THE PUBLIC EMPLOYEES RETIREMENT ASSOCIATION of NEW MEXICO

Public Employees
Retirement Association
of New Mexico

INVESTMENT POLICY

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THE PUBLIC EMPLOYEES RETIREMENT ASSOCIATION

INVESTMENT POLICY

I. INTRODUCTION

A. Statutory Authority

The Public Employees Retirement Association of New Mexico (PERA), created by law in 1947, is the entity established for the purpose of administering the provisions of the Public Employees Retirement Act of New Mexico, NMSA 1978, Sections 10-11-1 to 10-11-142, as amended, the Volunteer Firefighters Retirement Act, NMSA 1978, Sections 10-11A-1 to 10-11A-7, as amended, the Judicial Retirement Act, NMSA 1978, Sections 10-12B-1 to 10-12B-19, as amended, the Magistrate Retirement Act, NMSA 1978, Sections 10-12C-1 to 10-12C-18, as amended, and the Public Employees Reciprocity Act, NMSA 1978, Sections 10-13A-1 to 10-13A-4, Section 10-11-133.1, as amended, as well as other federal and State laws relating to the public employees retirement system in the State of New Mexico. As of March 2010, PERA administers thirty-one retirement plans covering state employees, municipal employees, county employees, police, firefighters, judges, magistrates, and legislators.

B. Standards of Care

Uniform Prudent Investor Act

The Uniform Prudent Investor Act (UPIA) [45-7-601 to 45-7-612 NMSA 1978] and Section 10-11-132 NMSA, 1978 govern NM PERA investments. In summary, the UPIA states that all persons responsible in making investment decisions for the Public Employees Retirement Fund (Fund) shall exercise the care, skill, prudence and diligence under the circumstances then prevailing that a prudent investor acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims. Investments are to be diversified so as to minimize the risk of large losses, unless under the circumstances, it is clearly prudent not to do so.

The statutes are the foundation for the PERA Policy. The Board adopts the following guiding principles for investment activity:

1. Preserve the long-term principal of the Fund.
2. Maximize total return within prudent risk parameters.
3. Act in the exclusive interest of PERA members, retirees and beneficiaries.

C. Ethics and Conflicts of Interest

Trustees and Staff involved in the investment process shall refrain from personal business activity that could conflict with the proper execution and management of the investment program, or that could impair their ability to make impartial decisions as addressed in Section III of the Board Policy and Procedures.

II. STATEMENT OF PURPOSE

A. Mission Statement

Public Employees Retirement Association of New Mexico (PERA) is governed by the Public Employees Retirement Board (Board). The Board has a fiduciary responsibility to the Retirement Fund's (Fund) members, retirees and beneficiaries. To acknowledge this responsibility, the Board has accepted the following as their Mission Statement:

The mission of the Board of the Public Employees Retirement Association is to preserve, protect, and administer the trust to meet its current and future obligations and provide quality services to Association members.

B. Purpose of the Investment Policy

The purpose of the Investment Policy (Policy) is to delineate the investment philosophy, objectives, guidelines and practices of PERA and has been developed as a reference point for the management of PERA's assets. The Policy is intended to capture investment opportunities while providing parameters that ensure prudence and care in the execution of the investment program. No investment or action pursuant to an investment may be taken unless permitted by this Policy or by action of the Board. Deviation from this Policy is not permitted without explicit written permission from the Board.

The Policy provides guidance for fiduciaries which include PERA's Board, Staff, investment consultants, investment managers, and custodians. It is the intent of the Policy to provide the foundation for management of the PERA's assets in a prudent manner including the standards and disciplines by which the Board can evaluate of Staff, investment consultants, investment managers and custodians.

III. INVESTMENT PHILOSOPHY

A. Primary Objective

The Fund's primary objective is to prudently invest assets in order to meet statutory obligations to its members. The Funds' assets will be managed in a manner that reflects both the Funds' unique liabilities and funding resources, incorporating accepted investment theory, prudent levels of risk and reliable, empirical evidence. Specifically, the Board has adopted the following principles:

- Strategic asset allocation is the most significant factor influencing long-term investment performance and asset volatility. The asset allocation targets adopted by the Board shall adhere to the guidelines contained in this Policy.

- Risk is an unavoidable component of investing and is a major factor that shall be taken into account in assessing investment policy and strategy. In evaluating specific investments, both the risks associated with that investment as well as the impact of the investment to the overall portfolio shall be considered.

- Diversification both by and within asset classes is the Fund's primary risk control element. Other risk control measures shall be implemented where appropriate.

- The Fund's liabilities are long term and the investment strategy must therefore be long-term in nature.

- Sufficient liquidity will be maintained to meet the anticipated cash flow requirements of the Fund.

B. Return

In order to meet the Fund's objective, the Board strives to achieve the highest level of investment performance that is compatible with its risk tolerance and prudent investment practices. Due to the long-term nature of the PERA's pension obligations and the inherent risks in short-term tactical investing, the Board must maintain a long-term perspective in formulating and implementing its investment policies, and in evaluating its investment performance. As such, the Board: (1) seeks to adopt a long-term rate of return goal commensurate with the actuarial assumed rate of return, (2) adopts an allocation policy that seeks to meet the rate of return goal over long periods of time, while minimizing volatility (risk) and (3) strives to minimize the costs associated with implementation of the asset allocation through efficient use of internal and/or external resources.

Investment performance is measured by three integrated long-term objectives in the following order of importance:

1. The actuarial assumed target rate of return is the key actuarial assumption affecting future funding rates and payment of pension obligations. Investment performance that exceeds or underperforms the target rate may materially impact future funding rates. The Board seeks to have long term investment performance that will reasonably exceed its actuarial assumed rate of return.

2. The Policy benchmark is calculated by applying the investment performance of the asset class benchmarks to the Fund's asset allocation targets. The Policy benchmark permits the Board to compare the Fund's actual performance to a total fund benchmark *(Section VII. A. Performance Benchmarks, Total Fund Benchmark)* and to measure the contribution of active investment management and policy adherence.

3. While the Board recognizes that other funds may have investment objectives and risk tolerances that differ substantially from PERA's, the Board will compare its total fund performance to appropriate public plan sponsor comparison universes. A universe comparison permits the Board to compare its performance to large statewide public and other pension plans.

C. Risk

The investment risk philosophy for the Fund is based on the precepts of capital market theory that are generally accepted and followed by institutional investors, who by definition are long-term oriented investors. This philosophy holds that:

1. Increasing risk is rewarded with compensating returns over time and, therefore, prudent risk taking is a necessary element of long term investing.

2. Risk can be mitigated through diversification of asset classes and investment approaches, as well as diversification of individual securities.

3. The primary determinant of long-term investment performance is the strategic or long-term allocation of assets among various asset classes.

4. Relative performance of various asset classes is unpredictable in the short term and attempts to shift tactically between asset classes or implementation strategies are unlikely to be rewarded.

Given these principles, the Board has established a long-term asset allocation policy that balances the returns intended to fund PERA's objectives and the risk level that is appropriate under existing and anticipated circumstances. In determining the returns sought, the Board takes into account the benefit levels and structure of the plans supported by the Fund. The Board will periodically conduct an asset/liability study to determine the extent to which the long-term asset allocation is consistent with the liabilities of the retirement plans. In determining what the Board believes is a prudent level of risk assumed in pursuit of those returns, the Board will consider total fund risk, the Fund's expected volatility, liquidity, and general sensitivity to the overall asset allocation and to equity, bond and other major assets classes utilized by the Fund. The Board will regularly measure and monitor Fund risks in its management of the Fund.

Investments shall be made to preserve and protect the long term investment results and benefits of the Fund.

D. Diversification

In order to achieve the actuarial assumed rate of return, the Board will rely on an investment strategy utilizing an appropriate long-term, diversified asset allocation model. Diversification distributes a portfolio across many investments to avoid excessive exposure to any one source of risk. Investors generally diversify their portfolios along the following lines: asset classifications (stocks, bonds, real estate, real assets, hedge funds. private equity, short-term investments, etc.), geography, industries, and maturity sectors. Other considerations in asset allocation modeling should take into account the purpose of the Fund, the size and financial condition of the Fund, and general business conditions. The factors mentioned here are not intended to be limiting; rather, they are outlined as a general indication of the importance of diversification to proper asset allocation. Under such an allocation, PERA's assets may be invested by some combination of active and passive managers. The Board will determine the proper allocation among asset classes and investment managers, based on advice and analysis provided by Staff and/or Consultants.

IV. ROLES AND RESPONSIBILITIES / DELEGATION OF AUTHORITY

The Board relies on both internal Staff and external contractors in order to properly administer the Fund and implement its investment strategies. Because of the number of parties involved, their roles as fiduciaries must be clearly identified. Such identification increases operational efficiency, ensures clear lines of responsibility, and reduces or eliminates duplication of effort.

A. Board of Trustees

The primary fiduciary responsibility of the Board is to ensure prudent investment and expenditure of the Fund's assets. It is the responsibility of the Board to administer the investments of PERA at reasonable cost, being careful to avoid diminishing quality. These costs include, but are not limited to, management and custodial fees, consulting fees, transaction costs and other administrative costs chargeable to PERA. The Board shall operate the investment program in compliance with all applicable federal and State laws and regulations concerning the investment of pension assets. The Board is responsible for establishing and maintaining all policies and guidelines by which the Fund is managed, and by which the Board operates. The Board shall meet to execute its duties on a quarterly basis or more frequently if appropriate.

B. Investment Committee

To assist the Board in carrying out its duties, it has established an Investment Committee (Committee).

Through New Mexico Administrative Code Rules (NMAC), the Board establishes the Committee and the Board Chair appoints the members of the Committee as well as the Committee Chair. The Committee makes recommendations to the Board on investment actions including, but not limited to: all Board approved policies related to the investment program including investment policy, re-balancing, and manager hiring, monitoring and termination; asset allocation targets and ranges; asset class structure; performance benchmarks; securities lending program; commission recapture and trade cost analysis; investment manager relationships; and consulting relationships.

The Committee meets prior to the regular meeting of the Board to address overall investment activities. Staff and Consultant(s) brief the Committee on any topics or issues pertinent to PERA's investment operations, and make recommendations to the Committee for appropriate courses of action. The Committee Chair shall have the duty and the authority to set Committee meeting agenda and request specific analysis and reports from the Staff and Consultants.

C. Executive Director

The Executive Director (Director) is appointed by, and serves at the pleasure of the Board. The Director is responsible for planning, organizing, and administering the operations of PERA under broad policy guidance and direction from the Board. The Director, with assistance of Staff (his/her designee), monitors the performance of the investment portfolio; ensures that funds are invested in accordance with Board policies; communicates with the Board, its Officers and Committee Chairs; studies, recommends, and implements policy and operational procedures that will enhance the investment program of PERA; and ensures that proper internal controls are developed to safeguard the assets of PERA. In fulfilling these investment responsibilities, the Director relies heavily on the Investment Staff and Consultant(s).

D. Chief Investment Officer and Investment Staff

The Internal Investment Staff (Staff) reports directly to the Chief Investment Officer (CIO) who in turn reports to the Director. The CIO has primary responsibility for the implementation of the investment program. The CIO, with the assistance of Staff, has the responsibility and authority to assist the Board and its committees in establishing investment and administrative policy, to implement the policies and programs established by the Board, to report to the Board and Legislature on the status of the Fund and the operations of PERA, and to carry out such other duties the Board or Committee shall delegate to him/her.

The Staff exercises the same fiduciary responsibility under applicable law as the Board. The CIO and the Staff shall manage the portfolio according to the Board's policies, advise and inform the Board about investments, assist with development and review of investment policies and procedures, report on the progress of the Fund in meeting its investment objectives, and compare the performance of the portfolio to established benchmarks.

