

# **Section VI**

# **Investment Policies**

**HOUSTON FIREFIGHTERS' RELIEF & RETIREMENT FUND  
INVESTMENT POLICY STATEMENT**

**INVESTMENT POLICY STATEMENT  
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## **1.0 PURPOSE**

The purpose of this Investment Policy Statement (IPS) is to assist the Board of Trustees (Board) of the Houston Firefighters' Relief and Retirement Fund (Fund) in the investment management of the Fund's assets. The authority to amend these policies and procedures rests solely with the Board. The Investment Committee is a committee of the whole Board and has the authority to act on all matters related to investments.

Nothing contained in this IPS shall be construed as either granting or conferring any rights or remedies upon any third parties with regard to this IPS or otherwise, nor as obligating the Fund to any party in any regard.

## **2.0 GOALS**

The goal of the Fund's investment program shall be to grow the corpus of the Fund's assets while maintaining the ability to pay the benefits promised by the Board to the Fund retirees and beneficiaries. This goal shall be achieved by earning an average annual return over rolling ten-year periods at least equal to the target rate of return which is currently 8.5% net of investment management fees. The Board may adjust the target rate of return when appropriate.

The Investment Committee is responsible for setting the Fund's asset allocation targets, ranges, benchmarks and objectives in accordance with this goal and broader purposes of the investment program.

## **3.0 OBJECTIVES**

In line with the stated goal of the Fund's investment program, the program's primary objective is to generate an aggregate return in excess of the Fund's Policy Benchmark net of investment management fees over a five-year period. The Policy Benchmark is a weighted average of the benchmarks established for each asset class with weights based on target allocations. The Fund's Policy Benchmark is specified in IPS Section 4.0.

The secondary objective of the program is to continually improve the administration, oversight, and Trustee education of the Fund's investment program.

#### 4.0 ASSET ALLOCATION AND BENCHMARKS

The Investment Committee establishes the Fund’s asset allocation targets, ranges, and benchmarks. Below are the asset allocation targets, ranges, and benchmarks as of the latest revision to this IPS.

<u>Asset Class</u>	<u>Range</u>	<u>Target</u>	<u>Benchmark</u>
<u>Market-Based Strategies</u>			
Cash	0.5% - 2%	1%	BofAML 9-12 Mo. US Treasury Index
Domestic Equities	12% - 30%	17%	Russell 3000 Index
International Equities	12% - 30%	17%	MSCI All Country World Ex-US Index
Fixed Income	20% - 35%	30%	Barclays US Aggregate Index
<u>Alternative Strategies</u>			
Hedge Funds	4% – 12%	8%	LIBOR plus 3%
Private Equity	11% - 25%	20%	CA US Private Equity 1QA
Real Estate	4% - 10%	7%	50% NCREIF Property / 50% NCREIF Timberland
<b>Policy Benchmark:</b> Russell 3000 (17%), MSCI AC World Ex-US(17%), BC US Aggregate Index (30%), LIBOR +3% (8%), CA US Private Equity Index (20%), NCREIF 50% Timberland/ 50% Property (7%), BofAML 9-12 Mo. US Treasury Index (1%)			

When necessary (usually appropriate every three to five years) the Investment Committee will undertake a comprehensive review of the Fund’s asset allocation targets and ranges. This may involve an asset-liability study that places the development of investment policy into the context of future benefit payments, liabilities, required funding and the prospective funded status of liabilities.

#### 5.0 ASSET ALLOCATION AND REBALANCING

##### A) Public Market Rebalancing

The Investment Committee has allocated the assets of the Fund to several asset classes with the objective of optimizing the investment return of the Fund within the framework of acceptable risk and diversification. Each asset class is allowed to operate within its specific

range established by the Investment Committee. In addition, a target allocation has been established for each asset class for the purpose of performance evaluation and rebalancing. If a public, non-cash asset class reaches an endpoint of its allocation range; the Chief Investment Officer (CIO), with the approval of the Chairman is allowed the discretion to effect a rebalance to within 2.5% of the target allocation. Upon completion, the CIO shall report the rebalance to the Investment Committee within the next Monthly Report of Investment Actions Taken.

