



# INVESTMENT POLICY STATEMENT

## AS OF MAY 2021



## Table of Contents

I.	INTRODUCTION AND STATEMENTS OF PURPOSE, PHILOSOPHY AND ETHICS.....	1
A.	Legal Authority and System Description.....	1
B.	Statement of Purpose .....	2
C.	Statement of Investment Philosophy .....	3
D.	Statement of Ethical Standards .....	4
II.	STATEMENT OF DUTIES AND RESPONSIBILITIES.....	5
A.	Board of Trustees.....	5
B.	Staff.....	5
C.	Investment Consultant .....	6
D.	Investment Managers.....	7
E.	Custodian .....	8
F.	Securities Lending Agent.....	9
G.	Transition Manager.....	10
III.	PROCEDURES .....	11
A.	Investment Policy Review .....	11
B.	Investment Manager Policy Exceptions .....	11
C.	Third Party Marketing and Referrals Disclosure Policy.....	11
D.	Request for Proposal Policy.....	12
E.	Additional allocations to a previously retained manager: .....	13
IV.	INVESTMENT GOALS AND OBJECTIVES .....	14
V.	INVESTMENT GUIDELINES AND CONSTRAINTS.....	15
A.	Public Market Separate Account Investments .....	15
B.	Private Market Partnership Interests and Commingled Account Investments .....	19
VI.	EVALUATION AND REVIEW .....	23
A.	Investment Staff Reporting Requirements.....	23
B.	Investment Consultant Reporting Requirements .....	23
C.	Investment Manager Reporting Requirements .....	23
	APPENDIX A - PERFORMANCE BENCHMARKS .....	25
	APPENDIX B - STRATEGIC ASSET ALLOCATION .....	26
	APPENDIX C - REBALANCING POLICY.....	27
	APPENDIX D - INVESTMENT MANAGER EXCEPTIONS TO INVESTMENT GUIDELINES .....	29

## **I. INTRODUCTION AND STATEMENTS OF PURPOSE, PHILOSOPHY AND ETHICS**

The Board of Trustees of the Teachers' Retirement System of Oklahoma, as the governing body for the System, deems it prudent and necessary to maintain this Investment Policy Statement to act as the principal governing document for the investment of System assets.

### **A. Legal Authority and System Description**

The System is established by statute; the legal authority and description of the System are detailed below.

#### Constitutional Authority

Section 62 of Article 5 of the Oklahoma Constitution was added as a result of the passage of State Question 306 on July 14, 1942. This section reads:

“The Legislature may enact laws to provide for the retirement for meritorious service of teachers and other employees in the public schools, colleges and universities in this State supported wholly or in part by public funds, and may provide for payments to be made and accumulated from public funds, either of the State or of the several school districts. Payments from public funds shall be made in conformity to equality and uniformity within the same classifications according to duration of service and remuneration received during such service.”

#### Statutory Authority

As a result of the passage of State Question 306, the Legislature enacted House Bill 297 in the 1943 legislative session that created the Oklahoma Teachers Retirement System (“System”). The legislation has been changed substantially in the years since its creation and is currently codified in Oklahoma Statutes Title 70, Sections 17-101 et. seq. (NOTE: In the remainder of this document, statutory references will follow the notation O.S. 70 § 17-101 to reference Oklahoma Statutes Title 70, Section 17-101.)

#### Purpose of System

In O.S. 70 § 17-102, paragraph 1 creates the Oklahoma Teachers Retirement System and outlines the purpose of the System as follows:

“A retirement system is hereby established and placed under the management of the Board of Trustees for the purpose of providing retirement allowances and other benefits under the provisions of this act for teachers of the State of Oklahoma.”

#### Board of Trustees Powers

The second paragraph of O.S. 70 § 17-102 provides the broad terms of the powers entrusted to the Board of Trustees (“Board”):

“The Board of Trustees shall have the power and privileges of a corporation and shall be known as the "Board of Trustees of the Teachers' Retirement System of Oklahoma", and by such name all of its business shall be

transacted, all of its funds invested, and all of its cash and securities and other property held in trust for the purpose for which received.”

Further powers vested upon the Board are set forth in O.S. 70 § 17-106, in part:

“(1) The general administration and responsibility for the proper operation of the retirement system and for making effective the provisions of the act are hereby vested in a Board of Trustees which shall be known as the Board of Trustees and shall be organized immediately after a majority of the trustees provided for in this section shall have qualified and taken the oath of office.”

and:

“(9) Subject to the limitations of this act, the Board of Trustees shall, from time to time, establish rules and regulations for the administration of the funds created by this act and for the transaction of its business.

Finally, O.S. 70 § 17-106.1, in part, defines the duties of the Board in relation to investment of fund assets:

“A. The Board of Trustees of the Teachers’ Retirement System of Oklahoma shall discharge their duties with respect to the System solely in the interest of the participants and beneficiaries and:

1. For the exclusive purpose of:

- a. providing benefits to participants and their beneficiaries, and
- b. defraying reasonable expenses of administering the System;

2. With the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims;

3. By diversifying the investments of the System so as to minimize the risk of large losses, unless under the circumstances it is clearly prudent not to do so; and

4. In accordance with the laws, documents and instruments governing the System.”

## **B. Statement of Purpose**

A primary purpose of this investment policy statement is to guide fiduciaries, including the Board of Trustees, System staff, investment managers, consultants and others responsible for overseeing and investing the assets of the Fund. This policy also communicates foundational tenets underlying its formulation. This policy provides specific guidance regarding investment objectives, asset allocation, risk management and the means by which investment objectives are intended to be achieved. Additional specific guidance is given in defining roles, delegated duties and accountabilities of System fiduciaries as well as setting forth logical, disciplined procedures for making decisions.

### C. **Statement of Investment Philosophy**

Since this policy is a communication tool for System fiduciaries, interested stakeholders as well as other external parties, the Board recognizes that it is important to articulate the underlying beliefs that are foundational in its formulation. Key aspects of the Board's investment philosophy are summarized in the following statements.

