

ILLINOIS STATE BOARD OF INVESTMENT
DIVERSITY POLICY

Objective

The Illinois State Board of Investment (“ISBI” or the “Board”) has adopted this Diversity Policy (the “Policy”) to increase access and opportunities for emerging managers and brokers who are minorities, women and persons with a disability as those terms are defined in the Business Enterprise for Minorities, Females, and Persons with Disabilities Act¹ and the Illinois Pension Code².

A. Emerging and Minority Investment Managers

It is the primary goal of ISBI to develop and maintain an investment program that will help secure the retirement benefits of the participating retirement plans. In order to achieve this objective, investment advisers are selected based on their long-term records of performance, depth of investment staff and consistency of approach among other characteristics.

However, the Board recognizes that even large, experienced and successful investment organizations were once small, start-up firms with few assets under management. Today many such firms are owned by minorities, women and persons with a disability. These firms are often started by experienced investment professionals, who show great promise, but find it difficult to compete with large majority owned organizations. The firms typically do not meet the minimum standards set for investment advisers by large investment programs such as ISBI. Consequently, they are not considered.

In order to take advantage of these emerging organizations, the Board has established an aspirational goal³ to use emerging investment managers⁴ for no less than 20% of the total portfolio funds under management within ISBI’s investment program.

Furthermore, the Board goes beyond the utilization of emerging managers and has adopted goals for the utilization of minority investment managers⁵. The Board has

¹ 30 ILCS 575

² 40 ILCS 5

³ Effective January 1, 2016, Public Act 99-0462 requires the Board to establish certain aspirational goals for the utilization of Minority Investment Managers.

⁴ Effective April 3, 2009, Public Act 96-0006 revised the definition of “emerging investment manager.” As a result, the current definition applicable to ISBI is found in 40 Ill. Comp. Stat. § 5/1-109(4) and is defined as “a qualified investment adviser that manages an investment portfolio of at least \$10,000,000 but less than \$10,000,000,000 and is a ‘minority owned business’, ‘female owned business’ or ‘business owned by a person with a disability’ as those terms are defined in the Business Enterprise for Minorities, Females, and Persons with Disabilities Act.”

⁵ For purposes of this Policy, the term “Minority Investment Manager” includes emerging investment managers and/or minority owned business, female owned business, or business owned by a person with a

established an aspirational goal to have no less than 20% of its investment advisors be minorities, females, and persons with a disability.

**Goals for Utilization of Emerging and Minority Investment Managers
Minority-Owned Businesses, Female-Owned Businesses, and Businesses Owned by
Persons with a Disability**

It is the goal of the Board that, subject to its fiduciary responsibility, the use of emerging investment managers shall be significant in each of the broad asset classes in which ISBI is invested and not concentrated in any particular asset class.

The Board has adopted the following minimum goals for the utilization of emerging and minority investment managers⁶:

**Goals for Utilization of Emerging and Minority Investment Managers
By Investment Manager Classification**

Classification	Percent of Total Portfolio	
	Emerging	Minority
Minority-Owned	5% - 7%	5% - 7%
Female-Owned	3% - 5%	3% - 5%
Disabled	0% - 1%	0% - 1%

**Goals for the Utilization of Emerging and Minority Investment Managers
By Asset Class**

Asset Class	Percent of Asset Class	
	Emerging	Minority
Equities	8% - 10%	8% - 10%
Fixed Income	10% - 12%	10% - 12%
Alternatives*	1% - 5%	1% - 5%

* Alternative investments are not subject to the requirements set forth in Public Act 96-0006.

These goals will be reviewed annually by Investment Staff and the Board.

disability as those terms are defined in the Business Enterprise for Minorities, Females, and Persons with Disabilities Act.

⁶ Public Act 96-0006 requires the establishment of “3 separate goals for (i) emerging investment managers that are minority owned businesses; (ii) emerging investment managers that are female owned businesses; and (iii) emerging investment managers that are businesses owned by a person with a disability.”