#### B) Cash Management

The CIO with the Chairman's approval is allowed the discretion to use the public markets portfolio, excluding Alternatives, to manage the cash level within the established asset class range set forth in Section 4.0. If the cash balance rises/falls above/below the asset class range limit or if there is expected to be a near-term large cash outflow, the short-intermediate bond, the Russell 3000 Index and, MSCI AWC xUS Index, and the MSCI EM Stock Index will be bought/sold (after any index rebalancing considerations) to rebalance cash. Upon completion, the CIO shall report the transaction to the Investment Committee within the next Monthly Report of Investment Actions Taken.

### **6.0 RISK MANAGEMENT**

The Fund ensures adequate risk control through the following means:

#### A) Diversification

The Investment Committee shall diversify the investment portfolio in order to minimize the impact of the loss from individual investments as may be relevant to an asset class. In addition to achieving diversification by asset class, the Investment Committee shall pay careful attention to diversification within each asset category and subcategory.

#### B) Portfolio Guidelines

Every portfolio that is a part of the Fund's overall investment portfolio shall operate under written guidelines (IPS Section 9.0 B) approved by the Investment Committee, which are designed to ensure that the portfolio meets its objective and operates within acceptable risk parameters.

### **7.0 PORTFOLIO PERFORMANCE MEASUREMENTS**

The reported investment performance of the Fund will be calculated by the Fund's custodian bank, an unaffiliated organization, with recognized expertise in this field and fiduciary level reporting responsibility to the Fund's Investment Committee. A calculation will be made for the Fund's aggregate, asset class, and investment manager performance using the Global Investment Performance Standards (GIPS®) or a similar standard. Additionally, each investment manager is required to keep performance records and report periodically to the Fund's custodian, internal investment staff, and third-party auditor.

Separately, internal calculations of the Fund's investment manager performance shall be developed by the Fund's investment staff. A time-weighted rate of return calculation shall be

used for all Market-Based Strategies and Hedge Funds. Private Equity and Real Estate investments shall be calculated using an internal rate of return.

The fiscal year of the Fund shall begin on July 1st and end on June 30th. The market value of the Fund shall be maintained on an accrual basis in compliance with Government Accounting Standards Board Statements, industry guidelines, state statutes, or whichever is applicable. The Fund's financial statements and investment returns shall be audited each fiscal year-end by an independent accounting firm in accordance with the Fund's Administrative Policies.

## **8.0 INVESTMENT PHILOSOPHY**

In developing the investment program, the Investment Committee is guided by a set of precepts from which all investment decisions are made and establishes the foundation and direction for all future activity. These precepts are applied by the Investment Committee, knowing the importance of asset allocation and the benefits of diversification. These guiding precepts are as follows:

- A) Long-term Focused - The Investment Committee recognizes the long-term (perpetual) nature of the Fund's liabilities and an appropriate investment program should have long-term assets and strategies, generally assumed to target a ten-year planning horizon.
- B) Value-Driven - The Investment Committee shows preference in buying lower-priced out-of-favor assets as a less risky approach to investment management, but may maintain exposure to growth strategies to enhance portfolio diversification.
- C) Relationship-Driven - The Investment Committee believes significant non-quantifiable benefits accrue to the Fund by fostering successful long-term relationships.
- D) Opportunistic - The Investment Committee can react with flexibility and agility to take advantage of investments which have a short decision time but exhibit an above-market opportunity, so long as proper due diligence is completed.
- E) Contrarian - The Investment Committee is willing to be different from other investors by considering investments, which are unconventional or may not be the current consensus thinking as long as the investment opportunity meets the previously mentioned guiding precepts.
- F) Active Management – The Investment Committee has adopted a predominately active manager based philosophy in the belief that over a long-term horizon active management in certain asset classes will provide excess risk-adjusted performance over passive strategies

## **9.0 MANAGER SELECTION, GUIDELINES, RETENTION, AND REVIEW**

To assist the Investment Committee in the investment management of the Fund's assets, professional investment managers will be retained to implement the strategies selected by the Investment Committee. This IPS section describes generally the manager screening and selection process (due diligence), the guidelines applicable to managers hired by the Fund, and the review and retention procedures for managers retained by the Investment Committee.

