:
   a) Appointment of Investment Managers;
   b) Appointment of the Investment Consultants;
   c) Appointment of the Custodian Bank.

4. The Investment Committee shall monitor the investment program of ACERA in accordance with all relevant policies of the Board. In general, the Investment Committee shall monitor:
   a) Compliance with and continued appropriateness of all ACERA investment policies;
   b) Progress towards achievement of investment goals;
   c) Progress towards implementation of the ACERA budget and Business Plan with respect to investments; and
   d) Cost effectiveness of the ACERA investment program.

5. In accordance with the provisions of the Open Meeting Law, the Investment Committee shall allow adequate opportunity for input from the public and shall respond to such input in a manner that reflects the Committee members' fiduciary duties as trustees of the Plan.

Frequency of Meetings

The Investment Committee shall generally meet monthly on the second Wednesday of the month, but may meet more or less frequently as required.

Committee Composition

The Investment Committee shall be composed of all Board members, one of whom shall serve as Committee Chair. Alternate members shall serve on the Investment Committee as provided by law.

Staff Contact

The Chief Executive Officer shall appoint a staff person to serve as a staff contact to the Investment Committee

SCHEDULE VIII

ACERA

TABLE OF AMENDMENT DATES

AMENDING RESOLUTIONS

Jun	27,	1985
Oct.	10,	1985
Jan.	9,	1986
Jan.	16,	1986
Mar.	13,	1986
May	22,	1986
Sep.	11,	1986
Oct.	9,	1986
Nov.	20,	1986
May	14,	1987
Aug.	13,	1987
Oct.	8,	1987
Apr.	21,	1988
July	28,	1988
Jan.	29,	1989(4)
Apr.	13,	1989(5)
May	18,	1989
July	13,	1989
Aug.	10,	1989
Nov.	16,	1989(2)
July	11,	1991
June	11,	1992
June	10,	1993
July	8,	1993
Nov.	18,	1993
May	14,	1994
Aug.	18,	1994
Nov.	20,	1994
Feb.	16,	1995
May	18,	1995
Jan.	16,	1997
Aug.	20,	1998
May	20,	1999
Jan.	31,	2000
Apr.	19,	2001
Jul.	18,	2002
Feb.	21,	2003
Feb.	19,	2004
Feb.	17,	2005
Jul.	20,	2006
Jun.	21,	2007

Alameda County Employees'
Retirement Association

ACERA

GENERAL INVESTMENT GUIDELINES, POLICIES AND PROCEDURES

AMENDED September 18, 2008

ACERA
GENERAL INVESTMENT GUIDELINES, POLICIES AND PROCEDURES
2008

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[1] Prepared for ACERA by Cortex Consulting; Adopted by the Board of ACERA on March 8, 2000; Revised on July 2008.

ACERA
GENERAL INVESTMENT GUIDELINES, POLICIES AND PROCEDURES

SECTION I: MISSION AND PURPOSE

The Alameda County Employees' Retirement Association (ACERA) exists for the purposes of providing accurate, timely benefits to its members and their beneficiaries and defraying reasonable expenses of administration.

The Board of Retirement (the Board), having exclusive authority and exclusive fiduciary responsibility for the investment and administration of the Trust Fund (the Fund), hereby establishes the following "General Investment Guidelines, Policies and Procedures" (the Policy) for the investment of ACERA's assets. The Board reserves the right to amend, supplement or rescind this Policy at any time.

The Board is directed by law and given discretion to prudently invest the retirement plan assets. The purpose of this statement of Policy is to assist ACERA in effectively supervising said investments and to encourage effective communication between ACERA and its investment managers (Manager(s)) and investment consultants (Consultant(s)).

ACERA's investment goal is to operate at a level of performance in the upper quartile of comparable pension funds on a risk-adjusted basis and to be as fully funded as possible so that ACERA's benefit costs do not become a burden upon future generations of members and taxpayers.

SECTION II: CONSTITUTIONAL REQUIREMENTS

Article 16 §17 of the California State Constitution provides in pertinent part as follows:

"Notwithstanding any other provisions of law or this Constitution to the contrary, the retirement board of a public pension or retirement system shall have plenary authority and fiduciary responsibility for investment of money and administration of the system, subject to the following:

a. The retirement board of a public pension or retirement system shall have the sole and exclusive fiduciary responsibility over the assets of the public pension or retirement system. The retirement board shall also have sole and exclusive responsibility to administer the system in a manner that will assure prompt delivery of benefits and related services to the participants and their beneficiaries. The assets of a public pension or retirement system are trust funds and shall be held for the exclusive purposes of providing benefits to participants in the pension or retirement system and their beneficiaries and defraying reasonable expenses of administering the system.

b. The members of the retirement board of a public pension or retirement system shall discharge their duties with respect to the system solely in the interest of, and for the exclusive purposes of providing benefits to participants and their beneficiaries, minimizing employer contributions thereto, and defraying reasonable expenses of administering the system. A retirement board's duty to its participants and their beneficiaries shall take precedence over any other duty.

c. The members of the retirement board of a public pension or retirement system shall discharge their duties with respect to the system with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with these matters would use in the conduct of an enterprise of a like character and with like aims.

d. The members of the retirement board of a public pension or retirement system shall diversify the investments of the system so as to minimize the risk of loss and to maximize the rate of return, unless under the circumstances it is clearly not prudent to do so.

e. The retirement board of a public pension or retirement system, consistent with the exclusive fiduciary responsibilities vested in it, shall have the sole and exclusive power to provide for actuarial services in order to assure the competency of the assets of the public pension or retirement system.

f. With regard to the retirement board of a public pension or retirement system which includes in its composition elected employee members, the number, terms, and method of selection or removal of members of the retirement board which were required by law or otherwise in effect on July 1, 1991, shall not be changed, amended, or modified by the Legislature unless the change, amendment, or modification enacted by the legislature is ratified by a majority of the electors of the jurisdiction in which the participants of the system are or were, prior to retirement, employed.

g. The Legislature may by statute continue to prohibit certain investments by a retirement board where it is in the public interest to do so, and provided that the prohibition satisfies the standards of fiduciary care and loyalty required of a retirement board pursuant to this section.

h. As used in this section, the term "retirement board" shall mean the board of administration, board of trustees, board of directors, or other governing body or board of a public employees pension or retirement system; provided, however, that the term "retirement board" shall not be interpreted to mean or include a governing body or board created after July 1, 1991, which does not administer pension or retirement benefits, or the elected legislative body of a jurisdiction which employs participants in a public employees pension or retirement system."

SECTION III: ROLES AND PRINCIPAL DUTIES

The Fund investments shall be prudently planned, implemented, managed, monitored and guarded. The Board, Investment Committee (the Committee), Investment Staff (Staff), Consultant, Custodian Bank (Custodian), and Manager shall coordinate this process. See the defined roles and principal duties of the above-mentioned parties below:

A. THE BOARD shall review and approve Committee recommendations. The Board also reviews, adopts and monitors all investment polices, guidelines and procedures required to prudently administer the Fund and to effectively mitigate risk to the Fund.

B. THE COMMITTEE shall identify issues pertinent to the effective investment and administration of the Fund and initiate analysis of such issues by Staff, Consultant or Managers. It also reviews Staff's and Consultant's recommendations regarding all investment policies and investment Fund management. The Committee provides recommendations to the Board for adoption, oversees implementation, and monitors the investment programs in accordance with all applicable laws and Board-established policies, guidelines and procedures. Refer to Schedule VII – Charter of ACERA's Investment Committee of the Board for detailed Committee responsibilities.

C. STAFF shall oversee the Fund's investment program activities, implement the Board/Committee's decisions, make recommendations to the Committee regarding Fund management, and recommend investment-related polices and procedures to the Committee. Additionally, Staff monitors the performance and compliance of Managers in accordance with all applicable laws, Board-established policies, guidelines and procedures, as well as "Specific Investment Guidelines" set out in the investment agreement between ACERA and each Manager (Agreement or Contract). Staff also facilitates the Committee meetings and completes activity as directed by the Board/Committee.

D. CONSULTANT shall review, analyze and evaluate the Fund's effectiveness and efficiency and make fund management related recommendations. Consultant assists Staff in implementing the Board/Committee's decisions and developing all investment-related policies. Consultant's responsibilities are detailed in the service agreement between ACERA and Consultant.

E. CUSTODIAN shall provide custody of ACERA's investment assets. Custodian's responsibilities are detailed in the service agreement between ACERA and Custodian.

F. MANAGER shall prudently manage its Managed Account (defined in Section VII – Eligible Asset Categories) in accordance with all applicable laws, Board-established policies, guidelines and procedures, as well as Specific Investment Guidelines. Manager's responsibilities are detailed in the Agreement.

SECTION IV: INVESTMENT PHILOSOPHY

The following is a summary of ACERA's investment philosophy. For the complete statement, please refer to Schedule VI of this document, "ACERA Investment Philosophy."

The Board believes that its investment policies, in aggregate, are the most important determinants of its investment success. Compliance with investment policies should, therefore, be monitored rigorously. The Board also believes that performance of the total portfolio, individual asset classes, and Managers should be monitored and compared to appropriate, predetermined benchmarks.

The Board believes that prudent management of risk is a central element of the investment function and that diversification among asset classes will reduce risk and enhance returns of the overall investment portfolio in the long term.

The Board believes that market efficiency and opportunities vary among asset classes and may change over extended periods of time; therefore, the Board believes that ACERA's portfolio management strategies should adapt over time to reflect the changing nature of capital markets.

The Board's primary goals in managing the Fund are

1. To ensure that sufficient funds are available to pay vested benefits and maintain supplemental benefits;
2. To comply with all applicable fiduciary standards; and
3. To add marginal value that will help reduce the costs of the plan and/or to increase benefits for the beneficiaries.

The Board believes that in order to achieve its goals, ACERA must invest the necessary resources to build and maintain an appropriate organizational infrastructure.

SECTION V: ASSET ALLOCATION AND REBALANCING

Asset allocation targets, a function of the returns and risks from various asset classes and the nature of the plan's liabilities, are set forth in Schedule I. A goal of asset allocation is balancing asset growth versus liability growth considering time horizons, liabilities and risk tolerance. ACERA's objective is to conduct an asset/liability study once every five years and an asset allocation study once every three years or more often if necessary.

Rebalancing is the risk control process of returning an allocation back to the desired target level after having drifted away from its targeted position. Equal probability bands, as defined by standard deviation factors that shall be used to define the acceptable ranges around the asset allocation targets are set forth in Schedule IA. The objective of rebalancing is to enhance the risk-adjusted performance of the asset allocation structure.

Staff shall be responsible for maintaining the relative weights of asset classes and allocations within the acceptable rebalancing ranges as reflected in Schedule IA. Should an asset class or allocation fall outside its target range, Staff shall rebalance the asset class or allocation back to the target weights as specified in the asset allocation structure in Schedule I.

Staff shall

1. Monitor the portfolio;
2. Determine whether or not any asset category is out of balance with its target asset allocation in excess of the specified tolerance range;
3. Determine whether or not any Manager within each asset category is out of balance with their target allocation in excess of the specified tolerance range;
4. And, if this is determined, either
   (a) instruct the relevant Managers to redirect cash income (interest coupon and dividends) in concert with an evaluation of pending commitments and other cash flows (employer and employee contributions), in order to bring the allocation(s) back to the adopted strategic target; and/or
   (b) instruct the relevant Managers to liquidate or acquire the appropriate dollar value of securities to reach the target and reallocate the cash thus generated or required to the other category(s) or Manager(s), as necessary.

Staff shall report to the Board on a regular basis the status of the Fund with respect to how categories are tracking relative to their allowable ranges, as well as any actions taken to rebalance the portfolio.

SECTION VI: INVESTMENT STRATEGY AND MANAGER STRUCTURE

A. U.S. EQUITY will be structured to capture exposure to the broad U.S. equity market as represented by the Russell 3000 Index. Passively managed (index) portfolios will be used in portions of the markets that are reasonably efficient. These portfolios are intended to provide broadly diversified market exposure with controlled (market) risk and minimal cost.

   Actively managed portfolios will be used when the Board determines that a Manager possesses special skills or abilities that enable that Manager to capture excess returns relative to the market, adjusted for risk and fees; or to exploit specialty markets that provide enhanced return with acceptable risk.

   A great part of the Russell 3000, on a market value basis, is comprised of large-cap stocks, which the Board believes are efficiently priced most of the time. Therefore, the Board has adopted a policy of obtaining overall exposure to this segment of the market via passively managed indexed products. In addition, some active Managers have been employed to enhance overall portfolio return on a risk- and fee-adjusted basis.

   The remainder of the Russell 3000 index is comprised of small to mid-cap companies. Some opportunities for active management enhancement exist in these securities due to market inefficiencies. ACERA will attempt to capture these opportunities through a mix of Managers who have the special skills required to identify smaller companies that may be undervalued or possess substantial growth potential.

The U.S. equity portfolio shall be allocated among the various styles and Managers. The U.S. equity manager structure is outlined in Schedule I.

B. INTERNATIONAL EQUITY represents an opportunity to diversify risk and capture enhanced returns within markets generally less efficient than the U.S. domestic equity market. 100% of the international equity portion of the Fund will be invested in actively managed portfolios.

   The international equity portfolio shall be allocated among the various styles and Managers. The international equity manager structure is outlined in Schedule I.

C. FIXED INCOME represents a means of reducing overall portfolio risk and capturing incremental returns either domestically or globally. Inefficiencies in the pricing and trading of fixed income securities create opportunities to add value through active management. 100% of the fixed income portion of the portfolio will be invested in actively managed portfolios.

   The fixed income portfolio shall be allocated among the various styles and Managers. The fixed income manager structure is outlined in Schedule I.

D. REAL ESTATE will be used as a means for diversifying the portfolio and capturing additional returns due to the low correlation between returns on real estate and financial assets. Due to the illiquid nature of real estate assets, distinctions between active and passive management are not applicable. Detailed information regarding real estate investments is included in ACERA's "Real Estate Strategic Plan," which is maintained as a separate document.

E. PRIVATE EQUITY AND ALTERNATIVES represents a means of further diversifying the portfolio and generating returns superior to those available in the public equity market to compensate the Fund for the long term and illiquid commitments associated with such investments. Due to the absence of an appropriate index for private equity and alternatives investments, distinctions between active and passive management are not applicable.

   The private equity and alternatives portfolio shall be allocated among the various sub-categories and Managers. The strategic allocation to the private equity and alternatives investment portfolio is outlined in ACERA's "Private Equity and Alternatives Return Leading Strategies Policy (PEARLS Policy)" which is maintained as a separate document.

In aggregate, investments in non-U.S. market across all asset classes shall not exceed 35% of the market value of the total Fund.

SECTION VII: ELIGIBLE ASSET CATEGORIES

The Fund shall hold assets in categories established by the Board. Any asset category may be held in direct form, in pooled form, or in both. Asset categories managed by one or more "Qualified Investment Managers" are called "Managed Accounts." Asset categories under the supervision of the County Treasurer are called the Treasurer's Accounts. Eligible asset categories are listed and defined below.

A. CASH AND CASH EQUIVALENT shall consist of, but not limited to, cash, short term (12 months or less) interest bearing investments of high quality such as U.S. Treasury issues, insured certificates of deposit of U.S. banks (fixed and/or variable), commercial paper rated A-1, P-1 or both, or other instruments of equal or better quality, and includes money market funds available through the Custodian.

B. U.S. EQUITY shall consist of, but not limited to, common stocks and other securities which are convertible into common stocks, and ADRs (American Depository Receipts), as well as cash (per "A" above) and fixed income (per "D" below) when used as temporary substitutes for common stocks.

C. INTERNATIONAL EQUITY shall consist of, but not limited to, common stocks and other securities convertible into common stocks of companies domiciled outside of the U.S., GDRs (Global Depository Receipts), IDRs (International Depository Receipts) and other depository receipts as well as cash/cash equivalents (per "A" above) and fixed income (per "D" below), domestic or international, which are being used as temporary substitutes for common stock.

D. FIXED INCOME shall consist of investments in, but not limited to, U.S. taxable bonds, debentures, notes and other evidences of debt. Fixed income may also include, but not limited to, non-dollar denominated bonds issued by corporations or governments domiciled outside of the U.S. as well as Brady Bonds. Other eligible investments include cash/cash equivalents (per "A" above) and convertible bonds and preferred stock.

E. REAL ESTATE shall consist of investments in real estate and equity real estate through the use of commingled or direct investments. Detailed information about real estate investments is included in ACERA's "Real Estate Strategic Plan," which is maintained as a separate document.

F. PRIVATE EQUITY AND ALTERNATIVES shall consist of investments including, but not limited to, venture capital, corporate buyouts, debt-related and special situations, commodities, absolute return strategies, and other non-traditional and uncorrelated investments. Private equity and alternatives investments may be denominated in U.S. dollars or other currencies. Detailed information about private equity and alternatives investments is included in ACERA's "PEARLS Policy" which is maintained as a separate document.

In aggregate, non-U.S. currency exposure across all asset classes shall not exceed 35% of the market value of the total Fund.

SECTION VIII: ASSET CATEGORIES OBJECTIVES

The general objective of the Board is to preserve capital and to earn a return from appreciation and income, as described herein:

1. To ensure the integrity of ACERA's actuarial funding plan, one minimum return objective for the Fund shall be the current actuarial interest assumption rate plus 25 basis points per year over a market cycle. Returns shall be calculated net of all fees (both administrative and investment fees).
2. To ensure that ACERA's assets grow appropriately to match salary increases which directly impact benefit levels, an additional minimum return objective for the Fund over a market cycle (up to five years) shall also be 400 basis points (4%) per year over the national Consumer Price Index, published by the U.S. Department of Commerce. Returns shall be calculated gross of investment management fees.
3. To ensure that ACERA's external investment manager structure, in aggregate, is performing satisfactorily. An additional minimum return objective for the Fund over a market cycle (up to five years) shall be equivalent to the Fund's Policy Index on a gross of investment management fee basis.

The objectives of each asset category are

A. CASH AND CASH EQUIVALENT

1. A rate of return in excess of 90-Day U.S. Treasury bills, and
2. A rate of return within the upper one half of a universe of like short-term funds.

B. U.S. EQUITY

1. A rate of return in excess of the U.S. equity market as measured by the Russell 3000 Index, and
2. A rate of return within the upper 33rd percentile of the Independent Consultants Cooperative (ICC)/State Street database or similar database of the performance of diversified equity portfolios.

C. INTERNATIONAL EQUITY

1. A rate of return in excess of the Morgan Stanley Capital International All Country World Index Ex U.S. (MSCI ACWI Ex U.S.), and
2. A rate of return within the top quartile of the ICC/State Street database or similar database of the performance of diversified international equity portfolios.

D. FIXED INCOME

1. A rate of return in excess of the Lehman Aggregate Bond Index, Citigroup World Government Bond Ex. U.S. and Lehman High Yield in a ratio of 75/15/10, and

2. A rate of return within the top quartile of the ICC/State Street database or similar database of the performance of diversified fixed income portfolios.

E. REAL ESTATE

1. Total Return – a minimum total gross return equivalent to the National Council of Real Estate Investment Fiduciaries (NCREIF) Property Index (NPI) over rolling five-year periods, and
2. Income Return – Income, which is defined as cash distributed to the Association, should comprise at least 2/3 of the total expected return over rolling five-year periods for all Stable (as defined in ACERA's "Real Estate Strategic Plan") products.

