AGENDA
Kansas Board of Regents
Retirement Plan Committee
September 19, 2017 at 12:30 p.m.
Regents Board Room

1. Introductions – new RPC chair, Regent Shane Bangerter, and new Regent for the committee Regent Joe Bain

2. Approve: Minutes from March 16, 2017

3. Segal Semi-Annual Review through June 30, 2017– Craig Chaikin

4. Fund line-up change recommendations – Craig Chaikin
   A. Replace the Voya VY FMR Diversified Mid Cap (IFDIX), which was eliminated and merged with the Voya Mid Cap Opportunities portfolio
   B. Add Islamic Law compliant fund

5. Request for Information to benchmark the Mandatory Retirement Plan

6. Executive Session

7. Good of the order

8. Next meeting – Tuesday, March 20, 2018, location TBA
The March 16, 2017, Retirement Plan Committee meeting was called to order by Regent Bangerter at 10:10 a.m.

Members Participating:
Regent Ann Brandau-Murguia, Chair
(by conference call)
Regent Shane Bangerter
President Allison Garrett, ESU
Dr. Rick Lecompte, WSU
Stacy Snakenberg, KU Medical Center
Also present: Craig Chaikin, Segal Marco Advisors, consultant; TIAA’s Nicolette Dixon, Senior Relationship Manager, Maggie Dehn, Managing Territory Director, Stephanie Mishak, Financial Consulting Director and Tom Carmody, Managing Director; Voya’s John O’Brien, Regional Vice President, Cindy Delfelder, Key Account Manager, and Amy Goodale, Strategic Relationship Manager; and from the Kansas Board of Regents Office, Theresa Schwartz, Associate General Counsel and Elaine Frisbee, Vice President Administration and Finance.

Participating by conference call were Michele Sexton, PSU; Adam Polacek, TIAA’s Managing Director Portfolio Management; and Bernie Heffernon, Voya’s Senior Vice President of Distribution. Leisa Julian, KU, was not able to attend the meeting.

**Introductions** – Regent Bangerter introduced President Allison Garrett, President of Emporia State University, representing COPs on the RPC.

**Minutes**
The minutes from the September 13, 2016 meeting were approved.

**Segal Semi-Annual Review through December 31, 2016**
Craig Chaikin shared information about Segal’s acquisition of Marco Consulting Group, which will provide additional research capabilities for searches and analyzing fund lineup information. There will be no changes for KBOR on the day-to-day interactions. Craig Chaikin reviewed information contained in the December 31, 2016 semi-annual report and indicated there were no recommendations for fund line-up changes from or for either TIAA or Voya.

Craig Chaikin stated that more lawsuits have been filed alleging fiduciary breaches under ERISA, and the Levin Law Firm has posted a list of over 100 colleges and universities on its home webpage encouraging past and current employees to join class action lawsuits. No Kansas Board of Regents state university is included in that listing and all listed institutions are private colleges and universities, not public. Craig Chaikin stated that it is much less likely that public entities will have suits brought against them as it is much harder to litigate against non-ERISA plans. However, he noted that anyone can file a law suit, even if it has less chance of being successful.

Craig Chaikin noted the inter-vendor fund transfers from Voya to TIAA. John O’Brien explained that Voya changed to using financial advisors dedicated to the KBOR plan, meaning that 70% or
more of their day-to-day work is with KBOR plan participants. As a result, some former advisors who were deselected were unhappy and assisted their clients in moving Voya assets to TIAA.

Reviewing the frozen vendor information, Craig Chaikin stated that it was discovered that asset information previously provided by both companies had historically been incorrect. The Board of Regents, in 2006, deselected Security Benefit and Lincoln National. As the assets with those two companies are in individual contracts, movement of the assets away from the deselected providers can only occur if the participant voluntarily elects to transfer the funds. At the request of the RPC, TIAA and Voya have conducted three separate educational outreaches to provide information to the participants still with those two companies, informing them about the fees they are being charged and the impact to their retirement savings, as well as offering to pay for any fees associated with asset movement. Thus, the Board believes it has met any fiduciary responsibilities toward those participants still invested in funds with the deselected vendors. Segal recommends moving forward to only provide line-item information for each of the deselected companies. Craig Chaikin stated that a footnote would be provided in the reports, to put into context the history about the deselected providers, the frozen assets, and prior action taken by the RPC/Board of Regents. The RPC approved this change in reporting procedure.

Nicolette Dixon asked whether there is any ability to control additional investment options being added by the deselected providers. Craig Chaikin responded that because participants have individual contracts, and those vendors are no longer part of the Board plan or subject to Board authority, it is up to each participant’s discretion and the retirement company what is being done with the investments in those contracts. Craig Chaikin noted that some of these participants have authorized financial advisors to trade within their contracts with fees being paid from the assets. There is no leverage that can be applied by the Board because the vendors have been deselected and are taking actions based upon participant instructions.

President Garrett asked whether there is information about participants who make active choices or who are who are defaulting into the Plan. Nicolette Dixon explained that prior to 2006 and the new TIAA platform that allows mutual funds, those who did not select a retirement plan company were defaulted to TIAA and into TIAA’s money market. Since 2006, TIAA is the default vendor and those who do not make an election are defaulted into the corresponding TIAA Life Cycle fund. President Garrett asked if information about performance by participant group is available. Nicolette Dixon responded that TIAA performs a Plan Outcome Assessment that would consider participant salary data and fund allocations to determine whether the participant is invested too aggressively or too conservatively.

