ND STATE INVESTMENT BOARD MEETING

Friday, June 26, 2015, 8:30 a.m.
Peace Garden Room, State Capitol
600 E Blvd, Bismarck, ND

AGENDA

I. CALL TO ORDER AND ACCEPTANCE OF AGENDA

II. ACCEPTANCE OF MINUTES (May 22, 2015)

III. INVESTMENTS

A. Asset and Investment Performance Overview - Mr. Hunter (enclosed) (20 min) *Informational*
B. Tobacco Prevention and Control Trust Fund Update - Mr. Hunter (enclosed) (20 min) **Board Action**
C. North Dakota Bankers Association - Mr. Hunter (enclosed) (10 min) *Informational*
D. Springbank - Mr. Hunter (enclosed) (10 min) *Informational*

IV. GOVERNANCE

A. Governance Policy Review - Mr. Hunter (enclosed) (20 min)
   1. Investments (Second Reading) **Board Action**
   2. Bylaws (First Reading) *Informational*

V. ADMINISTRATION

A. Legislative Update - Mr. Hunter (enclosed) (10 min) *Informational*
B. Staff Update - Mr. Hunter (enclosed) (5 min) *Informational*
C. Board Offsite Preview - Mr. Hunter (to follow) (5 min) *Informational*
D. Executive Director Compensation - Mr. Lech (to follow) (10 min) **Board Action**

VI. OTHER

Next Meetings:
SIB Retreat - July 24, 2015, 8:30 a.m. - University of Mary
SIB Audit Committee meeting - September 25, 2015, 1:00 pm - State Capitol, Peace Garden Room

VII. ADJOURNMENT

NORTH DAKOTA STATE INVESTMENT BOARD
MINUTES OF THE
MAY 22, 2015, BOARD MEETING

MEMBERS PRESENT: Drew Wrigley, Lt. Governor, Chair
Mike Sandal, Vice Chair
Lance Gaebe, Land Commissioner
Mike Gessner, TFFR Board
Adam Hamm, Insurance Commissioner (TLCF)
Rob Lech, TFFR Board
Mel Olson, TFFR Board
Yvonne Smith, PERS Board
Cindy Ternes, WSI designee
Tom Trenbeath, PERS Board

MEMBERS ABSENT: Kelly Schmidt, State Treasurer

STAFF PRESENT: Eric Chin, Investment Analyst
Connie Flanagan, Fiscal & Invt Op Mgr
Bonnie Heit, Assist to the SIB
David Hunter, ED/CIO
Fay Kopp, Dep ED/CRO
Terra Miller-Bowley, Supvr Audit Services
Cody Schmidt, Compliance Officer
Darren Schulz, Dep CIO

OTHERS PRESENT: Sarah Angus, Callan Associates
Paul Erlendson, Callan Associates
Clair Ness, Attorney General's Office

CALL TO ORDER:

Lt. Governor Wrigley called the State Investment Board (SIB) meeting to order at 8:30 a.m. on Friday, May 22, 2015, at the State Capitol, Peace Garden Room, Bismarck, ND.

AGENDA:

IT WAS MOVED BY MR. LECH AND SECONDED BY MS. SMITH AND CARRIED ON A VOICE VOTE TO ACCEPT THE AGENDA FOR THE MAY 22, 2015, MEETING AS DISTRIBUTED.

AYES:COMMISSIONER GAEBE, MR. SANDAL, MR. OLSON, MS. TERNES, MR. GESSNER, MR. TRENBEATH, MR. LECH, MS. SMITH, AND LT. GOVERNOR WRIGLEY
NAYS: NONE
MOTION CARRIED
ABSENT: TREASURER SCHMIDT, COMMISSIONER HAMM

MINUTES:

IT WAS MOVED BY MS. TERNES AND SECONDED BY MR. TRENBEATH AND CARRIED ON A VOICE VOTE TO APPROVE THE APRIL 24, 2015, MINUTES AS DISTRIBUTED.

AYES: MR. GESSNER, COMMISSIONER GAEBE, MS. SMITH, MS. TERNES, MR. LECH, MR. OLSON, MR. TRENBEATH, MR. SANDAL, AND LT. GOVERNOR WRIGLEY

NAYS: NONE
MOTION CARRIED
ABSENT: TREASURER SCHMIDT, COMMISSIONER HAMM

INVESTMENTS

Asset and Performance Overview – Mr. Hunter updated the SIB on the status of the portfolios they manage on behalf of their clients. Highlights as of March 31, 2015 - assets under management grew by approximately 19 percent or $1.66 billion in the last year.

The Pension Trust posted a net return of over 6.5 percent with gains of $293 million. All Pension Trust clients generated positive excess returns for the 1, 3, and 5 year periods ended March 31, 2015.

The Insurance Trust generated a net return of 5.4 percent with gains of $233 million. All Insurance Trust's clients generated positive excess returns for the 3 and 5 year periods ended March 31, 2015.

The Legacy Fund's net return was 5.7 percent and assets increased by 66 percent or $1.3 billion for the year ended March 31, 2015.

SIB client assets, based on unaudited valuations, exceeded $10.5 billion as of March 31, 2015.

Callan Associates Report – Mr. Erlendson provided Callan's insight on the economic and market environment for the period ended March 31, 2015.

Commissioner Hamm joined the meeting by teleconference.

Mr. Erlendson also reviewed the consolidated Pension Trust and Consolidated Insurance Trust performance for the period ending March 31, 2015.

IT WAS MOVED BY COMMISSIONER GAEBE AND SECONDED BY MR. SANDAL AND CARRIED BY A VOICE VOTE TO ACCEPT THE CALLAN REPORT AS PRESENTED.

AYES: MR. OLSON, MR. TRENBEATH, COMMISSIONER GAEBE, MR. GESSNER, COMMISSIONER HAMM, MS. SMITH, MR. SANDAL, MS. TERNES, MR. LECH, AND LT. GOVERNOR WRIGLEY
NAYS: NONE
ABSENT: TREASURER SCHMIDT

Executive Session

IT WAS MOVED BY MS. SMITH AND SECONDED BY MR. TRENBEATH AND CARRIED BY A VOICE VOTE TO MOVE INTO EXECUTIVE SESSION PER NDCC §44-04-19.1(9) AND NDCC §44-04-19.2 TO DISCUSS THE SPRINGBANK AGREEMENT.

AYES: MS. SMITH, MR. SANDAL, MR. OLSON, MR. GESSNER, MR. LECH, MR. TRENBEATH, MS. TERNES, COMMISSIONER HAMM, COMMISSIONER GAEBE, AND LT. GOVERNOR WRIGLEY
NAYS: NONE
MOTION CARRIED
ABSENT: TREASURER SCHMIDT

The SIB entered into Executive Session at 9:25 a.m. The SIB, Ms. Ness, Callan Associates representatives, and RIO personnel were present.

The SIB exited Executive Session at 10:07 a.m.

IT WAS MOVED BY MR. TRENBEATH AND SECONDED BY MS. TERNES AND CARRIED BY A VOICE VOTE TO ACCEPT THE FOLLOWING STAFF RECOMMENDATIONS: (1) ACCEPT CALLAN'S RECOMMENDATION TO EXTEND AND REVISE THE TERMS OF THE SPRINGBANK AGREEMENT; (2) AUTHORIZE RIO TO FINALIZE THE REVISED TERMS THROUGH SEPTEMBER 30, 2022.

AYES: MR. TRENBEATH, MR. OLSON, COMMISSIONER GAEBE, MR. LECH, MR. SANDAL, COMMISSIONER HAMM, MR. GESSNER, MS. SMITH, MS. TERNES, AND LT.GOVERNOR WRIGLEY
NAYS: NONE
MOTION CARRIED
ABSENT: TREASURER SCHMIDT

The SIB recessed at 10:09 a.m. and reconvened at 10:20 a.m.

GOVERNANCE

Legislative Update – Mr. Hunter updated the SIB on legislation affecting RIO. SB2022 which contains the biennial appropriation for RIO and the Public Employees Retirement System (PERS) was not approved by the 64th Legislative Assembly prior to the adjournment of the session. The bill had a number of amendments relating to PERS which were adopted by the Government Operations Sub-committee of the House Appropriations Committee. No amendments were adopted that affected RIO.

RIO and PERS requested the Attorney General provide an opinion on whether and to what extent the agencies are authorized to make expenditures during the next biennium. Both entities believe the opinion will be issued by the end of the biennium. After discussion,

IT WAS MOVED BY COMMISSIONER GAEBE AND SECONDED BY MS. TERNES AND CARRIED BY A VOICE VOTE TO AUTHORIZE STAFF TO SUBMIT AN APPLICATION TO THE EMERGENCY COMMISSION FOR ADDITIONAL FUNDING DURING THE NEXT BIENNIUM SO AS TO ALLOW RIO TO CONTINUE OPERATING UNDER NORMAL CONDITIONS UNTIL FURTHER NOTICE.

AYES: MS. TERNES, MR. OLSON, COMMISSIONER HAMM, COMMISSIONER GAEBE, MR. TRENBEATH, MR. LECH, MR. SANDAL, MS. SMITH, MR. GESSNER, AND LT. GOVERNOR WRIGLEY
NAYS: NONE
MOTION CARRIED
ABSENT: TREASURER SCHMIDT

Mr. Hunter also commented on the meetings with the ND Bankers Association (NDBA) representatives. The SIB's due diligence questionnaire was provided to the NDBA to allow North Dakota based investment firms an opportunity to elaborate on their backgrounds; specifically the firm's history, experience, size, and performance. The questionnaire is generally completed by all SIB investment managers on an annual basis. The information will serve to develop a better understanding of the North Dakota based investment firm's qualifications, experience, and areas of strength. Staff and Callan will be working with the North Dakota investment firms and applying all of the due diligence processes that are relevant to any investment manager of the SIB.

Audit Committee Report – Ms. Miller Bowley updated the SIB on the Audit Committee's activities as of May 21, 2015.

IT WAS MOVED BY MR. TRENBEATH AND SECONDED BY MR. SANDAL AND CARRIED BY A VOICE VOTE TO ACCEPT THE AUDIT REPORT AS PRESENTED.

AYES: COMMISSIONER HAMM, MS. TERNES, MR. OLSON, MR. SANDAL, MR. GESSNER, MS. SMITH, COMMISSIONER GAEBE, MR. LECH, MR. TRENBEATH, AND LT. GOVERNOR WRIGLEY
NAYS: NONE
MOTION CARRIED
ABSENT: TREASURER SCHMIDT

Governance Review - The Board received the second reading of the "Ends" policies. There were no modifications made to the policies. No action was taken.

The Board received the first reading of the "Investments" policies. The policies will be presented for a second reading at the next meeting.

MONITORING:

A "Watch List" as of March 31, 2015, was provided to the SIB. No action was taken.

OTHER:

Next scheduled meetings:

SIB Meeting – June 26, 2015, 8:30 a.m. – State Capitol, Peace Garden Room
SIB Audit Committee Meeting – September 25, 2015, 1:00 p.m. – State Capitol, Peace Garden Room

ADJOURNMENT:

With no further business to come before the SIB, Lt. Governor Wrigley adjourned the meeting at 10:48 a.m.

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Lt. Governor Wrigley, Chair
State Investment Board

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Bonnie Heit
Assistant to the Board

AGENDA ITEM III.A.

State Investment Board

Asset and Investment Performance Overview

June 19, 2015

Dave Hunter, Executive Director / CIO

Darren Schulz, Deputy Chief Investment Officer

ND Retirement & Investment Office (RIO)

State Investment Board (SIB)

State Investment Board – Client Assets Under Management

Fund Name	Market Values as of 4/30/15 (1)	Market Values as of 6/30/14 (2)	Market Values as of 4/30/14 (1)
Pension Trust Fund			
Public Employees Retirement System (PERS)	2,426,858,029	2,332,744,037	2,249,250,884
Teachers' Fund for Retirement (TFFR)	2,110,626,543	2,061,684,912	1,998,097,772
Job Service of North Dakota Pension	97,786,060	97,825,769	96,104,304
City of Bismarck Employees Pension	81,880,390	78,804,326	76,382,573
City of Grand Forks Employees Pension	56,545,187	57,896,611	53,188,539
City of Bismarck Police Pension	35,946,182	34,643,204	33,538,851
Grand Forks Park District	6,064,609	5,938,993	5,756,567
City of Fargo Employees Pension	1,470	9,702	35,175
Subtotal Pension Trust Fund	**4,815,708,470**	**4,669,547,555**	**4,512,354,666**
Insurance Trust Fund			
Legacy Fund	3,259,054,191	2,215,941,142	2,009,264,825
Workforce Safety & Insurance (WSI)	1,773,004,940	1,703,987,980	1,673,436,741
Budget Stabilization Fund	596,019,653	586,199,881	590,923,254
City of Fargo FargoDome Permanent Fund	41,875,148	41,775,992	39,591,287
PERS Group Insurance Account	40,704,421	37,425,567	38,825,872
State Fire and Tornado Fund	25,205,342	29,223,707	29,045,268
Petroleum Tank Release Compensation Fund	7,219,391	7,092,998	7,035,426
State Risk Management Fund	6,902,045	6,948,162	6,778,247
State Risk Management Workers Comp Fund	6,264,145	5,965,322	5,805,176
ND Association of Counties (NDACo) Fund	3,566,749	3,445,373	3,373,103
State Bonding Fund	3,208,073	3,268,991	3,240,441
Insurance Regulatory Trust Fund	2,658,625	1,146,038	1,126,691
ND Board of Medical Examiners	2,175,025	1,889,897	1,864,469
Bismarck Deferred Sick Leave Account	881,635	849,818	831,100
Cultural Endowment Fund	383,640	364,979	366,963
Subtotal Insurance Trust Fund	**5,769,123,023**	**4,645,525,847**	**4,411,508,863**
PERS Retiree Insurance Credit Fund	97,431,528	90,360,366	86,525,380
Total Assets Under SIB Management	**10,682,263,021**	**9,405,433,768**	**9,010,388,909**

(1) *4/30/15 and 4/30/14 market values are unaudited and subject to change.*

(2) *6/30/14 market values as stated in the Comprehensive Annual Financial Report.*

- SIB Client Assets Under Management grew by approximately 19% or $1.67 billion in the last year.
- The Pension Trust posted a net return of 7.3%, while the Insurance Trust generated a 4.9% net return in the last year. Investments were responsible for gains of $327 million for the Pension Trust and $217 million for the Insurance Trust.
- Legacy assets increased by 62% (or $1.3 billion) primarily due to tax collections, although net returns were 6.1% for the year ended April 30, 2015.
- SIB client assets exceeded $10.6 billion based on unaudited valuations as of April 30, 2015.

Strategic Initiatives – June 19, 2015 Update

RIO Budget Update (2Q) – The 64th Legislative Assembly reconvened on June 16th and approved Senate Bill 2022 including the biennial appropriation for RIO and PERS. Prior to this positive development, RIO and PERS obtained an Attorney General opinion which stated that RIO and PERS were authorized to make expenditures during the 2015-17 biennium. The AG Opinion stated, "it is my opinion that the express continuing appropriation authority granted these agencies combined with their independent legal obligations as fiduciaries of the plans they administer carry with them the implied authority to expend funds for the salaries and associated operating expenses of the individuals needed to effectuate those appropriations in order to fulfill their fiduciary obligations, to the extent the implied authority if not prohibited under state law. While I cannot, in a legal opinion, determine the amounts these agencies may expend pursuant to this implied authority, I will remind the governing Boards of these Agencies that they are and remain fiduciaries, and any expenditure of funds must be done prudently." The entire RIO team sincerely thanks the Office of the Attorney General for providing this favorable, timely and constructive guidance during a time of uncertainty.

Other Projects (2Q-3Q) – RIO continues to work with the Tobacco Prevention and Control Trust Fund (new client), Bank of North Dakota (Match Loan CD Program documentation enhancement), Land Board (jointly negotiated fee reductions and a review of operating synergies) and Risk Management (review of market leading risk management systems) among other projects.

Private Capital (3Q) - RIO commenced a review of our existing Timber, Infrastructure, Real Estate and Private Equity mandates in 2014 to confirm our investment approach to less liquid strategies, rationalize smaller investments, ease administrative reporting and identify potential fee savings. Over the next month, RIO intends to finalize successful contract negotiations with Timber Investment Resources with regards to the SIB's $116 million investment in Springbank. RIO will continue to review our existing Timber and Private Equity mandates during the second half of 2015.

Global Fixed Income (4Q) – RIO intends to complete a review of our existing fixed income strategies in mid- 2015 so as to confirm sector allocations in light of our long-term strategic goals and strong performance.

Governance and Board Education (Ongoing) – Each section of our Governance manual will be reviewed in detail during the first half of 2015 followed by a ½-day offsite in July so as to increase our overall awareness to pension governance trends and reconfirm our desire to maintain the existing governance model framework.

Legacy and Budget Stabilization Advisory Board Update

Background: On June 15, 2015, RIO updated the Legacy and Budget Stabilization Advisory Board on the status, asset allocation, fees and returns of the Legacy Fund and Budget Stabilization Fund.

Overview: In general, the Advisory Board appeared to be pleased with the overall investment performance of both funds which approximated 2.0% for the Budget Stabilization Fund and 5.7% for the Legacy Fund given that the actual returns of both funds exceeded their respective performance benchmarks (by approximately 1% and 0.33%, respectively).

Key Points/Take-Away: The Chairman of the Advisory expressed a concern about the liquidity requirements of the Budget Stabilization Fund noting it is intended to serve as a "rainy day fund". RIO acknowledged that liquidity is critical for the Budget Stabilization Fund and noted that over 80% of this funds current investments could be fully liquidated in 10-to-20 business days thereby substantially mitigating this liquidity concern. RIO also noted that it is currently reviewing the existing terms of the Bank of North Dakota Match Loan CD Program and intends to enhance documentation standards to clarify existing terms and further mitigate investment risks including duration, liquidity and credit risks.

Follow-Up: After the presentation, RIO provided the Advisory Board with investment manager performance metrics as of March 31 and April 30, 2015, and provided website links which can be used to easily access this information in the future. (A copy of which is attached along with the Advisory Board presentation materials.)

Legacy and Budget Stabilization Fund Advisory Board

June 15, 2015

Dave Hunter, Executive Director/Chief Investment Officer

Darren Schulz, Deputy Chief Investment Officer

ND Retirement & Investment Office (RIO)

State Investment Board (SIB)

Presentation Agenda

- Budget Stabilization Fund
  - Funding and disbursement history
  - Strategic asset allocation
  - Investment performance
  - Fund manager structure
- Legacy Fund
  - Policy timeline
  - Funding and disbursement history
  - Monthly contributions and market value
  - New policy allocation implementation update
  - Investment performance
  - Fund manager structure

Budget Stabilization Fund
Funding and Disbursement History

Budget Stabilization Fund

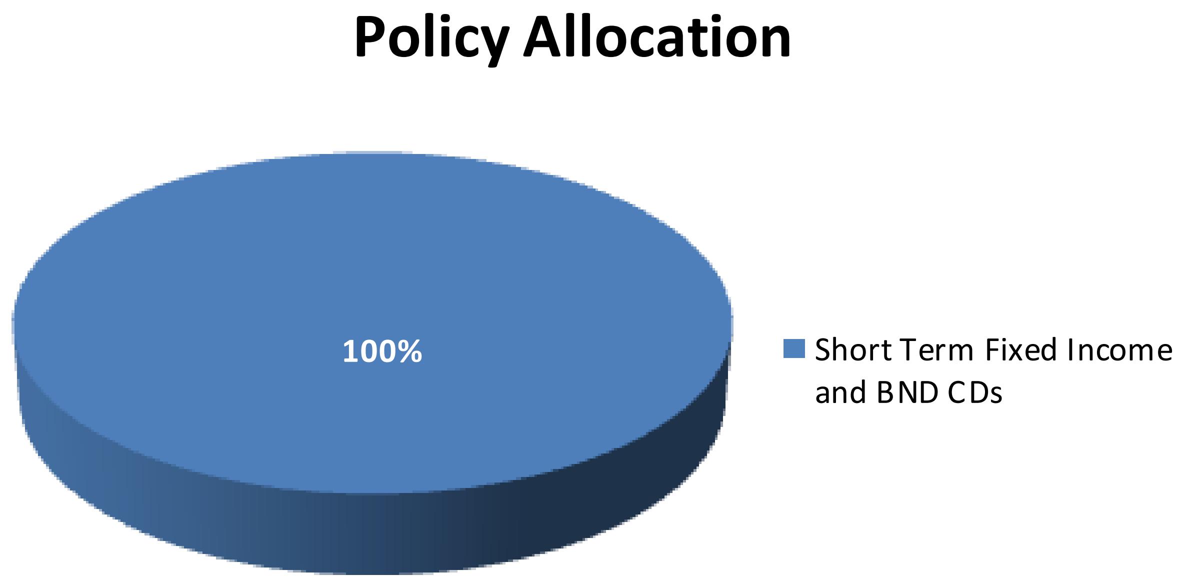
Through March 31, 2015

	New Money In	Net Increase	Income Distributions Out	Net Assets End of Period
FY2006 (Initial Funding - Sept. 2005)	99,472,631	3,611,730	(3,207,845)	99,876,516
FY2007	-	4,980,987	(4,981,500)	99,876,003
FY2008	100,527,369	122,430	(1,688,532)	198,837,270
FY2009	-	(8,736,058)	-	190,101,212
FY2010	124,936,548	21,464,258	(11,385,172)	325,116,846
FY2011	-	12,031,101	(11,474,863)	325,673,084
FY2012	61,414,562	7,867,160	-	394,954,806
FY2013	-	7,239,388	(1,036,797)	401,157,397
FY2014	181,060,584	10,966,393	(7,183,404)	586,000,970
FY2015	-	8,938,874	-	594,939,844
	567,411,694	68,486,263	(40,958,113)	

Net Increase - Inception to Date	68,486,263
Income Distributions Taken	(40,958,113)
Income Retained in Fund	27,528,150
March 31, 2015 MV	595,135,717

Note: Amounts are preliminary, unaudited and subject to change.

Budget Stabilization Fund Strategic Asset Allocation



Budget Stabilization Fund Performance as of 3/31/15

	1 Year	2 Year	3 Years	5 Years	7 Years	Since Inception*
Total Budget Stabilization Fund (Net)	2.04%	1.75%	1.97%	2.34%	2.23%	2.36%
Total Budget Stabilization Fund Policy	0.82%	0.57%	0.55%	0.40%	0.48%	1.57%
Excess Return	1.22%	1.18%	1.42%	1.94%	1.75%	0.79%

** Inception date: October 1, 2005*

Note: Fund performance are net of fees and unaudited and subject to change.
Source: Callan

Budget Stabilization Fund Manager Structure

	3/31/2015 Market Value	Actual Weight	Policy Weight
TOTAL BUDGET STABILIZATION FUND	**595,135,716**	**100.0%**	**100.0%**
BANK OF NORTH DAKOTA CDs	***102,767,901***	***17.3%***	***17.3%***
CASH EQUIVALENTS			
Northern Trust	7,336,677	1.2%	1.2%
TOTAL CASH EQUIVALENTS	**7,336,677**	**1.2%**	**1.2%**
SHORT TERM FIXED INCOME			
Babson Capital	244,224,152	41.0%	40.7%
JP Morgan	240,806,986	40.5%	40.7%
TOTAL SHORT TERM FIXED INCOME	**485,031,138**	**81.5%**	**81.5%**

NOTE: Monthly market values are preliminary and subject to change.

Budget Stabilization Fund
Schedule of Investment Fees

	FY 2014				FY 2013			
	Average Market Value	Fees in $	Fees in %	Contribution to Total Fees	Average Market Value	Fees in $	Fees in %	Contribution to Total Fees
Investment managers' fees:								
Short-term fixed income managers	466,375,734	507,502	0.11%	0.11%	295,529,418	353,973	0.12%	0.12%
Cash & equivalents managers	16,402,731	21,324	0.13%	0.00%	6,118,743	-	0.00%	0.00%
Total investment managers' fees	**482,778,465**	**528,824**	**0.11%**		**301,648,161**	**353,973**	**0.12%**	
Custodian fees		49,602	0.01%	0.01%		40,672	0.01%	0.01%
Investment consultant fees		17,623	0.00%	0.00%		12,539	0.00%	0.00%
Total investment expenses		**596,049**	**0.12%**			**407,183**	**0.13%**	

	FY 2014	FY 2013
Actual Investment Performance (Net of Fees)	**1.94%**	**1.87%**
Policy Benchmark	**0.61%**	**0.29%**
Outperformance	**1.33%**	**1.58%**

Note: Investment fees approximated **0.12%** for the prior fiscal year ended June 30, 2014.

Legacy Fund Policy Timeline

April 2013

- New strategic asset allocation for the Legacy Fund approved

June 2013

- SIB approved a transition plan to fully implement the new policy allocation over a period of 18 months

July 2013

- SIB approved the implementation of the new policy allocation through the use of existing managers within the Insurance Trust

August 2013

- RIO initiated the 18 month transition plan

January 2015

- Transition to new policy allocation fully implemented

Legacy Fund
Funding and Disbursement History

Legacy Fund

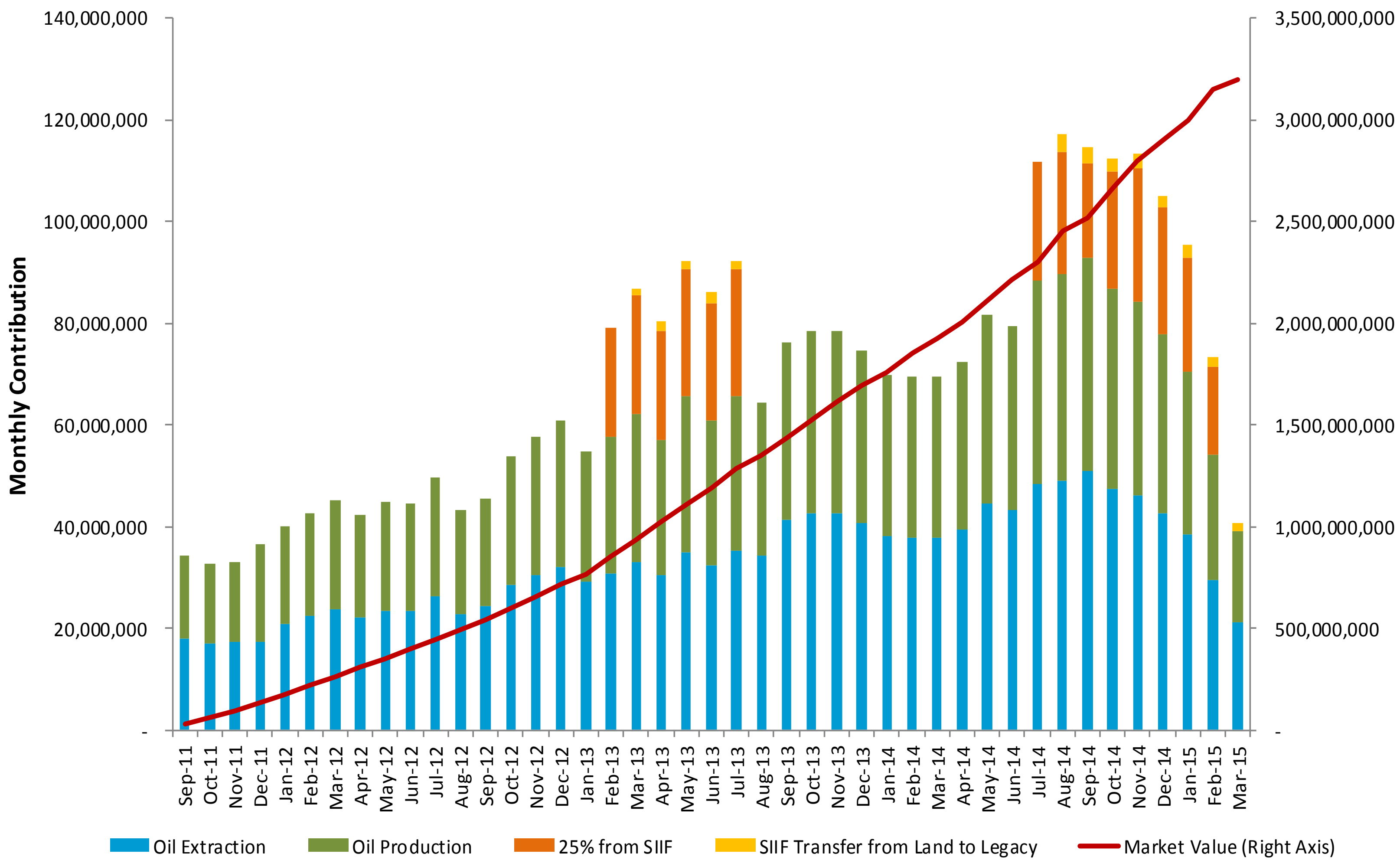
Through March 31, 2015

	New Money In	Net Increase	Income Distributions Out	Net Assets End of Period
FY2012 (Initial Funding - Sept. 2011)	396,585,658	2,300,225	-	398,885,883
FY2013	791,126,479	4,216,026	-	1,194,228,388
FY2014	907,214,971	113,153,662	-	2,214,597,021
FY2015	884,170,495	94,678,740	-	3,193,446,256
	2,979,097,603	214,348,653	-	

Net Increase - Inception to Date	214,348,653
Income Distributions Taken	-
Income Retained in Fund	214,348,653
March 31, 2015 MV	3,194,769,809

Note: Amounts are preliminary, unaudited and subject to change.

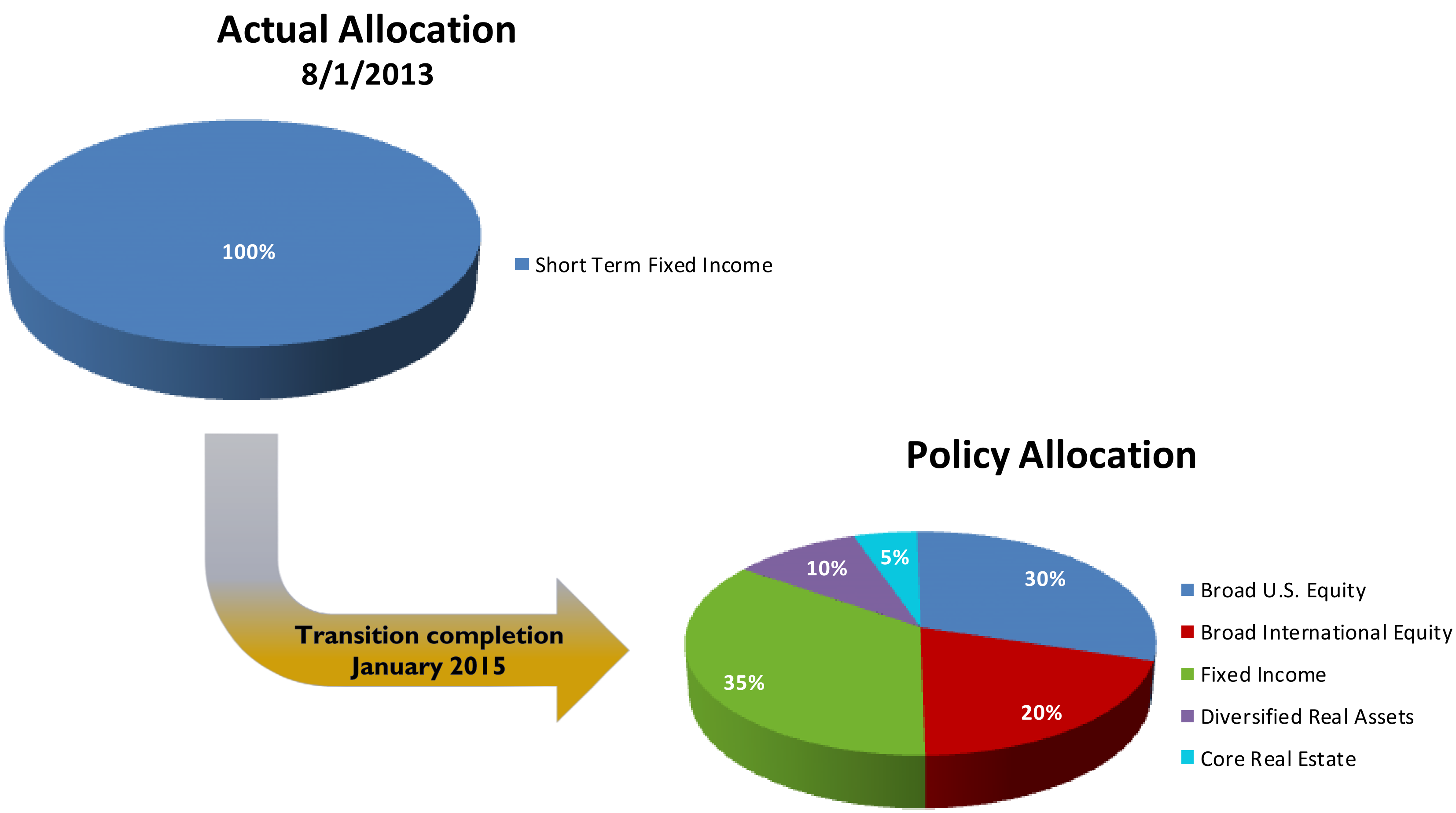
Legacy Fund
Monthly Contributions and Total Market Value



Source: Office of North Dakota State Treasurer

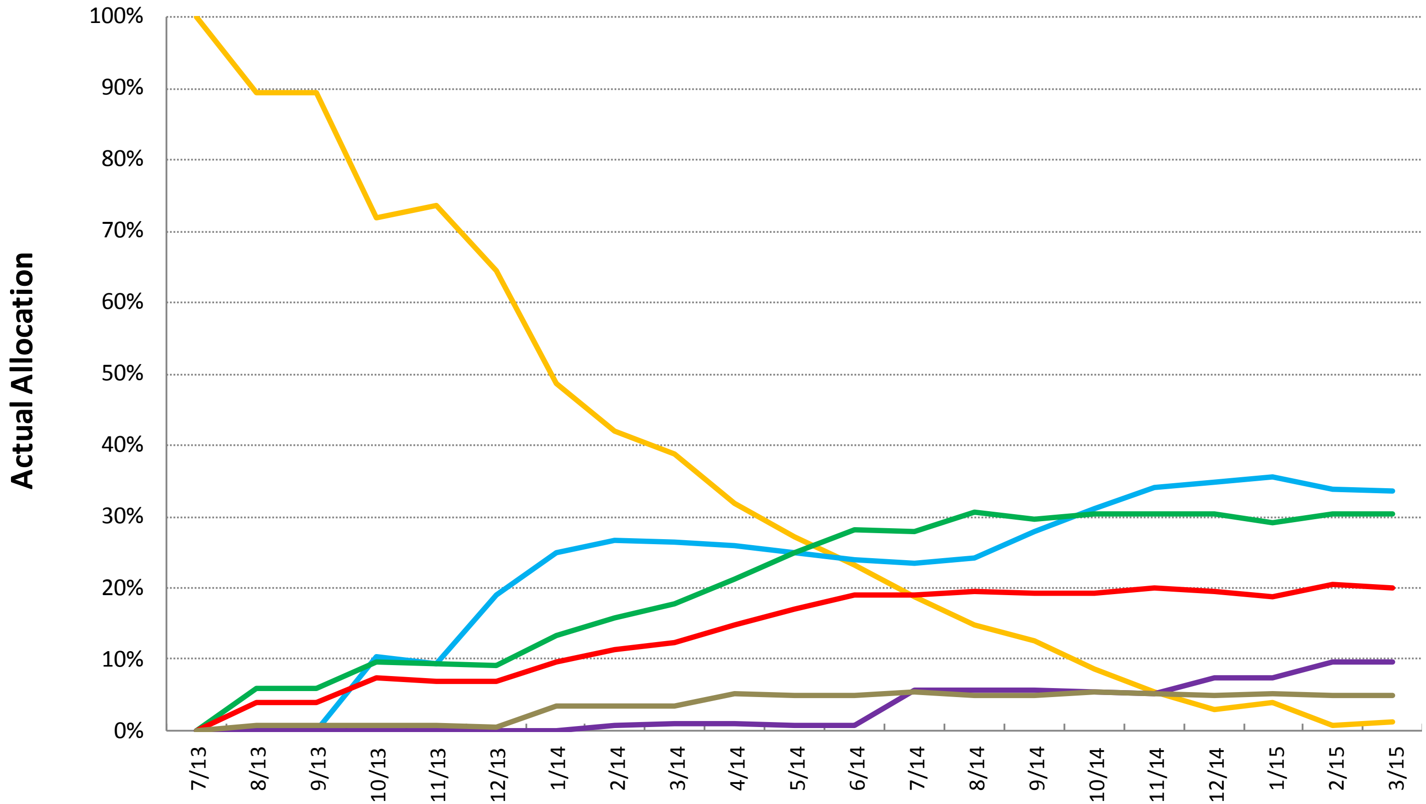
Note: Amounts are preliminary, unaudited and subject to change.

Legacy Fund Strategic Asset Allocation



Note: Amounts are preliminary, unaudited and subject to change.

