Northern Ireland Local Government Officers' Superannuation Committee

Investment Monitoring Guidelines

1 Introduction

1.1 The Northern Ireland Local Government Officers' Superannuation Committee ('NILGOSC' or the 'Committee') monitors and evaluates the performance of its appointed investment managers on a quarterly basis. The quarterly evaluation process incorporates qualitative as well as quantitative factors, and each individual manager is assessed against a range of pre-determined criteria.

1.2 A key action resulting from any formal investment monitoring exercise is the decision whether to retain or terminate an appointed investment manager. NILGOSC acknowledges that such decisions are not without cost, as: retaining poorly performing managers for too long; terminating a skilled manager prematurely; or transitioning assets between managers, all have a negative impact on the value of a Fund.

1.3 In addition, the inherent volatility of financial returns makes it difficult to accurately identify the optimum time to replace a manager. Even the most skilled managers will suffer periods of below par performance and it is difficult to determine if a newly appointed manager will perform any better than one considered for termination.

1.4 The guidelines seek to provide a systematic, consistent and transparent approach to investment manager monitoring, as well as an objective framework for making retention decisions. This approach is designed to:

- provide a long-term, forward-looking focus for investment manager evaluation;
- provide a framework for assessing both quantitative performance, and qualitative factors relevant to future performance;
- enhance and support communication with investment managers;
- provide a timely response to consecutive quarters of underperformance or other emerging issues; and
- provide an objective monitoring system which can be applied equally to all investment managers.

1.5 The Investment Monitoring Guidelines are designed to provide guiding principles, but are not intended to remove the discretion of the Committee to act outside of the guidelines in exceptional circumstances. Where such discretion is exercised, a formal record documenting the circumstances leading to the decision to set aside the Investment Monitoring Guidelines should be kept.

1.6 In addition to investment managers, NILGOSC also has a number of 'fund managers'. Unlike investment managers, which NILGOSC appoints to manage a specific portfolio of investments; NILGOSC enters into fund managers' specific Limited Partnerships, agreeing to their terms and conditions. Before entering such arrangements (e.g. infrastructure funds), thorough due diligence is carried out by NILGOSC, assisted by third party advisors, as required.

1.7 The funds are long-term investments and as such, although the Investment Team monitors quarterly fund updates, performance is typically only measured on a long-term basis. Some of the criteria applied in the quarterly evaluation process are not applicable to the fund managers, and given the nature of these funds, there is limited action NILGOSC can take. Instead fund managers are formally reviewed through an annual monitoring process. The 'Review of Alternative Investments' is performed each September, and covers all investments not reviewed quarterly in the Investment Monitoring Scorecard.

1.8 For clarity, these guidelines apply to all investment managers with which NILGOSC has an Investment Management Agreement (IMA) and not to fund manager investments where NILGOSC has entered into a Limited Partnership agreement.

2 Monitoring Process

2.1 The Committee has a fiduciary duty to monitor the performance of its managers. A consequence of this duty is the obligation to take action where managers are not delivering expected performance. The following monitoring process has been developed to assist the Committee in this respect.

2.2 At the end of each calendar quarter the Committee is presented with the following information:

- A report prepared by the Head of Investment Services, which includes a completed Investment Monitoring Scorecard. The report highlights any areas of concern identified during the monitoring process, together with any recommendations if appropriate.
- A report from the Fund's Investment Advisor which summarises market background, strategic performance, notable changes and/or issues for each manager and an investment update. This report also includes a performance measurement table summarising the individual returns for each manager compared to the performance target ('target').

3 Investment Monitoring Scorecard

3.1 An Investment Monitoring Scorecard (the 'Scorecard', Appendix A) is completed by the Head of Investment Services on a quarterly basis. The Scorecard evaluates each individual investment manager's performance against a series of pre-determined criteria. If a manager fails any of the criteria, an amber or red rating is recorded on the Scorecard under the relevant category. A brief description of the failure is recorded in the 'Comments' column.

3.2 A traffic light system is used whereby managers are awarded a green, amber or red rating based on their performance against each criterion throughout the quarter under review. The three ratings are defined as follows:

Green	There are no significant issues arising and the normal monitoring process should continue.
Amber	There are significant issues arising which cause concern and warrant further investigation. Minor deviations or non-recurring events which can be explained by specific circumstances will not generally warrant an amber rating.
Red	There are serious issues arising which cause concern and warrant further investigation.