### **A) Manager Selection**

The appropriateness of seeking a new or replacement investment manager will be determined by the Fund's most current investment strategy, philosophy, asset class ranges, capital availability or the need to replace an existing manager in accordance with Section 9.0 C of this IPS.

The investment staff with input from the Investment Committee shall use a disciplined due diligence process to screen and select managers consistent with the asset class placement under consideration. The Fund's investment staff shall develop and keep written records of the internal due diligence process. Additionally, the investment staff shall update and educate the Investment Committee of any changes to the process each time the Investment Committee engages in a manager search and selection.

No manager shall be given consideration by the Investment Committee until/unless the manager has been placed through the Fund's formal due diligence process. The Investment Committee or the Chief Investment Officer may engage an external consultant to assist with a search. The CIO shall report the use of an external consultant to the Investment Committee within the next Monthly Report of Investment Actions Taken. All new or replacement investment managers must be approved by the Investment Committee along with funding/commitment level subject to conclusion of any further appropriate negotiations or discovery

### **B) Manager Guidelines**

Manager guidelines include general guidelines applicable to all managers and specific guidelines unique to each manager. The CIO shall report any manager guideline violations to the Investment Committee within the next Monthly Report of Investment Actions Taken or via specific report during the earliest possible Investment Committee meeting.

#### **1) Public Market Investments**

- a. The specific guidelines along with contractual requirements for each manager will be developed cooperatively by the Fund's investment staff, legal counsel, and the investment manager and shall be incorporated into an Investment Management Agreement or other binding agreement as is appropriate for the investment.
- b. In case of conflict between the specific manager guidelines and the general guidelines, the specific guidelines, as approved by the Investment



Committee, shall supersede. The general guidelines are as follows:

- i. Manager investment philosophy, style, strategy, and structure shall remain consistent and shall not change without the Investment Committee's approval. The manager shall have discretion to manage the portfolio consistent with the style presented to the Investment Committee at the time of selection and further subject to the restrictions established by the policy herein.
- ii. The following transactions are prohibited: short sales, selling on margin, put and call options and the use of derivatives for speculation unless authorized by the Investment Committee.
- iii. Transactions that involve a broker acting as a principal, where such broker is also affiliated with the manager who is making the transaction are prohibited, unless specifically approved by the Investment Committee.
- iv. Transactions shall be executed at competitive costs or best execution.
- v. Managers shall maintain cash levels consistent with their style as presented to the Investment Committee at the time of selection. Any deviation shall be allowed only after notifying the CIO and should be related to unusual market conditions. The maximum cash level to be held by each manager will be addressed in the Investment Management Agreement or other binding agreement as is appropriate for the investment.

2) Private Market and Alternative Investments

- a. The investment specific guidelines for each manager will be incorporated in a Limited Partnership Agreement, Limited Liability Company Agreement, or other binding agreement as is appropriate for the investment.
- b. In case of conflict between the specific manager guidelines and the general guidelines, the specific guidelines, as approved by the Investment Committee, shall supersede. The general guidelines are as follows: Manager investment philosophy, style and strategy shall remain consistent and shall not change without the Investment Committee's approval. The manager shall have discretion to manage the portfolio consistent with the style presented to the Investment Committee at the time of selection and further subject to the restrictions established by the policy herein.

C) Manager Retention

Upon selection of a manager for placement of Fund assets, the Investment Committee's intent, according to the relationship-driven precept detailed in Section 8.0 of this IPS, is to develop and maintain a successful long-term relationship with the manager.