1. The Fund has an infinite time horizon and the assets should be invested and managed accordingly.
2. A central tenet in investing is the tradeoff between risk and return, meaning that the pursuit of higher expected returns is accompanied with higher expected risk. Bearing some degree of investment risk is necessary in the pursuit of investment return objectives.
3. Investment risk comes in many forms. The most common risk is the volatility of periodic returns measured by the statistical term known as standard deviation. Additionally, there are a variety of other risks to be considered. A partial list of these risks would include the risk of permanent loss of capital, the risk of not meeting objectives, illiquidity risk, credit risk, interest rate risk, inflation risk, leverage risk, concentration risk and manager risk. A primary focus of this investment policy is to balance, manage and, to the extent possible, control these various risks.
4. Funds with long term investment horizons are able to pursue higher expected returns associated with higher risk portfolios because they are able to remain invested when periodic declines in market values occur.
5. The Fund will best contribute to the primary goal of providing benefits to participants and their beneficiaries by realizing high risk-adjusted net returns.
6. The Board acknowledges that while other institutions may make investment decisions to pursue various worthy causes that may be admirable in their own right, the Board's investment decisions are made to achieve the primary goal of providing benefits to participants and their beneficiaries and defraying reasonable expenses.
7. Long-term investing success is best accomplished by adhering to a long-term strategic asset allocation rather than engaging in short term tactical market timing among asset classes.
8. Diversification among asset classes and securities is the primary means of controlling the risk of an investment portfolio.
9. The primary factor determining portfolio risk and return is how the portfolio is allocated among asset classes.
10. The decision-making process for investments should be both disciplined and logical deriving support from current academic theory and the application of rigorous analysis.
11. In less efficient markets where the probabilities of achieving net-of-fee outperformance relative to a passive market index are higher, active management is preferred. In more efficient markets where the probabilities of achieving net-of-fee outperformance relative to a passive market index are lower, low-cost index management is preferred.

12. Certain asset classes are only accessible in the form of private market interests which have very limited liquidity and normally higher costs relative to public market instruments. Investing a portion of the Fund in these illiquid asset classes is reasonable to the extent that they offer some desirable combination of the following relative to available public market asset classes: higher expected net return and/or risk reduction through diversification.

**D. Statement of Ethical Standards**

The Board of Trustees is committed to maintaining and promoting the highest ethical standards among Board members and among all parties involved in the administration of fund assets.

The Board expects all parties involved in the administration of fund assets, including all System fiduciaries, to conduct their activities according to the highest ethical standards adhering likewise to the principles expressed in the Board of Trustee Policy Manual Chapter 5 – Code of Conduct and Chapter 6 – Ethical and Fiduciary Conduct. Given the nature of fund management and investing, particular attention will be given to conflicts of interest. All parties involved in the administration of fund assets should be free of conflicts of interest to avoid even the appearance of not acting in the sole interests of System participants and their beneficiaries. Where any involved party becomes aware of an actual or potential conflict of interest it is their duty to disclose the conflict to the Board so that the Board may assess its seriousness.

## **II. STATEMENT OF DUTIES AND RESPONSIBILITIES**

### **A. Board of Trustees**

The Board of Trustees has the final decision-making authority for the System. The Investment Committee of the Board has the authority to make investment recommendations to the Board. The Board evaluates and decides whether or not to take action on recommendations from the Investment Committee. The Investment Committee's authority and responsibilities are set forth in the Investment Committee Charter contained in the Board of Trustees Policy Manual.

Trustee duties and responsibilities are listed in summary as follows:

1. Adopt, and when deemed necessary, amend this Investment Policy Statement.
2. Determine delegated duties to be performed by other qualified fiduciaries in order to ensure that the Fund is properly administered and regularly evaluated to assess progress towards achieving established objectives.
3. Receive and evaluate reports, presentations and other materials provided by investment consultant(s), staff, investment managers, and other retained advisors to monitor the administration of Fund assets in accordance with policy objectives and to regularly assess progress towards achieving the goals and objectives defined herein.
4. Select and contract with qualified professional advisory organizations to perform functions deemed necessary by the Board to manage the Fund in accordance with policy. Common professional advisory organizations would include investment consultant(s), investment managers, global custodians and securities lending agents.
5. Evaluating the performance of retained professional advisory organizations and staff to assess fulfillment of duties, achievement of goals and compliance with policy guidelines.
6. Annually conduct a formal review of the performance of Investment Consultant(s), normally to be performed in the month of April.
7. Terminating the contracts with any retained professional advisory organization when deemed necessary.
8. Review all costs of investment operations at least annually.

### **B. Investment Staff**

A summary of the duties and responsibilities of the Investment Staff is as follows:

1. Provide the Board and the Investment Committee with reports, presentations and any other materials to assist them in the fulfillment of their duties and responsibilities. The general content and focus of reporting from Investment Staff is further described in Section VI.
2. Serve as the primary liaison between the Board of Trustees and the investment consultant(s), investment managers, custodian, securities lending agent and transition manager(s).

3. Implement Board decisions regarding asset allocation, investment structure, portfolio rebalancing procedures and retention of investment consultant(s), investment managers, custodian and securities lending agent.
4. Coordinate the search, selection and evaluation processes for investment consultant(s), investment managers, custodian and securities lending agent on behalf of the Board of Trustees.
5. Monitor and review the performance of the total fund, asset class composites, and investment managers to evaluate achievement of objectives and compliance with policy guidelines.
6. Monitor and review all costs of investment operations including, but not limited to, fees paid to investment consultant(s), investment managers, and custodian, as well as portfolio transactions costs.
7. Manage the liquidity in the Total Portfolio as necessary to ensure timely payment of benefit payments, plan expenses and capital calls, etc. consistent with established asset allocation and portfolio rebalancing policies. The raising of cash amounts greater than two months' worth of benefit payments shall be subject to Board approval.
8. Conduct the search and selection of transition manager(s) in collaboration with the investment consultant(s) as directed by the Board.
9. Conduct due diligence in collaboration with the investment consultant(s) when investment managers fail to meet the expectations of the Board or are formally placed 'On Alert' or 'On Notice'.
10. Research and review innovative investment ideas and concepts in collaboration with the investment consultant(s) in an effort to identify potential modifications to improve the investment portfolio.
11. Monitor the performance of the total fund, asset class composites and investment managers to determine if any issues need to be addressed by the Investment Committee or the Board of Trustees.