3.3 In addition to assessing performance against individual criteria, managers are awarded an 'overall rating' of green, amber or red. A recommended overall rating is determined by the Head of Investment Services on a case-by-case basis, taking into consideration knowledge of the investment manager and mandate, as well as the nature of any breaches or concerns raised throughout the monitoring process.

3.4 On a quarterly basis, the Committee reviews the completed Scorecard and associated report prepared by the Head of Investment Services, and considers the overall rating assigned to each manager. Following the meeting, managers are notified of the overall rating and outcome of the quarterly review.

3.5 When a manager is given an overall amber rating, they are placed on a Watchlist. Once on the Watchlist a number of actions are taken:

- The manager is informed that they have been placed on the Watchlist, together with the reasons for concern;
- The manager is invited to address any concerns and/or take remedial action prior to the end of the next review quarter; and
- If considered appropriate, NILGOSC may request an on-site review with the manager.

3.6 A manager is normally only permitted to remain on the Watchlist for four consecutive quarters before a decision must be reached to move to either a green or a red rating. Placing a manager on the Watchlist should be viewed as an intermediate step towards either resolving a problem or replacing the manager. If after four consecutive quarters the Committee does not consider that the conditions which led to a manager being placed on the Watchlist have been resolved, an overall red rating must be given.

3.7 A manager can be given a red rating following an amber rating or can move immediately from a green to a red rating, where it is warranted by the circumstances. Once a manager has been given an overall red rating, the following steps are taken:

- The manager is informed that they have been given a red rating and that a full-scale review will commence shortly;
- A formal discussion takes place between NILGOSC and the manager;
- A formal retention review is undertaken with the assistance of the Investment Advisor; and
- A decision is made within two months to either retain or terminate the mandate.

3.8 If considered appropriate, a service review of the manager may be carried out at any time by the Investment Team, preferably on-site, to identify and/or resolve any performance issues.

4 Pre-determined Criteria

4.1 Traditional investment manager monitoring has focused heavily on quantitative data, with specific attention given to past historical returns. Previous financial returns are useful in determining if a manager has been successful in the past but are of limited use when trying to predict future performance. Accordingly, NILGOSC takes a number of qualitative factors into consideration alongside current financial returns when assessing investment performance.

4.2 The criteria are used as part of the quarterly monitoring process to assign a green, amber or red rating for each investment manager. The criteria also form the basis of the quarterly reports provided by the investment managers and the Investment Advisor.

4.3 The quantitative and qualitative criteria used to monitor investment manager performance are set out in the following two tables, along with any warning signs that would cause concern. These criteria are reviewed quarterly and unsatisfactory reviews may result in an amber or red rating being awarded.

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Qualitative Factors: Criteria and warning signs

Investment Style	Manager has deviated from stated investment style or philosophy Investment style no longer consistent with NILGOSC's investment objectives
Change in Ownership	There has been a change in ownership which could potentially affect future performance
Key Personnel	The departure of one or more key members involved in the decision-making process of the NILGOSC portfolio/strategy
Client Base	There has been a significant change in client base
Assets Under Management	There has been a significant change in assets under management (both an increase or a decrease)
Investment Advisor Ranking	There has been a downgrading in the ranking awarded by the Investment Advisor
Litigation	There is material litigation underway which may impact on the future of the manager or investment product
Client Servicing	There are material client service issues which impact on the ability to monitor performance
ESG Capabilities	There is insufficient evidence that the manager is taking ESG issues into account during the investment process

Quantitative Factors: Criteria and Warning signs

Performance relative to target	Manager underperforms their target for four consecutive quarters
Information Ratio	Information ratio is negative on a since inception basis
Tracking Error	Tracking error outwith acceptable range for the strategy
Turnover	Turnover levels outwith acceptable range for the strategy
Investment Guidelines Breach	A material breach of investment guidelines occurs

4.4 With respect to the performance relative to target criteria, the criterion ratings are applied as follows:

Green	Performance is ahead of target
Amber	Performance is ahead of the index but behind the target for four or more consecutive quarters
Red	Performance is behind both index and target for four or more consecutive quarters