Regent Bangerter asked about the level of assets in the TIAA Traditional fund. Tom Carmody responded that there are several reasons for the number of assets in the fund: 1) The Fund has a really good crediting rate, hovering at a guaranteed 4% for new money. 2) Historically, there were only two options for investing with TIAA, TIAA Traditional and CREF Stock. 3) The Fund also can be converted to lifetime income at retirement, which makes it attractive for those looking to manage retirement income. The Traditional fund is a high quality, low cost, fixed annuity product with a long history created for higher education. Regent Bangerter asked about the length of time needed to liquidate the fund and Tom stated it can be paid out in nine years and one day and the lower liquidity is needed in exchange for the high crediting rate received. Nicolette Dixon stated that when the 403(b) market was created, the requirement was to offer annuity contracts to provide a lifetime benefit, similar to a defined benefit plan, which offers lifetime income.
Michael Barnett asked whether management style of the target date funds is active or passive or a combination. Craig Chaikin stated it depends on the fund; all target date funds are actively managed since the glide-path and asset allocation are active decisions; however, implementation can be passive or active. The glide-path decision and how assets move from equity to fixed are active decisions by an investment manager, as well as choosing the underlying asset classes. Vanguard funds have an active glide-path with passive implementation. TIAA funds are a combination of active and passive investments. Gary Leitnaker noted those funds are among the lowest cost options within the Plan. Craig Chaikin stated they provide a real benefit for participants who either are not very engaged or who have little knowledge about what to do.

Segal specific recommendations for the following funds:

A. TIAA – Keep Royce Opportunity on the watch list due to continued performance struggles and place Wells Fargo Advantage Growth on the watch list due to relative performance over time versus the benchmark and peers.

B. Voya – Remove PIMCO Total Return from watch list as the portfolio team and organization have stabilized since Bill Gross’ departure. Performance has been average but is explained by portfolio positioning consistent with the top down approach.

KBOR Mandatory Plan Fee Overview
Craig Chaikin presented the fee overview materials reviewing fiduciary responsibility, current retirement plan lawsuits and legal environment, options for paying administrative costs, the information reviewed by the sub-committee and next steps for the RPC and Board.

Regarding the fiduciary responsibility for retirement plans, Craig Chaikin stated that non-ERISA plans, including the KBOR plan, may look to best practices where practical and he noted the RPC reviews each aspect of fund performance under the “to act solely in the interests of plan participants and beneficiaries” standard.

Craig Chaikin noted that the initial litigation in this arena was against corporate 401(k) plans but has now moved to private higher education plan sponsors. Allegations range from overpaying for investments, recordkeeping and administration to selection of funds not being solely in the best interest of participants, recordkeepers receiving excessive fees through ERISA prohibited transactions (revenue sharing), and having no prudent process in place to choose investments or to monitor fees.

Gary Leitnaker asked whether the Board’s plan has been prudent and Craig Chaikin responded “yes.” There is a defined decision making process in place, policies are documented and followed, and regular reviews are made and recorded in the RPC minutes. Even so, this would not preclude a lawsuit, but if one were filed, KBOR’s plan would likely be easier to defend because the RPC follows a prudent decision-making process. Craig Chaikin noted that when the lawsuits point to multi-vendor allegations, most have three or more vendors in the retirement plan.

Regent Bangerter asked whether there are many financial institutions following the proposed regulations now or will they wait until the regulations are finalized. Craig Chaikin responded that most of the bigger institutions are trying to implement the provisions because they see them as beneficial for their clients and to their business long-term, but others will wait to make changes until the final rules are published. John O’Brien stated that Voya is ready to comply with the regulation as of April with full compliance required by end of the year. A lot of the fiduciary focus is on
ERISA plans and the many of the services provided within the Mandatory Plan such as enrollment and general communication do not fall under the rule. The impact primarily applies to advisors working with participants about moving money out of the plan. Voya will be following the rule and has a best interest contract that will be utilized when the participant is considering moving funds out of the plan. Voya would become a fiduciary for the advice provided to the participant.

Maggie Dehn stated that some of the rule changes are process related: transparency in statements and ensuring a participant understands before recommendations are implemented. TIAA is already putting standards in place and many of the processes will be implemented by April 10th.

Craig Chaikin provided information about the current revenue sharing arrangement utilized to cover administration expenses for Voya and TIAA and alternative options that could be considered for the future including a per participant flat dollar fee, a per participant basis points fee or a combination.

Nicolette Dixon stated that for funds owned individually that are annuity contracts and funds in legacy account, there would be greater complexity as a flat dollar fee cannot be charged to individual contracts.

Several Committee members asked questions regarding the possibility of a per participant fee for the Mandatory program and both TIAA and Voya representatives commented about the transparency of the fee to participants and the flexibility of such fees. Amy Goodale commented that Voya does have the product flexibility to assess a per participant charge as well as other fee structures. It was noted that by instituting a per participant charge, participants with lower average account balances trying to save for retirement are penalized by paying more in fees in proportion to their retirement savings. In addition, it was noted that instituting a per participant charge could ultimately impact the overall servicing structure of the plans.

Amy Goodale and Nicolette Dixon noted that most participants do not currently understand what and how they are paying fees for the retirement plan, and there is a need to educate participants using various communication strategies. President Garrett suggested that if a change is made, providing comparative information to show the total fees paid for the past 2-3 years and what will be paid going forward might help participants understand that fees for administration are not new but that the method of charging fees is being changed. All commenters on this topic agreed that communication was a key component, if the Board changes how the retirement plan participants pay administrative fees.

Craig Chaikin recommended the following: Continue focusing on fiduciary processes; conduct an RFI in order to obtain information; and determine if the Board should make changes in the servicing fee structure at a later date, after more information is available. An RFI would not result in the award of a contract but would provide the RPC additional data on the appropriate servicing model and associated fees.

Regent Bangerter also requested that the RFI process include analyzing the pros and cons of using a single record keeper.

