



pennsylvania
STATE EMPLOYEES' RETIREMENT SYSTEM

**Commonwealth of Pennsylvania
State Employees' Retirement Board
Statement of Investment Policy**

**Adopted April 21, 2004
Amended March 8, 2017**

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**Commonwealth of Pennsylvania
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1. Introduction

The State Employees' Retirement Fund ("Fund") was established in 1923 by an act of the Pennsylvania legislature. The purpose of the Fund is the accumulation of funds exclusively for the benefit of the members and beneficiaries of members of the State Employees' Retirement System ("SERS" or the "System") for the payment of withdrawal, retirement, disability, and death benefits as provided in Pennsylvania Consolidated Statutes Title 71, Part XXV ("Retirement for State Employees and Officers"). The Fund is under the exclusive control and management of an eleven member Board of Trustees ("Board"). Six members are appointed by the Governor and confirmed by the State Senate to four-year terms. Two members of the Senate are appointed by the President Pro Tempore of the Senate, and two members of the House by the Speaker of the House, and serve on the Board for the duration of the terms for which they were elected. The State Treasurer serves as a member of the Board, ex-officio.

This Statement of Investment Policy ("Policy") was originally adopted by the Board on September 19, 1979 and was last revised by Board action on March 8, 2017.

2. Statement of Purpose of Investment Policy

This document specifically outlines the investment philosophy and practices of SERS and has been developed to serve as the governing policy for the management of the System's assets. The purpose of this Policy is to formalize the Board's investment objectives and policies, and to define the duties and responsibilities of the various individuals and entities involved in the investment process. The assets of SERS will be managed with the primary objectives of the payment of benefit obligations to participants in the plans as well as to maximize return with acceptable risk considerations and sufficient liquidity so that employer contributions can be minimized. Therefore, it is crucial that the Board adopt a long-term plan by which the assets of the System will be managed and enhanced through prudent investments. This Policy is intended to ensure that the level of assets is adequate to cover the accumulated liabilities of the System. This is an official investment policy document of SERS. Deviation from this document is not permitted without explicit written permission, in advance, from the Board.

In developing this Policy, the Board understands and accepts its fiduciary obligations to the members of the System. These obligations are legal in nature, and are outlined in Title 71, Pennsylvania Consolidated Statutes, Section 5931, a copy of which is attached hereto as Appendix I.

3. Prudent Investor Standard

The Board's investment authority is governed by the "prudent investor" standard as set forth in Title 71, Pennsylvania Consolidated Statutes, Section 5931(a):

Control and management of fund. The members of the board shall be the trustees of the fund. Regardless of any other provision of law governing the investments of funds under the control of an administrative board of the State government, the trustees shall have exclusive control and management of the said fund and full power to invest the same in accordance with the provisions of this section, subject, however, to the exercise of that degree of judgment, skill and care under the circumstances then prevailing which persons of prudence, discretion and intelligence, who are familiar with such matters, exercise in the management of their own affairs not in regard to speculation, but in regard to the permanent disposition of the funds, considering the probable income to be derived therefrom as well as the probable safety of their capital. The trustees shall

have the power to hold, purchase, sell, lend, assign, transfer or dispose of any of the securities and investments in which any of the moneys in the fund shall have been invested as well as of the proceeds of said investments, including any directed commissions which have accrued to the benefit of the fund as a consequence of the investments, and of any moneys belonging to said fund, subject in every case to meeting the standard of prudence set forth in this subsection.

No provision of this Policy shall be construed in contravention of the Board's statutory investment authority found in Title 71, Pennsylvania Consolidated Statutes, Section 5931.

4. Fiduciary Status, Duties, and Responsibilities of Board, Staff, Investment Managers, Other Agents, and State Treasurer

SERS is one of the larger public pension funds in the United States. Due to its size and investment structure, its operational requirements are complex. In order to administer the System and carry out its investment obligations, the Board relies heavily on both staff and external contractors. Because of the number of parties involved, their roles as fiduciaries must be clearly identified. Such identification increases operational efficiency, ensures clear lines of responsibility, and reduces or eliminates duplication of effort.

A. Board of Trustees

Title 71, Pennsylvania Consolidated Statutes, Section 5931(e) provides, in part, as follows:

The members of the board, employees of the board, and agents thereof shall stand in a fiduciary relationship to the members of the system regarding the investments and disbursements of any of the moneys of the fund and shall not profit either directly or indirectly with respect thereto.

In exercising this fiduciary responsibility, the members of the Board, employees of the Fund, and agents of the Fund are governed by the "prudent investor" standard and the exclusive benefit standard. The exclusive benefit standard requires these parties to act solely within the interests of SERS' participants and beneficiaries, and for the exclusive purpose of providing benefits to participants and beneficiaries.