For purposes of this Policy, the emerging and/or minority investment manager must provide to the Board documentation of a current State of Illinois certification⁷ or documentation of a current state-issued certification. For emerging and/or minority investment manager without a state issued certification, an attestation by the investment manager or General Partner stating that the investment manager or advisor is a “minority owned business”, “female owned business” or “business owned by a person with a disability”, as those terms are defined by the Illinois Business Enterprise for Minorities, Females and Persons with Disabilities Act⁸ must be provided. The emerging and/or minority investment manager is required to immediately notify ISBI as to any change in the matters covered by any such attestation. On an annual basis, the emerging and/or minority investment manager must certify to ISBI that its state-issued certification is in good standing or, alternatively, that nothing in its attestation stating that the investment manager or advisor is a “minority owned business”, “female owned business” or “business owned by a person with a disability”, as those terms are defined by the Illinois Business Enterprise for Minorities, Females and Persons with Disabilities Act, has changed. ISBI and the Board are relying on certifications and/or investment manager attestations for reporting purposes. In the event it is discovered an investment manager has misrepresented information to ISBI, such misrepresentation shall be grounds for termination of the relationship.

Minority investment managers may represent any asset class within ISBI’s asset allocation. Allocations of the Board’s assets to minority investment managers will be made in accordance with the fiduciary standards under which all ISBI investment advisers operate.

Asset Management

1. Investment Staff will review the statistical requirements for investment adviser searches as needed to provide better access to minority investment managers that have appropriate products.
2. Investment Staff will seek to include at least one minority investment manager in final Investment Staff interviews. Investment Staff will inform the Board of all minority investment manager candidates.
3. Investment Staff will regularly meet with Illinois-based minority investment managers on-site, and learn more about the Illinois-based minority investment manager community.

⁷ A “State of Illinois certification” is a certification granted by the Illinois Department of Central Management Services to a Minority Business Enterprise, a Female Business Enterprise or a Person with Disabilities Enterprise under the Business Enterprise Program for Minorities, Females, and Persons with Disabilities.

⁸ 30 ILCS 575

4. Investment Staff will encourage ISBI Consultants to be proactive and use creative approaches in achieving the Board’s objectives with respect to the use of minority investment managers.

B. Minority and Illinois Brokerage

The Board seeks to increase access and business with state certified, minority-owned broker/dealers and Illinois-based broker/dealers; therefore, the Board, as a part of this Policy, has adopted minimum expectations for the use of minority-owned broker/dealers⁹ by the Board’s investment advisers. The minimum expectations are established based on the asset class in which the investment adviser invests. In addition, the Board will encourage its investment advisers to direct 25% of their trades to Illinois-based¹⁰ broker/dealers. It is further the policy objective of the Board to encourage its investment advisers to seek to obtain best price execution at the Chicago Stock Exchange, which can be achieved by utilizing the Institutional Brokers of the Chicago Stock Exchange.¹¹

For purposes of this Policy, in order to be considered a minority-owned broker/dealer by the Board, documentation of a current state certification must be provided to the Board.

Transactions completed with minority-owned broker/dealers on behalf of the Board must be completed at rates fully competitive with the market. Subject to best execution, investment advisers for the Board’s separately managed investment portfolios are strongly encouraged to direct the below percentages of total eligible commission dollars or eligible trading volume to minority-owned broker/dealers.

<u>Asset Class</u>	<u>Minimum Goal as a Percentage</u>
U.S. Equity	30%
International Developed Equity	20%
Fixed Income	20%
International Fixed Income	0 – 5%
Hedged Equity	0 - 5%

These goals will be reviewed annually by Investment Staff.

Brokerage

1. Investment Staff will strongly encourage verbally and in writing the Board’s domestic and international equity and fixed income investment advisers to directly

⁹ In accordance with Public Act 96-0006, “minority-owned broker dealer” means “a qualified broker-dealer who meets the definition of ‘minority owned business’, ‘female owned business’, or ‘business owned by a person with a disability’, as those terms are defined in the Business Enterprise for Minorities, Females, and Persons with Disabilities Act.”

¹⁰ The definition of an “Illinois-based” firm is consistent with the Illinois Pension Code which defines “Illinois business” as “a business, including an investment adviser, that is headquartered in Illinois.” 40 Ill. Comp. Stat. § 5/1A-108.5(a).

¹¹ Article 17, Rule 3(d)

utilize minority-owned brokers/dealers. Investment staff will add additional asset classes when appropriate.