F. PRIVATE EQUITY AND ALTERNATIVES

1. A rate of return in excess of the Russell 3000 Index plus 150 basis points net of all fees and expenses over a full market cycle. Please refer to ACERA's PEARLS Policy, which is maintained as a separate document, for detailed information.

In addition, objectives that reflect a particular investment strategy or style employed by an individual Manager shall be outlined in the Specific Investment Guidelines attached to the Manager's Contract.

SECTION IX: ALLOCATION OF CASH FLOW

Cash flow not needed for benefit payments or administrative expenses shall be allocated to Managed Accounts in a ratio that best funds the overall targeted asset allocation as reflected in Schedules I and IA.

If cash flow is insufficient for the payment of benefits or to cover administrative expenses, then Managed Accounts shall be debited in a ratio that best satisfies the target allocation shown in Schedules I and IA. Such debits, if necessary, will be carried out as needed and with timely notice to Managers to facilitate effective funds transitions and performance measurement.

For all planned investments which may not need to be funded immediately, a reserve may be budgeted and invested in appropriate accounts in accordance with the asset allocation targets until such moneys are required. Alternatively, Managed Accounts within "overfunded" asset classes may be called upon to provide the required moneys.

SECTION X: PROHIBITED INVESTMENTS

Managers shall exercise prudent expert standards in defining prohibited investments. For example, prohibited investments include, but are not limited to, securities issued by the County of Alameda or any agency thereof.

SECTION XI: DIRECTED BROKERAGE

ACERA shall establish an open Directed Brokerage (DB) Program designed to maximize the recapture of brokerage commissions by enforcement of the target percentages of direction. ACERA's DB Program is governed by ACERA's DB Policy, which is maintained as a separate document.

The strategic objective of the DB Program is to take advantage of the industry-accepted recapture of a portion of trade commissions paid to brokers. The primary goals of the DB Program are to 1) recapture 50% or more of commissions paid on a specific percentage of trades sent to correspondent brokers on a timely basis; 2) construct the percentage of trades subject to recapture so as to allow investment managers to have access to the research they need; 3) seek "Best Execution" through third-party administration and outside consultant monitoring; and 4) encourage local and emerging broker participation through the use of an open correspondent network program.

SECTION XII: DERIVATIVE INSTRUMENT USAGE POLICY

Exposure to risk by use of derivative instruments must be consistent with ACERA's overall investment policy as well as an individual Manager's Specific Investment Guidelines. In general, derivatives shall not be used to establish a leveraged position (i.e., offsetting Cash positions must be maintained against all delayed settlement transactions). Should there be any conflict between an individual Manager's Specific Investment Guidelines and the Derivative Instrument Usage Policy, the Specific Investment Guidelines shall prevail.

SECTION XIII: SELECTION OF INVESTMENT MANAGERS

The Investment Committee shall direct Staff and/or a Consultant to initiate searches for Managers. Staff and/or the Consultant shall research for qualified candidates and present a list of finalists to the Investment Committee for its approval. Upon approval of the list, the finalists shall be interviewed by Staff and the Consultant (if applicable). Staff and the Consultant (if applicable) shall evaluate the interviews, rank the finalists, and make a recommendation to the Investment Committee to hire one or more firms attaining the highest rankings in a publicly noticed meeting at which no less than five (5) Investment Committee members shall be present. It is possible that none of the firms will be recommended for hire.

The above-mentioned procedures are developed for the convenience and benefit of ACERA, and shall not bind ACERA or invalidate the selection of a Manager, if different processes are used subsequent to the promulgation of this Policy. ACERA recognizes that some investments by their nature present unique opportunities and there may not be suitable competitors for a unique investment opportunity. ACERA also recognizes that due to inherent features of some investments, time constraints may require ACERA to use a different investment manager selection process.

SECTION XIV: EMERGING INVESTMENT MANAGERS

The Board has established the ACERA Emerging Investment Manager Policy ("EM Policy"), which is maintained as a separate document. The purpose of the EM Policy is to establish a framework for the development and administration of ACERA's Emerging Investment Manager Program ("EM Program"), consistent with the Board's fiduciary responsibilities in the investment of the Fund. The EM Policy states that the initial investment of the EM Program is not to exceed 1% of the total Fund.

The strategic objective of the EM Program is to add incremental value to the Fund through the hiring of the most talented Emerging Investment Managers (EMs) to manage ACERA's assets.

The primary goals of the EM Program are to 1) identify and gain early access to the most talented investment managers in their early business stages; 2) generate superior Fund return performance through the EM Program; 3) identify superior EMs and/or investment opportunities in the State of California and Alameda County that are equal to or superior to comparable available investments; and 4) further diversify the Fund's overall investment program, so as to enhance risk-adjusted returns of the Fund.

SECTION XV: AUTHORITY OF INVESTMENT MANAGERS

Subject to the laws of the United States and the State of California, and to the terms and conditions of this Policy, Managers shall have full discretion to direct the purchase, exchange, sale and reinvestment of the assets of the Managed Accounts. The Board expects that Managers will recommend changes to this Policy when any part of this Policy appears to be at variance with overall market and economic conditions.

Managers shall place orders to buy and sell securities and, by notice to the Custodian, shall cause the Custodian to deliver and receive securities on behalf of the Fund. Managers shall, upon Board inquiry, report placement of ACERA brokerage such that the Board shall be assured commissions were placed for the sole and exclusive benefit of the Fund.

Separate account Managers shall not vote proxies. Proxies shall be voted by ACERA, via a proxy voting service vendor, in accordance with "ACERA Proxy Voting Guidelines and Procedures" which is maintained as a separate document.

Securities lending shall be performed under the oversight of Staff, in accordance with Board-established procedures.

SECTION XVI: INVESTMENT GUIDELINES FOR THE MANAGED ACCOUNTS

Individual Manager discretion shall be governed by the Investment Guidelines for the Managed Accounts as well as the Specific Investment Guidelines for each Manager. Should there be any conflict between the Specific Investment Guidelines of an individual Manager and the Investment Guidelines for the Managed Accounts, the Specific Investment Guidelines shall prevail.

A. GENERAL

1. All investments shall comply with all applicable laws of the U.S. and the State of California governing the investment of pension trusts.
2. All securities transactions shall be executed by reputable broker/dealers, banks, or the Custodian, and shall be on a best-price and best-execution basis, and shall be reported to ACERA as is called for elsewhere in this Policy.
3. All Managers shall refrain from investing in a tobacco producer investment opportunity when, in their expert opinion, an alternative non-tobacco producer investment opportunity is available that will satisfy the same ACERA portfolio guidelines, instructions and objectives for risk, return and diversification.

B. EQUITY

Managers have full discretion to invest solely in readily marketable and diversified equity securities subject to the following:

1. For Managed Accounts, no more than 10% of the value (at time of purchase) of the account shall be invested in the securities of a single issuer.
2. ACERA shall not hold more than 10% of the equity securities of any issuer.
3. Equity securities shall possess value and quality corroborated by generally accepted techniques and standards of fundamental securities analysis.
4. Assets in a Managed Account not invested in equity securities shall be kept with interest in appropriate money market instruments, including any money market fund available through the Custodian.
5. A Managed Account shall be subject to ACERA's policy on derivatives.
6. All Managers shall endeavor to be fully invested in stocks at all times unless they have received specific authorization to the contrary from the Board. Cash holdings, as defined in this Policy, shall generally not exceed 5% of the portfolio on a market value basis.

C. FIXED INCOME

Managers have full discretion to invest solely in readily marketable and diversified securities including, but not limited to

1. Obligations of the U.S. and/or eligible foreign government's treasuries.
2. Obligations guaranteed by agencies of the U.S. and/or eligible foreign governments.
3. Insured certificates of deposit and banker's acceptances of credit worthy banks.
4. Corporate and other evidences of debt. At least 80% of this debt must be rated by Moody's Investor's Services or by Standard & Poors Corporation.
5. Commercial paper and banker's acceptances of issuers rated P-1 by Moody's Investor's Service or A-1 by Standard & Poors Corporation.
6. Excepting direct obligations of the U.S. and/or eligible foreign governments, and those explicitly guaranteed by the U.S. and/or eligible governments, no account shall hold more than 5%, at cost, of the obligations of any single issuer.
7. Excepting direct obligations of the U.S. and/or eligible foreign governments, and those explicitly guaranteed by the U.S. and/or eligible governments, no security shall comprise more than 5% of the account, as determined at the time of purchase.

8. Fixed income derivative investments shall be in accordance with ACERA's Derivative Instrument Usage Policy as described in Section XII of the Policy.

SECTION XVII: INVESTMENT MANAGER SPECIFICATIONS

A. Managers must be registered as investment advisers under the Investment Adviser's Act of 1940, a bank (as defined in that Act) or an insurance company qualified to perform investment management services under state law in more than one state, including the State of California. Unless an exception is granted by the Board, by accepting appointment as ACERA's Managers, Managers shall acknowledge that they are "Plan Fiduciaries" and "Qualified Investment Managers" as defined by the Employees' Retirement Income Security Act (ERISA) of 1974 (see or reference United States Code Title 29 Section 1001 et. seq.).

B. Managers shall maintain fiduciary insurance in the amount of 10% of the total assets managed in the ACERA account or $25 million, whichever is higher, unless the Contract specifies otherwise.

C. Managers shall promptly notify ACERA of changes that occur in any of the following:

   1. The investment strategy used in managing the subject product.
   2. The key personnel involved in managing ACERA's account.
   3. The ownership, key personnel, or organizational structure of the Manager's company.
   4. The Manager company's financial condition.
   5. The number of clients invested in the subject product and firm wide.
   6. The market value of the total assets managed in the subject product and firm-wide.

D. Managers shall promptly notify ACERA if they are subject to censure or disciplinary action by a regulatory agency.

E. Managers shall provide to ACERA all required documents and reports as set forth in Schedule V – ACERA's Compliance Schedule.

F. Managers shall not make contributions, provide gifts, reimbursements of expenses or provide personal benefits exceeding $250 in the aggregate within any 12-month period to any Trustee, fiduciary, employee or Consultant of ACERA. Donations of educational conferences and similar events and benefits, including travel, meals and accommodations will be made to ACERA and not directed to individuals. The Board will determine whether to accept any donations and will be solely responsible for selection of the Trustee, Staff, or other individual, who will attend or otherwise participate on behalf of ACERA.

SECTION XVIII: MANAGER MONITORING PROCEDURE

The Board has contracted with a number of external Managers to invest ACERA assets in the capital markets. As part of the Board's fiduciary duties to prudently select, monitor and supervise these Managers, the Board has adopted this Procedure. The intent of this Procedure is to notify

Managers of the standards by which they will be evaluated and to establish a structure which the Investment Committee and the Board can use to monitor the performance of the Managers.

Managers will be monitored to

1. Evaluate how well they achieve their investment objectives.
2. Ensure that they adhere to their established investment approach/style and do not attempt to index returns to preserve stellar performance or take extraordinary risk to overcome poor performance.
3. Identify issues or trends that have the potential to result in losses to the Fund.
4. Alert the Board when Managers are not performing to expectations so that appropriate remedial action can be taken.

Managers will be evaluated on the basis of the following: performance, style integrity, organizational stability, compliance, client service, and fees described in greater detail below.

A. PERFORMANCE

On a monthly basis Staff will monitor Manager holdings, activity, and performance.

On a quarterly basis Staff and/or a Consultant will furnish the Investment Committee and/or Board with an in-depth evaluation of each Manager which will include a comparison of the Manager to its Contract benchmark and a peer universe of Managers using a similar investment style. This report shall include an analysis of the sources of Managers' returns (stock selection, industry selection, asset allocation, etc.) and shall identify which decisions enhanced or diminished performance.

On a quarterly basis, trading costs will be evaluated in terms of commissions paid and execution of trades. Staff and/or Consultants shall furnish a report to the Investment Committee and/or Board regarding trading costs on an annual basis.

B. STYLE INTEGRITY

Each Manager will be analyzed at least annually to ensure that the Manager is continuing to invest the portfolio in the style for which they were originally hired. Style integrity is essential to maintain the Board's asset allocation policy. Any significant deviation in style will result in the overall portfolio having a different characteristic, in some measure, from the broad market which is represented by the Russell 3000 index. Significant variations in the portfolio characteristics from the style anticipated in the management Contract may indicate a change in its investment style.

This review also provides the Investment Committee and/or Board an opportunity to evaluate the Manager's continuing "fit" with the goals of the overall Fund. By monitoring the Manager style integrity, the Investment Committee and/or Board can assure that its Manager mix takes advantage of opportunities to increase diversification through lower correlation of returns among individual Managers.

C. ORGANIZATIONAL STABILITY

Managers' organizations will be monitored to ensure continuity of the intellectual and philosophical processes that went into developing the particular investment approach contracted for by ACERA. In addition, Managers will be monitored for business risk, quality of staff, departures of key investment personnel, change in ownership or acquisition, and potential conflicts of interest.

It is ACERA's intent that its portfolio comprises no more than 25% of the Manager's total assets under management (AUM)[2] at any time. Therefore, ACERA will monitor the Managers' assets, firm-wide, as well as in the subject product.

D. COMPLIANCE

Managers will be monitored to ensure they are adhering to federal and state laws regarding securities and the management of investment portfolios, trading, and pension investments; ethical practices of the investment professions; the Contract governing their relationship with ACERA; this Policy; and any other written directives issued by ACERA.

Each ACERA Contract will specify which investment vehicles a Manager is authorized to use, which markets the Manager is authorized to transact business in and any limitations within a market (small or large capitalization, value or growth orientation). The assets in each Manager's portfolio shall be reviewed monthly to ensure compliance with Contract guidelines.

All required documents and reports, set forth in Schedule V, must be submitted in a timely manner and in the format specified by ACERA.

Managers must provide prior notification and justification for failure to comply with rules, regulations, Contract provisions, deadlines or other directives. Managers must provide a time frame for curing any deficiencies. Staff shall evaluate each incident on a case-by-case basis and determine whether an exception may be granted.

E. CLIENT SERVICE

Managers are required to comply with routine portfolio investment guidelines and reporting deadlines and are also expected to cooperate with special requests for information. ACERA will establish reasonable time frames for all requests and reporting and will provide feedback to all external Managers regarding the perceived quality of their client service.

F. FEES

Managers are expected to charge ACERA investment management fees no greater than the fees charged for other clients with a similar investment style, investment objective, and account type,

[2] ACERA defines total AUM as the total market value of assets a Manager manages on behalf of investors under discretionary management where the client delegates responsibility to the Manager.

size and services. Should a Manager enter into a more favorable fee schedule with a similar client, the manager is expected to modify ACERA's fee schedule to reflect the more favorable terms.

ACERA Staff will endeavor to meet with each Manager at least twice a year by telephone or in person to review performance and other issues.

SECTION XIX: CONTRACT REVIEW PROCESS

If during the course of regular monitoring, ACERA determines that a Manager's performance, style integrity, organizational stability, compliance, client service, and/or fees have reached to unacceptable levels, ACERA may, at its discretion, subject the Manager to ACERA's Contract Review Process. As part of the Board's fiduciary duties to prudently select, monitor and supervise their Managers, the Board has approved this process. The purpose of this process is to ensure as little disruption as possible in the event that concerns or problems arise with respect to a Manager's performance. The Board does not confer any additional rights or protections to its Managers by the promulgation of this Policy and/or this process.

There are generally three stages of review: Watchlist, Probation, and Termination (described below). ACERA reserves the right to terminate an investment management Contract at any time, with or without 30 days notice, for any reason, and without resort to this Contract Review Process.

The Contract Review Process may result in one or more of the following:

1. Placement on Watchlist or Probation status
2. Movement from one stage of review to another, or removal from the Contract Review Process
3. Reduction of Assets Under Management
4. Revision of investment Contract guidelines for that Manager
5. Re-negotiation of fees
6. Termination of a Manager's Contract
7. Any other actions deemed appropriate by the Board

Each situation is unique. Action by the Board will vary depending on the type of Manager, the style/strategy, and the deficiency involved. The following describes the Contract Review Process:

A. INITIAL REVIEW

Prior to a Manager being considered for Watchlist, Probation or Termination, ACERA may take the following steps:

1. Analysis

Staff will conduct in-depth analyses of the perceived deficiency to verify that a deficiency exists, form an initial assessment of the severity of the deficiency, and make an initial determination of possible causes.

2. Discussion with the Manager

   Staff will contact the Manager to discuss the situation and the results of Staff's analysis.

3. Consultant Input

   ACERA may seek the services of Consultant to provide additional assessment and advice regarding the situation, depending on the severity of the deficiency.

All phases of account compliance may be reviewed during this step, in addition to the specific issue that originated the Review Process.

B. FORMAL ACTION

After completing the Initial Review, Staff may recommend to the Investment Committee and/or Board that the Manager be either placed on Watchlist or Probation or, in certain cases, Terminated. The Committee and/or Board will approve or reject the recommendation. However, if a Manager's deficiency satisfies the criteria as listed under Watchlist and Probation in this Review Process, Staff may place a Manager on Watchlist or Probation without the Committee and/or Board's prior approval. In that case, Staff will be required to report to the Committee on the action taken in this Review Process as soon as possible. The specific criteria for determining which stage of Contract Review to recommend is outlined later in this Policy section and summarized in tabular form in Schedule II.

Upon approval of a Watchlist or Probation recommendation:

1. Staff will notify the Manager of the Board's decision and will provide the Manager with a statement of concerns which outlines the areas which need improvement.
2. The Manager will be asked to respond in writing with an explanation of the issues and a proposed action plan to resolve the issues within 30 days of receipt of the statement of concerns.
3. Staff, a Consultant and the Manager will collectively draft a Plan of Action. The plan will identify the specific steps to be taken to correct the problem; the time frames for further review; and what additional monitoring may be required.

At the end of the time period specified in the Plan of Action, the Manager will be evaluated and one of the following actions may be taken:

(a) Removal from Contract Review: if the Manager successfully resolves the issues/deficiencies and demonstrates continued success in all other areas of its relationship with ACERA.

(b) Movement from Probation to Watchlist: if the Manager has satisfied all or most of the issues/deficiencies that caused it to be placed on Probation, yet Staff continues to have concerns about the Manager. If circumstances warrant, a Manager may also be moved from Watchlist to Probation at any time during the Contract Review Process.

(c) Extension of Contract Review: a Manager may be given additional time to satisfy the conditions of its Plan of Action if reasonable progress is being made. Extensions may also be granted if unfavorable market conditions or high costs make reallocation of assets inadvisable.

(d) Termination: if the Manager has not satisfactorily resolved the issues/deficiencies, Staff may recommend termination as described below. Termination may be recommended at any time during the Contract Review Process if circumstances warrant.

WATCHLIST

Watchlisting indicates an increased level of concern, but does not indicate major deficiencies. Managers may be placed on ACERA's Watchlist for one or more reasons stated below. The Watchlisting period is typically one year. Staff shall conduct a comprehensive evaluation of the Manager at the end of the one-year Watchlisting period to determine whether the Manager may be removed from Watchlist status. Any of the following may result in a Watchlist status:

A. UNDERPERFORMANCE

Please refer to Schedule IIA for specific Watchlist criteria for each Manager. Managers may be removed from ACERA's Watchlist if Managers' performance is improved to a level where all applicable specific performance criteria as set forth in Schedule IIB of this Policy have been met.