The Board may, when possible and consistent with its fiduciary duties imposed by law, including its obligation to invest and manage the Fund for the exclusive benefit of the members of the System, consider whether an investment in any project or business enhances and promotes the general welfare of the Commonwealth and its citizens. Where investment characteristics are equivalent, the Board's policy will favor investments that will have a positive impact on the economy of Pennsylvania.

The members of the Board are responsible as trustees for the proper management of the assets of the Fund. The Board has the responsibility of establishing and maintaining broad policies and objectives for all aspects of the System's operations. Specifically with regard to investments, the Board seeks the recommendations of the staff and consultants prior to taking action. In carrying out these duties, the Board will be responsible for:

1. Reviewing and approving a biennial Investment Plan that sets forth the direction of the Fund and work plan initiatives for the coming two years. This Investment Plan shall incorporate long-term allocation ranges to the asset classes.

2. Approving the engagement and termination of investment managers. Staff and consultants will identify potential candidates. Potential managers will be evaluated based on their ability to achieve the objectives outlined in the Investment Plan and their demonstrated experience and expertise for the specific mandate. Board suggestions for potential managers who meet these criteria will be evaluated by staff and consultants. While individual Board Members may meet with prospective managers, all group meetings involving a quorum of Board Members for a presentation by prospective managers shall be through formal Board meetings or Board Committee meetings. Staff and consultants are jointly responsible for carrying out the research and initial due diligence to identify qualified candidates. Staff and consultants are also jointly responsible for performing the on-going monitoring of investment managers and funds. Lastly, all prospective investment opportunities and/or investment manager terminations which are recommended to the Board must be supported by a memo from Staff and a memo from the relevant investment consultant.
3. Approving the engagement and termination of consultants.
4. Reviewing the investment performance and risk characteristics of the Fund.
5. Reviewing and approving the Comprehensive Annual Financial Report.
6. Reviewing and approving the annual actuarial report, assumptions and funding level and, reviewing and approving an actuarial experience study that is to be conducted no less than every five years.
7. Reviewing and approving the results of an asset liability study on a periodic basis, but not less than every five years.
8. Reviewing and adopting the proxy voting guidelines.
9. Oversight and monitoring of staff including, but not limited to the hiring of the Chief Investment Officer, the Executive Director, and the Director of Internal Audit.

In discharging these responsibilities, the Board has delegated certain functions to the staff and to various contractors who provide professional services to the Board. All persons who act as agents of the Board shall adhere to the highest standards of professional integrity and honesty.

B. State Employees' Retirement Board Staff

The Executive Director is responsible for administrative matters relating to the operations of the System. The Chief Investment Officer is charged with the coordination of all investment activities and matters within the System. The Investment Office reports to the Board on emerging trends and issues of concern to public pension funds generally and to the Fund in particular. The Investment Office is responsible to the Board to review and analyze the current investment climate, and to recommend adjustments with respect to this Policy that are appropriate to take optimum advantage of new conditions and strategies as they arise in the market place. To ensure that the goals and objectives of the Board are being fulfilled, the Investment Office also reviews and analyzes the philosophies, policies, and strategies employed by the investment managers, evaluating the appropriateness of their decision-making processes and their investment styles in relation to present and projected investment horizons.

The Chief Investment Officer of the System is charged with the following responsibilities:

1. To manage, on a day-to-day basis, the portfolio, its components, and agents;
2. To authorize receipt or payment for the acquisition or disposition of investments;
3. To act as liaison on behalf of the Board with all investment-related contractors;
4. To review and analyze all investment transactions for conformity to certain applicable laws, regulations, each manager's investment strategy statement, and this Policy;
5. To review investment proposals presented by investment managers, and where appropriate, summarize and recommend the same for Board consideration;
6. To analyze and summarize for the Board pertinent information from relevant publications, discussions, meetings, and research on current investment related topics;
7. To respond to inquiries from the Board and Pennsylvania Legislature, the membership, the press, other governmental representatives, and the public concerning the investments of the Fund;
8. To institute an Annual Implementation Plan ("AIP") detailing what the Fund will be doing in the next year in order to implement the Investment Plan. The purpose of the AIP is to report to the Board the status of what was accomplished and what will be accomplished going forward.
9. To prepare the Investment Plan and perform analysis and recommendations for action to present to the Board for approval and implementation consistent with this Policy and achievement of the Board's investment objectives; and
10. To perform such other duties as may be required to implement this Policy.