Theresa Schwartz asked about the timeframe to prepare and disseminate the RFI and to receive responses. Craig Chaikin stated that it could take 1 to 2 months to write and publish the RFI and they would normally provide five weeks for responses to be received and then an additional six
weeks to consolidate the responses.

Regent Bangerter moved that Craig Chaikin proceed with developing and drafting an RFI to gather information about fees, services and recordkeeping and that Board staff and RPC subcommittee work with Craig Chaikin to finalize the RFI and publish it. The motion was seconded by Mike Barnett and passed with one member, Gary Leitnaker, voting no.

**Next RPC meeting:**
The next regular RPC meeting is *tentatively* scheduled for 12:30 p.m. on Tuesday, September 19, 2017, in the Board Room.
Kansas Board of Regents

U.S. MID CAP GROWTH SEARCH

Defined Contribution Plan

Q1 2017

Craig Chaikin, CFA
Vice President
# Table of Contents

- **U.S. Mid Cap Growth Search**

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<th>Section</th>
<th>Page</th>
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<td>Overview</td>
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<tr>
<td>Product Comparison</td>
<td>2</td>
</tr>
<tr>
<td>Appendix</td>
<td>3</td>
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</table>
**Search Parameters**

- **Mandate:**
  - U.S. Mid-cap growth search for $5.3 million

- **Benchmark:**
  - Russell MidCap Growth Index

- **Peer Universe:**
  - Morningstar Category U.S. Fund Mid-Cap Growth

- **Purpose:**
  - The Plan is seeking to replace the VY FMR Diversified Mid Cap (IFDIX)

- **Candidates:**
  - AMG TimesSquare Mid Cap Growth Fund (TMDIX)
  - Champlain Mid Cap Fund (CIPIX)
  - Hartford MidCap Fund (HFMVX)

- **Basic Requirements:**
  - Registered investment advisor under the Investment Advisors Act of 1940.
  - Willing to assume discretionary investment responsibility in accordance with the Fund prospectus.
  - Provide periodic written reports and meetings with respect to their operations.
  - The firm must provide a Statement of Additional Information (SAI, also called Part B of the prospectus), upon request.
Asset Class Overview – U.S. Mid-Cap Growth

- **U.S. Mid-Cap Growth Investing:**
  - Concentrates on investing in mid-capitalization companies with prospects for above average growth; companies are typically identified by characteristics such as high price/book (P/B) ratios and high forecasted growth values.

- **U.S. Mid-Cap Growth Managers:**
  - Typically aim to outperform the Russell Midcap Growth Index over a full market cycle.
  - The Russell Midcap Growth Index measures performance of the growth segment of the Russell Midcap Index, which represents approximately 470 stocks out of 794 stocks in the broad U.S. equity mid-cap universe.
  - Constructed to provide a comprehensive and unbiased barometer of the mid-cap value market, the Russell Midcap Growth Index is completely reconstituted annually to ensure that larger stocks do not distort the performance and characteristics represent the true mid-cap growth opportunity set.
DC Research Overview

- **Background:** To augment Segal Marco Advisors’ (“SMA”) growth in the Defined Contribution (“DC”) marketplace, the firm created a DC Research team dedicated to mutual fund, target date fund, and stable value fund assessment to service our DC clients.

- **DC Research Process:** DC Research utilizes quantitative methods to scale the vast mutual fund universe and leverages SMA’s proprietary, independent research resources to select superior investment options. The **Segal Scoring System (“S3”)** is a proprietary quantitative mutual fund grading system that provides the foundation for mutual fund evaluation.
  - S3 seeks to identify funds with consistent metrics, relative to both its benchmark and Morningstar Category across five main categories:
    - Fund Style/Characteristics;
    - Manager Tenure;
    - Fees;
    - Performance; and
    - Risk.
  - Once DC Research screens the universe for mutual funds scoring A and B, a qualitative overlay is incorporated into the fund selection process by reviewing manager research and due diligence conducted by our Alpha Research. The manager selection process leverages Segal Marco Advisors' proprietary research framework, **Manager Research and Ranking (“MR2”)**. MR2 is a comprehensive research system applied consistently across all asset classes and utilizes both qualitative and quantitative research methods.
    - **Qualitatively:** Segal Marco Advisors' research teams require face-to-face meetings with key investment decision makers and firm leadership. Onsite visits are typical.
    - **Quantitatively:** The team will utilize a variety of tools, both proprietary and third party, to evaluate the investment returns and portfolios of these prospective managers.

- All information throughout this report is as of June 30, 2017 unless otherwise indicated.
Research Process

FUND EVALUATION

Segal Scoring System (S3)
- Scale mutual fund universe
- Streamline ongoing fund monitoring

RESULT: Depth of research and resources efficiently guide mutual fund evaluation

28,000+ mutual funds
- S3: A
  - Alpha: Recommended
- S3: B
  - Alpha: Recommended
- S3: C
  - Alpha: Recommended
- S3: A/B
  - Alpha: NR
- Funds
## Firm Summary

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<tr>
<th>Advisor</th>
<th>AMG TimesSquare¹</th>
<th>Champlain</th>
<th>Hartford Funds¹</th>
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<td>Headquarters</td>
<td>New York, NY</td>
<td>Burlington, VT</td>
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<td>Year Founded</td>
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<td></td>
<td>TimesSquare Capital Management, LLC</td>
<td>Wellington Management Company LLP</td>
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Source: eVestment Alliance 3/31/2017
Note: ¹ Represents sub-advising firm
# Fund Summary

## Fund Facts

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<tr>
<th>Ticker</th>
<th>Morningstar Institutional Category</th>
<th>Fund Inception Date</th>
<th>Primary Prospectus Benchmark</th>
<th>Prospectus Net Exp Ratio</th>
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<td>Champlain Mid Cap Institutional</td>
<td>CIPIX</td>
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<td>Russell Mid Cap TR USD</td>
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<td>Hartford MidCap R6</td>
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## Characteristics