B. STYLE DEVIATION

Managers are expected to adhere to the style of investment management for which they were originally hired. Changes in portfolio characteristics or style drift may lead to a Watchlist status.

C. ORGANIZATIONAL CHANGE

1. New Ownership

   Even relatively benign ownership changes, which impact personnel key to ACERA's portfolio management may be cause for a Watchlist status.

2. Turnover

   Significant turnover or reassignment in top management, portfolio Managers, research or trading staff, or marketing personnel may warrant Watchlisting.

3. Reorganization

Changes which signal management deterioration, departures or reassignment of key investment personnel, a change in ownership that increases risk to ACERA's investments, or hasty, uncontrolled growth in the firm with potential to disrupt the investment team hired for management of ACERA's account will mandate Watchlisting.

4. Assets Under Management

If the market value of ACERA's portfolio rises above 25% of the Manager's total AUM, Watchlist status may be warranted.

D. NON-COMPLIANCE

1. Contracts and Other Agreements

Managers are expected to comply with the investment management Contract, investment guidelines, or other directives. Non- or partial compliance may result in a Watchlist status.

2. Reporting

Staff will contact Managers to request past due reports. If the Manager's reports are consistently delinquent, the payment of fees may be delayed. If a Manager cannot comply with reporting deadlines, ACERA should be given prior notification. If warranted, a variance may be allowed. Managers are expected to resolve reporting problems immediately upon notification by ACERA. Repeated delinquency in reporting may result in a Watchlist status.

E. POOR CLIENT SERVICE

If a Manager is uncooperative and demonstrates a poor client service attitude, Watchlisting is appropriate. Managers are expected to resolve client service issues immediately upon notification by ACERA.

F. HIGH FEES

Watchlisting may be appropriate if a Manager

1. charges ACERA unreasonably high fees relative to what it charges its other clients with a similar investment style, investment objective, and account type, size and service, and/or
2. charges ACERA unreasonably high fees relative to the current market fee rate.

PROBATION

Probation indicates a level of serious deficiency and signals a need for closer contact with the firm. Probation necessitates a cautious, observant relationship with the Manager.

Managers may be placed on Probation with or without first being placed on Watchlist status for one or more reasons stated below. The Probation period is typically one year. Staff shall conduct a comprehensive evaluation of the Manager at the end of the one-year Probation period to determine whether the Manager may be removed from Probation status.

The following may result in Probation:

A. UNDERPERFORMANCE

Please refer to Schedule IIA for specific Probation criteria for each Manager. Managers may be removed from ACERA’s Probation if Managers’ performance is improved to a level where all applicable specific performance criteria as set forth in Schedule IIB of this Policy have been met.

B. STYLE DEVIATION

Probation may be warranted when a Manager’s portfolio characteristics are significantly different from its contractually specified style. In general, a Manager will be placed on Probation after four or more consecutive quarters of deviating from its style benchmark. In effect, if the Manager is no longer the same Manager that was retained for ACERA’s account, Probation and perhaps even Termination is appropriate.

C. ORGANIZATIONAL CHANGE

Changes in ownership, organizational assignments, departures of key investment personnel, a change in ownership that poses substantial risk to ACERA’s investments, or turnover that have the potential to seriously disrupt or destroy the investment management team that was hired to manage the ACERA account may result in Probation or Termination. When key personnel, such as top management, portfolio Managers, research and trading staff are no longer available for use on the ACERA portfolio and do not appear to be replaced or replaceable, Probation and perhaps even Termination is appropriate.

D. NON-COMPLIANCE

If a Manager does not comply with securities laws, industry regulations, standards of professional conduct or contractual provisions, Probation is appropriate. Certain circumstances may warrant Termination.

E. POOR CLIENT SERVICE

Failure to correct any issues that previously resulted in the Watchlist status shall result in Probation. Managers will generally be given one quarter to resolve client service issues.

F. HIGH FEES

Failure to reduce unreasonably high investment management fees shall result in Probation.

TERMINATION

Upon determining that the Manager has not made adequate improvement in the areas outlined in the Plan of Action, Staff may recommend to the Investment Committee and/or Board that the Manager be terminated. Prior to making the final decision to terminate the Manager, the Investment Committee may invite the Manager to make a presentation at the meeting in which the Termination recommendation is to be discussed. Staff will have analyzed the liquidity of the Manager's portfolio and will have a recommendation and plan for disposition of the assets.

Upon the Investment Committee's decision to terminate, Staff will notify the accounting division as well as the Board's legal counsel of the action. All outstanding issues between the Manager and ACERA's Master Custodian, brokers, Consultant, or other parties shall be resolved prior to closing out the Contract. The Manager Termination checklist is attached as Schedule IV.

The Contract Review Process described in this Policy does not provide any additional rights or protections to Managers, beyond what is provided in the Contract. The Board reserves the right to terminate an investment management Contract without resort to the Contract Review Process, at any time, with or without 30 days notice, for any reason or no reason.

SCHEDULE I

ACERA

ASSET ALLOCATION AND MANAGER STRUCTURE TARGETS

ASSET ALLOCATION TARGETS[3]

Asset Class	Target Allocation %	
U.S. Equities	37	
U.S. Large Cap		30
U.S. Small Cap		7
International Equities	23	
Fixed Income	24	
Real Estate	6	
Private Equity and Alternatives	10	

(cont.)

[3] The target asset allocation to each asset class was adopted by the Board in March 2008.

SCHEDULE I (cont.)

ACERA

ASSET ALLOCATION AND MANAGER STRUCTURE TARGETS

MANAGER STRUCTURE TARGETS

Managers		**Target Allocation % Within Asset Class**	**Total Fund**
U.S. Equity			
Large Cap (Core Index)	Mellon Capital	44.5	16.4
Large Cap (Growth)	Trust Company of the West	17.5	6.5
Large Cap (Value)	Pzena	17.5	6.5
Small Cap (Growth)	Next Century Growth	6.5	2.4
Micro Cap (Growth)	Next Century Growth	2.5	0.9
Small Cap (Value)	Brandywine	9.0	3.3
All Cap	Bivium	2.5	1
International Equity			
Core Non-U.S. Equity (Growth)	Capital Guardian	45	10.4
Core Non-U.S. Equity (Value)	Mondrian	35	8.0
Core Non-U.S. Equity (Quantitative)	AQR	20	4.6
Fixed Income			
Enhanced Index	Baird	55	13.2
Aggressive Core Plus	Loomis Sayles	25	6.0
Global Bond	Brandywine	20	4.8
Real Estate[4]			
Private Equity and Alternatives[4]			

[4] ACERA's real estate and private equity and alternatives manager structure targets are specified in ACERA's "Real Estate Strategic Plan" and "PEARLS Policy", respectively.

SCHEDULE IA

ACERA

ASSET ALLOCATION PORTFOLIO REBALANCING

The objective of rebalancing is to control risk and enhance the risk-adjusted return of the asset allocation strategy. For purposes of enhancing the risk-adjusted return of the asset allocation structure, the relative deviation of any liquid sub asset class away from its target weight (or liquidity-adjusted target weight) shall be no more than plus or minus 1.80 standard deviation factors of each allocation's expected volatility, relative to the other allocations in the asset mix. This standard deviation factor shall be used to define the range of allowable deviation from Policy target asset allocations. If any sub asset class reaches its allowable deviation from its target allocation, all sub asset classes will be evaluated.

The actual reallocation will be at the discretion of Staff (with oversight by the rebalancing Consultant) after reviewing the following: the relative magnitude of deviation from target for all other sub asset classes; the available cash liquidity of sub asset classes that could be used to fund rebalancing; pending cash flows (employer and employee contributions, or proceeds from a terminated Manager's portfolio); pending liquidity windows with commingled investment pools; pending investment commitments (real estate transactions and/or new funding commitments); and pending interest coupon and dividend cash flows.

Asset allocation and rebalancing status reports, and any rebalancing activity taken toward attaining the objective of the rebalancing program will be reported to the Board in a timely fashion or whenever a rebalancing transaction occurs.

Significant modifications to the asset allocation strategy shall be cause to review the appropriateness of maintaining this rebalancing parameter or revising it to a parameter more suitable to the revised asset allocation structure.

SCHEDULE IIA

ACERA

Watchlist/Probation Criteria for Underperformance [5]

Watchlist Criteria	Probation Criteria
U.S. Equity	**U.S. Equity**
• Large Cap Core Index: negative tracking error exceeds 5 bps on an annualized basis in any 1 year period. • Large Cap (Growth/Value): cumulative 5 year rolling return is below the benchmark for 2 consecutive quarters, or the Manager's peer ranking falls below median for 2 consecutive quarters in a cumulative 5 year rolling period. • Small/Micro Cap Growth: cumulative 5 year rolling return is below the benchmark for 2 consecutive quarters, or the Manager's peer ranking falls below median for 2 consecutive quarters in a cumulative 5 year rolling period. • Small Cap Value: cumulative 5 year rolling return is below the benchmark for 2 consecutive quarters, or the Manager's peer ranking falls below median for 2 consecutive quarters in a cumulative 5 year rolling period. • Large Cap Enhanced Core: cumulative 5 year rolling return is below the benchmark for 2 consecutive quarters, or the Manager's peer ranking falls below median for 2 consecutive quarters in a cumulative 5 year rolling period.	• Large Cap Core Index: negative tracking error exceeds 5 bps on an annualized basis in any period greater than 1 year, or negative tracking error exceeds 10 bps for any 2 consecutive quarters. • Large Cap (Growth/Value): cumulative 5 year rolling return is below the benchmark for 3 or more consecutive quarters, or the Manager's peer ranking falls below median for 3 or more consecutive quarters in a cumulative 5 year rolling period. • Small/Micro Cap Growth: cumulative 5 year rolling return is below the benchmark for 3 or more consecutive quarters, or the Manager's peer ranking falls below median for 3 or more consecutive quarters in a cumulative 5 year rolling period. • Small Cap Value: cumulative 5 year rolling return is below the benchmark for 3 or more consecutive quarters, or the Manager's peer ranking falls below median for 3 or more consecutive quarters in a cumulative 5 year rolling period. • Large Cap Enhanced Core: cumulative 5 year rolling return is below the benchmark for 3 or more consecutive quarters, or the Manager's peer ranking falls below median for 3 or more consecutive quarters in a cumulative 5 year rolling period.

[5] If the Fund history with a Manager is less than 5 years, ACERA will use a rolling 3 year period.

Watchlist Criteria	Probation Criteria
International Equity • Core Non-U.S. Equity (growth/value/quant.): cumulative 5 year rolling return is below the benchmark for 2 consecutive quarters, or the Manager’s peer ranking falls below median for 2 consecutive quarters in a cumulative 5 year rolling period.	**International Equity** • Core Non-U.S. Equity (growth/value/quant.): cumulative 5 year rolling return is below the benchmark for 3 or more consecutive quarters, or the Manager’s peer ranking falls below median for 3 or more consecutive quarters in a cumulative 5 year rolling period.
Fixed Income • Aggressive Core Plus: cumulative 5 year rolling return is below the benchmark for 2 consecutive quarters, or the Manager’s peer ranking falls below median for 2 consecutive quarters in a cumulative 5 year rolling period. • Global Bond: cumulative 5 year rolling return is below the benchmark for 2 consecutive quarters, or the Manager’s peer ranking falls below median for 2 consecutive quarters in a cumulative 5 year rolling period. • Enhanced Index: cumulative 1 year rolling return is below the benchmark for 2 consecutive quarters, or the Manager’s peer ranking falls below median for 2 consecutive quarters in a cumulative 5 year rolling period.	**Fixed Income** • Aggressive Core Plus: cumulative 5 year rolling return is below the benchmark for 3 or more consecutive quarters, or the Manager’s peer ranking falls below median for 3 or more consecutive quarters in a cumulative 5 year rolling period. • Global Bond: cumulative 5 year rolling return is below the benchmark for 3 more consecutive quarters, or the Manager’s peer ranking falls below median for 3 more consecutive quarters in a cumulative 5 year rolling period. • Enhanced Index: cumulative 1 year rolling return is below the benchmark for 3 or more consecutive quarters, or the Manager’s peer ranking falls below median for 3 or more consecutive quarters in a cumulative 5 year rolling period.

SCHEDULE IIB

ACERA

Performance Criteria for Watchlist/Probation Removal [6]

Watchlist Removal	Probation Removal
U.S. Equity • Large Cap Core Index: negative tracking error falls below 5 bps on an annualized basis in any 1 year period. • Large Cap (Growth/Value): cumulative 5 year rolling return exceeds the benchmark for 2 consecutive quarters, and the Manager's peer ranking exceeds median for 2 consecutive quarters in a cumulative 5 year rolling period. • Small/Micro Cap Growth: cumulative 5 year rolling return exceeds the benchmark for 2 consecutive quarters, and the Manager's peer ranking exceeds median for 2 consecutive quarters in a cumulative 5 year rolling period. • Small Cap Value: cumulative 5 year rolling return exceeds the benchmark for 2 consecutive quarters, and the Manager's peer ranking falls below median for 2 consecutive quarters in a cumulative 5 year rolling period. • Large Cap Enhanced Core: cumulative 5 year rolling return exceeds the benchmark for 2 consecutive quarters, and the Manager's peer ranking exceeds median for 2 consecutive quarters in a cumulative 5 year rolling period.	**U.S. Equity** • Large Cap Core Index: negative tracking error falls below 5 bps on an annualized basis in any period greater than 1 year, and negative tracking error falls below 10 bps for any 2 consecutive quarters. • Large Cap (Growth/Value): cumulative 5 year rolling return exceeds the benchmark for 3 or more consecutive quarters, and the Manager's peer ranking exceeds median for 3 or more consecutive quarters in a cumulative 5 year rolling period. • Small/Micro Cap Growth: cumulative 5 year rolling return exceeds the benchmark for 3 or more consecutive quarters, and the Manager's peer ranking exceeds median for 3 or more consecutive quarters in a cumulative 5 year rolling period. • Small Cap Value: cumulative 5 year rolling return exceeds the benchmark for 3 or more consecutive quarters, and the Manager's peer ranking exceeds median for 3 or more consecutive quarters in a cumulative 5 year rolling period. • Large Cap Enhanced Core: cumulative 5 year rolling return exceeds the benchmark for 3 or more consecutive quarters, and the Manager's peer ranking exceeds median for 3 or more consecutive quarters in a cumulative 5 year rolling period.

[6] If the Fund history with a Manager is less than 5 years, ACERA will use a rolling 3 year period. ACERA reserves the right not to remove a Manager from its Watchlist / Probation status even though the Manager may qualify for a removal based on the Performance Criteria for Watchlist/Probation Removal.

Watchlist Removal	Probation Removal
International Equity • Core Non-US Equity (growth/value/quant.): cumulative 5 year rolling return exceeds the benchmark for 2 consecutive quarters, and the Manager's peer ranking exceeds median for 2 consecutive quarters in a cumulative 5 year rolling period.	**International Equity** • Core Non-US Equity (growth/value/quant.): cumulative 5 year rolling return exceeds the benchmark for 3 or more consecutive quarters, and the Manager's peer ranking exceeds median for 3 or more consecutive quarters in a cumulative 5 year rolling period.
Fixed Income • Aggressive Core Plus: cumulative 5 year rolling return exceeds the benchmark for 2 consecutive quarters, and the Manager's peer ranking exceeds median for 2 consecutive quarters in a cumulative 5 year rolling period. • Global Bond: cumulative 5 year rolling return exceeds the benchmark for 2 consecutive quarters, and the Manager's peer ranking exceeds median for 2 consecutive quarters in a cumulative 5 year rolling period. • Enhanced Index: cumulative 1 year rolling return exceeds the benchmark for 2 consecutive quarters, and the Manager's peer ranking exceeds median for 2 consecutive quarters in a cumulative 5 year rolling period.	**Fixed Income** • Aggressive Core Plus: cumulative 5 year rolling return exceeds the benchmark for 3 or more consecutive quarters, and the Manager's peer ranking exceeds median for 3 or more consecutive quarters in a cumulative 5 year rolling period. • Global Bond: cumulative 5 year rolling return exceeds the benchmark for 3 or more consecutive quarters, and the Manager's peer ranking exceeds median for 3 or more consecutive quarters in a cumulative 5 year rolling period. • Enhanced Index: cumulative 1 year rolling return exceeds the benchmark for 3 or more consecutive quarters, and the Manager's peer ranking exceeds median for 3 or more consecutive quarters in a cumulative 5 year rolling period.

SCHEDULE III

ACERA

POLICY INDEX FOR TOTAL FUND AND BENCHMARKS FOR ASSET CLASSES AND INVESTMENT MANAGERS

POLICY INDEX FOR TOTAL FUND

37% Russell 3000/ 18% Lehman Aggregate/ 3.6% Citigroup World Government Bond Ex. U.S./ 2.4% Lehman High Yield/ 23% MSCI All Country World Index Ex U.S./ 6% NCREIF Property Index/10% Russell 3000 + 150 basis points (net)

BENCHMARKS FOR ASSET CLASSES

Asset Class	**Benchmark**
U.S. Equity	Russell 3000
International Equity	MSCI ACWI Ex. U.S.
Fixed Income	Lehman Aggregate /Citigroup World Government Bond Ex U.S./ Lehman High Yield in the ratio of 75/15/10
Real Estate	NPI
Private Equity and Alternatives	Russell 3000 + 150 basis points (net)

(cont.)

SCHEDULE III (cont.)

ACERA

POLICY INDEX FOR TOTAL FUND AND BENCHMARKS FOR ASSET CLASSES AND INVESTMENT MANAGERS

BENCHMARKS FOR INVESTMENT MANAGERS[7]

Manager	Benchmark
U.S. Equity	
Mellon Capital	S&P 500
Trust Company of the West	Russell 1000 Growth + 250 bps
Pzena	Russell 1000 Value + 200 bps
Next Century Growth (small growth)	Russell 2000 Growth + 250 bps
Next Century Growth (micro growth)	Russell 2000 Growth + 250 bps
Brandywine	Russell 2000 Value
Bivium	Russell 3000 + 200 bps
International Equity	
Capital Guardian	MSCI ACWI Ex U.S.
Mondrian	MSCI ACWI Ex U.S.
AQR	MSCI ACWI Ex U.S.
Fixed Income	
Baird	Lehman Aggregate
Loomis Sayles (Boston)	Lehman Brothers Baa Credit Index
Brandywine (Global Bond)	Citigroup World Government Bond Index
Real Estate[8]	
Private Equity and Alternatives[9]	

[7] Individual Manager's Contract contains more specific information about each Manager's benchmark.
[8] Benchmarks for real estate Managers are specified in ACERA's "Real Estate Strategic Plan". Currently ACERA has 7 real estate Managers managing 10 real estate funds.
[9] Benchmarks for private equity and alternatives Managers are specified in ACERA's "PEARLS Policy" or individual Manager's Contract. Currently, ACERA has no private equity and alternatives Manager.

SCHEDULE IV

ACERA

MANAGER TERMINATION CHECKLIST

This checklist is used to ensure that all details are covered when terminating investment management services.

1) Officially notify the Manager in question of the Board's decision to terminate.

2) Establish a plan of action for reallocating assets from the terminated portfolio; transfer assets to other portfolios or prepare for liquidation.

3) Review department files and logs to identify any outstanding issues.