C. Internal Audit

The Director of Internal Audit reports functionally to the Audit Committee and administratively to the Executive Director. The internal audit department is independent of the System's operational activity and is responsible for providing objective audit and review services for the entire System, including the Investment Office. Internal audit's services emphasize the promotion of adequate and effective internal controls at a reasonable cost and result in suggested improvements that will lead to economies and efficiencies in the Systems' operations.

With the advent of the Sarbanes-Oxley Act of 2002, the Board recognized the need for, and established an Audit Committee to provide additional oversight relating to the adequacy of internal controls applicable to financial reporting. The Audit Committee will meet quarterly to discuss audit related issues. The Audit Committee, at its discretion, may meet with the Director of Internal Audit in executive session. The Audit Committee may make recommendations for changes in internal controls for consideration by the Board but shall have no policy authority.

D. Investment Managers

The Board continually seeks to employ investment managers that possess superior capabilities in the management of assets of public retirement systems. The Fund has carefully documented its investment processes, including those related to hiring managers to manage the Fund's investments. Those processes are available for review on the Fund's intranet. Each manager has full discretion to carry out its investment mandate subject to the investment strategy statement contained in the investment management agreement and will be expected to conduct business on behalf of the System in accordance with the mandate for which they were retained. It is the Board's policy to limit the allocation of Fund investments such that no more than 15% of the total market value of Fund assets should be invested in any one investment product offered by an investment manager, except where management of such investments is of a passive nature (e.g., index funds). Notwithstanding any of the limitations contained in this section, no liquidation of an investment shall be required solely due to changes in market value.

Each manager's benchmark will reflect that manager's particular style or tactical role in SERS' investment process. Each benchmark will be clearly specified, measurable, and replicable. Benchmarks do not have to be published or widely recognized; they may be "customized" for a particular investment style or styles. The benchmark shall be determined in advance of funding by mutual agreement between the manager, staff, and consultant. In the event of a change in management style, agreed upon change in a manager's strategy, availability of a better benchmark construction methodology, or changes to or additions in indices, a manager's benchmark may be modified by mutual consent between the manager, staff, and consultant. Despite the foregoing, it is recognized that benchmarks in the investment industry may fail to capture the investment nuances of an investment manager, which leads to tracking error relative to the benchmark.

The Board further requires those public markets investment managers selected and working on its behalf to perform the following activities:

1. To execute investment decisions that are consistent within the scope of the approved investment guidelines expressed in the respective management agreement and other relevant documents.
2. To execute investment transactions on behalf of the Board in a manner that maximizes the investment value of each transaction from the viewpoint of the Fund, utilizing such brokers and dealers as they deem appropriate to obtain the best execution capabilities and/or valuable information with respect to the economy and the affairs of corporations at the lowest total cost to the Fund.
3. To report to the Board at least quarterly through the Investment Office, with the exact frequency and format of reporting to be determined by the Investment Office, on the composition and relative performance of the investments in their designated portfolios; the economic and investment outlook for the near and long term; significant changes in the portfolio during the preceding period; and the reasons for any significant differences between the performance of their portfolios and the appropriate market indices or metrics.
4. To make themselves available as needed for meetings with the Board, staff, or agents of the Board regarding investment matters.
5. To comply at all times with all laws, regulations, contractual investment guidelines, and reporting requirements as determined by staff.

6. To perform such additional activities as detailed in each manager's investment management agreement with SERS.

E. General Investment Consultant

The Board's general investment consultant acts as a fiduciary to the Fund, providing reports to the Board on emerging trends and issues of concern to public pension funds generally and to the Fund in particular. The general investment consultant also analyzes and makes recommendations with respect to the Board's asset allocation and investment structure, policies, the investment managers' implementation of policy and strategy, the appropriate investment horizon for the Fund given its actuarial characteristics, and provides such other research as may be required from time to time.

In addition to the general investment consultant, the Board may retain other investment consultants as required for specialized needs, such as for particular asset classes or unique investment projects. These specialty consultants will report to the Board on emerging trends and issues that are germane to their respective assignments and that are of concern to public pension funds generally and to the Fund in particular. Within the scope of their assignments, the specialty consultants will also analyze and make recommendations with respect to this Policy, the investment managers' implementation of policy and strategy, and provide such other research as may be needed from time to time.

The general and specialty consultants should be free of conflicts of interest or, where they potentially exist, make complete and total disclosure to the Board and obtain pre-clearance from the board.

F. Private Equity Consultant

The private equity consultant acts as a fiduciary to the Fund, and will provide non-discretionary private equity consulting services. The private equity consultant will assist staff in performing due diligence investigations on prospective private equity and private debt investment opportunities, assist staff with identifying and accessing investment opportunities, recommend specific private equity investments to SERS, and maintain a deal log of private equity investment opportunities. The private equity consultant will also participate in the development and refinement of private equity policies, objectives, strategies, benchmarking, risk assumptions, and asset mix appropriate for each sub-asset class; as well as perform qualitative and quantitative portfolio oversight procedures and prepare performance measurement. The private equity consultant will make presentations to the Board supporting investment recommendations as they arise, and review performance at least semi-annually.