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<tr>
<th>Fund Size</th>
<th># of Stocks</th>
<th>% Asset in Top 10</th>
<th>Avg Market Cap (mil)</th>
<th>P/E Ratio (TTM)</th>
<th>P/B Ratio (TTM)</th>
<th>Turnover Ratio %</th>
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Source: Morningstar Direct
# Asset Allocation

## Asset Allocation

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<th>Bond %</th>
<th>Other %</th>
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## Relative Sector Exposure

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<tr>
<th>Calculation Benchmark: Russell Mid Cap Growth TR USD</th>
<th>Basic Materials %</th>
<th>Communication Services %</th>
<th>Consumer Cyclicals %</th>
<th>Consumer Defensive %</th>
<th>Healthcare %</th>
<th>Industrials %</th>
<th>Real Estate %</th>
<th>Technology %</th>
<th>Energy %</th>
<th>Financial Services %</th>
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## Market Capitalization Exposure

- **Large %:** 22, 18, 22
- **Mid %:** 50, 75, 75, 76, 73
- **Small %:** 20, 16, 17, 4

Source: Morningstar Direct
Fund Exposure

Holdings-Based Style

Equity Sector Exposure

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<th>Fund Name</th>
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<th>Basic Materials</th>
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<td>5.04</td>
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<td>17.35</td>
<td>4.39</td>
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Source: Morningstar Direct
Segal Marco Overview

AMG TimesSquare Mid Cap Growth Fund

- **S3 Score: B**
  - The fund’s investment process focuses on high-growth companies with superior business models and strong management teams.
  - The fund consistently posts a lower tracking error than Champlain or Hartford.
  - Although the fund has encountered some headwinds in recent years, especially year-to-date 2017 and 2014, long-term performance remains strong. While it primarily emphasizes downside protection, strong performance in 2013 shows the fund can compete in strong bull markets as well.

Champlain Mid Cap Fund

- **S3 Score: B**
  - The fund seeks to invest in companies with the ability to grow and outperform the market consistently regardless of major market events.
  - The fund is the most conservative candidate with the best downside protection. It is also the only candidate to post a positive information ratio across all time periods.
  - While YTD performance so far this year has been below median, performance across longer time periods is consistently in the first quartile. This fund has seen the greatest growth over the last 10 years.

Hartford Mid Cap Fund

- **S3 Score: B**
  - The fund invests in high quality market leaders that are well positioned to outperform and should benefit from a positive catalyst in the future.
  - The fund consistently exhibited better upside capture than AMG or Champlain, but has not always protected on the downside, as demonstrated in 2011.
  - Performance has been strong, falling in the first quartile for all time period except year-to-date.
AMG TimesSquare Mid Cap Growth Fund

Manager Profile Report

Team:
- The Strategy is led by Grant Babyak and Tony Rosenthal, and supported by ten, senior level investment analysts. While the portfolio managers are generalists, the analysts maintain coverage of specific industries and sectors.
- Babyak and Rosenthal have been with the firm since inception and average 28 and 27 years of experience respectively, while the analyst team averages 18 years of experience and 8 years at TimesSquare.

Strategy:
- The team’s investment philosophy is that proprietary fundamental research, with particular emphasis on the assessment of management quality and an in-depth understanding of superior business models, will lead to the construction of a diversified portfolio of stocks that will generate superior risk-adjusted returns.
- The team requires that companies demonstrate the ability to consistently grow earnings and sales by at least 15% per year. This requirement reduces the investable universe to approximately 250 names that the analysts follow closely.
- Once the team has identified a high quality company, they model the company’s projected future growth, seeking 25-50% price appreciation over the next 12-18 months. The analysts set a target price for the security, which is monitored and adjusted as needed.

Portfolio:
- The Fund invests in 65-75 stocks.
- Annual turnover is 10-45%.
- Sector weights are limited to 45%.
- Portfolio holding weights are based on the portfolio management team’s conviction in the stock with a maximum size 7%.
- Cash balance is less than 10%.

* NOTE: Information contained in this document is of confidential nature and may not be redistributed without the explicit consent and authorization of Segal Marco Advisors.
Manager Profile Report

Team:
• The Strategy is led by Scott Brayman, who co-founded the firm in 2004 but has been in the industry since 1985. The Strategy is managed by a team of five senior investment professionals, including Brayman, as well as three senior associates and one associate analyst.
• Portfolio managers are supported by four SMID-cap research analysts, averaging 3 years of tenure and 7 years of industry experience.

Strategy:
• The team is focused on identifying companies with low product/service obsolescence risk, low exposure to business and interest rate cycles and those known for their innovation and problem solving skills. Ideally, businesses exhibit consistent and predictable earnings and cash flow streams, positive return on invested capital, low financial leverage, and proven business models.
• The team identifies favorable sector-specific factors it believes position companies to outperform sector peers. Once they identify well-positioned companies, they analyze the above company-specific quality factors through an Economic Value Added accounting framework to identify companies that consistently generate an economic profit.
• Finally, they run a valuation analysis to determine fair value. Once fair value is determined, they set a strict target level for purchase, generally a 20-25% discount to fair value.

Portfolio:
• The Fund invests in 50-75 stocks.
• Annual turnover is 35-50%.
• Initial position size is typically 2% with a maximum of 5%.
• Sector exposure is limited to +/-25% vs. the benchmark.
• Up to 15% in securities of foreign issuers listed either on the U.S. stock exchange or represented by the ADRs, although the historical high is 9.1%.
• Maximum cash position is up to 10%.
Hartford Mid Cap Fund

Manager Profile Report

Team:
- The Hartford Mid Cap Fund was launched in 1997 and is sub-advised by Wellington.
- The Fund is managed by lead portfolio manager Phil Ruedi (24 of investment experience) and associate portfolio manager Mark Whitaker (18 of investment experience), both of whom joined the firm in 2004.
- Joe Sicilian, research analyst, and Wellington's team of global industry analysts offer analytical support.