**C. Investment Consultant**

A summary of the duties and responsibilities of the investment consultant(s) retained by the Board is as follows:

1. Acknowledge status as a fiduciary to the System and remain in compliance both with this investment policy and with the current executed contract with the System.
2. Provide the Board and the Investment Committee with reports, presentations and any other materials to assist them in the fulfillment of their duties and responsibilities. The general content and focus of reporting from Investment Consultant is further described in Section VI.

3. Assist the Board in developing and modifying policy objectives and guidelines, including the development of asset allocation strategies, recommendations on long-term asset allocation and the appropriate mix of investment manager styles and strategies.
4. Assist the Board by monitoring compliance with this Investment Policy.
5. Provide assistance in investment performance evaluation, and analysis.
6. Provide assistance in investment manager searches and selection.
7. Provide timely information, written and/or oral, on investment strategies, instruments, managers and other related issues, as requested by the Board.
8. Monitor the System's investment managers and notify the Board and Investment staff of any material changes in the investment managers' organizational structure, their personnel or if there are performance issues.
9. Certify in writing to the Board on an annual basis as of the System's June 30 fiscal year end, the investment consultant's compliance with this Policy during the fiscal year period ending June 30.
10. Review with the Investment Staff the status and performance of current investment managers and determine if any issues need to be addressed by the Investment Staff or the Board of Trustees.
11. Provide assistance in the search and selection of transition manager(s) as directed by the Board.
12. Provide assistance in the conduct of due diligence when investment managers fail to meet the expectations of the Board or are placed 'On Alert' or 'On Notice'.
13. Explore, research, analyze and review new investment ideas and managers in collaboration with the Investment Staff in an effort to keep the system current with investment options.

**D. Investment Managers**

A summary of the duties and responsibilities of each separate account, public markets investment manager retained by the Board is listed below. Commingled account and private market investment managers whose investment activities are governed by subscription agreements or commingled trust documents should adhere to the duties and responsibilities contained herein to the extent possible and to the extent that they are not superseded by, or in conflict with, subscription agreements or commingled trust documents defining the relationship with the System.

1. Acknowledge status as a fiduciary to the System and remain in compliance both with this investment policy and with the current executed contract with the System.
2. Provide the Board, the Investment Committee, the staff and the investment consultant(s) with reports, presentations and any other materials to assist them in the fulfillment of their

duties and responsibilities. The general content and focus of reporting from Investment Managers is further described in Section VI.

3. Manage the Fund's assets in accordance with the policy guidelines and objectives expressed herein.
4. Prudently select investments based on thorough evaluation of all risks applicable to stated mandate.
5. Work with the custodian and the investment consultant to verify monthly accounting and performance reports.
6. Certify in writing to the Board on an annual basis as of the System's June 30 fiscal year end, the Investment Manager's compliance with this Policy during the fiscal year period ending June 30.
7. Act as a fiduciary in adopting and adhering to proxy voting policies, acknowledging that its proxy voting policies may affect the value of their respective portfolio.
8. Seek to obtain best execution in all securities transactions to minimize the costs of trading.

#### **E. Custodian**

A summary of the duties and responsibilities of the custodian bank(s) retained by the System is as follows:

1. Acknowledge status as a fiduciary to the System and remain in compliance both with this investment policy and with the current executed contract with the System.
2. Provide the Board, the Investment Committee, the staff and the investment consultant(s) with reports, presentations and any other materials to assist them in the fulfillment of their duties and responsibilities.
3. Accept daily instructions from designated staff.
4. Notify investment managers of proxies, tenders, rights, fractional shares or other dispositions of holdings.
5. Safekeeping of securities.
6. Timely collection of interest and dividends.
7. Daily cash sweep of idle principal and income cash balances.
8. Process and maintain records of all investment manager transactions.
9. Collect proceeds from maturing securities.
10. Disburse all income or principal cash balances as directed.

11. Perform regular reconciliations of holdings and transactions with the System's retained investment managers on at least a monthly basis.
12. Work with the System's staff and the investment consultant to ensure accuracy in reporting.
13. Manage and administer the System's directed brokerage program.
14. Calculate the investment performance of the System's investment accounts and composites.
15. Providing required reports to assist the System's staff and vendors with compliance with the Governmental Accounting Standards Board, the Internal Revenue Service, the Securities and Exchange Commission, the Financial Industry Regulatory Authority and other regulatory agencies.
16. Monitor, file and report on securities class action lawsuits and collect and record settlement proceeds.
17. Process and file Foreign Tax Reclaims on behalf of the System.

**F. Securities Lending Agent**

A summary of the duties and responsibilities of the securities lending agent retained by the System is as follows:

1. Acknowledge status as a fiduciary to the System and remain in compliance both with this investment policy and with the current executed contract with the System.
2. Provide the Board, the Investment Committee, the staff and the investment consultant(s) with reports, presentations and any other materials to assist them in the fulfillment of their duties and responsibilities.
3. Arrange terms and conditions of securities loans.
4. Monitor the market value of the securities lent and mark to market at least daily and ensure that any necessary calls for additional collateral are made and that such collateral is obtained on a timely basis.
5. Direct the investment of cash received as collateral in accordance with direction from the Board, provided that such investments are consistent with guidelines provided in this document.
6. Notify the Board of any changes to the investment guidelines in the Securities and Exchange Commission's rule 2A7 for consideration by the Board.
7. Notify the System's staff in the event that a recalled security has not been returned by a borrowing party within 10 days of the request.

## **G. Transition Manager**

The transition managers shall manage the transition of assets from one or more investment managers or asset categories to one or more other investment managers or asset categories. Transition managers shall be selected among those approved by the Board. Transition managers shall be utilized when such employment is likely to present significant opportunities for cost savings, technical efficiencies or other benefits to the System.

A summary of the duties and responsibilities of Transition Managers retained by the System is as follows:

1. Acknowledge status as a fiduciary to the System and remain in compliance both with this investment policy and with the current executed contract with the System.
2. Provide a pre-trade analysis, which will include, among other things, a trading liquidity analysis, portfolio sector analysis, volatility analysis, and estimated transaction costs.
3. Provide a detailed written plan of transition execution.
4. Provide a post-trade analysis, comparing the actual costs with the pre-trade estimates. The report will also include various trading statistics, benchmarking information, and detailed trade reports.
5. In all securities transactions, transition managers shall seek to obtain best execution to minimize the costs of trading.