The private equity consultant should be free of conflicts of interest or, where they potentially exist, make complete and total disclosure to the Board and obtain pre-clearance from the Board.

G. Real Estate Consultant

The real estate consultant acts as a fiduciary to the Fund, and will provide non-discretionary real estate investment consulting services. The real estate consultant will assist staff in performing due diligence investigations on prospective real estate opportunities, assist staff with identifying and accessing investment opportunities, recommend specific real estate investments to SERS, and maintain a real estate database. The real estate consultant will also

participate in the development and refinement of real estate policies, objectives and strategies, benchmarking, risk assumptions, and asset mix appropriate for each sub-asset class; as well as perform qualitative and quantitative portfolio oversight procedures and prepare performance measurement. The real estate consultant will make presentations to the Board supporting investment recommendations as they arise and review performance at least semi-annually.

The real estate consultant should be free of conflicts of interest or, where they potentially exist, make complete and total disclosure to the Board and obtain pre-clearance from the Board.

H. Portfolio Evaluation Advisor

The general investment consultant, or another third party approved by the Board as a portfolio evaluation advisor, will provide quarterly investment performance evaluation and analysis to the Board. The portfolio evaluation advisor will provide the Board with comparative performance measurements against appropriate benchmarks at the total fund, asset class, sub-asset class, and advisor levels for all asset classes (except real estate and private equity investments).

These benchmarks will be defined and presented in each quarterly performance report. They are hereby incorporated by reference.

I. State Treasurer

The State Treasurer serves as the custodian of the Fund, pursuant to Title 71, Pennsylvania Consolidated Statutes, Section 5931(c). In this capacity, the State Treasurer is responsible for the safe physical custody of investment instruments and the safe custody of any book-entry investment instruments that are held in depositories on behalf of the Commonwealth. As custodian, the State Treasurer is also responsible for preparing and delivering securities for settlement as authorized by the Board, attending to corporate actions, maintaining a book of record for these securities, facilitating an annual examination of these securities and books, and for preparing payment for securities transactions upon presentation of warrants properly signed and authorized. The State Treasurer may enter into a contract with a sub-custodian bank to assist in the execution of these responsibilities.

The State Treasurer is responsible for the temporary investment of cash balances until funds are required to meet disbursements or to acquire investments.

J. Actuarial Consultant

Pursuant to Title 71, Pennsylvania Consolidated Statutes, Section 5902(j), the Board engages an actuary to perform a valuation of the various accounts of SERS on an annual basis within six months of the close of each calendar year. In every fifth year, the Board shall have the actuary conduct an actuarial investigation and evaluation of the system based on data including the mortality, service, and compensation experience provided by the Board annually during the preceding five years concerning the members and beneficiaries.

5. Investment Objectives

The State Employees' Retirement Fund is a mature pension plan. The appropriate investment horizon is intermediate to long-term (five to ten years) with due consideration of the characteristics of the Fund's liabilities and liquidity requirements.

The objectives of the Fund are to provide benefit payments to participants and beneficiaries at the lowest cost to the Commonwealth and to fund the program through a carefully planned and executed investment program.

The Fund seeks to produce the highest return on investment that is consistent with acceptable investment risks and sufficient liquidity that will permit the Fund to meet the System's benefit obligations, and secondarily, control the cost of the Fund to the taxpayers. The investment program is premised on modern portfolio theory. The Board recognizes that many asset classes and investments can have volatile performance and that the Fund may not achieve investment results over shorter time periods. However, over longer time periods, a well-constructed portfolio and mix of asset classes will provide the optimal results.

The Board, with the help of the staff and consultants, is charged with building a portfolio by carefully assessing the risk and return potential of the global capital markets, and making those investments that are institutionally investable and are reasonably expected to contribute to the Fund's long-term objectives and goals.

Consistent with achieving these objectives, the Board has established the following goals relative to investment performance:

- Achieve a net total return equivalent to the actuarial interest rate assumption, or preferably, in excess of this rate in order to improve the funded ratio of the Fund through investment earnings and favorably impact future employer and employee contribution rates.
- Achieve a net, total long-term return that meets or exceeds an appropriate, composite plan benchmark index on a five-to ten-year rolling time horizon. The composite benchmark index will be based on the asset allocation set forth in the Investment Plan approved by the Board.