Strategy:
- The team seeks to outperform the mid cap benchmark and peers by investing in industry leading mid cap companies (market caps between $2 and $10 billion) that possess sustainable business models and strong growth prospects.
- The approach pursues this objective with a focus on quality, and diversification. Leveraging the firm’s resources, they perform bottom-up research with an emphasis on fundamentals, valuation, and earnings expectations. They focus on identifying market-leading companies with high market share, quality balance sheets, and strong management teams.
- The team considers a company's business model, growth drivers, management team, and valuation using various metrics, including price/cash flow, price/earnings, and discounted cash flow models.
- Ultimately, purchase candidates are attractive based on their fundamental outlook, have a positive catalyst such as accelerating earnings or revenue growth, or have a high probability of multiple expansion.

Portfolio:
- The portfolio is broadly diversified, with 70-120 securities.
- Position sizes generally will not be higher than 5%.
- While not a formal guideline, the portfolio will generally be invested across most major sectors, and should provide broad industry representation. Sector weights are limited to 2x the benchmark weight.
- The portfolio’s exposure to non-US securities can reach 20% of assets, but typically will be less than 10%.
- Portfolio turnover averaged between 25-45% in the past few years.

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Returns: Annualized QTD, YTD, 1, 3, 5, 7 & 10 Years

Performance Relative to Peer Group
As of Date: 6/30/2017  Peer Group (5-95%): Open End Funds - U.S. - Mid-Cap Growth

Trailing Returns

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<thead>
<tr>
<th>Return &amp; Peer Group Percentile</th>
<th>QTD</th>
<th>%</th>
<th>YTD</th>
<th>%</th>
<th>1 Year</th>
<th>%</th>
<th>3 Years</th>
<th>%</th>
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<th>%</th>
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Source: Morningstar Direct
Returns: Last 10 Calendar Years

Performance Relative to Peer Group
Peer Group (5-95%): Open End Funds - U.S. - Mid-Cap Growth

Calendar Year Returns

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Source: Morningstar Direct
Investment Growth

Time Period: 7/1/2008 to 6/30/2017

Source: Morningstar Direct
Upside vs. Downside

3-Yr Rolling
Time Period: 7/1/2010 to 6/30/2017

Source: Morningstar Direct

As of Date: 6/30/2017

<table>
<thead>
<tr>
<th>Down Capture Ratio</th>
<th>3 Years</th>
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<th>Up Capture Ratio</th>
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<td>US Fund Mid-Cap Growth</td>
<td>97.0</td>
<td>96.2</td>
<td>96.3</td>
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</table>

Source: Morningstar Direct
Investment Terminology

- **Alpha**: The excess return of a portfolio generally attributable to active manager skill. It is the extra risk-adjusted return over the benchmark. This risk-adjusted factor takes into account both the performance of the benchmark and the volatility of the portfolio. Positive alpha indicates that a manager has produced returns above expectations at that risk level. Negative alpha indicates that a manager has produced negative relative returns at that risk level. When selecting between active investment managers, a higher alpha is generally preferred. In contrast, a pure passive strategy would have an alpha of 0.

- **Batting Average**: A measurement of a manager’s ability to consistently match or exceed the benchmark. It is the number of periods of matching or excess performance as compared to the benchmark over the selected time horizon. A batting average of .750 indicates that the manager matched or exceeded the benchmark exactly three-quarters of the time (i.e., three out of four calendar quarters). Batting average does not quantify the magnitude of any excess performance.

- **Beta**: Measured by the slope of the least squares regression, beta is the measure of portfolio risk which cannot be removed through diversification. Beta is also known as market risk or systematic risk. Beta is a statistical estimate of the average change in the portfolio’s performance with a corresponding 1.0 percent change in the risk index. A beta of 1.0 indicates that the portfolio moves, on average, lock step with the risk index. A beta in excess of 1.0 indicates that the portfolio is highly sensitive to movements in the risk index. A beta of 1.5, for example, indicates that the portfolio tends to move 1.5 percent with every 1.0 percent movement in the risk index. A beta of less than 1.0 indicates that the portfolio is not as sensitive to movements in the risk index. A beta of 0.5, for example, indicates that the portfolio moves only 0.5 percent for every 1.0 percent movement in the risk index.

- **Correlation Coefficient (R)**: The correlation coefficient measures the extent of linear association between 2 variables. The range of possible correlation coefficients is –1.0 to +1.0. A correlation coefficient of 0.0 indicates that the 2 variables are not correlated. Zero correlation would imply that the 2 variables move completely independently of each other over time. The correlation coefficients –1.0 and +1.0 indicates perfect correlation. Negative correlation coefficients imply that the 2 variables move in opposite directions and positive correlation coefficients imply causality. The fact that 2 variables are highly correlated does not imply that one variable caused the other to behave in a particular fashion.

- **Coefficient of Determination (R2)**: Measures the strength of the least squares regression relationship between the portfolio (the dependent variable) and the risk index (the independent variable). The statistic reveals the extent to which the variability in the dependent variable can be explained by the variability in the independent variable. The strength of the R-squared statistic will reflect on the strength of alpha and beta. A weak R-squared, for example, would indicate that alpha and beta cannot be strictly interpreted. For example, with regard to an investment manager’s product being regressed against an index, a R-squared of 0.75 implies that 75% of that manager’s returns can be explained by the index.