E. General Counsel and Office of General Counsel Staff

The internal Office of General Counsel staff (OGC staff) reports directly to the General Counsel who in turn reports directly to the Director. The General Counsel is primarily responsible for legal compliance of the investment program and advises the Board on investment-related legal matters. The General Counsel, with the assistance of OGC staff, coordinates legal due diligence by external legal counsel for alternative investments, including transactional, regulatory and federal tax matters. OGC staff exercise the same fiduciary responsibility under applicable law as the Board.

F. Investment Consultant(s)

The Consultant(s) is hired by the Board, reports directly to the Board and is directly accountable to the Board. The Board may elect to retain one or more Consultants that specialize in specific areas of asset consulting. Investment Consultants agree to indemnify PERA as fiduciaries as provided in their Professional Services Agreement and will discharge their duties with respect to this Fund solely in the interest of the PERA membership and benefit recipients with the care, skill, prudence, and diligence under the circumstances then prevailing.

The Consultant's duty is to work with the Board, Committee and its Chair, and Staff in the management of the investment process. This includes regular meetings with the Board to provide an independent perspective on the Fund's goals, structure, performance and managers. In the course of the Consultant's normal functions, the Consultant will work directly with the Staff to review asset allocations and performance, and make recommendations to the Board as appropriate. The Consultant will assist Staff and the Committee with external investment manager selection and will promptly inform PERA and discuss the impact of material changes taking place within any current Manager's organization or investment process.

Relative to alternative investments, the Board may utilize the Consultant as a gatekeeper with discretionary authority and fiduciary responsibility for due diligence and investment recommendations.

G. External Investment Managers

The external Investment Managers (Managers) are selected by, and serve at the pleasure of, the Board. Each investment manager shall be a registered adviser under the Investment Advisers Act of 1940 (or appropriately exempt from registration) and operate under a formal contract that sets investment guidelines and administrative requirements and defines responsibilities and performance expectations for management of each mandate. Full discretion, consistent with this policy and contractual guidelines, is granted to all investment managers. Managers will provide performance reporting to the Staff utilizing standardized reporting formats and at intervals specified by Staff.

H. External Legal Counsel

Outside Legal Counsel agree to indemnify PERA as fiduciaries as provided in their Professional Services Agreement and discharge their duties with respect to this fund solely in the interests of the PERA membership and benefit recipients with the care, skill, prudence and diligence under the circumstances prevailing. Qualified Legal Counsel include those professionals with the background, expertise and demonstrated success as legal counsel for public funds and large institutional clients regarding alternative investments, including, but not limited to, private equity, hedge funds, real estate and real assets.

V. ASSET ALLOCATION

A. Strategic Asset Allocation Targets

The Board recognizes that over the long-term, asset allocation is the single greatest determinant of return and risk to the Fund. The Fund's asset allocation policy is intended to reflect, and be consistent with, the return objective and risk tolerance expressed in this Policy. It is designed to provide the highest probability of meeting or exceeding the Fund's objectives at a controlled level of risk that is acceptable to the Board. In establishing its risk tolerance, the Board will consider its ability to withstand short- and intermediate-term volatility in investment performance and fluctuations in financial condition of the Fund. In determining the appropriate strategic allocation among these asset classes, the Board, with assistance from Staff and Consultants will examine the historical and projected risk and return of the approved asset classes as well as the correlation among these asset classes. The Board will also consider the expected effect of investment performance on the obligations of the Fund. Based on its determination of the appropriate risk tolerance for PERA, and its long-term return expectations, the Board has chosen the following Strategic Asset Allocation Target:

Asset Class	Strategic Asset Allocation Target
Domestic Equity	27.0%
International Equity	27.0%
Fixed Income	26.0%
Private Equity	5.0%
Absolute Return	9.0%
Real Estate	3.0%
Real Assets	3.0%

The target allocation will be reviewed annually for reasonableness relative to significant economic and market changes or to changes in the Fund's long-term goals and objectives. A formal asset allocation study should be conducted at least every three years to verify or amend the targets. Recognizing that the long-term target allocation to alternative asset classes may take several years to implement prudently, the Board will work with Staff and Consultants to set interim asset allocation targets and alternative asset funding guidelines to be utilized until the alternative asset classes are fully funded.

B. Re-Balancing Strategy

Re-balancing is the term that describes the periodic movement of funds from one asset or asset class to another for the purpose of realigning the assets with the asset allocation target. A re-balancing strategy is an important element of asset allocation policy.

The Board has chosen to adopt a re-balancing policy that is governed by allocation ranges rather than time periods. Upper and lower allocation limits have been established for each asset class. The ranges, specified in the table below, are a function of the volatility of each asset class and the proportion of the total fund allocated to the asset class. Staff reviews the Fund's allocation on an ongoing basis. When the allocation to all asset classes remains within these limits, Staff will use cash flow to maintain the overall allocation as close as possible to the target.

Strategic Asset Allocation and Re-Balancing Ranges

Asset Class	Lower Limit	Strategic Asset Allocation Target	Upper Limit
Domestic Equity	22.0%	27.0%	32.0%
International Equity	22.0%	27.0%	32.0%
Fixed Income	23.0%	26.0%	29.0%
Private Equity	3.0%	5.0%	7.0%
Absolute Return	7.0%	9.0%	11.0%
Real Estate	1.0%	3.0%	5.0%
Real Assets	1.0%	3.0%	5.0%

When any one of the public market asset classes breaches an upper or lower limit, the asset class will be re-balanced to within its strategic asset allocation target range within ninety (90) days. Recognizing that it may be impractical or costly to reallocate illiquid alternative assets, if an alternative asset class breaches an upper or lower limit, the asset class will be re-balanced to within its strategic asset allocation range as soon as is practically possible, subject to reasonable transaction costs. The Board has authorized the CIO and Staff to re-balance the portfolio in accordance with policy guidelines on an on-going basis. The goal in implementing the re-balancing policy is to minimize transaction costs, market impact, and opportunity costs. Staff will prioritize the re-balancing strategies and methods employed based on the circumstances at the time, and Staff will report the results of re-balancing activity to the Committee and the Board at the next regular meeting. Staff will review the current and target allocations with the Committee and Board on a monthly basis.

The Board reserves to itself the authority to suspend or otherwise delay its basic re-balancing policy. Such action shall require approval by a majority of the Board members present at the time of the voting and must be reaffirmed via the same process quarterly. Absent reaffirmation, the Board's re-balancing policy will be automatically reinstated.

VI. PERFORMANCE BENCHMARKS

A. Total Fund Benchmark

As stated in *Section III. Investment Objectives*, an important return objective to be considered when evaluating the Fund's performance is measured by applying the investment performance of the asset class benchmarks to the Fund's Strategic Asset Allocation target (Policy Index). The Policy Index permits the Board to compare the Fund's actual performance to its total fund benchmark, and to measure the contribution of active investment management and policy adherence.

The Board has selected the following Policy Index:

Asset Class	Policy Index	Strategic Asset Allocation Target
Domestic Equity	Russell 3000 Index	27.0%
International Equity	MSCI All Country Ex US Index	27.0%
Fixed Income	Barclay Capital Aggregate Index	26.0%
Private Equity [1]	Actual Private Equity Performance through 2014, Venture Economics Pooled IRR thereafter	5.0%
Absolute Return[2]	HFRI Fund-of-Funds Index	9.0%
Real Estate	75% NCREIF Property Index +3%, 25% NAREIT	3.0%
Real Assets [3]	75% Cliffwater Private Energy Index, 25% S&P GSCI Light Energy Index	3.0%

[1]The Russell 3000 Index + 3% is also an appropriate long-term benchmark.
[2]LIBOR + 4% is also an appropriate long-term benchmark
[3]CPI + 6% is also an appropriate long-term benchmark. The Cliffwater Private Energy Index is a peer universe of private energy funds.

Recognizing that a long-term target allocation to alternative asset classes can often take a matter of years to implement prudently, the Board will also review an Interim Policy benchmark which will be adjusted as PERA makes progress towards its long-term strategic asset allocation target.

B. Mandate-Level Benchmarks

Individual managers will be evaluated using the following standards:

1. Against appropriate market indices on a nominal and risk-adjusted basis;
2. Against peers within their style group;
3. Based on adherence to their stated investment philosophy and style; and
4. Based on adherence to this Policy and the guidelines established in their contract.

Specific performance criteria for each sub-asset class are outlined as follows. Not all sub-asset classes will necessarily be in place at one time and exceptions may apply to the benchmarks stated below as detailed in the investment manager's PSA:

Sub-Asset Class	Index	Peer Universe
Domestic Large Cap Value Equity	Russell 1000 Value Index	US Value Large Cap Equity
Domestic Large Cap Core Equity	Russell 1000 Index	US Core Large Cap Equity
Domestic Large Cap Growth Equity	Russell 1000 Growth Index	US Growth Large Cap Equity
Portable Alpha	S&P 500 Index	US Large Cap Core Equity
Domestic Mid Cap Value Equity	Russell Mid Cap Value Index	US Value Mid Cap Equity
Domestic Mid Cap Core Equity	Russell Mid Cap Index	US Core Mid Cap Equity
Domestic Mid Cap Growth Equity	Russell Mid Cap Growth Index	US Growth Mid Cap Equity
Domestic Small/Mid Cap Value Equity	Russell 2500 Value Index	US Small/Mid Cap Value Equity
Domestic Small/Mid Cap Core Equity	Russell 2500 Index	US Small/Mid Cap Core Equity
Domestic Small/Mid Cap Growth Equity	Russell 2500 Growth Index	US Small/Mid Cap Growth Equity
Domestic Small Cap Value Equity	Russell 2000 Value Index	US Value Small Cap Equity
Domestic Small Cap Core Equity	Russell 2000 Index	US Core Small Cap Equity
Domestic Small Cap Growth Equity	Russell 2000 Growth Index	US Growth Small Cap Equity
International Developed Equity	MSCI EAFE Index (Gross)	International Active Equity
Portable Alpha	MSCI EAFE Index (Gross)	International Active Equity
International Small Cap Equity	MSCI World Ex US Small Cap Index (Gross)	International Small Cap Equity
International Emerging Equity	MSCI Emerging Markets Index (Gross)	Emerging Markets Equity
Global Equity	MSCI All Country World Index	Global Equity
Core Fixed Income	BC US Aggregate Bond Index	US Broad Market Core Fixed Income
Portable Alpha	BC US Aggregate Bond Index	US Broad Market Core Fixed Income
High Yield Fixed Income	BC US Corporate: High Yield Index	US High Yield Bonds
Global Fixed Income	BC US Aggregate Bond Index	Global Fixed Income
TIPS	BC U.S. TIPS Index	US TIPS
Commodities	S&P GSCI Light Energy Index	N/A
Energy	Cliffwater Private Energy Index	Cliffwater Private Energy Index

VII. EXTERNAL INVESTMENT MANAGEMENT OF TRADITIONAL ASSET CLASSES

In order to maintain continuity and the level of expertise required, the Fund's assets, excluding the PERA building, shall be 100% externally managed by investment professionals registered under the Investment Advisors Act of 1940 (or appropriately exempt from registration). The Board has elected to utilize a combination of active and passive management, to be implemented entirely by external investment managers. The Board will formally evaluate on a regular basis certain strategic decisions regarding the portfolio structure. The major types of strategic decisions include but are not limited to:

- The passive vs. active management mix;
- Any strategic overweights/underweights based on market capitalization, investment style, sector allocation or other factors.

A. Search and Selection

The Board has established the following objectives for hiring external investment managers for publically traded asset classes. In establishing these objectives, it is the Board's intention to assure all interested parties that decisions made in carrying out these actions occur in a full disclosure environment characterized by competitive selection, objective evaluation, and proper documentation. The overriding consideration with respect to all decisions is that they shall be made solely in the best interest of the Fund.

Any action to hire a manager will be based on one or more of the following circumstances:

- Identification of a new asset class or strategy which has been approved in advance by the Board;
- A need for enhancing diversification by style, method, or other factor, within an existing asset class;
- A need to replace an investment manager that the Board intends to terminate;
- A need to retain additional managers in order to reach an asset class target and avoid excessive manager concentration.