A. Rebalancing Policy

The primary strategic objectives of rebalancing the Fund are to mitigate risk and enhance returns while meeting the liquidity needs of SERS. The specific risk mitigation objective is to keep the asset allocation and overall investment structure of the Fund consistent with the Investment Plan and the policy asset allocation and asset class goals contained within it. Due to changes in market movements, actual asset class balances will inevitably deviate from target allocations. These deviations cause the Fund to diverge from the asset allocation chosen by the Board and the expected risk and return attributes associated with it. This divergence, or tracking error, heightens the risk that the Fund may not achieve returns sought by the Board at the risk levels they deem prudent. The Investment Office will have authority to rebalance asset class exposures as necessary and prudent pursuant to the rebalancing policy which is incorporated by reference into this policy.

6. Investment Guidelines

The allocation of funds to various types of investments is of utmost importance in structuring an efficient portfolio designed to meet the Fund's investment objectives. In order to assure the most beneficial allocation of funds, the Board shall, with the advice of SERS' investment staff, consultants, and investment managers, adopt an Investment Plan that will be revised and updated periodically but not less than every two years. This plan will set forth the long-term allocation ranges for the asset classes and identify work initiatives to be pursued over the near term. Furthermore, each investment manager shall abide by specific investment guidelines that will be consistent with this Policy and the Investment Plan so

as to ensure that the Fund's broad investment objectives will be met. The managers' specific investment guidelines may be amended from time to time by mutual written consent of the staff and the manager.

If at any time the economic, fiscal, or investment environment should change significantly during the investment horizon, it shall be the duty of the staff, investment managers, and consultants to so inform the Board and, if warranted, recommend modifications to the Investment Plan or adjustment to the allocation of investment assets.

In the application and implementation of this Policy and the Investment Plan, the Chief Investment Officer in consultation with the Board Chairman, has the authority to make investment decisions on behalf of the board in emergency situations. Emergency situations are defined as those that are unforeseeable and in the absence of action taken, the Fund may be adversely impacted. In the event such action is taken, the Board will be apprised as soon as practical, but no later than the next scheduled board meeting.

7. SERS Emerging Investment Manager Program (“SERS EIM Program”)

A. Objective

Consistent with the Board's fiduciary responsibilities, the Board has established the SERS EIM Program to:

1. Identify and gain early access to talented investment managers in their early stages to generate above benchmark returns (net of fees); and
2. Provide an evaluation platform of potential investment managers who have demonstrated superior risk-adjusted returns for consideration into the Fund.

B. Scope

The SERS EIM Program shall apply to emerging investment managers who manage long-only public equity assets.

C. Structure and Standards

The SERS EIM Program will be comprised of manager-of-managers selected in accordance with SERS' Hiring Investment Manager Process. The manager-of-managers will have the discretion and authority to select and invest with emerging investment managers based on the objectives and guidelines established by the Board and SERS' Investment Office. As part of SERS' Hiring Investment Manager Process, manager-of-managers' fees shall be disclosed to the Board for evaluation.

D. Emerging Investment Manager Criteria

Investment managers selected by the manager-of-managers to participate in the SERS EIM Program must meet the following criteria:

- Registered under the Investment Advisors Act of 1940 or has an exemption from registration (and will maintain such registration or exemption);
- Total firm assets under management of less than \$5 billion and/or an investment strategy of less than \$1 billion at the time of SERS' initial evaluation;

- A measureable track record for the investment product under consideration (or for a product with a similar investment philosophy and process as the product under consideration);
- Portfolio manager(s) with a minimum two-year track record (directly or indirectly attributable to that portfolio manager(s)) in an investment style and process similar to that which is under consideration;
- Historical performance must be CFA Institute compliant; and
- Disclosure of position and transaction level transparency (at least monthly).

As indicated in Section 4 of this Policy, “[t]he Board may, when possible and consistent with its fiduciary duties imposed by law, including its obligation to invest and manage the Fund for the exclusive benefit of the members of the System, consider whether an investment in any project or business enhances and promotes the general welfare of the Commonwealth and its citizens. Where investment characteristics are equivalent, the Board’s policy will favor investments that will have a positive impact on the economy of Pennsylvania.”

Therefore, when making their selections, manager-of-managers may favor emerging investment managers who meet the SERS EIM Program objectives and criteria noted above, plus having one or more of the following characteristics:

- Pennsylvania investment management firms headquartered or incorporated within the Commonwealth; and/or
- Investment management firms owned and/or controlled by a majority of persons who are women and/or minorities.

E. Administration

The Investment Office shall be responsible for the oversight of the SERS EIM Program by recommending program policies and manager-of-managers for the Board’s consideration.