- **Diversification**: Minimizing of non-systematic portfolio risk by investing assets in several securities and investment categories with low correlation between each other.
Investment Terminology

- **Downside/Upside Market Capture:** A measurement of portfolio performance as compared to the benchmark. Market capture indicates how much, on average, a portfolio captures in performance terms relative to its benchmark. A downside market capture of 90% indicates that, on average, if the benchmark is down 10% for a given period, the portfolio would only be down 9%. An upside market capture of 110% indicates that, on average, if the benchmark is up 10% for a given period, the portfolio would be up 11%. Market capture quantifies the average magnitude of any excess performance (or shortfall) as compared to the benchmark. All other factors being equal, an upside market capture of over 100% and a downside market capture of less than 100% is generally preferred, although the market capture can be an indication of overall portfolio volatility as compared to the benchmark.

- **Information Ratio:** A measurement of portfolio efficiency. It quantifies the excess return earned per unit of active risk assumed. The information ratio is the excess return divided by the tracking error. A relatively higher information ratio is indicative of excess positive, risk-adjusted performance. When comparing portfolios, the highest absolute information ratio is generally preferred.

- **Sharpe Ratio:** A measurement of reward per unit of risk, with risk being defined as a portfolio’s standard deviation. It is the risk-adjusted excess performance while taking into account the risk-free return (i.e. T-Bill or similar proxy) and the portfolio standard deviation. When comparing portfolios, the highest absolute Sharpe ratio is generally preferred.

- **Standard Deviation:** A statistical measure of relative dispersion as compared to the expected (average) return. Calculating the standard deviation is a method of quantifying the total risk of a portfolio, or the given benchmark. In general terms, the standard deviation of a portfolio will help to define a range of expected returns. In percentage terms, one standard deviation will encompass 68% of the expected returns, two standard deviations will encompass 95% of the expected returns and three standard deviations will encompass 99% of the expected returns. For example, if a portfolio has an expected return of 5% and a standard deviation of 2.5%, 68% of the time the portfolio expected return should be between 2.5 to 7.5%, 95% of the time between 0.0 to 10.0% and 99% of the time between 2.5 to 12.5%.

- **Tracking Error:** Tracking error is the standard deviation of the excess returns and is used as a measure to quantify active risk. The excess returns as compared to the benchmark can be positive or negative. Conceptually, tracking error is identical to standard deviation, although calculated from a different array of data. For example, if a portfolio has a tracking error of 2%, 68% of the time the portfolio expected return should be between +/- 2% of the benchmark return, 95% of the time between +/- 4% and 99% of the time between +/- 6%.

- **Volatility:** A measure of the size and frequency of the fluctuations in the value of a stock, bond or a portfolio. The greater the volatility, the higher the risk involved in holding the investment.
Segal Marco Disclosure Statement

Segal Marco has a fiduciary duty to act in the best interests of our clients at all times and to place their interests before our own. In seeking to honor this principle, we constantly abide by one overriding rule - an absolute commitment to independent and unbiased advice. Moreover, the Company has a fiduciary duty of full and fair disclosure of all material facts to its clients. The following disclosure addresses areas of perceived conflict of interest:

### Summit Alliance
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The above chart indicates whether or not managers included in this search book have an affiliated investment management company that purchases services from Segal Marco. Segal Marco has in affect mechanisms to ensure that investment managers are recommended by our consultants without regard to whether or not their affiliated investment management company purchases services from Segal Marco.
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Executive Summary

- **Islamic Compliant Investment Options**
  - There are two major Islamic compliant investment options in the US that are accessible to 403(b) retirement plans: Saturna Capital and Azzad Asset Management
  - Both firms have strict investment processes to ensure compliance with Islamic law and are overseen by independent Boards of renowned professionals in Islamic finance
  - Both firms follow The Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) guidelines for Islamic investing

- **Considerations**
  - **Saturna Capital**
    - The largest Islamic fund family offering in the US and has $3.4 billion in total assets under management; $1.6 billion in Amana Growth and $1.5 billion in Amana Income
    - Only 14 analysts covering both equity and fixed income across the globe support 14 investment products
  - **Azzad Asset Management**
    - Only $487 million in total assets: the Ethical fund ($68 million) and the Wise Capital fund ($104 million)
    - Both funds have recent changes to the investment manager and investment process so the longer-term track records are not attributable to the current investment manager teams

- **Recommendation**
  - Add the Amana Growth Fund (AMIGX) and Amana Participation Fund (AMAPX)
    - With more assets, Saturna appears to be a more stable firm than Azzad
    - A consistent investment approach has been applied on both funds
    - Including both options allows an investor exposure to both equity and fixed income options that meet Islamic investment principles
      - There are no assets in the institutional share class of the Participation Fund (AMPIX), which is why SMA is recommending using ticker AMAPX instead
  - The addition of specific investment options becoming more commonplace in higher education and governmental participant directed defined contribution plans as a reasonable accommodation of religious objections
  - Both options meet the guidelines of the Investment Policy Statement
    - The Appendix will need to be updated for the additions to the line-up
Saturna Capital

❯ Firm
Saturna Capital was founded in 1989 by Nick Kaiser and is headquartered in Bellingham, Washington. At the founding of the firm, they were an advisor to the Amana Income Funds, having secured this relationship from a preceding firm (Unified Asset Management) that was sold by Nick to a large insurance company. Saturna manages assets in mutual funds, separate accounts, discount brokerage and retirement plan services. The firm operates in both the US and Malaysia.

