



San Bernardino County Employees' Retirement Association

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Area: Investments
References:
Applicability: SBCERA systemwide

Due Diligence Policy

POLICY NO. 007

Policy

It is the Board's policy to conduct various levels of due diligence to engage investment managers and monitor investments for the purpose of meeting its fiduciary obligations.

Definition

Due Diligence is a broadly based term comprised of many meanings within the institutional investment community. In plain language, it means appropriate oversight. Within a legal sense, it means the degree of care that a prudent person would exercise. At SBCERA, the Board has elevated due diligence with the goal of providing an added level of risk management and oversight. This is done through the use of a multi-pronged approach which is comprised of distinct, but inter-related components, which are carried out over the life of the investment from pre-hire to wind-down.

These components include:

- Investment due diligence,
• Operational due diligence, and
• Legal due diligence and Compliance monitoring.

Investment due diligence differs from on-going portfolio monitoring in key ways. Monitoring meetings are often characterized by a portfolio/manager update or specific topical discussion related to the portfolio/manager; whereas due diligence consists of high-level review of the account as a whole which will include, but is not limited to, a review of the total portfolio and the resources the firm uses to implement the SBCERA mandate. The purpose of the investment due diligence meeting is to build familiarity with the manager, the manager's philosophy, personnel, process and portfolio strategy, performance review/expectations, and provide high-level investment education to the participating Trustees.

Background (The Search Process)

Once a search process is initiated and as part of the selection process, Pre-Hire Investment Due Diligence is conducted at the manager's business location (on-site) to further assess and confirm investment philosophy, strategy and implementation. This is an important step to verify the written documentation provided by the manager during the search process.

Investment Due Diligence

Pre-Hire:

- Conducted by Staff and/or Consultant
• Conducted at Manager's location or remotely
• Assess/confirm investment philosophy, strategy, and implementation
• Verify written documentation provided by manager during search

Post-Hire:

- Conducted by Staff, Consultant, and Trustees (see Brown Act Considerations)

- Conducted remotely, at SBCERA offices, or on-site
- Monitoring and Compliance

Operational Due Diligence

Pre-Hire:

- Conducted by an external, independent accounting and auditing firm, specializing in investment management compliance or audits, or an external, and independent, operational due diligence firm.
- Conducted at Manager's location, remotely, or a combination of the foregoing
- Establishes a baseline and overview of the firm's back office, trading and compliance capabilities
- Determines that proper risk management procedures and internal controls are in place prior to funding a manager (i.e., background investigations as to any formal or informal investigations by financial regulatory authorities, interviews with executives, portfolio managers, compliance, traders, and other staff).
- Assessment of the firm's general attitude and philosophy in regard to openness and compliance.

Post-Hire:

- Conducted remotely or on-site
- On-going visits and remote monitoring procedures to check for changes to programs, personnel, systems and ongoing compliance capabilities.
- Provide a verification of appropriate fees being charged with respect to the account.

Note: Standard operational due diligence reviews may range from one to three days in length, via on-site or remote channels, with follow-up visits at least every four years and periodic remote monitoring in the interim.

Legal Due Diligence and Compliance

Legal (Pre-Hire):

- Contracting process utilizes a team approach implemented by approved external law firms, in conjunction with Chief Counsel and investment staff.
- Review legal, pre-hire questionnaire required from each manager (External counsel)
- Ensure that the contract complies with applicable laws and regulations and that SBCERA is protected from legal risks (Internal and external counsel)
- Ensure the investment strategy purported is congruent in all legal documents; and that managers are held, at a minimum, to professional and fiduciary standards that are both prevalent to the manager's industry and satisfactory to SBCERA. (All)
- Review and confirm fees, hurdle rates, gating provisions, redemption provisions, prohibited transactions or exposures, and key man provisions. (All)
- Business related decisions are negotiated by Investment staff.

Note: The execution of the final negotiated contract is the responsibility of the Chief Executive Officer. The Chief Investment Officer shall then have the authority to execute any and all additional documents necessary to implement the Board's decision to approve the investment.