### **III. PROCEDURES**

#### **A. Investment Policy Review**

In order to keep the Investment Policy current the Board will, at least annually, review and modify as deemed necessary any portions of the policy. The annual review will consider, but not be limited to, the following: objectives and guidelines, the development of asset allocation strategies, recommendations on long-term asset allocation and the appropriate mix of investment manager styles and strategies.

The Board, both upon their own initiative and upon consideration of the advice and recommendations of staff, consultants, the investment managers and other fund professionals involved with the assets, may amend policy guidelines. Proposed modifications should be documented in writing to the Board.

#### **B. Investment Manager Policy Exceptions**

Requests for an exception to invest in securities precluded by section V. A. or the applicable mandate's specific policies, should be submitted in writing to the System and include justification for such request, , and a requested time period, up to three years. Exception requests will undergo a reevaluation and approval process at the end of each term. Staff and investment consultant will determine the investment manager's process for providing quarterly reporting on attribution analysis of the contribution of the allowed exception.

#### **C. Third Party Marketing and Referrals Disclosure Policy**

The Teachers' Retirement System of Oklahoma requires transparency and full disclosure of all relationships in proposed and committed investments with any third parties. A "third party marketer" is a person who represents an asset management firm or any other type of investment services provider, as an independent contractor rather than as an employee of the firm, for the purpose of making presentations or securing contracts with the System for the firm or provider. Any such third-party marketer must disclose himself or herself as a third-party marketer before or at the same time as contacting any member of the Board of Trustees, employee of the System or the outside investment consultant for the System. In addition, firms submitting investment proposals for consideration by Teachers' Retirement System of Oklahoma (including any sub-managers or consultants engaged by such firms) are hereby required to disclose the identity of all third-party marketers and/or individuals by whom the firm has been referred to Teachers' Retirement System of Oklahoma and further indicate those so identified that stand to receive fees or other consideration in the event that a contract between the firm and the Teachers' Retirement System of Oklahoma is secured. Any consideration paid or benefits received, or any relationship between such firm (including any sub-managers or consultants engaged by such firms) and third-party marketing entities and/or individuals, shall be disclosed. The disclosure requirements established by this Policy apply throughout the term of any contractual relationship Teachers' Retirement System of Oklahoma may have with any firm and represents a continuing obligation of disclosure. This Policy becomes effective immediately and applies to all firms currently managing Teachers' Retirement System of Oklahoma assets. All firms submitting investment proposals must

make the disclosures required by this Policy prior to any action being taken on the firm's investment proposal by the Board, as well as comply with the continuing obligation of disclosure.

#### **D. Request for Proposal Policy**

70 O.S. § 17-106.1(E) provides “The Board of Trustees may retain qualified investment managers to provide for the investment of the monies of the System. The investment managers shall be chosen by a solicitation of proposals on a competitive bid basis pursuant to standards set by the Board of Trustees. Subject to the overall investment guidelines set by the Board of Trustees, the investment managers shall have full discretion in the management of those monies of the System allocated to the investment managers[...].”

While TRS statutes provide that investment managers must be retained on a competitive bid basis, this process is not required to conform to the Oklahoma Central Purchasing Act. The process for investment manager selection and allocation shall conform to the following process:

1. The Board shall approve all request for proposals (RFPs) issued by the System.
2. Respondents to a proposal shall comply with the procedures and conform to the standards set forth in the RFP.
3. The issuance of an RFP does not commit the Board to award a contract or make an allocation to a manager or strategy. The Board reserves the right to accept or reject any or all proposals received, to negotiate with any and all qualified bidders, and to cancel in part or in its entirety a solicitation if it is in the best interests of the System to do so.
4. The Board shall award contracts to the most suitable bidder at a specified time and place which shall be open to the public pursuant to the Oklahoma Open Meetings Act.
5. Proposals shall be evaluated by the Investment Consultant and the Investment Staff. An evaluation report to identify potential managers shall be presented to the Investment Committee for recommendation to the Board.
6. Except for the purposes of seeking clarification of RFP responses, no member of the Board, staff, or Investment Consultant shall knowingly communicate concerning any matter that is material to the selection process with any party having a direct financial interest in the award of the contract, an officer or employee of that party, or a placement agent retained or employed by that party, unless the communication is part of the process expressly described in the RFP or part of any Board meeting prior to the award of the contract. Any bidder who knowingly participates in a communication that is prohibited by this subsection shall be disqualified from the contract award.
7. Due diligence shall be conducted on potential managers prior to the award of the contract. The nature of the due diligence shall be recommended to the Board by the Investment Committee with the advice of the Investment Consultant, Chief Investment Officer, and Executive Director.

**E. Additional allocations to a previously retained manager:**

1. The Board may at any time make an additional allocation to a manager currently under contract at its discretion in accordance with this Policy.
2. Additional allocations to subsequent or follow-on closed-end funds of a manager may be made without the necessity of an additional RFP provided the investment thesis and strategy of the subsequent or follow-on fund is substantially similar to the fund that was originally allocated on a competitive bid basis. To be substantially similar a fund must have the same benchmark, the same type of assets, and the investment decisions must be made by substantially the same people as were managing the original fund/strategy. Closed-end funds are generally in the form of ownership interests in limited partnerships and may include, but are not limited to, private equity, venture capital, mezzanine and distressed debt, real estate funds, and natural resource funds.

#### **IV. INVESTMENT GOALS AND OBJECTIVES**

To fulfill the System's Mission Statement set forth in Chapter 2 of the Board of Trustees Policy Manual, the Board has a goal of earning a nominal, long-term, time-weighted, annualized, net total return of 7.5% on the investment portfolio while maintaining liquidity necessary to fund net benefits and operations.

To achieve the goal above the Board believes that several investment objectives need to be attained. In setting the objectives the Board follows the criteria as recommended in "A Primer for Investment Trustees" (Bailey, Jeffery, Jesse Phillips and Thomas Richards. *A Primer for Investment Trustees*. Charlottesville: Research Foundation of CFA Institute, 2011).

