

San Jose Police and Fire Department Retirement Plan

Private Markets Manager Due Diligence

December 10, 2024

California Government Code - GOV § 6254.26

(a) Notwithstanding any provision of this chapter or other law, the following records regarding alternative investments in which public investment funds invest shall not be subject to disclosure pursuant to this chapter, unless the information has already been publicly released by the keeper of the information:

- (1) Due diligence materials that are proprietary to the public investment fund or the alternative investment vehicle.
- (2) Quarterly and annual financial statements of alternative investment vehicles.
- (3) Meeting materials of alternative investment vehicles.
- (4) Records containing information regarding the portfolio positions in which alternative investment funds invest.
- (5) Capital call and distribution notices.
- (6) Alternative investment agreements and all related documents.

Key Elements of Private Markets Strategy

1. **Ensure beta exposure above all else.**

Failure to execute the pacing plan guarantees not meeting objectives envisioned within the asset allocation.

Implication is that consistent commitments and vintage diversification matter more than anything else, including manager selection.

2. **Alpha is an outcome of process.**

Sources of alpha can be picking: better sub-sectors (beta timing), managers who are better at choosing the right investments (security selection), manager who operate more effectively (value creation), capital structure optimization (risk decomposition).

Consistently harvesting alpha from those sources requires a competitive advantage relative to all sources of private capital, which must be deliberately developed and maintained.

3. **Alignment of interests can overwhelm most other investment factors.**

Long-term illiquid commitments require careful due diligence and selection of partners.

Agency conflicts increase with (a) distance from the asset and (b) dispersion of ownership.

Fees are the result of a buy-versus-build decision and market forces.

Investment Constraints

California Public Pension Status

California public pension plans have transparency requirements in accordance California government code. These requirements are limiting to the extent that (a) certain investment managers do not want to be subject to such disclosures; and (b) Board and staff risk appetites can be altered by non-economic forces, such as headline risk.

Governance

- Investment Policy Statement
- Minimum qualifications – registered under Advisor’s Act or similar legislation unless it is exempt, fiduciary standard, nature and size of mandate consistent with asset allocation, concentration limits (strategy, transaction, pacing plan).

Resources

The availability and reliability of resources has the largest impact on strategy and execution, and includes:

- Time – the only resource that cannot be enhanced;
- Capabilities – personnel, external advisors, technology;
- Budget – the constraint on enhancing capabilities.

Private Markets Asset Classes

Buyout



- Large Buyout
- Small-/Mid- Buyout
- Special Situations
- Other

Equity investments in growing, established, and mature companies, with enterprise values generally ranging from \$20mm to \$20bn.

Venture



- Early Stage
- Mid Stage
- Late Stage
- Diversified

Primarily equity investments in start-ups and high growth companies.

Debt



- Par Credit
- Securitized
- Stress/Distress
- Other

Debt investments include credit expected to pay back original principal and interest (par credit), loans and bonds that have been packaged into special purpose vehicles (securitized), securities where the obligor is in a stressed or distressed financial situation (stress/distress), and unique strategies that have some or all the characteristics of debt investments.

Real Estate



- Value-Added
- Opportunistic
- Real Estate Debt
- Other

Equity and debt investments in operating companies and physical properties where the economic value is derived primarily through real estate-related activities. Value-added and opportunistic are distinguished by the level of risk associated with an investment.

Real Assets



- Infrastructure
- Energy
- Natural Resources
- Other

Investments in operating companies and physical assets where the economic value is derived primarily from the development, production, transport, or processing of natural resources, and the facilities supporting their downstream progress.