The selection of new investment managers will adhere to a consistent merit-based procurement process to ensure an open and competitive manager universe, proper evaluation and due diligence of all candidates, and selection. The evaluation process will follow the PERA of New Mexico Procurement Policy for Investment-Related Services *(Section XIV.E. Procurement Policy)*. All efforts should be conducted in an open, competitive and transparent environment in order to assure that qualified service providers are identified, that the objectives for the manager's mandate are clearly articulated, and that pricing is at market.

B. Monitoring and Evaluation

Manager retention decisions have the same potential impact on returns as manager selection decisions and should be afforded the same degree of attention. The Board recognizes the discipline necessary to maintain a long-term focus on the Fund and has designated the following framework for identification of existing and potential problems; it outlines how and when PERA should address specific issues and events thereby avoiding untimely or ad-hoc decisions that may adversely impact Fund returns. This Policy will apply to all of PERA's external managers, except where otherwise noted, and is intended to accomplish these objectives:

- Foster a long-term approach to manager evaluation;
- Provide a logical and statistically valid framework for manager evaluation;
- Promote timely responses to actual and potential performance issues;
- Provide flexibility to allow application across all asset classes, management styles, and market environments.

Monitoring and Evaluation Process

The framework for retention analysis relies on a formal performance reporting process that includes:

- Monthly performance reports from Custodian *(Section XI. B. Custodian)* and Consultant to Staff. These reports will detail overall performance of the Fund and the performance of individual managers.
- Quarterly performance reports from the investment managers to Staff.
- Regular quarterly reports from Staff and Consultant to the Committee at regular Committee meetings.

The formal performance reports per Section XII of this Policy are supplemented by qualitative analysis generated in the course of regular, on-going contact between the investment managers, Staff and the Consultant.

C. Watch List

A manager retention decision is very important to the continued success of a pension fund's investment strategy. As such, it should not be taken lightly nor should it be made with blind reliance on quantitative or qualitative guidelines. The ultimate decision rests with the Board following consultation with Staff and/or the Consultant.

Quantitative Factors Resulting in Watch List Additions

A number of factors may contribute to a manager's over- or under-performance at any given time such as - market dynamics, investment skill, and/or pure chance. Given this uncertainty, it is unwise to mandate termination purely for lagging performance at any specific point. The following represent guidelines to be used in making a recommendation to the Board with regards to placing a traditional asset class manager on the Watch List:

Test 1 If the manager's rolling, three-year return (gross of fees) falls below the rolling, three-year benchmark return for three (3) consecutive quarters.

Test 2 If the manager's rolling, three-year return (gross of fees) for three (3) consecutive quarters ranks in the bottom third of the Consultant's peer group universe.

The quantitative guidelines above refer to a minimum time frame of three (3) years, which is preferred, but not required for inclusion on the Watch List. If a negative performance trend for a manager with less than a three year track record with PERA becomes of concern to Staff, Consultant and/or the Board, Staff will ask the Consultant to conduct a "look back" review of the manager's strategy using longer-term composite information. The strategy will be put through the same tests as stated in the above guidelines.

The Committee can make a recommendation to the Board to place a manager on the Watch List based on the quantitative criteria. The Board may place the manager on the watch list at any time.

Once a manager is placed on a Watch List, the Committee will be notified by Consultant and/or Staff and performance will be closely monitored and scrutinized. All of the qualitative criteria should be reviewed along with an explanation of the underperformance from the manager. Additional actions could include Staff meetings with the manager and a formal re-interview of the manager by the Board. A recommendation from Staff and Consultant to terminate or retain the manager must be made to the Committee at the meeting following inclusion on the Watch List. The manager will remain on the Watch List pending a recommendation to the Committee by Staff and Consultant as to the manager's ongoing relationship.

Expectations will be established by Consultant and/or Staff on a case-by-case basis specific to the manager for recommendation to the Committee for removal from the Watch List. Failure to achieve these expectations shall result in termination. Generally, one period of a rolling, three (3) year return above the benchmark or above the bottom third of the Consultant's peer group universe following placement on the Watch List will be required for a manager's removal from the Watch List.

Qualitative Factors Resulting in Watch List Additions

A significant and potentially adverse event related, but not limited, to any of the following qualitative issues or events, will be considered a reason to add the manager to the Watch List. Examples include, but are not limited to, these events:

- Violation of investment guidelines;
- Deviation from stated investment style and/ or shifts in the firm's philosophy or process;
- Turnover of one or more key personnel;
- Change in firm ownership or structure;
- Significant loss of clients and/or assets under management;
- Significant and persistent lack of responsiveness to client requests;
- Litigation;
- Failure to disclose significant information, including potential conflicts of interest;
- Chronic violations of PERA's Policy;
- Any other issue or situation of which the Staff, Consultant and/or Committee become aware that is deemed material.

Should any of these events occur, the recommended courses of action are similar to those contained in the preceding section (*Quantitative Factors Resulting in Watch List Additions*). After an assessment of the nature of the problem or potential problem, the Committee should then make a determination as to the appropriate course of action at the meeting after notification. Possible responses include, but are not limited to, the following:

- No action;
- Placement on Watch List;
- Immediate Staff meetings with the manager;
- Formal re-interview of the manager by the Board;
- Initiation of a comprehensive review;
- Termination.

Additions and removals from the Watch List will be treated on a case-by-case basis by the Board, Staff and Consultant.

If an issue is considered serious enough, a special meeting of the Committee and/or Board may be requested by the Executive Director, based on recommendations by the CIO and/or Consultant.

D. Termination

From time to time it will be necessary for the Board to terminate a contractual relationship with an Investment Manager. These actions must be viewed in the context of a business decision. Due to the sensitivity of this issue, the Board has established the following guidelines to assist in making these termination decisions. In establishing these guidelines, it is the Board's intention to assure all interested parties that decisions made in carrying out these actions occur in a full disclosure environment characterized by objective evaluation and proper documentation. The overriding consideration with respect to all decisions is that they shall be made solely in the best interest of the Fund.

Any action to terminate a manager may be based on one or more but not limited to, the following primary criteria:

- Significant changes in firm ownership and/or structure
- Loss of one or more key personnel
- Significant loss of clients and/or assets under management
- Shifts in the firm's philosophy or process
- Significant and persistent lack of responsiveness to client requests
- Changes in PERA's investment strategy eliminating the need for a particular style or strategy
- Chronic violations of PERA's Policy
- Investment performance that has fallen below Policy expectations *(Section VII. B. Performance Benchmarks, Mandate-Level Benchmarks)*
- Identification of a new asset class or strategy which has been approved in advance by the Board
- A need for diversification of styles within an existing asset class
- Any other issue or situation of which the Staff, Consultant and/or Committee become aware that is deemed material.

According to provisions of the Professional Services Agreement (PSA) used by PERA, the Board may terminate an investment manager at any time with thirty (30) days notice.

Prior to the termination decision, the primary and other relevant considerations shall be identified and documented in Committee and Board minutes and supporting documents. It is the Board's intent to have a plan in place before termination of any manager including embracing the Request for Proposal process for traditional manager additions and replacements.

VIII. INVESTMENT GUIDELINES

The Board may invest and reinvest the funds in the following classes of securities and investment activities as long as such investments comply with the UPIA. Fund of Fund strategies are allowable in any of the asset classes. All investments are subject to approval of the Board and satisfactory legal review of applicable contractual terms and conditions.[1]

A. Permitted Investments

Equity

- Preferred stock, common stock, initial public offerings, securities of foreign issuers listed on U.S. Exchanges, and any security convertible to common stock or American Depository Receipts (ADRs) that are registered by the U.S. Securities and Exchange Commission (SEC) of any corporation whose securities are listed on at least one U.S. stock exchange that has been approved by or is controlled by the SEC or on the National Association of Securities Dealers (NASD). Global mandates may be considered.

- Preferred stock, common stock, and convertible issues of any non U.S. Corporation; which may be denominated in non U.S dollars, provided that the securities are traded on one or more national stock exchanges or included in a nationally recognized list of stocks; and provided that the funds of which the retirement board is trustee shall not be invested in more than ten percent of the voting stock of any company.

[1] Investments listed here are for general information purposes only. Each manager retained by the Board will be given specific guidelines with regard to permissible investments relevant to their role.

- Portable Alpha for the purpose of earning excess return of 3% above a designated index (i.e. the S&P 500, EAFE, Barclays Aggregate, or other commonly used indexes) by combining the alpha potential of hedge funds with beta exposure acquired through swaps and/or futures. Performance of the Portable Alpha Program shall combine: (i) investments in a diversified portfolio of hedge funds, (ii) a cash reserve of short term cash investments, and (iii) a set of S&P 500 Index or other reference index swaps and futures contracts. The beta overlay component shall replicate the returns of the difference between the S&P 500 Index return, or other reference index, and LIBOR through swaps and futures. The cash reserve component of the portfolio shall provide sufficient liquidity to provide for possible cash outflows stemming from net losses in the beta overlay and to earn a cash return equal to or above LIBOR at comparable risk. The target size of the cash reserve is 15% of Portable Alpha portfolio assets, but could vary significantly to settle periodic swap payments and receipts. The alpha generating hedge fund component is expected to deliver an absolute net of fee return between 3% and 4% per year in excess of LIBOR at a bond like level of risk. The target size of the hedge fund portfolio is 85% of Portable Alpha portfolio assets, but could vary due to periodic swap payments and receipts. *Appendix A. Portable Alpha* contains further details on the Portable Alpha program.

<u>Fixed Income</u>

- Bonds, notes or other obligations of the United States government, its agencies, government-sponsored enterprises, corporations, or instrumentalities for which the credit of the United States government is pledged for the payment of the principal and interest. Global mandates may be considered.

- Bonds, notes or other obligations issued by a state, its municipalities or other political subdivisions, that have received an investment grade bond rating, and are registered by the SEC or the Municipal Securities Rulemaking Board (MSRB).

- Bonds, notes, commercial paper or other obligations of any corporation organized and operating within the United States.

- Debt obligations of non-United States governmental or quasi-governmental entities, these may be denominated in foreign currencies; obligations, including but not limited to bonds, notes or commercial paper with an investment grade rating (unless otherwise approved by the Board) of any corporation organized outside of the United States. Currency transactions, including spot or cash basis currency transactions, forward contracts and buying or selling options or futures on foreign currencies, shall be permitted for the purposes of hedging foreign currency risk.

- Collateralized obligations, including but not limited to mortgages, held in trust that: (1) are publicly traded and are registered by the SEC or other Self Regulatory Organization (SRO) and (2) have underlying collateral that is either an obligation of the United States government or else has a credit rating above or equal to BBB according to the Standard and Poor's rating system or Baa according to the Moody's investors rating system or their equivalent by a national rating agency approved by the Board (unless otherwise approved by the Board).

<u>Real Estate and Real Assets</u>

- Real Estate Investment Trusts (REITS), including equity investments in publicly traded securities of a company dedicated to owning, and/or, operating income-producing real estate, including but not limited to apartments, shopping centers, offices and warehouses.

- Real Estate Partnerships, including investments in private vehicles through limited partnerships or limited liability companies that have an ownership interest in direct real estate properties, whether income-producing or non-income producing. The investment strategies may include "value added" strategies, which derive their return from both income and appreciation, and "opportunistic," which derive their return primarily through appreciation.

- Inflation-indexed bonds, including investments in actively or passively managed investment vehicles. Treasury Inflation Protected Securities (TIPS) are an example of inflation-indexed bonds.

- Commodities, including but not limited to futures and/or swaps on individually traded commodities or indexes comprising groups of commodities like the Goldman Sachs Commodity Index (GSCI) or Dow Jones – AIG Commodity Index (DJ-AIGCI). Commodities may be used as an overlay strategy on TIPS or other publicly traded instruments.

- Timber Partnerships, including but not limited to, investments in limited partnerships or limited liability companies that have an ownership interest in properties where the majority value of the property is derived from income-producing timber.