4) Notify ACERA Administration, Accounting Division, Legal Counsel, Consultant, Custodian and any other vendors of the termination. Identify and resolve all outstanding issues with these parties.

5) Have Manager and Custodian review and sign off on monthly market values and performance figures produced during the Contract period.

6) Hold payment of last invoice until all issues are resolved.

7) Retain terminated Manager files in the ACERA office for a minimum of one year; then send to ACERA archives.

8) Hold terminated Manager files in ACERA archives for a minimum of 5 years.

SCHEDULE V[10]

ACERA

Compliance Schedule

REQUEST	DUE DATE
MONTHLY	
Soft Dollar Commission Report (if applicable) (Submit each month regardless of activity.)	By the 20th of the month following the reported month
Minority Broker Commission Report (Submit each month regardless of activity.)	By the 20th of the month following the reported month
Accounting Report/Portfolio Valuation (Provide transaction data – buys/sells, a portfolio listing including cost and market values, and performance returns.)	By the 20th of the month following the reported month
Derivative Report (if applicable) (Submit each month regardless of whether any derivative instruments were used.)	By the 20th of the month following the reported month
Confirmation that monthly reconciliation with Custodian is performed. (Reconciliation should include market values, transactions and performance.)	By the 20th of the month following the reported month
Overall compliance checklist	By the 20th of the month following the reported month

[10] This Schedule is designed for all investment Managers of ACERA. However, Managers may be required to provide additional compliance reports based on their individual investment Agreements with ACERA. Should there be any conflict between individual investment Agreements with ACERA and ACERA's "General Investment Guidelines, Policies and Procedures," the individual investment Agreements shall prevail.

REQUEST	DUE DATE
QUARTERLY	
Fee Billings (Provide all pertinent backup documentation for fee calculations.)	Within 30 days following the end of the quarter
Confirmation of compliance with limitations on investment vehicles and investment markets[11]	Within 30 days following the end of the quarter
Confirmation of compliance with % limitations on cash holdings, on equity investment and, on fixed-income investment[11]	Within 30 days following the end of the quarter
Confirmation that ACERA's assets under management does not exceed 25% of the total assets under management firm-wide	Within 30 days following the end of the quarter
Market and Portfolio Analyses and Commentaries	Within 45 days following the end of the quarter
Additional requirements applicable to Real Estate Program[12]	
Operations Report/Financial Statements	Within 60 days following the end of the quarter
Preliminary Investment Packages (applicable to Individually Managed Account)	Within 30 days following the completion of the report, if applicable
Valuation Adjustments Memo (applicable to Individually Managed Account)	Within 90 days following the anniversary date of asset acquisition
Property Valuation Report (Applicable to Individually Managed Account)	Within 90 days following the anniversary date of asset acquisition

[11] Detailed information can be found in "Specific Investment Guidelines" section of each Manager's investment Contract.
[12] Detailed information can be found in ACERA's "Real Estate Strategic Plan."

REQUEST	**DUE DATE**
ANNUAL	
Annual Performance Fee Billing (if applicable) (Provide all backup documentation/ reconciliation sign-offs.)	Within 30 days following the end of the performance fee period
Organization Chart	Within 30 days following the end of the year or as soon as updated, whichever is earlier
Fidelity Bond/ Errors and Omissions Insurance (Submit an original certificate.)	Within 30 days of renewal
Audited Financial Statements	Within 90 days following the end of the year
Form ADV, Parts I and II (if applicable)	Within 30 days of filing
Statement or Summary of Code of Ethics	Within 30 days of any change
SEC Examination Reports	Within 30 days of receipt
Fair Political Policies Commission Form 700	On or before March 31st of each year
Additional requirements applicable to Real Estate Program[13]	
Tactical Plans/Management Investment Plans[14] (applicable to Individually Managed Account)	Within 30 days of completion
Asset Management and Budget Plan[14] (applicable to Individually Managed Account)	Within 30 days prior to fiscal year end
Audited Financial Statement for ACERA's Fund (applicable to Individually Managed Account)	Within 90 days following the end of the year

[13] Detailed information can be found in ACERA's "Real Estate Strategic Plan."
[14] 7 copies of this report shall be submitted to Staff.

SCHEDULE VI

ACERA

INVESTMENT PHILOSOPHY (REVISED JULY 2008)

This document describes the investment philosophy of the Alameda County Employees' Retirement Association (ACERA). Its purpose is to enunciate the basic principles and beliefs that underlie ACERA's investment policy and impact the overall management of the pension Fund. The Investment Philosophy (Philosophy) is designed to complement rather than replace the specific investment policies of ACERA. It is expected that ACERA's approach to investments, as reflected in its policies and strategies, will be consistent with the Philosophy over time. Though the Philosophy allows significant flexibility, it also raises some constraints or implications. Where these were deemed to be significant, they have been explicitly identified and labeled as *Implications*.

Future Boards may choose to amend the investment Philosophy, as their experiences and circumstances will almost certainly differ. The initial document and any subsequent changes will provide staff, advisors and future trustees with a frame of reference to help them understand how the investment program has evolved as well as the rationale behind its design. Future Boards may modify the Philosophy as their experiences and circumstances suggest is prudent.

The major sections of the Philosophy are

1. Mission
2. Risk Management
3. Diversification
4. Market Efficiency
5. Organizational Infrastructure and Communications
6. Performance Monitoring and Time Horizon

1. MISSION

a) The Board's primary goals in managing the Fund are

i) To ensure that sufficient funds are available to pay vested benefits and maintain supplemental benefits;

ii) To comply with all applicable fiduciary standards; and

iii) To create value added, where feasible, that will help reduce the costs of the plan, increase benefits, or both.

2. RISK MANAGEMENT

a) The Board believes that prudent management of risk is a central element of the investment function.

b) Though there are numerous risks involved in the management of a pension investment program, ACERA believes that the following warrant particular attention:

i) ***Funding-related Risk*** - The risk that the funds available in the Plan will be insufficient to pay the promised benefits, both vested and supplemental, or that contribution volatility will be unacceptably high. The primary methods for managing funding risk include regularly conducting integrated asset/liability studies, and establishing appropriate and prudent investment and funding policies.

0.1 In managing the relationship between assets and liabilities, the approved asset allocation of the Fund should provide an adequate level of certainty of meeting the projected liabilities of the Plan over a time period, as determined by the actuary.

ii) ***Benchmark-related Risk*** **–** The risk that the investment benchmarks adopted by the Fund are inappropriate, or that the aggregate of the individual Manager benchmarks within an asset class do not adequately reflect the benchmark for the asset class as a whole. The latter risk is a specific risk generally referred to as *benchmark misfit risk (i.e. style risk)*. Inappropriate benchmarks or excessive benchmark misfit risk could result in investment performance different than expected and could adversely impact decisions concerning the hiring or firing of investment managers.

0.1 The primary methods for effectively managing benchmark-related risk are

(a) regular review of the Fund's benchmarks; and

(b) regular measurement and monitoring of misfit risk using proper methodologies.

iii) ***Manager Risk*** - The risk of aberrant performance on the part of individual investment Managers, and the related active management risk for asset classes as a whole.

0.1 The primary methods for mitigating Manager risk are

(a) Prudent processes for selecting and monitoring investment Managers;

(b) Competent internal investment Staff;

(c) Effective investment consulting support; and

(d) Clear communication to investment Managers of ACERA's objectives, expectations, and investment time horizons.

0.2 The primary method for mitigating active management risk for asset classes include

(a) Establishment of appropriate asset class benchmarks;

(b) Careful monitoring of asset class performance relative to the benchmarks; and

(c) Prudent use of passive management.

iv) ***Fortitude Risk*** - The risk that the Board or Staff will fail to exercise the patience, judgment, or fortitude required to support long-term policies and strategies for the investment and funding program.

0.1 The keys to managing fortitude risk are believed to include

(a) Effective orientation and education with respect to institutional investing and actuarial science; and

(b) A commitment to continually refining, confirming, and communicating the investment philosophy and funding policy of the Association.

3. DIVERSIFICATION

a) ACERA acknowledges the basic tenets of modern portfolio theory, which suggest that diversification, or combining assets that are not perfectly correlated with each other, will reduce the long-term volatility of the overall portfolio.

b) It is generally desirable however to avoid overly complex asset structures, provided the allocation selected can reasonably be expected to meet the objectives of the Plan. ACERA believes that the benefits of diversification must be weighed against the costs

involved, which may include fees, liquidity, complexity, communication, internal staff resources and expertise and trustee knowledge and effort.

c) The following asset classes are appropriate candidates for inclusion in its portfolio:
   i) Domestic equity
   ii) International equity (including emerging markets)
   iii) Fixed income, including high yield fixed income and international fixed income
   iv) Real estate
   v) Private equity and alternatives

Implications

- A systematic methodology for re-balancing the investment portfolio is required to ensure proper implementation and adequate risk control concerning ACERA's asset allocation.
- Adding or deleting asset classes or investment Managers should be considered in light of the impact such decisions are likely to have on the general complexity and cost structure of the portfolio, as well as ACERA's ability to prudently achieve its investment and funding goals over the long run.

4. MARKET EFFICIENCY

a) ACERA does not believe in the viability of active management strategies that rely on market timing.

b) ACERA does not believe in the viability of management strategies that call for over weighting or under weighting styles or sectors within an asset class; i.e., benchmark misfit risk will not generate long-term alpha. Accordingly, ACERA generally believes that it should maintain exposures within an asset class (such as style or capitalization weightings) that are consistent with the broad benchmark for the asset class as a whole.

c) ACERA does believe that market efficiency varies among asset classes, creating opportunities for successful active management strategies based on securities selection.

d) Asset classes that can be demonstrated to be efficient should be managed passively in order to reduce active management risk and lower the costs of managing the portfolio.

e) For inefficient asset classes, ACERA believes that it has the ability and a duty to prudently exploit such inefficiencies through active securities selection strategies.

Implications

- ACERA should be conscious of any subtle forms of market timing that may arise in the course of managing the Fund, or that may be implicit in investment strategies presented to ACERA for inclusion in the investment program.

- ACERA must determine appropriate methodologies for determining whether an asset class is efficient or presents appropriate opportunities, thus providing insight to the Board on the use of particular strategies.

5. ORGANIZATIONAL INFRASTRUCTURE AND COMMUNICATIONS

a) ACERA believes that in order for the investment program to achieve its goals, ACERA must invest the necessary resources to build and maintain an appropriate organizational infrastructure, key elements of which include

i) A competent, internal investment staff comprised of a sufficient number of investment professionals possessing appropriate leadership, technical, and administrative skills.

0.1 Attracting a competent staff. ACERA recognizes that it competes with the private sector. It must therefore continually strive to create a total work environment that is challenging, rewarding, and competitive.

ii) A strong relationship with outside general investment Consultant(s) who are able to provide ACERA with the following:

0.1 A high degree of investment expertise;
0.2 Innovative and proactive advice and counsel;
0.3 Strong research support; and
0.4 Strong reporting capabilities.

iii) A broad-based information gathering and reporting system to present well-researched, relevant and timely data in a manner that is easily understood, and that supports rigorous and consistent monitoring of critical investment activities.

iv) An open channel of communication between the Board, management, and the ACERA's external investment professionals.

b) By providing the Board with timely, accurate, and thorough information, the organizational infrastructure will give the Board the high level of comfort it needs to set policy, make investment decisions, oversee the performance of the investment program, and maintain the fortitude necessary to support its investment philosophy, policies, and strategies.

Implications

- ACERA must determine what constitutes an appropriate internal investment staff structure, given the nature of the current investment program.

- ACERA must over time take concrete steps towards creating a work environment that will allow the Association to attract and retain needed staff.

- ACERA must recognize that developing its organizational infrastructure it needs – staffing, consulting support, information systems, and communication channels – cannot be achieved overnight, but rather will require an ongoing commitment of time and resources.

6. PERFORMANCE MONITORING AND TIME HORIZON

a) ACERA holds the following basic beliefs concerning performance monitoring practices and methodologies:

i) The various investment policies of the Fund, in the aggregate, are the most important determinants of investment success; compliance with investment policies should, therefore, be monitored rigorously;

ii) The performance of the total portfolio, individual asset classes, and investment Managers should be compared to appropriate, predetermined benchmarks;

iii) Peer comparisons are an additional valid tool in assessing individual Manager performance (supplementing the use of benchmarks), given that ACERA aims to select superior Managers within particular investment styles or mandates. Peer comparisons, or performance rankings, are also valid tools for measuring the performance of asset class portfolios; and

iv) Peer group comparisons may not be an appropriate means of assessing the performance of the total Fund, given that sponsors have different objectives and risk tolerance levels, and therefore may have different asset allocation policies.

v) Benchmark misfit risk, or the risk that the aggregate of individual investment Manager benchmarks in an asset class do not adequately reflect the benchmark for the asset class as a whole, should be explicitly measured on a regular basis.

vi) Investment Managers are generally hired to fulfill a specific role in a portfolio. Accordingly, ACERA believes it is important that ACERA monitor the extent to which Managers comply with their stated style and mandates.

b) ACERA believes that successful funding and investment decisions require a long-term perspective on the part of the Board and management:

i) It is the intention of the Retirement Board that commitments to asset classes and investment strategies should involve long time horizons that may include more than one business cycle (3-5 years each). Relatively illiquid asset classes may require even longer time horizons.

ii) The Board acknowledges that commitments to individual investment Managers also require a long time horizon of at least one business cycle (3-5 years).

iii) ACERA believes that proper reporting and monitoring systems; and clear communication among Consultants, management, investment Managers and the Board will enable the Board to maintain the necessary long term perspective on all investment decisions.

Implications

- Assessing the investment performance relative to appropriate, pre-determined, benchmarks is as applicable to the total portfolio and to individual asset classes as it is for individual investment Managers, and therefore warrants a commensurate share of the Board's time and attention.

- The Board will spend relatively little time assessing the performance of the Fund relative to that of comparable pension funds.

- ACERA will need to either develop in-house capabilities to regularly measure benchmark-related risk, or it will need to purchase such capabilities from external investment Consultants.

- ACERA will monitor all investment Managers to ensure they are complying with their stated investment style, regardless of whether they are performing well or poorly. Strongly performing Managers who are found to not be following their stated styles will be carefully scrutinized and may be subject to disciplinary action.

- ACERA will monitor all investment providers to ensure compliance with ACERA's "General Investment Guidelines, Policies and Procedures."

SCHEDULE VII

CHARTER OF ACERA'S INVESTMENT COMMITTEE OF THE BOARD

To identify issues pertinent to the effective management of the investment portfolio, initiate analysis of such issues by management or consultants, review all policy recommendations by staff and consultants, provide recommendations to the Board for adoption, and oversee the implementation of the investment program. Specific responsibilities include:

1. The Investment Committee shall review recommendations of staff and consultants and in turn provide its own recommendations to the Board on all investment policies, including investment philosophy, requiring Board approval. Said policies shall normally be contained in, or appended to, the *ACERA General Investment Guidelines, Policies and Procedures*.

2. The Investment Committee shall review and recommend additional policies for the Board's approval as requested by the Board and in accordance with the Policy Development Process.

3. The Investment Committee shall review recommendations of staff and consultants and in turn provide its own recommendation for Board approval on the following matters:
   a) Appointment of Investment Managers;
   b) Appointment of the Investment Consultants;
   c) Appointment of the Custodian Bank.

4. The Investment Committee shall monitor the investment program of ACERA in accordance with all relevant policies of the Board. In general, the Investment Committee shall monitor:
   a) Compliance with and continued appropriateness of all ACERA investment policies;
   b) Progress towards achievement of investment goals;
   c) Progress towards implementation of the ACERA budget and Business Plan with respect to investments; and
   d) Cost effectiveness of the ACERA investment program.

5. In accordance with the provisions of the Open Meeting Law, the Investment Committee shall allow adequate opportunity for input from the public and shall respond to such input in a manner that reflects the Committee members' fiduciary duties as trustees of the Plan.

Frequency of Meetings

The Investment Committee shall generally meet monthly on the second Wednesday of the month, but may meet more or less frequently as required.

Committee Composition

The Investment Committee shall be composed of all Board members, one of whom shall serve as Committee Chair. Alternate members shall serve on the Investment Committee as provided by law.

Staff Contact

The Chief Executive Officer shall appoint a staff person to serve as a staff contact to the Investment Committee.

SCHEDULE VIII

ACERA

TABLE OF AMENDMENT DATES

AMENDING RESOLUTIONS

Jun.	27,	1985
Oct.	10,	1985
Jan.	9,	1986
Jan.	16,	1986
Mar.	13,	1986
May.	22,	1986
Sep.	11,	1986
Oct.	9,	1986
Nov.	20,	1986
May.	14,	1987
Aug.	13,	1987
Oct.	8,	1987
Apr.	21,	1988
Jul.	28,	1988
Jan.	29,	1989(4)
Apr.	13,	1989(5)
May.	18,	1989
Jul.	13,	1989
Aug.	10,	1989
Nov.	16,	1989(2)
Jul.	11,	1991
Jun.	11,	1992
Jun.	10,	1993
Jul.	8,	1993
Nov.	18,	1993
May.	14,	1994
Aug.	18,	1994
Nov.	20,	1994
Feb.	16,	1995
May.	18,	1995
Jan.	16,	1997
Aug.	20,	1998
May	20,	1999
Jan.	31,	2000
Apr.	19,	2001
Jul.	18,	2002
Feb.	21,	2003
Feb.	19,	2004
Feb.	17,	2005
Jul.	20,	2006
Jun.	21,	2007
Sep.	18,	2008

Alameda County Employees'
Retirement Association

ACERA

GENERAL INVESTMENT GUIDELINES, POLICIES AND PROCEDURES

AMENDED May 20, 2013

ACERA
GENERAL INVESTMENT GUIDELINES, POLICIES AND PROCEDURES
2013

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[1] Prepared for ACERA by Cortex Consulting; adopted by the Board of ACERA on March 8, 2000; revised in May, 2013.

ACERA

GENERAL INVESTMENT GUIDELINES, POLICIES AND PROCEDURES

SECTION I: MISSION AND PURPOSE

The Alameda County Employees' Retirement Association (ACERA) exists for the purposes of providing accurate, timely benefits to its members and their beneficiaries and defraying reasonable expenses of administration.

The Board of Retirement (the Board), having exclusive authority and exclusive fiduciary responsibility for the investment and administration of the Trust Fund (the Fund), hereby establishes the following "General Investment Guidelines, Policies and Procedures" (the Policy) for the investment of ACERA's assets. The Board reserves the right to amend, supplement, or rescind this Policy at any time.

The Board is directed by law and given discretion to prudently invest the retirement plan assets. The purpose of this statement of Policy is to assist ACERA in effectively supervising said investments and to encourage effective communication between ACERA and its investment managers (Manager(s)) and investment consultants (Consultant(s)).

ACERA's investment goal is to operate at a level of performance in the upper quartile of comparable pension funds on a risk-adjusted basis and to be as fully funded as possible so that ACERA's benefit costs do not become a burden upon future generations of members and taxpayers.