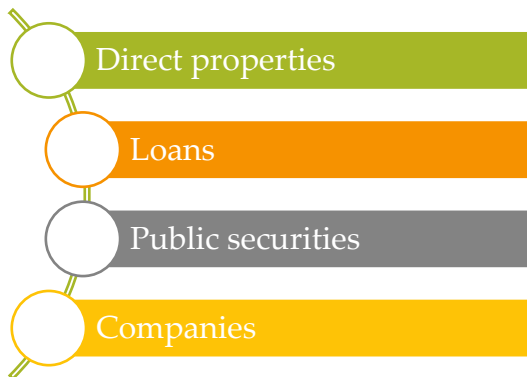
Due Diligence – Desired Exposures



Sector



Geography



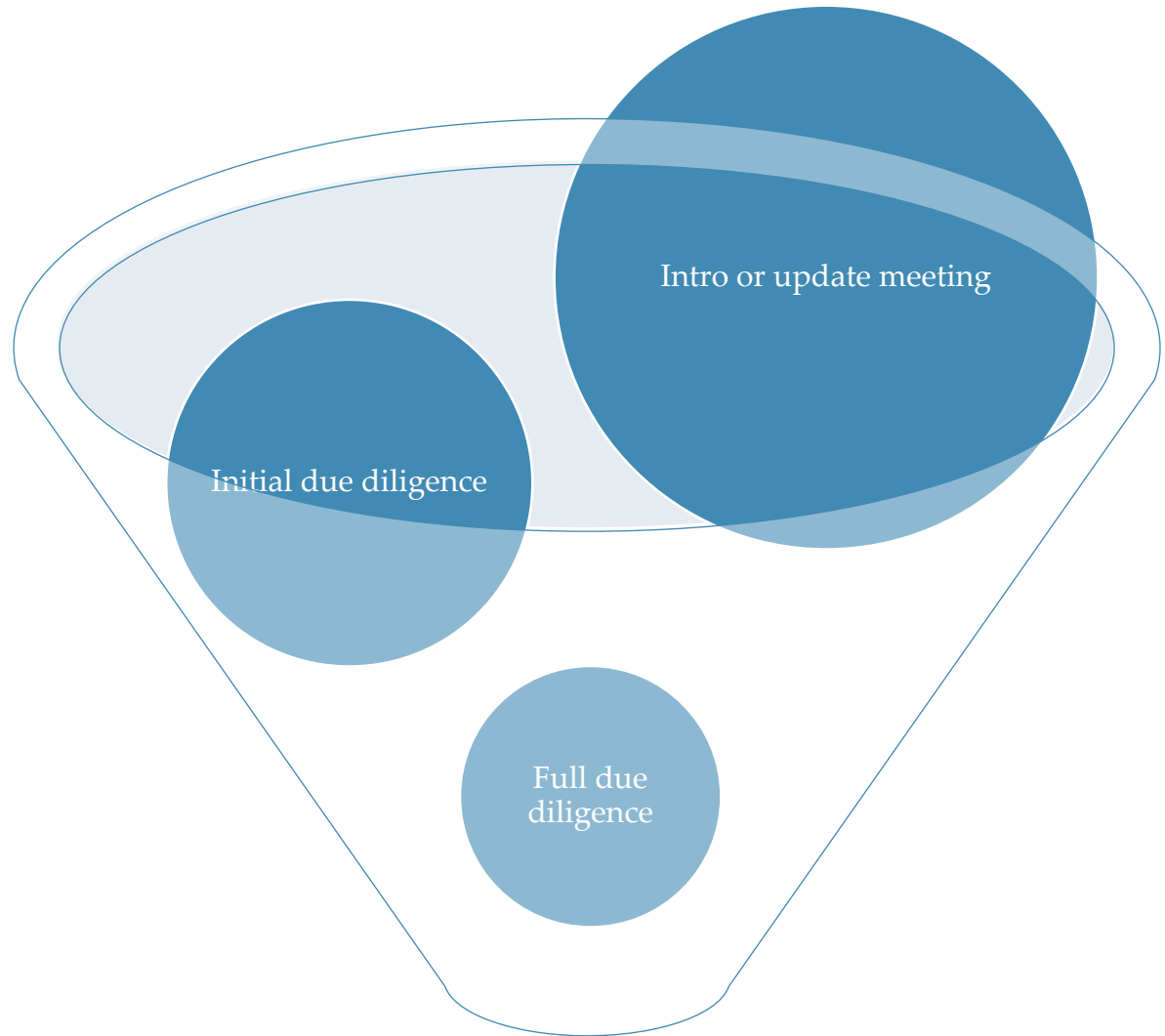
Investment Type



Risk Profile

Due Diligence – Sourcing

- Relationships
- Unsolicited introductions
- Consultants
- Peers
- Industry organizations
- Pitchbook
- eVestment