Legacy Fund Transition Plan



	7/13	8/13	9/13	10/13	11/13	12/13	1/14	2/14	3/14	4/14	5/14	6/14	7/14	8/14	9/14	10/14	11/14	12/14	1/15	2/15	3/15
Short-Term Fixed/Cash	100%	89%	89%	72%	74%	64%	49%	42%	39%	32%	27%	23%	19%	15%	12%	9%	5%	3%	4%	1%	1%
Broad Fixed Income	0%	0%	0%	10%	9%	19%	25%	27%	27%	26%	25%	24%	23%	24%	28%	31%	34%	35%	36%	34%	34%
US Equity	0%	6%	6%	10%	10%	9%	13%	16%	18%	21%	25%	28%	28%	31%	30%	30%	30%	30%	29%	30%	30%
Non-US Equity	0%	4%	4%	7%	7%	7%	10%	11%	12%	15%	17%	19%	19%	20%	19%	19%	20%	20%	19%	21%	20%
Diversified Real Assets	0%	0%	0%	0%	0%	0%	0%	1%	1%	1%	1%	1%	6%	6%	6%	5%	5%	7%	8%	10%	10%
Core Real Estate	0%	1%	1%	1%	1%	1%	4%	3%	3%	5%	5%	5%	5%	5%	5%	5%	5%	5%	5%	5%	5%

Legacy Fund Performance as of 3/31/15

	1 Year	2 Years	3 Years	Since Inception*
Total Legacy Fund (Net)	5.72%	4.73%	3.76%	3.42%
Total Legacy Fund Policy	5.39%	4.15%	2.97%	2.55%
Excess Return	0.33%	0.58%	0.79%	0.87%

** Inception date: October 1, 2011*

Note: Fund performance are net of fees, unaudited and subject to change.
Source: Callan

Legacy Fund Manager Structure

	3/31/2015 Market Value	Allocation Actual	Allocation Policy
TOTAL LEGACY FUND	**3,194,769,809**	**100.0%**	**100.0%**
LARGE CAP DOMESTIC EQUITY			
Los Angeles Capital (Growth)	215,038,068	6.7%	6.6%
LSV	211,420,771	6.6%	6.6%
Los Angeles Capital (Enhanced Core)	141,616,596	4.4%	4.4%
Clifton Group	140,324,506	4.4%	4.4%
TOTAL LARGE CAP DOMESTIC EQUITY	***708,399,941***	***22.2%***	***22.0%***
SMALL CAP DOMESTIC EQUITY			
Research Affiliates	86,309,721	2.7%	4.0%
Clifton	176,833,203	5.5%	4.0%
TOTAL SMALL CAP DOMESTIC EQUITY	***263,142,924***	***8.2%***	***8.0%***
INTERNATIONAL EQUITY			
Capital Group	254,045,516	8.0%	8.0%
LSV	256,497,055	8.0%	8.0%
DFA	64,291,680	2.0%	2.0%
Vanguard	65,735,413	2.1%	2.0%
TOTAL INTERNATIONAL EQUITY	***640,569,665***	***20.1%***	***20.0%***
FIXED INCOME			
Western Asset	349,582,566	10.9%	11.4%
Prudential	86,860,421	2.7%	2.8%
PIMCO (DiSCO)	40,878,015	1.3%	1.3%
PIMCO (BRAVO II)	15,141,639	0.5%	0.5%
Declaration (Total Return)	86,638,228	2.7%	2.7%
State Street	148,512,691	4.6%	4.9%
Wells Capital	347,530,745	10.9%	11.4%
TOTAL FIXED INCOME	***1,075,144,306***	***33.7%***	***35.0%***

	3/31/2015 Market Value	Allocation Actual	Allocation Policy
DIVERSIFIED REAL ASSETS			
Western Global TIPS	231,391,136	7.2%	7.6%
Grosvenor CIS II	1,968,559	0.1%	0.1%
JP Morgan (Infrastructure)	75,000,000	2.3%	2.3%
TOTAL DIVERSIFIED REAL ASSETS	***308,359,695***	***9.7%***	***10.0%***
REAL ESTATE			
JP Morgan	84,506,477	2.6%	2.5%
Invesco	74,554,166	2.3%	2.5%
TOTAL REAL ESTATE	***159,060,643***	***5.0%***	***5.0%***
CASH EQUIVALENTS			
Northern Trust (1)	39,796,990		
TOTAL CASH EQUIVALENTS	***39,796,990***	***1.2%***	***0.0%***
90 Day T-Bill			
SHORT TERM FIXED INCOME			
Babson Capital	295,646	0.0%	0.0%
TOTAL SHORT TERM FIXED INCOME	***295,646***	***0.0%***	***0.0%***

NOTE: Monthly returns and market values are preliminary and subject to change.

Legacy Fund
Schedule of Investment Fees

	FY 2014				FY 2013			
	Average Market Value	Fees in $	Fees in %	Contribution to Total Fees	Average Market Value	Fees in $	Fees in %	Contribution to Total Fees
Investment managers' fees:								
Domestic large cap equity managers	221,898,125	502,317	0.23%	0.03%	-	-	0.00%	0.00%
Domestic small cap equity managers	80,140,583	350,670	0.44%	0.02%	-	-	0.00%	0.00%
International equity managers	208,777,033	884,793	0.42%	0.05%	-	-	0.00%	0.00%
Domestic fixed income managers	341,169,338	1,199,773	0.35%	0.07%	-	-	0.00%	0.00%
Diversified real assets managers	8,725,730	33,040	0.38%	0.00%	-	-	0.00%	0.00%
Real estate managers	48,719,775	490,567	1.01%	0.03%	-	-	0.00%	0.00%
Short-term fixed income managers	854,086,155	1,053,958	0.12%	0.06%	847,626,340	881,957	0.10%	0.10%
Cash & equivalents managers	57,174,100	60,350	0.11%	0.00%	49,301	-	0.00%	0.00%
Total investment managers' fees	**1,820,690,839**	**4,575,468**	**0.25%**		**847,675,641**	**881,957**	**0.10%**	
Custodian fees		216,970	0.01%	0.01%		84,539	0.01%	0.01%
Investment consultant fees		68,630	0.00%	0.00%		104,210	0.01%	0.01%
Total investment expenses		**4,861,068**	**0.27%**			**1,070,706**	**0.13%**	
Performance Fees Paid								
Clifton		177,470				-		
PIMCO DiSCO		609,117				-		
Grosvenor (formerly Credit Suisse)		(3,076)				-		
Total Performance Fees Paid		**783,511**	**0.04%**			**-**	**0.00%**	
Actual Investment Performance (Net of Fees)			**6.64%**				**1.17%**	
Policy Benchmark			**5.54%**				**0.34%**	
Outperformance			**1.10%**				**0.83%**	

Note: Investment fees approximated **0.27%** in the prior fiscal year ended June 30, 2014.

Legacy & Budget Stabilization Fund Investment Manager Performance Links

Dear Legacy and Budget Stabilization Fund Advisory Board Members:

Per our advisory board meeting yesterday morning, I am forwarding RIO website links relating to investment manager performance for the Legacy Fund and Budget Stabilization Fund.

I am forwarding links for the two most recent month ends which are available at this time. We intend to include these 2-page summaries for each fund in future meetings.

I sincerely appreciate your continued support and look forward to addressing any questions or comments on the attached materials or any other related items.

Legacy Fund Performance – March 31, 2015

http://www.nd.gov/rio/RIO_ref/performance/Legacy/201503.pdf

Legacy Fund Performance – April 30, 2015

http://www.nd.gov/rio/RIO_ref/performance/Legacy/201504.pdf

Budget Stabilization Fund Performance – March 31, 2015

http://www.nd.gov/rio/RIO_ref/performance/budget/201503.pdf

Budget Stabilization Fund Performance – April 30, 2015

http://www.nd.gov/rio/RIO_ref/performance/budget/201504.pdf

Advisory Board Follow-Up Request:
This email was sent to the Advisory Board on the morning after our June 15, 2015 meeting to address underlying investment manager performance for each fund.

As noted in our meeting yesterday, the Legacy Fund and Budget Stabilization Fund are performing significantly better than our underlying performance benchmarks. The Legacy Fund generated a net investment return of 5.72% for the one-year period ended March 31, 2015, which exceeds its benchmark index by 1/3 of 1% (or 0.33%). The Budget Stabilization Fund is also performing well and generated a net investment return of 2.04% for the year ended March 31, 2015, which also exceeded its performance benchmark by a significant margin.

LEGACY FUND
INVESTMENT PERFORMANCE REPORT AS OF MARCH 31, 2015

	March-15					December-14					September-14					Current FYTD Returns		Prior Year FY14 Returns	
		Allocation		Quarter			Allocation		Quarter			Allocation		Quarter					
	Market Value	Actual	Policy	Gross(1)	Net	Market Value	Actual	Policy	Gross(1)	Net	Market Value	Actual	Policy	Gross(1)	Net	Gross(1)	Net	Gross(1)	Net
TOTAL LEGACY FUND	**3,194,769,809**	**100.0%**	**100.0%**	**2.89%**	**2.83%**	**2,900,880,837**	**100.0%**	**100.0%**	**2.12%**	**2.07%**	**2,516,568,041**	**100.0%**	**100.0%**	**-1.71%**	**-1.77%**	**3.27%**	**3.10%**	**6.83%**	**6.64%**
POLICY TARGET BENCHMARK				*2.38%*	*2.38%*				*1.80%*	*1.80%*				*-1.60%*	*-1.60%*	*2.56%*	*2.56%*	*5.54%*	*5.54%*
ATTRIBUTION ANALYSIS																			
Asset Allocation				**-0.08%**	**-0.08%**				**0.00%**	**0.00%**				**0.00%**	**0.00%**	**-0.08%**	**-0.08%**	**-0.01%**	**-0.01%**
Manager Selection				**0.58%**	**0.52%**				**0.32%**	**0.27%**				**-0.12%**	**-0.17%**	**0.79%**	**0.63%**	**1.30%**	**1.11%**
TOTAL RELATIVE RETURN				0.50%	0.44%				0.32%	0.27%				-0.12%	-0.17%	0.71%	0.54%	1.29%	1.10%
LARGE CAP DOMESTIC EQUITY																			
Los Angeles Capital	215,038,068	6.7%	6.6%	4.73%	4.68%	191,045,943	6.6%	6.6%	5.47%	5.42%	166,097,064	6.6%	6.6%	1.58%	1.54%	12.20%	12.05%	N/A	N/A
Russell 1000 Growth				***3.84%***	***3.84%***				***4.78%***	***4.78%***				***1.49%***	***1.49%***	***10.42%***	***10.42%***		
LSV	211,420,771	6.6%	6.6%	1.00%	0.92%	193,231,379	6.7%	6.6%	5.54%	5.46%	165,327,913	6.6%	6.6%	-0.46%	-0.52%	6.10%	5.89%	N/A	N/A
Russell 1000 Value				***-0.72%***	***-0.72%***				***4.98%***	***4.98%***				***-0.19%***	***-0.19%***	***4.02%***	***4.02%***		
Los Angeles Capital	141,616,596	4.4%	4.4%	***2.44%***	***2.41%***	128,032,469	4.4%	4.4%	***5.25%***	***5.22%***	110,457,407	4.4%	4.4%	***0.86%***	***0.83%***	8.75%	8.65%	N/A	N/A
Russell 1000				***1.59%***	***1.59%***				***4.88%***	***4.88%***				***0.65%***	***0.65%***	***7.25%***	***7.25%***		
Clifton Group	140,324,506	4.4%	4.4%	1.15%	1.15%	128,045,122	4.4%	4.4%	5.15%	5.15%	111,649,309	4.4%	4.4%	1.18%	1.11%	7.61%	7.54%	N/A	N/A
S&P 500				***0.95%***	***0.95%***				***4.93%***	***4.93%***				***1.13%***	***1.13%***	***7.13%***	***7.13%***		
TOTAL LARGE CAP DOMESTIC EQUITY	***708,399,941***	***22.2%***	***22.0%***	***2.37%***	***2.33%***	***640,354,913***	***22.1%***	***22.0%***	***5.50%***	***5.46%***	***553,531,693***	***22.0%***	***22.0%***	***0.62%***	***0.57%***	***8.67%***	***8.52%***	***N/A***	***N/A***
Russell 1000				***1.59%***	***1.59%***				***4.88%***	***4.88%***				***0.65%***	***0.65%***	***7.25%***	***7.25%***		
SMALL CAP DOMESTIC EQUITY																			
Research Affiliates	86,309,721	2.7%	4.0%	2.64%	2.56%	70,004,841	2.4%	4.0%	10.52%	10.44%	60,470,490	2.4%	3.8%	-7.00%	-7.07%	5.50%	5.25%	N/A	N/A
Clifton	176,833,203	5.5%	4.0%	4.99%	4.99%	168,529,618	5.8%	4.0%	10.44%	10.44%	129,761,488	5.2%	3.8%	-7.23%	-7.41%	7.57%	7.36%	N/A	N/A
TOTAL SMALL CAP DOMESTIC EQUITY	***263,142,924***	***8.2%***	***8.0%***	***4.27%***	***4.25%***	***238,534,459***	***8.2%***	***8.0%***	***10.46%***	***10.44%***	***190,231,978***	***7.6%***	***7.6%***	***-7.15%***	***-7.29%***	***6.95%***	***6.74%***	***N/A***	***N/A***
Russell 2000				***4.32%***	***4.32%***				***9.73%***	***9.73%***				***-7.36%***	***-7.36%***	***6.04%***	***6.04%***		
INTERNATIONAL EQUITY																			
Capital Group	254,045,516	8.0%	8.0%	3.84%	3.74%	227,657,125	7.8%	8.0%	-1.43%	-1.52%	196,357,964	7.8%	7.7%	-5.78%	-5.86%	-3.56%	-3.82%	N/A	N/A
LSV	256,497,055	8.0%	8.0%	5.28%	5.17%	225,288,693	7.8%	8.0%	-3.60%	-3.70%	194,250,108	7.7%	7.7%	-6.45%	-6.53%	-5.04%	-5.33%	N/A	N/A
MSCI EAFE				***4.88%***	***4.88%***				***-3.57%***	***-3.57%***				***-5.88%***	***-5.88%***	***-4.81%***	***-4.81%***		
DFA	64,291,680	2.0%	2.0%	4.68%	4.68%	56,897,869	2.0%	2.0%	-3.97%	-3.97%	48,150,927	1.9%	1.9%	-8.53%	-8.53%	-8.04%	-8.04%	N/A	N/A
Vanguard (1)	65,735,413	2.1%	2.0%	7.29%	7.29%	57,035,986	2.0%	2.0%	-3.50%	-3.50%	48,775,291	1.9%	1.9%	-5.84%	-5.84%	-2.52%	-2.52%	N/A	N/A
S&P/Citigroup BMI EPAC < $2BN				***6.19%***	***6.19%***				***-4.44%***	***-4.44%***				***-5.94%***	***-5.94%***	***-4.55%***	***-4.55%***		
TOTAL INTERNATIONAL EQUITY	***640,569,665***	***20.1%***	***20.0%***	***4.89%***	***4.80%***	***566,879,673***	***19.5%***	***20.0%***	***-2.73%***	***-2.81%***	***487,534,290***	***19.4%***	***19.4%***	***-6.41%***	***-6.48%***	***-4.52%***	***-4.74%***	***N/A***	***N/A***
MSCI EAFE				***4.88%***	***4.88%***				***-3.57%***	***-3.57%***				***-5.88%***	***-5.88%***	***-4.81%***	***-4.81%***		
FIXED INCOME																			
Western Asset	349,582,566	10.9%	11.4%	2.26%	2.23%	327,529,166	11.3%	11.3%	1.63%	1.60%	224,061,194	8.9%	8.9%	0.36%	0.32%	4.30%	4.20%	N/A	N/A
Prudential	86,860,421	2.7%	2.8%	2.50%	2.42%	81,921,935	2.8%	2.8%	1.97%	1.90%	56,647,412	2.3%	2.2%	-0.31%	-0.38%	4.19%	3.97%	N/A	N/A
PIMCO (DiSCO) (1)	40,878,015	1.3%	1.3%	1.55%	1.55%	39,412,622	1.4%	1.4%	-0.35%	-0.35%	32,793,038	1.3%	1.3%	1.43%	1.43%	2.65%	2.65%	N/A	N/A
PIMCO (BRAVO II) (1)	15,141,639	0.5%	0.5%	1.43%	1.43%	12,071,168	0.4%	0.4%	3.49%	3.49%	7,566,995	0.3%	0.3%	0.00%	0.00%	4.96%	4.96%	N/A	N/A
BC Aggregate				***1.61%***	***1.61%***				***1.78%***	***1.78%***				***0.17%***	***0.17%***	***3.59%***	***3.59%***		

LEGACY FUND
INVESTMENT PERFORMANCE REPORT AS OF MARCH 31, 2015

	March-15					December-14					September-14					Current FYTD Returns		Prior Year FY14 Returns	
		Allocation		Quarter			Allocation		Quarter			Allocation		Quarter					
	Market Value	Actual	Policy	Gross(1)	Net	Market Value	Actual	Policy	Gross(1)	Net	Market Value	Actual	Policy	Gross(1)	Net	Gross(1)	Net	Gross(1)	Net
Declaration (Total Return) (1)	86,638,228	2.7%	2.7%	1.77%	1.77%	77,893,283	2.7%	2.7%	0.99%	0.99%	58,399,014	2.3%	2.3%	0.65%	0.65%	3.45%	3.45%	N/A	N/A
3m LIBOR				***0.07%***	***0.07%***				***0.06%***	***0.06%***				***0.06%***	***0.06%***	***0.18%***	***0.18%***		
State Street	148,512,691	4.6%	4.9%	1.85%	1.84%	143,035,239	4.9%	4.9%	1.83%	1.82%	99,390,152	3.9%	3.9%	0.16%	0.15%	3.88%	3.86%	N/A	N/A
BC Gov/Credit				***1.84%***	***1.84%***				***1.80%***	***1.80%***				***0.17%***	***0.17%***	***3.85%***	***3.85%***		
Wells Capital	347,530,745	10.9%	11.4%	2.56%	2.51%	327,940,491	11.3%	11.3%	1.59%	1.55%	224,945,343	8.9%	8.9%	-0.12%	-0.17%	4.06%	3.92%	N/A	N/A
BC Credit Baa				***2.32%***	***2.32%***				***1.26%***	***1.26%***				***-1.60%***	***-1.60%***	***1.95%***	***1.95%***		
TOTAL FIXED INCOME	***1,075,144,306***	***33.7%***	***35.0%***	***2.24%***	***2.21%***	***1,009,803,904***	***34.8%***	***34.8%***	***1.55%***	***1.52%***	***703,803,147***	***28.0%***	***28.0%***	***0.20%***	***0.16%***	***4.03%***	***3.93%***	***N/A***	***N/A***
BC Aggregate				***1.61%***	***1.61%***				***1.78%***	***1.78%***				***0.17%***	***0.17%***	***3.59%***	***3.59%***		
DIVERSIFIED REAL ASSETS																			
Western	231,391,136	7.2%	7.6%	0.21%	0.18%	211,717,138	7.3%	7.3%	-0.43%	-0.46%	141,601,650	5.6%	5.6%	-2.09%	-2.13%	-2.31%	-2.41%	N/A	N/A
BC Global Inflation Linked Index				***-1.53%***	***-1.53%***				-0.14%	-0.14%				-2.76%	-2.76%	***-4.38%***	***-4.38%***		
Grosvenor CIS II	1,968,559	0.1%	0.1%	N/A	N/A	-	0.0%	0.0%	N/A	NA	-	0.0%	0.0%	N/A	N/A	N/A	N/A	N/A	N/A
JP Morgan (Infrastructure)	75,000,000	2.3%	2.3%	N/A	N/A	-	0.0%	0.0%	N/A	NA	-	0.0%	0.0%	N/A	N/A	N/A	N/A	N/A	N/A
CPI																			
TOTAL DIVERSIFIED REAL ASSETS	***308,359,695***	***9.7%***	***10.0%***	***0.39%***	***0.37%***	***211,717,138***	***7.3%***	***7.3%***	***-0.43%***	***-0.46%***	***141,601,651***	***5.6%***	***5.6%***	***-2.10%***	***-2.11%***	***-2.14%***	***-2.21%***	***N/A***	***N/A***
Benchmark				***-1.10%***	***-1.10%***				***-0.14%***	***-0.14%***				***-2.76%***	***-2.76%***	***-3.96%***	***-3.96%***		
REAL ESTATE																			
JP Morgan	84,506,477	2.6%	2.5%	5.97%	5.40%	78,672,478	2.7%	2.5%	3.84%	3.57%	72,301,896	2.9%	2.5%	0.00%	0.04%	10.04%	9.21%	N/A	N/A
Invesco	74,554,166	2.3%	2.5%	3.28%	3.19%	66,827,989	2.3%	2.5%	3.50%	3.40%	53,323,533	2.1%	2.5%	3.44%	3.35%	10.57%	10.27%	N/A	N/A
TOTAL REAL ESTATE	***159,060,643***	***5.0%***	***5.0%***	***4.69%***	***4.35%***	***145,500,467***	***5.0%***	***5.0%***	***3.69%***	***3.50%***	***125,625,429***	***5.0%***	***5.0%***	***1.43%***	***1.41%***	***10.10%***	***9.53%***	***N/A***	***N/A***
NCREIF Total Index				***3.57%***	***3.57%***				***3.04%***	***3.04%***				***2.63%***	***2.63%***	***9.54%***	***9.54%***		
CASH EQUIVALENTS																			
Northern Trust (1)	39,796,990			0.00%	0.00%	11,440,987			0.00%	0.00%	2,572,819			0.00%	0.00%	0.01%	0.01%	0.01%	0.01%
TOTAL CASH EQUIVALENTS	***39,796,990***	***1.2%***	***0.0%***	***0.00%***	***0.00%***	***11,440,987***	***0.4%***	***0.0%***	***0.00%***	***0.00%***	***2,572,819***	***0.1%***	***0.0%***	***0.00%***	***0.00%***	***0.01%***	***0.01%***	***0.01%***	***0.01%***
90 Day T-Bill				***0.01%***	***0.01%***				***0.00%***	***0.00%***				***0.01%***	***0.01%***	***0.02%***	***0.02%***	***0.06%***	***0.06%***
SHORT TERM FIXED INCOME																			
Babson Capital	295,646	0.0%	0.0%	N/A	N/A	43,642,546	1.5%	1.4%	0.45%	0.38%	172,382,049	6.8%	6.2%	0.28%	0.23%	N/A	N/A	2.82%	2.65%
BC 1-3 Year US Gov't Index									***0.19%***	***0.19%***				***0.03%***	***0.03%***			***0.77%***	***0.77%***
JP Morgan	-	0.0%	0.0%	N/A	N/A	33,006,749	1.1%	1.4%	0.04%	0.04%	139,284,985	5.5%	6.2%	0.04%	-0.04%	N/A	N/A	1.36%	1.24%
BC 1-3 Year Gov/Credit Index									***0.17%***	***0.17%***				***0.04%***	***0.04%***			***1.14%***	***1.14%***
TOTAL SHORT TERM FIXED INCOME	***295,646***	***0.0%***	***0.0%***	***N/A***	***N/A***	***76,649,296***	***2.6%***	***2.9%***	***0.25%***	***0.21%***	***311,667,035***	***12.4%***	***12.5%***	***0.16%***	***0.10%***	***N/A***	***N/A***	***2.10%***	***1.95%***
BC 1-3 Year US Gov't Index									***0.19%***	***0.19%***				***0.03%***	***0.03%***			***0.77%***	***0.77%***

Initial funding September 7, 2011.
NOTE: Monthly returns and market values are preliminary and subject to change.
Effective July 1, 2013, net of fee returns are calculated on a cash basis in the month paid. Prior years were accrual based and split evenly over the 12 months of the fiscal year.

(1) All limited partnership-type (and mutual funds as of 7/1/14) investment returns will only be reported net of fees, which is standard practice by the investment consultant.

LEGACY FUND
INVESTMENT PERFORMANCE REPORT AS OF APRIL 30, 2015

	April-15					March-15					December-14					September-14					Current FYTD		Prior Year FY14	
		Allocation		Month			Allocation		Quarter			Allocation		Quarter			Allocation		Quarter		Returns		Returns	
	Market Value	Actual	Policy	Gross[1]	Net	Market Value	Actual	Policy	Gross[1]	Net	Market Value	Actual	Policy	Gross[1]	Net	Market Value	Actual	Policy	Gross[1]	Net	Gross[1]	Net	Gross[1]	Net
TOTAL LEGACY FUND	**3,259,054,191**	**100.0%**	**100.0%**	**0.79%**	**0.77%**	**3,194,769,809**	**100.0%**	**100.0%**	***2.87%***	***2.81%***	**2,900,880,837**	**100.0%**	**100.0%**	***2.12%***	***2.07%***	**2,516,568,041**	**100.0%**	**100.0%**	***-1.71%***	***-1.77%***	**4.07%**	**3.88%**	**6.83%**	**6.64%**
POLICY TARGET BENCHMARK				*0.87%*	*0.87%*				*2.38%*	*2.38%*				*1.80%*	*1.80%*				*-1.60%*	*-1.60%*	*3.45%*	*3.45%*	*5.54%*	*5.54%*
ATTRIBUTION ANALYSIS																								
Asset Allocation				**0.00%**	**0.00%**				**-0.10%**	**-0.10%**				**0.00%**	**0.00%**				**0.00%**	**0.00%**	**-0.10%**	**-0.10%**	**-0.01%**	**-0.01%**
Manager Selection				**-0.07%**	**-0.09%**				**0.57%**	**0.52%**				**0.32%**	**0.27%**				**-0.12%**	**-0.17%**	**0.78%**	**0.62%**	**1.30%**	**1.11%**
TOTAL RELATIVE RETURN				-0.08%	-0.09%				0.48%	0.42%				0.32%	0.27%				-0.12%	-0.17%	0.61%	0.43%	1.29%	1.10%
LARGE CAP DOMESTIC EQUITY																								
Los Angeles Capital	213,162,713	6.5%	6.6%	-0.87%	-0.87%	215,038,068	6.7%	6.6%	4.73%	4.68%	191,045,943	6.6%	6.6%	5.47%	5.42%	166,097,064	6.6%	6.6%	1.58%	1.54%	11.22%	11.07%	N/A	N/A
Russell 1000 Growth				***0.50%***	***0.50%***				***3.84%***	***3.84%***				***4.78%***	***4.78%***				***1.49%***	***1.49%***	***10.98%***	***10.98%***		
LSV	212,906,547	6.5%	6.6%	0.77%	0.70%	211,420,771	6.6%	6.6%	1.00%	0.92%	193,231,379	6.7%	6.6%	5.54%	5.46%	165,327,913	6.6%	6.6%	-0.46%	-0.52%	6.92%	6.63%	N/A	N/A
Russell 1000 Value				***0.94%***	***0.94%***				***-0.72%***	***-0.72%***				***4.98%***	***4.98%***				***-0.19%***	***-0.19%***	***4.99%***	***4.99%***		
Los Angeles Capital	140,739,823	4.3%	4.4%	-0.62%	-0.62%	141,616,596	4.4%	4.4%	***2.44%***	***2.41%***	128,032,469	4.4%	4.4%	***5.25%***	***5.22%***	110,457,407	4.4%	4.4%	***0.86%***	***0.83%***	8.08%	7.97%	N/A	N/A
Russell 1000				***0.71%***	***0.71%***				***1.59%***	***1.59%***				***4.88%***	***4.88%***				***0.65%***	***0.65%***	***8.01%***	***8.01%***		
Clifton Group	141,860,563	4.4%	4.4%	1.10%	1.10%	140,324,506	4.4%	4.4%	1.15%	1.15%	128,045,122	4.4%	4.4%	5.15%	5.15%	111,649,309	4.4%	4.4%	1.18%	1.11%	8.79%	8.72%	N/A	N/A
S&P 500				***0.96%***	***0.96%***				***0.95%***	***0.95%***				***4.93%***	***4.93%***				***1.13%***	***1.13%***	***8.15%***	***8.15%***		
TOTAL LARGE CAP DOMESTIC EQUITY	***708,669,646***	***21.7%***	***22.0%***	***0.06%***	***0.04%***	***708,399,941***	***22.2%***	***22.0%***	***2.37%***	***2.33%***	***640,354,913***	***22.1%***	***22.0%***	***5.50%***	***5.46%***	***553,531,693***	***22.0%***	***22.0%***	***0.62%***	***0.57%***	***8.73%***	***8.56%***	***N/A***	***N/A***
Russell 1000				***0.71%***	***0.71%***				***1.59%***	***1.59%***				***4.88%***	***4.88%***				***0.65%***	***0.65%***	***8.01%***	***8.01%***		
SMALL CAP DOMESTIC EQUITY																								
Research Affiliates	84,739,990	2.6%	4.0%	-1.81%	-1.81%	86,309,721	2.7%	4.0%	2.36%	2.28%	70,004,841	2.4%	4.0%	10.52%	10.44%	60,470,490	2.4%	3.8%	-7.00%	-7.07%	3.31%	3.07%	N/A	N/A
Clifton	172,284,665	5.3%	4.0%	-2.57%	-2.57%	176,833,203	5.5%	4.0%	5.08%	5.08%	168,529,618	5.8%	4.0%	10.44%	10.44%	129,761,488	5.2%	3.8%	-7.23%	-7.41%	4.89%	4.69%	N/A	N/A
TOTAL SMALL CAP DOMESTIC EQUITY	***257,024,655***	***7.9%***	***8.0%***	***-2.32%***	***-2.32%***	***263,142,924***	***8.2%***	***8.0%***	***4.25%***	***4.23%***	***238,534,459***	***8.2%***	***8.0%***	***10.46%***	***10.44%***	***190,231,978***	***7.6%***	***7.6%***	***-7.15%***	***-7.29%***	***4.45%***	***4.24%***	***N/A***	***N/A***
Russell 2000				***-2.55%***	***-2.55%***				***4.32%***	***4.32%***				***9.73%***	***9.73%***				***-7.36%***	***-7.36%***	***3.34%***	***3.34%***		
INTERNATIONAL EQUITY																								
Capital Group	266,755,369	8.2%	8.0%	5.00%	5.00%	254,045,516	8.0%	8.0%	3.96%	3.86%	227,657,125	7.8%	8.0%	-1.43%	-1.52%	196,357,964	7.8%	7.7%	-5.78%	-5.86%	1.39%	1.11%	N/A	N/A
LSV	267,331,052	8.2%	8.0%	4.33%	4.22%	256,497,055	8.0%	8.0%	5.22%	5.10%	225,288,693	7.8%	8.0%	-3.60%	-3.70%	194,250,108	7.7%	7.7%	-6.45%	-6.53%	-0.99%	-1.40%	N/A	N/A
MSCI EAFE				***4.08%***	***4.08%***				***4.88%***	***4.88%***				***-3.57%***	***-3.57%***				***-5.88%***	***-5.88%***	***-0.92%***	***-0.92%***		
DFA	67,527,728	2.1%	2.0%	5.03%	5.03%	64,291,680	2.0%	2.0%	4.68%	4.68%	56,897,869	2.0%	2.0%	-3.97%	-3.97%	48,150,927	1.9%	1.9%	-8.53%	-8.53%	-3.42%	-3.42%	N/A	N/A
Vanguard (1)	68,004,714	2.1%	2.0%	3.45%	3.45%	65,735,413	2.1%	2.0%	7.29%	7.29%	57,035,986	2.0%	2.0%	-3.50%	-3.50%	48,775,291	1.9%	1.9%	-5.84%	-5.84%	0.85%	0.85%	N/A	N/A
S&P/Citigroup BMI EPAC < $2BN				***5.71%***	***5.71%***				***6.19%***	***6.19%***				***-4.44%***	***-4.44%***				***-5.94%***	***-5.94%***	***0.89%***	***0.89%***		
TOTAL INTERNATIONAL EQUITY	***669,618,863***	***20.5%***	***20.0%***	***4.58%***	***4.53%***	***640,569,665***	***20.1%***	***20.0%***	***4.87%***	***4.78%***	***566,879,673***	***19.5%***	***20.0%***	***-2.73%***	***-2.81%***	***487,534,290***	***19.4%***	***19.4%***	***-6.41%***	***-6.48%***	***-0.16%***	***-0.44%***	***N/A***	***N/A***
MSCI EAFE				***4.08%***	***4.08%***				***4.88%***	***4.88%***				***-3.57%***	***-3.57%***				***-5.88%***	***-5.88%***	***-0.92%***	***-0.92%***		
FIXED INCOME																								
Western Asset	352,652,316	10.8%	11.5%	-0.24%	-0.24%	349,582,566	10.9%	11.4%	2.26%	2.23%	327,529,166	11.3%	11.3%	1.63%	1.60%	224,061,194	8.9%	8.9%	0.36%	0.32%	4.05%	3.95%	N/A	N/A
Prudential	123,901,590	3.8%	2.8%	-0.44%	-0.49%	86,860,421	2.7%	2.8%	2.50%	2.42%	81,921,935	2.8%	2.8%	1.97%	1.90%	56,647,412	2.3%	2.2%	-0.31%	-0.38%	3.73%	3.46%	N/A	N/A
PIMCO (DiSCO) (1)	41,080,681	1.3%	1.3%	0.50%	0.50%	40,878,015	1.3%	1.3%	1.55%	1.55%	39,412,622	1.4%	1.4%	-0.35%	-0.35%	32,793,038	1.3%	1.3%	1.43%	1.43%	3.16%	3.16%	N/A	N/A
PIMCO (BRAVO II) (1)	15,554,001	0.5%	0.5%	2.72%	2.72%	15,141,639	0.5%	0.5%	1.43%	1.43%	12,071,168	0.4%	0.4%	3.49%	3.49%	7,566,995	0.3%	0.3%	0.00%	0.00%	7.82%	7.82%	N/A	N/A
BC Aggregate				***-0.36%***	***-0.36%***				***1.61%***	***1.61%***				***1.78%***	***1.78%***				***0.17%***	***0.17%***	***3.22%***	***3.22%***		

LEGACY FUND
INVESTMENT PERFORMANCE REPORT AS OF APRIL 30, 2015

	April-15					March-15					December-14					September-14					Current FYTD		Prior Year FY14	
		Allocation		Month			Allocation		Quarter			Allocation		Quarter			Allocation		Quarter		Returns		Returns	
	Market Value	Actual	Policy	Gross(1)	Net	Market Value	Actual	Policy	Gross(1)	Net	Market Value	Actual	Policy	Gross(1)	Net	Market Value	Actual	Policy	Gross(1)	Net	Gross(1)	Net	Gross(1)	Net
Declaration (Total Return) (1)	86,749,626	2.7%	2.7%	0.13%	0.13%	86,638,228	2.7%	2.7%	1.77%	1.77%	77,893,283	2.7%	2.7%	0.99%	0.99%	58,399,014	2.3%	2.3%	0.65%	0.65%	3.59%	3.59%	N/A	N/A
3m LIBOR				0.02%	0.02%				0.07%	0.07%				0.06%	0.06%				0.06%	0.06%	0.21%	0.21%		
State Street	157,613,697	4.8%	4.9%	-0.54%	-0.54%	148,512,691	4.6%	4.9%	1.85%	1.84%	143,035,239	4.9%	4.9%	1.83%	1.82%	99,390,152	3.9%	3.9%	0.16%	0.15%	3.32%	3.29%	N/A	N/A
BC Gov/Credit				-0.53%	-0.53%				1.84%	1.84%				1.80%	1.80%				0.17%	0.17%	3.30%	3.30%		
Wells Capital	349,880,406	10.7%	11.5%	-0.59%	-0.59%	347,530,745	10.9%	11.4%	2.56%	2.51%	327,940,491	11.3%	11.3%	1.59%	1.55%	224,945,343	8.9%	8.9%	-0.12%	-0.17%	3.44%	3.30%	N/A	N/A
BC Credit Baa				-0.54%	-0.54%				2.32%	2.32%				1.26%	1.26%				-1.60%	-1.60%	1.40%	1.40%		
TOTAL FIXED INCOME	1,127,432,317	34.6%	35.0%	-0.33%	-0.34%	1,075,144,306	33.7%	35.0%	2.24%	2.21%	1,009,803,904	34.8%	34.8%	1.55%	1.52%	703,803,147	28.0%	28.0%	0.20%	0.16%	3.69%	3.58%	N/A	N/A
BC Aggregate				-0.36%	-0.36%				1.61%	1.61%				1.78%	1.78%				0.17%	0.17%	3.22%	3.22%		
DIVERSIFIED REAL ASSETS																								
Western	247,888,077	7.6%	7.6%	1.92%	1.92%	231,391,136	7.2%	7.6%	0.24%	0.21%	211,717,138	7.3%	7.3%	-0.43%	-0.46%	141,601,650	5.6%	5.6%	-2.09%	-2.13%	-0.40%	-0.51%	N/A	N/A
BC Global Inflation Linked Index				2.14%	2.14%				-1.53%	-1.53%				-0.14%	-0.14%				-2.76%	-2.76%	-2.33%	-2.33%		
Grosvenor CIS II	1,968,559	0.1%	0.1%	0.00%	0.00%	1,968,559	0.1%	0.1%	N/A	N/A	-	0.0%	0.0%	N/A	NA	-	0.0%	0.0%	N/A	N/A	N/A	N/A	N/A	N/A
JP Morgan (Infrastructure)	75,000,000	2.3%	2.3%	0.00%	0.00%	75,000,000	2.3%	2.3%	N/A	N/A	-	0.0%	0.0%	N/A	NA	-	0.0%	0.0%	N/A	N/A	N/A	N/A	N/A	N/A
CPI				0.20%	0.20%																			
TOTAL DIVERSIFIED REAL ASSETS	324,856,636	10.0%	10.0%	1.44%	1.44%	308,359,695	9.7%	10.0%	0.39%	0.37%	211,717,138	7.3%	7.3%	-0.43%	-0.46%	141,601,651	5.6%	5.6%	-2.10%	-2.11%	-0.73%	-0.80%	N/A	N/A
Benchmark				1.68%	1.68%				-1.10%	-1.10%				-0.14%	-0.14%				-2.76%	-2.76%	-2.35%	-2.35%		
REAL ESTATE																								
JP Morgan	85,399,094	2.6%	2.5%	1.06%	1.06%	84,506,477	2.6%	2.5%	5.97%	5.40%	78,672,478	2.7%	2.5%	3.84%	3.57%	72,301,896	2.9%	2.5%	0.00%	0.04%	11.20%	10.36%	N/A	N/A
Invesco	81,553,843	2.5%	2.5%	0.08%	0.00%	74,554,166	2.3%	2.5%	3.28%	3.19%	66,827,989	2.3%	2.5%	3.50%	3.40%	53,323,533	2.1%	2.5%	3.44%	3.35%	10.66%	10.27%	N/A	N/A
TOTAL REAL ESTATE	166,952,937	5.1%	5.0%	0.58%	0.54%	159,060,643	5.0%	5.0%	4.69%	4.35%	145,500,467	5.0%	5.0%	3.69%	3.50%	125,625,429	5.0%	5.0%	1.43%	1.41%	10.74%	10.12%	N/A	N/A
NCREIF Total Index				1.18%	1.18%				3.57%	3.57%				3.04%	3.04%				2.63%	2.63%	10.83%	10.83%		
CASH EQUIVALENTS																								
Northern Trust (1)	4,302,864			0.00%	0.00%	39,796,990			0.00%	0.00%	11,440,987			0.00%	0.00%	2,572,819			0.00%	0.00%	0.01%	0.01%	0.01%	0.01%
TOTAL CASH EQUIVALENTS	4,302,864	0.1%	0.0%	0.00%	0.00%	39,796,990	1.2%	0.0%	0.00%	0.00%	11,440,987	0.4%	0.0%	0.00%	0.00%	2,572,819	0.1%	0.0%	0.00%	0.00%	0.01%	0.01%	0.01%	0.01%
90 Day T-Bill				0.00%	0.00%				0.01%	0.01%				0.00%	0.00%				0.01%	0.01%	0.02%	0.02%	0.06%	0.06%
SHORT TERM FIXED INCOME																								
Babson Capital	196,273	0.0%	0.0%	N/A	N/A	295,646	0.0%	0.0%	N/A	N/A	43,642,546	1.5%	1.4%	0.45%	0.38%	172,382,049	6.8%	6.2%	0.28%	0.23%	N/A	N/A	2.82%	2.65%
BC 1-3 Year US Gov't Index														0.19%	0.19%				0.03%	0.03%			0.77%	0.77%
JP Morgan	-	0.0%	0.0%	N/A	N/A	-	0.0%	0.0%	N/A	N/A	33,006,749	1.1%	1.4%	0.04%	0.04%	139,284,985	5.5%	6.2%	0.04%	-0.04%	N/A	N/A	1.36%	1.24%
BC 1-3 Year Gov/Credit Index														0.17%	0.17%				0.04%	0.04%			1.14%	1.14%
TOTAL SHORT TERM FIXED INCOME	196,273	0.0%	0.0%	N/A	N/A	295,646	0.0%	0.0%	N/A	N/A	76,649,296	2.6%	2.9%	0.25%	0.21%	311,667,035	12.4%	12.5%	0.16%	0.10%	N/A	N/A	2.10%	1.95%
BC 1-3 Year US Gov't Index														0.19%	0.19%				0.03%	0.03%			0.77%	0.77%

Initial funding September 7, 2011.
NOTE: Monthly returns and market values are preliminary and subject to change.
Effective July 1, 2013, net of fee returns are calculated on a cash basis in the month paid. Prior years were accrual based and split evenly over the 12 months of the fiscal year.

