



NOTICE OF PUBLIC MEETING

To: Due Diligence Committee:
Jason Gordo, Chair
Michael O'Neal, Trustee
Jeff Grover, Trustee

From: Rick Santos, Executive Director

SUBJECT: Annual Due Diligence Trips

The Due Diligence Committee will meet at 12:30 p.m., Wednesday, April 20, 2016 .

The Committee will meet in the Large Conference Room at StanCERA's Office, located at 832 12th Street, Suite 600, 6th Floor, Modesto.

AGENDA

1. Discussion and Action Regarding the Annual Due Diligence Trips [View](#)



April 20, 2016

TO: Due Diligence Committee

FROM: Rick Santos, Executive Director

- I. SUBJECT: Annual Due Diligence Trips
- II. ITEM NUMBER: 1
- III. ITEM TYPE: Discussion and Action
- IV. STAFF RECOMMENDATION: Discontinue the practice of annual due diligence trips, yet reserve future due diligence trips for manager/firm events that require additional, onsite oversight from the Committee and staff
- V. ANALYSIS: Historically, StanCERA staff, due diligence committee members and the investment consultant annually visited a subset of StanCERA money managers onsite to perform auxiliary due diligence. Generally, the process consisted of the investment consultant sending a lengthy questionnaire (120+ questions) to the manager. Staff, the investment consultant and the Committee would go over the answers in an attempt to detect any issues that may give rise to any concerns for StanCERA. This would be followed up by an onsite visit to the firm's headquarters. In researching the topic, it appears that this tradition started over 30 years ago when StanCERA began making significant equity allocations to one active manager. However, given today's diligence processes and enhanced technical abilities, the practice may be outdated.

Today, StanCERA has several layers of manager diligence it performs on a constant basis. Our first line of defense is of course the investment consultant. On average, the consultant research professionals formally meet with investment managers either on-site or in the firm's offices roughly 600 times per year. In addition to in-person meetings, the consultant's manager research professionals also conduct roughly 200 conference calls with investment managers each year. Additionally, each manager is required to meet on conference call at least once annually with the Board of Retirement, the investment consultant and staff regarding recent performance, market outlook and organizational issues that may warrant even further diligence. StanCERA staff itself is in regular contact with our entire manager lineup. It is estimated that on average, internal staff speaks to all managers in the StanCERA stable at least once every couple months and even some on a much more frequent basis. Per our most recent audit, StanCERA will now be requesting and reviewing annual SOC reports required to be completed by StanCERA managers.

A favorable outcome from the Board's desire to maintain greater awareness and diligence over our alternatives, was the creation of the quarterly auxiliary investment reports. These reports force staff to dig deep into the understanding and reporting of all fees StanCERA pays to our managers. StanCERA staff also has the ability to analyze risk contribution and benchmark adherence and has statistical tools that allow us to look at historical manager performance in an unbiased fashion. All these reports and tools came from the desire of the Board to maintain a greater level of analytical diligence over the fund.

Finally, the decision to abandon the annual due diligence trips does not mean that StanCERA would never undertake this type of diligence in the future. On the contrary, this strategy is very effective when initially funding a new strategy or when StanCERA is concerned about changes at a firm that may require more in-depth discussion and analysis.

Annual Due Diligence Costs

Another component that must be weighed in the decision to continue annual due diligence trips is the incremental increase in consultant cost. In past years, this cost was fixed and a part of the normal fee schedule. Going forward, this will be a variable cost to the System and could be considerable. If the Committee wishes to continue this practice, staff would recommend we seek a cost proposal from the investment consultant before a decision is made.

- VI. RISK: None
- VII. STRATEGIC PLAN: Strategic Objective IV: Refine StanCERA's business and policy practices in ways that enhance stakeholder awareness, the delivery of member services and the ability of the Organization to administer the System effectively and efficiently
- VIII. ADMINISTRATIVE BUDGET IMPACT: Administratively, the decision will not affect the administrative budget, however, the incremental costs will come directly from the StanCERA investment portfolio



Rick Santos, Executive Director



Kathy Herman, Fiscal Services Manager