Due Diligence – Evaluation

- Data room materials
- Using information advantages
- ILPA due diligence tools
- Performance appraisal
- Meet team members at various levels of the firm
- Supplemental data requests
- Negotiate terms
- Fund scoring matrix

Net IRR	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
Manager A															
Manager B															
Manager C															
Manager D															
Manager E															
Manager F															
Manager G															
Manager H															
<i>Burgiss Real Estate Median</i>															

Scoring Matrix	Weaker					Stronger
Investment	1	2	3	4	5	
Team	1	2	3	4	5	
Timing	1	2	3	4	5	
Risk	1	2	3	4	5	
Terms	1	2	3	4	5	
Fees	1	2	3	4	5	
Transparency	1	2	3	4	5	
Control	1	2	3	4	5	

Appendix

Pacing Plan

	FY 23-24		Pacing Plan				
	<u>Pacing Plan</u>	<u>Actual</u>	<u>FY 24-25</u>	<u>FY 25-26</u>	<u>FY 26-27</u>	<u>FY 27-28</u>	<u>FY 28-29</u>
Buyout	100	100	150	150	125	125	125
Venture Capital	35	58.5	35	35	35	35	35
Private Debt	64	63	80	80	90	90	100
Growth Real Estate	70	-	70	70	75	75	75
Private Real Assets	60	46	60	55	55	55	50
Total Private Markets	329	267.5	395	390	380	380	385

Values in \$ millions

IPS – Manager Selection Policy

VII. Manager Selection, Retention, Evaluation & Termination Policy

Background

- A. The Board has delegated to the CIO the authority to select and terminate all investment managers of the Plan subject to constraints and parameters contained herein. Such authority shall be further subject to Manager Selection, Retention, Evaluation & Termination Procedures (“Procedures”), approved by the CIO, that provide more detailed constraints and parameters.
- B. It is the Board’s intention that the CIO shall have the necessary authority and resources to effectively select, retain, evaluate, and terminate investment managers with the exception of co-investments (due to the investment concentration risk of co-investments). This exception does not pertain to funds where an external manager has discretion.
- C. Accordingly, the CIO shall have the authority to:
 - 1. Manage the Investment Personnel of the System, including:
 - a. Recommending to the CEO the appointment and duties of all professional, technical, and clerical employees of the Investment Division;
 - b. Directing and supervising all Investment Personnel on a day-to-day basis; and
 - c. Evaluating all Investment Personnel and managing their professional development.

IPS – Manager Selection Policy cont'd

2. Select and terminate investment consultants to assist in the selection, retention, evaluation, and termination of investment managers.
 - a. The CIO may use the services of the general investment consultant appointed by the Board. Alternatively, if the services of the general consultant can be unbundled to separate manager research services, the CIO may select a consultant(s) of his or her choice to carry out manager research services that would otherwise have been included in the general investment consultant scope of services.
 - b. The CIO shall ensure that the total fees and expenses associated with the consultants he or she selects are reasonable and shall provide a report of such fees and expenses to the Investment Committee and the Board on at least a quarterly basis.
 - c. While the CIO shall have the authority to select and terminate investment consultants to assist staff in selecting, retaining, evaluating and terminating investment managers, the Board shall approve all contracts with investment consultants selected by the CIO to ensure such contracts reflect fair and reasonable value for the Plan.
3. Delegation of authority to the CIO to select and terminate investment managers reflects the Board's desire to:
 - a. Promote efficiency and effectiveness in the manager selection and termination processes;
 - b. Focus the Board's time and attention on investment policy, asset allocation, and oversight, rather than manager selection and termination; and
 - c. Establish clear accountability on the part of the CIO and investment staff for manager selection, retention, evaluation, and termination.