Specifically, investment objectives should be

- unambiguous and measurable,
- specified in advance,
- actionable and attainable,
- reflective of the Trustees' risk tolerance and consistent with the System's mission.

The Board has established several objectives for the investment portfolio that meet the criteria above. These objectives listed below are specified at the Total Fund, Asset Class Composite and individual mandate/Investment Account level.

##### **Total Fund Investment Objectives**

- Achieve or exceed on a three-year rolling basis, absolute and risk-adjusted, net excess returns relative to the Total Fund Policy Index as specified in Appendix A.
- On a three-year rolling basis, maintain relative risk levels equal to or below that of the Total Fund Policy Index.

##### **Asset Class Investment Objectives**

- Achieve or exceed on a three-year rolling basis, absolute and risk-adjusted, net excess returns relative to the Asset Class Index as specified in Appendix A.
- On a three-year rolling basis, maintain relative risk levels equal to or below that of the Asset Class Index.

##### **Investment Account Objectives**

- Achieve or exceed on a three-year rolling basis, absolute and risk-adjusted, net excess returns relative to the Investment Account Index as specified in Appendix A.
- On a three-year rolling basis, maintain relative risk levels equal to or below that of the Investment Account Index.

## **V. INVESTMENT GUIDELINES AND CONSTRAINTS**

The System maintains a diversified portfolio with investments in multiple asset classes as defined by its strategic asset allocation. Investments in some asset classes can be made through public securities markets while investments in other asset classes are only possible through private market investment vehicles.

Generally, the System's public market investments are held by the System's Custodian in separate accounts managed by retained investment management firms. For these public market investments in separate accounts at the System's custody bank, the System defines the parameters within which the retained investment managers can manage the portfolio. In addition to public market investments held in separate accounts the System may choose to invest in commingled or partnership structures alongside other institutional investors where the System does not define the investment management parameters but rather accepts the investment management parameters as specified in commingled trust documents or in partnership agreements.

With the above distinctions in mind, this section of the Policy covering guidelines and constraints is divided into two subsections and further grouped by asset class. The first subsection addresses public market investments held in separate accounts by the System's Custodian. It communicates to the investment management firms retained to manage these accounts the parameters within which they are permitted to manage the portfolio.

The second subsection addresses commingled and private market investments where the System accepts the investment parameters as defined in trust documents or partnership agreements and other associated legal documents. This subsection documents the rationale for choosing a commingled or partnership structure and the general boundaries within which the System will seek to structure its private markets investments.

### **A. Public Market Separate Account Investments**

#### **1. Discretion and Prohibited Investments**

Full discretion, within the parameters of these guidelines is granted to the investment managers regarding the allocation of their portfolios, the selection of securities, and the timing of transactions. Any exception requests to the guidelines listed herein should be communicated to the System's Investment staff and Investment Consultant. Due to the ever-expanding variety of financial instruments and financial engineering methods, the following list of ineligible investments is not considered to be exhaustive. Any instrument, to which these Investment Guidelines do not explicitly prohibit, that is not expressly allowed by the applicable mandate specific guidelines, should be requested through the exception process, detailed in section III. B, prior to investment.

- a. Privately placed or other non-marketable debt, except securities issued under Rule 144A.
- b. Securities denominated in non-US currency, unless provided in accordance with an applicable mandate.

- c. Lettered, legend or other so-called restricted stock
- d. Physical commodities and commodity derivatives
- e. Short sales and purchases on margin; leverage is not allowed unless the System has expressly given the right to lever to a manager.
- f. Direct investments in private placements, real estate, oil and gas and venture capital, unless provided in accordance with an applicable mandate.

## **2. Index Portfolios**

- a. All index portfolios characteristics and returns are expected to closely resemble the designated benchmark.
- b. Index managers may use both full replication and stratified sampling portfolio construction methodologies.

## **3. Cash Rule for Equity Portfolios**

- a. Investment managers of portfolios consisting of equity securities should seek to remain fully invested. Fully invested for the purposes of this document shall mean normally maintaining a portfolio allocation to cash investments of 5% or less. Should the investment manager desire to maintain cash investments at a level greater than 5% for an extended period of time, the investment manager shall provide advanced written notification and explanation to the Investment Staff and Investment Consultant.
- b. No violation shall be deemed to occur if cash investment levels exceed the 5% due to instructions received from the System. If cash investments breach the 5% threshold for ten consecutive business days or 7% for three consecutive business days, the manager shall submit a written notice and explanation of each such event to Investment Staff and Investment Consultant.

## **4. Derivatives**

- a. Investment managers may be permitted, under the terms of individual investment contracts, to use derivative instruments as set forth in each manager's investment guidelines. A derivative is a security or contractual agreement that derives its value from some underlying security, commodity, currency or index. Some examples of derivatives for purposes of this Policy are (a) contracts such as forwards, futures, put and call options, and swaps and (b) non-traditional securities with embedded options such as collateralized mortgage obligations (CMOs) and structured note products. Traditional securities with options such as convertible bonds and preferred stock are not considered derivatives under this policy, nor are warrants.
- b. Derivatives shall not be used to introduce leverage, that is, the notional value of derivatives positions cannot exceed the cash or securities values available from the System's assets. Derivatives may not be used to create levered exposure to the assets

being managed. Derivatives may be used for the purpose of reducing effective cash exposure and for hedging currency risk and interest rate risk.

- c. Managers must ascertain and carefully monitor the creditworthiness of any third parties involved in derivative transactions.
- d. Foreign exchange forward contracts or currency swaps are permitted for currency hedging purposes. Posting of a “margin” deposit for these contracts is permitted in connection with foreign exchange forward contracts or currency swaps as such a deposit is not considered to be “purchases on margin” or “leverage”.