F. Source of Funding

Funding for the SERS EIM Program may come from assets within SERS’ Global Public Equity asset class or cash at the Board’s sole discretion, depending on the current equity allocation relative to the target allocation.

8. Prohibited Transactions

Investment managers are prohibited from entering into any transactions on behalf of the Fund that are not expressly authorized by this Policy or by specific investment manager guidelines and all applicable laws and regulations. All managers and consultants shall disclose any and all economic positions that may conflict with SERS’ investment objectives and guidelines.

9. Investment Manager Evaluations

The Board endeavors not to make adverse retention decisions about investment managers based upon performance absent at least three years of performance data, recognizing that investment strategies are best assessed over full market cycles.

The Board's time horizon to review performance trends shall normally be over full market cycles, although the trend in investment experience over other time periods may be judged important. Any extreme or unusual events or trends will be considered when evaluating intermediate and short-term investment results. The Investment Manager Monitoring Policy has been developed in order to assist staff in applying consistent criteria to evaluate investment managers.

Notwithstanding the above, the staff will review manager performance, portfolio positioning, and transactions at least annually.

10. Corporate Governance Standards

Good corporate governance promotes responsible business practices that serve as an integral component to a corporation's long-term value creation process and are an indispensable element of an effective corporate risk management program.

SERS is committed to improve corporate governance practices of the companies within the SERS portfolio. SERS' involvement includes: the development and periodic updating of the Board approved proxy-voting policy, voting proxies, active participation in groups working to improve and enhance corporate governance practices, and ad hoc responses to important issues that affect the value of the portfolio, such as letters responding to regulatory and legislative proposals.

The proposed updates to the proxy voting policies shall be prepared by the Investment Office and submitted to the Board for approval. In the update of the policies, the Investment Office shall seek to develop best practices. Best practices shall be developed through relationships with groups working to improve and enhance corporate governance practices and input that focuses on improving corporate governance practices from other prominent plan sponsors.

In addition, SERS monitors and, where appropriate, incorporates best corporate governance practice recommendations from organizations into the proxy voting guidelines. As good corporate governance practices are not static, the annual proxy voting modifications are designed to reflect the current trends in the marketplace.

A. Proxy Voting Procedures

Stock proxies are voted in accordance with the following procedures:

1. The custodian bank forwards to SERS' proxy servicer or manager proxy statements for securities that SERS owns, excluding securities that are on loan, or investments in the form of pooled funds and limited partnerships.
2. SERS' proxy servicer or manager will vote all proxies in accordance with the Board's proxy voting guidelines, except those where a specific concern has been raised by a Board Member, manager, consultant, or staff member.

3. The proxy servicer or manager may also vote any proxy involving other issues essentially the same as those on which the Board's proxy voting guidelines are well defined.
4. With regard to proxies requiring special attention under the Board's proxy voting guidelines, as well as special issues not covered or anticipated by the proxy voting guidelines, proxies and all pertinent reference material shall be sent to the Chief Investment Officer, who will evaluate the issues with respect to the intent of the proxy voting guidelines. On issues not covered by the proxy voting guidelines, controversial, high-profile, and contested change of control issues, the Chief Investment Officer will consult with the Board's chairman to determine how such proxies will be voted. The Chief Investment Officer will then direct the proxy servicer or manager to vote the proxies accordingly.
5. The Chief Investment Officer shall regularly report to the Board the types of special issues that are being considered or that have been voted by the Chief Investment Officer.
6. The Chief Investment Officer shall cause to be maintained by SERS' proxy servicer, or manager, a listing of proxy votes cast in a calendar year. This report, along with all individual actions, shall be available for public inspection on SERS' Internet web site.

B. Corporate Actions

The custodian bank has standing instructions to forward notices of all corporate actions received, such as dividends, stock splits, mergers, acquisitions, spin-offs, or class action suits to SERS and/or its investment managers.

11. Trading and Brokerage Practices

The Board delegates the responsibility for the selection of brokerage firms to its investment managers, provided the investment managers select and utilize brokers in accordance with Section IV, D-2 ("best execution") of this Policy. Notwithstanding this practice, the Board reserves the right to enter into brokerage commission recapture programs, and to establish goals for directed commissions provided the managers' investment processes are not being affected so as to adversely impact the Fund or place the Fund in a disadvantageous position relative to the managers' other accounts. As such, managers may be requested to direct a percentage of their brokerage activity on behalf of SERS. The Board will select the brokerage firms that are designated to receive such directed commissions, and will communicate this information to the managers.

The Board also seeks to have managers direct trades through minority owned firms and reserves the right to establish proposed trading targets. However, the responsibility for the selection and use of minority brokerage firms is delegated to the investment managers.

Finally, all things being equal, the Board seeks to have investment managers trade through Pennsylvania-based brokers.