(1) All limited partnership-type (and mutual funds as of 7/1/14) investment returns will only be reported net of fees, which is standard practice by the investment consultant.

BUDGET STABILIZATION FUND
INVESTMENT PERFORMANCE REPORT AS OF MARCH 31, 2015

	March-15					December-14					September-14					Current FYTD		Prior Year FY14		3 Years Ended 6/30/2014		5 Years Ended 6/30/2014	
		Allocation		Quarter			Allocation		Quarter			Allocation		Quarter		Returns		Returns					
	Market Value	Actual	Policy	Gross	Net	Market Value	Actual	Policy	Gross	Net	Market Value	Actual	Policy	Gross	Net	Gross	Net	Gross	Net	Gross	Net	Gross	Net
TOTAL BUDGET STABILIZATION FUND	**595,135,717**	**100.0%**	**100.0%**	***0.96%***	***0.93%***	**589,598,047**	**100.0%**	**100.0%**	***0.45%***	***0.44%***	**587,073,431**	**100.0%**	**100.0%**	***0.14%***	***0.11%***	**1.57%**	**1.48%**	**2.04%**	**1.94%**	**2.03%**	**1.95%**	**3.45%**	**3.37%**
POLICY TARGET BENCHMARK				*0.44%*	*0.44%*				*0.16%*	*0.16%*				*0.03%*	*0.03%*	*0.63%*	*0.63%*	*0.61%*	*0.61%*	*0.40%*	*0.40%*	*0.30%*	*0.30%*
Bank of ND CD'S	**102,767,901**	**17.3%**	**17.3%**	**0.65%**	**0.65%**	**102,973,885**	**17.5%**	**17.5%**	**0.67%**	**0.67%**	**104,153,995**	**17.7%**	**17.7%**	**0.67%**	**0.67%**	**2.01%**	**2.01%**	**2.81%**	**2.81%**	**3.63%**	**3.63%**	**3.91%**	**3.91%**
CASH EQUIVALENTS																							
Northern Trust (1)	7,336,677			0.00%	0.00%	6,372,078			0.00%	0.00%	8,396,369			0.00%	0.00%	0.01%	0.01%	0.01%	0.01%	N/A	N/A	N/A	N/A
TOTAL CASH EQUIVALENTS	***7,336,677***	***1.2%***	***1.2%***	***0.00%***	***0.00%***	***6,372,078***	***1.1%***	***1.1%***	***0.00%***	***0.00%***	***8,396,369***	***1.4%***	***1.4%***	***0.00%***	***0.00%***	***0.01%***	***0.01%***	***0.01%***	***0.01%***	***0.17%***	***0.17%***	***0.24%***	***0.24%***
90 Day T-Bill				***0.01%***	***0.01%***				***0.00%***	***0.00%***				***0.01%***	***0.01%***	***0.02%***	***0.02%***	***0.06%***	***0.06%***	***0.08%***	***0.08%***	***0.11%***	***0.11%***
SHORT TERM FIXED INCOME																							
Babson Capital	244,224,152	41.0%	40.7%	1.38%	1.33%	241,033,843	40.9%	40.7%	0.61%	0.57%	238,251,495	40.6%	40.4%	0.00%	-0.03%	2.01%	1.87%	2.39%	2.26%	N/A	N/A	N/A	N/A
BC 1-3 Year US Gov't Index				***0.54%***	***0.54%***				***0.19%***	***0.19%***				***0.03%***	***0.03%***	***0.77%***	***0.77%***	***0.77%***	***0.77%***				
JP Morgan	240,806,986	40.5%	40.7%	0.72%	0.67%	239,218,241	40.6%	40.7%	0.22%	0.22%	236,271,573	40.2%	40.4%	0.05%	0.00%	0.99%	0.90%	1.44%	1.31%	N/A	N/A	N/A	N/A
BC 1-3 Year Gov/Credit Index				***1.28%***	***1.28%***				***0.17%***	***0.17%***				***0.04%***	***0.04%***	***1.49%***	***1.49%***	***1.14%***	***1.14%***				
TOTAL SHORT TERM FIXED INCOME	***485,031,138***	***81.5%***	***81.5%***	***1.05%***	***1.00%***	***480,252,084***	***81.5%***	***81.5%***	***0.42%***	***0.40%***	***474,523,067***	***80.8%***	***80.8%***	***0.03%***	***-0.02%***	***1.49%***	***1.38%***	***1.91%***	***1.79%***	***1.44%***	***1.33%***	***3.94%***	***3.85%***
BC 1-3 Year US Gov't Index (1)				***0.54%***	***0.54%***				***0.19%***	***0.19%***				***0.03%***	***0.03%***	***0.77%***	***0.77%***	***0.77%***	***0.77%***				

NOTE: Monthly returns and market values are preliminary and subject to change.
Effective July 1, 2013, net of fee returns are calculated on a cash basis in the month paid. Prior years were accrual based and split evenly over the 12 months of the fiscal year.

BUDGET STABILIZATION FUND
INVESTMENT PERFORMANCE REPORT AS OF APRIL 30, 2015

	April-15					March-15				
		Allocation		Month			Allocation		Quarter	
	Market Value	Actual	Policy	Gross[1]	Net	Market Value	Actual	Policy	Gross	Net
TOTAL BUDGET STABILIZATION FUND	**596,019,653**	**100.0%**	**100.0%**	**0.15%**	**0.15%**	**595,135,717**	**100.0%**	**100.0%**	***0.96%***	***0.93%***
POLICY TARGET BENCHMARK				*0.04%*	*0.04%*				*0.44%*	*0.44%*
Bank of ND CD'S	**97,862,702**	**16.4%**	**16.4%**	**0.21%**	**0.21%**	**102,767,901**	**17.3%**	**17.3%**	**0.65%**	**0.65%**
CASH EQUIVALENTS										
Northern Trust (1)	12,456,547			0.00%	0.00%	7,336,677			0.00%	0.00%
TOTAL CASH EQUIVALENTS	***12,456,547***	***2.1%***	***2.1%***	***0.00%***	***0.00%***	***7,336,677***	***1.2%***	***1.2%***	***0.00%***	***0.00%***
90 Day T-Bill				***0.00%***	***0.00%***				***0.01%***	***0.01%***
SHORT TERM FIXED INCOME										
Babson Capital	244,717,015	41.1%	40.7%	0.19%	0.20%	244,224,152	41.0%	40.7%	1.38%	1.33%
BC 1-3 Year US Gov't Index				***0.05%***	***0.05%***				***0.54%***	***0.54%***
JP Morgan	240,983,389	40.4%	40.7%	0.07%	0.07%	240,806,986	40.5%	40.7%	0.72%	0.67%
BC 1-3 Year Gov/Credit Index				***0.08%***	***0.08%***				***1.28%***	***1.28%***
TOTAL SHORT TERM FIXED INCOME	***485,700,404***	***81.5%***	***81.5%***	***0.14%***	***0.14%***	***485,031,138***	***81.5%***	***81.5%***	***1.05%***	***1.00%***
BC 1-3 Year US Gov't Index (1)				***0.05%***	***0.05%***				***0.54%***	***0.54%***

	December-14					September-14				
		Allocation		Quarter			Allocation		Quarter	
	Market Value	Actual	Policy	Gross	Net	Market Value	Actual	Policy	Gross	Net
TOTAL BUDGET STABILIZATION FUND	**589,598,047**	**100.0%**	**100.0%**	***0.45%***	***0.44%***	**587,073,431**	**100.0%**	**100.0%**	***0.14%***	***0.11%***
POLICY TARGET BENCHMARK				*0.16%*	*0.16%*				*0.03%*	*0.03%*
Bank of ND CD'S	**102,973,885**	**17.5%**	**17.5%**	**0.67%**	**0.67%**	**104,153,995**	**17.7%**	**17.7%**	**0.67%**	**0.67%**
CASH EQUIVALENTS										
Northern Trust (1)	6,372,078			0.00%	0.00%	8,396,369			0.00%	0.00%
TOTAL CASH EQUIVALENTS	***6,372,078***	***1.1%***	***1.1%***	***0.00%***	***0.00%***	***8,396,369***	***1.4%***	***1.4%***	***0.00%***	***0.00%***
90 Day T-Bill				***0.00%***	***0.00%***				***0.01%***	***0.01%***
SHORT TERM FIXED INCOME										
Babson Capital	241,033,843	40.9%	40.7%	0.61%	0.57%	238,251,495	40.6%	40.4%	0.00%	-0.03%
BC 1-3 Year US Gov't Index				***0.19%***	***0.19%***				***0.03%***	***0.03%***
JP Morgan	239,218,241	40.6%	40.7%	0.22%	0.22%	236,271,573	40.2%	40.4%	0.05%	0.00%
BC 1-3 Year Gov/Credit Index				***0.17%***	***0.17%***				***0.04%***	***0.04%***
TOTAL SHORT TERM FIXED INCOME	***480,252,084***	***81.5%***	***81.5%***	***0.42%***	***0.40%***	***474,523,067***	***80.8%***	***80.8%***	***0.03%***	***-0.02%***
BC 1-3 Year US Gov't Index (1)				***0.19%***	***0.19%***				***0.03%***	***0.03%***

	Current FYTD Returns		Prior Year FY14 Returns		3 Years Ended 6/30/2014		5 Years Ended 6/30/2014	
	Gross	Net	Gross	Net	Gross	Net	Gross	Net
TOTAL BUDGET STABILIZATION FUND	**1.57%**	**1.48%**	**2.04%**	**1.94%**	**2.03%**	**1.95%**	**3.45%**	**3.37%**
POLICY TARGET BENCHMARK	*0.63%*	*0.63%*	*0.61%*	*0.61%*	*0.40%*	*0.40%*	*0.30%*	*0.30%*
Bank of ND CD'S	**2.01%**	**2.01%**	**2.81%**	**2.81%**	**3.63%**	**3.63%**	**3.91%**	**3.91%**
CASH EQUIVALENTS								
Northern Trust (1)	0.01%	0.01%	0.01%	0.01%	N/A	N/A	N/A	N/A
TOTAL CASH EQUIVALENTS	***0.01%***	***0.01%***	***0.01%***	***0.01%***	***0.17%***	***0.17%***	***0.24%***	***0.24%***
90 Day T-Bill	***0.02%***	***0.02%***	***0.06%***	***0.06%***	***0.08%***	***0.08%***	***0.11%***	***0.11%***
SHORT TERM FIXED INCOME								
Babson Capital	2.01%	1.87%	2.39%	2.26%	N/A	N/A	N/A	N/A
BC 1-3 Year US Gov't Index	***0.77%***	***0.77%***	***0.77%***	***0.77%***				
JP Morgan	0.99%	0.90%	1.44%	1.31%	N/A	N/A	N/A	N/A
BC 1-3 Year Gov/Credit Index	***1.49%***	***1.49%***	***1.14%***	***1.14%***				
TOTAL SHORT TERM FIXED INCOME	***1.49%***	***1.38%***	***1.91%***	***1.79%***	***1.44%***	***1.33%***	***3.94%***	***3.85%***
BC 1-3 Year US Gov't Index (1)	***0.77%***	***0.77%***	***0.77%***	***0.77%***				

NOTE: Monthly returns and market values are preliminary and subject to change.
Effective July 1, 2013, net of fee returns are calculated on a cash basis in the month paid. Prior years were accrual based and split evenly over the 12 months of the fiscal year.

Estimated YTD Through **6/23/2015**

(Actual returns are net of fees; estimates are gross indices)

			TFFR	PERS	WSI	Legacy	Budget Stabilization
Market Value		**30-Apr**	**2,110,626,543**	**2,426,858,029**	**1,773,004,940**	**3,259,054,191**	**596,019,653**
Total Fund Actual through		30-Apr	**3.77%**	**3.82%**	**3.96%**	**3.88%**	**1.63%**
Total Fund Policy through		30-Apr	3.15%	3.17%	3.60%	3.45%	0.67%
		31-May					
MSCI World		0.34%	16.0%	16.0%	0.0%	0.0%	0.0%
Russell 1000		1.31%	16.6%	16.6%	12.0%	22.0%	0.0%
Russell 2000		2.28%	4.8%	4.8%	4.0%	8.0%	0.0%
MSCI EAFE		-0.51%	11.8%	11.1%	9.0%	20.0%	0.0%
MSCI Emerging Mkts		-4.01%	2.8%	3.5%	0.0%	0.0%	0.0%
BC Aggregate		-0.24%	12.0%	12.0%	53.0%	35.0%	0.0%
High Yield		0.30%	5.0%	5.0%	0.0%	0.0%	0.0%
BC Global Agg ex US		-3.02%	5.0%	5.0%	0.0%	0.0%	0.0%
Real Estate		1.18%	20.0%	20.0%	6.0%	5.0%	0.0%
Private Equity		0.00%	5.0%	5.0%	0.0%	0.0%	0.0%
Real Assets		-1.68%	0.0%	0.0%	15.0%	10.0%	0.0%
ML 1-3Y Treasury		0.07%	0.0%	0.0%	0.0%	0.0%	100.0%
T-Bill		0.00%	1.0%	1.0%	1.0%	0.0%	0.0%
Est. MTD through	**5/31/2015**		**0.28%**	**0.26%**	**-0.11%**	**0.17%**	**0.07%**
		23-Jun					
MSCI World		1.04%	16.0%	16.0%	0.0%	0.0%	0.0%
Russell 1000		1.01%	16.6%	16.6%	12.0%	22.0%	0.0%
Russell 2000		4.04%	4.8%	4.8%	4.0%	8.0%	0.0%
MSCI EAFE		1.20%	11.8%	11.1%	9.0%	20.0%	0.0%
MSCI Emerging Mkts		-1.02%	2.8%	3.5%	0.0%	0.0%	0.0%
BC Aggregate		-1.43%	12.0%	12.0%	53.0%	35.0%	0.0%
High Yield		-0.85%	5.0%	5.0%	0.0%	0.0%	0.0%
BC Global Agg ex US		-0.26%	5.0%	5.0%	0.0%	0.0%	0.0%
Real Estate		4.82%	20.0%	20.0%	6.0%	5.0%	0.0%
Private Equity		0.00%	5.0%	5.0%	0.0%	0.0%	0.0%
Real Assets		-0.43%	0.0%	0.0%	15.0%	10.0%	0.0%
ML 1-3Y Treasury		-0.11%	0.0%	0.0%	0.0%	0.0%	100.0%
T-Bill		0.00%	1.0%	1.0%	1.0%	0.0%	0.0%
Est. MTD through	**6/23/2015**		**1.38%**	**1.36%**	**-0.14%**	**0.48%**	**-0.11%**
Estimated FYTD Return	**6/23/2015**		**5.49%**	**5.50%**	**3.70%**	**4.56%**	**1.59%**
Estimated FYTD Policy	6/23/2015		4.86%	4.84%	3.34%	4.13%	0.63%
Comparison to 8% return assumption pro-rated FYTD			***7.84%***	***7.84%***			

AGENDA ITEM III. B.

BOARD ACTION REQUESTED

To: State Investment Board

From: Dave Hunter, Executive Director / CIO

Date: June 19, 2015

RE: **Tobacco Prevention & Control ("TPC") Trust Fund - Investment Policy**

TPC Request:

In late-2014, TPC expressed interested in contracting for investment services with the SIB as allowed under NDCC 21-10-06 and as recommended in a recent TPC audit. The TPC trust fund has a current market value of $47 million and is projected to exceed $53 million over the next three years prior to declining by approximately $8 million per year between 2018 and 2024. <u>TPC funds are currently invested in short-term cash with the Bank of North Dakota and earning approximately 6 to 10 bps per annum</u>.

RIO has met with TPC representatives to discuss their investment objectives and risk tolerance, the benefits of developing a formal investment policy statement, and the stated desire to engage with the SIB for investment services. Based on extensive discussions, internal staff administrative capacity would not be materially affected by the establishment of this new fund which would be similar to the PERS Retiree Health Insurance Credit Fund if set-up as a standalone entity.

Recent SIB Actions:

At the SIB meeting on January 23, 2015, RIO staff presented the TPC request to the SIB. During this presentation it was noted that this fund had a non-tobacco investment requirement and that this requirement does not fit within the existing Insurance Trust structure. As a result, Board members requested further guidance regarding the SIB's ability to provide investment services for this fund because of this restriction. On February 20, 2015, legal counsel provided the attached memo which supports a conclusion that the SIB may not decline to provide investment management services for the TPC fund. **On March 27, 2015, the SIB approved RIO's recommendation to work towards securing an investment services contract with the TPC.**

Recent RIO Actions:

In accordance with SIB Governance Policy E-13 on "Accepting New Clients", RIO developed an investment policy statement for the TPC after assessing their investment criteria and risk tolerance, completing an asset liability study, and reviewing the investment services contract.

The attached investment policy statement was approved by the TPC Executive Committee on June 10, 2015. RIO intends to submit this investment policy statement along with all other required documentation to the Industrial Commission and request their approval on June 30, 2015.

Recommendation:

RIO recommends the SIB approve the attached TPC investment policy statement based on the following summary of our due diligence procedures.

1. Based on forecasted cash flows provided by the TPC, RIO worked with BlackRock to complete an asset liability review.
2. These results were shared with our investment consultant (Callan) without issue.
3. Based on our review procedures, RIO recommends TPC adopt a target asset allocation of 10% equities and 90% to fixed income/cash.
4. Although higher equity allocations were considered, RIO recommends a 10% equity allocation given that the Fund will commence a seven-year liquidation period in 2018.
5. The proposed 10% equity and 90% fixed income allocation did not experience a loss in any year during the past decade (and even posted a +2.4% return in 2008).
6. RIO's recommendation was discussed with TPC Executive Director, Jeanne Prom, on June 17, 2015, without any exceptions other than emphasizing that all investments must be intended to be "tobacco free".
7. **Based on the above recommended asset allocation, the Fund will have an expected long-term rate of return of approximately 2% with strong downside risk protection so as to preserve capital and benefit from higher return expectations, which are estimated to be 20 times higher than prior years (e.g. the expected 2.0% return is 20 times higher than the sub 0.1% return earned during the last four years).**
8. Future investment income is expected to increase by approximately $5 million as a result of this policy change.
9. RIO will provide the SIB with specific investment strategies to implement the above overall asset allocation recommendation at a future meeting.

NORTH DAKOTA TOBACCO PREVENTION AND CONTROL FUND

INVESTMENT POLICY STATEMENT

1. PLAN CHARACTERISTICS AND FUND CONSTRAINTS.

The North Dakota Tobacco Prevention and Control fund (fund) was established in 1999 for the purpose of creating and implementing a comprehensive statewide tobacco prevention and control plan (comprehensive plan). NDCC 54-27-25(2). The comprehensive plan is administered by the Executive Committee and is to be consistent with the centers for disease control best practices for comprehensive tobacco prevention and control programs. NDCC 23-42-01. The Executive Committee has the power and duty to provide direction to the state investment board for investment of the fund. NDCC 23-42-04(1).

2. FUND GOALS

The fund consists of the tobacco settlement dollars obtained by the state under section IX(c)(2) of the agreement adopted by the east central judicial district court in its judgment entered December 28, 1998 [Civil No. 98-3778] in *State of North Dakota, ex rel. Heidi Heitkamp v. Philip Morris, Inc.* Interest earned on the fund must be credited to the fund. NDCC 54-27-25(2). The fund Executive Committee recognizes that a sound investment program is essential to meet the goals of the comprehensive plan. As a result, the fund goal is to protect and sustain the fund in order to implement the comprehensive plan.

3. RESPONSIBILITIES AND DISCRETION OF THE STATE INVESTMENT BOARD (SIB).

The Executive Committee has entered into a contract with the SIB for investment services as allowed under NDCC 21-10-06. The Executive Committee is charged by law under NDCC 23-42-04 with the responsibility of providing direction to the state investment board for investment of the fund. The SIB is charged with implementing these policies and investing the assets of the fund in the manner provided in NDCC 21-10-07, the prudent investor rule. Under this rule, the fiduciaries shall exercise the judgment and care, under the circumstances then prevailing, that an institutional investor of ordinary prudence, discretion, and intelligence exercises in the management of large investments entrusted to it, not in regard to speculation but in regard to the permanent disposition of funds, considering probable safety of capital as well as probable income. The fund must be invested exclusively for the benefit of the members and their beneficiaries in accordance with this investment policy.

Management responsibility for the investment program not assigned to the SIB in Chapter 21-10 of the North Dakota Century Code (NDCC) is hereby delegated to the SIB, who must establish written policies for the operation of the investment program, consistent with this investment policy.

The SIB may delegate investment responsibility to professional money managers. Where a money manager has been retained, the SIB's role in determining investment strategy and security selection is supervisory, not advisory.

The SIB is responsible for establishing criteria, procedures, and making decisions with respect to hiring, keeping, and terminating money managers. SIB investment responsibility also includes selecting performance measurement services, consultants, report formats, and frequency of meetings with managers.

The SIB will implement changes to this policy as promptly as is prudent.

4. RISK TOLERANCE

The Executive Committee is unwilling to undertake investment strategies that might jeopardize the ability of the fund to finance the comprehensive plan.

The Executive Committee actively seeks to sustain the fund by taking on risk for which it expects to be compensated over the long term. The Executive Committee understands that a prudent investment approach to risk taking can result in periods of under-performance for the fund in which the funding status may decline. The Executive Committee believes that such an approach, prudently implemented, best serves the long-run interests of the State.

5. INVESTMENT OBJECTIVES

The Executive Committee's investment objectives are expressed in terms of reward and risk expectations relative to investable, passive benchmarks. The fund's policy benchmark is comprised of policy mix weights of appropriate asset class benchmarks as set by the SIB.

1. The fund's rate of return, net of fees and expenses, should at least match that of the policy benchmark over a minimum evaluation period of five years.
2. The fund's risk, measured by the standard deviation of net returns, should not exceed 115% of the policy benchmark over a minimum evaluation period of five years.
3. The risk-adjusted performance of the fund, net of fees and expenses, should at least match that of the policy benchmark over a minimum evaluation period of five years.

6. POLICY ASSET MIX

Asset allocation policy is critical because it defines the basic risk and return characteristics of the investment portfolio. Asset allocation targets are established using an asset-liability analysis designed to assist the Executive Committee in determining an acceptable volatility target for the fund and an optimal asset allocation policy mix. This analysis estimates the potential impact of various asset class mixes on key measures of total fund risk.

After consideration of all the inputs and a discussion of its own collective risk tolerance, the Executive Committee approves the appropriate policy asset mix for the fund.

Asset Class	Policy Target(%)	Rebalancing Range(%)
Global Equity	10	5-20
Global Fixed Income	75	60-90
Cash	15	10-20

While the Executive Committee recognizes fluctuations in market values will lead to short-term deviations from policy targets, the Executive Committee does not intend to engage in tactical asset allocation. Rebalancing of the fund to this target will be done in accordance with the SIB's rebalancing policy, but not less than annually.

7. RESTRICTIONS

While the SIB is responsible for establishing specific quality, diversification, restrictions, and performance objectives for the investment vehicles in which the fund's assets will be invested, it is understood that:

a. Futures and options may be used to hedge or replicate underlying index exposure, but not for speculation.
b. Derivatives use will be monitored to ensure that undue risks are not taken by the money managers.
c. No transaction shall be made which threatens the tax exempt status of the fund.
d. All assets will be held in custody by the SIB's master custodian or such other custodians as are acceptable to the SIB.
e. No unhedged short sales or speculative margin purchases shall be made.
f. The assets shall only be invested in securities issued by tobacco-free firms, defined as those which generate revenues of no greater than 0% from tobacco products. In the event of an inadvertent de minimis investment in a firm with any exposure to tobacco products, the inadvertent investment will be immediately divested upon discovery. For investment purposes "tobacco product" means tobacco or any product containing, made from, or derived from tobacco, in whole or in part, that is intended for human consumption, whether chewed, smoked, absorbed, dissolved, inhaled, snorted, sniffed, consumed, or ingested by any other means, including cigarettes, cigars, electronic smoking devices, pipe tobacco, chewing tobacco, snuff, snus, liquid, or other kinds and forms of tobacco. "Tobacco product" includes ny product or device that contains nicotine, in any form, that is derived from tobacco. Any product that contains nicotine shall be presumed to contain nicotine derived from tobacco unless the nicotine is confirmed to be derived from a different source.

g. Economically targeted investing is prohibited unless the investment meets the Exclusive Benefit Rule.

   For the purpose of this document economically targeted investment is defined as an investment designed to produce a competitive rate of return commensurate with risk involved, as well as to create collateral economic benefits for a targeted geographic area, group of people, or sector of the economy.

   Also, for the purpose of this document, the Exclusive Benefit Rule is met if the following four conditions are satisfied:

   (1) The cost does not exceed the fair market value at the time of investment.
   (2) The investment provides the fund with an equivalent or superior rate of return for a similar investment with a similar time horizon and similar risk.
   (3) Sufficient liquidity is maintained in the fund to permit distributions in accordance with the terms of the plan.
   (4) The safeguards and diversity that a prudent investor would adhere to are present.

   Where investment characteristics, including yield, risk, and liquidity are equivalent, the Executive Committee's policy favors investments which will have a positive impact on the economy of North Dakota.

8. INTERNAL CONTROLS

A system of internal controls must be in place by the SIB to prevent losses of public funds arising from fraud or employee error. Such controls deemed most important are the separation of responsibilities for investment purchases from the recording of investment activity, custodial safekeeping, written confirmation of investment transactions, and established criteria for broker relationships. The annual financial audit must include a comprehensive review of the portfolio, accounting procedures for security transactions and compliance with the investment policy.

9. EVALUATION AND REVIEW.

Investment management of the fund will be evaluated against the fund's investment objectives. Emphasis will be placed on five year results. Evaluation should include an assessment of the continued feasibility of achieving the investment objectives and the appropriateness of the Investment Policy Statement for achieving those objectives.

Performance reports will be provided to the Executive Committee quarterly and investment performance presentations will be provided to the Executive Committee upon request, but not less than annually. Such reports will include asset returns and allocation data as well as information regarding all significant and/or material matters and changes pertaining to the investment of the fund, including, but not limited to:

1. A list of the advisory services managing investments for the Executive Committee.
2. A list of investments at market value, compared to previous reporting period, of each fund managed by each advisory service.
3. Earnings, percentage earned, and change in market value of each fund's investments.
4. Comparison of the performance of each fund managed by each advisory service to other funds under the Executive Committee's control and to generally accepted market indicators.
5. All material legal or legislative proceedings affecting the SIB.
6. Compliance with this investment policy statement.

Executive Committee Adopted and Approved: June 10, 2015

ND Center for Tobacco Prevention and Control Policy	ND State Investment Executive Committee
Date_______________________	Date_______________________
_______________________	_______________________
Jeanne Prom Executive Director	David Hunter Executive Director / Chief Investment Officer North Dakota Retirement & Investment Office

POLICY TYPE: INVESTMENTS

POLICY TITLE: *ACCEPTING NEW CLIENTS*

NDCC 21-10-06 states *"The state investment board may provide investment services to, and manage the money of, any agency, institution, or political subdivision of the state, subject to agreement with the industrial commission. The scope of services to be provided by the state investment board to the agency, institution, or political subdivision must be specified in a written contract. The state investment board may charge a fee for providing investment services and any revenue collected must be deposited in the state retirement and investment fund."*

When a request is received by staff from a potential new investor requesting investment services from the State Investment (SIB), the following steps shall be followed.

1. Staff will conduct initial discussions with the potential client regarding type of fund, risk tolerance, size of fund, services to be provided, costs, etc.

2. Staff will recommend that an Asset/Liability study be conducted by the potential client if one has not been done recently. This discussion will include a description of the asset classes available for investment with the SIB to be included in their study.

3. If the potential client is still interested in participating in the SIB program, staff will bring the preliminary request to the SIB for acceptance. It shall be the policy of the SIB to take the following into consideration when determining if a new investor request will be accepted.

   a. Internal staff administrative capacity.
   b. Compatibility of new investor's goals and risk tolerances with the existing SIB program structure.
   c. Whatever other factors the SIB determines to be appropriate to the decision.

4. If the SIB chooses to accept the preliminary request, staff will provide the necessary template documents to the potential client for review and completion. These documents include a contract for services and investment guidelines.

5. Once documentation is completed, staff will request to have the issue included on the Industrial Commission's agenda for their approval. Copies of all documentation will be provided for their review.

6. If approved by the Industrial Commission, final documentation will be presented to the SIB for final acceptance.

7. If accepted, staff will work with the new client to set up transfer of funds and implementation of asset allocation as directed. All new clients will be brought in as of the last day of a calendar quarter.

8. Fees will be charged with the intention of covering all associated costs as described in RIO Fiscal Management procedure "Investment Fee Allocations".

Policy Implemented: November 20, 2009

MEMORANDUM

TO: Connie Flanagan, Retirement and Investment Office

FROM: Janilyn Murtha, Assistant Attorney General

RE: Tobacco Prevention and Control Trust Fund

DATE: February 20, 2015

At the January 23, 2015, meeting of the SIB, RIO staff presented the request of the Tobacco Prevention and Control Trust Fund to have the SIB provide investment management services. During this presentation it was noted that this fund had a non-tobacco investment requirement and that this requirement does not fit within the existing Insurance Trust structure. At this time Board members expressed a concern regarding the SIB's ability to provide investment management services for this fund because of this restriction. Subsequent to the meeting you asked whether the Board could deny the request for services by this fund. Please accept the following in response to your question.

The Tobacco Prevention and Control Trust Fund (hereinafter TPC fund) is created under N.D.C.C. § 54-27-25(2) and consists of a portion of the tobacco settlement dollars obtained by the state under the MSA (Master Settlement Agreement). The term MSA is the acronym used to identify the settlement agreement executed between a majority of states and tobacco manufacturers during the 1990s resolving claims between the parties. The TPC fund is further discussed under N.D.C.C. ch. 23-42 and defined in N.D.C.C. § 23-42-01(4) as consisting of all principal and interest of the TPC fund established by N.D.C.C. § 54-27-25. While there is not specific language in chapter 23-42 directing the SIB to invest the TPC fund, the powers of the TPC executive committee under N.D.C.C. § 23-42-04(1) include "providing direction to the state investment board for investment of the tobacco prevention and control fund." While this language does not contain an explicit mandate to have the SIB invest the fund because it is setting forth the powers of the executive committee and not the SIB, there is an implicit mandate to have the SIB invest the fund because the power of the executive committee to provide direction to the SIB can't be realized if the SIB declines to facilitate the investment.

The SIB is charged with the investment of the funds enumerated under N.D.C.C. § 21-10-06(1) and the TPC fund is not included in the list of funds so enumerated. Under N.D.C.C. § 21-10-06(3) the SIB may provide investment services to any agency, institution, or political subdivision of the state subject to agreement with the industrial commission. The SIB is therefore required to invest the funds listed under subsection 1 of N.D.C.C. § 21-10-06 but has the discretion to agree to invest the funds listed under subsection 3. It is reasonable to conclude that because TPC isn't included under subsection 1 of N.D.C.C. § 21-10-06 that the SIB would need to enter into a contract for providing investment services for it under subsection 3; however, it may not be reasonable to conclude that providing such services is discretionary.

While the word "may" in a statute ordinarily creates a discretionary, non-mandatory duty under settled principles of statutory construction, it can also be construed as a "must" where the context or subject matter compels that construction. See North Dakota Com'n on Medical Competency v. Racek, 527 N.W.2d 262 (N.D., 1995). Failure to include the TPC fund under subsection 1 of N.D.C.C. § 21-10-06, therefore, does not preclude a determination that the SIB is nonetheless charged with its investment by N.D.C.C. § 23-42-04; such that the "may" of subsection 3 be interpreted as a "must" when applied to investment of this fund. Another principle of statutory construction found in N.D.C.C. § 1-02-07 requires that conflicting provisions be reconciled if at all possible to give effect to both provisions but if the conflict between the two provisions is irreconcilable a special provision will prevail over that of a general provision. The direction provided by N.D.C.C. § 23-42-04 refers to a specific relationship between the executive committee and the SIB regarding the TPC fund, this provision is more specific than the contracting authority granted the SIB by N.D.C.C. § 21-10-06(3), such that adherence to N.D.C.C. § 23-42-04 should be favored. Therefore, applying these rules of statutory construction to the language at issue supports a conclusion that the SIB may not decline to provide investment management services for the TPC fund.

Please let me know if you have any questions or would like to discuss this further.

Tobacco Prevention and Control Trust

New SIB Client Status Update

June 18, 2015

Dave Hunter, Executive Director / CIO

Darren Schulz, Deputy Chief Investment Officer

ND Retirement & Investment Office (RIO)

State Investment Board (SIB)

Presentation Agenda

- Review of New Client Acceptance Procedures
- Projected Cash Flows, Liquidity Needs and Risk Tolerances
- Proposed Investment Management Framework
- State Investment Board Overview and Process
- Assets under management
- Next Steps (State Treasurer, BND and Lt. Governor pre-advised)
- Legal Counsel and Tobacco Prevention & Control Board Approval

Accepting New Clients – ND Century Code

NDCC 21-10-06 states *"<u>The state investment board may provide investment services to, and manage the money of, any agency, institution, or political subdivision of the state, subject to agreement with the industrial commission</u>. The scope of services to be provided by the state investment board to the agency, institution, or political subdivision must be specified in a written contract. The state investment board may charge a fee for providing investment services and any revenue collected must be deposited in the state retirement and investment fund."*

Accepting New Client Policies and Procedures

When a request is received by RIO from a potential new client requesting investment services from the State Investment (SIB), the following steps shall be followed.

1. Staff will conduct initial discussions with the potential client regarding type of fund, risk tolerance, size of fund, services to be provided, costs, etc. - Completed
2. Staff will recommend an asset liability study be conducted by the potential client if one has not been done recently. This discussion will include a description of the asset classes available for investment with the SIB to be included in their study. – Completed
3. If the potential client is still interested in participating in the SIB program, staff will bring the preliminary request to the SIB for acceptance. It shall be the policy of the SIB to take the following into consideration when determining if a new investor request will be accepted. a) Internal staff administrative capacity; b) Compatibility of new investor's goals and risk tolerances with the existing SIB program structure; and c) Other factors the SIB determines to be appropriate to the decision. - Completed
4. If the SIB chooses to accept the preliminary request, staff will provide the necessary template documents to the potential client for review and completion. These documents include a contract for services and investment guidelines. - Completed
5. Once documentation is completed, staff will request to have the issue included on the Industrial Commission's agenda for their approval. Copies of all documentation will be provided for their review. The Industrial Commission next two meetings are scheduled for June 30 and July 28, 2015
6. If approved by the Industrial Commission, final documentation will be presented to the SIB for final acceptance. The next two SIB meeting dates are scheduled for July 24 and August 28, 2015.
7. If accepted, staff will work with the new client to set up transfer of funds and implementation of asset allocation as directed. New clients are generally brought in on the last day of a month or quarter. July 31 or August 31, 2015
8. Fees will be charged with the intention of covering all associated costs as described in RIO Fiscal Management procedure "Investment Fee Allocations".

Key Assumptions

- Legal, BND and Office of the Treasurer Contact
- Projected Cash Flows
- Liquidity Needs
- Risk Tolerances
- Estimated Costs and Return Expectations
- Proposed Timeline (July, August or September of 2015)

Historical and Projected Cash Flows (2009 to 2024)

<u>Tobacco Prevention and Control Trust Fund ("TPCT Fund" or "Fund")</u>:

- **Since 2009, the Fund has grown from zero to over $43 million.**
- **The Fund is expected to peak at over $53 million during the fiscal year ended June 30, 2017.**
- **The Fund is expected to decline by approximately $8 million per year for seven consecutive years (between 2018 and 2024) and decline to zero in the fiscal year ended June 30, 2024.**

July 1- June 30 Fiscal Year	Strategic Contribution Fund Deposit	CDC Best Practice Recommendation	CDC Tobacco Prevention Grant	Community Health Trust Fund to DOH 80%	Tobacco Prevention and Control Trust Fund	Tobacco Prevention and Control Trust Fund Balance
2009	14.1			2.3		14.1
2010	12.2	9.3	1.1	2.1	3.5	22.8
2011	11.2	9.3	1.1	1.9	4.6	29.4
2012	11.4	9.3	1.1	2	5.7	35.1
2013	11.4	9.3	1.1	2	6.8	39.7
2014	11.4	12.2	1	1.6	7.9	43.2
2015	11.4	12.8	0.6	1.6	7.9	46.7
2016	11.4	10.9	0.6	1.6	8	50.1
2017	11.4	11.3	0.6	1.6	8	53.5
2018	0	11.3	0.6	1.6	8	45.5
2019	0	11.3	0.6	1.6	8	37.5
2020	0	11.3	0.6	1.6	8	29.5
2021	0	11.3	0.6	1.6	8	21.5
2022	0	11.3	0.6	1.6	8	13.5
2023	0	11.3	0.6	1.6	8	5.5
2024	0					

Actual and Budgeted Investment Income (5.6 to 10 bps)

- **During the last biennium, investment income as a % of assets was less than 0.10% per year.**
- **For 2013-15, investment income was appropriated at 0.085% (or 8.5 basis points) per annum.**
- **For 2015-17, investment income was budgeted at 0.056% (or 5.6 basis points) per year.**

Tobacco Prevention and Control Trust Fund
Status Statement

	2011-13 Actual[1]	2013-15 Legislative Appropriation	2013-15 Revised Estimate	2015-17 Executive Budget
Beginning Balance	$29,556,426	$40,123,720	$40,123,720 [2]	$46,874,286
Revenue:				
Fiscal year 1 payments	$11,392,521	$11,327,123	11,205,876 [3]	11,304,243 [4]
Fiscal year 2 payments	$11,402,609	11,327,123	11,304,243 [4]	11,304,243 [4]
Investment income	60,000	74,000	56,275	56,521
Total revenue	$22,855,130	$22,728,246	$22,566,394	$22,665,007
Expenditures:				
Appropriated expenditures	($12,287,836)	($15,815,828)	($15,815,828)	($16,109,756)
Total expenditures	($12,287,836)	($15,815,828)	($15,815,828)	($16,109,756)
Ending Balance	$40,123,720	$47,036,138	$46,874,286	$53,429,537

[1] Final revenue and expenditures per state accounting system reports dated June 30, 2013.
[2] Actual July 1, 2013 balance.
[3] Actual revenue received during fiscal year 2014.
[4] Estimated revenues based on average of fiscal year 2013 and 2014 actual amounts.