IPS – General Constraints and Parameters

General Constraints and Parameters

- A. The CIO's authority to select and terminate investment managers shall be subject to the following general constraints and parameters:
1. Investment managers shall meet the following **minimum qualifications** to be selected to manage any assets of the fund:
 - a. Be **registered as an investment advisor** under the Investment Advisor's Act of 1940 or comparable legislation, unless the manager represent and warrants that it is exempt from such registration under applicable law.
 - b. Agree to enter into a contract with the Plan requiring them to perform their services consistent with the fiduciary services established under (a) the Investment Advisor's Act of 1940; (b) California law applicable to fiduciaries of public employee retirement systems, which includes the California State Constitution, Art. XVI sec. 17 and the San Jose Municipal Code and/or (c) terms and conditions substantially comparable to the foregoing that are satisfactory to the Plan.
 2. The nature and size of the manager's mandate shall be consistent with:
 - a. The asset allocation policy of the Plan;
 - b. Applicable constraints (e.g. **manager or strategy concentrations**) contained in this Investment Policy Statement; and the total Plan **active risk limit(s)¹ contained in the risk section of this IPS.**

IPS – Limits

3. Notwithstanding paragraph 2) b) above, the CIO shall not approve the selection of an investment management firm for mandates that exceed the following limits:

Basis*	Description	Strategy Limit ²
Vehicle	Separately managed accounts (active)	15%
	Commingled funds and SMAs (public, passive)	No limit ³
	Commingled funds (public, active)	15%
	Commingled funds (hedge funds)	15%
	Commingled funds (private strategies)	15% ⁴
Public Markets ⁵	Passive strategies	No limit
	Active strategies	15%
Private Markets		Transaction Limit⁶
	Total \$ commitment to asset class (e.g. Private Debt)	150% of Board-approved pacing plan (cumulative) ⁷
	Primary fund commitment (1st allocation to mgr.)	2%**
	Primary fund commitment (follow-on)	3%**
	Secondary fund investment	1%**

¹ Active risk or tracking error limits may apply at the total fund level, or another aggregation (e.g. public markets assets only, excluding private markets). Risk limits may also be based on concentration, expressed for example, as a percentage (%) of some total amount of risk.

² Percentage (%) of total Plan assets allowable per investment strategy

³ Rationale: Fund is constrained by the asset allocation. This is the “default” option for investing, and scale determines pricing.

⁴ For private strategies, limit applies to the capital invested plus future callable commitments.

⁵ Some of these limits related to public markets may be “interim”, to be replaced by risk-based limits for example.

⁶ Percentage (%) of total Plan assets allowable per investment manager.

⁷ This would allow, for example, a commitment in Year 1 that is 50% above “plan”. The “cumulative” provision would allow for a “catch-up” for any slower-than-planned investments in prior years.

* To be selected, the manager must satisfy the “Vehicle” constraint and the appropriate “Public Markets” or “Private Markets” constraints

** Percentage (%) of total plan assets

4. When a market movement is the cause of a breach in the above limits, it should be reported to the IC at the earliest of a mutually agreed-upon time during which the Investment Committee could convene with a quorum, or at the next regularly scheduled Investment Committee meeting, along with a report on how the breach was addressed, or a recommendation to address the breach.

IPS – Manager Selection Process

Manager Selection Process

- A. The process used to select an investment manager shall, at a minimum, include the following elements:
1. Imposition of a Quiet Period/No Contact policy. Board members and non-investment staff shall not have contact with parties who are under consideration for engagement by the Plan in response to an RFP, RFI, purchase order, other solicitation or other contracting process that has reached the point of specific focus on such parties, except in accordance with the published terms of the contracting process or except for, and limited to, contact necessary in connection with ongoing Plan business with a party. The Plan's communications with such parties shall include notice that a no-contact "quiet period" will be in place from a specific date until the contracting decision is finalized with respect to such parties, such that these communications shall not occur, except as provided above. As part of the contracting process, potential contracting parties (a) shall be informed by investment staff of the quiet period requirements and that violations of the quiet period requirements will cause immediate disqualification from their being engaged by the Plan; (b) shall be required to disclose potential conflicts of interest; and (c) shall make the placement agent disclosures required by law and Plan policies. Board members and non-investment staff shall not influence or attempt to influence, the Plan's decision-making process, outside of the authorized actions on behalf of the Plan.
 2. Identification of a mandate to implement the Board's SAA Policy Portfolio.
 3. Comprehensive **operational due diligence** performed by the investment staff, qualified investment consultant, or qualified quasi-discretionary investment manager;
 4. **Legal review** by qualified investment counsel of the manager agreement and related documentation;
 5. **An internal meeting of investment officers, including the CIO** and the officer responsible for the asset class in question, during which staff's due diligence analysis is reviewed and debated and a staff recommendation is made;
 6. **Approval by the CIO;**
 7. **Concurrence by a qualified investment consultant** or quasi-discretionary investment manager as to the reasonableness of the selection decision; and
 8. The CIO shall provide the Investment Committee with a summary of all active manager level transactions semi-annually.