## **5. Domestic Equity**

- a. Domestic Equity portfolios will not concentrate more than the greater of a 2% benchmark-relative active weight or 7% of market value of funds under advisement in holdings of a single issuer.
- b. Domestic Equity portfolios will not hold greater than 5% of the outstanding shares of a single issuer.
- c. Domestic Equity portfolios will be limited to holdings of common stock, American Depository Receipts (ADRs) listed on a domestic exchange, non-midstream MLP units and any security type that is a constituent in the portfolio’s benchmark index.
- d. Domestic Equity portfolios may hold, sell or exercise rights, warrants or other instruments received by virtue of corporate actions.
- e. Domestic Equity portfolios may purchase unlevered Exchange Traded Funds (ETFs) linked to the portfolio’s benchmark index solely for the purpose of reducing temporarily high cash exposure.

## **6. International Equity**

- a. International Equity portfolios will not concentrate more than the greater of a 2% benchmark-relative active weight or 7% of market value of funds under advisement in holdings of a single issuer.
- b. International Equity portfolios will not hold greater than 5% of the outstanding shares of a single issuer.
- c. International Equity portfolios will not concentrate more than the greater of a 5% benchmark-relative active weight or 35% of the market value of funds under advisement in issuers from the UK or Japan and no more than 30% of the market value of funds under advisement in issuers from any other single country.
- d. International Equity portfolios will invest no less than 50% of the portfolio in companies located in developed markets as determined by MSCI.

- e. International Equity portfolios will be limited to holdings of common stock, American Depository Receipts (ADRs) listed on a domestic exchange and any other security type that is a constituent in the portfolio's benchmark index.
- f. International Equity portfolios may hold, sell or exercise rights, warrants or other instruments received by virtue of corporate actions.
- g. International Equity portfolios may purchase unlevered Exchange Traded Funds (ETFs) linked to the portfolio's benchmark index or country sub index solely for the purpose of reducing temporarily high cash exposure. International Equity portfolios may also hold commingled fund units to gain exposure to markets where individual company share purchases are either inefficient or not possible.

## **7. Fixed Income**

- a. Fixed Income portfolios will not concentrate greater than 5% of market value of funds under advisement in holdings of a single issuer. This restriction does not apply to sovereign issues.
- b. Fixed Income portfolios will not hold greater than 5% of the issued securities of a single issuer.
- c. Fixed Income portfolios will not concentrate greater than 20% in non-USD denominated obligations.
- d. Fixed Income portfolios will not concentrate greater than 10% in developing or emerging markets issuers as determined by MSCI.
- e. Fixed Income portfolios may hold shares of common stock converted from embedded corporate actions. At the time of conversion, managers should communicate issues converted into common shares to the System's Investment staff and Investment Consultant.
- f. **Core Plus Full Discretion Fixed Income**
  - i. Core Plus portfolios will not concentrate greater than 50% in issues which are rated Ba1 or lower by Moody's, or Moody's equivalent rating by an SEC registered NRSRO. If the ratings assigned to an instrument by an SEC registered NRSRO are not the same, the highest rating of these rating agencies will be used. If an instrument is not rated by an SEC registered NRSRO, the equivalent rating determined by the Manager's internal rating system will be used.
  - ii. Core Plus portfolios may hold up to 5% of the market value of the account in any combination of the following: issues which internally or externally are rated below Caa2 Moody's, or Moody's equivalent rating by an SEC registered NRSRO, common stock, preferred stock, closed-end funds or exchange-traded funds..

- iii. All holdings of unrated securities and securities subject to the 5% limitation above shall be subject to monthly reporting requirements as set forth in Section VI. 3. of this Policy.
- iv. The Core Plus portfolio manager may not invest more than 10% of the portfolio in unrated securities.

**g. Active Duration Fixed Income**

- i. Active duration portfolios may concentrate holdings up to 100% at any maturity along the U.S. Treasury term structure.
- ii. Active duration portfolio accounts are limited to holding securities backed by the full faith and credit of the U.S. government and units of the short-term investment fund of the System's custodial bank.

**h. Securities Lending Collateral Pool**

- i. The investments of the securities lending collateral are governed by a separate investment policy document therefore they are not addressed herein.

**B. Private Market Partnership Interests and Commingled Account Investments**

The System recognizes that private market investments and commingled fund investments are governed by subscription agreements, limited partnership agreements, trust documents and other related legal documents. Additionally, the System recognizes that in the event of a conflict between the aforementioned documents and this Investment Policy Statement, the subscription agreements, limited partnership agreement and other related legal documents shall take precedence in the governance of these investments.

The System determines how it will select and structure its private market and commingled fund investments this section sets forth the guidelines the System will follow for structuring the portion of the portfolio invested in private market and commingled fund investments.

**1. Private Equity and Private Debt**

- a. Private Equity portfolios will be comprised of buyout funds, growth capital funds, turnaround funds venture capital funds and other primarily equity focused strategies approved by the System.
- b. Private Debt will be comprised of distressed debt funds, mezzanine debt funds, as various types of credit funds and other primarily debt focused strategies approved by the System.
- c. For Strategic Asset Allocation purposes, the System regards Private Equity as an asset class and Private Debt as a sub-category of the Private Equity asset class.

- d. In order to achieve a diversified private equity portfolio, the following sub-allocations shall be used as an overall target for commitment levels within the portfolio:

<u>Segment</u>	<u>Long-Term Allocation Ranges</u>
Corporate Finance <sup>1</sup>	80% - 100%
Venture Capital	0% - 20%

<sup>1</sup> Includes buyout, turnaround and debt related strategies

<u>Region</u>	<u>Long-Term Allocation Ranges</u>
U.S. and Western Europe	80% - 100%
Other	0% - 20%

- e. The minimum Private Equity or Private Debt commitment is \$10 million.
- f. Commitments will not be made to a primary fund which exceeds an amount equal to 20% of the total amount raised for a proposed fund. For the purposes of this provision, primary fund is defined as a private partnership formed by a fund manager to invest in underlying operating companies and does not include fund of fund, secondary or co-investment vehicles.
- g. Aggregate commitments to a General Partner may not be greater than 25% of funds under advisement.
- h. For new commitments identified by a retained private markets consulting firm, the private markets consulting firm shall provide detailed information on the opportunity, including a final memorandum summarizing all due diligence performed, to the Staff, and the Investment Consultant.
- i. The System will not invest funds into opportunities that intend to purchase remaining assets from a previous fund.
- j. Funds that meet the following criteria will not be considered eligible for initial evaluation or potential funding commitments:
- i. Vehicles which are not backed by accredited investors, as that term is defined in Section 2 of the Federal Securities Act of 1933, as amended, (15 U.S.C. Section 77(b)) and rules and regulations promulgated under that section.
  - ii. Investments representing direct equity ownership in individual companies or other business entities, without the benefit of an intermediate partnership or other indirect ownership structure. However, this exception shall not include direct equity ownership which results from the distribution of securities from partnerships to the System. This rule does not restrict the possibility of a co-investment in Private Equity; contingent upon a third-party consultant providing the recommendation and vehicle for investment.
  - iii. Investments which would violate resolutions passed by the System's Board.