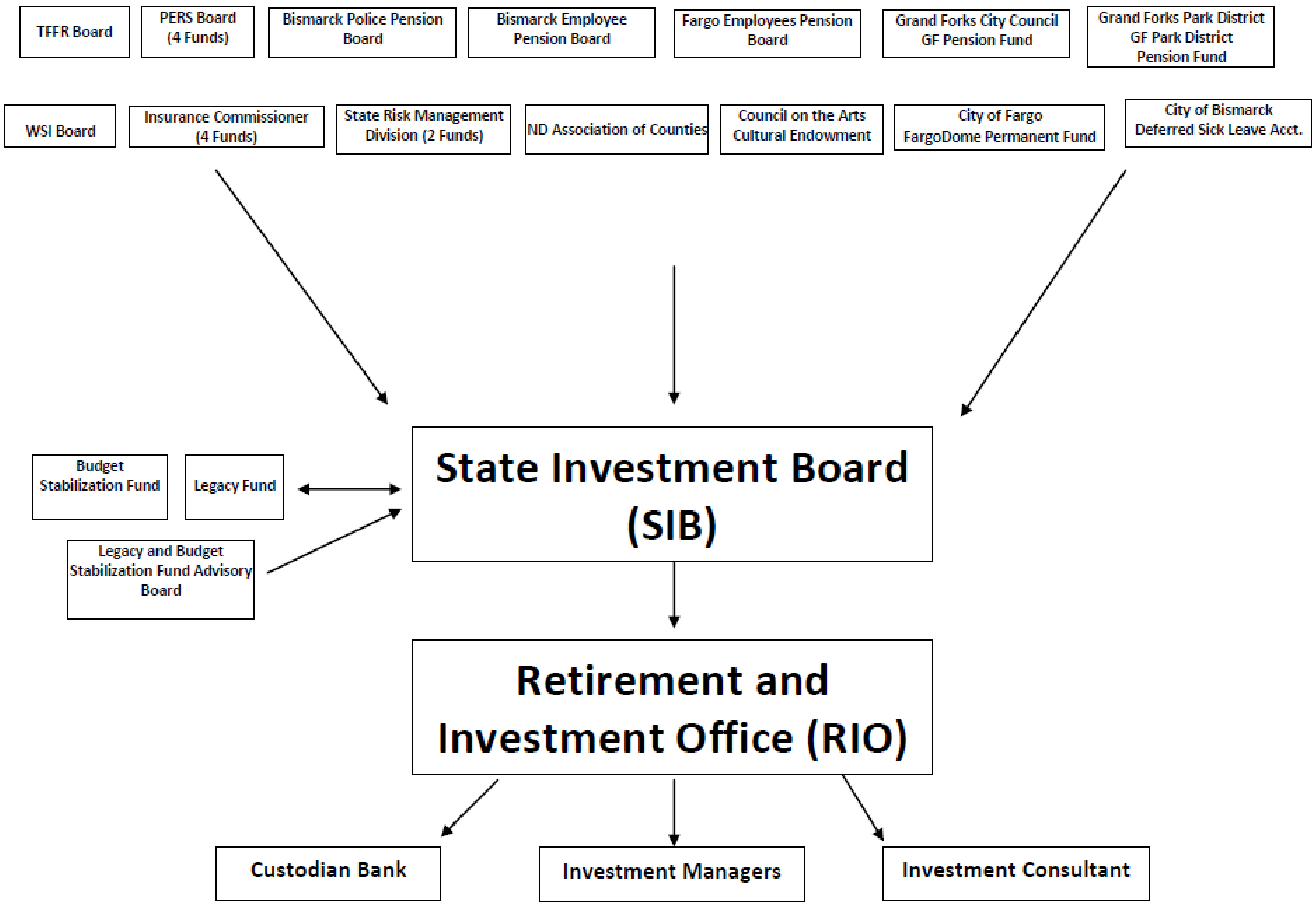
Notes:

In November 2008, voters approved Measure No. 3, which created a tobacco prevention and control trust fund. All tobacco settlement strategic contribution fund payments received by the state will be deposited in the fund. After 2017, no additional strategic contribution fund payments are anticipated.

2009 House Bill 1015, based on the intent of Measure No. 3, creates the Tobacco Prevention and Control Committee as a state agency. Section 35, appropriates funding for the 2009-11 biennium. Section 36, provides retroactive funding for expenditures that occurred during the period of January 1, 2009, through June 30, 2009. Section 39 changes language in the measure concerning the ability to spend funding from the water development trust fund. The legislature required that water development trust fund moneys may only be spent pursuant to legislative appropriation.

A basis point is equal to one one-hundredth of one percent (or 0.01%) such that 100 basis points is equivalent to 1%.

State Investment Board Process



State Investment Board Process

Client Responsibilities: (Per NDCC 21-10-02.1) The governing body of each fund (client) shall establish policies on investment goals and objectives and asset allocation that must include:

- Acceptable rates of return, liquidity and levels of risk
- Long-range asset allocation goals

State Investment Board Responsibilities: (Per NDCC 21-10):

- Implement client asset allocations
- Apply Prudent Investor Rule when investing for fund under its supervision
- Approve general types of securities for investment
- Set policies and procedures regulating securities transactions on behalf of the clients
- Select custodian servicer
- Select investment director and/or investment consulting service
- Create investment pools

State Investment Board Process

Retirement and Investment Office Staff Responsibilities (on behalf of SIB):

- Administer overall investment strategy
- Advise SIB on ways to maximize risk/return opportunities within each asset class
- Act as liaison between SIB and managers, consultant and custodian
- Monitor individual clients' investment guidelines and asset allocations
- Maintain separate accounting for client accounts

Custodian Bank Responsibilities:

- Safe-keep assets
- Settle trades
- Record-keeper

Investment Manager Responsibilities:

- Implement specific mandates or "investment missions"
- Make buy/sell decisions based on investment guidelines
- Report to RIO Staff on regular basis
- Provide education to SIB

State Investment Board Process

Investment Consultant Responsibilities:

- Performance measurement of investment managers
- Manager search assistance
- Provide education to SIB
- Special projects

SIB Members (as of June 17, 2015):

- Lt. Governor Drew Wrigley, *Chair*
- State Treasurer Kelly Schmidt
- Cindy Ternes (WSI Designee)
- Mike Gessner (TFFR)
- Lance Gaebe, University & School Land
- Mel Oslen (TFFR)
- Mike Sandal, *Vice Chair* (PERS)
- Adam Hamm, Insurance
- Rob Lech, *Parliamentarian* (TFFR)
- Yvonne Smth (PERS)
- Tom Trenbeath (PERS)

State Investment Board – Client Assets Under Management

Fund Name	Market Values as of 3/31/15 [1]	Market Values as of 6/30/14 [2]	Market Values as of 3/31/14 [1]
Pension Trust Fund			
Public Employees Retirement System (PERS)	2,401,309,136	2,332,744,037	2,243,514,709
Teachers' Fund for Retirement (TFFR)	2,090,299,471	2,061,684,912	1,995,969,373
Job Service of North Dakota Pension	98,026,580	97,825,769	95,949,225
City of Bismarck Employees Pension	81,230,926	78,804,326	76,180,588
City of Grand Forks Employees Pension	56,504,623	57,896,611	53,425,887
City of Bismarck Police Pension	35,631,338	34,643,204	33,473,553
Grand Forks Park District	6,033,693	5,938,993	5,744,021
City of Fargo Employees Pension	1,489	9,702	36,523
Subtotal Pension Trust Fund	**4,769,037,256**	**4,669,547,555**	**4,504,293,878**
Insurance Trust Fund			
Legacy Fund	3,194,769,809	2,215,941,142	1,930,191,282
Workforce Safety & Insurance (WSI)	1,770,406,238	1,703,987,980	1,660,256,351
Budget Stabilization Fund	595,135,717	586,199,881	589,665,298
City of Fargo FargoDome Permanent Fund	41,752,458	41,775,992	39,463,100
PERS Group Insurance Account	41,205,242	37,425,567	39,225,538
State Fire and Tornado Fund	25,431,804	29,223,707	28,883,451
Petroleum Tank Release Compensation Fund	7,232,124	7,092,998	6,993,990
State Risk Management Fund	6,929,517	6,948,162	6,738,970
State Risk Management Workers Comp Fund	6,290,439	5,965,322	5,777,405
ND Association of Counties (NDACo) Fund	3,562,951	3,445,373	3,352,331
State Bonding Fund	3,339,532	3,268,991	3,219,350
ND Board of Medical Examiners	2,168,964	1,889,897	
Bismarck Deferred Sick Leave Account	881,132	849,818	825,231
Insurance Regulatory Trust Fund	658,357	1,146,038	1,122,648
Cultural Endowment Fund	383,865	364,979	366,130
Subtotal Insurance Trust Fund	**5,700,148,149**	**4,645,525,847**	**4,316,081,075**
PERS Retiree Insurance Credit Fund	96,499,236	90,360,366	85,940,208
Total Assets Under SIB Management	**10,565,684,641**	**9,405,433,768**	**8,906,315,161**

[1] *3/31/15 and 3/31/14 market values are unaudited and subject to change.*

[2] *6/30/14 market values as stated in the Comprehensive Annual Financial Report.*

- SIB Client Assets Under Management grew by approximately 19% or $1.66 billion in the last year.
- The Pension Trust posted a net return of over 6.5%, while the Insurance Trust generated a 5.4% net return in the last year. Investments were responsible for gains of $293 million for the Pension Trust and $233 million for the Insurance Trust.
- Legacy assets increased by 66% (or $1.3 billion) primarily due to tax collections, although net returns were 5.7% for the year ended March 31, 2015.
- SIB client assets exceeded $10.5 billion based on unaudited valuations as of March 31, 2015.

TPCT Fund Investment Allocation

RIO Recommendation:

- Based on forecasted cash flows provided by the TPCT Fund, RIO worked with BlackRock to complete an asset liability review.
- These results were then shared with our investment consultant (Callan) without issue.
- Based on our review procedures, **RIO recommends the TPCT Fund adopt a target asset allocation of 10% equities and 90% to fixed income/cash**.
- Although higher equity allocations were considered, RIO recommends a 10% equity allocation given that the Fund will commence a seven-year liquidation period in 2018.
- The proposed 10% equity and 90% fixed income allocation did not experience a loss in any year during the past decade (and even posted a +2.4% return in 2008).
- RIO's recommendation was discussed with TPCT Executive Director, Jeanne Prom, on June 17, 2015, without any exceptions other than emphasizing that all investments must be intended to be "tobacco free".
- **Based on this asset allocation, the Fund will have an expected long-term rate of return of approximately 2%** with strong downside risk protection so as to preserve capital and benefit from higher return expectations, which are estimated to be 20 times higher than prior years (e.g. the expected 2.0% return is 20 times higher than the sub 0.1% return earned during the last four years).
- **Future investment income is expected to increase by approximately $5 million as a result of this policy change.**

Review of Prior Discussions & Next Steps

- In compliance with NDSIB Governance Policy E-13, RIO provided the TPCT Fund with information about becoming a new SIB investment client. Staff was contacted by Jeanne Prom, Executive Director, and Samantha Doll, Business Manager, of the Tobacco Control and Prevention Trust regarding its investment fund. They currently are invested in short-term cash funds with the Bank of North Dakota and earning approximately 6 to 10 bps per annum. They are interested in contracting for investment services with the SIB as allowed under NDCC 21-10-06 and as recommended in a recent audit.
- The fund has a market value of approximately $47 million as of December 31, 2014 and is projected to exceed $50 million over the next two years prior to declining by approximately $8 million per year between 2018 and 2023. Darren, Connie and I met with Ms. Prom and Ms. Doll on December 3, 2014 and Ms. Doll and Mr. Robert Yost on January 8, 2015 to discuss their investment objectives and risk tolerance and the possible benefits of conducting an asset liability study. Staff has provided additional information as follow-up.
- Based on the initial discussions, internal staff administrative capacity would not be affected by this small fund and the client's goals and risk tolerances <u>although the non-tobacco investment requirement does not fit within the existing Insurance Trust structure</u>.
- **<u>RIO Recommendation as of June 19, 2015</u>: As required by Governance Policy E-13, RIO will request approval from the Industrial Commission to allow the SIB to enter into a contract for investment services with the Tobacco Control and Prevention Trust Fund on or before September 30, 2015.**

Institutional iShares

June 2015

Linh Pham, *Vice President,* Institutional Client Business

Martha Shear, *Vice President,* Institutional iShares

Sunil Shah, CFA, *Director,* Multi-Asset Portfolio & Investment Consulting

Bart Sikora, CFA, *Vice President,* Multi-Asset Portfolio & Investment Consulting

 Created for North Dakota Retirement & Investment Office's Use

Biographies

***Linh Pham*, Vice President**, is a member of the US and Canada Institutional team within BlackRock's Institutional Client Business. She is responsible for developing and maintaining relationships with institutional investors, including public and private pension plans, foundations and endowments.

Ms. Pham's service with the firm dates back to 1999, including her years with Barclays Global Investors (BGI), which merged with BlackRock in 2009. At BGI, she was a client relationship officer in the Americas Institutional Business group, working with defined benefit and defined contribution plans, foundations and endowments. Prior to joining BGI, she was a consulting associate at Callan Associates working with clients on manager searches and performance evaluation for their plans.

Ms. Pham earned her BA degree in economics from the University of California at Los Angeles.

***Martha Shear,* Vice President,** is a member of the iShares Institutional Sales team, based in San Francisco, responsible for managing relationships with foundation and endowment clients across the United States. Ms. Shear advises clients on portfolio construction utilizing passive instruments, with a focus on ETFs, and develops custom solutions addressing the complete range of investment objectives across all asset classes.

Prior to joining BlackRock in 2010, Ms. Shear was a member of the Investment Industry Finance corporate banking group at ING Capital in New York, providing clients with structured finance solutions. Ms. Shear was also previously a member of the loan syndications team at ING Capital. She began her career at Advent International.

Ms. Shear earned a BA in both International Relations and History from Roanoke College.

***Sunil B. Shah,* Director,** is a member of BlackRock's Global Client Group. He works within the iShares group as part of the Product Services and Analytics team.

Mr. Shah's service with the firm dates back to 2009, including his time with Barclays Global Investors (BGI), which merged with BlackRock in late 2009. Prior to joining BGI in 2009, Mr. Shah worked in Fixed Income at Delaware Investments, managing portfolios of insurance assets for multiple clients. Prior to that, he worked at Cambridge Associates developing customized hedge fund-of-fund programs for a variety of endowments and foundations.

Mr. Shah earned an MBA degree from The Anderson School at UCLA and a BBA degree in Actuarial Science from Georgia State University. Mr. Shah is a Chartered Financial Analyst and an Associate of the Society of Actuaries.

***Bart Sikora*, Vice President,** is a member of the Multi-Asset Portfolio & Investment Consulting team (MAPIC) within the Multi-Asset Strategies Group, working with RIA, Pensions/Foundations & Endowments, and Insurance clients.

Before joining the group in 2011, Bart was a Senior Portfolio Manager in the Global Asset Allocation team at Mellon Capital Management, managing long/short portfolios and relative value hedge funds. Prior to that, Bart spent five years at Barclays Global Investors, most recently as a Portfolio Manager in the Global Equity group, managing and helping to launch international equity iShares portfolios.

Bart holds a BS degree in Business Administration from the University of California at Berkeley and MBA in Finance and Accounting from UCLA. Bart also holds the CFA designation.

Table of Contents

I. Institutional Uses of ETFs

BlackRock at a glance

BlackRock Mission Statement

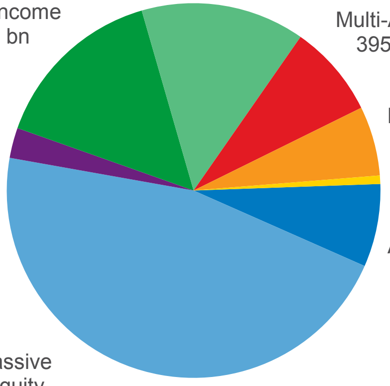
Create a better financial future for our clients by building the most respected investment and risk manager in the world

BlackRock facts *

- Established in 1988
- NYSE: BLK
- $4.77 trillion assets under management
- More than 12,000 employees
- More than 1,800 investment professionals **
- Offices in over 30 countries
- 28 primary investment centers **
- Clients in over 100 countries
- Over 700 iShares® ETFs
- Through BlackRock Solutions, the Firm provides risk management and enterprise investment services for over 200 clients
- Financial Markets Advisory business managed or advised on over $8 trillion in asset and derivative portfolios
- Transition Management team partners with clients to save costs and reduce risks when changing investment exposures

* As of 31 March 2015
** As of 31 December 2014

$4.77 trillion managed across asset classes



Assets as of 31 March 2015
[1] Includes commodity and currency mandates

iShares ETFs development rooted in over 40 years of index leadership

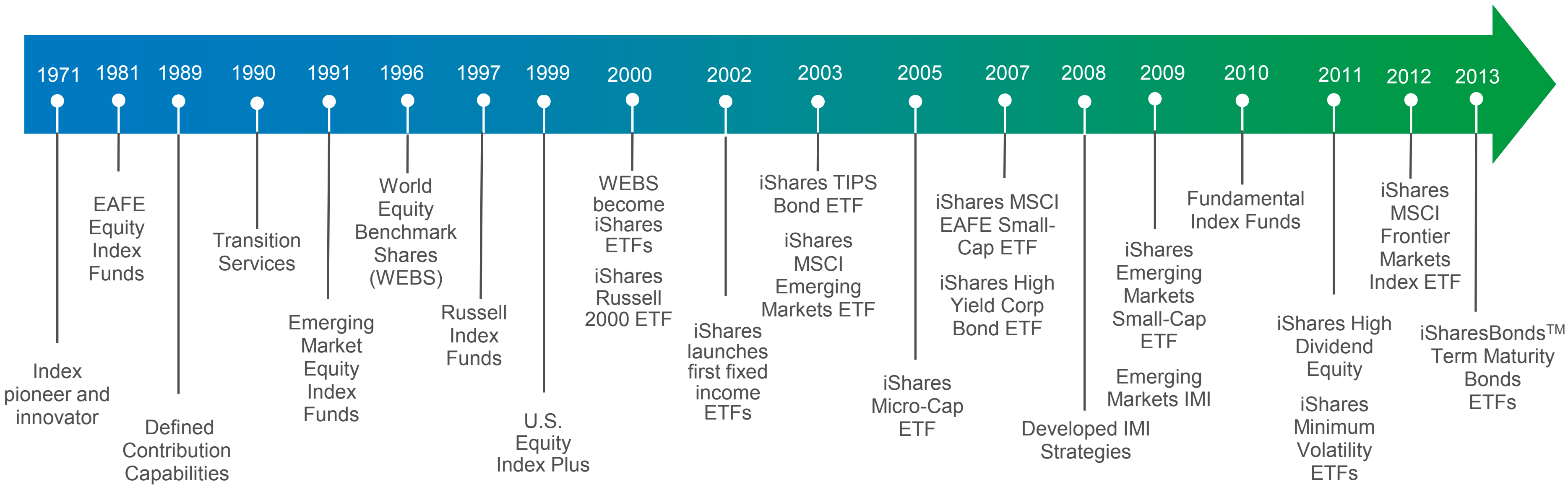
The BlackRock difference – helping to deliver on client objectives

Sole focus on asset management
- Pure play asset manager with independent ownership and governance
- Clear fiduciary objective with clients
- Focus on best execution across trading platforms
- Leading "voice" in institutional asset management industry

Experience and innovation
- 40+ years of indexing experience, innovation and index advocacy
- Integrated/customized solutions to help meet client objectives
- Risk-managed index solutions is a core BlackRock business

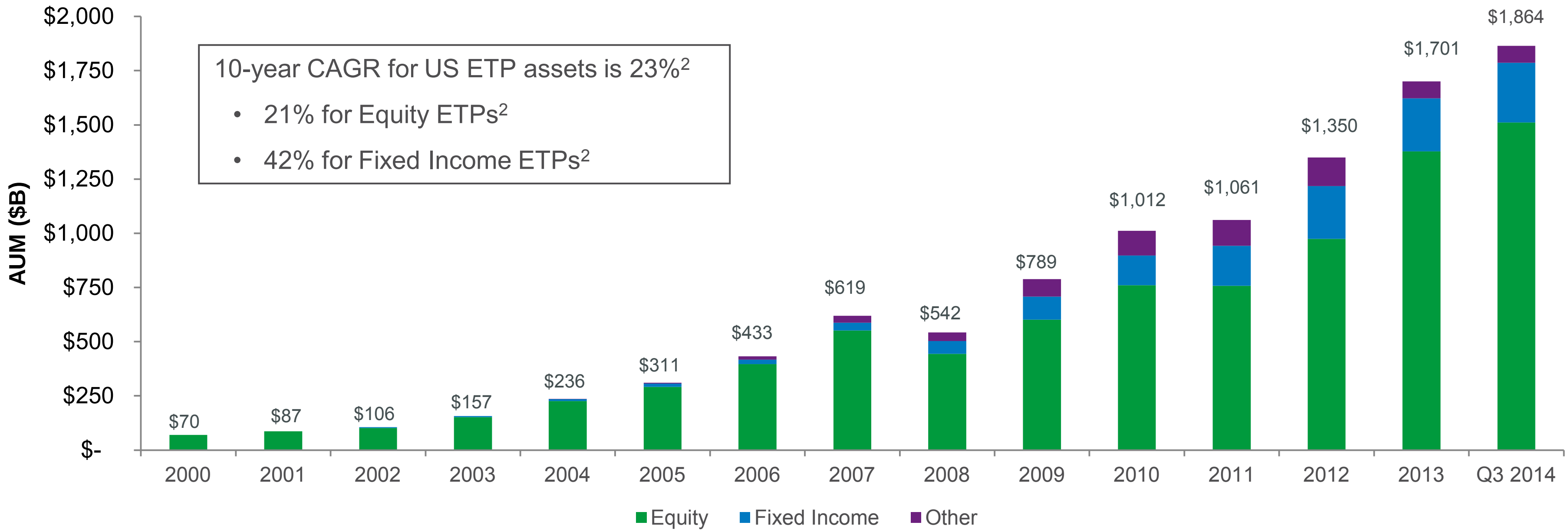
Scale and scope of indexing business
- Uniquely positioned as the world's largest asset manager
- Leveraging scale into reduced fund management costs
- Client access to depth of research, portfolio management and trading resources and experience

Unique dedication of research and technology resources
- Dedicated team focused on index methodology and research
- State of the art portfolio management system and transaction cost model a key differentiator
- Implementation of industry's most respected enterprise risk system



Growth of exchange traded funds in the US

Increasing adoption of exchange traded products (ETPs)[1]



Source: BlackRock, Bloomberg, ICI as of 9/30/14. "Other" category includes alternatives, commodities, currency, target date, asset allocation, and fund of funds.

Notable statistics[3]

- US ETP AUM has risen from $70.6 billion in 2000 to $1.9 trillion YTD in 2014. US ETPs had ~$124 billion of inflows in 2014
- iShares is the largest ETP provider in the US, with $660 billion of the $1.7 trillion in 2013, representing a 39% market share
- ETFs represented ~25% of US daily equity trading volume in 2013[3]

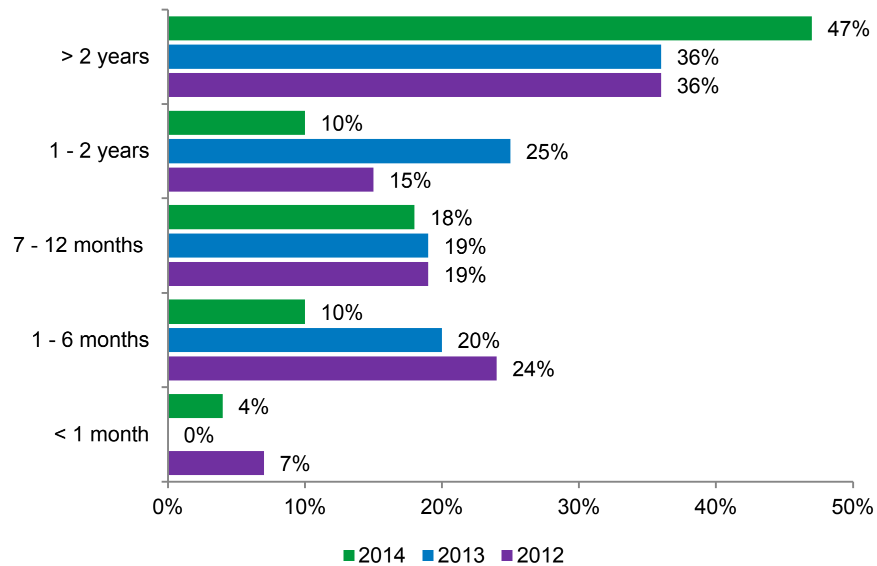
1."ETP" (or exchange traded product) as referred to above means any portfolio exposure security that trades intraday on a US exchange. ETPs include exchange traded funds (ETFs) registered with the SEC under the Investment Company Act of 1940 (open-end funds and unit investment trusts or UITs) and certain trusts, commodity pools and exchange traded notes (ETNs) registered with the SEC under the Securities Act of 1933. Statistics as of 9/30/14 unless otherwise noted.
2.Data is as of September 30th, 2014. ETP flows and assets are sourced using shares outstanding and net asset values from Bloomberg. Inflows for years prior to 2010 are sourced from Strategic Insights Simfund. Asset classifications are assigned by the BlackRock based on product definitions from provider websites and product prospectuses. Other static product information is obtained from provider websites , product prospectuses, provider press. The 10-year CAGR for Equity and Fixed Income ETPs are calculated by BlackRock. CAGR, or Compound Annual Growth Rate, is the year over year growth rate over a specified period of time.
3.Source: BlackRock ETP Research, Bloomberg, NYSE Arca.

ETF applications: pensions, foundations, endowments

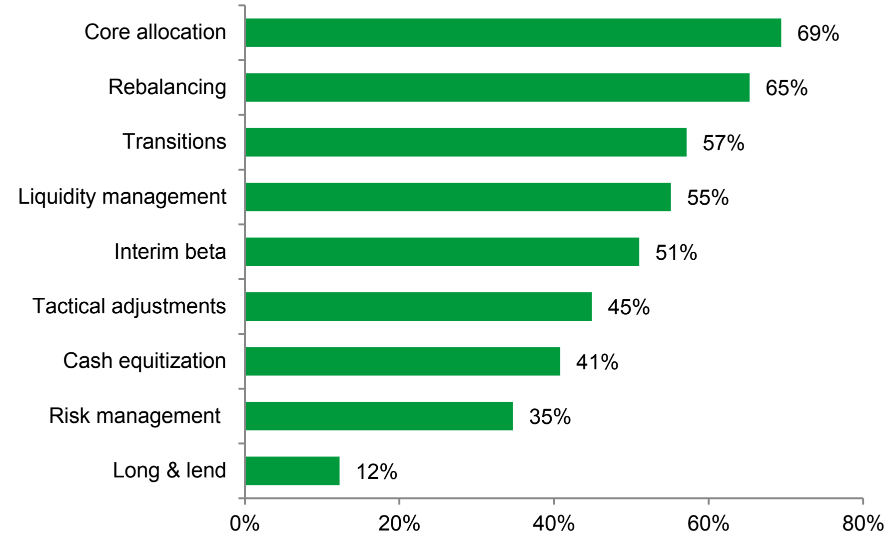
While institutional funds continue to extend holding periods, the most commonly cited use of ETFs is to obtain core portfolio exposures.

- Longer holding periods: 47% reported typically holding ETFs for over two years, up from 36% in 2013
- Increased citation of strategic use, with “core allocation” as the most common application

Institutional Fund ETF Holding Periods



ETFs Usage Trends



49% of institutional funds surveyed reported average ETF holding periods of two years or longer, up from 39% in 2013

Institutional funds are continuing to apply ETFs to a broad mix of portfolio functions

Source: Greenwich Associates. “ETFs: An Evolving Toolset for U.S. Institutions.” Report is based on interviews with 49 “institutional funds” (defined as U.S. corporate and public pension funds, endowments, and foundations) conducted between February and April 2014.

Access to dedicated iShares ETF expertise and resources

Institutional Client Access

Multi-Asset Portfolio & Investment Consulting Group
- Deliver consulting across asset classes and product structures
- Help clients with portfolio structure decisions and product selection

Product Development
- Engine of innovation to deliver relevant client solutions
- Responsive to client needs and current trends

Portfolio Management
- Index research
- Portfolio construction insight
- In-depth product knowledge

Dedicated Institutional Team
- Experienced market professionals
- Product-specific knowledge
- Solutions provider

Capital Markets
- Liquidity sourcing
- iShares transaction cost analysis
- iShares execution strategies

Equity/Fixed Income Trading
- Real-time, "on the ground" market insight
- Technology implementation
- Seeking best execution

Capital Markets can help you achieve a positive trading experience

Market Insights

Analyse the effect of global markets on trading & liquidity

We sit in the center of the ETF ecosystem with continuous live market updates from our partners

Trade Guidance

What is the expected impact for this trade?

We use proprietary Pre-Trade Analytics to deliver customized trade guidance

iShares Capital Markets

We will direct you to one of our broker dealer partners given our knowledge of their inventory and capabilities

Broker Resources

Which broker dealers have been active in this name?

We provide customized trading strategies (VWAP, block trade) depending on implementation timeline and investment objectives

Trade Strategy

What alternatives are available to help minimize the impact?

Layers of liquidity

The iShares Capital Markets Team generates Transaction Cost Analyses (TCA) to enable clients to receive best execution and find the most cost efficient source of liquidity

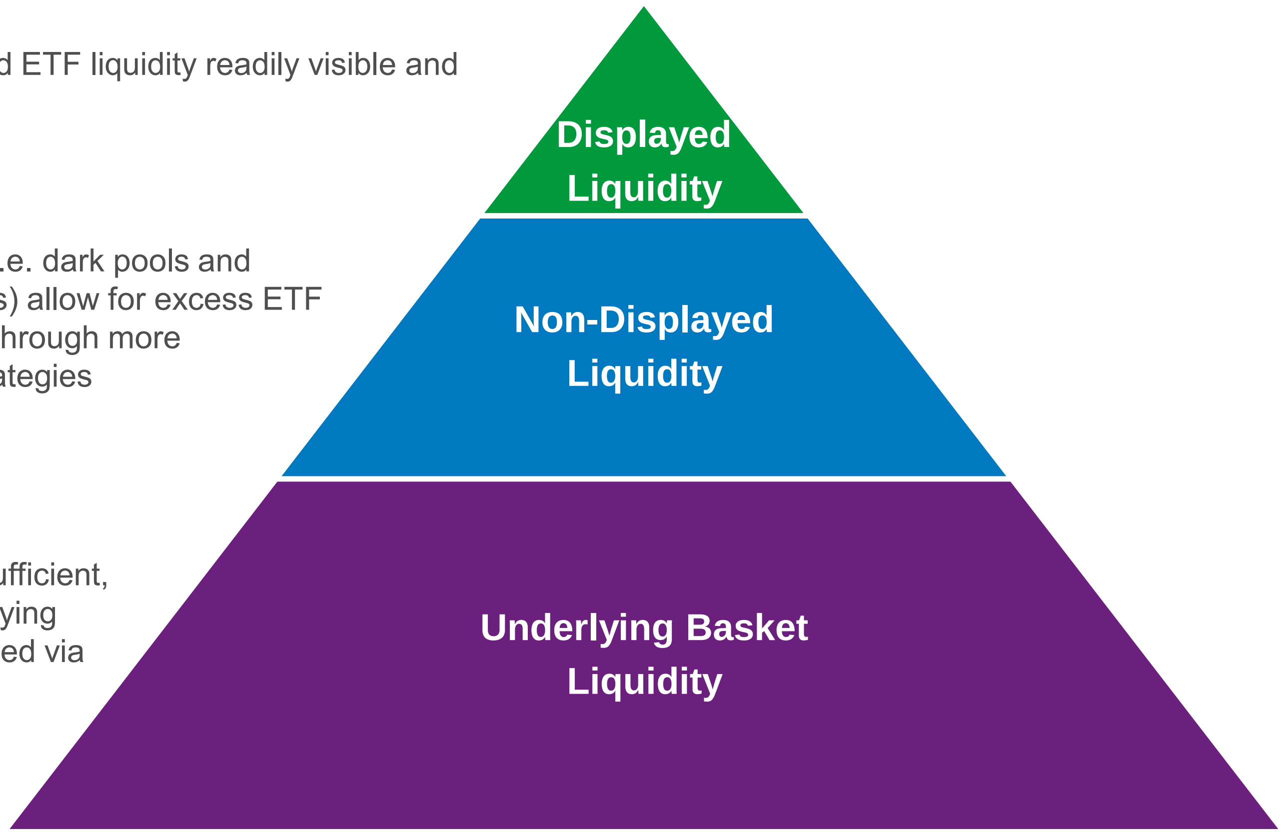
ETF Liquidity

Represents the displayed ETF liquidity readily visible and available to trade

Non-displayed liquidity (i.e. dark pools and market maker indications) allow for excess ETF liquidity to be accessed through more sophisticated trading strategies

Underlying Liquidity

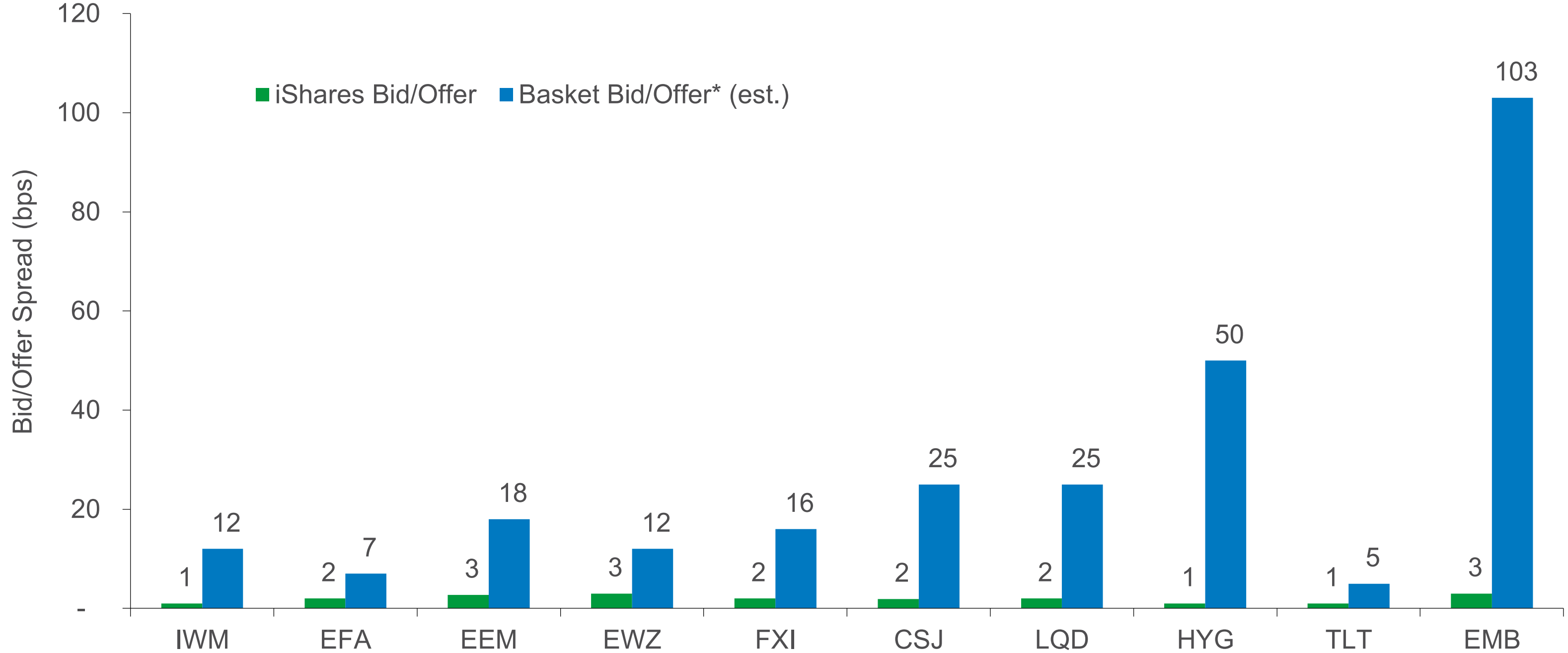
If the ETF liquidity is insufficient, the liquidity of the underlying securities can be accessed via the creation/redemption process



There can be no assurance that an active trading market for shares of an ETF will develop or be maintained.

iShares ETFs offer low-cost, market access

iShares ETFs generally offer price improvement, making the ETF less expensive to trade than the underlying securities of the respective index



iShares ETF Name	Russell 2000	MSCI EAFE	MSCI Emerging Markets	MSCI Brazil Capped	FTSE China 25	Barclays 1-3 Year Credit	Markit iBoxx USD Investment Grade Corporate	Markit iBoxx USD High Yield Corporate	Barclays 20+ Year Treasury	iShares JP Morgan USD EM Bond ETF
iShares ADV($M)**	4,365	1,402	2,207	775	772	48	252	782	840	137
iShares AUM ($M)	26,233	52,223	32,189	3,996	5,988	10,967	19,310	14,380	6,446	4,401

*Market Bid/Offer spread refers to the underlying securities of the respective index

**20-day average daily volume, as of 12/31/14.

For illustrative purposes only. Source: BlackRock, Bloomberg, Barclays, NYSE Arca, as of 12/31/14.

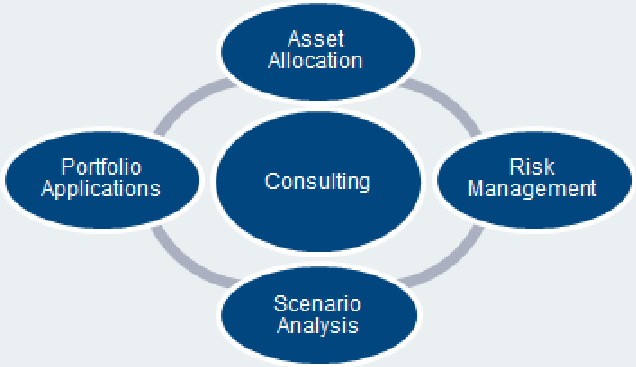
II. Responsible Investing Solutions

Multi-Asset Portfolio and Investment Consulting

Multi-Asset Portfolio & Investment Consulting

The Multi-Asset Portfolio and Investment Consulting (MAPIC) Group is a dedicated team of BlackRock consultants who provide clients with premium access to comprehensive, objective, institutional-caliber portfolio and investment expertise. We help clients think through their most pressing investment-related issues and construct customized portfolio solutions tailored to their unique circumstances.

Overview



Our goal

Our goal is to partner with each client by tailoring portfolio and investment solutions to fit their unique investment philosophy. Our team provides additional value by providing insights regarding current and emerging investment trends based on our unique perspective within BlackRock and the investment industry.

Our value

Our clients often consider us an independent consulting team or an extension of their portfolio and investment research team.

Our difference

Each firm has the benefit of leveraging our team of consultants that has unique and direct access to resources across the globe. These resources include BlackRock's deep history of thought leadership, innovation in active and passive investing, and robust analytical capabilities.

Who we are

Collectively, the consulting team has over 50 years of investment-related experience with backgrounds ranging from portfolio managers to institutional consultants to researchers. We bring a wide set of professional experiences to help clients solve problems.

Consultants hold graduate degrees and/or CFAs.

Consultants sit within and leverage the broader Investment Research & Strategy team at Blackrock in order to provide robust portfolio solutions to clients.

Overview of Responsible Investing Solution Approach

The following was provided to BlackRock by North Dakota Retirement & Investment Office (NDRIO) on behalf of the fund:

Objective: Diversify current allocation of cash to equities and bonds in the hopes of achieving an increased return compared to recent annual returns of approximately 5.6 bps.

