



Agenda Item 7a

November 18, 2013

ITEM NAME: Contracts Administration: Extension of Existing Investment Manager Contracts

PROGRAM: Investment Office

ITEM TYPE: Organizational Systems & Controls – Action

RECOMMENDATION

The Investment Office recommends that the Investment Committee (IC) approve a one-year contract extension for external investment manager contracts, consistent with procurement policies adopted by the Board.

EXECUTIVE SUMMARY

The Investment Office selects and monitors the performance of external investment managers on an ongoing basis. There are 42 external investment manager contracts that require IC approval to extend the contract duration. Approving the contract extensions will ensure compliance with procurement policies and improve operational efficiency. A list of the contracts recommended for extension is included as Attachment 1.

STRATEGIC PLAN

This item supports the CalPERS Strategic Plan goal to cultivate a high-performing, risk-intelligent and innovative organization. Approval of the extension of the external investment manager contracts supports CalPERS mitigation of investment and operational risks by ensuring the continuation of services.

INVESTMENT BELIEFS

This agenda item supports the following CalPERS Investment Beliefs:

- Investment Belief 8 – Costs matter and need to be effectively managed
- Investment Belief 10 – Strong processes and teamwork and deep resources are needed to achieve CalPERS goals and objectives

BACKGROUND

In February 2012, the Board of Administration (Board) adopted the Board Governance Policy which identified the roles and powers reserved to the Board and clarified the delegations to each committee and to staff. Based on the Board Governance Policy and the IC delegation (IC-11-01), the IC's role in the selection of external investment managers was revised from the selection of external investment managers to oversight of external investment managers. In this context, overseeing external investment managers is defined as the IC requiring adequate information to

monitor and provide direction and support, as appropriate. The Chief Investment Officer delegation (INV-12-01) specifies that staff has the authority to select and monitor external investment managers.

Per Board Resolution No. 92-04-B4 (Attachment 2), all contracts for goods and/or services can be for no more than a five-year period unless otherwise extended by the Board. Previously, the IC approved external investment managers and granted a one-year extension of the contracts during the annual asset class program reviews. The IC no longer selects and approves the external investment managers, so staff has developed an approach to obtain approval for these investment manager contracts that exceed the five-year duration.

ANALYSIS

Resolution No. 92-04B-4 allows the Board to extend contracts beyond the five-year maximum term upon an affirmative determination by the Board that a longer term is necessary to fulfill the Board's duty to serve the interests of CalPERS members and beneficiaries. Extending the external investment management contracts will avoid interruption of services from these external investment managers, assist in keeping the costs of external management services low and retain current alignment of interests between CalPERS and its existing external investment managers.

With the Board's authority to extend the contract duration, the Investment Office recommends that the IC extend the external investment manager contracts for an additional year. Investment staff will continue to select and monitor the performance of external investment managers consistent with the Board Governance Policy and the IC delegation. All external investment manager contracts have a provision that allows the contracts to be terminated with a 30-day notice.

Annually, staff will seek IC approval for one-year extensions for all external investment manager contracts.

BUDGET AND FISCAL IMPACTS

Not approving the extension of the duration of these contracts for one year could result in the higher costs for investment management services to the Investment Office. Should the current contracts fail to be renewed, additional fiscal impacts could include:

- Higher fees and staff resource costs associated with negotiating and establishing new external investment manager solicitations and contracts
- Misalignment of interests between CalPERS and external investment managers

BENEFITS/RISKS

The review and approval of one-year extensions of the external investment manager contracts, on an annual cycle, would streamline processes and ultimately create a cost-savings by reducing staff's involvement in the procurement process. The simplification of taking all contracts at one time streamlines the process and eliminates the operational risk of a contract not being extended. This will be consistent with the alignment of interests between CalPERS and investment managers. Failure to approve the investment manager contract extensions may cause interruption of critical services and may impede the execution of the Board's fiduciary duty to CalPERS members and beneficiaries.

ATTACHMENTS

Attachment 1 – External Investment Manager Contract Extension List
Attachment 2 – Board Resolution 92-04B-4

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