



# Board of Retirement Regular Meeting

## Sacramento County Employees' Retirement System

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### Agenda Item 13

**MEETING DATE:** September 20, 2017

**SUBJECT:** Investment Consultant Contract Amendments to Extend and Specify Contract Duration

**SUBMITTED FOR:**  Consent       **Deliberation and Action**       **Receive and File**

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### **RECOMMENDATION**

Staff recommends the Board extend the terms of the contracts with SCERS' investment consultants; Verus Advisory, Inc. as general investment consultant, Cliffwater LLC as alternative assets consultant, and Townsend Holdings, LLC as real estate investment consultant, and make an adjustment to the consultant team from Verus as follows:

- Extend the term of the contract with Verus Advisory, Inc. from March 3, 2016 through June 30, 2019, and that Margaret Jadallah replace John Meier as Co-Consultant.
- Extend the term of the contract with Cliffwater, LLC from February 17, 2014 through June 30, 2020.
- Extend the term of the contract with Townsend Holdings, LLC from August 16, 2017 through June 30, 2019.

### **PURPOSE**

To specifically define the length (or "term") of SCERS' investment consultant contracts rather than using the current unspecified or continuing term language. In addition, staff recommends establishing a periodic review of investment consultant contracts going forward.

### **BACKGROUND**

SCERS utilizes three investment consultants to provide non-discretionary advice within SCERS' investment program. The investment consultants include:

1. Verus Advisory, Inc. (general investment consultant)
2. Cliffwater LLC (alternative assets consultant)
3. Townsend Holdings, LLC (real estate investment consultant)

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SCERS' staff has undertaken a project to aggregate, review and examine compliance with SCERS' service provider and investment manager contracts. This has entailed making sure that all contracts are stored in a central location, and that all contracts are currently in compliance as it relates to their terms and duration, if applicable.

As background, most SCERS investment manager contracts do not have specific end dates. Investment management contracts for the traditional/liquid asset classes, particularly the separate account mandates, are structured with immediate termination rights, while most commingled funds have specific redemption schedules, varying from daily to quarterly. Within the alternative asset classes, the ability to terminate an investment manager is defined within the contractual agreement with the manager. Open-end funds, including Absolute Return and Real Estate investments, typically have monthly and quarterly termination rights, subject to lock-up periods and investor level gates. Closed-end funds within the private markets, including Private Equity, Private Credit, Real Assets and Real Estate, are generally illiquid structures with five to thirteen year holding periods.

However, service provider contracts, including those for general and specialist investment consulting services, typically have a specified term length and generally include an option to renew or extend the term length by mutual written amendment. While SCERS investment consultants are non-discretionary "service providers", these contracts have historically been viewed as contracts whose services continue without end until terminated by either party. These types of contracts are commonly referred to as "evergreen" contracts.

Each of SCERS' three original investment consultant contracts uses the same contract language in the clause defining contract duration:

"The term of the Agreement shall commence on the effective date of the Agreement and continue for three years, or until terminated as provided in this Agreement". In the case of Townsend, the language reads "for five years."

Both SCERS and its investment consultants have historically interpreted this language to define an evergreen contract since the language references the phrase "or until terminated as provided in this Agreement". It should be noted that each investment consultant contract allows for SCERS to terminate the agreement at any time without cause by providing written notice of termination to the specific investment consultant 30 days prior to the requested effective date of the termination. An investment consultant may terminate its contract with SCERS upon 90 days written notice. As discussed, both Staff and the consultants have interpreted and believed the original and existing contracts to be in effect until either party terminates the contract, without a specific end date and each has operated under that premise for years.

The Verus contract (which was formerly an SIS contract, but assigned to Verus subsequent to the merger between SIS and Verus in 2016) was amended in 2014 due to personnel changes within the firm, and to set a specific term. The rationale was that in light of the personnel changes, review of Verus might be in order after an evaluation period. That contract was amended in March of 2014 with a specific termination date of March 3, 2016. Staff

understands that it is accountable for allowing this termination date to pass without further amendment to extend the term. Staff concluded that if we were going to remedy the term issue and amend the Verus contract, the Cliffwater and Townsend contracts should also be amended for clarity. This discovery has provided Staff the opportunity to amend the contract and establish a systematic, periodic review of investment consultants going forward.

### **REVISED INVESTMENT CONSULTANT CONTRACT PROCESS**

Upon reviewing the contracts for all three of SCERS' investment consultants, Staff believes it is prudent to have defined duration for each of SCERS' investment consultants, and keep the contracts consistent with each other, and with other SCERS service provider contracts.

Staff also recommends that SCERS establish a process to periodically evaluate its service providers with multi-year contracts. When appropriate, the evaluation should be performed by the Retirement Board, with input from SCERS' Staff regarding the delivery of services and day-to-day working relationship. As you will recall, the engagement of SCERS' investment consultants is a role and responsibility of the Board, and cannot be delegated to Staff.