IPS – Manager Selection Process (cont'd)

- B. The Procedures shall include any **checklists and templates** to be used in the due diligence process. Such Procedures shall be presented to the Investment Committee for review and input at least every three years, or sooner upon request of the Investment Committee or any member of the Board.
- C. Whenever amendments are made to the Procedures, a copy shall be provided to the Investment Committee at its next regularly scheduled meeting.
- D. Should any Investment Officer responsible for performing manager due diligence and preparing manager selection and termination recommendations to the CIO cease to be employed by the City for any reason, the CIO shall inform the Investment Committee immediately.
- E. The selection of an investment manager that would contravene a provision of this policy or the Procedures shall require Investment Committee approval.
- F. A file or files shall be established to serve as a permanent record of the due diligence process for each investment manager hired and shall contain a summary of the due diligence information and analysis generated during the search process, as well as the legal documentation.
- G. The **internal audit plan** of the internal auditor shall include a review of a random sample of investment manager selection decisions at least once per year to confirm compliance with this policy and the Procedures approved by the CIO, the scope of which shall not include the investment performance of such selection decisions. The results of such review shall be reported to the Audit Committee and the Investment Committee.

IPS – Manager Selection Process (cont'd)

- H. A “**Watch List**” will be established for underperforming managers and managers under extraordinary review for qualitative reasons, and will be maintained by the General Consultant.
 1. Quantitative criteria for underperformance which would trigger placement on the Watch List includes manager underperformance versus the appropriate benchmark over a three and/or five year period.
 2. Potential actions resulting from placement on the Watch List include finding appropriate resolution of outstanding issues, renewed confidence in the manager or strategy, or determination that the termination of the manager or strategy is appropriate.
 3. Investment staff will identify underperforming managers in conjunction with consultants.
 4. As necessary, nuanced investment strategies or fund types may require customized review.
- I. The Plan will seek alignment of interests when negotiating fees while pursuing the best net of fees performance results. Investment costs shall be monitored, controlled, and whenever possible negotiated to ensure cost effectiveness. The Board shall give consideration to the impact of administrative expenses, external management fees and performance fees when establishing the asset mix policy of the Plan. The Board will be provided reports on investment costs of the Plan at least annually.
- J. The Plan’s staff, in coordination with its investment consultants and legal counsel, will negotiate, monitor, and report on fees with investment managers regularly to ensure market competitiveness and appropriateness.
- K. The Plan will seek to ensure that excessive fees are not being paid for alternative assets by reviewing manager fees at least annually. Fee structures could incorporate fixed fees, performance based fees, high water marks, waterfall, hurdles, floors and caps. The Plan may also incorporate multi-year performance periods with clawbacks as needed.

