

December 1, 2010 IOC Meeting

Presentation of ERB Private Equity Selection Process

The private equity process is similar to the other alternative programs such as real estate and real assets. It encompasses the following steps:

1. NEPC (the private equity consultant for ERB) and Staff agree on a strategic plan for the next twelve months. This includes pace of investing and sector allocations
2. Both staff and NEPC survey the marketplace for funds in the fundraising stage. This is an ongoing effort as various funds are looking for new investors at certain times and other funds are closing as they have raised sufficient funds. This is a limited time process. A fund will raise enough money for a given vintage fund; let's call it "Fund #1. When they the general partners (GPs) have sufficient commitments from investors, they will cease fundraising and focus on investing the capital from Fund #1 and building profitable companies. At some point in time, usually years after closing the fundraising period, the investor's capital committed to Fund #1 has been invested. At this juncture, the GPs may elect to duplicate the process and begin soliciting investors to participate in Fund #2 and repeat the process. Fund #2 may not be soliciting investment until several years after the fundraising for Fund #1 has ceased. Thus, at any point in time, ERB may not have access to a given fund or fund management team. The time frame for a fund to raise money varies given market conditions and the stature or success of a given GP. For a successful fund with a stable group of investors in a bull market, that period may be 30 days or less. An RFP process will take multiple months, thus causing ERB to forgo certain desirable opportunities. As a result of the market realities, ERB and NEPC must constantly monitor the market place to determine which desirable funds are available for investment and cannot rely on a cumbersome RFP process.
3. Once it is determined a fund is in fundraising mode and that it is a general fit for the ERB portfolio, preliminary due diligence begins. This is simply a high level review of the fund details and narrows the field for more focused review.
4. If the fund passes the preliminary review, both staff and NEPC undertake detailed due diligence. This entails requiring the GP to complete detailed due diligence questionnaires from both NEPC and ERB staff, and includes face to face meetings and site visits. A portion of this review includes a placement agent review in adherence to our placement agent policy. This review includes the use of an outside law firm hired by ERB. If a placement agent is involved, the disclosures required are very exhaustive, usually including hundreds of pages of documents. Note that the review is a parallel

process, with both NEPC and staff gathering data independently and ultimately sharing that data. This process is in part an outgrowth of “lessons learned” from the questionable behavior engaged in by the previous private equity consultant and is designed as one safeguard to prevent future occurrences.

5. If both NEPC and staff are in favor of proceeding with the investment, it is scheduled for consideration at a monthly public meeting of the ERB Investment Committee.
6. The Investment Committee meeting, in open session, hears an in-person presentation from the GP, NEPC and staff. The Committee also reviews written recommendations and analysis from staff and NEPC. These presentations include public disclosure of relevant placement agent information, a review of the fit for the ERB portfolio and strategic plan, as well as a discussion of the general pros and cons of the investment. The investment is then approved or disapproved by a formal Investment Committee vote. All materials presented are available to the public under IPRA.
7. If the investment is approved, staff and outside legal counsel negotiate with the GP on final terms and conditions in accordance with New Mexico law and ensure all terms, including fees, are within industry and normal ERB standards. Once negotiations are concluded, appropriate signatories from each party execute a limited partner agreement. This is the contract that governs the activities of the fund and ERB’s participation.
8. The entire process is outlined in and governed by the ERB Private Equity Policy: <http://www.nmerb.org/pdfs/privateequitypolicy.pdf>
9. Policies governing real estate, natural resources, infrastructure, and hedge fund investing are also available on ERB’s website, as is the ERB general investment policy and placement agent disclosure policy: <http://www.nmerb.org/invpolicies.htm>