2. Investment Staff will strongly encourage verbally and in writing investment advisers to direct 25% of their trades to Illinois-based broker/dealers.
3. Investment Staff will strongly encourage verbally and in writing investment advisers to obtain best price execution at the Chicago Stock Exchange (“CHX”), which may be achieved by utilizing the list of Institutional Brokers of the CHX. For purposes of this Policy, the most current list of Institutional Brokers of the CHX can be accessed via the CHX website.⁷
4. Investment Staff will provide verbally and in writing to minority-owned broker/dealers the contact information for the Board’s domestic and international equity and fixed income investment advisers.
5. Investment Staff will monitor the use of Illinois-based broker/dealers and minority-owned broker/dealers by the Board’s investment advisers, and report results to the Board on a quarterly basis. If an investment adviser reports less than their encouraged percentage of minority-owned broker/dealer utilization, Investment Staff will require the adviser to report in writing the reason for the shortfall, at which time the Board will decide if the adviser’s practices are in accordance with this Policy.
6. Investment Staff will consider the use of Illinois-based broker/dealers and minority-owned broker/dealers when evaluating existing investment advisers.
7. Step outs and correspondence are prohibited. With regard to international fixed income and hedged equity allocations, best efforts by ISBI’s investment advisers shall be applied.

Consequences of Non-Compliance

The Board continuously monitors investment advisers’ compliance with this Policy and has established a series of consequences for those advisers who continually fail to meet the Board’s expectations. The investment advisers are expected to achieve the desired levels of brokerage usage over a fiscal year period. The following steps will occur if the investment adviser continues to fall short of expectations:

1. A follow-up letter will be distributed to the investment advisers not achieving the minimum level of minority-owned broker/dealer usage. The investment advisers will be reminded of the brokerage usage expected by the Board.
2. Not achieving the desired level of minority-owned broker/dealer usage will be noted in the annual investment adviser review presented to the Board.

3. Investment Staff will conduct a meeting with the investment adviser to discuss the reasons for not achieving the desired level of brokerage usage.
4. Investment advisers not achieving the expected levels of minority-owned broker/dealer usage may be subject to a moratorium on additional funding.
5. If an investment adviser fails to comply with the request, they may be invited to appear before the Board to explain why they are unable to achieve the desired level of brokerage usage.
6. The investment adviser may be placed on the Investment Advisers Watch List.

C. Minority Contract and Service Utilization

Public Act 96-0006 (“PA 96-6”) states that the Board shall adopt a policy which sets forth goals for the utilization of businesses owned by minorities, females, and persons with disabilities for all contracts and services. According to PA 96-6, “The goals shall be based on the percentage of total dollar amount of all contracts let to minority owned businesses, female owned businesses, and businesses owned by a person with a disability, as those terms are defined in the Business Enterprise for Minorities, Females, and Persons with Disabilities Act.”

In furtherance of the Act, the Board, subject to its fiduciary responsibility, has set forth a minimum goal of 0-1% of the total dollar amount for all contracts for the utilization of businesses owned by minorities, females, and persons with disabilities.

In addition, pursuant to Public Act 99-0462, ISBI has set an aspirational goal to have no less than 20% of the total service contracts awarded for information technology, accounting, insurance brokerage, and legal services to be let to businesses owned by minorities, females, and persons with a disability, as those terms are defined in the Business Enterprise for Minorities, Females and Persons with Disabilities Act.

D. Fiduciary Diversification

The Board acts as fiduciary for the General Assembly Retirement System, the Judges’ Retirement System of Illinois and the State Employees’ Retirement System of Illinois. As a fiduciary, the Board is responsible for managing, investing, reinvesting, preserving and protecting fund assets.¹²

It is the policy objective of the Board to comply with all federal and state statutes, rules and regulations pertaining to the Board’s investments. PA 96-6 encourages the Board to increase the racial, ethnic, and gender diversity of its fiduciaries, to the greatest extent feasible within the bounds of financial and fiduciary prudence.¹³

¹² See 40 ILCS 5/1-101.2

¹³ See 40 Ill. Comp. Stat. § 5/1-109.1

In furtherance of the Act, it is the goal of the Board to use its best efforts to increase the racial, ethnic, and gender diversity of its fiduciaries, including its consultants and senior staff, within the bounds of financial and fiduciary prudence.

Due to the small size of the staff and the number of individuals in these categories during the past fiscal year, there is no underutilization. As vacancies occur, the Board will make every effort to increase the racial, ethnic, and gender diversity of its consultants and senior staff in accordance with this Policy and within the bounds of financial and fiduciary prudence.

In accordance with its Affirmative Action Plan, the Board submits quarterly Workforce Analysis and Workforce Transaction Reports to the Department of Human Rights. The Board will continue to report to the Department of Human Rights on both a quarterly and an annual basis.

This goal will be monitored and reviewed annually in conjunction with the annual Affirmative Action Plan.

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