While SCERS continually evaluates its investment consultants, and other service providers, Staff suggests initiating a formal evaluation of the investment consultants prior to the end of the contract terms extensions proposed herein. At this time, Staff would come to the Board seeking input related to the investment consultant. This would likely include a survey presented to the Board seeking responses to a variety of evaluation questions, followed by discussion with the Board. During this process, the Board, with input from Staff, would determine the level of satisfaction with the consulting relationship, whether any adjustment to the scope of services the consultant provides is needed, and whether or not the Board wishes to survey the consultant market by conducting a competitive search for consulting services.

At the conclusion of the evaluation, if SCERS is satisfied with the performance of an existing consultant, then the term of that contract could be extended and one or more subsequent evaluations would be conducted during the next term. The term of a contract extension would typically be between three and five years, and may depend on the duration and timing of initiatives or projects anticipated or currently underway involving that consultant. However, if SCERS is not satisfied with the performance of the existing consultant, or if SCERS is interested in surveying the consultant landscape across key area such as scope of services, terms and best practices, then a competitive search could be considered.

### **DISCUSSION**

#### **Extension Of Terms For SCERS' Investment Consultants**

Staff is not recommending any other changes to the investment consulting contracts at this time, other than the extension of terms, and updating the consulting team at Verus. All other existing terms of the agreements will remain in full force and effect. It is important to note that Staff is recommending relatively short extensions—to fiscal year end 2019 or 2020-- rather than a typical three to five year extension. SCERS has not formally evaluated its current investment consultants since they were hired in 2011 and 2012. Therefore, Staff believes it is

prudent to set the end dates of the extensions more near-term. Where feasible, Staff would prefer to stagger the expiration years of SCERS' investment consultant contracts.

### **Proposed Contract Amendments**

#### **General Investment Consultant**

**Amend the contract with Verus Advisory, Inc. to be extended from March 3, 2016 through June 30, 2019, and that Margaret Jadallah be added as a Co-Consultant, replacing John Meier.**

March 3, 2016 is the defined end date of the existing contract with Verus. Staff recommends that this contract be amended to establish a termination date of June 30, 2019. The proposed duration of the extension will allow SCERS to continue to evaluate Verus subsequent to the merger between SIS and Verus in early 2016. In addition, the current contract with Verus is an SIS contract that was created by SCERS. The broader Verus organization uses a different template for its client contracts than SIS did. The proposed nearer-term expiration will allow the parties to establish a new/merged contract template if the Board decides prior to the contract expiration to further extend its relationship with Verus.

#### **Alternative Assets Consultant**

**Amend the contract with Cliffwater, LLC to be extended from February 17, 2014 through June 30, 2020.**

February 17, 2014 is the date that corresponds to the end of the three year period since inception within the current contract with Cliffwater. While the existing language is ambiguous as it relates to a defined end date, the recommended extension would eliminate this ambiguity and set the end date of the contract at June 30, 2020. SCERS will formally review the Cliffwater relationship prior to the extended termination date.

#### **Real Estate Investment Consultant**

**Amend the contract with Townsend Holdings, LLC to be extended from August 16, 2017 through June 30, 2019.**

August 16, 2017 is the date that corresponds to the end of the five year period since inception within the current contract with Townsend. While the existing language is ambiguous as it relates to a defined end date, the recommended extension would eliminate this ambiguity and set the end date of the contract at June 30, 2019.

The expiration of the extended term of this contract coincides with the expiration of the general investment consultant contract; however, Staff believes the Townsend contract should be reviewed at this date for a couple of reasons.

First, the scope of service for the real estate consulting mandate could potentially change over the next year as SCERS reduces/eliminates its separate account real estate portfolio. As you

will recall, SCERS recently modified the structure of the Real Estate asset class, which includes the unwinding of the core real estate separate account direct investments in favor of investing in core real estate through open-end commingled funds. The implementation of this change could be completed within the next year, so the scope of real estate investment consulting services SCERS requires should be re-evaluated.

Second, Townsend has had multiple ownership changes over the past year. First, in early 2016, Townsend was acquired by NorthStar Asset Management, which subsequently merged with Colony Capital. Then, it was recently announced this month that Townsend was acquired by consulting firm Aon. There appear to be synergies with the Townsend acquisition, as the real estate expertise of Townsend will complement Aon's broader consulting practice. It is expected that the Aon real estate consulting practice will be folded into Townsend, and the Townsend brand will be kept. The expiration of the extended term of this contract will allow SCERS to continue to evaluate Townsend subsequent to this acquisition.

### **ATTACHMENTS**

Amendment to General Investment Consulting Agreement  
Amendment to Alternative Assets Investment Consulting Agreement  
Amendment to Real Estate Investment Consulting Agreement

Prepared by:

/s/  
\_\_\_\_\_  
Steve Davis  
Chief Investment Officer

/s/  
\_\_\_\_\_  
Robert L. Gaumer  
General Counsel

Reviewed by:

/s/  
\_\_\_\_\_  
Annette St. Urbain  
Interim Chief Executive Officer

## **SECOND AMENDMENT TO GENERAL INVESTMENT CONSULTING AGREEMENT**

This Second Amendment (Second Amendment) is entered into by and between the Sacramento County Employees' Retirement System (SCERS) and Strategic Investment Solutions (Consultant), as of September 20, 2017.

