



## Agenda Item 7a

November 17, 2014

**ITEM NAME:** Investment Policy Revision Project Update

**PROGRAM:** Total Fund Program

**ITEM TYPE:** Policy & Delegation – Information

### **EXECUTIVE SUMMARY**

The purpose of this item is to update the Investment Committee (Committee) on the status of the Investment Policy Revision Project (Project). On August 18, 2014, staff provided the Committee with an update on Investment Beliefs activities. At that time, staff outlined recommendations that included the creation of an annual program review template that was linked to Investment Policies. Presently, staff is engaged in Phase 2 of the Project with the primary objective of consolidation of cross Program policies into a new Total Fund Investment Policy and simplification of current policies through removal of procedures. The benefits of completing the Project include enhanced Investment Policy standardization and removal of duplicative conflicting language.

### **STRATEGIC PLAN**

This agenda item supports the CalPERS Strategic Plan to improve long-term pension and health benefit sustainability. The proposed policy revisions will ensure that CalPERS is able to effectively achieve the System's investment objectives through clear and current investment policy documentation.

### **BACKGROUND**

The most recent Investment Policy review project took place between 2006 and 2008. Since that time adoption of the CalPERS Investment Beliefs, organizational changes, and modifications to individual policies require another comprehensive policy review in order to restore consistency.

The importance of clearly articulating and executing investment goals and performance measures while creating strong processes and teamwork are emphasized in Investment Beliefs 5 and 10, respectively.

### **ANALYSIS**

Investment Policy review and revisions are identified as initiatives in both the 2014-16 Roadmap and Target Operating Model (TOM). The purpose of this item is to update the Committee on the current status of the Project. The key objectives of the Project include:

- Enhancement of Investment Policy standardization and transparency.
- Consolidation of cross Program policy elements into the Total Fund Investment Policy to avoid duplication and conflicting language within Program policies. (Proposed Total Fund Investment Policy consolidation summary is included as Attachment 2).
- Relocation of procedure language from Investment Policies to procedure documents to enhance controls and provide staff flexibility to address ongoing Program functions.

As part of the Project, staff conducted a detailed review of each policy in order to assess the current condition. Staff determined that the following key risks are present:

- Policies are procedural in nature, duplicative in some cases and no longer applicable in others.
- Generally, there is a lack of consistency of content across Programs.
- The large current number of Investment Policies introduces a level of operational and compliance risk from an administrative, tracking, and testing perspective that is difficult to control.

Committee approval of the Global Derivatives and Counterparty Risk Policy (May 2014) provided staff with guidance regarding streamlining Investment Policies and removal of procedure language.

- Wilshire opined that, “a good deal of procedural language has been removed” and “while those types of items have previously been decided by the Board, the governance changes made over the past few years have delegated this to the staff and the new policy has therefore eliminated all of these specifics.”
- Wilshire provided further support in a letter dated July 9, 2014 when current Committee reporting cycle language was modified to “no less than annually” citing “significant and robust compliance controls and systems” as justification for the changes.

Staff engaged Wilshire Associates to opine on the elements and timing of the Project and a Consultant Opinion Letter is provided as Attachment 3. Program staff is now being engaged in review of components that have been removed from individual policies and incorporated into the Total Fund Investment Policy as well as contemplating the impact of transferring procedural language to testable Program procedure documents.

Due to the magnitude of the Project, staff determined that the most proficient approach is to initially focus on consolidation and streamlining of the Total Fund Investment Policy. Once the Committee has reviewed and approved the Total Fund Investment Policy, staff envisions proceeding with a similar process for individual Program policies metered to coincide with annual program reviews. This is anticipated to be accomplished as part of core workload rather than a continuance of this focused Project.

Staff has concluded that continuing with the Investment Policy Revision Project is a worthwhile undertaking and intends to pursue consolidation of cross Program Investment Policies into one Total Fund Investment Policy which will be presented to the Committee for initial review in February 2015.

### **BUDGET AND FISCAL IMPACTS**

Not Applicable.

### **BENEFITS/RISKS**

Staff's recommendation for continuing with the streamlining of Investment Policies is consistent with the TOM objectives to design, develop, and implement a robust operating model that minimizes complexity, improves transparency, and strengthens processes, systems, governance, and controls.

Specific benefits associated with the recommendations are:

- Review and revise existing Investment Policies for consistency and completeness.
- Reduce operational risk by development of clear metrics and operational risk management processes/governance.
- Establish processes for developing new policies.
- More effectively manage changes and monitor compliance.

Specific risks associated with the recommendations are:

- As presently drafted, policies are procedural lacking consistency and clarity across Programs elevating operational risk concerns.
- The present quantity of policies poses challenges from an administrative, tracking, and testing perspective.

**ATTACHMENTS**

Attachment 1 – Presentation Overview

Attachment 2 – Proposed Total Fund Investment Policy Consolidation

Attachment 3 – Wilshire Opinion Letter

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