



# Policy Consultation: Slides for Presentation

*Presentation to the Investment Advisory Committee*

September 21, 2016



North Carolina Department of State Treasurer  
*Investment Management*

*Learn. Invest. Grow. Prosper.*

# Purpose of session

- New statute (G.S. 147-69.11) requires consultation with IAC on certain key ethics policies
  - *For text of statute, see policy supplement, page P-1*
    - Effective date of new statute: January 31, 2017
- At this meeting:
  - Placement Agent Policy -- consultation under G.S. 147-69.11(a)(4)
  - Conflict of Interest Certification – consultation under G.S. 147-69.11(a)(5)
  - Code of Ethics – consultation under G.S. 147-69.11(a)(1)
  - Outside Activity / Secondary Employment Policy – consultation under G.S. 147-69.11(a)(5)
- At November meeting:
  - Employee Training Policy – consultation under G.S. 147-69.11(a)(2)
  - Gift Ban – consultation under G.S. 147-69.11(a)(3)
  - Insider Trading Policy – consultation under G.S. 147-69.11(a)(2)
  - Other policies at your request
- All of the above policies except Outside Activity Policy are already in existence and have existed for several years.
- Goal is IAC consultation & input on changes, improvements, and any additional areas to cover.



# Placement Agent Policy

- *For text of policy, see policy supplement, pages P-4 to P-20*
- *For text of investment manager's disclosure form, see pages P-21 to P-30*
- *For text of placement agent's disclosure form, see pages P-31 to P-40*
  
- Original policy adopted in September 2009; revised substantially in December 2013
- This is revised version 2.1 of policy, on track to go into effect in October
  
- Goals for discussion:
  - Is the policy too restrictive or too weak?
  - What can we do better?
  - How can we make the policy shorter and easier to read?



# Placement Agent Policy: Overall themes (1/3)

- Not a flat ban on placement agents
- However, placement agents are heavily restricted
  - If DST has used the investment manager within the last two years, the investment manager can't compensate a placement agent (*page P-12*)
  - The placement agent must be registered with SEC or FINRA (*page P-11*)
  - No tail fees (*page P-12*)
- The external investment manager must pay the placement agent's cost
  - If external investment manager wants to use a placement agent, the investment manager must ultimately bear the entire cost of the placement agent. (*page P-12*)
  - Offset of management fees permitted if (i) terms of management fee offset are fully disclosed, (ii) placement agent and compensation are fully disclosed in approved disclosure letters, and (iii) NC Funds do not ultimately bear any placement agent fees and expenses (*page P-12, footnote 5*)



# Placement Agent Policy: Overall themes (2/3)

- NC can't recommend a placement agent (*pages P-12 to P-13*)
- Disclosures
  - Lengthy disclosure forms required (*pages P-21 to P-40*)
  - Evaluation by outside Compliance Counsel (*page P-13*)
  - Compliance Counsel or General Counsel has to approve form (*page P-11*)
  - If something is disclosed, potential responses range from prohibition, to recusal, to simple notice, depending on the type of disclosed relationship (*pages P-13 to P-15*)
- Significant remedies for violation of the policy
  - Repayment of aggregate management or advisory fees paid for most recent two years in respect to the Treasurer's business (*page P-9*)
  - Any other remedies at law or equity (*page P-9*)



# Placement Agent Policy: Overall themes (3/3)

- Political contributions (section
  - This topic is heavily regulated by the SEC Rule (75 Fed. Reg. 41017, as amended)
  - Basics of SEC Rule:
    - Bottom line: an investment advisor doing work for a public fund can't be compensated if it made a political contribution greater than the *de minimis* limit to an elected official making decisions for that fund.
    - Two-year lookback period
    - Remedy is disgorgement of fees
  - It is the external investment manager's obligation to follow the SEC Rule. SEC Rule applies to the external manager, not DST.
  - Text on this topic in DST's Placement Agent Policy is a secondary check in case managers aren't fulfilling their compliance obligations to the SEC.
  - DST's disclosure forms require potential investment manager to certify that there were no SEC-barred donations (pages P-16 and P-29)



# Placement Agent Policy: Implementation points

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- Implementation points
  - Requiring new disclosure letters only for substantive amendments (*page P-19*)
  - Exception for secondary market transactions – no negotiating leverage to get the disclosure letter or the remedy (*pages P-16 to P-17*)
  - Exception for international “placement agents” required under certain countries’ laws (*page P-18*)



# Conflict of Interest Certification

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- *See policy supplement, pages P-41*
- Policy originally adopted in June 2013
- This is revised version 2.1 of form, effective September 2016
  
- Should any other certifications be added?
  - How critical is it that the certification be one page?
  
- Costs and benefits of electronic signatures on a document like this



# Code of Ethics and Conduct

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- *See policy supplement, pages P-42 and P-43*
- Policy originally adopted in June 2013
- This is revised version 1.1 of policy, effective January 2014
  
- Any missing concepts?
- Other policies incorporated into this code
- Who should sign acknowledgement every year?



# Supplemental Ethics Policy on Outside Activity

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- *See policy supplement, pages P-44 to P-49*
- Should this be a rule?
- We have listed multiple options for several topics. We are interested in exploring where there is consensus within the IAC on these topics.





**Thank You!**

*Together we can build and maintain a fiscally strong and prosperous North Carolina.*

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