- Energy Partnerships, including but not limited to limited partnerships or limited liability companies that have an ownership interest in energy-related businesses. Investments may include those across the industry spectrum from upstream (exploration and production), to midstream (processing and transportation), to downstream (refining and distribution).

<u>Absolute Return (Hedge Funds)</u>

- Hedge Funds shall invest primarily in publicly traded securities and derivatives and use long and short positions and leverage, within limits as specified in each hedge fund's governing documents, to reduce market exposure in order to profit from security selection. Hedge funds shall manage at least $100 million in the investment strategy for which they are hired. Funds-of-funds investment vehicles may be used for up to 20% (1/5) of the hedge fund strategic allocation target of 9% of total fund assets.

- Market Neutral strategies such as equity market neutral, fixed income arbitrage, and convertible bond arbitrage.

- Credit strategies that typically invest in high yield bonds, bank loans and structured credit products.

- Distressed strategies that seek to take advantage of corporate securities in default, under bankruptcy protection, in distress or heading toward such a condition or in liquidation.

- Event Driven strategies that take advantage of transaction announcements and other one-time events, including merger arbitrage, spin-offs and restructurings.

- Equity long/short strategies where there is a combination of long and short positions primarily in publicly traded equities, with a net market exposure less than that of the overall equity market. Strategies may be focused on U.S., non-U.S., and/or specialty mandates.

- Global Macro strategies such as all market portfolios, opportunistic long-only, managed futures, currency, dedicated short selling strategies or other specialty strategies.

- Multi-strategy hedge funds that invest using a combination of previously described strategies.

Private Equity

- Private investments that provide capital for company start-up, expansion, buyout/acquisition, recapitalization, debt financing (either distressed debt or mezzanine financing), or other business purposes. Private equity includes buyouts, venture capital, non-U.S., and distressed debt. Private equity managers shall have a verifiable track record and long-term experience of at least 5 years working together as a team.

- Buyouts, including investments in acquisitions, growth equity, recovery investments, subordinated debt, and special situations, which represent a diversified strategy across many sub-categories. Investments shall be made across the market capitalization spectrum and involve the purchase of a control position (primarily majority positions, with some minority positions) in an established company. The use of leverage is acceptable. Investments are typically made in years one through six and returns typically occur in years three through ten. Investments may be made in companies that are either U.S. or non-U.S. domiciled.

- Venture Capital, including investments in companies in a range of stages of development from start-up/seed-stage, early stage, and later/expansion stage. Investments are typically made in years one through six and returns typically occur in years four through ten. Investments may be made in companies that are either U.S. or non-U.S. domiciled.

- Distressed Debt, including investments in the debt instruments of companies which may be publicly traded or privately held that are financially distressed and are either in bankruptcy or likely candidates for bankruptcy. Typical holdings are senior and subordinated debt instruments and bank loans. Equity exposure is acceptable as debt positions are often converted to equity during the bankruptcy reorganization process. Investments are typically made in years one through five and returns typically occur in years three through ten. Investments may be made in companies that are either U.S. or non-U.S. domiciled.

Operating Cash Management

For cash management, the Board may utilize the services of the State Treasurer for overnight investment of short-term assets. The Board may also utilize a separate or commingled short-term investment fund ("STIF") approved by the Board and administered by the Custody Bank which is designated by the State Treasurer or the State Board of Finance. PERA can only utilize STIF accounts that invest in those securities authorized by PERA's statutes, Policy and investment guidelines. Investment managers shall invest all cash in PERA's approved STIF funds.

Currency

Active currency strategies which do not necessarily hedge existing international holdings, but instead, seek absolute return which may include leverage, cross-hedging, emerging markets, and interest rate futures are allowable.

Repurchase Agreements

Contracts for the purchase of specific securities and subsequent resale at a specified date and price in the future, of duration not to exceed one year. No such contract shall be entered into unless the contract is fully secured by obligations of the United States, or other securities backed by the United States, having a market value of at least one hundred two percent of the amount of the contract. Prior to approval of the State Board of Finance with respect to the Custodial Bank agreement, tri-party repurchase agreements are proper investments under this Policy. No such contract shall be entered into unless the contracting bank, brokerage firm or recognized institutional investor has a net worth in excess of five hundred million dollars ($500,000,000).

Mutual Funds and Commingled Investments

Mutual funds or other similar commingled investments as an alternative to investing in separately managed portfolios of stocks and bonds. Such investments may be in stocks or shares of a diversified investment company or mutual fund registered under the Federal Investment Company Act of 1940, provided that the investment company has total assets under management of at least one hundred million dollars ($100,000,000); individual, common or collective trust funds of banks or trust companies, provided that the investment company has assets under management of at least one hundred million dollars ($100,000,000); provided that the board may allow reasonable administrative and investment expenses to be paid directly from the income or assets of these investments.

Exchange Traded Funds (ETFs)

The investment managers whose account is structured as a separate account shall limit their use of ETFs to those situations where a comparable investment yielding comparable investment results cannot be obtained on a separately managed basis except as provided in their governing documents or PSA and will be subject to review by Staff and Consultant.

Borrowing and Use of Derivatives

- **Leverage**. Leverage used with any investment strategy will be consistent with the discipline for which the Board hired the investment manager. Use of leverage will be controlled as appropriate in each manager's respective governing documents and will be subject to review by Staff and Consultant.

- **Authorized Uses of Derivatives**. Investment managers shall not purchase securities on margin, sell short, use individual stock options, puts, calls, or trade in futures contracts, unless specified in the governing documents entered into by PERA and the investment manager.

1. The Board delegates to Staff, in consultation with the investment consultants, the ability to equitize cash through the use of futures or other exchange traded derivatives for the purpose of reducing cash "drag."

2. The Board delegates to Staff, in consultation with the investment consultants, the ability to use futures or other exchange traded derivatives for the purpose of re-balancing to long-term policy allocation targets.

- **Compliance and Reporting**. Each traditional asset investment manager is required to report to the Board the market value of derivatives exposure in the portfolio, both quarterly and annually. Each separate account investment manager is required to report to the Board in their quarterly and annual report the market value of ETFs, commingled funds and mutual funds if these investments are contained in the portfolio. The Consultant shall provide Staff, at least annually, an estimate of the market value of derivatives exposure and an estimate of the leverage within the alternative assets.

B. Prohibited Investments

Per UPIA guidelines, the Board, all investment managers, and Staff are expected to perform their fiduciary duties as a prudent investor would and to conform to all applicable federal and state statutes governing the investment of retirement funds. The following investments are prohibited:

- Investments precluded by law or regulation.
- Transactions that involve a broker acting as a "principal" where such broker is also the investment manager who is making the transaction are prohibited unless otherwise approved in each manager's respective PSA.
- Any other investments as specified in each manager's respective PSA.

C. Diversification

- Portfolios managed on behalf of PERA should not hold more than 10% of the outstanding securities of any single issuer, unless specified in their governing documents.
- Individual manager diversification will be addressed in each manager's respective PSA.
- Refer to *Section III.D. Investment Objectives, Diversification.*

IX. ALTERNATIVE ASSET PROGRAM

A. Asset Allocation

The CIO and Consultant shall aggregate investment vehicle data within each alternative investment asset class and perform analysis on each aggregate portfolio, paying careful attention to individual investment vehicle allocations and strategy/sector concentrations to strive to achieve proper diversification within the specific alternative investment class.

Real Assets and Real Estate

- PERA shall endeavor to limit the potential for any one investment to materially harm the long-term results of the Real Asset and Real Estate Program by investing across a variety of industries and geographic locations.

- PERA shall not comprise more than 20% of any one investment vehicle, unless that vehicle is a separately managed account, and any one investment vehicle may not comprise more than 10% of the Real Assets and Real Estate Program once it is fully invested, calculated on a committed capital basis. The optimum number of investment vehicles in the portfolio and the maximum exposure to any one investment vehicle varies with time and will be evaluated as part of the annual plan for the Real Assets and Real Estate Program.

- PERA shall strive to limit the potential for any one investment to negatively impact the long-term results of the Real Assets and Real Estate Program by investing across business cycles and vintage years.

- Private investment vehicles are illiquid and typically have expected holding periods of 10-12 years. Investments are typically held until maturity and selling prior to maturity may result in realizing a sales price that reflects a discount to fair market value. Liquidity risk is managed by minimizing the possibility of forced sales that may arise from exceeding maximum exposure limits or lowering asset allocation targets to private real assets or real estate investments.

- PERA shall ordinarily direct the sale of securities distributed by its investment vehicles as soon as practically possible and strive to not impair the value of the security.

- The targeted and range of investment exposures to the various real asset and real estate styles are shown in the table below. These exposures should be measured on a fair value basis, once the Real Asset and Real Estate Program is fully invested. During the Real Asset and Real Estate Program's ramp-up period, exposures can be estimated using percentages of committed capital.

Style	Target	Minimum	Maximum
Real Estate Partnerships	37.5%	30%	45%
REITS	12.5%	5%	20%
Commodities	12.5%	7%	18%
Timber	12.5%	0%	18%
Energy Partnerships	25%	20%	45%
Total	100%		

Absolute Return (Hedge Funds)

- Funds-of-funds investment vehicles may be used for up to 20% (1/5) of the absolute return strategic allocation target of 9% of total fund assets. Over the long-term (3-5 years), performance of the Absolute Return Program is expected to exceed LIBOR by 4% annualized, net of fees and expenses.

- Over the short-term, performance of the Absolute Return Program is expected to exceed the HFRI Fund-of-Funds Composite Index, net of fees and expenses.

- No more than 15% of the Absolute Return Program's market value of assets may be invested in any hedge fund at the time of investment. If a hedge fund's market value exceeds 20% of the Absolute Return portfolio's market value, Staff will implement a plan to reduce the exposure to 15% or less over a six month period. Staff will report its re-balancing plan to the Committee and the Board at the next regular meeting. During the investment period the weightings to individual funds and exposures may temporarily exceed the limits previously indicated. In addition, the weightings to individual funds and exposures may temporarily exceed the limits previously indicated to the extent that lock-up periods or other liquidity restrictions with respect to a hedge fund prevent an immediate reallocation. No investments shall be made in any hedge fund if the combined Absolute Return and Portable Alpha investments in that hedge fund represent more than 1% of total PERA assets at the time of investment. If any hedge fund's combined Absolute Return and Portable Alpha market value exceeds 1.75% of total PERA assets, Staff and consultant will implement a plan to reduce the exposure below 1.75% of total PERA assets over a six month period. Staff will report its re-balancing plan to the Committee and the Board at the next regular meeting.

- Individual hedge fund investments may have specified liquidity parameters defining lock-up periods and withdrawal frequency. Liquidity risk is managed by monitoring and maintaining a schedule of the liquidity of the individual hedge funds and aggregating it at the total Absolute Return Program level.

- The performance of individual hedge funds will be evaluated compared to their expected return premium over LIBOR (300-500 basis points) over trailing 5 year periods, net of all fees and expenses, as well as their respective peer universe over shorter time periods, as measured by a recognized hedge fund index provider.

Absolute Return (Hedge Fund) Investment Targets:

Style	Target	Minimum	Maximum
Market Neutral	5%	0%	20%
Credit	15%	5%	25%
Distressed	10%	5%	20%
Event Driven	20%	10%	30%
Equity Long/Short	25%	15%	45%
Global Macro	5%	0%	20%
Multi-Strategy	20%	15%	50%
Total	100%		

Private Equity

- It is recognized that it may take three to five years for the Private Equity Program to be fully invested and that there may be deviations from the Private Equity Investment Targets during the initial funding period.

- Private equity investments are typically private equity limited partnerships, but may also include other entities such as limited liability companies or offshore corporations. These investment vehicles may invest in any type of security throughout the capital structure.

- PERA shall endeavor to limit the potential for any one investment to materially harm the long-term results of the Private Equity Program by investing across a variety of industries and geographic locations. For investments in venture capital, it is recognized that opportunities may be most readily available in a relatively limited number of industries.