SECTION II: CONSTITUTIONAL REQUIREMENTS

Article 16 §17 of the California State Constitution provides in pertinent part as follows:

"Notwithstanding any other provisions of law or this Constitution to the contrary, the retirement board of a public pension or retirement system shall have plenary authority and fiduciary responsibility for investment of moneys and administration of the system, subject to all the following:

a. The retirement board of a public pension or retirement system shall have the sole and exclusive fiduciary responsibility over the assets of the public pension or retirement system. The retirement board shall also have sole and exclusive responsibility to administer the system in a manner that will assure prompt delivery of benefits and related services to the participants and their beneficiaries. The assets of a public pension or retirement system are trust funds and shall be held for the exclusive purposes of providing benefits to participants in the pension or retirement system and their beneficiaries and defraying reasonable expenses of administering the system.

b. The members of the retirement board of a public pension or retirement system shall discharge their duties with respect to the system solely in the interest of, and for the exclusive purposes of providing benefits, to participants and their beneficiaries, minimizing employer contributions thereto, and defraying reasonable expenses of administering the system. A retirement board's duty to its participants and their beneficiaries shall take precedence over any other duty.

c. The members of the retirement board of a public pension or retirement system shall discharge their duties with respect to the system with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with these matters would use in the conduct of an enterprise of a like character and with like aims.

d. The members of the retirement board of a public pension or retirement system shall diversify the investments of the system so as to minimize the risk of loss and to maximize the rate of return, unless under the circumstances it is clearly not prudent to do so.

e. The retirement board of a public pension or retirement system, consistent with the exclusive fiduciary responsibilities vested in it, shall have the sole and exclusive power to provide for actuarial services in order to assure the competency of the assets of the public pension or retirement system.

f. With regard to the retirement board of a public pension or retirement system which includes in its composition elected employee members, the number, terms, and method of selection or removal of members of the retirement board which were required by law or otherwise in effect on July 1, 1991, shall not be changed, amended, or modified by the Legislature unless the change, amendment, or modification enacted by the Legislature is ratified by a majority vote of the electors of the jurisdiction in which the participants of the system are or were, prior to retirement, employed.

g. The Legislature may by statute continue to prohibit certain investments by a retirement board where it is in the public interest to do so, and provided that the prohibition satisfies the standards of fiduciary care and loyalty required of a retirement board pursuant to this section.

h. As used in this section, the term "retirement board" shall mean the board of administration, board of trustees, board of directors, or other governing body or board of a public employees' pension or retirement system; provided, however, that the term "retirement board" shall not be interpreted to mean or include a governing body or board created after July 1, 1991 which does not administer pension or retirement benefits, or the elected legislative body of a jurisdiction which employs participants in a public employees' pension or retirement system."

SECTION III: ROLES AND PRINCIPAL DUTIES

The Fund investments shall be prudently planned, implemented, managed, monitored and guarded. The Board, Investment Committee (Committee), Investment Staff (Staff), Consultant, Custodian Bank (Custodian), and Manager shall coordinate this process. See the defined roles and principal duties of the above-mentioned parties below:

A. THE BOARD shall review and approve Committee recommendations. The Board also reviews, adopts and monitors all investment policies, guidelines and procedures required to prudently administer the Fund and to effectively mitigate risk to the Fund.

B. THE COMMITTEE shall identify issues pertinent to the effective investment and administration of the Fund and initiate analysis of such issues by Staff, Consultant or Managers. It also reviews Staff's and Consultant's recommendations regarding all investment policies and investment Fund management. The Committee provides recommendations to the Board for adoption, oversees implementation, and monitors the investment programs in accordance with all applicable laws and Board-established policies, guidelines and procedures. Refer to Schedule VII – Charter of ACERA's Investment Committee of the Board for detailed Committee responsibilities.

C. STAFF shall oversee the Fund's investment program activities, implement the Board/Committee's decisions, make recommendations to the Committee regarding Fund management, and recommend investment-related policies and procedures to the Committee. Additionally, Staff monitors the performance and compliance of Managers in accordance with all applicable laws, Board-established policies, guidelines and procedures, as well as "Specific Investment Guidelines"[2] set out in the investment agreement between ACERA and each Manager (Agreement or Contract). Staff also facilitates the Committee meetings and completes activity as directed by the Board/Committee.

D. CONSULTANT shall review, analyze and evaluate the Fund's effectiveness and efficiency and make fund management related recommendations. Consultant assists Staff in implementing the Board/Committee's decisions and developing all investment-related policies. Consultant's responsibilities are detailed in the service agreement between ACERA and Consultant.

E. CUSTODIAN shall provide custody of ACERA's investment assets. Custodian's responsibilities are detailed in the service agreement between ACERA and Custodian.

F. MANAGER shall prudently manage its Managed Account (defined in Section VII – Eligible Asset Categories) in accordance with all applicable laws, Board-established policies, guidelines and procedures, as well as Specific Investment Guidelines. Manager's responsibilities are detailed in the Agreement.

[2] Includes the Objectives/Guidelines of all comingled funds.

SECTION IV: INVESTMENT PHILOSOPHY

The following is a summary of ACERA's investment philosophy. For the complete statement, please refer to Schedule VI of this document, "ACERA Investment Philosophy."

The Board believes that its investment policies, in aggregate, are the most important determinants of its investment success. Compliance with investment policies should, therefore, be monitored rigorously. The Board also believes that performance of the total portfolio, individual asset classes, and Managers should be monitored and compared to appropriate, predetermined benchmarks.

The Board believes that prudent management of risk is a central element of the investment function and that diversification among asset classes will reduce risk and enhance returns of the overall investment portfolio in the long term.

The Board believes that market efficiency and opportunities vary among asset classes and may change over extended periods of time; therefore, the Board believes that ACERA's portfolio management strategies should adapt over time to reflect the changing nature of capital markets.

The Board's primary goals in managing the Fund are

1. To ensure that sufficient funds are available to pay vested benefits and maintain supplemental benefits;
2. To comply with all applicable fiduciary standards; and
3. To add marginal value that will help reduce the costs of the plan and/or to increase benefits for the beneficiaries.

The Board believes that, to achieve its goals, ACERA must invest the necessary resources to build and maintain an appropriate organizational infrastructure.

SECTION V: ASSET ALLOCATION AND REBALANCING

Asset allocation targets, a function of the returns and risks from various asset classes and the nature of the plan's liabilities, are set forth in Schedule I. A goal of asset allocation is balancing asset growth versus liability growth considering time horizons, liabilities and risk tolerance. ACERA's objective is to conduct an asset/liability study once every five (5) years and an asset allocation study once every three (3) years or more often if necessary.

Rebalancing is the risk control process of returning an allocation back to the desired target level after having drifted away from its targeted position. Equal probability bands, as defined by standard deviation factors, shall be used to define the acceptable ranges around the asset allocation targets as set forth in Schedule IA. The objective of rebalancing is to enhance the risk-adjusted performance of the asset allocation structure.

Staff shall be responsible for maintaining the relative weights of asset classes and allocations within the acceptable rebalancing ranges. Should an asset class or allocation fall outside its target range, Staff shall rebalance the asset class or allocation back to the target weights as specified in the asset allocation targets in Schedule IA.

Staff shall:

1. Monitor the portfolio;
2. Determine whether or not any asset category is out of balance with its target asset allocation in excess of the specified tolerance range;
3. Determine whether or not any Manager within each asset category is out of balance with its target allocation in excess of the specified tolerance range;
4. And, if this is determined, either
   (a) instruct the relevant Managers to redirect cash income (interest coupon and dividends) in concert with an evaluation of pending commitments and other cash flows (employer and employee contributions), in order to bring the allocation(s) back to the adopted strategic target; and/or
   (b) instruct the relevant Managers to liquidate or acquire the appropriate dollar value of securities to reach the target and reallocate the cash thus generated or required to the other category(s) or Manager(s), as necessary.

Staff shall report to the Board on a regular basis the status of the Fund with respect to how categories are tracking relative to their allowable ranges, as well as any actions taken to rebalance the portfolio.

SECTION VI: INVESTMENT STRATEGY AND MANAGER STRUCTURE

A. U.S. EQUITY will be structured to capture exposure to the broad U.S. equity market as represented by the Russell 3000 Index. Passively managed (index) portfolios will be used in portions of the markets that are reasonably efficient. These portfolios are intended to provide broadly diversified market exposure with controlled (market) risk and minimal cost.

   Actively managed portfolios will be used when the Board determines that a Manager possesses special skills or abilities that enable that Manager to capture excess returns relative to the market, adjusted for risk and fees; or to exploit specialty markets that provide enhanced return with acceptable risk.

   A great part of the Russell 3000 Index, on a market value basis, is comprised of large-cap stocks. The Board has adopted a policy of obtaining overall exposure to this segment of the market via passively managed indexed products. In addition, some active Managers have been employed to enhance overall portfolio return on a risk- and fee-adjusted basis.

   The remainder of the Russell 3000 Index is comprised of small to mid-cap companies. Some opportunities for active management enhancement exist in these securities due to market inefficiencies. ACERA will attempt to capture these opportunities through a mix of Managers who have the special skills required to identify smaller companies that may be undervalued or possess substantial growth potential.

The U.S. equity portfolio shall be allocated among the various styles and Managers. The U.S. equity asset allocation and manager structure targets are outlined in Schedules IA and IB.

B. INTERNATIONAL EQUITY represents an opportunity to diversify risk and capture enhanced returns within markets generally less efficient than the U.S. domestic equity market. 100% of the international equity portion of the Fund will be invested in actively managed portfolios.

The international equity portfolio shall be allocated among the various styles and Managers. The international equity asset allocation and manager structure targets are outlined in Schedules IA and IB.

C. FIXED INCOME represents a means of reducing overall portfolio risk and capturing incremental returns either domestically or globally. Inefficiencies in the pricing and trading of fixed income securities create opportunities to add value through active management. 100% of the fixed income portion of the portfolio will be invested in actively managed portfolios.

The fixed income portfolio shall be allocated among the various styles and Managers. The fixed income asset allocation and manager structure targets are outlined in Schedules IA and IB.

D. REAL ESTATE will be used as a means for diversifying the portfolio and capturing additional returns due to the low correlation between returns on real estate and financial assets. Due to the illiquid nature of real estate assets, distinctions between active and passive management are not applicable. Detailed information regarding real estate investments is included in ACERA's "Real Estate Strategic Plan," which is maintained as a separate document.

The real estate portfolio shall be allocated among the various styles and Managers. The real estate portfolio asset allocation target is outlined in Schedules IA and IB.

E. PRIVATE EQUITY AND ALTERNATIVES represents a means of further diversifying the portfolio and generating returns superior to those available in the public equity market to compensate the Fund for the long term and illiquid commitments associated with such investments. Due to the absence of an appropriate index for private equity and alternatives investments, distinctions between active and passive management are not applicable.

The private equity and alternatives portfolio shall be allocated among the various sub-categories and Managers. The private equity and alternatives total portfolio asset allocation target is outlined in Schedules IA and IB. Specific details on the strategic allocation to the private equity and alternatives investment portfolio are outlined in ACERA's "Private Equity and Alternatives Return Leading Strategies Policy (PEARLS Policy)" which is maintained as a separate document.

F. REAL RETURN POOL investments are expected to produce positive returns with a goal of protecting the Fund against unexpected U.S. inflation and increasing U.S. inflation expectations.

   The real return pool portfolio shall be allocated among the specific types of Managers. The real return pool total portfolio allocation target is outlined in Schedules IA and IB. See the Addendum for additional detail.

In aggregate, investments in non U.S. markets across all asset classes shall not exceed 45% of the market value of the total Fund.

SECTION VII: ELIGIBLE ASSET CATEGORIES

The Fund shall hold assets in categories established by the Board. Any asset category may be held in direct form, in pooled/commingled form, or in both. Asset categories managed by one or more "Qualified Investment Managers" are called "Managed Accounts or Funds." Eligible asset categories are listed and defined below.

A. CASH AND CASH EQUIVALENT shall consist of, but not be limited to, cash, short term (12 months or less) interest bearing investments of high quality such as U.S. Treasury issues, insured certificates of deposit of U.S. banks (fixed and/or variable), commercial paper rated A-1, P-1 or both, or other instruments of equal or better quality, and money market funds available through the Custodian.

B. U.S. EQUITY shall consist of, but not be limited to, common stocks and other securities which are convertible into common stocks, and ADRs (American Depository Receipts), as well as cash (per "A" above) and fixed income (per "D" below) when used as temporary substitutes for common stocks.

C. INTERNATIONAL EQUITY shall consist of, but not be limited to, common stocks and other securities convertible into common stocks of companies domiciled outside of the U.S., GDRs (Global Depository Receipts), IDRs (International Depository Receipts) and other depository receipts as well as cash/cash equivalents (per "A" above) and fixed income (per "D" below), domestic or international, which are being used as temporary substitutes for common stock.

D. FIXED INCOME shall consist of investments in, but not be limited to, U.S. taxable bonds, debentures, notes and other evidences of debt. Fixed income may also include, but not be limited to, non-dollar denominated bonds issued by corporations or governments domiciled outside of the U.S. Other eligible investments shall include cash/cash equivalents (per "A" above), convertible bonds, and preferred stock.

E. REAL ESTATE shall consist of investments in real estate and equity real estate through the use of commingled or direct investments. Detailed information about real estate investments is included in ACERA's "Real Estate Strategic Plan," which is maintained as a separate document.

F. PRIVATE EQUITY AND ALTERNATIVES shall consist of investments including, but not limited to, venture capital, corporate buyouts, debt-related and special situations, absolute return strategies, and other non-traditional and uncorrelated investments. Private equity and alternatives investments may be denominated in U.S. dollars or other currencies. Detailed information about private equity and alternatives investments is included in ACERA's "PEARLS Policy" which is maintained as a separate document.

G. REAL RETURN POOL shall consist of investments including, but not be limited to, commodities, TIPS, Inflation Break-evens, and REITs. All Real Return Pool investments/ strategies are Alternative Investments. See the Addendum for additional detail.

In aggregate, non U.S. currency exposure (net) across all asset classes shall not exceed 45% of the market value of the total Fund.

SECTION VIII: ASSET CATEGORIES OBJECTIVES

The general objective of the Board is to preserve capital and to earn a return from appreciation and income, as described herein:

1. To ensure the integrity of ACERA's actuarial funding plan, one minimum return objective for the Fund shall be the current actuarial interest assumption rate plus 25 basis points per year over a full market cycle. Returns shall be calculated net of all fees (both administrative and investment fees).
2. To ensure that ACERA's assets grow appropriately to match salary increases which directly impact benefit levels, an additional minimum return objective for the Fund over a full market cycle (up to five (5) years) shall also be 400 basis points (4.00%) per year over the national Core Consumer Price Index, published by the U.S. Department of Commerce. Returns shall be calculated gross of investment management fees.
3. To ensure that ACERA's external investment manager structure, in the aggregate, is performing satisfactorily, an additional minimum return objective for the Fund over a market cycle (up to five (5) years) shall be to achieve annualized investment returns equivalent to the Fund's Policy Index on a gross of investment management fees basis.

The objectives of each asset category are

A. CASH AND CASH EQUIVALENT

1. An annualized rate of return in excess of 90-Day U.S. Treasury bills, and
2. An annualized rate of return within the upper one half of a universe of like short-term funds.

B. U.S. EQUITY

1. An annualized rate of return in excess of the annualized U.S. equity market returns as measured by the Russell 3000 Index, and

2. An annualized rate of return within the upper 33rd percentile of the InvestorForce database or similar database of the annualized returns of diversified domestic equity portfolios.

C. INTERNATIONAL EQUITY

1. An annualized rate of return in excess of the Morgan Stanley Capital International All Country World Investable Market Index Ex U.S. (MSCI ACWI Ex U.S. IMI), and
2. An annualized rate of return within the top quartile of the InvestorForce database or similar database of the annualized returns of diversified international equity portfolios.

D. FIXED INCOME

1. An annualized rate of return in excess of the Barclay's Aggregate Bond Index, Citigroup World Government Bond Ex. U.S. and Barclay's High Yield Index in a ratio of 75/15/10, and
2. A rate of return within the top quartile of the InvestorForce database or similar database of the performance of diversified fixed income portfolios.

E. REAL ESTATE

1. Total Net Return – equivalent to the National Council of Real Estate Investment Fiduciaries Open-End Diversified Core Equity (NFI ODCE) as a minimum return for the total portfolio over rolling five-year periods, and
2. Income Return – Income, which is defined as cash distributed to ACERA , should comprise generally 50% of the total expected return over rolling five-year periods for all Core (as defined in ACERA's "Real Estate Strategic Plan") products.

F. PRIVATE EQUITY AND ALTERNATIVES

1. An annualized rate of return in excess of the Russell 3000 Index plus 100 basis points net of all fees and expenses over a full market cycle. Please refer to ACERA's PEARLS Policy, which is maintained as a separate document, for detailed information.

G. REAL RETURN POOL

1. An annualized rate of return in excess of the Core Consumer Price Index plus 300 basis points (3.00%). See the Addendum for additional detail.

In addition, objectives that reflect a particular investment strategy or style employed by an individual Manager shall be outlined in the Specific Investment Guidelines attached to the Manager's Contract.

SECTION IX: ALLOCATION OF CASH FLOW

Cash flow not needed for benefit payments or administrative expenses shall be allocated to Managed Accounts in a ratio that best funds the overall targeted asset allocation as reflected in Schedules IA and IB.

If cash flow is insufficient for the payment of benefits or to cover administrative expenses, then Managed Accounts shall be debited in a ratio that best satisfies the target allocation shown in Schedules IA and IB. Such debits, if necessary, will be carried out as needed and with timely notice to Managers to facilitate effective funds transitions and performance measurement.

For all planned investments which may not need to be funded immediately, a reserve may be budgeted and invested in appropriate accounts in accordance with the asset allocation targets until such moneys are required. Alternatively, Managed Accounts within "overfunded" asset classes may be called upon to provide the required moneys.

SECTION X: PROHIBITED INVESTMENTS

Managers shall exercise prudent expert standards in defining prohibited investments. For example, prohibited investments include, but are not limited to, securities issued by the County of Alameda or any agency thereof.

SECTION XI: DIRECTED BROKERAGE

ACERA has established an open Directed Brokerage (DB) Program designed to maximize the recapture of brokerage commissions by enforcement of the target percentages of direction. ACERA's DB Program is governed by ACERA's DB Policy, which is maintained as a separate document.

The strategic objective of the DB Program is to take advantage of the industry-accepted recapture of a portion of trade commissions paid to brokers. The primary goals of the DB Program are to 1) recapture 50% or more of commissions paid on a specific percentage of trades sent to correspondent brokers on a timely basis; 2) construct the percentage of trades subject to recapture so as to allow investment managers to have access to the research they need; 3) seek "Best Execution" through third-party administration and outside consultant monitoring; and 4) encourage local and emerging broker participation through the use of an open correspondent network program.

SECTION XII: DERIVATIVE INSTRUMENT USAGE

Exposure to risk by use of derivative instruments must be consistent with ACERA's overall investment policy as well as an individual Manager's Specific Investment Guidelines. In general, derivatives shall not be used to establish a leveraged position (i.e., offsetting Cash positions must be maintained against all delayed settlement transactions). Should there be any conflict between an individual Manager's Specific Investment Guidelines and this Policy statement regarding the use of derivative instruments, the Specific Investment Guidelines shall control.