Saturna specializes in values-based asset management, and its largest strategy takes religious values into the selection process. In particular, it operates in the Islamic mutual fund space for US-based investors. The Amana Funds are the largest Islamic screened investment options distributed in the US. The values-based approach permeates the Investment Committee and is a cornerstone of the long-term investment horizon. From a 3-person, family-run firm started in 1989, Saturna now has 68 employees with $3.4 billion in total AUM across 14 strategies. Two of the firm’s largest strategies are the Amana Growth fund ($1.6 B) and the Amana Income fund ($1.3 B), which make up 70% of the firm’s assets.

❯ Team
Founder Nick Kaiser leads the team. He is listed as a Portfolio Manager (PM) on all of the strategies; however, he is only lead PM on the Amana Growth and Income strategies while Scott Klimo is lead on Developing Markets and Patrick Drum is lead on Participation. They are supported by 11 other individuals. The team is broken out into 11 equity investors and 3 fixed income investors based in Bellingham, WA and Kuala Lumpur, Malaysia.

❯ Strategy
Four funds are offered under the Amana umbrella:

- **Income**: US focused and targeted to investors seeking current income and preservation of capital. Tends to invest in large, dividend-paying companies (either with a high yield or consistently increasing dividend).
- **Growth**: US focused and targeted to investors seeking long-term capital growth. Generally large cap stocks.
- **Developing Markets**: Emerging Market focused and targeted to investors seeking value and diversification beyond developed markets.
- **Participation**: Global focus and targeted to investors seeking current income and preservation of capital. Able to invest in short-term and intermediate-term Islamic compliant income-producing investment certificates (i.e., sukuk, murabaha, wakala). This is a more conservative approach and targets 3-5% return.

Strategies are typically low turnover (approximately 20% per year depending on strategy), as they seek to be as tax efficient as possible. Each of the funds holds approximately 30-50 stocks, with about 5 to 10% overlap between the two large cap funds.
Saturna Capital

➤ Process
At its core, the equity investment philosophy focuses on identifying growing, well-managed, profitable, cash-generating businesses trading at attractive valuations. The screening and global investing expertise helps Saturna uncover opportunities in every region. The team conducts fundamental analysis, covering a company’s suppliers, customers, competitors and industry trends. All the analysts cover their industries on a global level. The research process is managed from corporate headquarters in Bellingham, Washington.

Saturna uses a proprietary screening system, Neptune, which is applied across all of Amana’s funds. To start, the screen filters out alcohol, pornography, gambling and insurance. There are other considerations included, such as the debt to market cap ratio as well as the accounts receivable ratio. If the debt to market cap is above 33%, they will not invest. Accounts receivable to market value is limited to 45% as anything more becomes speculative. Saturna relies heavily on the AAOIFI Global Standards for guidance on Islamic compliant investing.

The negative screens are reviewed internally each month by Saturna and Amanie Advisors Sdn Bhd, a leading consultant specializing in Islamic Finance, to ensure compliance with the Global Standards. Additionally, Saturna works with the Fiqh Council of North America (FCNA), a non-profit organization serving the Muslim community, to review and revise its screening guidelines as necessary.

After the screens, the 11,000 stock universe is filtered to about 5,000-6,000 companies. These stocks are further screened based on fundamental metrics (such as traditional valuation and growth metrics). The goal is not to go through each name but to identify companies that are attractive and should go into the recommended list. The Recommended List currently has 300 securities.

The fundamental data for the screens is from FactSet. Individual review is up to the analyst who utilize Bloomberg and Factset.

➤ Considerations:
• Saturna is the largest Islamic fund family offering in the US
• It appears that Saturna has the most robust suite of Islamic based investment options
• 14 analysts work on all Saturna strategies; teams are based in Kuala Lumpur or Bellingham, WA. The expertise of the analysts in Kuala Lumpur is impressive, given the region is the largest in the Islamic investing space. However, there are only 14 analysts covering both equity and fixed income across the globe and providing ideas for all 14 Saturna strategies.
Azzad Asset Management

Firm
Azzad Asset Management was founded in 1997 by Bashar Qasem and is based in Falls Church, VA. The entire firm is focused on halal investing; however of the firm’s ten total strategies, only two are Islamic compliant mutual funds. Total assets under management is $487 million with the Azzad funds comprising $170 million. Only half of the assets are in qualified plans.

Third party investment firms manage the majority of the firm’s strategies though Azzad does have a small team of in-house investors for its REIT and Dividends products. The internal team ensures the funds are AAOIFI compliant. In addition, Azzad has an in-house Islamic investing compliance officer. The firm has an independent Sharia Advisory board, which consists of an active 3-members who are also practitioners in Islamic investing. The Board independently vets Azzad’s processes, and its responsibilities include:

- Providing guidance to the company on Islamic investing compliance matters and helping to create a strong internal Islamic investing compliance control system;
- Ruling on religious financial matters for circumstances in which there is no precedent from AAOIFI;
- Training Azzad employees on matters related to Islamic financial transactions;
- Reviewing the method by which the company calculates zakah and purification amounts for clients;
- Reviewing the annual Islamic investing compliance verification process;
- Periodically conducting an Islamic investing compliance audit or overseeing such an audit by an external auditor; and
- Issuing an annual Islamic investing compliance statement.

Additionally, Azzad has an independent, third party auditor, Islamic Finance Advisory and Assurance Services (IFAAS) conduct an independent audit.

Team
Azzad manages and oversees its portfolios on a team basis through a 5-person Investment Committee. The Committee reviews, analyzes and discusses the various forces and factors that affect the financial markets and, in turn, the portfolios. The committee’s review includes (but is not restricted to) macroeconomic trends, risk/reward profiles for various markets, strategy allocations, portfolio characteristics, and performance. Currently, the Committee members include Manal Fouz, Bashar Qasem, Fatima Iqbal, Jamal Elbarmil, and Ahsan Raheem.