- The Fund shall not comprise more than 20% of any one investment vehicle, and any one investment vehicle may not comprise more than 8% of the Private Equity Program once it is fully invested, calculated on a committed capital basis. The optimum number of investment vehicles in the portfolio and the maximum exposure to any one investment vehicle varies with time and shall be evaluated as part of the annual plan for the Private Equity Program.

- The potential for any one investment to negatively impact the long-term results of the Private Equity Program shall be limited by investing across business cycles and vintage years. Investments shall be selected with the goal of gaining exposure to the array of financing stages by opportunistically exploiting the best investments at different stages of the business cycle.

- Private equity investments are illiquid and long term in nature (10-12 years), typically held until maturity. Selling prior to maturity may result in realizing a sales price that reflects a potentially substantial discount to fair market value. Liquidity risk shall be managed by minimizing the possibility of forced sales that may arise from exceeding maximum exposure limits or lowering asset allocation targets to private equity investments.

- Should PERA receive distributions of securities in-kind from its private equity investments, PERA, subject to the Limited Partnership Agreement, shall direct the sale of those securities as soon as practically possible without impairing the value of the security.

- Individual investment vehicle performance, as measured by the internal rate of return, shall be evaluated compared to the performance of respective peer universes and vintage years, as provided by a recognized private equity data provider such as Venture Economics or Cambridge Associates. It is recognized that immature private equity investments will ordinarily have a "J-curve effect" whereby there are low to negative returns in the initial years due to the payment of investment management fees during a period when investments are typically carried at cost and returns have not been realized.

- The performance of the Private Equity Program, net of fees and expenses, is expected to exceed the PERA U.S. Equity asset class benchmark by 3% annualized over periods greater than five years.

- Within 3 to 5 years after the program is fully invested, performance of the Private Equity Program is expected to exceed the median return of a peer universe as provided by a recognized private equity data provider (e.g.Venture Economics or Cambridge Associates) for the respective vintage years.

- The targeted and range of investment exposures to the various private equity styles are shown in the table below. These exposures should be measured on a fair value basis, once the Private Equity Program is fully invested. During the Private Equity Program's ramp-up period, exposures can be estimated using percentages of committed capital.

Private Equity Investment Targets

Style	Target	Minimum	Maximum
Buyout	55%	30%	70%
Venture Capital	20%	10%	30%
Non-U.S.[1]	15%	5%	25%
Distressed Debt[2]	10%	0%	40%
Total	100%		

[1] Non-U.S. exposure refers to private equity funds with a primary investment focus outside of the U.S. and/or significant operations outside of the U.S., rather than to where the underlying investments are domiciled.

[2] The wide investment target range for Distressed Debt reflects the cyclical nature of this investment style. The amount of money raised by distressed debt managers and the performance expectations for distressed investments tends to increase during economic downturns. Private equity investors typically commit greater amounts to distressed debt in periods of economic distress, while reducing amounts in periods of economic strength.

B. Search and Selection

The Alternative Investment approval process is a thorough and comprehensive process that considers each individual investment. Staff reviews the Consultant's due diligence report for each investment recommendation and discusses each recommendation with the Consultant. The Committee also reviews the Consultant's due diligence report and Staff's written analysis for each recommended alternative investment. Each recommendation is presented to the Committee for its consideration to recommend to the Board. The Board reviews these same written reports for alternative investments recommended by the Committee, with the Board having final authority to approve each investment recommendation. The General Counsel and External Legal Counsel review the legal documents for all approved alternative investments. All investments are subject to satisfactory legal review.

Below is the schematic that PERA follows for search and selection.

PERA Alternative Investment Asset Program Process Schematic				
	Consultant	**Staff**	**Committee**	**Board**
1) Consultant and Staff collaborate on potential investments, discussing the merits, "fit," and competitive advantages of each	2) Consultant performs thorough due diligence	4) Staff reviews Consultant's written recommendation and any additional due diligence materials [1]	6) Consultant/Staff make recommendation to Committee	8) Committee makes recommendation to Board; Board approves/disapproves, subject to legal review and governing document negotiation
	3) Consultant provides written recommendation to Staff	5) Staff and Consultant provide written recommendation to Committee	7) Committee reviews and approves/ disapproves recommending to the Board	
	9) Legal documents reviewed by General Counsel, External Counsel, Staff, and Consultant			
	10) Negotiation of legal documents by internal and External Counsel, Staff, fund managers, and Consultant			
		11) Executive Director/designee executes governing document		
	12) Staff/Consultant monitors partnership, Consultant prepares monthly and quarterly reports			

[1]The Procurement Policy provides that in fulfilling this responsibility the CIO may, at his or her discretion, or as directed by the Board, meet directly with alternative investment managers under review and engage in other activities that enhance PERA's knowledge of and satisfaction with the recommendation of the Consultant.

On or before December 31 of each year, Consultant will provide the Staff with a proposed commitment budget and action plan for the upcoming calendar year for their review. The purpose of this plan is to provide PERA with the Consultant's outlook for the assets that constitute the private asset program as well as an overview of the Consultant's specific investment objectives and goals for PERA for the upcoming year. The plan should address the following:

1. An overview of the Consultant's outlook for the market.

2. The Consultant's recommended investment strategy for PERA for the following calendar year. The investment strategy should include recommended commitment budgets for

each private asset class, as well as projected asset class sub-strategy allocations for each of the private asset classes.

3. A review of the previous year's commitment budget, actual commitments made, and actual cash flows; the review should include a model of projected cash flows and assumptions for arriving at the recommended commitment budgets.

4. An estimate of the number partnerships the Consultant expects to recommend to PERA for the following year and the amount of capital connected therewith.

C. Due Diligence

The Staff and Consultant will also conduct due diligence with the respective alternative investment managers to understand the underlying drivers of performance and risks associated with the managers' strategies. Additionally, the Staff and Consultant shall conduct portfolio reviews and on-site due diligence as necessary. Site visits will be performed to confirm that appropriate infrastructure is in place to support the investment process. The Staff and Consultant shall provide the Board with regular performance reports and advise the Board of other matters, including providing redemption recommendations, as appropriate.

D. Placement Fees

PERA shall not invest with any investment manager, other than with managers of publicly traded equities or publicly traded fixed-income securities, unless the investment manager discloses the identity of any third-party marketer who rendered services on behalf of such investment manager in obtaining the investment and also discloses the amount of any fee, commission or retainer paid to the third-party marketer for the services rendered. "Third-party marketer" means a person who, on behalf of an investment fund manager or other person seeking an investment from the fund and under a written or implied agreement, receives a fee, commission or retainer for such services from the person seeking an investment from the fund. PERA Staff and/or Consultant will review affected managers on an annual basis.

E. Monitoring

These requirements shall apply to the Real Assets and Real Estate, Absolute Return, and Private Equity Programs. Through the monitoring process, Staff and Consultant will extend the initial due diligence into monthly performance reports, quarterly portfolio reports and annual reviews. This monitoring process regularly seeks to determine whether the investment is meeting the specific alternative investment asset class objectives and other requirements. In the broadest sense, the monitoring process is intended to determine whether the initial reasons for selecting the strategy and investment vehicle remain valid. The monitoring process should disclose whether there has been any material deviation from the investment philosophy and process; the personnel responsible for managing the investment vehicle are still in place; the organization continues to be stable; performance and risk meet expectations; and the investment vehicle manager adheres to its investment and other requirements. The underlying principle of the monitoring program is to determine whether all risks to which PERA is exposed through the use of outside investment advisors have been identified, understood, and, to the extent possible, controlled. The monitoring process focuses on four areas:

- Compliance with reporting and valuation requirements;
- Continuity of investment philosophy and process;
- Stability of personnel and organization; and
- Performance and risk management.

The Consultant will place an alternative investment on its Watch List if serious concerns exist. The Consultant provides Staff with a Watch List report for each investment on the Consultant's Watch List. The Consultant reports all Watch List investments to the Committee and provides the Committee with frequent updates on all Watch List investments. A Watch List designation is not a prerequisite for redemptions.

X. SAFEKEEPING AND CUSTODY

A. State Treasurer

The Board shall utilize the services of the State Treasurer for holding PERA's assets. The State Treasurer at the direction of the Board shall deposit said assets with a bank or trust company for safe keeping or servicing.

B. Custodian

The Custodian holds assets directly, through its agents, its sub-custodians, or designated clearing systems, assets. The Custodian is accountable for registration of those designated assets in good delivery form, collection of income generated by those assets, and any corporate action notification. The Custodian is responsible for delivery and receipt of securities of the aforementioned transactions. The Custodian is responsible for the ongoing pricing and valuation of all assets; investment managers of traditional assets must reconcile their values to those of the Custodian. Alternative investment managers will provide PERA's capital account statements to the Custodian. The Custodian is to cooperate with, and provide assistance to, PERA and its investment managers in the reconciliation process. The Board may opt to designate other duties to the Custodian as stipulated in its agreement with the State Board of Finance. The Custodian is required to provide online records and reports, performance reporting, accounting reports and other services included in the agreement.

XI. REPORTING REQUIREMENTS

A. External Managers for Traditional Assets

Within thirty days after the close of every fiscal year, each investment manager of traditional assets must certify that its internal portfolio accounting statements reconcile with those of PERA for the year just ended. The certified portfolio detail must be reported to PERA by July 31 of each year. If reconciliation cannot be completed within the designated period, a list of discrepancies must be provided along with an explanation of how they shall be resolved.

An investment manager of traditional assets under contract to PERA must preliminarily reconcile the differences between market values of securities as reported by the Custodian and the market values as shown on the monthly report of the investment manager's records and report such to PERA staff on a monthly basis not later than 30 days after month end. In the event of a disagreement between PERA and the investment manager as to the market value of securities or the "market value of account" for the purposes of any fee agreement, the market value of securities or "market value of account" as determined by PERA shall prevail.

The Board reviews the investment performance of the managers against their stated objectives, both gross and net of fees, at least quarterly. At the sole discretion of the Board, each investment manager may be expected to meet with the Board at least annually to review its portfolio and investment results in the context of this Policy.

An investment manager under contract must report to PERA, as soon as administratively possible, if at any time there is:

- A change in investment philosophy;
- A loss of one or more key professionals;
- A new portfolio manager on PERA's account;
- A change in ownership structure of its firm;
- Any occurrence which might potentially impact the management, professionalism, integrity or financial position of the management firm.

Each investment manager is required to annually report to the Board the market value of derivatives exposure in the portfolio. Each separate account investment manager is required to report to the Board in their quarterly and annual reports the market value of ETFs, commingled funds, mutual funds and currency hedges if contained in their portfolio.

B. External Managers for Alternative Assets

Alternative investment managers will provide PERA's capital account statements to the Custodian. The CIO and Consultant shall provide the Board with regular performance reports and advise the Board of other matters as appropriate. Additional guidelines are included in *Section X.E. Alternative Asset Program, Monitoring.*

C. Custodian

The Custodian will, as directed by Staff, provide periodic performance reports to Staff and Consultant. These reports shall detail the individual performance of managers and the overall performance of the Fund.

D. Consultant(s)

The Consultant(s) will provide quarterly performance reports to Staff and the Board at its regular meetings. In preparing these reports, the Consultant will rely upon asset values and performance calculations reported by the Custodian.

E. Staff

Staff will be responsible for ensuring that performance reports are received in a timely manner from these parties and will provide continual supervision of external performance reporting on the portfolio. Staff will work with the Consultant to complete a detailed performance measurement report on a quarterly basis. The executive summary will, at a minimum, include information for the most recently available one, three, and five year periods.

XII. REVIEW AND APPROVAL OF INVESTMENT POLICY

The Board shall review the Policy from time-to-time to determine if modifications are necessary or desirable but will delegate Staff to review the Policy on an annual basis. Staff will recommend modifications as warranted. If modifications are made, they shall be promptly communicated to all investment managers and other interested persons.