Restriction guidelines: Ex-tobacco, low risk tolerance given projected cash outflows (table below).

Based on this objective and the guidelines provided, the following analysis includes two potential asset allocation solutions which are then compared from a forward-looking (ex-ante) perspective:

- **Solution 1:** Equity/Fixed Income Allocation Proposal - An equity and fixed income portfolio with a low volatility target, analysed from both a historical perspective and using a Monte-Carlo simulation with cash flows built into the analysis
- **Solution 2:** Fixed Income Allocation Proposal - A fixed income portfolio with specified investment fixed income allocations with explicit investment end-dates for further reduction of uncertainties

Fiscal Year July 1 to 30-Jun	Beginning Balance	Fiscal Year Cash Flows Inflows	Outflows	Net Flows	($ in millions) Ending Balance
2009	$0.00	$14.10	$0.00	$14.10	$14.10
2010	$14.10	$12.20	($3.50)	$8.70	$22.80
2011	$22.80	$11.20	($4.60)	$6.60	$29.40
2012	$29.40	$11.40	($5.70)	$5.70	$35.10
2013	$35.10	$11.40	($6.80)	$4.60	$39.70
2014	$39.70	$11.40	($7.90)	$3.50	$43.20
2015	$43.20	$11.40	($7.90)	$3.50	$46.70
2016	$46.70	$11.40	($7.90)	$3.50	$50.20
2017	$50.20	$11.40	($7.90)	$3.50	$53.70
2018	$53.70	$0.00	($7.90)	($7.90)	$45.80
2019	$45.80	$0.00	($7.90)	($7.90)	$37.90
2020	$37.90	$0.00	($7.90)	($7.90)	$30.00
2021	$30.00	$0.00	($7.90)	($7.90)	$22.10
2022	$22.10	$0.00	($7.90)	($7.90)	$14.20
2023	$14.20	$0.00	($7.90)	($7.90)	$6.30
2024	$6.30	$0.00	($6.30)	($6.30)	$0.00

Source: NDRIO

Proposed Solutions

Outline
Solution 1: Equity/Fixed Income Allocation

Solution 1: Equity/Fixed Income Allocation Proposal displays allocation combinations of an ex-tobacco equity fund and a low duration U.S. Treasury fund for a potentially low relative volatility level with the objective of reduced risk of missing future cash flow payments.

Funds[1]:
iShares MSCI USA ESG Select ETF (ticker: KLD)
Benchmark: MSCI USA ESG Select Index
Fund expense ratio: 50 bps
Inception date: 1/24/2005
Net assets: $313M

iShares 1-3 Year Treasury Bond ETF (ticker: SHY)
Benchmark: Barclays U.S. 1-3 Year Treasury Bond Index
Fund expense ratio: 15 bps
Inception date: 7/22/2002
Net assets: $8.167B

[1] *Fund data as of 1/13/15. Source: Bloomberg*

Outline

Solution 2: Fixed Income Allocation – Corporate iBonds

Solution 2: Fixed Income Allocation Option displays ladder allocation combinations using iBonds®, a suite of specified investment end-date "bullet" funds, which may be used to help manage interest rate risk if held to maturity. In turn, the laddered allocation could minimize the shortfall risks of fulfilling future cash outflow obligations. Similar to individual bonds held to maturity, the risk of default remains. However, unlike individual bonds, the extent of default risk may be mitigated by the diversified holdings of the fund. Re-investment risk does not apply as the portfolio will be fully liquidated.

Funds:
iBonds® Mar 2016 Corporate ETF (ticker: IBDA)
iBonds® Mar 2018 Corporate ETF (ticker: IBDB)
iBonds® Mar 2020 Corporate ETF (ticker: IBDC)
iBonds® Mar 2023 Corporate ETF (ticker: IBDD)

Outline

Solution 3: Fixed Income Allocation – Municipal iBonds

Solution 3: Fixed Income Allocation Option displays ladder allocation combinations using iBonds®, a suite of specified investment end-date "bullet" funds, which may be used to help manage interest rate risk if held to maturity. In turn, the laddered allocation could help minimize the shortfall risks of fulfilling future cash outflow obligations. Similar to individual bonds held to maturity, the risk of default remains. However, unlike individual bonds, the extent of default risk may be mitigated by the diversified holdings of the fund. Re-investment risk does not apply as the portfolio will be fully liquidated.

Funds:
iBonds® Sep 2017 AMT-Free Muni Bond ETF (ticker: IBMF)
iBonds® Sep 2018 AMT-Free Muni Bond ETF (ticker: IBMG)
iBonds® Sep 2019 AMT-Free Muni Bond ETF (ticker: IBMH)
iBonds® Sep 2020 AMT-Free Muni Bond ETF (ticker: IBMI)

Next Steps

- Identification of the most attractive allocation
- Further allocation adjustment on weights and tickers, if needed
- Additional metrics and analysis, if needed

Appendix

Important information regarding iShares ETFs

Carefully consider the Funds' investment objectives, risk factors, and charges and expenses before investing. This and other information can be found in the Funds' prospectuses or, if available, the summary prospectuses which may be obtained by visiting www.iShares.com or www.blackrock.com. Read the prospectus carefully before investing.

Investing involves risk, including possible loss of principal.

Fixed income risks include interest-rate and credit risk. Typically, when interest rates rise, there is a corresponding decline in bond values. Credit risk refers to the possibility that the bond issuer will not be able to make principal and interest payments. Non-investment-grade debt securities (high-yield/junk bonds) may be subject to greater market fluctuations, risk of default or loss of income and principal than higher-rated securities. An investment in the Fund is not insured or guaranteed by the Federal Deposit Insurance Corporation or any other government agency and its return and yield will fluctuate with market conditions. Securities with floating or variable interest rates may decline in value if their coupon rates do not keep pace with comparable market interest rates. A fund's income may decline when interest rates fall if most of the debt instruments held by the fund have floating or variable rates. There is no guarantee that dividends will be paid.

When comparing stocks or bonds and iShares Funds, it should be remembered that management fees associated with fund investments, like iShares Funds, are not borne by investors in individual stocks or bonds. The annual management fees of iShares Funds may be substantially less than those of most mutual funds. Buying and selling shares of iShares Funds will result in brokerage commissions.

International investing involves risks, including risks related to foreign currency, limited liquidity, less government regulation and the possibility of substantial volatility due to adverse political, economic or other developments. These risks often are heightened for investments in emerging/developing markets, in concentrations of single countries or smaller capital markets.. Narrowly focused investments, including REIT, mining, preferred stock, factor and floating rate note funds may be subject to higher volatility and risks specific to those sectors. The iShares Minimum Volatility ETFs may experience more than minimum volatility as there is no guarantee that the underlying index's strategy of seeking to lower volatility will be successful.

Investment in a fund of funds is subject to the risks and expenses of the underlying funds.

Actively managed funds do not seek to replicate the performance of a specified index and may have higher portfolio turnover than index funds.

Important information regarding iShares ETFs

A fund's use of derivatives may reduce a fund's returns and/or increase volatility and subject the fund to counterparty risk, which is the risk that the other party in the transaction will not fulfill its contractual obligation. A fund could suffer losses related to its derivative positions because of a possible lack of liquidity in the secondary market and as a result of unanticipated market movements, which losses are potentially unlimited. There can be no assurance that any fund's hedging transactions will be effective. The iShares Funds are distributed by BlackRock Investments, LLC (together with its affiliates, "BlackRock").

The iShares Funds are not sponsored, endorsed, issued, sold or promoted by FTSE International Limited ("FTSE"), India Index Services & Products Limited, JPMorgan Chase & Co., MSCI Inc., Markit Indices Limited or S&P Dow Jones Indices LLC. None of these companies make any representation regarding the advisability of investing in the Funds. BlackRock is not affiliated with the companies listed above.

Not FDIC Insured • No Bank Guarantee • May Lose Value

Important information regarding iBonds® ETFs

The iShares® iBonds® ETFs ("iBonds") will terminate within the month and year in each Fund's name. An investment in the iBonds is not guaranteed, and an investor may experience losses and/or adverse tax consequences, including near or at the termination date. In the final months of each iBond's operation, its portfolio will transition to cash and cash-like instruments. As a result, its yield will tend to move toward prevailing money market rates, and may be lower than the yields of the bonds previously held by the Fund and lower than prevailing yields in the bond market. The iBond's distributions and liquidation proceeds are not predictable at the time of investment and the iBonds do not seek to return any predetermined amount.

Investment in a fund of funds is subject to the risks and expenses of the underlying funds.

AGENDA ITEM III.C.

INFORMATIONAL – NO BOARD ACTION REQUESTED

TO: State Investment Board

FROM: Dave Hunter

DATE: June 19, 2015

SUBJECT: North Dakota Bankers Association ("NDBA") Meeting Update

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Background:

Rick Clayburgh, NDBA President and CEO, arranged a meeting with RIO to improve our mutual understanding of the investment services offered by our North Dakota based firms and review the search process and selection criteria utilized by the SIB and RIO. RIO's CIO & Deputy CIO attended this meeting on April 13, 2015, along with Paul Erlendson of Callan and 10 North Dakota based investment professionals.

Overall Observations:

1) The vast majority of our North Dakota based investment firms specialize in providing multi-asset class solutions;
2) Bell State Bank has the ability to provide single and multi-asset class solutions;
3) SIB clients have historically utilized single asset class investment strategies over multi-asset class solutions;
4) All attendees expressed a strong desire to improve their ability to work together;
5) There was a general concern about the appropriateness of the Callan manager database due to a perceived or actual "poor fit";
6) There was a favorable response to the NDSIB Due Diligence Questionnaire; and
7) RIO gained a better understanding of the concerns raised by the group attending this meeting.

Prior Actions:

Based on the favorable response to # 6, RIO supplied the NDSIB Due Diligence Questionnaire to Rick Clayburgh on April 13, 2015, who subsequently distributed the document to interested firms. RIO noted this nine-page questionnaire is generally required to be completed by all SIB investment managers at least once a year.

Recent Actions:

During the past two months, RIO has received a completed Due Diligence Questionnaire (and other supporting documentation) from the following five firms:

1) First Western Bank and Trust - Chris Lamoureux, SVP;
2) First International Bank and Trust - Cal Perleberg, Wealth Management Officer (John Stibbe);
3) Alerus Financial - Paul Dadlez, Director Wealth Advisory Services - Twin Cities (Ann McCoon);
4) Bell Wealth Management - Patrick Chaffee, EVP - Managing Director; and
5) American Trust Center - Joseph Heringer, J.D. - Personal Trust Manager (Bob Willer).

RIO intends to review the responses of these five firms over the next month, share the data with Callan shortly thereafter, and provide a further update to the SIB in a subsequent meeting.

AGENDA ITEM III. D.

INFORMATIONAL ONLY

TO: State Investment Board

FROM: Dave Hunter, Executive Director/CIO

DATE: June 19, 2015

SUBJECT: Timber Investment Resources ("TIR") - Springbank Update

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Background:

The Pension Trust currently has a $116 million timber investment in **Springbank**, which is managed by TIR.

- In our March meeting, the SIB approved RIO's recommendation to engage Callan to conduct an in-depth evaluation of this investment and the investment manager (TIR).
- In April, the SIB approved a three month extension to the existing management agreement (to 9/30/15) so as to allow additional time to negotiate a long-term contract extension.
- In May, the SIB accepted Callan's recommendation to extend and revise the terms of the Springbank agreement and authorized RIO to finalize the revised terms to extend the Springbank agreement through 2022.

Update:

On June 18, 2015, RIO and TIR mutually agreed to reasonable business terms to extend the Springbank agreement through 2022 along with the following key provisions:

1. TIR's ability to serve notice to resign as manager was extended from 60 days to 120 days;
2. Investors gained the right to select an independent appraisal firm in the event of a contested property valuation;
3. Investors no longer waive the right to initiate legal action to seek dissolution;
4. The asset management fee has been significantly reduced versus TIR's original proposal;
5. An earned incentive fee will be paid, however, the "holdback portion" of the incentive fee will be eliminated;
6. Interim incentive fee payments will be eliminated after the above "account adjustment"; and
7. The final incentive fee will be based on the Investors "waterfall" method, not the method previously used to derive the "holdback portion" of the incentive fee referenced in point 5.

NOTE: All terms are subject to approval by the Houston Firefighters' Retirement and Relief Fund (which maintains a 24% interest, while the SIB retains its 76% interest) and satisfactory legal documentation.

AGENDA ITEM IV.A.

TO: State Investment Board

FROM: Dave Hunter, Executive Director/CIO

DATE: June 26, 2015

SUBJECT: SIB Governance Manual Review – **BOARD ACTION**

As directed by SIB Governance Manual Policy B-7 Section 4.C, the SIB conducted an annual review of the governance manual on September 26, 2014. Based on Board member discussion during this annual review, the Executive Director proposed a section by section review of the governance manual during the first half of 2015 which will culminate in a "Governance Day Offsite" scheduled for July 24, 2015. The Governance Day Offsite is intended to take the place of a regularly scheduled SIB meeting, but is expected to be expanded in length to allow for a deeper and more holistic discussion of overall Board governance policies.

January 2015	Governance Process – Accepted 2-27-2015
February	Executive Limitations – Accepted 3-27-2015
March	Board Staff Relationship – Accepted 4-24-2015
April	Ends – Board Acceptance – Accepted 5-22-2015
May	**Investments – "Second Reading" (Board Action)**
June	**By-Laws – "First Reading" (Informational)**
July	Governance Day Offsite

RIO will conduct a "second reading" of the "Investments" section of the Governance Manual at this meeting and then request SIB acceptance. RIO will then seek to review the "By-Laws" section of the Governance ("first reading") with the SIB.

NOTE: If the "By-Laws" section can be read in advance of our meeting, we may be able to reduce our combined review time.

Sections E. and H. of the SIB Governance Manual on "Investments" and "By-Laws" follow.

E. *INVESTMENTS*

PAGE

EXHIBITS

POLICY TITLE: *FIDUCIARY DUTIES*

By virtue of the responsibilities assigned to the SIB by North Dakota Century Code Chapter 21-10, the members of the SIB are fiduciaries for twelve statutory funds. Through contractual obligations, fiduciary responsibility extends to eleven additional funds.

A fiduciary is a person who has discretionary authority or management responsibility for assets held in trust to which another has beneficial title or interest. The fiduciary is responsible for knowing the "prudent requirements" for the investment of trust assets. Remedial actions may be assessed against fiduciaries for violations of fiduciary duty.

North Dakota state law provides broad fiduciary guidelines for the SIB members. NDCC 21-10-07 specifies that "the state investment board shall apply the prudent investor rule in investing for funds under its supervision. The "prudent investor rule" means that in making investments, the fiduciaries shall exercise the judgment and care, under the circumstances then prevailing, that an institutional investor of ordinary prudence, discretion, and intelligence exercises in the management of large investments entrusted to it, not in regard to speculation but in regard to the permanent disposition of funds, considering probable safety of capital as well as probable income."

Procedural prudence is a term that has evolved to describe the appropriate activities of a person (or persons) who act in a fiduciary role. Court decisions to date indicate that procedural prudence is more important in assessing fiduciary activities than actual portfolio performance. A fiduciary cannot be faulted for making the "wrong" decision provided that proper due diligence was performed.

The key to successfully discharging the SIB's fiduciary duties is the establishment of and adherence to proper due diligence procedures. While not bound by ERISA (Employee Retirement and Income Security Act of 1974), the SIB will use the procedural prudence outlined by ERISA as guidance in developing its procedures:

1. An investment policy must be established for each fund and must be in writing.

2. Plan assets must be diversified, unless under the circumstances it would be prudent not to do so.

3. Investment decisions must be made with the skill and care of a prudent expert.

4. Investment performance must be monitored.

5. Investment expenses must be controlled.

6. Prohibited transactions must be avoided.

Policy Implemented: September 20, 1995.
Amended: May 30, 1997; January 22, 1999; February 27, 2009

POLICY TYPE: INVESTMENTS

POLICY TITLE: *INVESTMENT PROCESS*

The SIB believes that an investment program must be built and managed like any good business, with a clear statement of mission, overall objectives, roles and responsibilities, and policies and guidelines. Major issues to be faced by the SIB will revolve around:

Asset allocation targets:

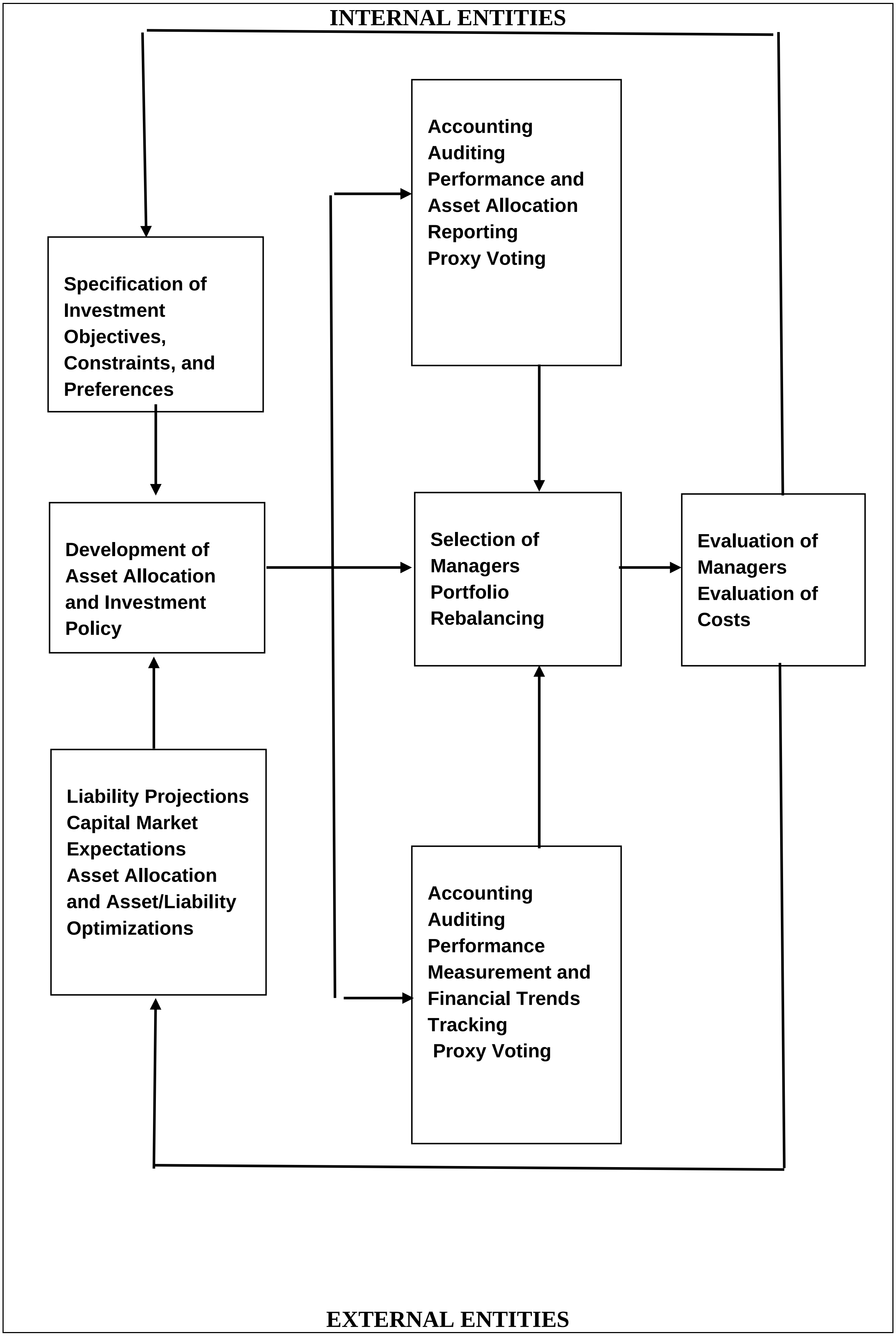
- Setting appropriate benchmarks.
- Finding the right managers.
- Monitoring the program.
- Searching for appropriate new opportunities.

To ensure rigorous attention to all aspects of the investment program, the SIB follows an established investment process. This process, described by the diagram on the following page, involves three phases:

- Investment policy development/modification.
- Implementation/monitoring.
- Evaluation.

The first column of boxes describes the policy development phase, the middle column implementation/monitoring, and the last box on right evaluation. Activities associated with internal entities are shown along the top. Those associated with external entities are shown along the bottom. The middle shows activities that internal and external entities work on together.

Policy Implemented: September 20, 1995.


INTERNAL ENTITIES
Accounting
Auditing
Performance and
Asset Allocation
Reporting
Proxy Voting
Specification of
Investment
Objectives,
Constraints, and
Preferences
Development of
Asset Allocation
and Investment
Policy
Selection of
Managers
Portfolio
Rebalancing
Evaluation of
Managers
Evaluation of
Costs
Liability Projections
Capital Market
Expectations
Asset Allocation
and Asset/Liability
Optimizations
Accounting
Auditing
Performance
Measurement and
Financial Trends
Tracking
Proxy Voting
EXTERNAL ENTITIES

The key responsibilities of the entities involved in the investment program are:

Fund Governing Bodies

1. Establish policy on investment goals and objectives.
2. Establish asset allocation.
3. Hire actuary when required.

SIB

1. Invest funds entrusted by statute and contracted entities.
2. Set policies on appropriate investments and investment practices for entrusted funds.
3. Approve asset allocation and investment policies of participating trust funds.
4. Report the investment performance of the funds to each fund's governing authority.
5. Hire and terminate money managers, custodians, and consultants.

Investment Officer and RIO Staff

1. Implement investment policies approved by the SIB.
2. Provide research and administrative support for SIB projects.
3. Recommend investment regulations appropriate for governing the investment of entrusted funds.
4. Assist fund governing bodies in developing asset allocation and investment policies.
5. Evaluate money manager adherence to investment objectives.
6. Provide performance reports to the SIB and boards of participating funds.
7. Recommend hiring or terminating money managers, custodians, consultants, and other outside services needed to effectively manage the investment funds.
8. Develop and maintain appropriate accounting policies and systems for the funds entrusted to the SIB.

Investment Consultant

1. Measure money manager performance and monitor adherence to investment goals, objectives, and policies.
2. Conduct annual evaluation of program policies and results, and assist in development of annual work plan.
3. Assist in implementation of annual work plan.
4. Conduct asset allocation or asset/liability studies.
5. Conduct requested money manager searches.
6. Assist in development of investment policies and manager structure and rebalancing guidelines.
7. Extension of staff for special projects.

Actuary

1. Assist fund governing bodies in developing benefit and funding policies.
2. Measure actuarial soundness of plan.
3. Perform experience studies as requested by plan sponsor.
4. Provide liability projections as needed.
5. Conduct annual evaluation of program policies and results, and assist in developmental of annual work plan.
6. Assist in implementation of annual work plan.

Auditor

1. Measure, validate, and offer an opinion on agency financial statements and management.
2. Assist in developing appropriate accounting policies and procedures.
3. Bring technical competence, sound business judgment, integrity, and objectivity to the financial reporting process.

Master Custodian

1. Provide safekeeping of all securities purchased by managers on behalf of the SIB.

2. Provide global custody services.

3. Collect interest, dividend, and principal payments in a timely manner.

4. Provide for timely settlement of securities.

5. Price all securities and post transactions daily.

6. Maintain short-term investment vehicles for investment of cash not invested by SIB managers. Sweep all manager accounts daily to ensure all available cash is invested.

7. Provide monthly, quarterly, and annual accounting reports for posting to RIO's general ledger.

8. May manage a securities lending program to enhance income.

9. Provide electronic access to accounting reports.

10. Provide other services that assist with the monitoring of managers and investments.

Portfolio Managers

1. Manage portfolios as assigned by the SIB.

2. Provide liquidity, as required, in a timely and cost-efficient manner.

3. Vote proxies.

4. Provide educational assistance to board.

Policy Implemented: September 20, 1995.
Amended: February 27, 2009

All funds under SIB management must have a written investment policy. Investment policy forms the cornerstone of the management of any investment program. A sound investment policy ensures that fund assets are managed in a disciplined process, based on long-term fundamental investment principles.

For the larger, more complex trust funds, consultants are used to assist in policy and asset allocation development. Their specialized skills are needed to model and analyze the many variables that go into determining a proper asset allocation.

Policy development starts with the specification of investment objectives, constraints, and preferences. Fund trustees must address a number of factors:

- What is the fund's objective(s)?
- What is the board's tolerance for risk or threshold for under-performance?
- What are the fund's liquidity needs and cash flow characteristics?
- What are the board's asset class preferences and constraints?
- What is the actuarial earnings assumption?
- What are the legal or political considerations?
- What is the investment time horizon?

Since the ultimate objective of fund investments is to provide for the payment of future capital needs, claims, or other monetary requirements, it is essential that the investment policy be developed within the context of fund liabilities or spending policy. The development of investment policy, therefore, is always unique to the circumstances of each fund.

Complex actuarial models are used to quantify the liabilities of the pension plans and Workforce Safety and Insurance. Internal entities develop cash flow forecasts for the smaller funds based on past claims or anticipated expenditures.

Asset allocation optimizations are used to quantify the range of future investment outcomes. Investment consultants contribute needed expertise on capital market expectations and in identifying the risks associated with a particular asset allocation.

For some funds, the risk/return tradeoffs of alternative portfolios are not well represented by expected returns and standard deviation. More important are the expected results for required sponsor and participant contributions and funded ratios over time. Asset/liability modeling is the tool that allows the governing boards to examine and assess the tradeoffs leading to an appropriate investment policy.

The results of the optimizations are a description of the range of financial results that might realistically be expected to occur. These results provide the basis for determining an asset allocation.

POLICY TYPE: INVESTMENTS

POLICY TITLE: *INVESTMENT POLICY DEVELOPMENT – TRUST FUNDS*

In accordance with NDCC 21-10-02.1, RIO staff works with each fund's governing authority, and consultants as needed, to develop an investment policy, which includes an appropriate asset allocation, for each of the statutory funds. Contracted entities are responsible for their own policy development.

Each policy, as a minimum, will include the following information:

1. Fund characteristics and constraints.

    a. An explanation as to the purpose of the portfolio and its legal structure.

    b. Size of portfolio and the likelihood and amount of future contributions and disbursements

    c. Participant demographics when applicable.

    d. Fiscal health of fund.

    e. Constraints.

    f. Unique circumstances.

2. Responsibilities of SIB.

3. Investment objectives.

4. Standards of investment performance.

5. Asset allocation policy and guidelines.

6. Evaluation and review.

Policy Implemented: September 20, 1995.
Amended: February 27, 2009

POLICY TYPE: INVESTMENTS

POLICY TITLE: *INVESTMENT POLICY DEVELOPMENT – INVESTMENT POOLS*

The SIB does no in-house investment of funds. All investment activity is delegated to outside money managers. Within each asset class there are numerous manager styles (i.e. market sector specializations) that may be employed by the SIB to affect exposure to the various asset classes.

SIB investment pool policy statements will define the following for each asset class:

1. Strategic objectives.
2. Performance objectives.
    a. Appropriate capital market benchmarks.
    b. Excess return targets, after payment of investment management fees.
    c. Peer-group ranking.
    d. Risk characteristics.
    e. Termination factors.
3. Portfolio constraints.
    a. Quality of securities/portfolio (security – BAA/portfolio – AA).
    b. Quality held (maximum in company/industry/economic sector).
    c. Other specific restrictions if applicable (ADRs, 144A securities, prohibited transactions, etc.).
4. Investment structure.
    a. Percent of assets per manager cycle.
    b. Ranges for rebalancing.
5. Control Procedures
    a. Duties and responsibilities of the SIB
    b. Duties and responsibilities of money managers.
    c. Reporting requirements.

Policy Implemented: September 20, 1995.
Amended: February 27, 2009

The SIB will ensure that appropriate monitoring mechanisms are in place at all times. The three basic mechanisms are:

- Accounting
- Auditing
- Performance Measurement

The primary objective of these functions is to provide useful information to decision makers (fiduciaries and legislators). These monitoring functions are needed to keep track of assets and manager activity and to control the asset mix. Different aspects of these activities will be conducted internally by RIO staff and externally by the master custodian, auditors, and investment consultants.

Accounting

The master custodian will provide RIO staff with such accounting detail and at such frequency as the staff deems necessary to fulfill the SIB's reporting requirements.

From this information, RIO accounting staff will generate monthly and annual financial statements for each of the trust funds managed by the SIB.

RIO management is responsible to ensure the proper valuation of all assets. Formal valuation policies must be developed and implemented utilizing industry best practices and GAAP accounting requirements.

Compliance

RIO management is responsible for developing and implementing compliance procedures utilizing industry best practices. A summary of compliance procedures and results will be presented to the SIB annually.

Auditing

The North Dakota State Auditor is responsible for the external audit of RIO. They may assign this responsibility to an outside firm which they select by way of the RFP process. The SIB Audit Committee may make recommendations to the State Auditor concerning the selection, evaluation, and termination of this firm. This firm conducts an extensive financial and management audit for each fiscal year. The audited financial statements are filed with the Legislative Audit and Fiscal Review Committee.

RIO has a dedicated internal audit function that reports to the SIB Audit Committee. The internal audit function encompasses both the investment and retirement divisions of RIO. The SIB Audit Committee has oversight responsibilities as outlined in the SIB Audit Committee charter.

Performance Measurement and Reporting

The third element of monitoring entails measuring the performance of the individual investment managers and the total fund performance of each of the funds under the SIB. The SIB will retain reputable investment consultants or performance measurement services to provide comprehensive quarterly performance measurement information. This information will include data on the capital markets, other plan sponsors, and other investment managers. Performance results for SIB accounts will be calculated from data provided by the master custodian and compared to relevant capital market benchmarks, other public funds, manager peer groups, and investment goals specified in the asset class investment policy. Time periods covered by the report may vary but generally will include the most recent quarter, last 12 months, last three years, five years, and longer time periods (as data is available).

POLICY TYPE: INVESTMENTS

POLICY TITLE: *MONITORING*

RIO staff will use appropriate sources to compile monthly performance reports for each of the funds under the SIB that show recent performance and asset mix.

Policy Implemented: September 20, 1995.
Amended: February 27, 2009, February 25, 2011.

STATEMENT OF POLICY

It shall be the policy of the State Investment Board (SIB) to vote all proxies appurtenant to shares held in the various plans administered by the Board, and to vote said shares in a manner that best serves the system's interests. Specifically, all shares are to be voted with the interest of preserving or enhancing share value. The Board endorses the Department of Labor opinion that proxies have economic power which shareholders are obligated to exercise to improve corporate performance. The Board further recognized that proxy issues are frequently complex, requiring expert guidance; accordingly, it has adopted procedures that employ such experts.

The objectives of these policies are as follows:

1. Exercise the value empowered in proxies.

2. Maintain or improve share value for the exclusive benefit of the participants.

3. Achieve changes for the common good whenever these do not conflict with the exclusive benefit objective.

PROCEDURES

DISTINCTION OF RESPONSIBILITIES

Master Custodian

The system's master custodian shall be responsible for timely receipt and distribution of proxy ballots to the appropriate investment management institutions.

Managers

The managers shall be responsible for promptly voting all proxies pursuant to the Board's policies, and in keeping with the managers' best judgments.

Staff

Staff, in concert with the master custodian and the managers, shall be responsible for monitoring the receipt and voting of all proxies.

Board

The Board shall administer and enforce its policies. This administration and enforcement requires reporting from responsible persons, as discussed in the following.

REPORTING

Master Custodian

The master custodian shall report quarterly in writing on all pertinent proxy issues, including (1) receipt of proxy material; (2) nature of issues; (3) due date; (4) names of managers and dates forwarded; and (5) deficiency reports covering proxies that should have been received but were not.

Managers

Managers shall report quarterly in writing on how proxies have been voted, with explanations given whenever the Board's guidelines have not been followed.

Staff

Internal audit staff shall report annually on the efficiency of the process, the portion of total proxies that have actually been voted, and compliance with Board directives.

GUIDELINES

The Board believes that good corporate investment decisions require good corporate governance, and that social responsibilities cannot be ignored in these decision processes. Accordingly, the practice of faithfully voting with management will *not* be tolerated, nor will the "Wall Street Rule" which advocates the sale of shares if there is disagreement with management.

In keeping with the Board's philosophy, the managers are encouraged to vote *for* proposals that *increase* or enhance the following, and against those that decrease or diminish the same:

- Health of the population
- Environmental conditions
- Management and Board accountability
- Abolition of management entrenchment
- Control of executive compensation
- Shareholder rights and ownership
- Fair labor practices

Guidelines may be altered periodically by the Board as situations warrant.

Policy Implemented: September 20, 1995.
Amended: February 27, 2009

The SIB hires investment managers with the intention of maintaining long-standing relationships. Care is taken to select managers for defined roles based on their strengths in designated areas. The hiring process is done in accordance with all applicable state and federal laws.

Some manager selections are conducted by the consultant while others may be directed by the staff in coordination with the SIB. Ultimately, the selection process is often a team effort involving the investment consultants, SIB members, and RIO staff. A consultant may be invaluable in this activity due to the large volume of data that needs to be collected, verified, and summarized. Also, their ongoing dialogue with money management firms provides useful qualitative input.

The investment management business has rapidly evolved since the 1990's. It is recognized that many viable firms have been formed as the result of spin-offs or start-ups and may not have a traditional long-term investment performance history in accordance with the following guidelines. There has also been a tremendous increase in the types of strategies available to institutional investors resulting in the need for flexibility in the establishment of investment criteria. Subject to the case-by-case acceptance of deviation by the SIB members, money managers must meet the following minimum selection criteria for inclusion in a manager search:

- Must be a registered investment adviser, bank, insurance company, or investment company (mutual fund). Should provide ADV Part II (registered investment adviser) prospectus (investment company) or comparable information (bank or insurance company).

- Provide at least five years of actual quarterly performance data that is time weighted a representative composite of accounts, and meets Global Investment Performance Standards (GIPS).

- Provide information that illustrates the key investment personnel have been together for at least five years and the capabilities of the firm can handle the current level of investment activity.

- Able to articulate the firm's investment strategies and philosophy in a manner understandable by the Board, and provide a statement that the strategy has been followed for at least five years.

- Disclose any pending or past litigation or censure.

- Be willing to acknowledge their fiduciary status in writing (mutual funds are exempted from this requirement).

The following steps will be followed in the selection process, subject to modification relative to investment strategy and manager search circumstances:

- Develop a profile of the type of manager needed. This is based on the investment goals and asset allocations. Included in the profile are such things as:

  Quantitative characteristics, such as GIPS-compliant composite return data, risk-adjusted rates of return and relevant portfolio characteristics.

Qualitative characteristics, such as key personnel, investment philosophy, investment strategy, research orientation, decision making process, and risk controls.

Organizational factors, such as type and size of firm, ownership structure, client servicing capabilities, ability to obtain and retain clients, and fees.

- The Investment Officer will give a written report to the SIB on the due diligence process conducted by the Investment Officer, RIO staff, and the SIB in the manager selection process. This report will include selection steps followed and process steps excluded.

- Consultant and/or staff use the profile to screen their data base for managers that meet SIB criteria.

- Consultant and/or staff reduce the group to the top candidates and prepare a summary report. The report will contain pertinent data on each of the candidates.

- When appropriate, on-site visits may be made by staff and board members to the candidates' home offices. Visits by board members to potential manager sites must have board approval.

- When appropriate the Investment Officer will conduct fact-finding pre-interviews. SIB trustees and RIO staff will receive notice of these pre-interviews.

  Interviews are conducted with each of the finalists in Bismarck. All are required to bring the potential portfolio manager to the interview. Particular attention is paid to gaining an understanding of the investment process and determining the manager's compatibility with the SIB's guidelines and objectives.

  The Investment Officer will schedule manager interviews with the SIB. Following these interviews, the Investment Officer, with the advice of RIO staff and consultants, will make recommendations to the SIB on manager selection.

- The SIB will select the investment manager by majority vote.

- Manager(s) selected by the SIB are notified immediately by RIO staff. Unsuccessful candidates are notified by consultant.

- Investment management contracts are reviewed and finalized, sent to the Attorney General for approval, and executed.

- Accounts are set up at the master custodian and on the internal general ledger.

- Consultant is notified when to begin the measurement of the investment performance of the manager(s).

Policy Implemented: September 20, 1995
Amended: February 27, 2009

Portfolio Rebalancing

The need to rebalance the portfolio can arise due to a new asset allocation or because market activity has driven the actual distribution of assets away from the desired mix. To minimize transaction costs due to rebalancing, RIO works with the investment consultants to determine appropriate ranges around the target mix (which are specified in the policy statement). Rigidly adhered to, such a policy is a valuable risk control tool. By maintaining asset mix within reasonably tight ranges, the SIB avoids making unintentional "bets" in the asset mix and avoids market-timing decisions.

All of the funds the SIB oversees have an asset allocation with minimum and maximum limits assigned. RIO's rebalancing policy requires the asset mix to be determined at the end of each month. At the end of each quarter, all portfolios deviating from the target beyond the acceptable limits are rebalanced to target.

Policy Implemented: September 20, 1995.

The SIB will follow an annual evaluation cycle for the investment program to ensure systematic review of investment policies and performance results and the development and implementation of corrective action plans. Evaluation of the program seeks to answer such questions as:

- Are all investment goals being met?
- What has worked and what has not?
- Have changes occurred in the capital markets, plan design, or board philosophy to warrant changes in investment policy?
- Are money managers meeting our expectations?
- Is continued confidence in the money managers warranted?
- Are accounting practices sound and fair to participating funds?
- Is service delivered in the most cost-effective manner?

The SIB's consultants play a key role in helping to answer some of these questions. The external auditor's report provides insight on accounting practices and cost effectiveness.

Evaluation of Money Managers

Achievement of the SIB's performance goals hinges on the success of the investment strategies and money managers it employs. Evaluation of each money manager must consider the following:

- Has the manager achieved the SIB's performance objectives?
- Has the firm adhered to the investment philosophy for which it was hired?
- Have there been any organizational or personnel changes that may negatively affect future performance?
- Are areas of concern being adequately addressed?
- Can the manager perform well in the future, regardless of whether extraordinary events, long-term performance, and/or short-term performance argue for termination?

These criteria are assessed by quantitative and qualitative means:

- Analyses provided by the investment consultant.
- Annual meetings with each manager in Bismarck to discuss performance, investment philosophy, organizational changes, economic outlook, and areas of concern.

Longer periods of time are better than shorter time periods when assessing a manager's performance. Ideally, performance should be assessed over a market cycle. Market cycles have varying lengths but have historically averaged 5-7 years. The SIB will use a minimum five-year period to evaluate manager performance against long-term performance standards. Long-term performance standards will be a market index that the manager has previously agreed to be measured against.

Shorter-term performance standards will also be established for each money manager. These standards will incorporate a minimum three-year measurement period and measure the manager against a previously agreed-upon peer group or style market index.

Long-term performance standards, short-term performance standards, extraordinary events, and termination factors will be incorporated in the written asset class investment policies.

Evaluation of Program Costs

Costs will be broken out by internal administration, investment consultants, master custodian, and external manager fees. Reports will detail this information by investment pool, managers, and by fund.