WHEREAS, SCERS and Consultant entered into an General Investment Consulting Agreement for general investment consulting services as of March 3, 2011 (Agreement); and

WHEREAS, the Agreement was subsequently amended extend its term to March 3, 2016, specify changes to designated personnel and increase the annual fee for services (First Amendment); and

WHEREAS, on December 15, 2015, SCERS and Consultant agreed in writing to assign the First Amendment from Consultant to Verus Advisory, Inc., (VERUS) while preserving the terms and provisions under the Agreement and the First Amendment

WHEREAS, SCERS and VERUS desire and intend to amend the terms of the First Amendment as described in paragraphs 1 and 2 of the First Amendment.

NOW, THEREFORE, in consideration of the covenants and conditions set forth herein, SCERS and Verus hereby replaces in their entirety paragraphs 1 and 2 of the First Amendment and substitutes the following two paragraphs in their place:

### Paragraph 1

The term of this Second Amendment shall commence on March 3, 2016 and continue until and including June 30, 2019, unless otherwise terminated prior to that date under the "Termination" provisions specified in paragraph 7 of the Agreement.

### Paragraph 2

Personnel. Barry Dennis, John Nicolini and Margaret Jadallah shall be designated as Primary Consultants to SCERS, and shall attend Board meetings and meet with SCERS staff, whether jointly or individually, as reasonably requested by SCERS. VERUS shall request written consent from SCERS prior to making any changes in assignment or responsibilities of the Primary Consultants.

Except as so amended, all other terms and conditions of the Agreement and the Amended terms of the First Amendment shall remain in full force and effect.

IN WITNESS WHEREOF, SCERS and VERUS have caused this Second Amendment to be duly executed by their respective authorized representatives.

Sacramento County Employees'  
Retirement System

Dated: \_\_\_\_\_

By: \_\_\_\_\_  
Richard B. Fowler II  
SCERS Board President

Verus Advisory, Inc.

Dated: \_\_\_\_\_

By: \_\_\_\_\_

**AMENDMENT TO ALTERNATIVE ASSETS INVESTMENT CONSULTING  
AGREEMENT**

This Amendment (Amendment) is entered into by and between the Sacramento County Employees' Retirement System (SCERS) and Cliffwater, LLC (Consultant), as of September 20, 2017; and

WHEREAS, SCERS and Consultant entered into an Alternative Investment Consulting Agreement for alternative investment consulting services as of February 17, 2011 (Agreement); and

WHEREAS, SCERS and Consultant desire and intend to amend the terms of the Agreement as specified in paragraph 6 of the Agreement.

NOW, THEREFORE, in consideration of the covenants and conditions set forth herein, SCERS and Consultant hereby replaces in its entirety paragraph 6 and replace it with the following language:

The term of this Amendment shall commence on February 17, 2014 and continue until and including June 30, 2020, unless otherwise terminated prior to that date under the "Termination" provisions specified in paragraph 7 of the Agreement.

Except as so amended, all other terms and conditions of the Agreement shall remain in full force and effect.

IN WITNESS WHEREOF, SCERS and the Consultant have caused this Amendment to be duly executed by their respective authorized representatives.

Sacramento County Employees'  
Retirement System

Dated: \_\_\_\_\_

By: \_\_\_\_\_  
Richard B. Fowler II  
SCERS Board President

Cliffwater, LLC

Dated: \_\_\_\_\_

By: \_\_\_\_\_

**AMENDMENT TO REAL ESTATE INVESTMENT CONSULTING AGREEMENT**

This Amendment (Amendment) is entered into by and between the Sacramento County Employees' Retirement System (SCERS) and Townsend Holdings LLC (Consultant), as of September 20, 2017.

WHEREAS, SCERS and Consultant entered into an Real Estate Consulting Agreement for real estate consulting services as of August 16, 2012 (Agreement); and

WHEREAS, SCERS and Consultant agreed in writing on December 21, 2015, to the merger transaction between Consultant and NorthStar Asset Management Group, Inc; and

WHEREAS, SCERS and Consultant desire and intend to amend the term of the Agreement as that word is defined in paragraph 6 of the Agreement.

NOW, THEREFORE, in consideration of the covenants and conditions set forth herein, SCERS and Consultant hereby replaces in its entirety paragraph 6 of the Agreement and substitutes it with the following language:

The term of this Amendment shall commence on August 16, 2017 and continue until and including June 30, 2019, unless otherwise terminated prior to that date under the "Termination" provisions specified in paragraph 7 of the Agreement.

Except as so amended, all other terms and conditions of the Agreement shall remain in full force and effect.

IN WITNESS WHEREOF, SCERS and the Consultant have caused this Amendment to be duly executed by their respective authorized representatives.

Sacramento County Employees'  
Retirement System

Dated: \_\_\_\_\_

By: \_\_\_\_\_  
Richard B. Fowler  
SCERS Board President

Townsend Holdings, LLC.

Dated: \_\_\_\_\_

By: \_\_\_\_\_  
Jack Koch  
Principal