Modifications may occur due to:

- Operational problems that become apparent during the investment management process;
- Changes in economic prospects, Fund characteristics, the development of new investment instruments or strategies, or sponsoring employer organizations;
- Other causes as determined by the Board.

By signing this Statement of Investment Policy the Board through its Chair, indicates its agreement therewith.

Adopted:	June 25, 1992
Amended:	September 14, 1993
Amended:	April 28, 1994
Amended:	September 28, 1995
Amended:	January 29, 1998
Amended:	March 23, 1998
Amended:	January 27, 2000
Amended:	September 26, 2002
Amended:	July 31, 2003
Amended:	October 31, 2003
Amended:	July 1, 2005
Amended:	September 28, 2005
Amended:	December 29, 2005
Amended:	July 27, 2006
Amended:	August 31, 2006
Amended:	September 28, 2006
Amended:	June 1, 2007
Amended:	August 30, 2007
Amended:	July 31, 2008
Amended:	June 24, 2010

By: Cynthia D. Borrego

Cynthia D. Borrego, Chairperson
Public Employees Retirement Association of New Mexico

XIII. APPENDICES

A. Portable Alpha Program

Hedge Funds

- Investment is authorized in hedge funds that use abroad array of various hedge fund styles, including but not limited to Market Neutral, Credit, Distressed, Event Driven, Equity long/short, Global Macro and Multi-Strategy.

- For the 85% target allocation to the hedge fund component of the Portable Alpha Portfolio, the targeted and range of investment exposures to the various hedge fund styles are shown in the following table:

Style	Target	Minimum	Maximum
Market Neutral	**5%**	**0%**	**20%**
Credit	**15%**	**5%**	**25%**
Distressed	**10%**	**5%**	**20%**
Event Driven	**20%**	**10%**	**30%**
Equity Long/Short	**0%**	**0%**	**15%**
Global Macro	**5%**	**0%**	**20%**
Multi-Strategy	**30%**	**20%**	**50%**
Total	**85%**		

- Separate accounts and/or a variety of commingled vehicles, such as limited partnerships, limited liability companies, or offshore corporations are permissible.

- No more than 15% of the Portable Alpha portfolio's market value of assets may be invested in any hedge fund at the time of investment. If a hedge fund's market value exceeds 20% of the Portable Alpha portfolio's market value, Staff will implement a plan to reduce the exposure to 15% or less over a six month period. Staff will report its re-balancing plan to the Committee and the Board at the next regular meeting. During the investment period the weightings to individual funds and exposures may temporarily exceed the limits previously indicated. In addition, the weightings to individual funds and exposures may temporarily exceed the limits previously indicated to the extent that lock-up periods or other liquidity restrictions with respect to a hedge fund prevent an immediate reallocation. No investments shall be made in any hedge fund if the combined Absolute Return and Portable Alpha investments in that hedge fund represent more than 1% of total PERA assets at the time of investment. If any hedge fund's combined Absolute Return and Portable Alpha market value exceeds 1.75% of total PERA assets, Staff and Consultant will implement a plan to reduce the exposure below 1.75% of total PERA assets over a six month period. Staff will report its re-balancing plan to the Committee and the Board at the next regular meeting.

- Individual hedge fund investments may have specified liquidity parameters defining lock-up periods and withdrawal frequency. Liquidity risk is managed by monitoring and maintaining a schedule of the liquidity of the individual hedge funds and aggregating it at the total Portable Alpha portfolio level.

- The performance of individual hedge funds will be evaluated compared to their expected return premium over LIBOR (300-400 basis points) over trailing 5 year periods, net of all fees and expenses, as well as their respective peer universe over shorter time periods, as measured by a recognized hedge fund index provider.

Beta Overlay

- The beta overlay will be implemented using index futures and/or swaps.
- All swap agreements shall be consistent with International Swaps and Derivatives Association (ISDA) recommendations.
- Swap terms can vary but will generally have a one year maturity (tenor) with quarterly resets.
- The notional dollar size of the swaps should equal the value of hedge funds plus the cash reserve.
- Swap counterparties should be rated at least A- or equivalent by two major rating agencies.
- The notional value of swaps should be diversified across several (at least three or more) counterparties.
- Quarterly reset periods should be diversified across months with approximately one-third of total value of notional swaps resetting every month.
- Swap maturities should be diversified so that re-pricing is not concentrated at a single point in time.

Cash Reserve

- Only short term maturity, high quality, liquid investments are permitted that exhibit little or no principal risk.
- If the level of the cash reserve exceeds 18% of the total Portable Alpha portfolio, cash should be re-balanced back to 15%; cash reserve may exceed 18% temporarily due to re-balancing in the hedge fund portfolio.
- Generally when the level of the cash reserve falls below 15% of the total Portable Alpha portfolio due to negative beta overlay returns, the cash reserve should not be re-balanced upward since it is anticipated that positive swap returns that are normally exhibited will increase cash reserves back to the 15% level.

B. Proxy Voting Guidelines

The active voting of proxies is considered an integral part of the investment process and may be delegated to the discretion of the investment managers, subject to any guidelines which are established by the Board (see Proxy Voting Policy).

C. Securities Lending

The Board may authorize a securities lending program for all or any portion of the assets held as investments by PERA. The lending of securities may be accomplished by the Board contracting with one or more designated agents that are experienced in providing securities lending services.

Securities may only be loaned by the designated agent(s) through the entering of contracts for the temporary exchange of securities for the use by broker-dealers, banks or other recognized institutional investors, for periods not to exceed one year, for a specified fee or consideration. Each contract must be fully secured by collateral in the form of cash or U.S. government or government agency securities of at least one hundred and two percent of the market value plus accrued interest for domestic securities and of at least one hundred and five percent of the market value of the securities plus accrued interest for international securities. All international loans and proceeds shall be negotiated and settled in U.S. dollars.

D. Transition Management

Transitions are an important and inevitable element of portfolio management. The optimal method to use in executing a transition may vary significantly from one transition to another based on the types of assets involved and the timeframe in question. PERA's general objective in a manager transition is to implement the change in a cost-effective, timely manner while maintaining the appropriate market exposure. It is imperative to note that the cost of transition is not commissions alone, but also bid/ask spread, market impact and opportunity cost. The market impact cost is the effect trading will have on the market price of the shares being traded. The opportunity cost, sometimes referred to as implementation shortfall, is the cost of market movements over the time it takes to trade. Efforts should be made to minimize the total cost rather than any single cost component.

E. Class Actions

When the Fund has sustained investment losses that may be recoverable through class action securities litigation, the Fund will participate as a member of the class. In accordance with industry practice, the Fund's Custodian is responsible for filing all claims and other documents on behalf of the Fund to ensure that the Fund receives its pro rata share of any recovery.

Investment staff will monitor the Custodian's compliance with its class action procedures. Staff will forward all notices and information concerning potential or pending class action litigation that are received in the Fund's offices to the Custodian for research. Staff will report periodically to the Board on recoveries realized as a result of class action participation.

It is Board's policy not to serve as a lead plaintiff in securities class action litigation unless PERA is among the largest shareholders of the defendant issuer and service as a lead plaintiff is determined to be in the best interest of the Fund. The Board's decision to pursue active involvement will be made in consultation with the Executive Director, Staff, General Counsel's Office and such other professional advisors as the Board deems appropriate.

E. Procurement Policy

Public Employees Retirement Association
Procurement Policy for Investment-Related Services

1. Scope

Pursuant to NMSA 1978, Section 13-1-98(Y) (2005) the Public Employees Retirement Association ("PERA") is exempt from the Procurement Code (NMSA 1978, Sections 13-1-1 et seq.) for all contracts for investment advisory services, investment management services or other investment-related services. This Procurement Policy for Investment-Related Services ("Policy") sets out the procedures and guidelines by which PERA shall procure investment-related services.

2. Purposes

The purposes of this Policy are: 1) to provide an open and fair competitive process to acquire competent and qualified investment-related services; 2) to allow PERA to respond to unacceptable performance and market changes in a flexible, efficient and timely manner; and 3) to comply with all relevant laws, statutes and ethical codes of conduct.

3. Statutory and Rule References

PERA operates under the authority of the Public Employees Retirement Act, NMSA 1978, Sections 10-11-1 to 10-11-141, as amended, the Volunteer Firefighters Retirement Act, NMSA 1978, Sections 10-11A-1 to 10-11A-7, as amended, the Judicial Retirement Act, NMSA 1978, Sections 10-12B-1 to 10-12B-19, as amended, the Magistrate Retirement Act, NMSA 1978, Sections 10-12C-1 to 10-12C-18, as amended, and the Public Employees Reciprocity Act, NMSA 1978, Sections 10-13A-1 to 10-13A-4, as amended.

Members of the Public Employees Retirement Board and PERA staff members are subject to the Governmental Conduct Act, NMSA 1978, Sections 10-16-1 et seq.

PERA's Board Policies and Procedures apply to the procurement of investment-related services.

4. Application

This Policy applies to the procurement of investment-related services and investment-related legal services for alternative investments entered into by the PERA Board, as delegated to the Investment Division and Office of General Counsel of PERA, including investment adviser, investment manager, and investment-related services. This Policy shall not apply to the procurement of tangible goods and services purchased through State of New Mexico statewide purchasing agreements or otherwise required for the administration of the Investment Division.

5. Definitions

a. "alternative investments" are defined as a category of assets, often less liquid than traditional stocks and bonds, but designed to provide higher risk-adjusted returns and/or enhanced diversification when compared to traditional asset classes. Alternative investments include, but are not limited to, private equity, absolute return, real assets and real estate.

b "corrupt practice" is defined as offering, giving, soliciting or receiving anything of value to influence the action of a public official or employee, or threatening injury or harm to any person or their property, position or reputation in connection with any procurement in order to obtain or retain business or any other advantage in the conduct of business.

c. "gatekeeper" is defined as a person, individual, or entity serving in a discretionary and fiduciary capacity with respect to alternative investments including but not limited to searching, sourcing, screening, performing due diligence and making investment recommendations to the Public Employees Retirement Board.

d. "incumbent provider" means a current contractor providing investment-related services under a professional services agreement with the PERA Board through the PERA Investment Division.

e. "Investments Director" means the Director of the Public Employees Retirement Association Investments Division or his or her designee, or, in the event of a vacancy, the individual designated as Acting Director.

f. "emergency" means unexpected circumstance(s) that require a rapid decision to prevent a significant financial loss to the PERA Fund where the normal processes required in this Policy would not prevent or avoid such loss. Poor performance by a contractor is not to be considered an "emergency." By way of example, "emergency" can include, although it is not limited to, the departure of a portfolio manager or other key personnel from a contractor firm without notice, SEC investigation or action against a contractor firm or individuals within the firm, or a contractor firm's unexpected loss of its organizational capabilities.

g. "fraudulent practice" means misrepresenting any fact in order to influence any procurement.

h. "offeror" means any person or persons responding to a Request for Proposals.

i. "PERA" means the Public Employees Retirement Association.

j. "procurement manager" means the Investments Director or his or her designee.

k. "runner(s)-up" means one or more RFP offeror not initially selected for award but qualified for award by meeting or complying with all mandatory criteria and formally designated as runner(s)-up by the evaluation committee based on points awarded.

l. "small purchase" means the procurement of investment-related services for flat-fee compensation that does not exceed fifty-thousand dollars ($50,000.00). For purposes of this Policy, "small purchase" procurement includes professional services or investment-related services or tangible property but does not include performance-fee compensation contracts for investment management services.