- iv. Investments in which the General Partner has committed to invest no personal or firm assets.

## **2. Real Estate**

- a. Real estate investments will be categorized as Core and Non-Core. The objectives of real estate investments are to provide diversification benefits to the overall portfolio, provide protection against inflation, generate stable income, produce attractive risk-adjusted return and preserve capital.
- b. Real estate exposure shall be acquired primarily through comingled fund vehicles, both open end and closed end, and, to a lesser extent, joint venture limited partnerships and separate accounts.
- c. The real estate portfolio will be diversified by property type, geographic region and investment strategy.
- d. Real estate funds will not concentrate, in any single property, an amount exceeding 25% of the total Gross Asset Value (GAV) of the overall investment fund.
- e. Core real estate funds will include investments that are operating and substantially leased, primarily invested in the four main property types including office, industrial, retail and multi-family. Other property types may be included to a lesser extent. Current income will comprise a majority of the total return over an investment cycle.
- f. Core real estate funds will not concentrate greater than 20% of the total GAV of the investment fund in Non-Core properties.
- g. Core real estate funds will not carry leverage in excess of 35% of the GAV of the investment fund.
- h. Non-Core real estate funds will include Value-add and Opportunistic investment strategies. Non-core funds may purchase and manage, in addition to the four main property types, other specialty properties that may require renovation, rehabilitation or development. Current income may comprise a minority and appreciation may represent the majority of the total return of these investments.

## **3. Opportunistic Private Market Investments**

- a. The Opportunistic Investment category describes investments that are not adequately classified within the other investment mandates. Allocations to opportunistic investments may range from 0% to 5% of total portfolio. The Board shall determine appropriate commitment levels subject to the constraints below.
- b. The Board shall not make commitments to a single portfolio greater than 20% of the total amount of the proposed portfolio.

- c. The Board shall not concentrate aggregate commitments to a single investment manager's firm greater than 25% of the firm's total assets under management.

## **VI. EVALUATION AND REVIEW**

### **A. Investment Staff Reporting Requirements**

The Investment Staff will at regular periodic Board and Investment Committee meetings report as needed on the following: asset class and manager account variances relative to targets, updates regarding changes within the portfolio including rebalancing and transition events, portfolio risk exposures, asset class structure reviews, special project reports and any other areas of investment portfolio analysis as directed by the Board.

### **B. Investment Consultant Reporting Requirements**

The Investment Consultant will report on investment portfolio performance at regular periodic Board and Investment Committee meetings. These reports will cover the following: recent capital markets developments and consequent impacts on investment portfolio performance both gross and net of fees, asset allocation, return attribution, multi-period analyses of the performance of all investment portfolio accounts and composites relative to benchmarks and comparable universes, analyses of the risks of investment portfolio accounts and composites relative to benchmarks.

In addition to reporting on investment portfolio performance, the Investment Consultant will report to the Board any material recent organizational or personnel developments at the investment firms retained by the System. The Investment Consultant will also report to the Board regarding the investment firms retained by the System any significant changes in clients and assets under management.

To assist the Board in their annual review of the Investment Consultant, the Investment Consultant will provide a report covering material organizational or personnel developments at the firm as well as any significant changes in number of clients and/or assets under advisement. The Investment Consultant will also provide a certification signed by the investment consultant firm's Chief Compliance Officer or designee that the firm has for the fiscal year remained in compliance with all applicable elements of this Policy, the investment consulting agreement between the firm and the System and any other contractual instruments defining the relationship between the investment consultant and the System. The Investment Consultant will also provide any additional information or disclosures the Board determine necessary to conduct their annual review.

### **C. Investment Manager Reporting Requirements**

Each Investment Manager will timely report to Investment Staff and Investment Consultant any material organizational or personnel developments at their firm as well as any significant changes in number of clients and/or assets under management either for the mandate in which the System is invested or for the entire firm.

In addition to the requirements stated herein, each investment manager will provide any reports as may be required in the investment management agreement or subscription agreement between the firm and the System and any other contractual instruments defining the relationship between the investment manager and the System.

On a quarterly basis each Investment Manager will provide to Investment Staff and Investment Consultant performance, transaction and market value data as requested in electronic or hardcopy form to assist Staff and the Investment Consultant in their roles of monitoring the investment portfolio on behalf of the Board. The data requested will be designed by Staff and Investment Consultant to correspond with the Investment Manager's particular asset class assignment. In their regular quarterly reporting, Core Plus Full Discretion Fixed Income managers will provide a line-item holdings report for unrated securities and investments subject to the 5% limitation as referenced in Section V. A. 7. f. iii.

On a yearly basis for the System's June 30 fiscal year each Investment Manager shall provide the Staff and the Investment Consultant an annual report consisting of the following:

1. A certification signed by the investment management firm's Chief Compliance Officer or designee that the firm has for the fiscal year remained in compliance with all applicable elements of this Policy, and any investment guidelines within the investment management agreement or subscription agreement and any other contractual instruments defining the relationship between the investment manager and the System.
2. For firms that cast proxy votes on behalf of the System, a summary of the firm's philosophy with respect to voting proxies along with a detailed report showing all proxy votes cast during the fiscal year.
3. A detailed report showing investment management fees and expenses charged by the firm to the System whether invoiced or deducted during the fiscal year.
4. A disclosure of any payments, monetary or otherwise, to System fiduciaries including Staff, Investment Consultant or Trustees.
5. A review of the Investment Manager's investment philosophy and process as well as a June 30 fiscal year summary of any material organizational or personnel developments at the firm as well as any significant changes in number of clients and/or assets under management either for the mandate in which the System is invested or for the entire firm during the fiscal year.
6. Each investment manager is required to report to the System's Investment Staff and Investment Consultant the types of derivative instruments used along with a narrative explanation of the rationale for using such instruments in their portfolio management process during the past year highlighting risks mitigated and or efficiencies achieved.