Private Markets Due Diligence Checklist

Stage	Due Diligence Process	Action Items/Documentation	Lead	Date	
Stage 1	Manager Search	Identify manager candidates	Pipeline, consultant recommendations, third party marketers		
		Perform initial qualitative due diligence	Manager Marketing Materials		
			Manager Organizational Chart		
			Firm-wide AUM and Returns Disclosure		
		Perform initial quantitative due diligence	Returns Stats (Net IRR, Net MOIC, Vintage Quartiles, Loss Ratios)		
		Funding considerations	Check capacity		
Stage 2	Investment Due Diligence	Perform DD calls & meetings w/ managers	Determine optimal & initial investment size		
			Determine source of funding		
			Check consultant coverage, initial feedbacks		
			Inform IG of top candidates		
			Manager DDQ		
		Complete full quantitative due diligence	Supplemental DDQ (ad hoc)		
			ILPA DDQ/PREA DD Guidelines		
			LP List		
			Historical Fund Returns		
			Historical Strategy AUM and Holdings		
Seek internal and external feedbacks	Historical Sub-strategy Returns and Attribution (if applicable)				
	Historical Risk & Exposure Reports (if applicable)				
	Manager Monthly/Quarterly Strategy Update/Research				
	Manager Current Risk and Exposure Reports (if applicable)				
	Quantitative Analysis - Internal Risk System				
Prepare Scoring Matrix & Proposal Memo	Fund suitability analysis: expected return, risk, exposure analysis				
	Consultant investment DD Report				
	Conduct calls with consultant analysts				
	Quantitative Analysis - Consultant				
Stage 3	ODD	Solicit feedback from IOs/CIO			
		Private Fund Scoring Matrix			
		Blackbook			
		Manager ADV			
		Review of Financial Statements (Consultant)			
		Valuation Policy			
		Historical Annual Financial Statements (if applicable)			
Reference Checks					
Stage 4	Terms Review & Negotiations	Background checks (if applicable)			
		Operational DD Report (Consultant)			
		Evaluate fees and core terms	Manager Fees/Terms		
		Review Manager standard LPA/PPM/side letter			
		CIO Review	CIO Meets with manager		
Stage 5	Approval	Prepare final documents	Due Diligence Process Review & Checklist w/ Signoff		
		Blackbook			
		Obtain Consultant supporting memo			
Stage 6	Communication	Make final fund selection decision	Key Legal Documents (IMA, PPM/OM, LPA, Sub-Docs etc.)		
		CIO Approval	CIO approval form		
Stage 6	Communication	Federated IC notification			
		P&F IC notification			

** Differences to public markets in red text*

Manager Decisions – December 2024

Plan	Asset Class	Manager	Strategy	Action	Amount (\$MM)	Consistent with IPS?	Date	Meketa Opinion of New Managers
P&F HCT	Core Real Estate	TA Realty	TA Realty Core Property Fund, L.P.	Commitment to Existing Manager	6	Yes	9/30/2024	N/A
P&F HCT	Core Real Estate	Clarion Partners LLC	Lion Industrial Trust	Reduction	-0.6	Yes	10/4/2024	N/A
P&F HCT	Core Real Estate	TA Realty	TA Realty Core Property Fund, L.P.	Secondary Purchase	1.9	Yes	10/31/2024	N/A
P&F Pension	Public Equity	Redwheel	Emerging Markets	Reduction	-5	Yes	7/31/2024	N/A
P&F Pension	Emerging Markets Debt	Payden & Rygel	Emerging Markets Debt	Additional funding to Existing Manager	5	Yes	9/27/2024	N/A
P&F Pension	Private Real Assets	Primary Wave	Primary Wave Music IP Fund 4, L.P.	Hire	18	Yes	9/27/2024	Supportive
P&F Pension	Core Real Estate	TA Realty	TA Realty Core Property Fund, L.P.	Commitment to Existing Manager	25	Yes	9/30/2024	N/A
P&F Pension	Absolute Return	Crabel Capital Management	Crabel Fund LP-Class H	Additional funding to Existing Manager	12	Yes	10/1/2024	N/A
P&F Pension	Core Real Estate	Clarion Partners LLC	Lion Industrial Trust	Reduction	-4.8	Yes	10/4/2024	N/A
P&F Pension	Venture Capital	Tiger Iron Capital	Tiger Iron SJPF, L.P.	Commitment to Existing Manager	10	Yes	10/11/2024	N/A
P&F Pension	Private Real Assets	Pelican Energy Partners	Pelican Energy Base Zero, L.P.	Hire	18	Yes	10/25/2024	Supportive
P&F Pension	Core Real Estate	TA Realty	TA Realty Core Property Fund, L.P.	Secondary Purchase	9.5	Yes	10/31/2024	N/A
P&F Pension	Private Debt	Silver Point Capital	Silver Point Specialty Credit Fund III, L.P.	Hire	28	Yes	11/15/2024	Supportive