The committee is responsible for the management of the in-house products as well as the manager selection of the sub-advised funds.
Azzad Asset Management

Strategy

The two, Islamic Compliant funds are Azzad Wise Capital (Fixed Income) and Azzad Ethical (Equity). Wise Capital is sub-advised by Federated Investors out of Pittsburg, PA and Ethical is sub-advised by Ziegler Capital out of Chicago, IL.

The Ethical fund has a track record dating back to December 2000 and has $68 million in total assets. However, the track record prior to July 2013 is from another investment team and investment process. The Wise Capital fund has a track record dating to April 2010 and has $104 million. The track record prior to January 2016 is from another investment team and investment process.

Process

Prior to 2013, the Azzad Ethical fund was actively managed by an in-house team through a fundamental, bottom-up research process. However, the management committee decided to hire Ziegler, who employs an enhanced, optimized index strategy, as sub-advisor in 2013. Azzad selected Ziegler due to its experience and comfort level with Ziegler who had managed Azzad’s large cap growth strategy.

Azzad launched the Wise fund in April 2010 following a yearlong process with the SEC to get registration. With its launch, the Wise fund became the first Halal SRI Fixed Income fund in the U.S. At the time, the fund was managed internally and invested in sukuks, Islamic bank deposits and dividend paying equity stocks. The management committee determined using a sub-advisor was more efficient and began vetting fixed income managers. Federated was ultimately selected in July 2013 because of its track record of already investing in sukuks for its conventional fixed income portfolios. Today, about half of the strategy is invested in sukuks with the other half in Islamic banking deposits and a small percentage (8.4%) in equity dividend stocks.

Considerations:

- Both Azzad funds have recent changes to the investment manager and investment process so the longer-term track records are not attributable to the current investment manager teams
  - For the Wise fund, the transition from Azzad’s in-house team to Federated took nearly two years and was not completed until late 2015
- Overall, the firm has a low level of assets and has not gained much traction in its two Islamic investing compliant options, the Ethical or Wise Capital
Key Terms

- **The Accounting and Auditing Organization for Islamic Financial Institutions**: Established in 1991 is the leading international not-for-profit organization primarily responsible for development and issuance of standards for the global Islamic finance industry. Has issued 94 standards in the areas of Shari’ah, accounting, auditing, ethics and governance. Standards are adopted by central banks and regulatory authorities in a number of countries, either on a mandatory basis or as basis of guidelines. AAOIFI is supported by numbers of institutional members, including central banks and regulatory authorities, financial institutions, accounting and auditing firms, and legal firms, from over 45 countries.

- **Sukuk**: Bonds structured in such a way as to generate returns to investors without infringing on Islamic law, which prohibits riba (interest). Represents undivided shares in the ownership of tangible assets relating to particular projects or special investment activity. Structures may be significantly more complicated than conventional bonds and often include a series of entities created specifically to support the sukuk structure. Are largely created in or otherwise subject to the risks of developing economies, many of which have weak or inconsistent accounting, legal, and financial infrastructure. The structural complexity of sukuk, along with the weak infrastructure of the sukuk market, increases risks of investing in sukuk, including operational, legal, and investment risks. As compared to rights of conventional bondholders, holders of sukuk may have limited ability to pursue legal recourse to enforce the terms of the sukuk or to restructure the sukuk in order to seek recovery of principal. Sukuk are also subject to the risk that some Islamic scholars may deem certain sukuk as not meeting Islamic investment principles subsequent to the sukuk being issued and therefore classify the investments as noncompliant with Islamic principles.
Overview

As advised by Segal Marco Advisors, the Kansas Board of Regents Retirement Plan Committee (KBOR RPC), at its March 2017 meeting, approved conducting a Request for Information (RFI) for defined contribution recordkeeping and participant services with the goal of:

- Benchmarking the current administrative fees
- Benchmarking the current administrative & participant services
- Reviewing the market of defined contribution administrators
- Exploring different servicing models

The RFI was issued on May 31, 2017

Segal Marco Advisors sent the RFI directly to the following companies; it was also posted on the KBOR website and the Kansas Registrar:

- Fidelity
- Lincoln
- TIAA
- Transamerica
- VALIC
- Vanguard
- Voya

Respondent questions were submitted by June 8, 2017 with replies transmitted back on June 15, 2017

Three of the companies contacted directly elected to not submit a response:

- Vanguard will not reply to any relationship with multiple providers unless a move to a sole provider is certain
- Transamerica and VALIC did not respond despite multiple follow-up attempts

Responses were received on June 29, 2017 from the following four service providers:

- Fidelity
- Lincoln
- TIAA (incumbent)
- Voya (incumbent)

All four service providers meet the qualifications as outlined in the RFI

While there has been a trend towards recordkeeper consolidation in the 403(b) market, there are still many Optional Retirement Plans and higher education 403(b) programs that retain multiple recordkeepers; common consolidation has been from many down to two
Sub-Committee Recommendation & Next Steps

After review of the responses to the RFI, the RPC sub-committee recommends:

- Remaining with the current two-vendor structure
- Retaining TIAA and Voya as the two vendors
  - Since consolidation to two vendors in 2006, Voya has consistently enrolled 25% of the eligible population, even though it is not the default company for those who do not select a mandatory retirement company.
  - Having two vendors helps to ensure healthy competition and allows participants a choice in fund selection and a different service model that provides a high level of touch.
- Implementing fees and services proposed in the RFI
  - Both TIAA and Voya lowered their administrative fees, which are competitive relative to the services provided
  - The current servicing model under both single and multi-vendor models is higher than that proposed by Fidelity and Lincoln
  - TIAA and Voya offer different models that are popular among different participant bases

Since no formal Request for Proposal, next steps would be:

- Amending existing contracts to new administrative pricing
- Implementing any additional services contained in the RFI (e.g. increasing onsite education services)