



## Finance and Administration Committee

# Agenda Item 4b

---

**December 18, 2018**

**Item Name:** Contracts Administration: Affirmation of Investment Manager Contracts Without Defined Duration

**Program:** Investment Office

**Item Type:** Action Consent

### **Recommendation**

Approve staff's recommendation that an additional one-year contract term extension is necessary for the external investment manager contracts without a defined duration listed in Attachment 1, to fulfill the Board's duty to serve the interests of System members and beneficiaries, including the interest in defraying administrative expenses.

### **Executive Summary**

In order to improve operating efficiency and enhance negotiating capabilities, the Investment Office recommends that the Finance and Administration Committee (Committee) approve a one-year extension for the investment manager contracts listed in Attachment 1, consistent with procurement policies adopted by the Board in Resolution 92-04B-4.

Consistent with CalPERS policy, contracts for goods and services are limited to a term of five years. The Board, by resolution, has defined circumstances where the duration of a contract may extend beyond this five-year period. Staff requests approval to extend the investment manager contracts that exceed the five-year duration, for an additional year.

### **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 investment manager contracts supports CalPERS mitigation of investment and operational risks by ensuring the continuation of services. The one-year extension of investment manager contracts supports CalPERS Strategic Plan and is aligned with:

- Goal B: Cultivate a high-performing, risk-intelligent and innovative organization.
- Goal C: Engage in State and national policy development to enhance the long-term sustainability and effectiveness of our programs.

## **Background**

CalPERS contracts for goods and services are limited to a duration of five (5) years unless approved by the Board pursuant to Resolution No. 92-04B-4. This Resolution requires, among other things, that the Board affirmatively determine that a longer contract term is necessary to fulfill the Board's duty to serve the interests of System members and beneficiaries, including the interest in defraying administrative expenses. Such a determination shall only be made after considering the following factors (among any other the Board may deem prudent under the particular circumstances):

- The impact of a longer term upon the System's interests in obtaining quality services at a reasonable cost; and
- The System's ability to monitor the performance of contractors with such lengthy contract terms, and to take corrective active (including expeditious termination of the contract) if necessary to fulfill the Board's fiduciary duties.

## **Analysis**

With the authority to extend the contract duration residing with the Board, the Investment Office requests the Committee to extend these external investment managers' contract durations for an additional year. Investment Office staff will continue to be responsible for the selection and continuous monitoring of the external investment managers. All investment manager contracts provide staff the ability to terminate the contract within 30 days' notice. Staff will continue to present investment manager contracts without a defined duration, to the Committee on an annual basis, at which time, staff will also request the Committee to reaffirm the undefined duration and approve a subsequent one-year extension.

Investment staff believes contracting with investment managers without a defined duration is in the best interest of the System and satisfies both factors listed in Resolution 92-04B-4 for the following reasons: 1) The undefined duration allows CalPERS the ability to better negotiate fees; 2) CalPERS' standard contracting terms for investment managers allow for termination that is favorable to CalPERS interests; and 3) the Investment Office's robust operational systems and teams monitor external manager performance and should the need arise, is able to take action to promptly defund the manager. It is worth noting that over the last three years the Investment Office has reduced the total number of external managers from over 300 in 2014 to 140 as of September 30, 2018.

## **Budget and Fiscal Impacts**

The potential budget and fiscal impacts of not approving the duration extension will delay the timely execution of contracts and may nullify existing investment manager contracts, which could result in increased costs in the procurement and management of new external investment manager contracts.

## **Benefits and Risks**

The benefits of this process include:

- Provides transparency and ensures Board awareness of significant contracts; and
- Informs the Board regarding staff's contract decisions thereby satisfying their monitoring responsibilities.

The benefits of approving the recommendation include:

- Reduced costs by eliminating the requirement to enter into new contracts with existing investment managers, into lengthy and costly negotiations contracts with investment managers; and
- Reduced risk of re-negotiating fees during periods that may not be advantageous to CalPERS.

The risks of not approving staff's recommendation include:

- Interruption of critical services provided by external investment managers currently managing CalPERS' assets; and
- Potential impact on the ability of the Board and staff to fulfill its fiduciary obligations to CalPERS members and beneficiaries.

### **Attachments**

Attachment 1 – Investment Manager Contracts Without Defined Duration Extension List

Attachment 2 – Resolution No. 92-04B-4

---

Elisabeth Bourqui  
Chief Operating Investment Officer