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RETIREMENT SYSTEMS DIRECTOR**Memorandum**

To: The North Carolina Supplemental Retirement Board of Trustees
From: Mary Buonfiglio, Deputy Director, Supplemental Retirement Plans
Date: May 9, 2016
Subject: Investment Guideline Compliance Reporting

A primary goal of the supplemental retirement plans (SRP) unbundling project was to enhance the compliance monitoring of Investment Manager Guidelines. Historically, guidelines were monitored quarterly at a “point in time” with Mercer Investment Consulting coordinating activities across several SRP service providers. While effective, this process was manual and represented a “snapshot” at the end of each quarter.

Working directly with BNYM, SRP staff can now leverage an automated system that provides daily, real-time insight into the SRP portfolios at the issue, industry, sector and country level. Not only does this enhance our ability to monitor guidelines, but it provides a clear “view” into how each portfolio is being managed.

During the first quarter, the primary objective was to ensure the compliance monitoring system was set up correctly and to implement the DST statewide Iran Divestment Policy across the portfolios.

First quarter milestones include:

1. Performance and Risk Analytics Agreement between NC SRP and BNY Mellon was signed on January 4, 2016. The agreement includes the compliance monitoring service.
2. Shortly thereafter, NC SRP staff provided the BNYM Global Risk Solutions (GRS) team with investment guidelines for all active, separately managed portfolios. BNYM GRS began programming their compliance system with the guidelines. The first sample report was received by the NC SRP staff on February 25.
3. Throughout March, meetings were held between NC SRP and BNYM Mellon GRS staff to finalize the report format.
4. Initial internal compliance review procedure was established: SRP Compliance Officer will coordinate with IMD Portfolio Manager and Senior Analyst in order to identify new exceptions, contact the managers in breach of guidelines to define, implement and monitor resolution.
5. The Policy resulting from the Iran Divestment Act of 2015, effective February 26, 2016 was implemented.
 - a. The Act Prohibits:
 - The North Carolina Retirement Systems or the Department of State Treasurer from investing funds with individuals or companies engaging in certain defined investment activities in Iran.

- State agencies, local government units, and other political subdivisions of the State from contracting with individuals or companies on the Department of State Treasurer's Final Divestment List.

The DST Iran Divestment Policy was provided to BNYM GRS and upon review, BNYM team requested that Bloomberg security identifiers be provided to aid in correct programming of the prohibited securities (currently, the policy lists only company names). NC SRP staff worked with IMD and OST policy team to obtain ISIN numbers, as Bloomberg identifiers were not readily available from the vendor, Sustainalytics.

- 29 individual ISINs were added to the compliance monitoring system; this list encompasses Iranian "do not hold" as well as "be informed" holdings and will expand in the future: NC SRP staff continues to coordinate with IMD/OST staff in the matter.
- BNYM also custodies the NC DST defined benefit plan assets and it was discovered that two policies applicable to DB plan only, Sudan Divestment and Payday Lending, crossed over to the defined contribution plan compliance monitoring. Both BNYM and NC SRP teams are currently working to remedy the situation.

A summary compliance monitoring report will be presented to the Supplemental Investment Subcommittee quarterly for review. This report will indicate what breaches, if any, have occurred over the course of the quarter and the status of error resolution.