Efforts to monitor and control trading costs will be ongoing, and may include the periodic use of formal trading cost analyses.

12. Public Access to Records

Records of investment transactions are maintained by the System at its office located at 30 North Third Street, Harrisburg, PA 17101. Requests for public inspection or copies of documents that are a matter of public record will be honored in a manner consistent with the Pennsylvania Right-to-Know Law (RTKL), 65 P.S. §§ 101 - 3104, and SERS' Right-To-Know Law Policy regarding the dissemination of public information. Inquiries should be directed to SERS' Right-to-Know Law Open-Records Officer. This Right-to-Know Law Policy is incorporated by reference into this Policy.

13. Procedures for Amending this Policy Statement

This Policy may be amended from time to time by a majority vote of the Board.

14. Separate Documents Related to this Policy Statement

The following documents are incorporated by reference into this Policy and as such are considered part of this Policy as though they were presented in entirety within this Policy:

1. SERS' Investment Plan
(adopted by the Board)
2. Public Markets Investment Manager Investment Strategy Statements
(negotiated as part of the contracting process after Board appointment)
3. Real Estate Statement of Investment Policy
(adopted by the Board)
4. Private Equity Statement of Investment Policy
(adopted by the Board)
5. U.S. and International Proxy Voting Policy
(adopted by the Board)
6. Investment Manager Monitoring Policy
(reviewed by Board)
7. Right-To-Know Law Policy
(adopted by the Board)
8. Derivatives Investment Policy Statement
(reviewed by Board)
9. Portfolio Rebalancing Policy
(adopted by Board)
10. Investment Manager, Asset Class, and Fund Benchmarks as reported in the Quarterly Performance Report
(reviewed by Board)
11. SERS' Securities Litigation Policy
(adopted by Board)
12. SERS' Securities Lending Policy
(reviewed by Board)

15. Glossary of Terms

Asset Allocation – Investment choice made among broad asset classes such as equities, fixed income securities, real estate, etc.

Asset Liability Study - A study that examines how well alternative investment strategies (differing asset allocations) address the objectives of a fund, specifically the fund’s “liabilities”. The study acts as a guidepost for the strategic asset allocation.

Brokerage Commission – Payment for administrative costs of trading securities; the cost for execution.

Brokerage Commission Recapture – Reimbursement to the Fund for a portion of the fee paid to a broker for executing a trade.

Comprehensive Annual Financial Report (CAFR) - A set of U.S. government financial statements comprising the financial report of a state, municipal or other governmental entity that complies with the accounting requirements outlined by the Governmental Accounting Standards Board.

Corporate Governance – The procedures by which a corporation conducts its affairs.

Corpus –Specifically, the investment portfolio of SERS.

Fiduciary – A fiduciary is a legal or ethical relationship of trust between two or more parties where one party has undertaken to act for and on behalf of another party in a particular matter in circumstances which give rise to a relationship of trust and confidence.

Funded Ratio - The ratio of a pension’s assets to its liabilities. A funded ratio greater than 100% indicates the pension has accumulated more assets than its liabilities. A funded ratio less than 100% indicates the pension does not have enough assets to cover its liabilities.

Net Total Return – Interest or dividend income plus any realized or unrealized capital gain (or loss) on an investment, net of any capital contributions or distributions from the corpus.

Proxy – An instrument empowering an agent to vote for a shareholder.

Qualitative Oversight – Analysis that evaluates important factors that cannot be precisely measured, e.g., experience, caliber of management, investment philosophy and strategy.

Quantitative Oversight – Analysis dealing with measurable factors, such as value of securities, the cost of capital, historical and projected patterns of sales, costs, profitability, returns, risk. Used in tandem with qualitative oversight to arrive at sound business and financial judgments.

Risk – The uncertainty of outcome or the likelihood of not meeting an objective.

Sarbanes Oxley Act - Congress passed the Sarbanes Oxley Act in 2002 that mandated new or enhanced standards for all U.S. public company boards, management and public accounting firms to improve financial disclosures in order to protect investors from the possibility of fraudulent accounting activities by corporations.

Tracking Error – The annual standard deviation of a manager’s performance results in comparison to the manager’s benchmark.

16. Appendix I

Title 71, Pennsylvania Consolidated Statutes, 5931. Management of fund and accounts.