## APPENDIX A - PERFORMANCE BENCHMARKS

<b>Composite</b>	<b>Benchmark Index</b>
Total Portfolio	Policy Index*
U.S. Equities	Russell 3000
International Equities	MSCI ACWI ex.US IMI
Fixed Income	Core Plus Fixed Income**
Real Estate	NCREIF Property
Private Equity	Russell 2000 + 4%
Large Cap U.S. Equities	Russell 1000
Mid Cap U.S. Equities	Russell Mid Cap
Small Cap U.S. Equities	Russell 2000
Small Cap International Equities	MSCI World ex US Small Cap

*\*The Policy Index is a composite index composed of the monthly asset class benchmark returns weighted by their respective strategic asset allocation targets.*

*\*\* The Core Plus Fixed Income index is a composite index composed of 70% Bloomberg Barclays U.S. Aggregate Index and 30% ICE BofA US High Yield Constrained Index.*

A current listing of the System's investment managers, accounts and benchmarks can be found on the System's website at <https://oklahoma.gov/trs/publications/trs-investment-policy-statement.html>

## APPENDIX B - STRATEGIC ASSET ALLOCATION

The assets of the Plan shall be invested with a focus on meeting long-term objectives in order to fulfill the System's Mission Statement. Recognizing the goals and objectives of the System, the following strategic asset allocation target has been adopted:

U.S. Equities	43.5%
International Equities	19.0%
Fixed Income	22.0%
Real Estate	9.0%
Private Equity	6.5%
Cash	0%

While the Board of Trustees has adopted the strategic asset allocation above and the rebalancing policy below, the number of investment managers or mandates used is not specifically set forth by policy. The number and type of investment managers to be hired within an asset class shall be determined by the Board of Trustees based upon periodic analyses of asset class portfolio structures.

## APPENDIX C - REBALANCING POLICY

In the event the Plan's market values change to the extent that asset class percentage allocations fall below defined minimum percentage allocations or exceed defined maximum percentage allocations, staff shall prepare a plan to rebalance the portfolio according to the guidelines shown below:

	Minimum	Low Rebalance Point	Target	High Rebalance Point	Maximum
U.S. Equity	36.5%	40.0%	43.5%	47.0%	50.5%
International Equity	14.0%	16.5%	19.0%	21.5%	24.0%
Fixed Income	17.0%	19.5%	22.0%	24.5%	27.0%
Real Estate*	6.5%	7.8%	9.0%	10.3%	11.5%
Private Equity*	4.5%	5.5%	6.5%	7.5%	8.5%

\* Private capital investment valuations, by their nature, lag traditional public market investment valuations by several months. In addition, the offering documents of private capital investments define the required timing of contributions, reinvestment provisions and distributions resulting in constraints on liquidity. As a result, the current allocation to private capital investments may fall outside the allowable ranges for these investments for periods of time. Annual commitment levels to private capital investments will be determined through a multi-year investment pacing analysis and planning horizon, including forecasted future cash flows with a goal of achieving and maintaining target allocations over time.

When allocations move outside minimum or maximum boundaries, they will be rebalanced half of the way back to the target percentage. Due to the asymmetrical nature of maximum and minimum boundaries, a full rebalancing of each asset class may not be possible. In such cases, rebalancing asset classes up from their minimums shall take priority. Cash held in short-term investments with the Custodian shall be considered as domestic fixed income for rebalancing purposes. In highly stressed market environments where volatility and transaction costs are elevated, a rebalancing plan designed to reduce tracking error and transaction costs may be developed and substituted for the normal rebalancing approach defined by the boundaries above.

In rebalancing the portfolio, staff shall consider asset class liquidity in determining the timeframe over which the rebalancing should take place in an attempt to reduce transaction costs. Securities may be transferred in lieu of cash, if feasible, to achieve lower transaction costs. Staff and the investment consultant may consult with those managing the affected investment accounts to determine the appropriate incremental amounts to be transferred as well as the appropriate duration of the rebalancing. The primary goal of rebalancing will be to control risk by correcting variances from minimum and maximum asset class allocations: minimizing transaction costs and diversifying across time will be secondary goals. In the event that Plan asset market values change to correct variances from minimum and maximum asset class allocations, rebalancing programs may be halted prior to the anticipated date of completion.

Upon the development of a rebalancing plan consistent with these guidelines, staff will advise the Plan's Custodian of the upcoming changes and direct affected investment managers to implement the required purchases and sales in a manner that leaves the resulting portfolios in concert with their current strategies.

The Staff may defer any element of the rebalancing with concurrence of the Chairman of the Board of Trustees under circumstances where percentage allocation variances outside of minimum and maximum boundaries are minimal and appear to be only temporary in nature or in the event that such rebalancing would not be in the best interest of the Plan.

Annually, staff may present an optional strategy for rebalancing all asset classes near target allocations, giving due consideration to potential transaction costs.

## APPENDIX D - INVESTMENT MANAGER EXCEPTIONS TO INVESTMENT GUIDELINES

Any exception requests subsequent to the approval of these guidelines should be submitted according to the framework established in Section III, B.

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**Requesting firm:** *Hotchkis & Wiley Mid Cap Equity*

**Exception requested:** *Section V.A.5.c.; Allow non-U.S. dollar denominated securities traded in local markets and securities of non-U.S. companies (including ADRs) traded over the counter in the U.S. market.*

**Proposition for attribution:** *Provide quarterly reporting with and without non-U.S. holdings.*

**Requested term:** *12/31/2021*

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**Requesting firm:** *Wellington Management International Small Cap Equity*

**Exception requested:** *Section V.A.6.c.; Increase the maximum portfolio exposure in Japan from 35% to 40%.*

**Proposition for attribution:** *When the portfolio exposure in Japan exceeds 35%, provide quarterly reporting illustrating the contribution to total return.*

**Requested term:** *12/31/2021*