4.5 In order to prevent a manager with a recent history of red or amber performance ratings effectively restarting the clock with a single quarter of green performance, an additional control is applied. Where the performance rating awarded in the previous quarter was not green, the following three bullet points should be followed when determining the performance rating for the quarter under review:

- If a manager with a red rating in the previous quarter outperforms the index but remains behind the target, an amber rating may be considered appropriate, after taking into consideration the third bullet point.
- If a manager with a red or amber rating in the previous quarter outperforms the index and target, a green rating may be considered appropriate, after taking into consideration the third bullet point.
- When applying the previous two points and considering returning a rating to a more positive colour, consideration must first be given to the ratings over the previous four quarters:
    - If two or more quarters in the last four have demonstrated red or amber performance, then the criterion rating for the quarter under review should be red.
    - If two or more quarters in the last four have demonstrated amber performance, then the criterion rating for the quarter under review should be amber.
    - If one quarter in the last four has demonstrated red or amber performance, then the criterion rating will be green, until underperformance is recorded for four consecutive quarters.

4.6 Performance returns are provided by NILGOSC's Global Custodian for quarterly, annual, three year and five-year timeframes. In order to discourage short-termism, the Scorecard focuses on the three and five year returns. One year performance returns are provided in the narrative report for information.

4.7 In addition to the Watchlist criteria, there may be specific circumstances which warrant an immediate retain or terminate decision. Such events may include, but are not limited to: the departure of a key member of the team; a sudden loss of clients or assets under management; or a fundamental change in strategic direction. In such extreme circumstances, managers can be given an overall red rating prompting an immediate retention review.

5 Role of Investment Advisor

5.1 NILGOSC's Investment Advisor prepares a quarterly report for the Committee on fund performance as a whole, as well as the contribution of individual managers. Each quarter, the Investment Advisor also issues each investment manager with a quarterly monitoring questionnaire, providing the Head of Investment Services with the outputs as well as commentary on the managers' performance. The Head of Investment Services feeds information from both deliverables into the Scorecard, for use as part of the review process.

5.2 The Investment Advisor also monitors the managers quarterly and assesses each manager in the following areas:

- Performance;
- Terms and Conditions;
- Environmental, Social and Corporate Governance (ESG);
- Staff;
- Process;
- Risk;

- Business; and
- Operational Due Diligence.

Investment Advisor ratings are applied to each of the preceding eight areas as follows:

- Operational due diligence is assessed as a: Pass (A1 or A2); Conditional Pass; or Fail.
- ESG ratings apply to strategies and have four categories: Advanced; Integrated; Limited; or Not Applicable.
- Each remaining area is individually rated from '1' to '4,' where '1' is weak and '4' is strong.

An overall rating is then derived for each manager based on all of the individual ratings. The Investment Advisor's overall rating can be interpreted as follows:

Buy	Recommends clients invest with or maintain existing allocation to 'Buy' rated products
Buy (closed)	Recommends clients invest with or maintain existing allocation to 'Buy' rated products, however it is closed to new investors
Qualified	A number of criteria have been met and the Investment Advisor considers the investment manager is qualified to manage client assets
Sell	Recommends termination of client investments in this investment product
In Review	The rating is under review as the Investment Advisor evaluates factors that may cause a change to the rating

5.3 NILGOSC considers these independent ratings as part of the Scorecard and retention review process. Particular attention is paid to managers receiving a 1 or 2 rating against individual criteria or an overall rating of 'In Review' or 'Sell'.

5.4 The Committee is responsible for placing managers on the Watchlist, and for any subsequent retain or terminate decisions. It is considered appropriate to seek expert advice from the Investment Advisor when making such decisions.

5.5 Once a manager has been given an overall red rating the Investment Advisor is asked to undertake a formal review ('retention review'), the outcome of which must be either a recommendation to retain or a recommendation to terminate the manager assessed.

6 Retention Review

6.1 NILGOSC acknowledges that fluctuating financial returns are a key characteristic of securities markets, particularly when viewed over a short period of time. Accordingly, NILGOSC has determined that three to five years is a suitable time period over which a manager's performance can justifiably be compared to the relevant target.