These costs will be compared to other funds on an annual basis. The most reliable source of comparison currently available is the cost survey prepared by the Canadian consulting firm Cost Effectiveness Measurement, Inc. The information contained in this survey is not available anywhere else. Staff is encouraged to identify other cost-comparison sources.

Policy Implemented: September 20, 1995.

POLICY TYPE: INVESTMENTS

POLICY TITLE: ***PERFORMANCE RELATED INVESTMENT MANAGER REVIEW***

The North Dakota State Investment Board (SIB) recognizes the inherent importance of assessing an investment manager because of performance. Thus, the following process of evaluation includes quantitative *and* qualitative input. This procedure is structured to assist the SIB in recognizing potentially distressed investment managers, initiating a formal review process, and providing guidelines for termination if necessary. Note: The "Manager Review" terminology or concept is not meant to cause the manager to make substantive changes in investment philosophy, style, or strategies. Rather, it is intended to define a period of close scrutiny of the manager's activities, circumstances, and investment results.

Factors which may result in a Manager Review:

Significant changes in organizational structure

Significant changes in investment philosophy

Significant deviation in portfolio management from stated philosophy (style drift)

Substandard investment performance

Diminished confidence in manager

Manager Review Procedures:

Information is submitted to, or generated by, the Board which initiates consideration of a Manager Review.

If warranted, the Board takes action to initiate a Manager Review.

Based on the situation and with input from the Investment Director, the SIB suggests appropriate action to facilitate the Review. Action may include telephone conferencing, local or on-site visits with manager, investigation by consultants, appearance of manager before a select committee of the SIB, or appearance of the manager before the SIB. Investment Director initiates investigation of situation based on direction from SIB.

The Investment Director report's findings to SIB at a subsequent meeting.

After considering findings of the Manager Review, SIB may:

- Remove manager from Review status
- Suggest additional action to facilitate Manager Review
- Relieve manager of duties

In the case where continued investigation is warranted, the Investment Director will report new information and/or recommendations to the SIB as appropriate. It will be considered the responsibility of the Investment Director to maintain awareness and consideration of the Review until the situation is resolved.

It is important to recognize that situations occasionally arise of such a serious nature that a Manager Review process must be immediately initiated. In such cases, the Investment Director is granted the authority to place an investment manager under Review, including the freezing of assets if necessary, and report on such action at the next meeting of the State Investment Board.

In every case, the Investment Director is responsible for documenting the Manager Review process including recognition of:

- Reason of Manager Review
- Action taken to investigate the situation
- Report on results of investigation
- Report on resultant action taken by SIB
- Notification of investigation and conclusions to manager and consultants

A complete record of Manager Review activities and history shall be maintained at the ND Retirement and Investment Office.

Policy Implemented: June 27, 1997.

POLICY TYPE: INVESTMENTS

POLICY TITLE: *BANK OF NORTH DAKOTA MATCH LOAN PROGRAM*

The SIB has a commitment to the Bank of North Dakota Match Loan Program. The purpose of the program is to encourage and attract financially strong companies to North Dakota. The program is targeted to manufacturing, processing and value-added industries.

The SIB provides capital to the program by purchasing Certificates of Deposit (CD's) from the Bank of North Dakota. The CD's are guaranteed by the state, typically have seven to fifteen year maturities and pay interest pegged to US Treasury notes.

The source of funding for CD's shall be determined by the Investment Director; that funding to be from the most appropriate source consistent with liquidity and relative yield and return objectives and constraints.

Policy Implemented: April 24, 1998.
Amended: February 27, 2009

POLICY TYPE: INVESTMENTS

POLICY TITLE: *ACCEPTING NEW CLIENTS*

NDCC 21-10-06 states *"The state investment board may provide investment services to, and manage the money of, any agency, institution, or political subdivision of the state, subject to agreement with the industrial commission. The scope of services to be provided by the state investment board to the agency, institution, or political subdivision must be specified in a written contract. The state investment board may charge a fee for providing investment services and any revenue collected must be deposited in the state retirement and investment fund."*

When a request is received by staff from a potential new investor requesting investment services from the State Investment (SIB), the following steps shall be followed.

1. Staff will conduct initial discussions with the potential client regarding type of fund, risk tolerance, size of fund, services to be provided, costs, etc.

2. Staff will recommend that an Asset/Liability study be conducted by the potential client if one has not been done recently. This discussion will include a description of the asset classes available for investment with the SIB to be included in their study.

3. If the potential client is still interested in participating in the SIB program, staff will bring the preliminary request to the SIB for acceptance. It shall be the policy of the SIB to take the following into consideration when determining if a new investor request will be accepted.

    a. Internal staff administrative capacity.
    b. Compatibility of new investor's goals and risk tolerances with the existing SIB program structure.
    c. Whatever other factors the SIB determines to be appropriate to the decision.

4. If the SIB chooses to accept the preliminary request, staff will provide the necessary template documents to the potential client for review and completion. These documents include a contract for services and investment guidelines.

5. Once documentation is completed, staff will request to have the issue included on the Industrial Commission's agenda for their approval. Copies of all documentation will be provided for their review.

6. If approved by the Industrial Commission, final documentation will be presented to the SIB for final acceptance.

7. If accepted, staff will work with the new client to set up transfer of funds and implementation of asset allocation as directed. All new clients will be brought in as of the last day of a calendar quarter.

8. Fees will be charged with the intention of covering all associated costs as described in RIO Fiscal Management procedure "Investment Fee Allocations".

Policy Implemented: November 20, 2009

EXHIBIT E-I

State Investment Board (SIB) Members 2014-2015:

Position	**Incumbent**	**Designation**	**Term Expiration**
Lt. Governor	Drew Wrigley	Ex officio	Open
State Treasurer	Kelly Schmidt	Ex officio	Open
State Insurance Commissioner	Adam Hamm	Ex officio	Open
Commissioner University & School Lands	Lance Gaebe	Appointed	N/A
Executive Director Workforce Safety & Insurance	Bryan Klipfel	Appointed	N/A
Trustee, TFFR	Mel Olson	Appointed by TFFR Board	6/30/18
Trustee, TFFR	Michael Gessner	Appointed by TFFR Board	6/30/16
Trustee, TFFR	Rob Lech	Appointed by TFFR Board	6/30/20
Trustee, PERS	Mike Sandal	Appointed by PERS Board	6/30/17
Trustee, PERS	Tom Trenbeath	Appointed by PERS Board	6/30/15
Trustee, PERS	Yvonne Smith	Appointed by PERS Board	6/30/19

Retirement and Investment Office (RIO) Staff:

Position	Incumbent	Education
Executive Director/ Chief Investment Officer	David Hunter	BS, Accounting, Northern Illinois University MBA, Finance, University of Chicago
Deputy Chief Investment Officer	Darren Schulz	BBA, Finance, Georgia State University, CFA
Fiscal and Investment Operations Mgr	Connie Flanagan	BS, Accounting, University of Mary
Deputy Executive Director/ Chief Retirement Officer	Fay Kopp	BS, Business, Valley City State University, CRC, CRA

<u>External</u>

Function	Firm	Date Hired
Investment Consultant	Callan Associates Inc.	4/84
Actuary (TFFR)	Segal	7/11
Auditor	CliftonLarsonAllen	4/12
Master/Global Custodian	The Northern Trust Company	12/83

H. BY-LAWS

PAGE

CHAPTER 1 - AUTHORITY

Section 1-1. The State Investment Board (SIB) has the authority to maintain an administrative office under Chapter 54-52.5, North Dakota Century Code.

Section 1-2. The SIB has the authority and responsibility for providing administrative services to the North Dakota Teachers' Fund for Retirement (TFFR) and the North Dakota State Investment Board. This includes organizing, staffing, and maintaining an administrative office.

Section 1-3. The SIB has the authority and responsibility for developing and monitoring the agency budget.

Section 1-4. The SIB has the authority and responsibility to maintain office records, an accounting system, and data processing support services.

Section 1-5. The SIB has the authority to pay all claims and investment expenses filed with TFFR and the SIB.

Policy Implemented: June 23, 1995.

CHAPTER 2 - BOARD

Section 2-1. Members of the State Investment Board (SIB) are the Governor, State Treasurer, Commissioner of University and School Lands, director of Workforce Safety & Insurance, Commissioner of Insurance, three members of the Teachers' Fund for Retirement (TFFR) Board, two of the elected members and one member of the Public Employees Retirement System (PERS) Board as selected by those boards. The PERS and TFFR Boards may appoint an alternate designee with full voting privileges to attend meetings of the SIB when a selected member is unable to attend. The director of Workforce Safety and Insurance may appoint a designee, subject to approval by the Workforce Safety and Insurance board of directors, to attend the meetings, participate, and vote when the director is unable to attend.

Section 2-2. The SIB will have general charge and management of the business of TFFR and the SIB, subject to law, administrative rules and regulations, and governance policies. The SIB will make such policy as necessary to fulfill this obligation.

Section 2-3. When the statutes allow a Deputy to represent a member of the SIB or an alternate to represent the TFFR or PERS Board, the Chair will recognize the individual for the record, and the individual(s) will then have the right to vote on matters before the SIB.

Section 2-4. The SIB will be responsible for the operation of an administrative office that will provide support services to TFFR and the SIB.

Policy Implemented: June 23, 1995.
Amended: July 22, 2011.

CHAPTER 3 - OFFICERS AND DUTIES

Section 3-1. The officers of the SIB are a Chair and Vice Chair, one of which must be an appointed or elected member of the TFFR or PERS Board. The officers will be elected by the SIB to a one-year term at the first regularly scheduled meeting following July 1 of each year. Vacancies will be filled by the SIB at the first scheduled meeting following the vacancy.

Section 3-2. Chair. The Chair will preside at all meetings of the SIB.

Section 3-3. Vice Chair. In the absence of the Chair, the Vice Chair will perform the duties of the Chair.

Section 3-4. Executive Director. An Executive Director will be retained by the SIB. The Executive Director will serve at the SIB's pleasure, be responsible for keeping the records of the SIB and TFFR Board actions, and perform such duties as the SIB prescribes. The Executive Director will make out and give out all notices required to be given by law, procedures, or rules and regulations of the two boards.

Policy Implemented: June 23, 1995.

CHAPTER 4 - MEETINGS

Section 4-1. Regular meetings of the SIB to conduct business are to be held as often as necessary. The SIB will meet at least once each quarter. Notice of all meetings will be made in accordance with North Dakota Century Code, Section 44-04-20.

Section 4-2. Meetings of the SIB may be called by the Chair or two members of the SIB upon reasonable notice in writing to the other members of the Board. (NDCC 21-10-04)

Section 4-3. A quorum will be six (6) members of the SIB.

Section 4-4. Voting on matters before the SIB will be contained in the minutes which will show the recorded vote of each SIB member.

Section 4-5. All meetings of the SIB are open to the public.

Section 4-6. A record of procedures will be kept by the Executive Director on all meetings of the SIB. The records of these proceedings are public documents, and copies will be distributed to the TFFR, SIB, and PERS Boards and upon request.

Section 4-7. Public participation during meetings of the SIB may be allowed at the discretion of the Chair.

Section 4-8. SIB members, except elected and appointed officials, will be paid the amount specified in NDCC 21-10-01 per SIB meeting attended.

Expenses will be paid according to state law and OMB policies.

Policy Implemented: June 23, 1995.
Amended: July 22, 2011.

CHAPTER 5 - COMMITTEES

Section 5-1. The SIB will establish one standing committee: Audit Committee.

Section 5-1-1. Audit Committee. The Audit Committee will consist of five members. They will be selected by the SIB. Three members of the committee will represent the three groups on the SIB (TFFR Board, PERS Board, and elected and appointed officials). The other two members will be selected from outside of the SIB and be auditors with at least a Certified Public Accountant (CPA) or Certified Internal Auditor (CIA) designation.

The Audit Committee will have responsibility for oversight of financial reporting, auditing, and internal control. The Audit Committee will be responsible for developing a written charter, to be approved by the SIB, which puts forth the authority, responsibilities, and structure of the Audit Committee. It will also be the responsibility of the Audit Committee to supervise the audit activities of the internal audit staff, work with the State Auditor/external auditors, and develop reports for the SIB.

The Executive Director shall supervise the administrative activities of the internal/external audit programs such as travel, securing contracts, paying fees, maintaining official reports, etc.

The supervisor of the internal audit function will be the staff member directly responsible to the Audit Committee.

Membership on the Audit Committee will be for one year or termination of term on the SIB. Vacancies will be filled by the SIB at the first scheduled meeting following the vacancy. There will be no limit to the number of terms served on the Audit Committee.

Section 5-2. No member of the SIB will be paid, other than expenses, for attending seminars, conferences, or other such educational meetings.

Policy Implemented: June 23, 1995.

CHAPTER 6 - <u>RULES OF ORDER</u>

Section 6-1. All SIB meetings will be conducted in accordance with Robert's Rules of Order Newly Revised except as superseded by these by-laws and board governance policies.

Policy Implemented: June 23, 1995.

CHAPTER 7 - ADMINISTRATIVE OFFICE

Section 7-1. For the purpose of carrying out the day-to-day business of TFFR and the SIB, an administrative office will be maintained in Bismarck, North Dakota. This office is called the Retirement and Investment Office (RIO).

Section 7-2. The Executive Director will be the administrator of the office.

Policy Implemented: June 23, 1995.

CHAPTER 8 - AMENDMENTS

Section 8-1. These by-laws may be amended by a two-thirds vote of SIB members. All amendments must be mailed to SIB members at least thirty (30) days prior to the meeting at which they are considered.

Section 8-2. All amendments must include an effective date.

Policy Implemented: June 23, 1995.

INFORMATIONAL – NO BOARD ACTION REQUESTED

TO: **State Investment Board**

FROM: **Dave Hunter**

DATE: **June 19, 2015**

SUBJECT: **Legislative Update – Cover Memo**

Senate Bill 2022:

The 64th Legislative Assembly reconvened on June 16th and approved SB 2022 including the biennial appropriation for RIO and PERS. Prior to this positive development, RIO and PERS obtained an Attorney General opinion which stated that RIO and PERS were authorized to make expenditures during the 2015-17 biennium. The AG Opinion stated, "it is my opinion that the express continuing appropriation authority granted these agencies combined with their independent legal obligations as fiduciaries of the plans they administer carry with them the implied authority to expend funds for the salaries and associated operating expenses of the individuals needed to effectuate those appropriations in order to fulfill their fiduciary obligations, to the extent the implied authority if not prohibited under state law. While I cannot, in a legal opinion, determine the amounts these agencies may expend pursuant to this implied authority, I will remind the governing Boards of these Agencies that they are and remain fiduciaries, and any expenditure of funds must be done prudently." It is important to note that SB 2022 included a provision to add two legislators to the PERS board. Given that three PERS board members serve on the SIB, the proposal to add legislators to the PERS Board could result in one legislator being added to the SIB.

Current Status:

RIO is awaiting approval of SB 2022 by Governor Jack Dalrymple on or before July 1, 2015.

Sixty-fourth Legislative Assembly of North Dakota
In Regular Session Commencing Tuesday, January 6, 2015

SENATE BILL NO. 2022
(Appropriations Committee)
(At the request of the Governor)

AN ACT to provide an appropriation for defraying the expenses of various state retirement and investment agencies; to provide various transfers; to create and enact section 54-52.1-05.1 of the North Dakota Century Code, relating to the terms of public employees retirement system contracts for uniform group health insurance benefits coverage; to amend and reenact subsection 17 of section 54-52-01 and sections 54-52-03 and 54-52.1-05 of the North Dakota Century Code, relating to the public employees retirement system board and disclosure of information by uniform group health insurance benefits coverage carriers; and to limit the use of health insurance program reserves.

BE IT ENACTED BY THE LEGISLATIVE ASSEMBLY OF NORTH DAKOTA:

SECTION 1. APPROPRIATION. The funds provided in this section, or so much of the funds as may be necessary, are appropriated out of any moneys from special funds derived from income, to the retirement and investment agencies listed in this section for the purpose of defraying their expenses, for the biennium beginning July 1, 2015, and ending June 30, 2017, as follows:

Subdivision 1.

RETIREMENT AND INVESTMENT OFFICE

	Base Level	Adjustments or Enhancements	Appropriation
Salaries and wages	$3,772,504	$568,047	$4,340,551
Accrued leave payments	71,541	(71,541)	0
Operating expenses	973,324	17,550	990,874
Contingencies	82,000	0	82,000
Total special funds	$4,899,369	$514,056	$5,413,425
Full-time equivalent positions	19.00	0.00	19.00

Subdivision 2.

PUBLIC EMPLOYEES RETIREMENT SYSTEM

	Base Level	Adjustments or Enhancements	Appropriation
Salaries and wages	$5,016,339	$1,399,021	$6,415,360
Accrued leave payments	103,217	(103,217)	0
Operating expenses	2,280,894	397,169	2,678,063
Contingencies	250,000	0	250,000
Total special funds	$7,650,450	$1,692,973	$9,343,423
Full-time equivalent positions	33.00	1.50	34.50

Subdivision 3.

BILL TOTAL

	Base Level	Adjustments or Enhancements	Appropriation
Grand total special funds	$12,549,819	$2,207,029	$14,756,848
Full-time equivalent positions	52.00	1.50	53.50

SECTION 2. ONE-TIME FUNDING - EFFECT ON BASE BUDGET - REPORT TO SIXTY-FIFTH LEGISLATIVE ASSEMBLY. The following amounts reflect the one-time funding items approved by the sixty-third legislative assembly for the 2013-15 biennium and the 2015-17 one-time funding items included in the appropriation in section 1 of this Act:

One-Time Funding Description	2013-15	2015-17
Public employees retirement system - temporary salaries	$0	$100,000
Total special funds	$0	$100,000

The 2015-17 one-time funding amounts are not part of the entity's base budget for the 2017-19 biennium. The public employees retirement system shall report to the appropriations committees of the sixty-fifth legislative assembly on the use of the one-time funding for the biennium beginning July 1, 2015, and ending June 30, 2017.

SECTION 3. APPROPRIATION LINE ITEM TRANSFERS. Upon approval of the respective boards, the retirement and investment office and the public employees retirement system may transfer from their respective contingencies line items in subdivisions 1 and 2 of section 1 of this Act to all other line items. The agencies shall notify the office of management and budget of each transfer made pursuant to this section.

SECTION 4. AMENDMENT. Subsection 17 of section 54-52-01 of the North Dakota Century Code is amended and reenacted as follows:

17. "Retirement board" or "board" means the ~~seven persons designated by this chapter as the~~ governing authority ~~for the retirement system~~ created under section 54-52-03.

SECTION 5. AMENDMENT. Section 54-52-03 of the North Dakota Century Code is amended and reenacted as follows:

54-52-03. Governing authority.

A state agency is hereby created to constitute the governing authority of the system to consist of a board of ~~seven persons~~nine individuals known as the retirement board. No more than one elected member of the board may be in the employ of a single department, institution, or agency of the state or in the employ of a political subdivision. ~~No~~An employee of the public employees retirement system or the state retirement and investment office may not serve on the board.

1. Two members of the legislative assembly must be appointed by the chairman of the legislative management to serve on the board.

    a. If the same political party has the greatest number of members in both the house and senate, one member must be from that majority party and one member from the political party with the next greatest number of members in the house and senate.

    b. If the same political party does not have the greatest number of members in both the house and senate, one member must be from the majority party in the house and one member must be from the majority party in the senate.

2. One member of the board must be appointed by the governor to serve a term of five years. The appointee must be a North Dakota citizen who is not a state or political subdivision employee and who by experience is familiar with money management. The citizen member is chairman of the board.

~~2.~~3. One member of the board must be appointed by the attorney general from the attorney general's legal staff and shall serve a term of five years.

~~3.~~4. The state health officer appointed under section 23-01-05 or the state health officer's designee is a member of the board.

~~4.~~5. Three board members must be elected by and from among the active participating members, members of the retirement plan established under chapter 54-52.6, members of the retirement plan established under chapter 39-03.1, and members of the job service North Dakota retirement plan. Employees who have terminated their employment for whatever reason are not eligible to serve as elected members of the board under this subsection. Board members must be elected to a five-year term pursuant to an election called by the board. Notice of board elections must be given to all active participating members. The time spent in performing duties as a board member may not be charged against any employee's accumulated annual or any other type of leave.

~~5.~~6. One board member must be elected by and from among those ~~persons~~individuals who are receiving retirement benefits under this chapter. The board shall call the election and must give prior notice of the election to the ~~persons~~individuals eligible to participate in the election pursuant to this subsection. The board member shall serve a term of five years.

~~6.~~7. The members of the board are entitled to receive one hundred forty-eight dollars per day compensation and necessary mileage and travel expenses as provided in sections 44-08-04 and 54-06-09. This is in addition to any other pay or allowance due the chairman or a member, plus an allowance for expenses they may incur through service on the board.

~~7.~~8. A board member shall serve a five-year term and until the board member's successor qualifies. Each board member is entitled to one vote, and ~~four~~five of the ~~seven~~nine board members constitute a quorum. ~~Four~~Five votes are necessary for resolution or action by the board at any meeting.

SECTION 6. AMENDMENT. Section 54-52.1-05 of the North Dakota Century Code is amended and reenacted as follows:

54-52.1-05. Provisions of contract - Term of contract.

1. Each uniform group insurance contract entered ~~into~~ by the board must be consistent with the provisions of this chapter, must be signed for the state of North Dakota by the chairman of the board, and must include the following:

~~1.~~ a. As many optional coverages as deemed feasible and advantageous by the board.

~~2.~~ b. A detailed statement of benefits offered, including maximum limitations and exclusions, and such other provisions as the board may deem necessary or desirable.

2. The initial term or the renewal term of a fully insured uniform group insurance contract for hospital benefits coverage, medical benefits coverage, or prescription drug coverage may not exceed two years.

a. The board may renew a contract subject to this subsection without soliciting a bid under section 54-52.1-04 if the board determines the carrier's performance under the existing contract meets the board's expectations and the proposed premium renewal amount does not exceed the board's expectations.

b. In making a determination under this subsection, the board shall:

(1) Use the services of a consultant to concurrently and independently prepare a renewal estimate the board shall consider in determining the reasonableness of the proposed premium renewal amount.

(2) Review the carrier's performance measures, including payment accuracy, claim processing time, member service center metrics, wellness or other special program participation levels, and any other measures the board determines relevant to

making the determination and shall consider these measures in determining the board's satisfaction with the carrier's performance.

(3) Consider any additional information the board determines relevant to making the determination.

c. If the board determines the carrier's performance under the existing contract does not meet the board's expectations or the proposed premium renewal amount exceeds the board's expectations and the board determines to solicit a bid under section 54-52.1-04, the board shall specify its reasons for the determination to solicit a bid.

SECTION 7. Section 54-52.1-05.1 of the North Dakota Century Code is created and enacted as follows:

54-52.1-05.1. Health insurance benefits coverage - Insured and provider data disclosure.

Except as necessary for treatment, payment, or health care operations, a carrier providing health insurance benefits coverage under this chapter may not disclose identifiable or unidentifiable insured or provider data or information to a related or unrelated health care delivery entity. The board may establish exceptions to the disclosure limitations under this section for the limited purpose of addressing public interest and benefit activities or for the limited purpose of addressing research, public health, or health care operations. An exception established by the board under this section may not be more permissive than allowed under state and federal privacy laws.

SECTION 8. HEALTH INSURANCE RESERVE FUNDS - LIMITATIONS. Notwithstanding any other provision of law, during the 2015-17 biennium, the public employees retirement system board may not spend any moneys in the fund created under section 54-52.1-06 or from any other source for the purpose of reducing any increase in uniform group insurance premium amounts beyond the rates used by the sixty-fourth legislative assembly for developing 2015-17 state agency budgets.

President of the Senate ____________________ Speaker of the House ____________________

Secretary of the Senate ____________________ Chief Clerk of the House ____________________

This certifies that the within bill originated in the Senate of the Sixty-fourth Legislative Assembly of North Dakota and is known on the records of that body as Senate Bill No. 2022.

Senate Vote:	Yeas 38	Nays 6	Absent 3
House Vote:	Yeas 73	Nays 16	Absent 5

____
Secretary of the Senate

Received by the Governor at ________M. on ________________________________, 2015.

Approved at ________M. on ____, 2015.

____
Governor

Filed in this office this ___________day of ________________________________, 2015,

at ________ o'clock ________M.

____
Secretary of State

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Wayne Stenehjem
ATTORNEY GENERAL

RECEIVED
JUN 0 5 2015
NDRIO

LETTER OPINION
2015-L-04

June 4, 2015

Mr. Sparb Collins
Public Employees Retirement System
PO Box 1657
Bismarck, ND 58502-1657

Mr. Dave Hunter
Retirement and Investment Office
PO Box 7100
Bismarck, ND 58507-7100

Dear Mr. Collins and Mr. Hunter:

Thank you for your letter requesting my opinion on whether and to what extent the North Dakota Public Employees Retirement System and the North Dakota Retirement and Investment Office are authorized to make expenditures during the 2015-2017 biennium, without a biennial appropriation approved by the Legislature.

For the following reasons, it is my opinion that the express continuing appropriation authority granted these particular agencies, governed by boards which have fiduciary responsibilities over funds held in trust, carries with it the implied authority to expend funds for the salaries and associated operating expenses of the individuals needed to effectuate those appropriations, to the extent the implied authority is not prohibited under state law.

ANALYSIS

You have indicated that the Sixty-Fourth Legislative Assembly adjourned without approving Senate Bill 2022, and that this bill contained the biennial appropriations for both the North Dakota Public Employees Retirement System (NDPERS) and the North Dakota Retirement and Investment Office (NDRIO).[1] As introduced, S.B. 2022 proposed to appropriate funds to these agencies for salaries and wages, operating expenses, and

[1] See S. and H. Journals, S.B. 2022, 2014 N.D. Leg.

contingencies during the 2015-2017 biennium.[2] Subsequent to its introduction, various amendments were made to S.B. 2022 unrelated to the biennial appropriation for these agencies.[3] Ultimately the Legislature adjourned without passing S.B. 2022.[4] The Legislature did not, however, repeal, rescind, or otherwise alter the responsibilities of these agencies toward program participants and investment clients.

AGENCY RESPONSIBILITIES

While the Legislature did not approve a biennial appropriation for the salaries and wages of agency employees, board members, or other operating expenses, these agencies are and continue to be charged with the management, investment, and processing of total funds in excess of $10.5 billion on behalf of the state, various political subdivisions, and public employees.[5] Unlike many other state agencies, NDRIO and NDPERS are governed by boards that function in a fiduciary capacity and must satisfy the legal obligations of that role. Pursuant to state law, NDPERS is responsible for the administration of a myriad of programs that provide benefits to public employees, retirees, and their dependents and beneficiaries. These programs include the North Dakota public employees defined benefit hybrid retirement plan ("defined benefit plan"),[6] the defined contribution retirement plan, the highway patrolmen's retirement system, the job service retirement plan established under N.D.C.C. § 52-11-01, the deferred compensation plan, the pre-tax benefits program, and the uniform group insurance program.[7] The NDRIO is responsible for administration of both the North Dakota Teachers' Fund for Retirement (NDTFFR) plan and the investment program overseen by the North Dakota State Investment Board (NDSIB).[8] The retirement plan established to provide retirement benefits to the teachers of this state and their beneficiaries is NDTFFR.[9] The NDSIB is the body charged with the investment of multiple funds on behalf of the state and political subdivisions including NDPERS, NDTFFR, and the Legacy fund.[10]

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[2] As introduced, S.B. 2022 proposed a total biennial appropriation of slightly more than $15 million for salaries and wage, operating expenses, and contingencies, as well as 55.50 full-time equivalent positions, for these two agencies.
[3] S. and H. Journals, S.B. 2022, 2014 N.D. Leg.
[4] Id.
[5] The Investment Performance Summary published by NDRIO indicates that the NDSIB for the quarter ended March 31, 2015 has over $10.5 billion of assets under management; NDPERS and the NDTFFR are included in the funds under management.
[6] The defined benefit plan encompasses the North Dakota judges retirement plan under N.D.C.C. § 54-52-06.1 and the law enforcement and national guard security officers and firefighters retirement plans under N.D.C.C. §§ 54-52-06.2, 54-52-06.3, and 54-52-06.4.
[7] N.D.C.C. §§ 54-52-04, 54-52.3-02, 54-52.6-04.
[8] N.D.C.C. § 54-52.5-01.
[9] N.D.C.C. § 15-39.1-09.
[10] N.D.C.C. § 21-10-06.

APPROPRIATION AUTHORITY

Under these unique circumstances, your question requires an examination of what, if any, appropriation authority these agencies have absent a specified biennial appropriation from the Legislature. An appropriation "is the setting apart from the public revenue of a definite sum of money for the specified object in such manner that officials of the government are authorized to use the amount so set apart, and no more, for that object."[11] The Legislature is not prohibited, however, from enacting continuing appropriations.[12] "A continuing appropriation is an appropriation running from year to year, without further legislative action, until the purpose of the levy and appropriation is accomplished."[13] The North Dakota Supreme Court has stated that a continuing appropriation is a valid appropriation first made by the Legislature, and it remains continuing only if future legislative assemblies choose not to repeal or modify it.[14] In a prior opinion I observed that continuing appropriations have long been recognized as valid in this state and are nothing new to the legislative process.[15]

NDPERS CONTINUING APPOPRIATION AUTHORITY

Previous legislative assemblies have granted NDPERS express continuing appropriation authority for almost all of the payments associated with the programs it is responsible for administering. For example, NDPERS has express continuing appropriation authority for: the payment of the benefits, consulting fees, and making of investments for the defined benefit plan;[16] costs related to the making of investments and payments to beneficiaries of the North Dakota highway patrolmen's retirement system;[17] the administrative and consultant expenses of the defined contribution plan;[18] the payment of consultants, vendors providing claims administrations services, any insurance costs associated with the medical spending account, and medical reimbursement for the medical spending account if necessary, and payments to the employees participating in, the pretax benefits

[11] Gammons v. Sorlie, 219 N.W. 105, 108 (N.D. 1928).
[12] N.D.A.G. 2004-L-78.
[13] 81A C.J.S. States § 405.
[14] Gange v. Burleigh Cnty. Dist. Ct., 429 N.W.2d 429, 436 (N.D. 1988).
[15] N.D.A.G. 2004-L-78.
[16] N.D.C.C. §§ 54-52-04(6), 54-52-13, 54-52-13.1, 54-52-14.1.
[17] N.D.C.C. § 39-03.1-05.
[18] N.D.C.C. § 54-52.6-06. This section provides for an explicit continuing appropriation for a consultant for the plan and indicates that any administrative expenses must be paid by the plan participants and authorizes the board or its contracted vendor to charge and deduct those expenses directly from the participants' account.

program;[19] the consulting fees and insurance benefits related to the uniform group insurance program, including investments of and contributions toward benefits permitted under the retiree health benefits fund, the payment of claims and costs as provided under the contingency reserve fund, the acceptance and expenditure of third party payments for the benefits, premiums and administrative expenses of the uniform group insurance program, and use of funds that may become available from various sources for a collaborative drug therapy program.[20]

Notably, there is no express continuing appropriation authority for the payment of benefits for the deferred compensation plan established under N.D.C.C. § 54-52.2-01 or the retirement plan established under N.D.C.C. § 52-11-01 and administered by NDPERS ("job service retirement plan"). For the following reasons, however, there exists sufficient authority under state law to permit the payment of benefits under these programs.

Generally funds held in trust are not subject to the appropriation power of the Legislature:

> To be subject to the appropriation power of the Legislature, funds held by state officers or agencies must belong to the state. Funds held in trust to be distributed according to legislatively prescribed conditions are not subject to appropriation, even though they are received on account of the state and the state treasurer is designated custodian.[21]

Both the deferred compensation program and job service retirement plan are comprised of funds held in trust by NDPERS.

Prior opinions of this office have observed that the administration of the deferred compensation program is for the benefit of the employees and involves the deferral of the employees' compensation pursuant to the employees' direction.[22] State law requires NDPERS to act as administrator and fiduciary for the deferred compensation program.[23]

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[19] N.D.C.C. §§ 54-52.3-03, 54-52.3-06. While this section does provide a continuing appropriation for many of the costs associated with the pre-tax benefits program, this continuing appropriation authority is not unlimited. N.D.C.C. § 54-52.3-03 goes on to state that "[a]ll other expenses of administering the program must be paid in accordance with the agency's appropriation authority as established by the legislative assembly." The language is indicative of a requirement for a biennial appropriation for the remaining administrative expenses of the program. N.D.A.G. Letter to Collins (May 16, 1990).

[20] N.D.C.C. §§ 54-52-04(6), 54-52.1-03.2, 54-52.1-04.3, 54-52.1-06, 54-52.1-06.1, 54-52.1-15, 54-52.1-16.

[21] 63C Am. Jur. 2d Public Funds § 28.

[22] N.D.A.G. Letter to Rolfson (Mar. 29, 1985); N.D.A.G. Letter to Person (Oct. 14, 1988)(1).

[23] N.D.C.C. § 54-52.2-03.

Further, administrators of the program are authorized to make payments or investments as specified by the employee, and, by statute such payments or investments are not a prohibited use of the general assets of the state, county, city, or other political subdivision.[24] Given that the funds of the deferred compensation program are held in trust for the participating employees, NDPERS is a fiduciary of those funds and has the authority to disburse and invest them, and state law specifically designates that such disbursement will not constitute a prohibited use of general assets of a governmental body, the investment and benefit payments of the deferred compensation program are not subject to the Legislature's appropriation authority.

Likewise, the job service retirement plan is a pension plan that was established for employees of Job Service North Dakota having assets held in trust for its members.[25] In another prior opinion, this office has observed that "it has been successfully argued that the assets of a state pension plan are owned by the members of the system and not the state."[26] As a result, the payment of benefits from the job service retirement plan is also not subject to legislative appropriation authority.[27]

Additionally, it should be noted S.B. 2022 did not contain a biennial appropriation for benefits payable under the job service retirement plan. In finding appropriation authority was intended in a situation where a biennial appropriation was not made, the North Dakota Supreme Court has opined:

> Where the meaning of a statute is doubtful, the construction placed upon it by the officers charged with the administration thereof is entitled to considerable weight; and this is especially so if it is apparent that the members of the state Legislature in dealing with the subject must have been aware of the construction which had been placed upon the statute by those administering it and failed to indicate any disapproval of such construction.[28]

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[24] N.D.C.C. § 54-52.2-05.
[25] N.D.C.C. § 52-11-01.
[26] N.D.A.G. Letter to Person (Jan. 11, 1988).
[27] Also, it is reasonable to conclude that there is continuing appropriation authority for benefit payments from the job service retirement fund. N.D.C.C. §§ 54-52-04(6) and 54-52-13.1 each provide continuing appropriation for benefit payments from a retirement fund administered by NDPERS. State statutory construction principles allow singular words to be interpreted to include the plural, so likewise it is reasonable to conclude there is continuing appropriation authority for benefit payments from the job service retirement fund as well. N.D.C.C. §1-01-35.
[28] Gammons v. Sorlie, 219 N.W. 105, 108 (N.D. 1928).

In this case, the administrators and legislators exhibited agreement that NDPERS had appropriation authority to make payments from the job service retirement plan and did not need additional legislative action to effectuate it.

NDRIO CONTINUING APPROPRIATION AUTHORITY

The governing boards supported by NDRIO have also been granted express continuing appropriation authority for almost all of the payments associated with the programs the agency is responsible for administering. The responsibility for the administration of NDTFFR and for the investment program overseen by NDSIB lies with NDRIO. Express continuing appropriation authority has been granted for NDTFFR for the payment of benefits and consultant fees.[29] The NDSIB is charged with the investment of various funds, and the board is granted continuing appropriation authority for the associated investment costs and "all moneys required for the making of investments of funds under the management of the board."[30] Additionally, NDRIO itself also has some continuing appropriation authority for the cost of operation of the agency. Section 54-52.5-03, N.D.C.C., establishes the state retirement and investment fund and provides a continuing appropriation from the funds managed by the NDSIB to the state retirement and investment fund for the actual amount of administrative expenses incurred by NDRIO for services rendered. This section goes on to state that the actual amount of administrative expenses incurred by NDRIO must be paid from the fund in accordance with the agency's appropriation authority.[31] This statute provides continuing appropriation authority to transfer money to the retirement and investment fund from investment clients for the payment of administrative expenses but restricts disbursement from the fund to an amount established by the Legislature.

IMPLIED AUTHORITY

Given that the Legislature had granted these agencies continuing appropriation authority, and adjourned without approving a biennial appropriation, but left in place the appropriation authority and the responsibility to administer the programs, it is necessary to consider whether the continuing appropriation authority can be effectuated without funding for staff and other operational expenses.

While appropriation acts are strictly construed, they should not be construed so strictly as to defeat their manifest objects.[32] Further, "an appropriation for a stated purpose or object may be used for any matter reasonably included within that purpose or object."[33] "An

[29] N.D.C.C. § 15-39.1-05.2(4).
[30] N.D.C.C. §§ 21-10-05, 21-10-06, 21-10-06.2.
[31] N.D.C.C. § 54-52.5-03.
[32] 81A C.J.S. States § 409.
[33] 81A C.J.S. States § 410.

agency has only those powers given to it by the Legislature or necessarily implied therefrom."[34] In the absence of a state law to the contrary, an implied power may exist for an action if an express power cannot be effectuated without it.[35]

As previously noted, NDPERS and NDRIO are expressly charged with the management, investment, and processing of funds on behalf of the state, various political subdivisions, and public employees. The boards supported by NDPERS and NDRIO act as fiduciaries for the funds invested and the programs overseen.[36] As fiduciaries holding funds in trust for the members, beneficiaries, and clients, the boards and their supporting agencies have legal obligations to administer those funds prudently. Those obligations must be fulfilled as long as there are member, beneficiary, and client funds managed by the agencies.[37] For the reasons below, those fiduciary obligations and the agencies' express authority to administer the funds give rise to the agencies' implied authority for the wages and operating costs of the individuals necessary to effectuate the continuing appropriations.

As fiduciaries, these boards and their supporting agencies must prudently administer the funds with which they are entrusted. The Legislature has provided continuing appropriations for most of the functions these agencies need to carry out as prudent plan administrators. To the extent these agencies lack express appropriation authority for necessary and prudent administrative and operating expenses, however, their legal obligations as fiduciaries would be frustrated without some implied appropriation authority.[38] For example, a continuing appropriation for the payment of any benefit under the programs is of no effect unless there is a person available to authorize the payment; nor is a continuing appropriation for the retention of consultants effective unless there is a person available and authorized to negotiate and sign the contract with the consultant; nor a continuing appropriation for the making of investments or payment of investment costs

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[34] N.D.A.G. 2014-L-03.
[35] Id.
[36] N.D.C.C. chs. 54-52, 15-39.1; N.D.C.C. § 21-10-07; N.D.A.G. Letter to Omdahl (May 29, 1990).
[37] There is no indication in the legislative history that the Legislature's failure to pass a budget for these agencies was intended to defund or terminate the plans and programs the agencies administer.
[38] The failure of the Legislature to provide express appropriation authority for these activities places the agencies in a position where, absent implied appropriation authority, they could be subject to legal action by members, beneficiaries, and clients of the programs at issue.

unless there is a person available to authorize and monitor the investment.[39] It is not reasonable to conclude that these employees or board members could responsibly perform the necessary functions for administration of the various programs without incurring operating expenses including but not limited to expenses for office space, office supplies, appropriate equipment and technology support, necessary insurance, and being able to travel and engage in appropriate professional development activities.