1) Public Market and Alternative Investments

The Investment Committee with assistance from the investment staff shall review each manager's performance and adherence to style, strategy, and manager-specific

guidelines. It is the Investment Committee's discretion to take corrective action by replacing a manager if they deem it appropriate at any time. Quantitative and qualitative performance measures shall be monitored as are appropriate to each investment. The CIO, with the assistance of the Investment staff shall conduct comprehensive monitoring and assessment of all the managers on regular basis and report all public market managers performance summary, including risk adjusted performance statistics, contribution to risk, contribution to returns and other relevant factors.

a. Manager Termination

The CIO may recommend, to the Investment Committee that to be prudent and consistent with the terms of the applicable agreement and the Fund's Goals and Objectives a manager be replaced or terminated. No manager shall be terminated without the formal approval of the Investment Committee. The CIO recommendation and justification for the termination may be based on any of the following reasons:

- i. Changes in key staff of the manager
- ii. Organizational changes of the manager (including changes in ownership or legal structure);
- iii. Non-compliance with investment guidelines or other contract requirements;
- iv. Issues with SEC compliance, regulatory, legal, reputational and ethical issues, or litigation;
- v. Change in investment style, strategy, or process;
- vi. Long term net of fee risk adjusted and / or nominal under performance;
- vii. Adjustment in portfolio construction;
- viii. Client service and reporting issues;
- ix. Performance that is highly unusual or outside expectations;
- x. Further retention of the manager does not advance the interests of the Fund's investment program.

2) Private Market Investments

The Investment Committee with assistance from the investment staff shall review each Private Equity and Real Estate manager's performance and adherence to strategy and manager specific guidelines. Quantitative and qualitative performance measures shall be monitored as are appropriate to each investment.

Private Equity and Real Estate investment manager retention, to the extent applicable is governed in most cases by Limited Partnership Agreements, Limited Liability Company Agreements, or other binding agreements. As such, retention/termination actions may not be available to the Fund. However, to the extent that discretion is available, the Investment Committee may take corrective action by removing, replacing, or terminating a manager, or the investment, as applicable.

D) **Manager Review**

Investment staff shall meet with Fund investment manager's on regular basis. The meetings may take place at a posted Investment Committee Meeting, at the Fund office, at the investment manager's office, by phone call or at the designated location of an investment manager's sponsored portfolio review.

For all meetings with staff outside an Investment Committee meeting, any written report shall be maintained by the Investments Department.

Any manager may be requested to make a presentation to the Investment Committee as deemed appropriate by the CIO or the Investment Committee.

**10.0 INTERNAL REPORTING**

The CIO coordinates the preparation of reports of the investment performance of the Fund. At a minimum the following formal periodic reports to the Investment Committee shall be the responsibility of the CIO:

- A) Annual report of the Fund's aggregate, asset class, and investment manager investment performance calculated as described in Section 7.0 of this IPS
- B) Consolidated Quarterly Report - line item of each mandate's investment performance and cash flow activity including fees and expenses if applicable
- C) Quarterly Trust Universe Comparisons Services (TUCS) Report as prepared by Wilshire
- D) Monthly Asset Allocation Report
- E) Monthly Report of Investment Actions Taken
- F) Chief Investment Officer's Monthly Report
- G) Senior Investment Officer's Monthly Report

## 11.0 OPERATIONAL PROCEDURES

### A) Signatures

The signature of all agreements, amendments, consents, and letters of instruction shall be in accordance with the Fund's Policies and Procedures Manual Administrative Policies Section 1.0. Unless clearly ancillary, consequent, or otherwise in furtherance of an existing or approved investment, no investment agreements shall be executed on behalf of the Fund without formal approval by the Investment Committee.

### B) Amendments and consents

With the recommendation of the CIO, the Chairman may execute amendments, consents, extensions, and ancillary documents related to existing investments or those already approved by the Investment Committee without the approval of the Investment Committee if the resulting changes or allowances do not constitute additional investment or capital committed and (i) are provided for in the governing documents as previously approved by the Investment Committee or HFRRF or (ii) if the CIO reasonably believes that such action would have no adverse economic impact on the investment.

