



Agenda Item 5e

June 17, 2013

ITEM NAME: Revision of the Supplemental Income Plans (SIP) Target Retirement Date and POFF Funds Policies

PROGRAM: Affiliate Investment Programs

ITEM TYPE: Policy & Delegation – Action

RECOMMENDATION

Approve the revised “Statement of Investment Policy for Supplemental Income Plans (SIP)” and “Statement of Investment Policy for Supplemental Income Plans CalPERS Target Retirement Date and POFF (State Peace Officers’ and Firefighters’ Defined Contribution Plan, i.e. the “POFF”) Funds” policies as shown in Attachment 2 and 3, respectively. The Wilshire Associates’ Opinion Letter is provided in Attachment 4.

EXECUTIVE SUMMARY

On May 14, 2013, the Pension and Health Benefits Committee approved the SIP fund lineup change. Today, staff will present the analysis for the SIP Investment Lineup (Attachment 1) and Target Retirement Date Fund asset allocations.

STRATEGIC PLAN

This agenda item supports the CalPERS Strategic Plan goal to improve long-term pension and health benefit sustainability. Regular review of the SIP investment fund lineup is important to help ensure that CalPERS meet participants’ retirement savings needs while being competitive in the supplemental savings market place.

BACKGROUND

The CalPERS SIP consists of the CalPERS 457 Plan, POFF, Supplemental Contributions Plan (SCP), and Placer Country 401(k) Plan. Staff provided information on the Strategic Review of the SIP to the Investment Committee in October 2012 and the Pension and Health Benefits Committee in April and May 2013. Highlights from the Strategic Review include:

- In late 2011, staff initiated the Strategic Review of the SIP to gauge the value proposition and competitiveness of the CalPERS SIP design and fund lineup. Though CalPERS monitors and evaluates performance of each investment fund option on an ongoing basis, staff wanted to undertake another holistic review of the fund lineup since it was implemented in 2008 to include CalPERS customized Target Retirement Date and Risk-based Funds.

- A survey conducted by RV Kuhns of employers and members about their supplemental savings preferences, and a review of the competitive environment for supplemental savings plans and investment offerings, including information on CalPERS SIP strengths and opportunities for improvement.
- RV Kuhns reviewed and recommended an investment fund lineup and refreshed the asset allocations for the Target Retirement Date and POFF funds.

ANALYSIS

The Investment Office, along with the Customer Support & Services leadership team, collaborated on the investment lineup review. Due to the various asset classes involved in this review, the Investment Office project team representatives included equity, fixed income, operations and compliance.

The project began with the team drafting guiding principles for the investment fund lineup based on the RV Kuhns research and Investment Office strategic priorities.

The guiding principles include:

- An appropriate range of investment options intended to avoid an overly complex fund lineup that might confuse the average participant
- A cash equivalent option is important
- Custom Target Date Funds should be in the SIP fund lineup
- Self-Managed Account (SMA) Brokerage windows provide choices for participants looking for options beyond the SIP fund lineup
- Costs matter to participants
- Passively managed funds are less costly and generally preferred by participants
- Investment management could be internal or external
 - Internal capabilities
 - Costs
 - Operational risks

The Revised SIP Fund Lineup

As part of the Strategic Review project, the Investment Office worked with RV Kuhns to recommend an investment fund lineup while considering these principles and where possible, to leverage the investment management services of State Street Global Advisors (SSgA). SSgA was selected and awarded a contract in 2012 from the Investment Office Multi-Strategy Index Fund Request for Proposal solicitation process. The SSgA contract allows for the affiliate funds, including the SIP, to utilize the diversified menu of SSgA passive index funds that provide exposure across asset classes.

RV Kuhns recommended an investment fund lineup that was adopted by the project team, as shown below under the “Fund” column, in the New Fund Lineup table. This investment lineup was approved by the Pension and Health Benefits Committee on May 14, 2013.

New Fund Lineup

Current Lineup		New Lineup	
Fund	Fund Manager	Fund	Fund Manager
Active: Target Date	CalPERS and External	Passive: Target Date Funds	CalPERS and SSgA
Active: Risk-Based	CalPERS and External		
Cash: Short-Term Investment	SSgA	Cash: Short-Term Investment	SSgA
Active: U.S. Equity Small-Mid Cap (SMID) Growth	The Boston Company	Passive: U.S. Equity Index	SSgA
Active: U.S. Equity SMID Value	The Boston Company		
Passive: U.S. Equity SMID Index	CalPERS		
Passive: U.S. Equity Large Cap Index	CalPERS		
Active: International Equity	Pyramis Global Advisors	Passive: International Equity Index	SSgA
Passive: International Equity	CalPERS		
Active: Short-Term Bond	PIMCO	Passive: Short-Term Bond	SSgA
Active: Intermediate Bond	CalPERS	Passive: Intermediate Term Bond	SSgA
Active: Treasury Inflation Protected Securities (TIPS)	CalPERS	Passive: Real Assets*	SSgA
Self-Managed Account (SMA) Brokerage Window	SSgA	Self-Managed Account (SMA) Brokerage Window	SSgA

***Real Assets** – SSgA (State Street Global Advisors) Real Asset strategy objective is to mitigate the risk of loss of purchasing power by investing in TIPS, Commodities, Real Estate Investment Trusts (REITs) and resource stocks.