6.2 The retention review is designed to provide independent and expert advice to the Committee on whether to retain or terminate a manager. The review is normally carried out by the Investment Advisor. The review encompasses all elements of a manager's performance, both quantitative and qualitative, and should not be dissimilar to the analysis performed during the selection process. Consideration is also given to any steps taken by the investment manager to address concerns raised.

6.3 The retention review also considers the likelihood that the manager will be able to meet its investment objectives over its mandated performance period. As part of the retention review, financial returns are plotted and projected over the relevant period. Consideration is given as to whether a manager can realistically meet its target given acceptable levels of risk and volatility. Where it is statistically improbable that a manager will meet its target over the mandated timeframe, and the target is still considered to be appropriate for the strategy, a decision should be made to terminate.

6.4 In certain circumstances, it may be appropriate to retain a manager and make adjustments to the target and/or mandate to reflect current market conditions.

6.5 In addition to a detailed quantitative and qualitative analysis, the retention review report should include the following:

- Clear recommendation to retain or terminate the manager;
- Detailed rationale to support the recommendation;
- Where the recommendation is to retain a manager, the key issues which should be closely monitored going forward; and
- Where the recommendation is to terminate a manager, the options for redistributing the assets.

6.6 Retention reviews should be completed within one month of commencement.

6.7 In the case of a newly appointed manager, it is unlikely that financial performance alone would warrant a retention review within the first 24 months unless the underperformance is significantly different from the pre-appointment returns or is combined with significant qualitative failures.

7 Termination Decisions

7.1 Where the outcome of the retention review is such that it is not recommended that a particular manager is retained, a number of actions are available for consideration:

- Remove/reduce the amount of funds under management and reallocate to an existing active manager(s);
- Remove/reduce the amount of funds under management and reallocate to an existing passive manager(s);
- Remove/reduce the amount of funds under management and reallocate to a shortlisted manager(s) from a previous selection exercise; or

- Commence selection exercise for a replacement manager(s).

7.2 There are significant costs and administration issues incurred when replacing an investment manager and therefore any decision should include a strategy for minimising costs and disruption.

7.3 In certain circumstances, consideration may be given to reducing the funds under management rather than outright termination. However, the reasons for removing some but not all funds from a particular manager should be clearly documented. The reduction of funds under management is not used as an alternative to termination in circumstances where there has been a fundamental loss of confidence in a product or manager.

7.4 Termination decisions should be completed within two months of the decision to undertake a retention review.

7.5 The Committee does not make termination decisions without undertaking rigorous due diligence and any decision to replace a manager is made on a prudent basis. In those circumstances where the retention review indicates that the funds currently under management are at risk, and there is insufficient time to appoint a replacement manager, consideration will be given to moving the funds to existing active and/or passive managers. Such action allows funds to be transferred quickly and with minimum transition costs.

7.6 In normal circumstances, a transition manager is appointed, and the transition properly planned to allow any stocks common to both the outgoing and incoming manager to be transferred rather than liquidated. The liquidation of assets which are not required by the incoming manager are carefully controlled so as not to adversely impact on the sales price and to also limit market exposure.

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Appendix A

This Investment Monitoring Scorecard template has intentional blank cells in the body part of the table as it highlights the respective manager's overall rating broken down into qualitative and quantitative criteria, followed by any comments regarding the scores.

Manager	**Overall Rating**	**Qualitative Criteria**									**Quantitative Criteria**					**Comments on Ratings**
		Invest Style	Change in Ownership	Key Personnel	Client Base	AUM	Ranking	Litigation	Client Service	ESG	Performance v Target 3 / 5 years	Info Ratio	Tracking Error	Turn-over	IMA Breach	
Manger 1																
Manger 2																
Manger 3																
Manger 4																
Manger 5																
Manger 6																
Manger 7																
Manger 8																
Manger 9																
Manger 10																

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Key for Overall Rating:

Green	There are no significant issues arising and the normal monitoring process should continue.
Amber	There are significant issues arising that cause concern and warrant further investigation. Minor deviations or non-recurring events which can be explained by specific circumstances would not generally warrant an amber rating.
Red	There are serious issues arising that require a formal retention review be to be undertaken.
N/A	Not applicable.