SECTION XIII: SELECTION OF INVESTMENT MANAGERS

The Investment Committee shall direct Staff and/or a Consultant to initiate searches for Managers. Staff and/or the Consultant shall research for qualified candidates and present a list of finalists to the Investment Committee for its approval. Upon approval of the list, the finalists shall be interviewed by Staff and the Consultant (if applicable). Staff and the Consultant (if applicable) shall evaluate the interviews, rank the finalists, and make a recommendation to the Investment Committee to hire one or more firms attaining the highest rankings in a publicly noticed meeting at which no less than five (5) Investment Committee members shall be present. It is possible that none of the firms will be recommended for hire.

The above-mentioned procedures are developed for the convenience and benefit of ACERA, and shall not bind ACERA or invalidate the selection of a Manager, if different processes are used subsequent to the promulgation of this Policy. ACERA recognizes that some investments by their nature present unique opportunities and there may not be suitable competitors for a unique investment opportunity. ACERA also recognizes that due to inherent features of some investments, time constraints may require ACERA to use a different investment manager selection process.

SECTION XIV: EMERGING INVESTMENT MANAGERS

The Board has established the ACERA Emerging Investment Manager Policy (EM Policy), which is maintained as a separate document. The purpose of the EM Policy is to establish a framework for the development and administration of ACERA's Emerging Investment Manager Program (EM Program), consistent with the Board's fiduciary responsibilities in the investment of the Fund. The EM Policy states that the initial investment of the EM Program is not to exceed 1% of the total Fund.

The strategic objective of the EM Program is to add incremental value to the Fund through the hiring of the most talented Emerging Investment Managers (EMs) to manage ACERA's assets.

The primary goals of the EM Program are to 1) identify and gain early access to the most talented investment managers in their early business stages; 2) generate superior Fund return performance through the EM Program; 3) identify superior EMs and/or investment opportunities in the State of California and Alameda County that are equal to or superior to comparable available investments; and 4) further diversify the Fund's overall investment program, so as to enhance risk-adjusted returns of the Fund.

SECTION XV: AUTHORITY OF INVESTMENT MANAGERS

Subject to the laws of the United States and the State of California, and to the terms and conditions of this Policy, Managers shall have full discretion to direct the purchase, exchange, sale and reinvestment of the assets of the Managed Accounts. The Board expects that Managers will recommend changes to this Policy when any part of this Policy appears to be at variance with overall market and economic conditions.

Managers shall place orders to buy and sell securities and, by notice to the Custodian, shall cause the Custodian to deliver and receive securities on behalf of the Fund. Managers shall, upon Board inquiry, report placement of ACERA brokerage activities such that the Board shall be assured commissions were placed for the sole and exclusive benefit of the Fund.

Separate account Managers shall not vote proxies. Proxies shall be voted by ACERA, via a proxy voting service vendor, in accordance with "ACERA Proxy Voting Guidelines and Procedures" which is maintained as a separate document.

Securities lending shall be performed under the oversight of Staff, in accordance with Board-established procedures.

SECTION XVI: INVESTMENT GUIDELINES FOR THE MANAGED ACCOUNTS

Individual Manager discretion shall be governed by the Investment Guidelines for the Managed Accounts as well as the Specific Investment Guidelines for each Manager. Should there be any conflict between the Specific Investment Guidelines of an individual Manager and the Investment Guidelines for the Managed Accounts, the Specific Investment Guidelines shall prevail.

A. GENERAL

1. All investments shall comply with all applicable laws of the U.S. and the State of California governing the investment of pension trusts.
2. All securities transactions shall be executed by reputable broker/dealers, banks, or the Custodian, and shall be on a best-price and best-execution basis, and shall be reported to ACERA as is called for elsewhere in this Policy.
3. All Managers shall refrain from investing in a tobacco producer investment opportunity when, in their expert opinion, an alternative non-tobacco producer investment opportunity is available that will satisfy the same ACERA portfolio guidelines, instructions and objectives for risk, return and diversification.

B. EQUITY

Managers have full discretion to invest solely in readily marketable and diversified equity securities subject to the following:

1. For Managed Accounts, no more than 10% of the value (at time of purchase) of the account shall be invested in the securities of a single issuer.
2. ACERA shall not hold more than 10% of the equity securities of any issuer.
3. Equity securities shall possess value and quality corroborated by generally accepted techniques and standards of fundamental securities analysis.
4. Assets in a Managed Account not invested in equity securities shall be kept with interest in appropriate money market instruments, including any money market fund available through the Custodian.

5. A Managed Account shall be subject to ACERA's Policy statement on the use of derivatives in Section XII.
6. All Managers shall endeavor to be fully invested in stocks at all times unless they have received specific authorization to the contrary from the Board. Cash holdings, as defined in this Policy, shall generally not exceed 5% of the portfolio on a market value basis.

C. FIXED INCOME

Managers have full discretion to invest solely in readily marketable and diversified securities including, but not limited to

1. Obligations of the U.S. and/or eligible foreign government treasuries.
2. Obligations guaranteed by agencies of the U.S. and/or eligible foreign governments.
3. Insured certificates of deposit and banker's acceptances of credit worthy banks.
4. Corporate and other evidences of debt. At least 80% of this debt must be rated by Moody's Investor's Services or by Standard & Poors Corporation.
5. Commercial paper and banker's acceptances of issuers rated P-1 by Moody's Investor's Service or A-1 by Standard & Poors Corporation.
6. Excepting direct obligations of the U.S. and/or eligible foreign governments, and those explicitly guaranteed by the U.S. and/or eligible governments, no account shall hold more than 5%, at cost, of the obligations of any single issuer.
7. Excepting direct obligations of the U.S. and/or eligible foreign governments, and those explicitly guaranteed by the U.S. and/or eligible governments, no security shall comprise more than 5% of the account, as determined at the time of purchase.
8. A Managed Account shall be subject to ACERA's Policy on the use of derivatives as stated in Section XII.

SECTION XVII: INVESTMENT MANAGER SPECIFICATIONS

A. Managers must be registered as investment advisers under the Investment Adviser's Act of 1940, a bank (as defined in that Act) or an insurance company qualified to perform investment management services under state law in more than one state, including the State of California. Unless an exception is granted by the Board, by accepting appointment as ACERA's Managers, Managers shall acknowledge that they are "Plan Fiduciaries" and "Qualified Investment Managers" as defined by the Employees' Retirement Income Security Act (ERISA) of 1974 (see or reference United States Code Title 29 Section 1001 et. seq.).

B. Managers shall maintain fiduciary insurance in the amount of 10% of the total assets managed in the ACERA account or $25 million, whichever is higher, unless the Contract specifies otherwise.

C. Managers shall promptly notify ACERA of changes that occur in any of the following:

1. The investment strategy used in managing the subject product.
2. The key personnel involved in managing ACERA's account.
3. The ownership, key personnel, or organizational structure of the Manager's company.

4. The Manager company's financial condition.
5. The number of clients invested in the subject product and firm wide.
6. The market value of the total assets managed in the subject product and firm-wide.

D. Managers shall promptly notify ACERA if they are subject to censure or disciplinary action by a regulatory agency.

E. Managers shall provide to ACERA all required documents and reports as set forth in Schedule V – ACERA's Compliance Schedule.

F. Managers shall not make contributions, provide gifts, reimbursements of expenses or provide personal benefits exceeding $440.00[3] in the aggregate within any 12-month period to any Trustee, fiduciary, employee or Consultant of ACERA. Donations of educational conferences and similar events and benefits, including travel, meals and accommodations will be made to ACERA and not directed to individuals. The Board will determine whether to accept any donations and will be solely responsible for selection of the Trustee, Staff, or other individual, who will attend or otherwise participate on behalf of ACERA.

SECTION XVIII: MANAGER MONITORING PROCEDURE

The Board has contracted with a number of external Managers to invest ACERA assets in the capital markets. As part of the Board's fiduciary duties to prudently select, monitor and supervise these Managers, the Board has adopted this Procedure. The intent of this Procedure is to notify Managers of the standards by which they will be evaluated and to establish a structure which the Investment Committee and the Board can use to monitor the performance of the Managers.

Managers will be monitored to:

1. Evaluate how well they achieve their investment objectives.
2. Ensure that they adhere to their established investment approach/style and do not attempt to index returns to preserve stellar performance or take extraordinary risk to overcome poor performance.
3. Identify issues or trends that have the potential to result in losses to the Fund.
4. Alert the Board when Managers are not performing to expectations so that appropriate remedial action can be taken.

Managers will be evaluated on the basis of the following: performance, style integrity, organizational stability, compliance, client service, and fees described in greater detail below.

A. PERFORMANCE

On a monthly basis Staff will monitor Manager holdings, activity, and performance.

On a quarterly basis Staff and/or a Consultant will furnish the Investment Committee and/or Board with an in-depth evaluation of each Manager which will include a comparison of the

[3] Updated annually by the California Fair Political Practices Commission.

Manager to its Contract benchmark and a peer universe of Managers using a similar investment style. This report shall include an analysis of the sources of Managers' returns (stock selection, industry selection, asset allocation, etc.) and shall identify which decisions enhanced or diminished performance.

On a quarterly basis, trading costs will be evaluated in terms of commissions paid and execution of trades. Staff and/or Consultants shall furnish a report to the Investment Committee and/or Board regarding trading costs on an annual basis.

B. STYLE INTEGRITY

Each Manager will be analyzed at least annually to ensure that the Manager is continuing to invest the portfolio in the style for which it was originally hired. Style integrity is essential to maintain the Board's asset allocation policy. Any significant deviation in style will result in the overall portfolio having a different characteristic, in some measure, from the broad market which is represented by the Russell 3000 Index. Significant variations in the portfolio characteristics from the style anticipated in the management Contract may indicate a change in its investment style.

This review also provides the Investment Committee and/or Board an opportunity to evaluate the Manager's continuing "fit" with the goals of the overall Fund. By monitoring the Manager style integrity, the Investment Committee and/or Board can assure that its Manager mix takes advantage of opportunities to increase diversification through lower correlation of returns among individual Managers.

C. ORGANIZATIONAL STABILITY

Managers' organizations will be monitored to ensure continuity of the intellectual and philosophical processes that went into developing the particular investment approach contracted for by ACERA. In addition, Managers will be monitored for business risk, quality of staff, departures of key investment personnel, change in ownership or acquisition, and potential conflicts of interest.

It is ACERA's intent that its portfolio comprises no more than 25% of the Manager's total assets under management (AUM)[4] at any time. Therefore, ACERA will monitor the Managers' assets, firm-wide, as well as in the subject product.

D. COMPLIANCE

Managers will be monitored to ensure they are adhering to federal and state laws regarding securities and the management of investment portfolios, trading, and pension investments; ethical practices of the investment professions; the Contract governing their relationship with ACERA; this Policy; and any other written directives issued by ACERA.

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[4] ACERA defines total AUM as the total market value of assets a Manager manages on behalf of investors under discretionary management where the client delegates responsibility to the Manager.

Each ACERA Contract will specify which investment vehicles a Manager is authorized to use, which markets the Manager is authorized to transact business in and any limitations within a market (small or large capitalization, value or growth orientation). The assets in each Manager's portfolio shall be reviewed monthly to ensure compliance with Contract guidelines.

All required documents and reports, set forth in Schedule V, must be submitted in a timely manner and in the format specified by ACERA, unless otherwise agreed to.

Managers must provide prior notification and justification for failure to comply with rules, regulations, Contract provisions, deadlines or other directives. Managers must provide a time frame for curing any deficiencies. Staff shall evaluate each incident on a case-by-case basis and determine whether an exception may be granted.

E. CLIENT SERVICE

Managers are required to comply with routine portfolio investment guidelines and reporting deadlines and are also expected to cooperate with special requests for information. ACERA will establish reasonable time frames for all requests and reporting and will provide feedback to all external Managers regarding the perceived quality of their client service.

F. FEES

Managers are expected to charge ACERA investment management fees no greater than the fees charged for other clients with a similar investment style, investment objective, and account type, size and services. Should a Manager enter into a more favorable fee schedule with a similar client, the manager is expected to modify ACERA's fee schedule to reflect the more favorable terms.

ACERA Staff will endeavor to meet with each Manager at least twice a year by telephone or in person to review performance and other issues.

SECTION XIX: CONTRACT REVIEW PROCESS

If during the course of regular monitoring, ACERA determines that a Manager's performance, style integrity, organizational stability, compliance, client service, and/or fees have reached to unacceptable levels, ACERA may, at its discretion, subject the Manager to ACERA's Contract Review Process. As part of the Board's fiduciary duties to prudently select, monitor and supervise their Managers, the Board has approved this process. The purpose of this process is to ensure as little disruption as possible in the event that concerns or problems arise with respect to a Manager's performance. The Board does not confer any additional rights or protections to its Managers by the promulgation of this Policy and/or this process.

There are generally three stages of review: Watchlist, Probation, and Termination (described below). ACERA reserves the right to terminate an investment management contract at any time, with or without thirty (30) calendar days notice, for any reason, and without resort to this Contract Review Process.

The Contract Review Process may result in one or more of the following:

1. Placement on Watchlist or Probation status
2. Movement from one stage of review to another, or removal from the Contract Review Process
3. Reduction of Assets Under Management
4. Revision of investment Contract guidelines for that Manager
5. Re-negotiation of fees
6. Termination of a Manager's Contract
7. Any other actions deemed appropriate by the Board

Each situation is unique Action by the Board will vary depending on the type of Manager, the style/strategy, and the deficiency involved. The following describes the Contract Review Process:

A. INITIAL REVIEW

Prior to a Manager being considered for Watchlist, Probation or Termination, ACERA may take the following steps:

1. Analysis

   Staff will conduct in-depth analyses of the perceived deficiency to verify that a deficiency exists, form an initial assessment of the severity of the deficiency, and make an initial determination of possible causes.

2. Discussion with the Manager

   Staff will contact the Manager to discuss the situation and the results of Staff's analysis.

3. Consultant Input

   ACERA may seek the services of Consultant to provide additional assessment and advice regarding the situation, depending on the severity of the deficiency.

All phases of account compliance may be reviewed during this step, in addition to the specific issue that originated the Review Process.

B. FORMAL ACTION

After completing the Initial Review, Staff may recommend to the Investment Committee and/or Board that the Manager be either placed on Watchlist or Probation or, in certain cases, Terminated. The Committee and/or Board will approve or reject the recommendation. However, if a Manager's deficiency satisfies the criteria as listed under Watchlist and Probation in this Review Process, Staff may place a Manager on Watchlist or Probation without the Committee and/or Board's prior approval. In that case, Staff will be required to report to the Committee on the action taken in this Review Process as soon as possible. The specific criteria for determining which stage of Contract Review to recommend is outlined later in this Policy section and summarized in tabular form in Schedule II.

Upon approval of a Watchlist or Probation recommendation:

1. Staff will notify the Manager of the Board's decision and will provide the Manager with a statement of concerns which outlines the areas which need improvement.
2. The Manager will be asked to respond in writing with an explanation of the issues and a proposed action plan to resolve the issues within thirty (30) calendar days of receipt of the statement of concerns.
3. Staff, a Consultant and the Manager will collectively draft a Plan of Action. The plan will identify the specific steps to be taken to correct the problem; the time frames for further review; and what additional monitoring may be required.

   At the end of the time period specified in the Plan of Action, the Manager will be evaluated and one of the following actions may be taken:

   (a) Removal from Contract Review: if the Manager successfully resolves the issues/deficiencies and demonstrates continued success in all other areas of its relationship with ACERA.
   (b) Movement from Probation to Watchlist: if the Manager has satisfied all or most of the issues/deficiencies that caused it to be placed on Probation, yet Staff continues to have concerns about the Manager. If circumstances warrant, a Manager may also be moved from Watchlist to Probation at any time during the Contract Review Process.
   (c) Extension of Contract Review: a Manager may be given additional time to satisfy the conditions of its Plan of Action if reasonable progress is being made. Extensions may also be granted if unfavorable market conditions or high costs make reallocation of assets inadvisable.
   (d) Termination: if the Manager has not satisfactorily resolved the issues/deficiencies, Staff may recommend termination as described below. Termination may be recommended at any time during the Contract Review Process if circumstances warrant.

WATCHLIST

Watchlist status indicates an increased level of concern, but does not indicate major deficiencies. Managers may be placed on ACERA's Watchlist for one or more reasons stated below. The Watchlist period is typically one year. Staff shall conduct a comprehensive evaluation of the Manager at the end of the one-year Watchlist status period to determine whether the Manager may be removed from Watchlist status. Any of the following may result in a Watchlist status:

a. UNDERPERFORMANCE

Please refer to Schedule IIA for specific Watchlist criteria for each Manager. A Manager may be removed from ACERA's Watchlist if the Manager's performance has improved to a level where all applicable specific performance criteria as set forth in Schedule IIB of this Policy have been met.

b. STYLE DEVIATION

Managers are expected to adhere to the style of investment management for which they were originally hired. Changes in portfolio characteristics or style drift may lead to a Watchlist status.

c. ORGANIZATIONAL CHANGE

1. New Ownership

   Even relatively benign ownership changes, which impact personnel key to ACERA's portfolio management may be cause for a Watchlist status.

2. Turnover

   Significant turnover or reassignment in top management, portfolio Managers, research or trading staff, or marketing personnel may warrant Watchlist status.

3. Reorganization

   Changes which signal management deterioration, departures or reassignment of key investment personnel, a change in ownership that increases risk to ACERA's investments, or hasty, uncontrolled growth in the firm with potential to disrupt the investment team hired for management of ACERA's account will mandate Watchlist status.

4. Assets Under Management (AUM)

   If the market value of ACERA's portfolio rises above 25% of the Manager's total AUM, Watchlist status may be warranted.

d. NON-COMPLIANCE

1. Contracts and Other Agreements

   Managers are expected to comply with the investment management Contract, investment guidelines, or other directives. Non- or partial compliance may result in a Watchlist status.

2. Reporting

Staff will contact Managers to request past due reports. If the Manager's reports are consistently delinquent, the payment of fees may be delayed. If a Manager cannot comply with reporting deadlines, ACERA should be given prior notification. If warranted, a variance may be allowed. Managers are expected to resolve reporting problems immediately upon notification by ACERA. Repeated delinquency in reporting may result in a Watchlist status.

e. POOR CLIENT SERVICE

If a Manager is uncooperative and demonstrates a poor client service attitude, Watchlist status is appropriate. Managers are expected to resolve client service issues immediately upon notification by ACERA.

f. HIGH FEES

Watchlist status may be appropriate if a Manager

1. Charges ACERA unreasonably high fees relative to what it charges its other clients with a similar investment style, investment objective, and account type, size and service, and/or
2. Charges ACERA unreasonably high fees relative to the current market fee rate.

PROBATION

Probation indicates a level of serious deficiency and signals a need for closer contact with the firm. Probation necessitates a cautious, observant relationship with the Manager.

Managers may be placed on Probation with or without first being placed on Watchlist status for one or more reasons stated below. The probation period is typically one year. Staff shall conduct a comprehensive evaluation of the Manager at the end of the one-year Probation period to determine whether the Manager may be removed from Probation status.