The investment staff shall notify the Investment Committee of all actions taken within the next Monthly Report of Investment Actions Taken. If the Committee does not vote to reverse the action (where possible), the Committee shall be deemed to have ratified the action.

Any other amendments, consents, or other such changes are to be formally approved by the Investment Committee.

As a matter of clarification, in those situations in which the Fund (or an employee of the Fund) holds a position on the advisory board or similar body of a Private Equity or Real Estate investment, the appropriate staff member(s) as identified by the Fund's CIO may provide consents, votes, etc. as may be required or appropriate of an advisory board member. Any matter put before such an advisory board that could be expected to result in action taken by the investment manager that in turn could reasonably be expected to materially adversely affect the economic interests of the Fund shall be reported to the Investment Committee at the next Investment Committee meeting.

### C) Communications of Intent

No representative of the Fund (Board or staff) shall represent, written or otherwise, that an investment will be made or an approval of the Investment Committee will be given, without the formal approval of the Investment Committee, which is subject to Section 9.0 A of this IPS.

### D) Distributions from Private Equity or Real Estate Investments

Asset and/or foreign currency distributions from Private Equity or Real Estate Investments with a market value less than 0.25% of total Fund assets may be liquidated

by the CIO, with written approval of the Chairman. Since the Investment Committee views these assets as a return from the Private Equity or Real Estate investment and does not intend to contribute these assets to other asset class managers, these assets should be liquidated in a prudent and timely manner. Furthermore, since the Investment Committee does not actively manage currency internally and does not intend to contribute foreign currencies to the international equity allocation, these positions should also be liquidated in a prudent and timely manner. The CIO may defer immediate liquidation if specific knowledge provides a reasonable expectation of value improvement through a longer holding period. The investment staff shall notify the Investment Committee of all actions taken within the next Monthly Report of Investment Actions Taken.

E) Securities Lending

The Investment Committee has engaged in the lending of the Fund securities for the purpose of generating income from the investment of the related collateral. The income is divided between the Fund and the securities lending agent. The investment staff monitors the program and ensures that the lending income is split in accordance with the negotiated rate between the Fund and the securities lending agent.

F) Commission Recapture

The Investment Committee has implemented a brokerage commission recapture program for the purpose of lowering the Fund's transactions costs. The investment staff monitors the program and ensures that the recaptured income is directed into the manager's account according to the commissions generated and the recapture rate negotiated with the brokers used by the manager.

## 12.0 GOVERNANCE

The Fund acknowledges the importance and significance of adhering to the Exclusive Benefit Rule as expressed in 401(a) of the Internal Revenue Code of 1986, Chapter 16, Section 67, of the Constitution of the State of Texas and Chapter 802 of the Texas Government Code.

The primary responsibility of the Fund fiduciaries is to run the plan solely in the interest of participants and beneficiaries and for the **exclusive** purpose of providing benefits and paying plan expenses. Fiduciaries must act prudently and must diversify the Fund's investments in order to minimize the risk of losses. Fiduciaries also must avoid conflicts of interest. In other words, they may not engage in transactions on behalf of the Fund for the purpose of benefiting parties whether related or unrelated to the Fund, such as other fiduciaries, themselves (other than as part of the whole body of plan participants and beneficiaries), service providers, special interest groups, or the plan sponsor.

For the purpose of this IPS, the Exclusive Benefit Rule is met if the following conditions are satisfied:

- A) The investment is to fulfill a specific investment strategy need or to replace a planned or recent termination of a current mandate.
- B) The investment provides the Fund with an equivalent or superior rate of return for a similar investment with a similar time horizon and similar risk.
- C) The investment management fees do not exceed industry standard at the time of investment
- D) The investment meets all the typical criteria for investment as defined within this IPS.

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