The implied authority to effectuate express appropriation authority necessary to fulfill fiduciary obligations is strictly limited, however.[40] First, those same fiduciary obligations to plan beneficiaries that permit the existence of implied authority in this situation also circumscribe the agencies' authority to incur administrative and operating costs. By law, the boards must limit staffing and operating expenses to levels that do not exceed those which are required to prudently administer the programs for which these boards are responsible.[41]

Second, I have previously found implied authority may exist only when it is not prohibited by other law.[42] While there is no express authority which generally prohibits a state agency from operating entirely on a continuing appropriation,[43] I refer to any limit specifically placed on the agencies' authority to expend funds for administrative expenses. Such explicit limitation would additionally curtail the agencies' implied appropriation authority.

[39] While I have found implied authority for these agencies to pay their board members, there is an argument to be made that the Legislature has already granted a continuing appropriation to these boards for board member pay. Generally "an unrepealed and unmodified legislative act which creates an office, fixes the salary, and designates the time, mode, or manner of payment constitutes a continuing appropriation." 63C Am. Jur. 2d Public Funds § 27; see State v. Jorgenson, 142 N.W. 450, 457 (N.D. 1913). The authority, amount, and frequency for payments to the board members of NDTFFR, NDSIB, and NDPERS are set forth in N.D.C.C. §§ 15-39.1-08, 21-10-01, 54-52-03.

[40] In an opinion provided to the North Dakota Wheat Commission I indicated that a theory of continuing appropriation could implicate the debt limit prohibition found in N.D. Const. art. X, § 13. N.D.A.G. 2004-L-78. I have considered, but do not find, the debt limit prohibition implicated here because the continuing appropriation authority relied on is still subject to repeal or modification by future legislative assemblies. See Lesmeister v. Olson, 354 N.W.2d 690, 700 (N.D. 1984).

[41] It is reasonable to assume the current staffing levels and operating expenses fall within these limits.

[42] N.D.A.G. 2014-L-03.

[43] For example there exist multiple state entities under N.D.C.C. title 4.1 that are wholly funded by continuing appropriations. N.D.C.C. §§ 4.1-02-19, 4.1-03-16, 4.1-04-17, 4.1-05-14, 4.1-06-18, 4.1-07-18, 4.1-08-05, 4.1-09-22, 4.1-10-15, 4.1-11-15, 4.1-12-08, 4.1-13-21, 4.1-52-11, 4.1-72-07.

Of particular note is the limitation on NDRIO's disbursement of funds otherwise appropriated for the payment of administrative expenses under N.D.C.C. § 54-52.5-03. This section provides continuing appropriation authority to transfer money to the retirement and investment fund for the payment of administrative expenses by NDRIO but limits disbursement of that money to amounts set by the Legislature. While the language of this limitation may be clear on its face, a latent ambiguity was created when read together with the continuing appropriation authority otherwise granted the investment and retirement programs it manages, and as applied to this particular set of facts. Statutes which contain a latent ambiguity when applied to a particular situation make it appropriate to consider the statute's meaning in light of extrinsic aids, which may include the object sought to be attained and the consequences of a particular construction.[44]

The Legislature has granted NDRIO a continuing appropriation for the funds necessary to pay the benefits and consultants of the retirement program, the funds necessary to make and pay the cost of investments for the investment program, and the funds necessary to pay the administrative costs of these programs.[45] By adjourning without acting on S.B. 2022, the Legislature did not negate the funding of these programs, rather it failed to meet its obligation to advise NDRIO on how to spend the funds that had already been appropriated. There is no indication in the legislative history that the Legislature's failure to pass a budget for these agencies was intended to defund or terminate the plans and programs the agencies administer. A conclusion that this inaction prevents NDRIO from spending funds otherwise appropriated would result, for the reasons herein discussed, in a termination of the programs and a failure of fiduciary obligations. Therefore this latent ambiguity must be resolved in favor of NDRIO's implied authority to effectuate its continuing appropriations and fulfill the fiduciary obligations of the boards and the plans they administer.[46]

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[44] N.D.A.G. 2011-L-05.

[45] N.D.C.C. §§ 15-39.1-05.2(4), 21-10-05, 21-10-06.2.

[46] In addition, both the retirement and investment programs are responsible for administering funds having constitutional protection. The retirement program administers the TFFR plan, which is the successor fund to the teachers' insurance and retirement fund, assuming all of its money, rights and obligations. N.D.C.C. §§ 15-39.1-01, 15-39.1-02, and 15-39.1-03. N.D. Const. art. X, § 12 appropriates the funds necessary for payments required by law to be paid to beneficiaries of the teachers' insurance and retirement fund. Therefore, TFFR enjoys the special status conferred on the teachers' insurance and retirement fund. N.D.A.G. Letter to Hanson (Feb. 25, 1987). Likewise the investment program overseen by the NDSIB has a constitutional mandate to invest the legacy fund. N.D.A.G. 2011-L-05. Neither the Legislature nor the people may refuse to fund a constitutionally mandated function. N.D.A.G. 2011-L-05.

CONCLUSION

NDPERS and NDRIO are large, complex agencies governed by a myriad of state statutes. Among those statutes are a few laws that specifically require biennial legislative appropriation to pay certain expenses.[47] To the extent the agencies rely on their implied appropriation authority, they must recognize these express limits and, where practicable, avoid expending funds for activities that explicitly require biennial legislative action. Where such activities are inescapably intertwined with other agency activities, however, it would be unreasonable to require the agencies to separate them, especially considering that neither the agencies nor the members, beneficiaries, or clients of the funds they administer are responsible for the current circumstances necessitating this opinion.

Under these unique circumstances, it is my opinion that the express continuing appropriation authority granted these agencies combined with their independent legal obligations as fiduciaries of the plans they administer carry with them the implied authority to expend funds for the salaries and associated operating expenses of the individuals needed to effectuate those appropriations in order to fulfill their fiduciary obligations, to the extent the implied authority is not prohibited under state law. While I cannot, in a legal opinion, determine the actual amounts these agencies may expend pursuant to this implied authority, I will remind the governing Boards of these agencies that they are and remain fiduciaries, and any expenditure of funds must be done prudently.

Sincerely,

Wayne Stenehjem
Attorney General

This opinion is issued pursuant to N.D.C.C. § 54-12-01. It governs the actions of public officials until such time as the question presented is decided by the courts.[48]

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[47] See, e.g., N.D.C.C. §§ 54-52.3-03, 54-52-04(11), 39-03.1-04.
[48] See State ex rel. Johnson v. Baker, 21 N.W.2d 355 (N.D. 1946).

NORTH DAKOTA RETIREMENT AND INVESTMENT OFFICE

INTRA-QUARTER MONITORING UPDATE

As of June 19, 2015

STAFFING UPDATE

Michael Dewitt resigned as Data Processing Coordinator for RIO effective May 29, 2015, to pursue other opportunities. We were sad to learn of Michael's decision to leave given the knowledge and experience he brought to our team since joining RIO in April of 2014, but we wish him the best in his future endeavors.

Rich Nagel, as Supervisor of Information Systems, will expand his considerable duties and responsibilities to fulfill our IT needs while we seek a qualified candidate over the next several months.

AGENDA ITEM V.C.

INFORMATIONAL – NO BOARD ACTION REQUESTED

TO: State Investment Board

FROM: Dave Hunter

DATE: June 22, 2015

SUBJECT: Pension Governance Offsite

Overview:

At the request of the SIB, RIO will invite SIB client board members to attend a pension governance offsite on the morning of July 24, 2015, at the University of Mary from 8:30 am to Noon. Our notable guest presenter will be Keith Ambachtsheer of *KPA Advisory Services*. Keith has been a leader in pension fund governance for over 30 years and serves as the Academic Director of the Rotman-ICPM Board Effectiveness Program for Pension Funds and Other Long-Horizon Investment Institutions. Mr. Ambachtsheer also founded KPA Advisory Services in 1985 and co-founded CEM Benchmarking in 1991, the latter of which benchmarks the organizational performance of some 400 major pension funds around the world. Keith's background is attached.

Mr. Ambachtsheer intends to present on the following three major areas of interest:

1) "How Effective is Pension Fund Governance Today and Do Pensions Invest for the Long Term" (a review and discussion of recent survey findings);
2) "The Evolving Meaning of 'Fiduciary Duty': Is Your Board Keeping Up"; and
3) "Rethinking Investment Beliefs for the 21st Century".

University of Mary Campus and Meeting Location:

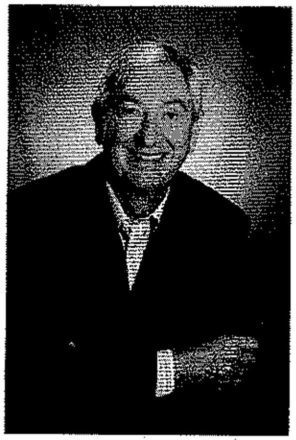
The University of Mary is located at 7500 University Drive in Bismarck about 2.5 miles south of Bismarck Municipal Airport. The presentation will be held in the Board Room at the Harold Schafer Leadership Center (Building 1 on the attached University of Mary Campus Map). Attendees can access parking via the South Entrance and park in the lot in front of the School of Business then walk across the white railed concrete pedestrian bridge into the Benedictine Center (where signs will be posted directing you to the Board Room).

Pre-Meeting Materials:

Mr. Ambachtsheer has requested attendees to read the attached articles in advance of our offsite, if possible.

NOTE: SIB clients are likely required to follow North Dakota Open Records and Meetings Law in the event a quorum is reached for their respective governing group.

KPA ADVISORY SERVICES LTD



KEITH AMBACHTSHEER
President
KPA Advisory Services

Keith has been a participant in the pensions and investments industry since 1969. He founded his own firm *KPA Advisory Services* in 1985. Through it, he provides strategic advice to a global clientele in person, and through the monthly *Ambachtsheer Letter*. He is the author of three best-selling books, and has been a regular contributor to industry publications since the 1970s. He was the Editor of the *Rotman International Journal of Pension Management* from 2008 to 2014.

In 1991, Keith co-founded *CEM Benchmarking* which benchmarks the organizational performance of some 400 major pension funds around the world. In 2005, he played a major role in founding the *Rotman International Centre for Pension Management (Rotman ICPM)*. He was appointed Director of *Rotman ICPM* and Adjunct Professor of Finance at the *Rotman School of Management, University of Toronto.* He was appointed Director Emeritus in 2014.

At the start of 2011, he was appointed Academic Director of the Rotman-ICPM Board Effectiveness Program for Pension Funds and Other Long-Horizon Investment Institutions. He has personal governance experience as a member of two corporate boards, and has served as Board Chair of a major medical foundation.

His research, writing and advice have influenced pension and endowment design, policy, and organizational structure in Canada and elsewhere. He has won major awards, including CFA Institute's Award for Professional Excellence in 2011 for "exemplary achievement, excellence of practice, and true leadership", and the EBRI Lillywhite Award in 2010, given in recognition of outstanding lifetime contributions to Americans' economic security. In July of 2009 Keith was awarded James Vertin Award from the *CFA Institute* for his contributions "of enduring value" to investment theory and practice. In 2007, he was honoured with the Outstanding Industry Contribution Award by *Investments and Pensions Europe.* In 2003, he was named 'One of the 30 Most Influential People in Pensions and Investments' by *Pensions and Investments* in the USA. In 2013, *aiCIO* named him one of the globe's "10 most influential academics in institutional investing", and the globe's #1 "knowledge broker" in institutional investing in 2014.

HOW EFFECTIVE IS PENSION FUND GOVERNANCE TODAY?

AND

DO PENSION FUNDS INVEST FOR THE LONG-TERM?

FINDINGS FROM A NEW SURVEY

"We need to move from long-term investing solutions to actions.........

First, we need to address the issue of governance of financial institutions."

Angel Gurria

General Secretary - OECD

Keith Ambachtsheer and John McLaughlin

January 2015

Background to this Study

This study marks the continuation of a series of survey-based research projects on pension fund governance by the authors and colleagues that stretch back over 20 years. A catalyst for this new effort was the *Focusing Capital on the Long Term (FCLT)* initiative launched by Dominic Barton (McKinsey) and Mark Wiseman (CPP Investment Board) in 2013.[1] In a subsequent Harvard Business Review article that provided context for the *FCLT* initiative, they wrote: *"If asset owners and managers are to do a better job of investing for the long-term, they need to run their organizations in a way that supports and reinforces this."*[2]

Obviously, the quality of the governance function in asset owner organizations is critical to this "do a better job of investing for the long-term" quest. Given our prior survey experience in the governance area, we offered to update our work in support of the *FCLT* initiative, and at the same time, gain a better understanding of the degree to which pension funds actually practice 'long-termism' in investing. We sent out a survey in June 2014 to 180 CEOs (or equivalents) of major pension (and related) organizations around the world. The survey's governance component was identical to prior surveys sent out in 1997 and 2005. Two months later we began the work of analyzing the 81 completed surveys, comparing the 2014 governance-related responses to those provided in 1997 and 2005, and interpreting the responses in the long-term investing part of the survey. This paper sets out our findings, and their implications for raising the effectiveness of the governance and investment functions of pension (and related) organizations.

Organization of this Paper

The paper is organized into six parts:

Part I: Study Summary and Conclusions

Part II: Key Findings from Prior Governance Research

Part III: Description of the 2014 Survey and the Survey Respondents

Part IV: 2014 Survey Findings on Governance

Part V: 2014 Survey Findings on Long-Term Investing

Part VI: Key Take-Aways from the 2014 Survey Findings

About the Authors

Keith Ambachtsheer is Director Emeritus of the International Centre for Pension Management (ICPM) and Academic Director of the Rotman-ICPM Board Effectiveness Program at the Rotman School of Management, University of Toronto. He is co-founder and President of KPA Advisory Services, and co-founder and Board Member of CEM Benchmarking Inc.

John McLaughlin is co-founder and Board Chair of CEM Benchmarking Inc. He is also a Board Member of a number of public and private enterprises and a graduate of the ICD / Rotman Directors Education Program and a holder of the ICD.D designation.

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[1] For more information on the *FCLT* initiative, visit *www.FCLT.org*.

[2] From Barton and Wiseman (2014) "Focusing Capital on the Long-Term", Harvard Business Review, Jan-Feb. Barton and Wiseman also published a follow-up article in the Jan-Feb 2015 issue of the HBR titled "Where Boards Fall Short".

PART I: STUDY SUMMARY AND CONCLUSIONS

We recently conducted a survey-based study on the effectiveness of pension fund governance, and on long-horizon investment attitudes and practices. A broadly-based group of 81 major pension organizations from around the world with aggregate assets of USD $5 trillion participated in the study. Here we set out the major study findings.

On Pension Fund Governance

Prior studies on the effectiveness of pension fund governance over the course of the last 20 years all reached the conclusion that there was considerable room for improvement. Despite evidence that board effectiveness is marginally improving, our survey-based study conducted in 2014 finds that much work still needs to be done:

- Board selection and improvement processes continue to be flawed in many cases.
- The board oversight function in many organizations needs to be more clearly defined and executed.
- Competition for senior management and investment talent is often hampered by uncompetitive compensation structures.

It will require a concerted, ongoing joint effort by pension plan stakeholders, pension organization boards, regulators, and legislators to change the current situation.

On Long-Horizon Investing

There was broad consensus among the survey participants that conceptually and aspirationally, long-horizon investing is a valuable activity for both society, and for their own fund. However, there is a significant gap between aspiration and reality to be bridged. Barriers to putting good long-horizon investing intentions into practice include:

- Regulations that force short-term thinking and acting.
- A short-term, peer-sensitive environment that makes it difficult to truly think and act long-term.
- The absence of a clear investment model, performance metrics, and language that fit a long-term mindset.
- Alignment difficulties in outsourcing, and compensation barriers to in-sourcing.

Here too a concerted effort (both inside pension organizations and among them) will be required to break down these barriers.

On The Relationship between Governance and Long-Horizon Investing

We found statistically positive relationships between the governance quality rankings and the long-horizon investment quality rankings. This raises the question of causation. Is the measured correlation merely a statistical artifact of the biases of the 81 survey respondents? Or is better governance really driving long-horizon investing quality? The qualitative commentary provided by the survey respondents make a plausible case for the latter interpretation.

PART II: KEY FINDINGS FROM PRIOR GOVERNANCE RESEARCH

Anthropologists O'Barr and Conley caused quite a stir in 1992 with their book "Fortune and Folly: The Power and Wealth of Institutional Investing".[3] After observing the behavior of nine major US pension funds over a two-year period, they concluded that the aim of the funds appeared to be focused more on responsibility deflection and blame management than on good governance and creating value for fund stakeholders. This observed behavior is very much in line with Keynes' 1936 remark about investment committees that "worldly wisdom teaches that it is better for reputation to fail conventionally than to succeed unconventionally...".[4]

A 1995 study in which we were involved surveyed 50 senior US pension fund executives on what they estimated the "excellence shortfall" to be in their organization. In other words, if the known barriers to excellence could be lifted out of their organizations, by how much might long-term investment performance improve? The median response was 66 bps. When asked to identify the sources of excellence shortfall, respondents most frequently cited poor decision-making processes, inadequate resources, and a lack of focus and clarity of mission.[5] Studies by Clark et al. in the UK (2006 and 2007) and by Clapman et al. in the USA (2007) confirmed the presence of these challenges in many pension organizations.[6]

An article by Clark and Urwin in the inaugural issue of the Rotman International Journal of Pension Management[7] (RIJPM Fall 2008) made these key observations about Boards of pension organizations:

- Understanding human behavior and cognitive biases is an important element in designing effective Board governance structures.
- Board members must be collegial, representative, and make a collective commitment to understand and fairly balance stakeholder interests.
- In reality, Boards often suffer from unacknowledged differences in individual decision-making styles, lack focus, and are overwhelmed by the range of issues they must deal with.
- In this context, the Board Chair role is critically important. The Chair must ensure there is a clear link between stakeholder expectations and the organization's culture, its strategic plan, and how it executes that plan. Most importantly, this person must command strong personal respect.

An article by Ambachtsheer, Capelle, and Lum in that same RIJPM issue[8] describes a pension fund governance survey first carried out by the authors in 1997, and repeated in 2005. Its key findings and conclusions are set out below.

Understanding the Pension Governance Deficit

The survey posed two open-ended questions to pension fund CEOs. One was about Board priorities; the other about organizational priorities. It also asked participants to rank 45 statements about governance, management, and operational effectiveness in their organizations. They were asked to indicate their

[3] O'Barr and Conley (1992) "Fortune and Folly: The Wealth and Power of Institutional Investing". Irwin Books.
[4] Keynes (1936) "The General Theory of Employment, Interest and Money", Chapter 12. Palgrave Macmillan.
[5] Ambachtsheer, Boice, Ezra, McLaughlin (1995), "Excellence Shortfall in Pension Fund Management: Anatomy of a Problem", unpublished working paper.
[6] The studies by Clarke et al. are summarized in (2008) "Best-Practice Pension Fund Governance". Journal of Asset Management. See also Clapman (2007) "Model Governance Provisions to Support Pension Fund Best-Practice Principles". Stanford University Law School.
[7] Clark and Urwin (2008) "Making Pension Boards Work: The Critical Role of Leadership". Rotman International Journal of Pension Management, Fall.
[8] Ambachtsheer, Capelle, and Lum (2008) "The Pension Governance Deficit: Still With Us". Rotman International Journal of Pension Management, Fall.

disagreement/agreement with each statement on a scale from 1 (total disagreement) to 6 (complete agreement). Each statement was crafted so that the higher the assigned number, the greater the perceived effectiveness. The survey elicited 80 responses in 1997 and 81 in 2005 from diverse groups of pension organizations by type, size, and geography.

Table 1 sets out the CEO responses to the Board and managerial priorities questions in the 2005 survey. They saw big challenges for Board governance in three areas: Agency/Context issues, Board Effectiveness issues, and Investment/Risk Management issues. The biggest managerial challenge is strategic planning and its execution. Table 2 provides greater detail about each of these four perceived challenge areas. Note that while, on the one hand, the four areas are distinct, they are also the four key pieces of a larger pension governance and management puzzle. They revolve around the following questions:

1. How clear are pension Boards about the pension contracts they are overseeing and about the fiduciary duties of loyalty and even-handedness that oversight involves?
2. Does the Board understand the difference between Board governance and management accountability for achieving clearly agreed-on organizational goals? Can the Board ask the right questions about strategy and its execution?
3. Has the organization worked out a set of well-articulated investment beliefs that both the Board and management understand and truly believe in? Is it clear which stakeholders are bearing what risks?
4. Does the organization have the necessary resources to execute its strategic plan? If not, what are the blockages and what is the plan for removing them?

The relevance and importance of these questions is reinforced by the outcomes of the scoring process of the 45 survey statements. Table 3 compares the six lowest-scoring statements in 1997 and 2005. Note they are almost identical, and that, directly or indirectly, all six relate to Board effectiveness problems. Specifically, they point to Board selection and evaluation difficulties, to ineffective delegation to management, and to attracting and retaining top talent into the organization.

Table 1: Pension Fund Oversight and Management: What Really Matters?

1. What are the more important oversight issues?	**Proportion of Responses**
a. Agency / context issues	44%
b. Governance effectiveness issues	36%
c. Investment beliefs / risk management issues	20%
2. What are the more important management issues?	**Proportion of Responses**
a. Strategic planning / management effectiveness	73%
b. Agency / context issues	15%
c. Investment beliefs / risk management issues	12%

Source, RIJPM, Fall, 2008

Table 2: Pension Fund Governance and Management: Specific Challenges

1. **Agency / Context Issues**
   a. Balancing stakeholder interests
   b. Understanding the legal / regulatory environment
2. **Oversight effectiveness issues**
   a. Appropriate skill / knowledge set for the Board
   b. Clear delegation to management
3. **Investment beliefs / risk management issues**
   a. Understanding context-based risk and its management
   b. Informed investment beliefs and their relevance
   c. Shift to risk budget-based investment process
4. **Strategic planning / management effective issues**
   a. Resource planning, organization design, and compensation
   b. Clear delegation from the Board
   c. Effective information-technology (IT) systems

Source, RIJPM, Fall, 2008

Table 3: The Six Lowest Scoring Statements in 1997 and 2005

Ranking	1997	2005	Ranking
40	Compensation levels in our organization are competitive	Compensation levels in our organization are competitive	40
41	My Board of Governors does not spend time assessing individual investment managers or investments.	My Board of Governors does not spend time assessing individual investment managers or investments.	41
42	My Board of Governors examine and improve their effectiveness on a regular basis.	My Board of Governors examine and improve their effectiveness on a regular basis.	42
43	Our fund has an effective process for selecting, developing, and terminating members of the Board of Governors.	I have the authority to retain and terminate investment managers. .	43
44	I have the authority to retain and terminate investment managers.	Our fund has an effective process for selecting, developing, and terminating members of the Board of Governors.	44
45	Performance-based compensation is an important component of our organization design.	Performance-based compensation is an important component of our organization design.	45

Source: RIJPM, Fall, 2008

Recommendations for Action

Based on these findings, the article identified six opportunities for fixing the documented governance deficit that still existed in many pension organizations in the middle of the first decade of the 21st Century:

1. Redesign pension contracts to eliminate any existing incompleteness, over-complexity, and/or unfairness problems. This is usually not something Boards themselves can do, but their views will likely be carefully listened to by the contracting parties.
2. Create a Board skill/experience matrix to reflect the reality that while pension Boards need to be seen to be representative and hence legitimate, that is not enough. They must also possess the requisite collective skills and experience to be an effective governance body.
3. Initiate a Board self-evaluation protocol in order to identify and address weaknesses.
4. Ensure clarity between Board and management roles. Lack of clarity causes organizational gaps, compressions, and a great deal of frustration.
5. Adopt a high-performance stance through-out the organization and ensure it has the necessary human and technical resources to turn the aspiration into reality.
6. Make Board effectiveness a regulatory requirement. It would be a simple matter for pension regulators to require that pension organizations annual disclose the steps they are taking to ensure that an effective governance function is in place.

A significant outcome of this work was the establishment of the week-long Rotman-ICPM Board Effectiveness Program (BEP) for Pension and Other Long-Horizon Investment Organizations in 2011. Its curriculum covers all six of the 'action' opportunities listed above. The Program has been offered five times thus far, resulting in 153 BEP 'graduates' from 56 different organizations and 11 countries.[9]

[9] BEP6 and BEP7 will be offered February 9-13 and November 30-December 4 in 2015, Visit https://www.rotman.utoronto.ca/ProfessionalDevelopment/Executive-Programs/CoursesWorkshops/Programs/Pension-Management.aspx for more information

PART III: DESCRIPTION OF THE 2014 SURVEY AND THE SURVEY RESPONDENTS

An interesting dimension in the cited 2008 RIJPM article was the ability to compare the assigned CEO scores to the same statements in 1997 and 2005. Based on the average 1997/2005 scores, we found four statements related to strategic planning, Board self-evaluation, and HR/compensation practices showed the greatest improvement over the period. However, Table 3 indicates that these dimensions of pension fund governance and management were still among the lowest ranked among all 45 statements in 2005. The implication was that much work remained to be done.

The introduction to this paper noted that with nine years having passed since the 2005 survey, we decided to conduct the pension fund governance survey a third time in 2014. To focus more directly on Board governance matters, we pruned the 45 original survey statements down to the 23 that focused most directly on the governance function. Once again, we were able to achieve the high response rates of 1997 and 2005. Table 4 compares the demographics of the 2014 responding organizations with those of 1997 and 2005. Note that the 2014 responding group was considerably larger, less corporate, and more geographically diverse than the 1997 and 2005 groups.[10] Aggregate assets amounted to about USD $5 trillion. Table 5 indicates that the people who completed the survey were generally senior, long-tenured pension organization executives.

Table 4: Demographics of the 1997, 2005, and 2014 Responding Groups

Survey Respondents	1997	2005	2014
Number of Respondents	80	81	81
US	54%	44%	29%
Canada	46%	41%	28%
Europe		11%	31%
Asia, Australia, New Zealand		4%	14%
Public Sector	24%	41%	60%
Corporate	63%	38%	19%
Other	14%	21%	21%
Median plan size Billion USD	2.1	3.7	22.7

Table 5: Demographics of the People Completing the 2014 Survey

Global 23 Canadian 22 European 25 United States 11 Asia, Australia, NZ	Senior 54 CEO, CIO, Executive or Managing Director 27 Other Senior Titles
Long tenured in organization Average 12 years with organizations Range 1 to 35 years	**Long tenured in positions** Average 7 years in position Range 1 to 27 years

29 respondents represent ICPM Research Partners

[10] The "Other" category in Table 4 was a mix of multi-employer pension plans, union pension plans, fiduciary managers, and special-purpose organizations such as workers compensation insurers.

PART IV: 2014 SURVEY FINDINGS ON GOVERNANCE

We explained above that the respondents to the earlier 1997 and 2005 surveys were asked to rank 45 statements about governance, management, and operational effectiveness in their organizations. They were asked to indicate their disagreement/agreement with each statement on a scale from 1 (total disagreement) to 6 (complete agreement). Each statement was crafted so that the higher the assigned number, the greater the perceived effectiveness. As already noted, the 2014 survey was reduced to the 23 statements directly related governance effectiveness. In the analysis that follows, the 2014 responses to these 23 statements were compared to the 1997 and 2005 responses to the same 23 statements.

Insights from the Rankings

Figure 1 displays the distribution of responses to the 23 governance statements in 1997, 2005, and 2014. The general bias towards high rather than low scores is a common phenomenon with this type of survey design. However, note that the average ranking marginally increased over to the 17-year period (i.e., from 4.5 to 4.7 to 4.8), possibly indicating a marginal improvement in the effectiveness of pension boards over this period.

Figure 1: The Response Distributions in 1997, 2005, and 2014

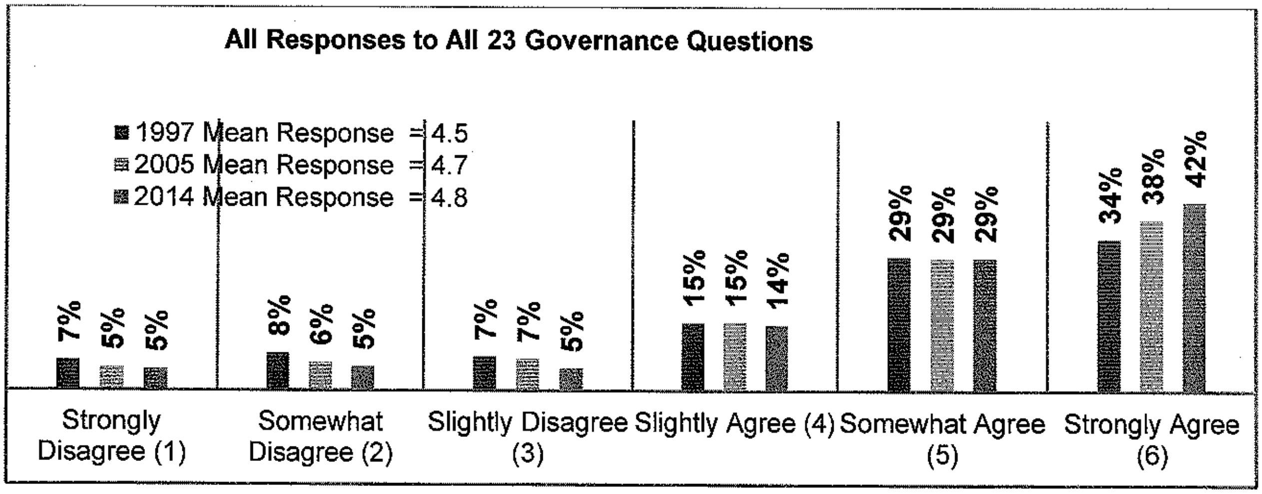


Table 6 compares the five highest-scoring statements in 2014 (i.e., indicating the highest satisfaction levels) with the five lowest-scoring statements (i.e., indicating the lowest satisfaction levels). Readers are invited to draw their own conclusions from Table 6. It seems to us there are elements of contradiction in these two sets of survey responses. For example, how is it possible for senior executives in pension organizations to, on the one hand, say they are getting the resources necessary to do their job, but on the other, say that compensation levels in the organization are uncompetitive? Similarly, how is it possible for senior executives in pension organizations to say that their Boards hold them accountable for results, but on the other, that they meddle in operational matters (e.g., the hiring and firing of investment managers)?

Table 6: Areas of Highest vs. Lowest CEO Satisfaction

GOVERNANCE

Highest agreement in latest survey	Mean Score 2014 Rank
My governing fiduciaries do a good job of representing the interests of plan stakeholders.	1
Developing our investment policy required considerable effort on the part of myself and the governing fiduciaries and it reflects our best thinking.	2
There is a clear allocation of responsibilities and accountabilities for fund decisions between the governing fiduciaries and the pension investment team.	3
My governing fiduciaries hold me accountable for our performance and do not accept subpar performance.	4
My governing fiduciaries approve the necessary resources for us to do our work.	5

Lowest agreement in latest survey	Mean Score 2014 Rank
I have the authority to retain and terminate investment managers.	19
Compensation levels in our organization are competitive.	20
My governing fiduciaries have superior capabilities relevant knowledge, experience, intelligence, skills necessary to do their work.	21
Our fund has an effective process for selecting, developing and terminating its governing fiduciaries.	22
Performance based compensation is an important component of our organizational design.	23

Table 7 compares the five lowest-scoring statements in 1997, 2005, and 2014. Remarkably, they were the same five each time. To us, they offer the clearest indication of where the challenges with governance in the pensions field continue to lie, and the consequences they continue to lead to. Specifically, inadequate selection processes for board members continue to lead to ineffective board oversight protocols, which in turn continue to lead to board meddling in operational matters, and to inadequate resourcing in such key functional areas as investing.

Table 7: The Five Lowest-Scoring Statements in 1997, 2005, and 2014

GOVERNANCE

Lowest agreement over 3 surveys	Mean Score 1997 Rank	Mean Score 2005 Rank	Mean Score 2014 Rank
Compensation levels in our organization are competitive.	18	18	20
My governing fiduciaries examine and improve their own effectiveness on a regular basis.	20	20	17
I have the authority to retain and terminate investment managers.	22	21	19
Our fund has an effective process for selecting, developing and terminating its governing fiduciaries.	21	22	22
Performance based compensation is an important component of our organizational design.	23	23	23

Table 8 assesses the regional variations in how the 23 statements were ranked. The clear message here is that the European respondents scored a number of governance statements materially lower than their counterparts in North America and the Pacific Rim. At the other end of the spectrum, pension organizations in Canada, Australia, and New Zealand were more likely to feature a performance-based element in their compensation arrangements.

Table 8: Regional Variations in Governance Quality

GOVERNANCE

Regional variation from mean response to questions	Europe	Canada	USA	Asia Australia New Zealand	All plan mean response
Performance based compensation is an important component of our organizational design.	−	+		+	3.7
My governing fiduciaries set a clear, appropriate, understandable and well-communicated framework for values and ethics.	−				5.1
My governing fiduciaries set clear, appropriate, understandable and well communicated standards for our organizational performance.	−				4.9
My governing fiduciaries do a good job of balancing over-control and under-control.	−				4.8
I have the necessary managerial authority to implement long term asset mix/balance sheet risk policy within reasonable limits.	−		+		5.0
There is a clear allocation of responsibilities and accountabilities for fund decisions between the governing fiduciaries and the pension investment team.				−	5.4

+	Response more than 0.5 above mean
−	Response more than -0.5 below mean

Additional Insights on Governance from Respondent Comments

In addition to ranking the 23 governance statements, survey participants were asked to address the question: "What do you see as the most important governance questions facing your Board at this time?" This is what they told us:

<u>Board Composition and Skills</u>

- *"Our board members should be more experienced and have more skills and intelligence."*
- *"Getting timely appointments..."*
- *"Board turnover: too much among beneficiary reps and legislative reps. Too little among appointed investment experts. Control rests with state legislature"*
- *"Too much board turnover (due to term limits). Too much staff turnover (due to retirements) Even though policies are well documented, the loss of institutional memory and continuity has the potential for negative outcomes..."*
- *"The most important issue in governance ...is illiteracy in committee members regarding pension fund management. Governance is in place but hardly operational..."*
- *"Selection of pension committee members with sufficient investment expertise ..."*

- *"Education of Board members..."*
- *"Getting new governing fiduciaries up to speed on pensions, pension investing, and fiduciary management (80% turnover) ..."*
- *"...Ensuring ongoing Board capacity for increasing oversight and risk management functions.."*
- *"...Securing the ability of the board to actually handle the (increasing) responsibilities allocated to the board through regulatory changes..."*

Board Process

- *"The board spends too much time on administrative issues and individual approvals of investments and not enough time on overall strategic positioning of the portfolio and longer-term macro risks and opportunities for the fund and the business. "*
- *"...blessed with a ...truly outstanding group...., but they are collectively flying just above the tree tops instead of a higher fiduciary altitude. ... time is largely spent at the deal and manager level..."*
- *"Refused to delegate manager hiring and firing..."*
- *"...(Management) can terminate while (Board) Investment Committee retains managers"*
- *"Time management: spending more time on interviewing and meeting with investment managers versus strategic business decisions... "*
- *"Staying purposefully high level/ strategic in their decision making and understand/ be comfortable with the importance of clear delineation of responsibilities between the board and the organization.... "*
- *"The board spends too much time on administrative issues and individual approvals of investments and not enough time on overall strategic positioning of the portfolio and longer-term macro risks and opportunities for the fund and the business."*

Compensation

- *"The design and implementation of market-competitive compensation plans to attract and retain high-caliber investment and senior management talent. As (a public entity we are) subject to restraint legislation and policies affecting compensation and business-related expenses. "*
- *"Alternative compensation models: no appetite to review or discuss these. "*

Clearly, these respondent comments strongly re-enforce the insights extracted from the survey statement rankings.

PART V: 2014 SURVEY FINDINGS ON LONG-TERM INVESTING

Consistent with the design of the governance component of the survey, respondents were also asked to rank their agreement/disagreement with 22 statements related to the organization's attitudes and practices regarding long-horizon investing on a scale from 6 to 1. Below, we report their responses, both to the 22 statements and to our invitation to share any comments they might have on the topic.

Insights from the Rankings

Figure 2 displays the distribution of assigned rankings to the 22 long-horizon investing statements. Note the shape of the distribution is the same as those of the governance quality rankings, with a strong bias towards assigning high rankings. Recall that the average 2014 governance quality ranking was 4.8, almost identical to the average long-horizon investing satisfaction ranking of 4.9.

Figure 2: The Long-Horizon Investment Ranking Distribution

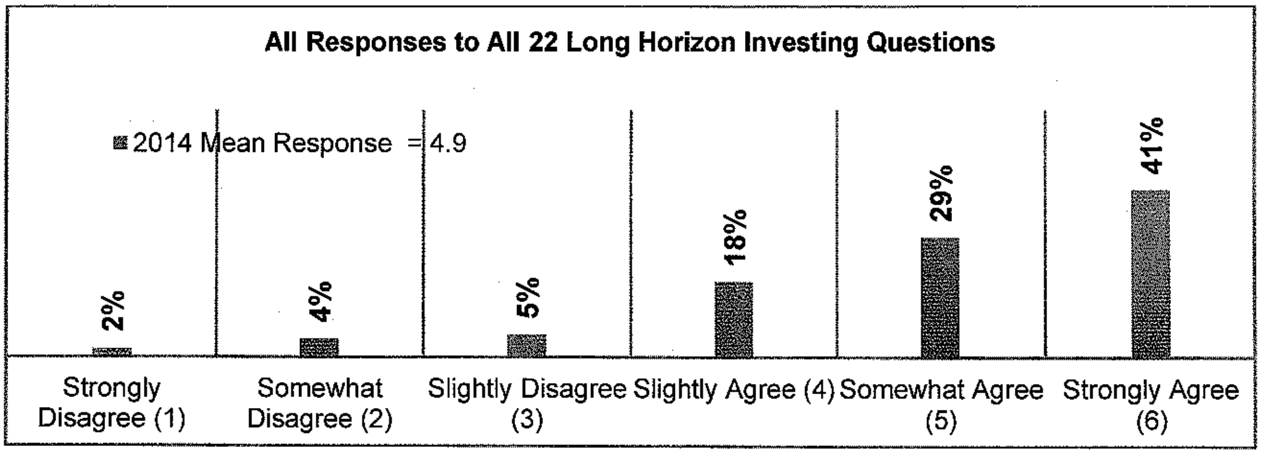


Table 9 shows a strong dichotomy between highly-ranked aspirational statements about long-horizon investing, and the much lower-ranked implementation realities. For example, on the one hand, pension funds seem to have good policy intentions and strong beliefs that long-horizon investing is a potentially promising value-adding activity. On the other hand, survey respondents indicate they have considerable difficulties with such implementation activities as creating proper incentives for long-horizon investing, participating in constructive Environmental, Social, and Governance-related and engagement strategies, and designing effective performance monitoring and measurement systems.