The following may result in Probation:

a. UNDERPERFORMANCE

Please refer to Schedule IIA for specific Probation criteria for each Manager. A Manager may be removed from ACERA's Probation if its performance has improved to a level where all applicable specific performance criteria as set forth in Schedule IIB of this Policy have been met.

b. STYLE DEVIATION

Probation may be warranted when a Manager's portfolio characteristics are significantly different from its contractually specified style. In general, a Manager will be placed on Probation after four or more consecutive quarters of deviating from its style benchmark. In effect, if the Manager is no longer the same Manager that was retained for ACERA's account, Probation and perhaps even Termination is appropriate.

c. ORGANIZATIONAL CHANGE

Changes in ownership, organizational assignments, departures of key investment personnel, a change in ownership that poses substantial risk to ACERA's investments, or turnover that have the potential to seriously disrupt or destroy the investment management team that was hired to manage the ACERA account may result in Probation or Termination. When key personnel, such as top management, portfolio Managers, research and trading staff are no longer available for use on the ACERA portfolio and do not appear to be replaced or replaceable, Probation and perhaps even Termination is appropriate.

d. NON-COMPLIANCE

If a Manager does not comply with securities laws, industry regulations, standards of professional conduct or contractual provisions, Probation is appropriate. Certain circumstances may warrant Termination.

e. POOR CLIENT SERVICE

Failure to correct any issues that previously resulted in the Watchlist status shall result in Probation. Managers will generally be given one calendar quarter to resolve client service issues.

f. HIGH FEES

Failure to reduce unreasonably high investment management fees shall result in Probation.

TERMINATION

Upon determining that the Manager has not made adequate improvement in the areas outlined in the Plan of Action, Staff may recommend to the Investment Committee and/or Board that the Manager be terminated. Prior to making the final decision to terminate the Manager, the Investment Committee may invite the Manager to make a presentation at the meeting in which the Termination recommendation is to be discussed. Staff will have analyzed the liquidity of the Manager's portfolio and will have a recommendation and plan for disposition of the assets.

Upon the Investment Committee's decision to terminate, Staff will notify the relevant ACERA Staff regarding this decision (See Section IV). All outstanding issues between the Manager and ACERA's Master Custodian, brokers, Consultant, or other parties shall be resolved prior to closing out the Contract. The Manager Termination checklist is attached as Schedule IV.

The Contract Review Process described in this Policy does not provide any additional rights or protections to Managers, beyond what is provided in the contract. The Board reserves the right to terminate an investment management contract without resort to the Contract Review Process, at any time, with or without thirty (30) calendar days notice, for any reason or no reason.

In the event of an emergency or crisis, such as an imminent, foreseeable threat to a Managed Account within the Fund, the following procedure shall be followed to protect the portfolio (with the advice and assistance of the appropriate ACERA consultant(s):

(a) Staff shall make a concerted attempt to arrange a special meeting (in person and/or by telephone) of the Board to consider and to resolve the matter.
(b) If (a) is not practicable within the time necessary to protect the portfolio, the Board delegates temporary authority to the Board Chair (and/or Vice Chair) and the Committee Chair (and/or Vice Chair) to consider and to resolve the matter.

The temporary authority delegated under subsection (b) shall be strictly limited to the matter itself and any related actions that may be necessary and appropriate. Under subsection (b), at least two (2) persons of the four persons identified would be required to consider and resolve the matter. The temporary delegated authority shall be as full and complete as the Board's authority which means that Managed Accounts and funds may be terminated and/or redeemed.

Staff and the consultants shall prepare and submit a full report on any and all actions taken under this section for presentation at the next scheduled Investment Committee meeting.

SCHEDULE IA

ACERA

ASSET ALLOCATION TARGETS[5]

Asset Class	Target Allocation %
U.S. Equities	32
U.S. Large Cap	26
U.S. Small Cap	6
International Equities	27
Fixed Income	15
Real Estate	6
Private Equity and Alternatives	15
Real Return Pool	5
Cash	0

[5] The target asset allocation to each asset class was adopted by the Board in September 2012.

SCHEDULE IB

ACERA

MANAGER STRUCTURE TARGETS

Managers		**Target Allocation % Within Asset Class**	**Target Allocation % Within Total Fund**
U.S. Equity			
Large Cap (Core Index)	Mellon Capital	44.5	14.2
Large Cap (Growth)	Trust Company of the West	17.5	5.6
Large Cap (Value)	Pzena	17.5	5.6
Small Cap (Growth)	Next Century Growth	6.5	2.1
Micro Cap (Growth)	Next Century Growth	2.5	0.8
Small Cap (Value)	Kennedy Capital	9.0	2.9
All Cap	Bivium	2.5	0.8
International Equity			
Core Non-U.S. Equity (Growth)	Capital Guardian	40.0	10.8
Core Non-U.S. Equity (Value)	Mondrian	30.0	8.1
Core Non-U.S. Equity (Quantitative)	AQR	20.0	5.4
Core Non-U.S. Equity (Small Cap)	Franklin Templeton	10.0	2.7
Fixed Income			
Enhanced Index	Baird	50.0	7.5
Aggressive Core Plus	Loomis Sayles	25.0	3.8
Global Bond	Brandywine	25.0	3.8
Real Estate[6]			6.0
Private Equity and Alternatives[6]			15.0
Real Return Pool			5.0
Cash			0.0

[6] ACERA's real estate, private equity, and alternative manager structure targets are specified in ACERA's "Real Estate Strategic Plan" and "PEARLS Policy," respectively.

SCHEDULE IC

ACERA

ASSET ALLOCATION PORTFOLIO REBALANCING

The objective of rebalancing is to control risk and enhance the risk-adjusted return of the asset allocation strategy. For purposes of enhancing the risk-adjusted return of the asset allocation structure, the relative deviation of any liquid sub asset class away from its target weight (or liquidity-adjusted target weight) shall be no more than plus or minus 1.80 standard deviation factors of each allocation’s expected volatility, relative to the other allocations in the asset mix. This standard deviation factor shall be used to define the range of allowable deviation from Policy target asset allocations. If any sub asset class reaches its allowable deviation from its target allocation, all sub asset classes will be evaluated.

The actual reallocation will be at the discretion of Staff (with oversight by the rebalancing Consultant) after reviewing the following: the relative magnitude of deviation from target for all other sub asset classes; the available cash liquidity of sub asset classes that could be used to fund rebalancing; pending cash flows (employer and employee contributions, or proceeds from a terminated Manager’s portfolio); pending liquidity windows with commingled investment pools; pending investment commitments (real estate transactions and/or new funding commitments); and pending interest coupon and dividend cash flows.

Asset allocation and rebalancing status reports, and any rebalancing activity taken toward attaining the objective of the rebalancing program will be reported to the Board quarterly.

Significant modifications to the asset allocation strategy shall be cause to review the appropriateness of maintaining this rebalancing parameter or revising it to a parameter more suitable to the revised asset allocation structure.

SCHEDULE IIA

ACERA

Watchlist/Probation Criteria for Underperformance[7]

Watchlist Criteria	Probation Criteria
U.S. Equity • Large Cap Core Index: negative tracking error exceeds 5 bps on an annualized basis in any 1 year period. • Large Cap (Growth/Value): cumulative 5 year rolling return is below the benchmark for 2 consecutive quarters, or the Manager's peer ranking falls below the median for 2 consecutive quarters in a cumulative 5 year rolling period. • Small/Micro Cap Growth: cumulative 5 year rolling return is below the benchmark for 2 consecutive quarters, or the Manager's peer ranking falls below the median for 2 consecutive quarters in a cumulative 5 year rolling period. • Small Cap Value: cumulative 5 year rolling return is below the benchmark for 2 consecutive quarters, or the Manager's peer ranking falls below the median for 2 consecutive quarters in a cumulative 5 year rolling period. • Large Cap Enhanced Core: cumulative 5 year rolling return is below the benchmark for 2 consecutive quarters, or the Manager's peer ranking falls below the median for 2 consecutive quarters in a cumulative 5 year rolling period.	**U.S. Equity** • Large Cap Core Index: negative tracking error exceeds 5 bps on an annualized basis in any period greater than 1 year, or negative tracking error exceeds 10 bps for any 2 consecutive quarters. • Large Cap (Growth/Value): cumulative 5 year rolling return is below the benchmark for 3 or more consecutive quarters, or the Manager's peer ranking falls below the median for 3 or more consecutive quarters in a cumulative 5 year rolling period. • Small/Micro Cap Growth: cumulative 5 year rolling return is below the benchmark for 3 or more consecutive quarters, or the Manager's peer ranking falls below the median for 3 or more consecutive quarters in a cumulative 5 year rolling period. • Small Cap Value: cumulative 5 year rolling return is below the benchmark for 3 or more consecutive quarters, or the Manager's peer ranking falls below the median for 3 or more consecutive quarters in a cumulative 5 year rolling period. • Large Cap Enhanced Core: cumulative 5 year rolling return is below the benchmark for 3 or more consecutive quarters, or the Manager's peer ranking falls below the median for 3 or more consecutive quarters in a cumulative 5 year rolling period.

[7] If the Fund history is less than 5 years, ACERA will use a rolling 3 year period.

Watchlist Criteria	Probation Criteria
International Equity • Core Non-U.S. Equity (growth/ value/ quant/ small cap): cumulative 5 year rolling return is below the benchmark for 2 consecutive quarters, or the Manager's peer ranking falls below median for 2 consecutive quarters in a cumulative 5year rolling period.	**International Equity** • Core Non-U.S. Equity (growth/value/quant/small cap): cumulative 5 year rolling return is below the benchmark for 3 or more consecutive quarters, or the Manager's peer ranking falls below median for 3 or more consecutive quarters in a cumulative 5 year rolling period.
Fixed Income • Aggressive Core Plus: cumulative 5 year rolling return is below the benchmark for 2 consecutive quarters, or the Manager's peer ranking falls below the median for 2 consecutive quarters in a cumulative 5 year rolling period. • Global Bond: cumulative 5 year rolling return is below the benchmark for 2 consecutive quarters, or the Manager's peer ranking falls below the median for 2 consecutive quarters in a cumulative 5 year rolling period. • Enhanced Index: cumulative 5 year rolling return is below the benchmark for 2 consecutive quarters, or the Manager's peer ranking falls below the median for 2 consecutive quarters in a cumulative 5 year rolling period.	**Fixed Income** • Aggressive Core Plus: cumulative 5 year rolling return is below the benchmark for 3 or more consecutive quarters, or the Manager's peer ranking falls below the median for 3 or more consecutive quarters in a cumulative 5 year rolling period. • Global Bond: cumulative 5 year rolling return is below the benchmark for 3 more consecutive quarters, or the Manager's peer ranking falls below the median for 3 more consecutive quarters in a cumulative 5 year rolling period. • Enhanced Index: cumulative 5 year rolling return is below the benchmark for 3 or more consecutive quarters, or the Manager's peer ranking falls below the median for 3 or more consecutive quarters in a cumulative 5 year rolling period.

SCHEDULE IIB

ACERA

Performance Criteria for Watchlist/Probation Removal [8]

Watchlist Removal	Probation Removal
U.S. Equity	**U.S. Equity**
• Large Cap Core Index: negative tracking error falls below 5 bps on an annualized basis in any 1 year period. • Large Cap (Growth/Value): cumulative 5 year rolling return exceeds the benchmark for 2 consecutive quarters, and the Manager's peer ranking exceeds the median for 2 consecutive quarters in a cumulative 5 year rolling period. • Small/Micro Cap Growth: cumulative 5 year rolling return exceeds the benchmark for 2 consecutive quarters, and the Manager's peer ranking exceeds the median for 2 consecutive quarters in a cumulative 5 year rolling period. • Small Cap Value: cumulative 5 year rolling return exceeds the benchmark for 2 consecutive quarters, and the Manager's peer ranking exceeds the median for 2 consecutive quarters in a cumulative 5 year rolling period. • Large Cap Enhanced Core: cumulative 5 year rolling return exceeds the benchmark for 2 consecutive quarters, and the Manager's peer ranking exceeds the median for 2 consecutive quarters in a cumulative 5 year rolling period.	• Large Cap Core Index: negative tracking error falls below 5 bps on an annualized basis in any period greater than 1 year, and negative tracking error falls below 10 bps for any 2 consecutive quarters. • Large Cap (Growth/Value): cumulative 5 year rolling return exceeds the benchmark for 3 or more consecutive quarters, and the Manager's peer ranking exceeds the median for 3 or more consecutive quarters in a cumulative 5 year rolling period. • Small/Micro Cap Growth: cumulative 5 year rolling return exceeds the benchmark for 3 or more consecutive quarters, and the Manager's peer ranking exceeds the median for 3 or more consecutive quarters in a cumulative 5 year rolling period. • Small Cap Value: cumulative 5 year rolling return exceeds the benchmark for 3 or more consecutive quarters, and the Manager's peer ranking exceeds the median for 3 or more consecutive quarters in a cumulative 5 year rolling period. • Large Cap Enhanced Core: cumulative 5 year rolling return exceeds the benchmark for 3 or more consecutive quarters, and the Manager's peer ranking exceeds the median for 3 or more consecutive quarters in a cumulative 5 year rolling period.

[8] If the Fund history with a Manager is less than 5 years, ACERA will use a rolling 3 year period. ACERA reserves the right not to remove a Manager from its Watchlist/Probation status even though the Manager may qualify for removal based on the Performance Criteria for Watchlist/Probation Removal.

Watchlist Removal	Probation Removal
International Equity • Core Non-U.S. Equity (growth/value/quant./ small cap): cumulative 5 year rolling return exceeds the benchmark for 2 consecutive quarters, and the Manager’s peer ranking exceeds the median for 2 consecutive quarters in a cumulative 5 year rolling period.	**International Equity** • Core Non-U.S. Equity (growth/value/quant./ small cap): cumulative 5 year rolling return exceeds the benchmark for 3 or more consecutive quarters, and the Manager’s peer ranking exceeds the median for 3 or more consecutive quarters in a cumulative 5 year rolling period.
Fixed Income • Aggressive Core Plus: cumulative 5 year rolling return exceeds the benchmark for 2 consecutive quarters, and the Manager’s peer ranking exceeds the median for 2 consecutive quarters in a cumulative 5 year rolling period. • Global Bond: cumulative 5 year rolling return exceeds the benchmark for 2 consecutive quarters, and the Manager’s peer ranking exceeds the median for 2 consecutive quarters in a cumulative 5 year rolling period. • Enhanced Index: cumulative 5 year rolling return exceeds the benchmark for 2 consecutive quarters, and the Manager’s peer ranking exceeds the median for 2 consecutive quarters in a cumulative 5 year rolling period.	**Fixed Income** • Aggressive Core Plus: cumulative 5 year rolling return exceeds the benchmark for 3 or more consecutive quarters, and the Manager’s peer ranking exceeds the median for 3 or more consecutive quarters in a cumulative 5 year rolling period. • Global Bond: cumulative 5 year rolling return exceeds the benchmark for 3 or more consecutive quarters, and the Manager’s peer ranking exceeds the median for 3 or more consecutive quarters in a cumulative 5 year rolling period. • Enhanced Index: cumulative 5 year rolling return exceeds the benchmark for 3 or more consecutive quarters, and the Manager’s peer ranking exceeds the median for 3 or more consecutive quarters in a cumulative 5 year rolling period.

SCHEDULE III

ACERA

POLICY INDEX FOR TOTAL FUND AND BENCHMARKS FOR ASSET CLASSES AND INVESTMENT MANAGERS

POLICY INDEX FOR TOTAL FUND

32% Russell 3000/ 11.25% Barclay's Aggregate/ 2.25% Citigroup World Government Bond Ex. U.S./ 1.50% Barclay's High Yield/ 27% MSCI All Country World Index Ex U.S. IMI/ 6% ODCE /15% Russell 3000 + 100 basis points (net)/5% Core CPI + 300 basis points.

BENCHMARKS FOR ASSET CLASSES

Asset Class	**Benchmark**
U.S. Equity	Russell 3000
International Equity	MSCI ACWI Ex. U.S. IMI
Fixed Income	Barclay's Aggregate /Citigroup World Government Bond Ex U.S./ Barclay's High Yield in the ratio of 75/15/10
Real Estate	NCREIF ODCE
Private Equity and Alternatives	Russell 3000 + 100 basis points (net)
Real Return Pool	Core CPI + 300 basis points

SCHEDULE III (cont.)

ACERA

POLICY INDEX FOR TOTAL FUND AND BENCHMARKS FOR ASSET CLASSES AND INVESTMENT MANAGERS

BENCHMARKS FOR INVESTMENT MANAGERS[9]

Manager	**Benchmark**
U.S. Equity	
Bivium	Russell 3000 + 200 bps
Kennedy Capital	Russell 2000 Value + 250 bps
Mellon Capital	S&P 500
Next Century Growth (small growth)	Russell 2000 Growth +250 bps
Next Century Growth (micro growth)	Russell Microcap Growth + 250 bps
Pzena	Russell 1000 Value + 200 bps
Trust Company of the West	Russell 1000 Growth + 250 bps
International Equity	
AQR	MSCI ACWI Ex U.S.
Capital Guardian	MSCI ACWI Ex U.S.
Franklin Templeton	MSCI ACWI Ex U.S. Small Cap
Mondrian	MSCI ACWI Ex U.S.
Fixed Income	
Baird	Barclay’s Aggregate Index
Brandywine (Global Bond)	Citigroup World Gov. Bond Index
Loomis Sayles (Boston)	Barclay’s Baa Credit Index
Real Estate[10]	NFI ODCE
Private Equity and Alternatives[11]	Russell 3000 + 100 bps
Real Return Pool	Core CPI + 300 bps

[9] Individual Manager’s Contract contains more specific information about each Manager’s benchmark.
[10] Benchmarks for real estate Managers are specified in ACERA’s “Real Estate Strategic Plan.”
[11] Benchmarks for Private Equity and Alternatives Managers are specified in ACERA’s “PEARLS Policy” and/or individual Manager’s Contract.

SCHEDULE IV

ACERA

MANAGER TERMINATION CHECKLIST

This checklist is used to ensure that all details are covered when terminating investment management services.

1) Officially notify the Manager in question of the Board's decision to terminate.

2) Establish a plan of action for reallocating assets from the terminated portfolio; transfer assets to other portfolios or prepare for liquidation.

3) Review department files and logs to identify any outstanding issues.

4) Notify ACERA Administration, Fiscal Services Department, Legal Counsel, Consultant, Custodian and any other vendors of the termination. Identify and resolve all outstanding issues with these parties.

5) Have Manager and Custodian review and sign off on monthly market values and performance figures produced during the Contract period.

6) Hold payment of last invoice until all issues are resolved.

7) Retain terminated Manager files in the ACERA office for a minimum of one year; then send to ACERA archives.

8) Hold terminated Manager files in ACERA archives in accordance with the ACERA Record Retention Policy and Schedule or applicable securities laws and accounting practice.

SCHEDULE V[12]

ACERA

Compliance Schedule

REQUEST	**DUE DATE**
MONTHLY	
Soft Dollar Commission Report (if applicable) (Submit each month regardless of activity.)	By the 20th calendar day of the month following the reported month
Broker Commission Report (Submit each month regardless of activity.)	By the 20th calendar day of the month following the reported month
Accounting Report/Portfolio Valuation (Provide transaction data – buys/sells, a portfolio listing including cost and market values, and performance returns.)	By the 20th calendar day of the month following the reported month
Derivative Report (if applicable) (Submit each month regardless of whether any derivative instruments were used.)	By the 20th calendar day of the month following the reported month
Confirmation that monthly reconciliation with Custodian is performed. (Reconciliation should include market values, transactions, and performance.)	By the 20th calendar day of the month following the reported month
ACERA overall compliance checklist	By the 20th calendar day of the month following the reported month

[12] This schedule is designed for all investment Managers of ACERA. However, Managers may be required to provide additional compliance reports based on their individual Investment Agreements with ACERA. Should there be any conflict between individual Investment Agreements with ACERA and ACERA's "General Guidelines, Policies and Procedures," the individual Investment Management Agreements shall prevail.