6. Request for Proposals Process Required; Exceptions

All procurement of PERA investment services in publicly traded securities by the Investment Division shall be achieved by a competitive Request for Proposals process ("RFP") in accordance with this Policy, except under the following circumstances:

a. A supermajority (9 of the 12 members) of the PERA Board votes that an incumbent provider, currently providing satisfactory service under a contract for a given mandate that is the result of an RFP, should be given the opportunity to negotiate a new contract in connection with the expiring term of the current contract for the same or substantially similar mandate on the equivalent or better terms to PERA. In no event, however, shall the term of the contract awarded under this subsection, including any and all extensions, exceed eight (8) years without being competitively bid. This exemption shall be exercised by PERA at least thirty (30) days prior to the expiring term of the current contract;

b. After termination of an investment manager contract for performance reasons, a supermajority (9 of the 12 members) of the PERA Board votes that it is necessary to transition the assets subject to the terminated contract to another incumbent provider who 1) is currently providing any investment management services under a contract that is the result of an RFP process; and 2) is qualified to serve as a replacement for the asset class under consideration. A new or amended contract should be negotiated in connection with the transitioning of assets on the equivalent or better terms to PERA. In no event, however, shall the term of the contract awarded under this subsection, including any and all extensions, exceed eight (8) years without being competitively bid;

c. A supermajority (9 of the 12 members) of the PERA Board votes that an incumbent provider currently providing satisfactory service under a contract that is the result of an RFP process, should be given the opportunity to negotiate a new or amended contract in connection with the provision of new services or a new mandate not provided by that incumbent under the existing contract. In no event, however, shall the term of the contract awarded under this subsection exceed eight (8) years without being competitively bid;

d. The procurement is a small purchase procurement as defined in this policy;

e. The procurement is an alternative investment as defined in this policy; or

f. The procurement is an emergency procurement as defined in this policy. Performance under any contract awarded under this subsection shall be reviewed by the Board within twelve (12) months. In no event, however, shall the term of the contract awarded under this subsection, including any and all extensions, exceed two (2) years without being competitively bid.

7. Selection of Alternative Investments.

The PERA Board is responsible for the selection of alternative investments. For purposes of this policy, "alternative investments" are defined as provided in Paragraph 5 a of this policy and are drawn from one of the following categories:

- Private equity – investments in businesses made through means other than through publicly traded securities such as buyout investments and venture capital.

- Absolute Return (Hedge Funds) – investment strategies with the goal of achieving positive returns with a degree of independence from movements in financial markets and independent of traditional performance benchmarks.
- Real assets – investments in assets, other than publicly traded securities, that have a return linked to inflation, such as timber, energy related investments and other commodity-based investments.
- Real estate – investments in assets, other than publicly traded securities, that invest in properties directly or private securities of companies that invest in properties directly.

Alternative investments are typically made through an interest in a limited partnership but also may be made through another vehicle (e.g., separate account, commingled fund, offshore entity, etc.), as appropriate for the individual investment.

The Board shall select alternative investments that enable PERA to meet its long-term return objectives set forth for the respective asset classes from recommendations made by its Alternative Investment Consultant acting in its capacity as gatekeeper for alternative investments.

The Alternative Investment Consultant(s) shall, at a minimum, consider the following criteria when recommending alternative investments:

- Firm organization and stability;
- Quality and stability of the investment team;
- Proposed investment strategy;
- Investment track record; and
- Legal and economic terms governing the investment.

Consistently applying the investment criteria listed above, the Alternative Investment Consultant(s) shall review and analyze the most appropriate investments from a comprehensive universe of investment opportunities. Those investments that meet the criteria above shall be subject to an extensive due diligence analysis by the Alternative Investment Consultant(s) resulting in a written due diligence report and a recommendation that shall be reviewed by the Director of Investments for completeness and rationale. In fulfilling this review responsibility, the Director of Investments may, in his discretion or as directed by the Board, meet directly with alternative investment managers under review and engage in other activities that enhance PERA's knowledge of and satisfaction with the recommendations of the Alternative Investment Consultant(s). The Director of Investments shall prepare a written report to the Board indicating whether or not he concurs with the conclusions and recommendations of the Alternative Investment Consultant(s). Subject to satisfactory review by the Director of Investments, the Alternative Investments Consultant(s) shall, where appropriate in its discretion, prepare and present to the Board a written recommendation to invest for the Board's evaluation and final approval. All Board decisions on recommendations to invest shall be subject to satisfactory review by PERA's Office of General Counsel, or its designated outside counsel, who shall review and approve investment partnership documents for legal sufficiency and consistency with PERA's internal policies and procedures for alternative investments.

The Director of Investments, the Alternative Investment Consultant(s) and the Board shall be disciplined in applying investment criteria. If investments in a particular sub-market (i.e. early-stage venture capital) cannot be found that meet the Board's criteria for quality, expected return, and risk, investments in such sub-market should be de-emphasized until market conditions improve. The Director of Investments, the Alternative Investment Consultant(s) and the Board shall not make alternative investments solely for diversification purposes.

8. **Public Notice**

Notice of an RFP shall be published at least twenty-one (21) calendar days prior to the date set for opening of responses. All notices referred to in this policy may be published or furnished electronically, in print, or both at the Investment Director's discretion. Notice shall be published in a commercially reasonable way and shall be posted on PERA's website. Notice may be published in newspapers and/or trade journals in this or any other state, and may be made in any way likely to notify prospective offerors. PERA may also provide notice to persons or businesses identified through independent investment services data bases.

9. **Requests for Proposals**

a. All RFPs shall be issued by the Investment Director, or in the case of investment-related legal services for alternative investments, by the Office of General Counsel upon approval by the PERA Board, and shall contain:

i. Specifications of the services to be procured including clearly identified "mandatory" and "preferred" (discretionary) criteria and/or minimum mandatory qualifications for prospective offerors;

ii. The proposed term of the anticipated contract, not to exceed eight (8) years;

iii. Description of any mandatory contract terms including but not limited to a term stating that the contractor accepts fiduciary status with respect to assets managed on behalf of PERA;

iv. The anticipated compensation formula for the services to be procured;

v. The location and method where responses shall be delivered and a secure method for receipt and safeguarding of the proposals. Each RFP shall state that PERA shall have no responsibility or obligation to accept incorrectly delivered proposals or to provide for redelivery of incorrectly sent proposals;

vi. The deadline for receipt of proposals including the calendar date and the time. Deadlines may only be extended by the Board on the request of the Investment Director, for good cause shown. Any extension must be requested and approved, with notice given to prospective offerors, prior to the original deadline;

vii. A proposal cover sheet, to be completed and signed by the offeror and submitted in original form;

viii. Description of a formal question and answer process;

ix. The relative weight to be given to the selection criteria and/or qualifications in the evaluation of the responses;

x. The date, time and location when responses will be reviewed;

xi. Notice of all applicable statutes, rules and policies; and

xii. Any other information the Investment Director or the Office of General Counsel believes will be useful in procuring the services sought to be procured.

b. RFPs may be modified or amended prior to the recommendation for contract award for the limited purposes of:

i. clarifying or correcting errors or defects; or

ii. modifying the schedule for the submission of responses and the deadline for receipt of responses.

c. The requirement for notice of amendment of an RFP shall:

i. be the same as for the initial RFP if it occurs before the deadline for receipt of responses; and

ii. be achieved by written notice to all offerors if it occurs after the deadline for receipt of responses.

10. Sufficiency of Responses; Receipt, Acceptance and Rejection

a. Proposals received after the deadline will be rejected.

b. Timely responses meeting all mandatory requirements shall be accepted for consideration without the opportunity for correction or modification.

c. Responses must include an original proposal cover sheet, which has been fully completed, and signed. Responses provided electronically shall simultaneously provide a fully completed, signed original proposal cover sheet on or before the deadline for responses to the RFP. Failure to provide this original document will be cause for rejection of the proposal.

d. Telephone and other types of inquiries concerning the proposal, outside the formal question and answer process, shall be discouraged.

e. Successful offerors and runners up will meet or comply with all "mandatory" criteria and/or qualifications. Failure to meet or comply with the mandatory criteria, requirements and/or qualifications shall be cause for rejection of the proposal.

11. Selection Criteria

The selection criteria to be used in selecting successful offerors will be fully and specifically described in each RFP. PERA may utilize internet-based or analytic software applications to research, evaluate, compare and select investment products across asset classes and vehicle types.

12. Evaluation Process

a. The PERA Board Chair, with the advice of the Committee Chair, shall appoint an evaluation committee for each RFP. The size of the evaluation committee is at the discretion of the Board Chair with the advice of the Investment Director. The evaluation committee may include members of the Board, the Executive Director and PERA staff.

b. The evaluation committee in whole or in part may, in its sole discretion, conduct interviews, discussions or negotiations with some or all offerors whose proposals have been accepted for the purpose of clarifying the terms of the proposals.

c. The evaluation committee may, but need not, provide the opportunity for offerors who have participated in interviews, discussions or negotiations to submit best and final offers.

d. There is no right to interviews, discussions, negotiations or the opportunity for best and final offers and the evaluation committee may recommend contract awards without conducting interviews, discussions or negotiations and without providing the opportunity for best and final offers.

e. The evaluation committee shall create a record, including but not limited to uniform scoring sheets, showing the basis for its recommendation to the Board and shall prepare a written report culminating with its designation of a runner-up and its recommendation to the Board of the successful offeror(s). The Investment Director shall retain the scoring sheets and evaluation committee report for at least the stated term of the resulting contract.

f. Scoring may include the opportunity for an offeror to receive a point score for a variety of factors including but not limited to the offeror's business approach and methodology, consistency of key personnel, philosophy and process, references, experience with the asset class under consideration, verified or verifiable performance and portfolio data of a sufficient duration to include a variety of economic and market environments, and a history of consistently strong and successful performance versus peers and relevant benchmarks.

g. The evaluation committee shall make a selection recommendation to the Board. The Board shall select the successful offeror(s).

13. <u>Award</u>

a. Following a vote by the Board, successful offeror(s) shall be promptly notified in writing of the award, subject to due diligence and successful contract negotiations conducted by the Investment Director.

b. Contracts may be awarded to more than one successful offeror as a result of a single RFP process.

c. Contracts may be awarded to one or more offeror(s) designated as runner(s)-up by the evaluation committee within two (2) years of the initial deadline set for receipt of RFP responses subject to due diligence and successful contract negotiations conducted by the Investment Director.

14. <u>Public Access</u>

After award, any written determination of award, any evaluation committee report and all proposals may be subject to public inspection in accordance with applicable public records laws including the New Mexico Inspection of Public Records Act, NMSA 1978, Sections 14-2-1 et seq. Any material claimed to be privileged, confidential, proprietary or trade secret material must be clearly designated as such in advance and provided on separate pages.

15. Protest Procedure

PERA's procurement of investment-related services is exempt from the New Mexico Procurement Code (NMSA 1978, Sections 13-1-1 et seq.) and offerors have no access to the protest procedures set out in the New Mexico Procurement Code (NMSA 1978, Sections 13-1-172 through 176) or related portions of the New Mexico Administrative Code involving investment-related services procurement. As a trust fund, PERA has no authority to award money damages, costs or attorney's fees. In the interest of providing a fair, open and competitive procurement process for investment-related services, the following protest procedure is provided.

a. An offeror who is not awarded an investment-related services contract may file a Notice of Protest with PERA.

b. A Notice of Protest must be in writing and received or post-marked within ten (10) calendar days of the award by the Board that gives rise to the protest.

c. A Notice of Protest shall state the full factual basis for the protest.

d. A Notice of Protest shall be sent or delivered to: PERA Office of General Counsel (Attention: Award of Contract Protest), P.O. Box 2123/33 Plaza La Prensa, Santa Fe, New Mexico 87504/87507.

e. The filing and receipt of a Notice of Protest shall not stop or delay the execution of an investment-related services contract between PERA and the successful offeror.

f. The PERA General Counsel or his or her designee shall conduct an interview with the protestor, either in person or telephonically and may, in his or her sole discretion, conduct interviews with others who have or may have information relating to the award and/or the protest.

h. The PERA General Counsel shall promptly issue a written recommendation to the Board. The written recommendation shall state whether or not the General Counsel recommends that the contract whose award gave rise to the protest process should be terminated, and whether or not the General Counsel recommends an alternative contract award to the protester or whether the RFP should be cancelled and competitively rebid. The written recommendation shall state the full factual basis for the recommendation.

i. The PERA Office of General Counsel shall mail the written recommendation to the protestor and shall provide written notice of the scheduled Board vote on the recommendation.

j. The Board shall vote on the recommendation at its first normally scheduled meeting following the issuance of the written recommendation.

k. The Office of General Counsel shall notify the protestor, in writing, of the Board vote.