Compliance (Post-Hire):

- Monitor contracts to ensure that agreed upon terms outlined within the contract are met over the life of the contract. (e.g., Key man provisions, insurance coverage, and assets under management). (Investment staff)
- Monitor for compliance factors (e.g., guideline monitoring, use of leverage, style drift, proxy voting, trade allocations, soft dollar trades, commission recapture, security pricing procedures, account administration, reporting, etc.). (Investment Staff)

Other:

The Board has engaged the services of a third-party provider to monitor securities litigation and track the compliance and performance of the Plan's custodian with regard to this investment related program.

Remote vs. On-site Due Diligence

Monitoring and Compliance consists of two components – both remote and on-site reviews.

Remote strategy reviews consist of in-person, video, or audio teleconferences held at SBCERA offices, or other selected venues, with investment managers on at least an annual basis. More frequent video

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teleconferencing and other forms of communication may be utilized as market conditions or manager-specific issues warrant. Managed Custodial Account (MCA) managers will typically be consulted more often throughout the year. These sessions are an economical and prudent method to ensure staff and the Board stay abreast of manager or strategy-related issues.

On-site or remote investment due diligence is required for all managers, at least once every three years. Typically, managers will be subject to such due diligence every other year. Managers that will not be visited at least once every three years must be approved for exception by the Board. A minimum of one staff member is required at each meeting; consultant support is recommended but not required. The precise manner of conducting investment due diligence shall be decided based upon the following criteria: (1) cost; (2) whether due diligence can be effectively conducted by video conference or other remote means, or whether physical access to the manager's staff and facilities is required; (3) if travel to the manager's facilities is required and the manager is based outside the continental United States, whether due diligence can be effectively conducted by a visit to an office in the continental United States, or whether overseas travel is necessary; (4) the length of time that has passed since due diligence has been conducted for the manager; (5) whether staff, trustees, or consultants are aware of specific concerns regarding the manager; (6) the avoidance of any appearance of waste or impropriety; and (7) other considerations as appropriate.

Note: Chief Investment Officer may defer selected remote or on-site meetings depending upon schedule conflicts or other business considerations.

Responsibility and Frequency

Due Diligence	On-Site	Responsible				Frequency				
		Staff	Trustees	Consultant	External Contractor	Monthly	Annually	Every 3-years	Every 4-years	As Needed
PRE-HIRE										
Investment	X	X		X		Pre-hire Investment due diligence is performed prior to presentation / recommendation to the board. Pre-hire Operational and Legal contracting due diligence are performed after presentation to the board.				
Operational	X**				X					
Legal Contracting		X			X					
MONITORING/COMPLIANCE										
Investment	X	X	X*	X*				X		
Remote Investment		X	X*	X*			X			
Guideline Compliance		X			X	X				
Operational Review	X**	X***			X				X	
Legal Compliance		X			X					X

*Attend meetings as available

**May be conducted remotely as determined by auditor

***Staff provides feedback and additional direction as needed.

Exceptions

On-site and remote due diligence is conducted on all investment managers unless presented to the Board to request an exception to the policy. Exceptions are typically sought primarily when an investment is in a redemption status, also referred to as the investment being in "wind-down".

Brown Act Considerations

For reasons relating to The Brown Act (Government Code §54950-54962) governing meeting access for local public bodies, no more than two (2) Investment Committee members and no more than four (4) total Board members may attend the same scheduled due diligence trip or remote due diligence session, regardless of the number of manager reviews.

Delegation

The Board delegates the development and the implementation of the SBCERA due diligence program as provided in this policy. The Chief Investment Officer is granted authority to approve all travel related to pre-hire, on-site due diligence.

Attachments



Approval Signatures

Step Description	Approver	Date
Investment Committee	Donald Pierce: Chief Investment Officer	pending
Investment Committee	Erin Calicchio: Sr Executive Secretary	pending
Chief Executive Officer Review	Debby Cherney: Chief Executive Officer	9/6/2024
Chief Counsel Review	Barbara Hannah: Chief Counsel	7/9/2024
Investment Services Review	Donald Pierce: Chief Investment Officer	7/2/2024
Investment Services Review	Eydie Cox: Sr Investment Analyst	6/27/2024

Applicability

SBCERA, SBCERA Internal

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