Table 10 provides a geographic breakdown of the long-horizon investing rankings. It shows an interesting contrast with Table 8, which provided a geographic breakdown of the governance quality rankings. Whereas European pension organizations scored lower on a number of key governance criteria in Table 8, they score higher on two key long-horizon investing criteria (e.g., in engagement strategies and in integrating ESG criteria into investment decision-making).

Table 9: Highly-Ranked vs. Lowly-Ranked Long-Horizon Investing Statements

LONG HORIZON INVESTING

Highest agreement	Mean Score 2014 Rank
We believe that the capability to invest for the long-term is a significant advantage in creating value.	1
Our organization's statement of investment policy explicitly states that we invest for the long-term.	2
Specific components of our Fund are explicitly designated to focus on investing for the long-term.	3
We have a specific overall allocation policy to implement a long-term orientation in our Fund.	4
We believe that our long-term investing protocols create significant value.	5

Lowest agreement	Mean Score 2014 Rank
We (or our managers on our behalf) have explicit policies for engaging corporations (or other organizations) we invest in when we think proactive engagement is warranted.	18
The mandates for each long-term component explicitly express long-term objectives and shorter-term downside tolerance.	19
Our approach to evaluating long-term fund components is meaningfully different from other components.	20
The investment manager compensation for the long-term fund components has been explicitly designed to reflect the long investment horizon.	21
We (or our managers on our behalf) explicitly integrate environmental and social factors into deciding which corporations we invest in.	22

Table 10: Regional Variations in Long-Horizon Investing Rankings

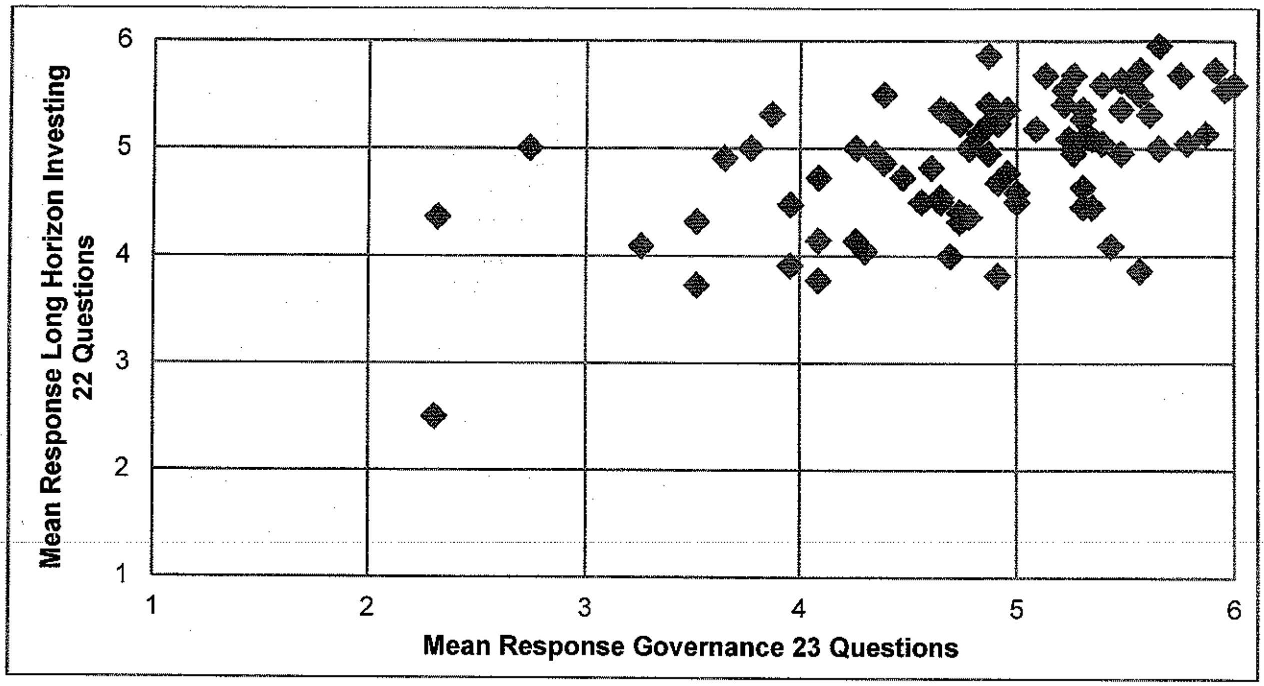
LONG HORIZON INVESTING

Regional variation from mean response to questions	Europe	Canada	USA	Asia Australia New Zealand	All plan Mean Response
We or our managers on our behalf have explicit policies for engaging corporations or other organizations we invest in when we think proactive engagement is warranted.	+	−			4.4
We or our managers on our behalf explicitly integrate environmental and social factors into deciding which corporations we invest in.	+	−	−		4.1
Specific components of our Fund are explicitly designated to focus on investing for the long-term.				−	5.5

+	Response more than 0.5 above mean
−	Response more than -0.5 below mean

It is tempting to attach considerable weight to the positive correlation between the governance scores and the long-horizon investing scores indicated in Figure 3.[11] Does stronger pension governance really lead to a greater emphasis on long-horizon investing? Or does it simply reflect a consistent high/low ranking bias by the survey participants? (i.e., some participants may have a consistently positive ranking bias, while other may have a consistently negative bias). The written participant comments below shed light on how these questions might be answered.

Figure 3: A Positive Correlation between Governance and Long-Horizon Investing Scores?



Additional Insights on Long-Horizon Investing from Respondent Comments

In addition to ranking the 22 long-horizon investing statements, survey participants were asked to address the question: "Please feel free to elaborate on any of the rankings you have assigned. We would also like to learn more about your organization's journey towards long-horizon investing to date, and your intentions over the next three years." This is what they told us:

- *"...(We have) long term strategic planning, but we are facing regulation that forces us to think short term..."*
- *"...It is difficult to describe differences in our approach with respect to long-term and short-term investing. Our due diligence processes are consistently applied with a view to longer-term performance."*
- *"Really at the start of the journey but progressing fast. ... DB funds not always as long-term as they would like to be given de-risking."*
- *"In a peer sensitive environment, it is generally difficult to be truly long-term in investing. Even if the current board and investment team take long-term positions, competitive pressures can stand to dominate. In such cases, a change in the board can bring risks of change in approach. Extraction from long-term positions can be very expensive."*

[11] The correlation coefficient is 0.55. Its t-value is 5.9, indicating a high degree of statistical significance.

- *"The long-term investing belief is now firmly rooted... A lot of work had to be done on policy making, mandate formulation and actually starting long-term mandates. We find it challenging to define a monitoring and guidance framework for long-term investing (we feel we need new "Language" there, Not many people seem to have answers to these questions)... "*
- *"...competitive advantage accrues to investors able to take a long view. This (led us to) high weightings in illiquid or semi-liquid investments. Returns have mostly been good but ... returns to external managers have been much better (fees!) ... long-termism did not sufficiently permeate our liquid investments...organized around market index-relative metrics. We are in the process of developing a much more joined-up approach, with ...internal investment selection...buy-to-hold and more substantial approach to sustainable ownership."*
- *"All our investments, apart from short term liquidity, are invested with a long-term perspective. ...We do not believe that the interests of external fund managers are genuinely aligned with ours..."*
- *"Long-term investing is less about time frame and more about alignment with long-term objectives of the investor and long-term structural trends (e.g. climate change). It is when you invest with an interest in the cashflow-generating potential of the investment over the long-term. It is not a buy and hold strategy. Investors who are permanently invested in equity indices are not long-term investors, even if they have low turnover/ no turnover"*
- *"...having long term liabilities does not entail a particular – and particularly patient – approach to investment. We may buy assets, that you would think of as "long term" – e.g. infrastructure or forests – but if markets or other developments create a situation where we find that selling is in the better interest of our clients, that is what we will do."*

To us, these comments suggest that the measured statistical correlation between the Survey governance quality rankings and the long-horizon investment quality rankings are likely not to simply reflect survey respondent biases. Plausibly, the comments suggest that better-governed pension funds do indeed 'think smarter', and as a result, have more effective long-horizon investment programs.

PART VI: KEY TAKE-AWAYS FROM THE 2014 SURVEY FINDINGS

In our view, the survey findings lead to three key conclusions:

1. On Governance: while there is some evidence of improvement in the governance of pension organizations since 1997, major concerns about how board members are selected and trained, about the effectiveness of board oversight processes, and about the ability to attract and retain key executive and professional skills remain.
2. On Long-Horizon Investing: the comfort with, and the aspirations for the concept of long-horizon investing has yet to be matched with the design and application of an effective suite of implementation strategies that can realize those aspirations.
3. On the Relationship between Governance and Long-Horizon Investing: the survey offers plausible evidence of a positive relationship between governance quality and long-horizon investing quality. This relationship is likely not a spurious one.

In short, there is still much work to do to materially strengthen the effectiveness of both the governance and long-horizon investing functions in pension organizations. Likely, better governance also means better long-horizon investing, which in turn likely means higher return investing.[12]

[12] See Ambachtsheer (2014) "The Case for Long-Termism", Rotman International Journal of Pension Management (Fall) for more on the connection between investment performance and long-horizon investing.

The AMBACHTSHEER Letter

Sustainable Pension Design • Effective Pension Management

December 2014

THE EVOLVING MEANING OF 'FIDUCIARY DUTY':

IS YOUR BOARD OF TRUSTEES KEEPING UP?

"Years of focus on the duty of prudence by fiduciaries has generated myopic investment herding behaviors, undermined intergenerational pension equity, and disrupted attention to the duty of loyalty and impartiality.... ".

From "Reclaiming Fiduciary Duty Balance"
By Hawley, Johnson, and Waitzer (2011)

"The duty of impartiality requires fiduciaries to consider and balance the divergent interests of beneficiaries....including the intergenerational implications of their decisions.... ".

From "Reconnecting the Financial Sector and the Real Economy: A Plan for Action"
By Waitzer and Sarro (2014)

Pension Boards Lag Courts in Interpreting 21st Century 'Fiduciary Duty'

One of the most important, and possibly most underappreciated research projects funded by the Rotman International Centre for Pension Management (ICPM) over the course of the last four years was on the evolving meaning of 'fiduciary duty' for boards of pension organizations in the 21st Century. This work was conducted by legal scholars Jim Hawley, Keith Johnson, Doug Sarro, and Ed Waitzer. Their work led to the two articles in the Rotman International Journal of Pension Management (RIJPM) from which we quote above.[1] The two quotes capture the essence of their message: pension boards lag 'the trajectory of the law' in their understanding of their fiduciary duties. Boards have some serious 'catch-up' work to do.

This *Letter* summarizes the conclusions of the ICPM 'fiduciary duties' project, and sets out a work plan for pension boards that want to keep up with the evolving meaning of 'fiduciary duties' in the 21st Century, rather than suffering the regret f having to play 'catch up' ball in possibly unpleasant circumstances a few years down the road.

Why Now?

Why now? The authors point to four 'inflection point' catalysts that argue for proactive action by the boards of pension organizations now, rather than reactive action later:

- <u>The Growth of Pension Funds</u>: collectively, the global pension fund sector has become a major global financial force, with assets somewhere in the $30T-$40T range. The growing sovereign wealth fund and the foundation/endowment fund sectors add materially to these numbers. Collectively, these massive asset pools represent the multi-generational financial interests of hundreds of millions if not billions of beneficiaries. Collectively, the investment decisions of these pools directly impact both how the global financial markets work, and how the global real economy works. With their scale and necessarily long-term perspective to understand and meet the retirement income needs their members, pension organizations should be highly motivated to ensure they understand, and are in fact fulfilling their fiduciary duties.

- The Pervasive Influence of Agents and Emphasis on the Short-Term: while the investment policy documents of pension organizations tend to emphasize long-termism, actual practices continue to reflect short-termism in many cases. This dichotomy is re-enforced through multiple channels: the media, how performance is measured, how incentive compensation is structured, and through the presence multiple intermediary agents (e.g., consultants, money managers). There is no natural alignment between the financial interests of these agents and those of trust beneficiaries. In such an increasingly complex world, fiduciaries are seriously challenged to articulate the best short and long-term interests of current and future beneficiaries, and to demonstrate they are actually serving these interests in a balanced manner through their investment policies.

- Over-Reliance on Simplistic Investment Theories: while investment theories such as the Efficient Markets Hypothesis (EMH) are elegant, the assumptions behind them are far from reflecting reality. For example, in the case of the EMH, material information about individual investments is not always known by all investors all the time; further, information that is generally known is not always interpreted identically by all investors, and is not always accurately reflected in asset prices. Also, investors are not always 'rational', and risk tolerances are not always stable. Investment returns are not independently and identically distributed. As a result, while events like the Global Financial Crisis (GFC) cannot happen in an EMH world, they do happen in the real world. The point is that attempting to exercise the fiduciary duties of prudence, loyalty, and impartiality by taking the assumptions and implications of the EMH as 'reality' is not defensible conduct today. Board of trustees have an obligation to understand the world as it is, and not as it is posited in order to create elegant investment theory.

- Recent Legal Responses to Financial System Dysfunction: the four legal experts in the two RIJPM articles point to a number of recent legal opinions and actions that bear on the evolving meaning of 'fiduciary duty' in the 21st Century. In a pensions dispute, the US Supreme Court ruled that fiduciary duty requires "trustees to take impartial account of all beneficiaries...both present and future". The Dutch pension act requires fiduciaries to take into account the interests of all plan stakeholders in setting policy and making decisions. The GFC prompted a number of actions against financial institutions and individuals working in these institutions for fiduciary misbehavior. In contrast, the Supreme Court of Canada recently ruled against a class action initiated by a corporation's bond holders against its board of directors, ruling that the board had made reasonable decisions reflecting not only the interests of the corporation's creditors and shareholders, but also the corporation's broader obligations "as a good corporate citizen". Emerging out of these opinions and judgments is a new 'reasonable expectations' standard for the exercise of fiduciary duty. This emerging view contrasts sharply with the historical view that attention to fiduciary duty could be demonstrated by engaging in a standard box-checking exercise drawn up by legal counsel.

There is a fifth 'why now' argument we would add to the four offered by the cited legal experts:

- Passive Acceptance of Unsustainable Pension Designs: readers of this *Letter* know of our discomfort with the traditional DB and DC pension designs. In our view, neither design fully acknowledges the differing needs of the young and the old today, as well as the financial interests of the young and the old of tomorrow. As a result, these traditional designs are problematic in a number of ways (e.g., the one-size-fits-all problem, the fuzzy property rights problem, the fuzzy risk definition and allocation problem). We set these views out in detail in a recent invited paper titled "Taking the Dutch Pension System to the Next Level: a View from the Outside".[2] If the duty of impartiality requires pension fiduciaries to consider and balance the divergent interests of various classes of beneficiaries and other risk-bearing stakeholders (including the intergenerational implications of their decisions), then it is reasonable to expect that these fiduciaries also have a duty to test the pension design of the plan they are governing for its long-term sustainability and for fairness regarding all plan stakeholder groups, present and future.

Now we move on from the 'why now?' question to the 'what now?' question. How should pension organizations individually, and collectively at the national and global pension community levels, respond to these five catalysts for action? The four cited law experts have some thoughts on these questions, as do we.

Responses at the Pension Organization Level

Stating the obvious, nothing much will happen at the organizational level unless its Board of Trustees (led by the Board Chair) is prepared to own the 'fiduciary duties' file. If that is the case, the following six-point check list may be helpful:

- Pension Design: do we have a fair, sustainable, understandable pension formula? How can we best address this question? What we would do if our formula doesn't pass a reasonable fair/ sustainable/understandable test?

- Stakeholder Communications: are we clear about who are stakeholders are? Do we communicate with them effectively about pension design? About the value the pension organization is creating for them? How do we know our communication strategies are effective?

- Organization Design: do we have a cost-effective organization that produces 'value for risk' and 'value for money' in its key functions? How can we best address this question? What would we do if our organization doesn't benchmark well in its key functions, using credible metrics?

- Board Effectiveness: how effective are we as a Board? Do we have the right mix of skills and experience? Are we seen as trustworthy by our plan stakeholders? Are we public-minded? Do we measure our own effectiveness and improve our own performance?

- Risk Management: what risks do we need to measure and manage? Do we have the people, protocols, and technology to do this well? If not, what are we going to do about it?

- Investment Beliefs and Policies: do we have an investment program geared to generate plan member wealth through long-horizon return compounding? Is it working well? How do we know? Do we have an investment program geared to meeting the payment obligations to retirees? Is it working well? How do we know?

While living by this six-point checklist would undoubtedly produce a good score on the organizational 'fiduciary duties' scale, there is another 'fiduciary duty' dimension that also needs attention.

Collective Responses at the National and Global Levels

In their 2014 "Reconnecting the Financial Sector to the Real Economy" article, Waitzer and Sarro propose four specific initiatives that financial institutions such as pension organizations, as well as law makers and regulators, could collectively undertake to strengthen the expectations and responsibilities attached to the fulfilling 'fiduciary duties':

- Foster 'Win-Win' Collaborations: there is a 'trust dilemma' in situations where there is no clear short-term net (i.e., after-cost) benefit for a single organization to become a 'first mover' on an issue that may be of great long-term collective benefit. The way out of such a dilemma is for multiple parties to agree on the importance of the issue, and to share the cost of addressing it. Examples of such collaborations already exist (e.g., ICGN, PRI, WEF, ICPM, CII, CCGG, Eumedion, NAPF, ASFA, ACSI, ICPM).[3] The recent FCLT (*Focusing Capital on the Long-Term*) initiative opens up the prospect of direct investor/investee collaboration on such issues as fostering a long-term perspective in investing and the measurement of organization success.

- Create Legal Mechanisms to Protect Future Generations: a possible measure to fight short-termism in political decision-making is to establish a commissioner or ombudsman to represent the rights of future generations. Such mechanisms already exist in the environmental and human rights spheres. More day-to-day decision-making could be delegated to non-partisan, independent agencies or to senior administrators with guaranteed term lengths.

- Rethink Legislation: much post-GFC financial legislation and regulation has spawned "complicated rules breeding complicated systems", which in turn feed a box-checking 'is it legal?' mentality. A far-better approach would be to specify far-fewer broad, coherent, concise, enforceable rules that focus on core expectations. Courts can also play a constructive role here through emphasizing the 'reasonable expectations' principle.

- Reassert the Social Utility of the Financial Sector: the GFC and the events that followed it greatly exacerbated the lack of public trust and understanding of the financial system writ large. Many years of hard work will be required to regain that public trust, and to enhance public understanding of the vital role the financial sector in general, and the pensions sector in particular, play in mobilizing capital and in pricing and allocating financial risks in a well-functioning economy. The CFA Institute's *Future of Finance* initiative is an example of the work already underway to address this challenge.

In the exercise of their fiduciary duties, pension boards of trustees need to be aware of these collective national and global initiatives, and they need to understand the roles their organizations are playing (or should be playing) in moving one or more of these four initiatives towards successful implementation.

Doing the Right Thing

In conclusion, Waitzer and Sarro argue that too much of board governance in the financial sector has, and continues to focus on 'doing things right'. That is, on technical compliance with whatever rules exist at the time a decision needs to be made. They argue a fundamental mind shift is required. Instead of focusing on 'doing things right', boards must begin to focus on 'doing the right thing'. In their view, this will be the basis on which their decisions and actions will increasingly be judged, both in courts of law, and of public opinion.

So 'doing the right thing' based on balancing the financial interests of all relevant stakeholder groups is the new 21st Century standard for testing the proper fulfillment of 'fiduciary duty'. It is all a board of trustees can reasonably be expected to do. Is your board meeting this standard?

Endnotes

1. *The two articles are required reading for participants in the Rotman-ICPM Board Effectiveness Program (BEP). The articles and as well as information about BEP can be accessed through the ROTMAN ICPM website.*
2. *Presented and discussed in Amsterdam this past December 11 and 12. Accessible through the KPA ADVISORY SERVICES website.*
3. *Collaboration theory and practices is another unique area where Rotman ICPM has invested research monies. See Danyelle Guyatt's RIJPM articles "Pension Collaboration: Strength in Numbers" (2008), and "Effective Investor Collaboration: Enhancing the Shadow of the Future" (2013).*

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The AMBACHTSHEER Letter
Sustainable Pension Design • Effective Pension Management

March 2015

RETHINKING INVESTMENT BELIEFS FOR THE 21ST CENTURY

"Piketty sees the 60-year WW1-1970s period as an anomaly....which is now well behind us.... Future annual returns on capital will likely fall below the 5% experience of the 18th and 19th Centuries...."

The Ambachtsheer Letter - April 2014

Rethinking MPT

When we entered the investment business 45 years ago, the big new thing was Modern Portfolio Theory, or MPT for short. It was elegant and radical at the same time: elegant because it embodied a simple, understandable set of investment beliefs....and radical because these beliefs were at odds with the conventional wisdom of the day.

Today, MPT is no longer new, and no longer seen by most as elegant or radical. Just as Thomas Piketty (of "Capital in the 21st Century" fame) saw the 60-year period from World War 1 to the 1970s as a socio-economic anomaly in the grander sweep of things, so is MPT increasingly seen as an interesting anomaly in an investment context. At its core lay the Efficient Markets Hypothesis (EMH). It posits that investors act rationally, have access to the same information sets, interpret that information the same way, and consequently, hold the same risky market portfolio. Investors expressed their different tolerances for risk-bearing through their different weightings of this risky market portfolio and a risk-free asset.

Today, we recognize that we cannot invoke MPT as a substitute for thinking about how investment markets really work, and for thinking about how the resulting investment beliefs should lead us to invest the financial wealth of other people. This *Letter* traces the evolution of our own investment beliefs over the course of the last four decades, and the investment policy conclusions they lead to today.

The Lo and Minsky Contributions

MIT's Andrew Lo offers a plausible alternative to the EMH: the Adaptive Markets Hypothesis, or AMH for short.[i] Lo explains it as taking a biological/evolutionary approach to understanding investment markets and the people in it, rather than a robotic 'physics' approach. It is fear and greed that drives these markets, more than sober, rational calculation. In a similar vein, Washington University's Hyman Minsky posited the Financial Instability Hypothesis (FIH), arguing that financial stability in developed economies would naturally become a source of future instability through speculative risk-taking. His work was largely ignored until people acknowledged that the Global Financial Crisis offered a text book example (a 'Minsky Moment') of the FIH in action.[ii]

In the tradition of Lo's AMH and Minsky's FIH, long-time readers of this publication will recognize Table 1 on the next page. It has played a central role in our prognostications about capital markets prospects for many years now, for three reasons:

1. The table reflects the FIH by reminding us that financial markets have mindsets that swing from extended periods of growing optimism to extended periods of growing pessimism.
2. It also reflects the AMH because these mindset swings impact pricing in the capital markets in predictable ways. Growing optimism leads to rising prices for risk assets, generous risk premium realizations, and hence falling

prospective risk premiums. Conversely, growing pessimism leads to falling prices for risk assets, negative risk premium realizations, and hence rising prospective risk premiums.

3. The table facilitates focused conversations about past investment eras, about the current one we are living through, and about periods during which one era transitions into another.

We stated the belief in our January 2014 *Letter* that the *Double Bubble Blues* era ended around 2010/2011, and that we have been transitioning into a new era which we called *Mature Capitalism.* Our challenge now is to visualize how a *Mature Capitalism* era might play out. A clue from Table 1 is that we should give it an optimistic spin, contrary to the prevailing mood of pessimism.

Conventional Narratives about the *Mature Capitalism* Era

As noted, most prognostications today about the unfolding future paint a rather dreary picture of it, with four defining elements:

- Demographics: as populations age and worker/retiree ratios fall from 4:1 to 2:1 in the developed world, consumption, capital formation, productivity will weaken, and hence economic growth will also weaken.
- Fiscal Deficits: both families and governments are borrowing to make ends meet. This cannot go on forever. Eventually, a day of reckoning will come. This too will dampen future economic demand, and hence growth prospects.
- Geopolitical Risks: seem to always be with us, with an assertive China, a belligerent Russia, and an unsettled Middle East making current headlines.
- Environmental Risks: are also in play in the form of global warming and changing weather patterns, which in turn cause wide-spread floods and droughts. The concomitant financial risk relates to assets becoming 'stranded' as the full costs of production are internalized (e.g., for carbon emission and water pollution).

If these four elements fully defined the now-unfolding *Mature Capitalism* era, one would think they would be reflected in how markets are pricing long-horizon financial assets such as equities. Yet, the earnings yield of the S&P500 is about 5% today, versus a long term average somewhere between 6% and 7%. In short, the pessimism embedded in the demographics, debt, geopolitical conflict, and climate change narratives don't seem to be embedded in the pricing of risky USA-based assets. European and Emerging Markets equities appear to be somewhat more conservatively priced at earnings yields of 6% and 7% respectively.[iii] Why are equity prices not deep in the dumps? Our January 2014 *Letter* referenced an *FAJ* article by William Bernstein titled "The Paradox of Wealth" as an explanation.

The Paradox of Wealth

Bernstein offers four reasons for why *Mature Capitalism* might turn out better than most people expect:

Table 1: Entering the Eighth Capital Markets Era Since WW1

Investment Era	Investor Mindset	Approximate Time Span	Dividend Yield Change	Realized *ERP**
The WW I Decade	Pessimistic	10 years	5% → 7%	- 5%
Roaring Twenties	Optimistic	10 years	7% → 4%	+ 12%
Dirty Thirties/ Fateful Forties	Pessimistic	20 years	4% → 7%	0%
Pax Americana I	Optimistic	20 years	7% → 3%	+ 8%
Scary Seventies	Pessimistic	10 years	3% → 6%	- 3%
Pax Americana II	Optimistic	20 years	6% → 1%	+ 9%
Double-Bubble Blues	Pessimistic	10 years	1% → 2%	- 6%
Mature Capitalism?	Optimistic?	20 years?	2% → ?%	?%

* Stock returns come from *Triumph of the Optimists* by Dimson, Marsh, Staunton. Bond returns are based on a hypothetical CPI-linked bond with a real yield of 2.5%. If the actual LT TIPS return had been used for the *Double-Bubble Blues* era, the realized ERP would have been -10%.

Table 2: S&P500 Fundamentals in Transition from *Double Bubble Blues* to *Mature Capitalism*

Year	Dividend Yield	Net Buy-Back Yield	Payout Yield	Plow-Back Yield	Earnings Yield	LT TIPS Yield	Implied ERP	Index Value	Trailing Earnings
2000	1.20%	0.70%	1.90%	1.70%	3.60%	3.70%	-0.10%	1320	$50
2001	1.30%	0.80%	2.10%	0.00%	2.10%	3.50%	-1.40%	1148	$25
2002	1.60%	0.80%	2.40%	0.60%	3.00%	2.70%	0.30%	880	$28
2003	1.80%	1.10%	2.90%	2.10%	5.00%	2.30%	2.70%	1112	$49
2004	1.70%	1.50%	3.20%	1.80%	5.00%	1.90%	3.10%	1212	$59
2005	1.80%	1.70%	3.50%	2.50%	6.00%	2.00%	4.00%	1248	$70
2006	1.90%	2.20%	4.10%	2.00%	6.10%	2.80%	3.30%	1418	$82
2007	1.90%	4.10%	6.00%	-1.50%	4.50%	2.50%	2.00%	1468	$66
2008	2.60%	2.40%	5.00%	-3.60%	1.40%	2.40%	-1.00%	903	$15
2009	2.50%	0.90%	3.40%	2.30%	5.70%	2.00%	3.70%	1115	$51
2010	2.00%	2.10%	4.10%	2.70%	6.80%	1.80%	5.00%	1258	$77
Mean	1.80%	1.70%	3.50%	1.00%	4.50%	2.50%	2.00%		
2011	2.10%	3.10%	5.20%	1.80%	7.00%	0.80%	6.20%	1258	$87
2012	2.30%	2.60%	4.90%	1.40%	6.30%	0.40%	5.90%	1426	$87
2013	2.10%	2.40%	4.50%	1.60%	6.10%	1.60%	4.50%	1848	$100
2014	2.10%	2.60%	4.70%	0.70%	5.40%	0.80%	4.60%	2059	$103
Mean	2.10%	2.70%	4.80%	1.40%	6.20%	0.90%	5.30%		

Sources: Bloomberg, Standard & Poor's, Garland, Lazonick

Should investors still be comfortable? Certainly 'yes' relative to the 2000 situation. And plausibly 'yes' if (a) US stocks in the index can maintain or grow their real earnings from here, and (b) if there is no permanent spike up in the LT TIPS yield from current levels. Further, recall our observation earlier that European and Emerging Markets equites are priced more cheaply than US equities.

Table 2 points to another unfolding trend: an apparent secular rise in Net Share Buybacks, from under 1% of the S&P500 index value in the early 2000s….to figures approaching 3% today, compared to a dividend yield of 2%. So corporations are now using more of their earning to buy back stock than they are to pay dividends. Further, when you add the two yields together (i.e., the Payout Yield), the sum of the two almost approaches the Earnings Yield. The implication is that corporations are now returning most of their earnings to shareholders in the form of dividends and share buy-backs, and retaining little for capital re-investment. This is yet another indication of the arrival of *Mature Capitalism*.

So where does all this lead to? The most important conclusion is that, despite the strong rise in the S&P500 in first four years of the *Mature Capitalism*, its valuation is not in 'bubble' territory. Pricing is consistent with a lower return-on-capital, lower growth, lower long-term interest rate environment. In such an environment, an equity risk premium in the 4% area does not seem out of line.

However, we advise readers to re-read last month's *Letter* on the excess return potential of what we called high-sustainability 'stakeholder value-creation' companies. There is a strong case that emphasizing this type of investment will continue to produce excess returns relative to the market portfolio in the *Mature Capitalism* era.

<u>*Endnotes:*</u>

i. *See, for example, Lo's 2011 book "A Non-Random Walk Down Wall Street".*
ii. *Look for a new film titled "Boom Bust Boom" on Hyman Minsky and his Financial Instability Hypothesis. Contact Marja Koolschijn at Cardano for more information. (m.koolschijn@cardano.com)*
iii. *See GMO's 4Q Quarterly Letter for more on this topic.*
iv. *For more on the share buy-back phenomenon, see William Lazonick's article "Profits Without Prosperity" in HBR – September 2014.*

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Hunter, David J.

From: Medora M. Sletten <mmsletten@umary.edu>
Sent: Monday, June 22, 2015 11:12 AM
To: Hunter, David J.
Subject: HSLC Map
Attachments: Map to Harold Schafer Leadership Center1.pdf

Hi Dave,

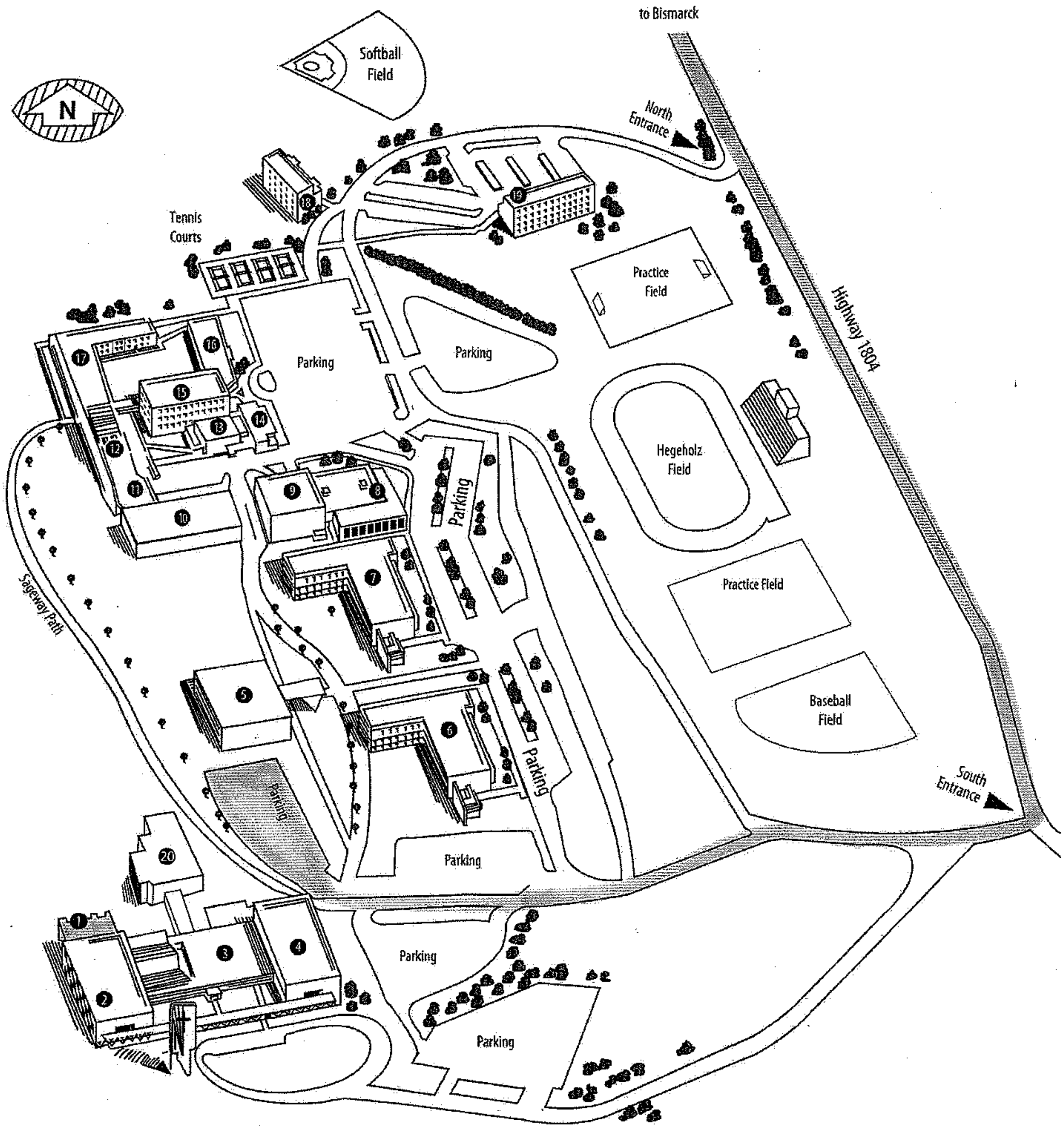
I have a map attached.

Take the south entrance onto campus. Guests can park in front of the School of Business and take the white pedestrian bridge into the brick Benedictine Center. Once inside, directional signs will be leading guests to the Harold Schafer Leadership Center down the long hallway.

Thanks,

Medora

Medora Sletten
Hospitality Coordinator
Office of Public Affairs
University of Mary
701.355.8089



UNIVERSITY OF MARY • BISMARCK, NORTH DAKOTA

1. Harold Schafer Leadership Center
2. Boniface Riverview Residence
3. Benedictine Center for Servant Leadership
4. Boniface Hall
5. Welder Library
6. Greg Butler Hall
7. Hillside Hall
8. Richard Tschider Center for Health Science
9. McDowell Activity Center
10. Leach Field House
11. Leach Center for Student Life
12. University Hall
13. Arno Gustin Hall
14. Clairmont Center
15. Harold J. Miller Center
16. Casey Center for Nursing Education
17. North Campus Residence Hall
18. Deichert Hall
19. Boyle Hall
20. Tharaldson School of Business

Revised 23 May 2008

STATE INVESTMENT BOARD MEMO
June 26, 2015

RE: Recommendation on ED/CIO Compensation

FROM: Robert Lech, Chairperson of Executive Review Subcommittee

BOARD FOCUS: Action

The purpose of this memo is to provide a recommendation from the Executive Review Committee regarding the salary increase for Mr. David Hunter, Executive Director/Chief Investment Officer (ED/CIO) for the North Dakota Retirement and Investment Office.

Compensation Recommendation
At the March 27, 2015 meeting of the State Investment Board, the Executive Review Committee presented a recommendation of a 5%-7% increase for the ED/CIO position which was approved by the SIB Board.

At the June 22, Executive Review Committee meeting, discussion was held on the 5%-7% salary increase range and it is the recommendation of the Executive Review Committee to offer Mr. David Hunter an increase of 7% for the fiscal year beginning on July 1, 2015. Based on his present salary of $210,000, this would bring his salary to $224,700.

Compensation Rationale
The 7% recommendation is based upon exemplary work as evidenced by the comprehensive formal evaluation approved by the State Investment Board on March 27, 2015, a compensation study of public fund directors, comparison to other staff classification's compensation increase systems, as well as consideration for the fact that Mr. Hunter has received no other compensation increase since his hiring at the North Dakota Retirement and Investment Office. As the State Investment Board members are aware, Mr. Hunter did not receive a probationary increase or an annual increase on July 1, 2014. His salary has remained constant at $210,000 since beginning his position as the ED/CIO of NDRIO on December 2, 2013.

The Executive Review Committee studied both the historical increases of ED/CIOs for NDRIO as well as the McLagan Study of public fund directors dated September 25, 2012. Based upon the McLagan study, the average compensation for an ED/CIO position was $205,000 for the fiscal year beginning on July 1, 2012. When considering a 3% annual increase to that average compensation, which would be $211,150, Mr. Hunter's initial salary of $210,000 was commensurate with average ED/CIOs in the fiscal year beginning on July 1, 2014. Given this same aging of the median salary, however, his present salary would warrant an adjustment to maintain an average compensation amongst his peers. As outlined in the table on page 2 of this memo, aging this study with the same methodology to the fiscal year beginning on July 1, 2015, a comparative salary would be $224,009, which equates to 6.67%.

While the ED/CIO position is not considered a classified position, the Executive Review Committee did analyze the classified state employee's compensation increase process for a comparison. When considering the standard 6-month probationary 5% increase and the annual compensation increase ranges of 2%-4%, the recommended salary for Mr. Hunter is reasonable. As outlined in the table below, even with an annual increase of 2%, Mr. Hunter would have been provided a salary of $229,408 for the fiscal year beginning July 1, 2015. That would increase to $233,928 and $238,492 respectively with a 3% and 4% annual increase comparison.

McLagan Compensation Study (September 25, 2012)	
Median Salary for Year Beginning on July 1, 2012	$205,000
Median Salary for Year Beginning on July 1, 2013 (Aged by 3%)	$211,150
Median Salary for Year Beginning on July 1, 2014 (Aged by 3%)	$217,485
Median Salary for Year Beginning on July 1, 2015 (Aged by 3%)	$224,009
Mr. Hunter's Salary from December 2, 2013 to June 30, 2015	$210,000

State Employee Compensation Model Comparison			
Beginning Salary	Probationary 5%	Annual 2% (July 1, 2014)	Annual 2% (July 1, 2015)
$210,000	$220,500	$224,910	$229,408
Beginning Salary	Probationary 5%	Annual 3% (July 1, 2014)	Annual 3% (July 1, 2015)
$210,000	$220,500	$227,115	$229,320
Beginning Salary	Probationary 5%	Annual 4% (July 1, 2014)	Annual 4% (July 1, 2015)
$210,000	$220,500	$229,320	$238,492

Considering the State Investment Board's approved range of a 5% - 7% increase, it is the consensus of the Executive Review Committee that Mr. Hunter's performance merits the full 7% salary increase to $224,700.

Recommended Action:
Approve a salary increase of 7% to $224,700 for Mr. Hunter beginning on July 1, 2015.