REQUEST	DUE DATE
QUARTERLY	
Fee Billings (Provide all pertinent backup documentation for fee calculations)	Within 30 calendar days following the end of the quarter
Confirmation of compliance with limitations on investment vehicles and investment markets[13]	Within 30 calendar days following the end of the quarter
Confirmation of compliance with % limitations on cash holdings, on equity investment and on fixed-income investment[13]	Within 30 calendar days following the end of the quarter
Confirmation that ACERA's assets under management do not exceed 25% of the Total assets under management firm-wide	Within 30 calendar days following the end of the quarter
Market and Portfolio Analyses and Commentaries	Within 45 calendar days following the end of the quarter
Additional requirements applicable to Real Estate Program	
Operations Report/Financial Statements	Within 60 calendar days following the end of the quarter
Preliminary Investment Packages (Applicable to Individually Managed Account)	Within 30 calendar days following the completion of the report, if applicable
Valuation Adjustments Memo (Applicable to Individually Managed Account)	Within 90 calendar days following the anniversary date of asset acquisition
Property Valuation Report (Applicable to Individually Managed Account)	Within 90 calendar days following the anniversary date of asset acquisition

[13] Detailed information can be found in "Specific Investment Guideline" section of each Manager's Investment Contract.

REQUEST	DUE DATE
ANNUAL	
Annual Performance Fee Billing (if applicable) (Provide all backup documentation/ reconciliation sign-offs.)	Within 30 calendar days following the end of the performance fee period
Organization Chart	Within 30 calendar days following the end of the year or as soon as updated, whichever is earlier
Fidelity Bond/ Errors and Omissions Insurance (Submit an original certificate.)	Within 30 calendar days of renewal
Audited Financial Statements	Within 90 calendar days following the end of the year
Form ADV, Parts 1 and 2A and 2B (Brochures) (as applicable)	Within 30 calendar days of filing
Statement or Summary of Code of Ethics	Within 30 calendar days of any change
SEC Examination Reports	Within 30 calendar days of receipt
Fair Political Policies Commission Form 700	On or before March 31^{st} of each year
Placement Agent Policy Update	Within 30 calendar days, provide an update of any change to the information included in the most recently filed Placement Agent Information Disclosure Form.
Additional requirements applicable to Real Estate Program	
Tactical Plans/Management Investment Plans[14] (applicable to Individually Managed Account)	Within 30 calendar days of completion
Asset Management and Budget Plan[14] (applicable to Individually Managed Account)	Within 30 calendar days prior to fiscal year end
Audited Financial Statement for ACERA's Fund (applicable to Individually Managed Account)	Within 90 calendar days following the end of the year

[14] Seven copies of this report shall be submitted to Staff.

SCHEDULE VI

ACERA

INVESTMENT PHILOSOPHY (REVISED MAY 2013)

This document describes the investment philosophy of the Alameda County Employees' Retirement Association (ACERA). Its purpose is to enunciate the basic principles and beliefs that underlie ACERA's investment policy and impact the overall management of the pension Fund. The Investment Philosophy (Philosophy) is designed to complement rather than replace the specific investment policies of ACERA. It is expected that ACERA's approach to investments, as reflected in its policies and strategies, will be consistent with the Philosophy over time. Though the Philosophy allows significant flexibility, it also raises some constraints or implications. Where these were deemed to be significant, they have been explicitly identified and labeled as *Implications*.

Future Boards may choose to amend the investment Philosophy, as their experiences and circumstances will almost certainly differ. The initial document and any subsequent changes will provide staff, advisors and future trustees with a frame of reference to help them understand how the investment program has evolved as well as the rationale behind its design. Future Boards may modify the Philosophy as their experiences and circumstances suggest is prudent.

The major sections of the Philosophy are:

1. Mission
2. Risk Management
3. Diversification
4. Market Efficiency
5. Organizational Infrastructure and Communications
6. Performance Monitoring and Time Horizon

1. MISSION

a) The Board's primary goals in managing the Fund are:

   i) To ensure that sufficient funds are available to pay vested benefits and maintain supplemental benefits;

ii) To comply with all applicable fiduciary standards; and

iii) To add value, where feasible, that will help reduce the costs of the plan, increase benefits, or both.

2. RISK MANAGEMENT

a) The Board believes that prudent management of risk is a central element of the investment function.

b) Though there are numerous risks involved in the management of a pension investment program, ACERA believes that the following warrant particular attention:

i) ***Funding-related Risk*** - The risk that the funds available in the Plan will be insufficient to pay the promised benefits, both vested and supplemental, or that contribution volatility will be unacceptably high. The primary methods for managing funding risk include regularly conducting integrated asset/liability studies, and establishing appropriate and prudent investment and funding policies.

0.1 In managing the relationship between assets and liabilities, the approved asset allocation of the Fund should provide an adequate level of certainty of meeting the projected liabilities of the Plan over a time period, as determined by the actuary.

ii) ***Benchmark-related Risk*** **–** The risk that the investment benchmarks adopted by the Fund are inappropriate, or that the aggregate of the individual Manager benchmarks within an asset class do not adequately reflect the benchmark for the asset class as a whole. The latter risk is a specific risk generally referred to as *benchmark misfit risk (i.e. style risk)*. Inappropriate benchmarks or excessive benchmark misfit risk could result in investment performance different than expected and could adversely impact decisions concerning the hiring or firing of investment managers.

0.1 The primary methods for effectively managing benchmark-related risk are

(a) regular review of the Fund's benchmarks; and

(b) regular measurement and monitoring of misfit risk using proper methodologies.

iii) ***Manager Risk*** - The risk of aberrant performance on the part of individual investment Managers, and the related active management risk for asset classes as a whole.

0.1 The primary methods for mitigating Manager risk are:

(a) Prudent processes for selecting and monitoring investment Managers;

(b) Competent internal investment Staff;

(c) Effective investment consulting support; and

(d) Clear communication to investment Managers of ACERA's objectives, expectations, and investment time horizons.

0.2 The primary method for mitigating active management risk for asset classes include:

(a) Establishment of appropriate asset class benchmarks;

(b) Careful monitoring of asset class performance relative to the benchmarks; and

(c) Prudent use of passive management.

iv) ***Fortitude Risk*** - The risk that the Board or Staff will fail to exercise the patience, judgment, or fortitude required to support long-term policies and strategies for the investment and funding program.

0.1 The keys to managing fortitude risk are believed to include:

(a) Effective orientation and education with respect to institutional investing and actuarial science; and

(b) A commitment to continually refining, confirming, and communicating the investment philosophy and funding policy of the Association.

3. DIVERSIFICATION

a) ACERA acknowledges the basic tenets of modern portfolio theory, which suggest that diversification, or combining assets that are not perfectly correlated with each other, will reduce the long-term volatility of the overall portfolio.

b) It is generally desirable however to avoid overly complex asset structures, provided the allocation selected can reasonably be expected to meet the objectives of the Plan. ACERA believes that the benefits of diversification must be weighed against the costs

involved, which may include fees, liquidity, complexity, communication, internal staff resources and expertise and trustee knowledge and effort.

c) The following asset classes are appropriate candidates for inclusion in its portfolio:
   i) Domestic equity
   ii) International equity (including emerging markets)
   iii) Fixed income, including high yield fixed income and international fixed income
   iv) Real estate
   v) Private Equity and Alternatives
   vi) Real Return Pool

Implications

- A systematic methodology for re-balancing the investment portfolio is required to ensure proper implementation and adequate risk control concerning ACERA's asset allocation.
- Adding or deleting asset classes or investment Managers should be considered in light of the impact such decisions are likely to have on the general complexity and cost structure of the portfolio, as well as ACERA's ability to prudently achieve its investment and funding goals over the long run.

4. MARKET EFFICIENCY

a) ACERA does not believe in the viability of active management strategies that rely on market timing.

b) ACERA does not believe in the viability of management strategies that call for over weighting or under weighting styles or sectors within an asset class; i.e., benchmark misfit risk will not generate long-term alpha. Accordingly, ACERA generally believes that it should maintain exposures within an asset class (such as style or capitalization weightings) that are consistent with the broad benchmark for the asset class as a whole.

c) ACERA does believe that market efficiency varies among asset classes, creating opportunities for successful active management strategies based on securities selection.

d) Asset classes that can be demonstrated to be efficient should be managed passively in order to reduce active management risk and lower the costs of managing the portfolio.

e) For inefficient asset classes, ACERA believes that it has the ability and a duty to prudently exploit such inefficiencies through active securities selection strategies.

Implications

- ACERA should be conscious of any subtle forms of market timing that may arise in the course of managing the Fund, or that may be implicit in investment strategies presented to ACERA for inclusion in the investment program.

- ACERA must determine appropriate methodologies for determining whether an asset class is efficient or presents appropriate opportunities, thus providing insight to the Board on the use of particular strategies.

5. ORGANIZATIONAL INFRASTRUCTURE AND COMMUNICATIONS

a) ACERA believes that, in order for the investment program to achieve its goals, ACERA must invest the necessary resources to build and maintain an appropriate organizational infrastructure, key elements of which include:

i) A competent, internal investment staff comprised of a sufficient number of investment professionals possessing appropriate leadership, technical, and administrative skills.

0.1 Attracting a competent staff. ACERA recognizes that it competes with the private sector. It must therefore continually strive to create a total work environment that is challenging, rewarding, and competitive.

ii) A strong relationship with outside general investment Consultant(s) who are able to provide ACERA with the following:

0.1 A high degree of investment expertise;
0.2 Innovative and proactive advice and counsel;
0.3 Strong research support; and
0.4 Strong reporting capabilities.

iii) A broad-based information gathering and reporting system to present well-researched, relevant and timely data in a manner that is easily understood and that supports rigorous and consistent monitoring of critical investment activities.

iv) An open channel of communication among the Board, management, and ACERA's external investment professionals.

b) By providing the Board with timely, accurate, and thorough information, the organizational infrastructure will give the Board the high level of comfort it needs to set policy, make investment decisions, oversee the performance of the investment program, and maintain the fortitude necessary to support its investment philosophy, policies, and strategies.

Implications

- ACERA must determine what constitutes an appropriate internal investment staff structure, given the nature of the current investment program.

- ACERA must, over time, take concrete steps toward creating a work environment that will allow the Association to attract and retain needed staff.

- ACERA must recognize that developing the organizational infrastructure it needs – staffing, consulting support, information systems, and communication channels cannot be achieved overnight, but rather will require an ongoing commitment of time and resources.

6. Performance Monitoring and Time Horizon

a) ACERA holds the following basic beliefs concerning performance monitoring practices and methodologies:

i) The various investment policies of the Fund, in the aggregate, are the most important determinants of investment success; compliance with investment policies should, therefore, be monitored rigorously;

ii) The performance of the total portfolio, individual asset classes, and investment Managers should be compared to appropriate, predetermined benchmarks;

iii) Peer comparisons are an additional valid tool in assessing individual Manager performance (supplementing the use of benchmarks), given that ACERA aims to select superior Managers within particular investment styles or mandates. Peer comparisons, or performance rankings, are also valid tools for measuring the performance of asset class portfolios; and

iv) Peer group comparisons may not be an appropriate means of assessing the performance of the total Fund, given that sponsors have different objectives and risk tolerance levels, and therefore may have different asset allocation policies.

v) Benchmark misfit risk, or the risk that the aggregate of individual investment Manager benchmarks in an asset class do not adequately reflect the benchmark for the asset class as a whole, should be explicitly measured on a regular basis.

vi) Investment Managers are generally hired to fulfill a specific role in a portfolio. Accordingly, ACERA believes it is important that ACERA monitor the extent to which Managers comply with their stated style and mandates.

b) ACERA believes that successful funding and investment decisions require a long-term perspective on the part of the Board and management:

i) It is the intention of the Retirement Board that commitments to asset classes and investment strategies should involve long time horizons that may include more than one business cycle (3-5 years each). Relatively illiquid asset classes may require even longer time horizons.

ii) The Board acknowledges that commitments to individual investment Managers also require a long time horizon of at least one business cycle (3-5 years).

iii) ACERA believes that proper reporting and monitoring systems; and clear communication among Consultants, management, investment Managers and the Board will enable the Board to maintain the necessary long term perspective on all investment decisions.

Implications

- Assessing the investment performance relative to appropriate, pre-determined, benchmarks is as applicable to the total portfolio and to individual asset classes as it is for individual investment Managers and, therefore, warrants a commensurate share of the Board's time and attention.

- The Board will spend relatively little time assessing the performance of the Fund relative to that of comparable pension funds.

- ACERA will need either to develop in-house capabilities to measure benchmark-related risk regularly or to purchase such capabilities from external investment Consultants.

- ACERA will monitor all investment Managers to ensure they are complying with their stated investment style, regardless of whether they are performing well or poorly. Strongly performing Managers who are found not to be following their stated styles will be carefully scrutinized and may be subject to disciplinary action.

- ACERA will monitor all investment providers to ensure compliance with ACERA's "General Investment Guidelines, Policies and Procedures."

SCHEDULE VII

CHARTER OF ACERA'S INVESTMENT COMMITTEE OF THE BOARD

To identify issues pertinent to the effective management of the investment portfolio, initiate analysis of such issues by management or consultants, review all policy recommendations by staff and consultants, provide recommendations to the Board for adoption, and oversee the implementation of the investment program. Specific responsibilities include:

1. The Investment Committee shall review recommendations of staff and consultants and in turn provide its own recommendations to the Board on all investment policies, including investment philosophy, requiring Board approval. Said policies shall normally be contained in, or appended to, the *ACERA General Investment Guidelines, Policies and Procedures*.

2. The Investment Committee shall review and recommend additional policies for the Board's approval as requested by the Board and in accordance with the Policy Development Process.

3. The Investment Committee shall review recommendations of staff and consultants and in turn provide its own recommendation for Board approval on the following matters:
   a) Appointment of Investment Managers;
   b) Appointment of the Investment Consultants;
   c) Appointment of the Custodian Bank.

4. The Investment Committee shall monitor the investment program of ACERA in accordance with all relevant policies of the Board. In general, the Investment Committee shall monitor:
   a) Compliance with and continued appropriateness of all ACERA investment policies;
   b) Progress towards achievement of investment goals;
   c) Progress towards implementation of the ACERA budget and Business Plan with respect to investments; and
   d) Cost effectiveness of the ACERA investment program.

5. In accordance with the provisions of the Open Meeting Law, the Investment Committee shall allow adequate opportunity for input from the public and shall respond to such input in a manner that reflects the Committee members' fiduciary duties as trustees of the Plan.

Frequency of Meetings

The Investment Committee shall generally meet monthly on the second Wednesday of the month, but may meet more or less frequently as required.

Committee Composition

The Investment Committee shall be composed of all Board members, one of whom shall serve as Committee Chair. Alternate members shall serve on the Investment Committee as provided by law.

Staff Contact

The Chief Executive Officer shall appoint a staff person to serve as a staff contact to the Investment Committee.

SCHEDULE VIII

ACERA

TABLE OF AMENDMENT DATES

AMENDING RESOLUTIONS

Jun.	27,	1985
Oct.	10,	1985
Jan.	9,	1986
Jan.	16,	1986
Mar.	13,	1986
May.	22,	1986
Sep.	11,	1986
Oct.	9,	1986
Nov.	20,	1986
May.	14,	1987
Aug.	13,	1987
Oct.	8,	1987
Apr.	21,	1988
Jul.	28,	1988
Jan.	29,	1989(4)
Apr.	13,	1989(5)
May.	18,	1989
Jul.	13,	1989
Aug.	10,	1989
Nov.	16,	1989(2)
Jul.	11,	1991
Jun.	11,	1992
Jun.	10,	1993
Jul.	8,	1993
Nov.	18,	1993
May.	14,	1994
Aug.	18,	1994
Nov.	20,	1994
Feb.	16,	1995
May.	18,	1995
Jan.	16,	1997
Aug.	20,	1998
May	20,	1999
Jan.	31,	2000
Apr.	19,	2001
Jul.	18,	2002
Feb.	21,	2003
Feb.	19,	2004
Feb.	17,	2005
Jul.	20,	2006
Jun.	21,	2007
Sep.	18,	2008
May	20,	2013

ADDENDUM

Real Return Pool

I. SCOPE

In April 2011,[15] the ACERA Board of Retirement adopted the establishment of a Real Return Pool Asset Class with a target allocation of 5% of the total Fund. This Addendum is an integral part of the Policy If there is any conflict between this Addendum and the Policy pertaining to investments in the Real Return Pool asset class, this Addendum prevails.

II. DEFINITION

Real Return Pool investments consist of Real Assets that are expected to produce positive returns with a bias toward periods of unexpected U.S. inflation and increasing U.S. inflation expectations. The strategy is implemented using a diverse set of exposures to inflation sensitive instruments, hedges intended to reduce various risk exposures, and active strategies intended to provide additional sources of absolute returns by under- and over-weighting the strategic risk target of the various inflation sensitive instruments and securities. Instruments and securities employed include, but are not limited to, commodity futures and swaps on commodity futures, global exchange-traded equities issued by publicly held corporations in natural resource related sectors, publicly-traded real estate investment trusts ("REITs"), treasury inflation protected securities (TIPS) and currency forwards. It is expected that the Real Return Pool portfolio will also consist of short positions in equity index futures and currency forwards used to hedge partially the equity exposure of the portfolio. Limited leverage and short positions are employed to build certain hedging and long investment positions in the Real Return Pool portfolio. All Real Return Pool investments/strategies are Alternative Investments.

[15] ACERA Investment Committee, April 13, 2011; ACERA Board of Retirement, April 22, 2011.

III. PURPOSE/OBJECTIVE

Real Return Pool investments are principally intended to hedge against inflation, provide significant real returns during periods of unexpected or rising U.S. inflation, and provide long-term protection of purchasing power. Real Return Pool Assets are expected to exhibit low correlations to equity or fixed income assets and thus provide an additional diversifying benefit to the overall ACERA portfolio.

IV. INVESTMENT PARAMETERS/DIVERSIFICATION

The Real Return Pool will invest in a broad, diverse set of inflation-hedging and return-seeking instruments. The Real Return Pool portfolio should generally provide return and risk above bonds but below equity, with generally low correlations to both asset categories.

V. TARGET ALLOCATION

The target allocation to the Real Return Pool Asset Class is 5% of the total Fund.

Class	Target	Range
Commodities	40%	30-50%
Other Inflation Hedging Assets	60%	50-70%

It is expected that the Real Return Pool assets will be managed on a discretionary basis by investment managers under specific investment guidelines which are consistent with the intent of this Addendum.

VI. INVESTMENTS

Real Return Pool investments include, but are not limited to, the following:

1. Commodities
2. Treasury Inflation Protected Securities (TIPS), Inflation Break-evens
3. Developed and Emerging Market Currencies
4. Natural Resources Related Equities
5. Gold, Other Precious Metals
6. Publicly-traded Real Estate Investment Trusts (REIT's)
7. Hard Assets
8. Farmland, Timber
9. Publicly-traded Energy Master Limited Partnerships (MLP's)
10. Infrastructure
11. Other Inflation-Hedging Assets

VII. BENCHMARK

Core Consumer Price Index Plus 300 Basis Points Annualized