(a) Control and management of fund.--The members of the board shall be the trustees of the fund. Regardless of any other provision of law governing the investments of funds under the control of an administrative board of the State government, the trustees shall have exclusive control and management of the said fund and full power to invest the same in accordance with the provisions of this section, subject, however, to the exercise of that degree of judgment, skill and care under the circumstances then prevailing which persons of prudence, discretion and intelligence, who are familiar with such matters, exercise in the management of their own affairs not in regard to speculation, but in regard to the permanent disposition of the funds, considering the probable income to be derived therefrom as well as the probable safety of their capital. The trustees shall have the power to hold, purchase, sell, lend, assign, transfer or dispose of any of the securities and investments in which any of the moneys in the fund shall have been invested as well as of the proceeds of said investments, including any directed commissions which have accrued to the benefit of the fund as a consequence of the investments, and of any moneys belonging to said fund, subject in every case to meeting the standard of prudence set forth in this subsection.

(b) Crediting of interest.--The board, annually, shall allow the required interest on the mean amount for the preceding year to the credit of each of the accounts. The amount so allowed shall be credited thereto by the board and transferred from the interest reserve account.

(c) Custodian of fund.--The State Treasurer shall be the custodian of the fund.

(d) Payments from fund.--All payments from the fund shall be made by the State Treasurer in accordance with requisitions signed by the secretary of the board, or his designee, and ratified by resolution of the board.

(e) Fiduciary status of board.--The members of the board, employees of the board and agents thereof shall stand in a fiduciary relationship to the members of the system regarding the investments and disbursements of any of the moneys of the fund and shall not profit either directly or indirectly with respect thereto. The board may, when possible and consistent with its fiduciary duties imposed by this subsection or other law, including its obligation to invest and manage the fund for the exclusive benefit of the members of the system, consider whether an investment in any project or business enhances and promotes the general welfare of this Commonwealth and its citizens, including, but not limited to, investments that increase and enhance the employment of Commonwealth residents, encourage the construction and retention of adequate housing and stimulate further investment and economic activity in this Commonwealth. The board shall, through the Governor, submit to the General Assembly annually, at the same time the board submits its budget covering administrative expenses, a report identifying the nature and amount of all existing investments made pursuant to this subsection.

(f) Name for transacting business.--By the name of "The State Employees' Retirement System" or "The State Employees' Retirement System" all of the business of the system shall be transacted, its fund invested, all requisitions for money drawn and payments made, and all of its cash and securities and other property shall be held, except that, any other law to the contrary notwithstanding, the board may establish a nominee registration procedure for the purpose of registering securities in order to facilitate the purchase, sale or other disposition of securities pursuant to the provisions of this law.

(g) Deposits in banks and trust companies.--For the purpose of meeting disbursements for annuities and other payments in excess of the receipts, there shall be kept available by the State Treasurer an amount, not exceeding 10% of the total amount in the fund, on deposit in any bank or banks in this Commonwealth organized under the laws thereof or under the laws of the United States or with any trust company or companies incorporated by any law of this Commonwealth, provided any of such banks or trust companies shall furnish adequate security for said deposit, and provided that the sum so deposited in any one bank or trust company shall not exceed 25% of the paid-up capital and surplus of said bank or trust company.

(h) Venture capital, private placement and alternative investments.--The board in its prudent discretion may make any venture capital investment, private placement investment or other alternative

investment of any kind, structure or manner which meets the standard of prudence set forth in subsection (a).

(i) Vehicles for authorized investments.--The board in its prudent discretion may make any investments which meet the standard of prudence set forth in subsection (a) by acquiring any type of interest in a business organization existing under the laws of any jurisdiction, provided that, in any such case, the liability of the State Employees' Retirement Fund shall be limited to the amount of its investment.

(j) Legislative declaration concerning certain authorized investments.--The General Assembly finds and declares that authorized investments of the fund made by or on behalf of the board under this section whereby the board becomes a joint owner or stockholder in any company, corporation, association or other lawful business organization are outside the scope of the original intent of and therefore do not violate the prohibition set forth in section 8 of Article VIII of the Constitution of Pennsylvania. (Oct. 7, 1975, P.L.348, No.101, eff. imd.; Mar. 4, 1982, P.L.141, No.45, eff. imd.; June 29, 1984, P.L.450, No.95, eff. imd.; Aug. 5, 1991, P.L.183, No.23, eff. imd.; Apr. 29, 1994, P.L.159, No.29, eff. imd.; Dec. 20, 1995, P.L.689, No.77, eff. imd.; May 17, 2001, P.L.26, No.9, eff. imd.)

2001 Amendment. Act 9 amended subsecs. (h), (i) and (j). See section 24 of Act 9 in the appendix to this title for special provisions relating to authorized investments.

1994 Amendment. See section 14 of Act 29 in the appendix to this title for special provisions relating to authorized investments of the State Employees' Retirement Board as described in subsec. (i).

Cross References. Section 5931 is referred to in section 5102 of this title; section 5611 of Title 53 (Municipalities Generally).