16. Emergency and Small Procurements

In the case of emergency and small purchase procurements, as defined in this Policy, the Investment Director may, with the prior approval of the Board, pre-select or invite a provider of investment-related services to present an offer. The Investment Director, in his or her discretion, may negotiate a contract with that provider if the offer is deemed acceptable and subject to the following conditions:

a. The small purchase procurement for investment-related professional services must have a value not exceeding fifty thousand dollars ($50,000), excluding applicable state and local gross receipts taxes in accordance with applicable professional services contract procedures promulgated by the department of finance and administration.

b. Notwithstanding the requirements of subsection a, the Investment Director may procure investment-related tangible property or services having a value of not more than fifty thousand dollars ($50,000) by issuing a direct purchase order to a contractor based upon the best obtainable price.

c. Procurements shall not be artificially divided to fall within the small purchase procurement exemption;

d. Performance under emergency procurements shall be reviewed by the Board within twelve (12) months of the effective date of the emergency contract.

17. Research and Information

At any time and irrespective of any existing contracts, PERA may conduct independent research or may issue a request for information to survey the marketplace about the availability, quality and price of investment related services.

18. Penalties for Corrupt and Fraudulent Practices

Felony penalties are imposed for fraud, bribes, gratuities and kickbacks in violation of the Criminal Code, NMSA 1978, Section 30-16-1 et seq.

Civil penalties are imposed for violation of the Governmental Conduct Act, NMSA 1978, Sections 10-16-1 et seq.

Civil penalties are imposed for antitrust violations of the Trade Practices and Regulation Act, NMSA 1978, Sections 57-1-1 and 6.

Upon discovery of any corrupt or fraudulent practice as defined in this Policy, the Board may reject a proposal, reject a recommendation for an award or declare an individual or firm ineligible for a stated period of time or the Board may impose any combination of these measures.

19. Ethical Disclosures and Conflicts of Interest.

Members of the Public Employees Retirement Board and PERA staff members are subject to NMSA 1978, Section 10-11-130.1, which prohibits acceptance of anything of value directly or indirectly from a person or organization that has a current contract with PERA, is a potential bidder, offeror or contractor of services to PERA, or is authorized to invest public funds pursuant to state or federal law. For purposes of this Policy, potential bidder means any person or entity that may provide services to PERA within the next twelve months.

All offerors or incumbent providers are required to disclose any interest, direct or indirect, which would conflict in any manner or degree with the performance or services required under any contract with PERA. Offerors and incumbent providers shall certify that the requirements of the Governmental Conduct Act, NMSA 1978, Section 10-16-1 et seq. regarding contracting with a public officer or state employee have been followed.

SIGNATURES

By signing this Procurement Policy for Investment-Related Services, the Board through its Chair, indicates its agreement therewith.

Adopted: January 26, 2006

Amended: August 31, 2006

Amended November 30, 2006

By:_______________________________

David A. Baca, Chairman NM PERA

F. GLOSSARY OF TERMS

Agency Security – a U.S. government-issued security that was not issued by the Treasury Department and may be backed by the full faith and credit of the United States depending upon the issuing agency.

Agent – any individual or entity acting on behalf of another.

Alpha – the premium an investment portfolio earns above a certain benchmark (such as the Standard & Poor's 500 Index). A positive alpha indicates the investor earned a premium over that index.

American Depository Receipts (ADRs) – certificates issued by a U.S. bank and traded in this country as domestic shares. The certificates represent the number of foreign securities the U.S. bank holds in that security's country of origin. ADRs make trading foreign securities easier by eliminating currency exchange, legal obstacles, foreign ownership transfers, and the need to trade on a foreign exchange.

Asset Allocation Decision – choosing among broad asset classes such as equities, fixed-income securities and real estate.

Basis Point – one one-hundredth of one percent. For example, an addition of 40 basis points to a yield of 7.50 percent would increase the yield to 7.90 percent. Basis points are normally used when quoting yields or returns, alpha, or fees paid to investment managers.

Benchmark – a gauge in the securities market by which investment performance can be measured, such as the Standard & Poor's 500 Index.

Bid and Ask – the highest price an investor will pay for a security (bid), or the lowest price someone will sell a security (ask).

Board Chair – Chairperson of the Board of Trustees, as elected by the Board of Trustees.

Buyouts - investments in acquisitions, growth equity, recovery investments, subordinated debt, and special situations, which represent a diversified strategy across many sub-categories.

CIO – Chief Investment Officer

Commingled Fund – a pooling of funds from multiple investors, managed as one account. The client owns units in the pool. Similar to a mutual fund.

Committee – the Committee, which is a sub-committee of the Board.

Committee Chair – Committee Chairperson as appointed by the Board Chair.

Commodities – investments in basic goods often used as inputs in the production of other goods or services. Notable examples include oil, natural gas, gold, and other precious metals.

Credit Quality -

S&P	Moody's	Explanation
Higher Credit Quality - Investment Grade		
AAA	Aaa	Prime grade, highest safety
AA+	Aa1	High credit quality
AA	Aa2	
AA-	Aa3	
A+	A1	Upper-medium credit quality
A	A2	
A-	A3	
BBB+	Baa1	Lower-medium credit quality
BBB	Baa2	
BBB-	Baa3	
Lower Credit Quality - Speculative Grade		
BB+	Ba1	Speculative - low quality
BB	Ba2	
BB-	Ba3	
	B1	Highly speculative
B	B2	
	B3	
Extremely Low Credit Quality - High Speculative or in Default		
CCC+	Caa	Very high risk, poor quality
CCC		
CC	Ca	May be in default soon
C	C	Very speculative
CI		For income bonds - interest not being paid
D		Securities already in default

Credit Strategies – a hedge fund strategy that typically invests in high yield bonds, bank loans and structured credit products.

Discretionary Authority – the authority provided to investment managers and consultants to make investment decisions on behalf of PERA.

Distressed Debt – investments in the debt instruments of companies which may be publicly traded or privately held that are financially distressed and are either in bankruptcy or likely candidates for bankruptcy.

Distressed Strategies – a hedge fund strategy that seeks to take advantage of corporate securities in default, under bankruptcy protection, in distress or heading toward such a condition or in liquidation.

Diversification – spreading a portfolio over many investments (or may types of investments) to avoid excessive exposure to any one source of risk.

Duration – the average time to receipt of all the cash flows of a bond weighted by the present value of each of the cash flows. The duration value of the bond gives bond investors an indication of how interest rate changes will affect the bond's price. It is the percentage by which the bond's price will move, given a 100 basis point change in yield.

EAFE – the **MSCI EAFE** Index is a stock market index that is designed to measure the equity market performance of developed markets (Europe, Australasia, Far East), excluding the US & Canada.

Energy Partnership – investments in private vehicles with a focus on oil and gas exploration, or other alternative energy strategy.

Equity Investment – claims held by the residual owners of a firm. May also be referred to as common stock. Investments in Real Estate and certain Private Markets classifications may also be considered equity.

Equity Long/Short Strategies – a hedge fund strategy where there is a combination of long and short positions primarily in publicly traded equities, with a net market exposure less than that of the overall equity market. Strategies may be focused on U.S., non-U.S., and/or specialty mandates.

ETFs – Exchange Traded Funds.

Event Driven Strategies – a hedge fund strategy that takes advantage of transaction announcements and other one-time events, including merger arbitrage, spin-offs and restructurings.

Fiduciary – one who can exercise discretionary authority or can control important aspects of a pension Fund's management.

Fixed Income Investment – a security issued by a borrower that obligates the issuer to make specified payments to the holder over a specific period. Fixed income may also be referred to as "debt" or "bonds."

Fund-of-Fund Investment Vehicles – an investment fund comprised of any number of underlying investment funds

Gatekeeper – as defined in the PERA Procurement Policy: a person, individual, or entity serving in a discretionary and fiduciary capacity with respect to alternative investments including but not limited to searching, sourcing, screening, performing due diligence and making investment recommendations to the Public Employees Retirement Board.

Global Macro Strategies – a hedge fund strategy with a focus on all-market portfolios, opportunistic long-only, managed futures, currency, dedicated short selling strategies or other specialty strategies.

HFRI – Hedge Fund Research, Inc.

Inflation-Indexed Bonds - investments in bonds with the principal component linked to inflation. Treasury Inflation Protected Securities (TIPS) are the most common example of inflation-indexed bonds.

Initial Public Offering (IPO) – the first time an equity securities issue is available for the public to buy.

In-Kind Distribution - a distribution made in the form of a security rather than cash.

IRR (Internal Rate of Return) - an appropriate performance benchmark for private equity investments. In simple terms, it is a time-weighted return expressed as a percentage. IRR uses the present sum of cash drawdowns (money invested), the present value of distributions (money returned from investments) and the current value of unrealized investments and applies a discount.

Leverage – in investments, this is the control of a large amount of money by a smaller amount of money, such as buying on margin. In finance, this is the relationship of debt to equity on a company's balance sheet in the form of the debt/equity ratio.

Limited Partnership – a partnership with at least one of the partners holding only a limited liability. Commonly utilized in the Private Equity asset class.

Market Cycle or Full Market Cycle – a period of time (typically three to five years) where a market experiences increasing prices (bull market), decreasing prices (bear market), and a return to the original starting point of market strength.

Market Neutral Strategies – a hedge fund strategy that seeks complete avoidance (zero correlation) of market risk. Various forms of hedging strategies are typically employed.

NMAC – New Mexico Administrative Code Rules.

Multi-Strategy Hedge Funds – a hedge fund that invests using a combination of any number of hedge fund strategies.

Proxy – an instrument empowering an agent to vote for a shareholder.

PSA – Professional Service Agreement.

Qualitative Analysis – a subjective analysis of a security, with the judgment not based on financial information, such as that found on a balance sheet or income statement. Instead, the judgment may be based on such issues as labor relations.

Quantitative Analysis – an analysis of a security, with the judgment based on financial information such as that found on a balance sheet or an income statement.

Real Estate Partnerships – investments in private vehicles through limited partnerships or limited liability companies that have an ownership interest in direct real estate properties, whether income-producing or non-income-producing. This may include "value added" strategies, which derive their return from both income and appreciation, and "opportunistic" strategies which derive their return primarily through appreciation.

Re-balancing – realigning the proportions of assets in a portfolio as needed.

REITs – equity investments in publicly traded securities of a company dedicated to owning and/or operating income-producing real estate, including but not limited to apartments, shopping centers, offices, and warehouses.

Risk – the chance that an investment's actual return will be different than expected. This includes the possibility of losing some or all of the original investment. Risk is usually measured by calculating the standard deviation of the historical returns.

Separate Account – funds managed on an individual account basis; no pooling with other investors. The client owns the securities.

Short-Term Investments – any fixed income investment with less than one year to maturity.

Split Rating – situation where rating agencies have assigned different ratings to a particular issue or issuer.

Spread – the difference between the bid price and the ask price.

Standard Deviation – a measure of the degree to which an individual probability value varies from the distribution mean. The higher the number, the greater the risk.

Supermajority – as defined in the PERA Procurement Policy, a vote of 9 out of 12 Board Members.

"To Be Announced" (TBA) Security – a forward mortgage-backed securities trade, generally 48 hours prior to an established trade settlement date.

Timber Partnership – investments in private vehicles with a focus on the timber industry.

Total Return – interest or dividend income plus any realized or unrealized capital gain (or loss) on an investment, net of any capital contributions or distributions from the corpus.

UPIA – Uniform Prudent Investor Act.

Venture Capital - investments in companies in a range of stages of development from start-up/seed-stage, early stage, and later/expansion stage.