The new investment fund lineup reflects the elements from RV Kuhns’ research and analysis, as well as the project team’s guiding principles. It offers a diverse range of alternatives with materially different risk and return characteristics with broad market exposures, while avoiding an overly complex fund lineup that might confuse the average participant, and reduces operational complexity and risks. The Supplemental Income Plans Investment Policy which has been revised to reflect these principles and the new investment fund lineup, is provided in Attachment 2.

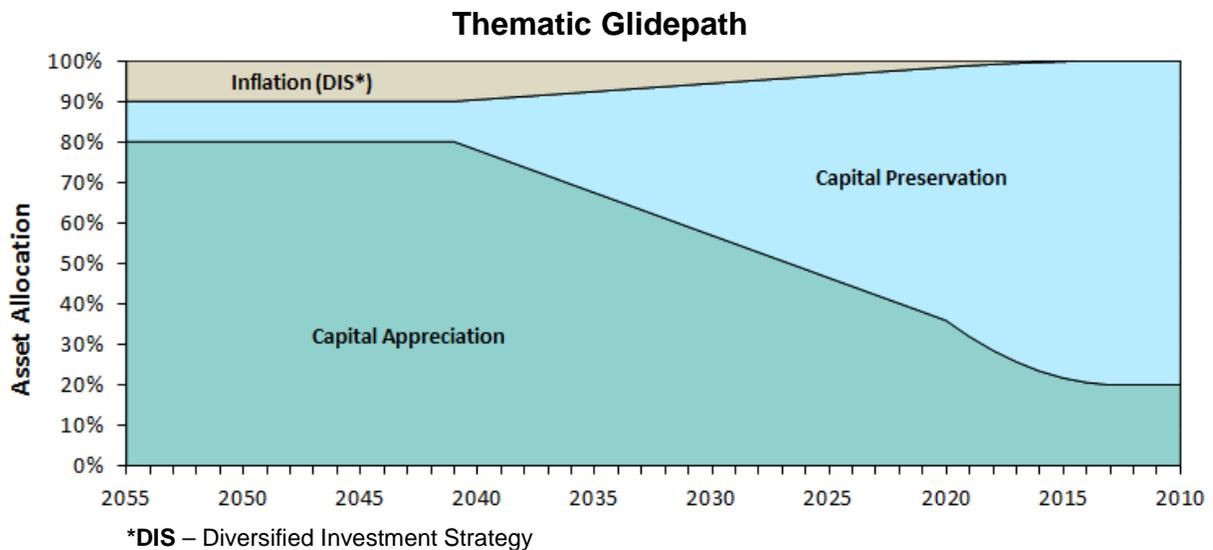
Target Retirement Date Funds

Another piece of the SIP fund lineup review included updating the Target Retirement Date Funds' asset allocations based on current market return assumptions, correlations and participant data. To do this, RV Kuhns gathered and analyzed member pension benefit and demographic data provided by the CalPERS Actuarial Office and the SIP record-keeper's systems.

RV Kuhns' analysis shows the average SIP participant:

- Retires around age 60
- Receives approximately 78% of their retirement income from their pension and social security
- Utilizes the SIP as a supplemental savings tool rather than for monthly income replacement
- Takes a complete distribution of their account in the first year after retirement

From this research, RV Kuhns analyzed the current SIP Target Retirement Date Funds' asset allocations and recommended a revised allocation by increasing capital preservation throughout the investment strategy and increasing liquidity near retirement. For 2013, the recommended asset allocation for each of the Target Retirement Date Funds is shown below in the Thematic Glidepath.



This graph is called a “glidepath” since it demonstrates how the asset allocation would change or “glide” as participants move toward retirement. As an example, an 18 year old participant in the 2055 fund would have an 80% allocation to capital appreciation. In contrast, a participant at or near 60 years of age and retirement would only have a 20% allocation to capital appreciation. The glidepath stops changing near the retirement date and becomes focused on capital preservation intended to protect participant retirement savings near the distribution date.

The POFF Fund

The POFF Fund consists of employer only contributions invested in the Moderate Risk-based fund. The new POFF Fund will maintain similar risk characteristics and a static asset allocation that is equivalent to the Target Retirement Date Fund 2030 shown in the Thematic Glidepath chart.

In Attachment 3, the Statement of Investment Policy for Supplemental Income Plans CalPERS Target Retirement Date and POFF Funds policy has been revised to include updated asset allocation targets and ranges for the Target Retirement Date and the POFF funds.

BENEFITS/RISKS

The new investment fund lineup requires changing the existing fund lineup with new funds where participants will be given an opportunity to select a new fund. If participants' contributions are invested in a fund that will be removed, they can control how those assets are redirected by affirmatively instructing the transfer of such assets to another investment fund offered under the SIP. If participants do not provide affirmative instructions, their assets will be mapped to the applicable new investment fund. To help ensure that participants understand their options and the new fund lineup, staff is developing an extensive communication plan with multiple communications to participants to request that participants provide affirmative instruction if they do not want their assets mapped to the applicable replacement fund.

ATTACHMENTS

- Attachment 1 – Supplemental Income Plans Investment Lineup
- Attachment 2 – Revised Statement of Investment Policy for Supplemental Income Plans
- Attachment 3 – Revised Statement of Investment Policy for Supplemental Income Plans CalPERS Target Retirement Date Funds and POFF Fund
- Attachment 4 – Wilshire Associates' Opinion Letter

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