



STATE OF WISCONSIN  
Department of Employee Trust Funds  
Robert J. Conlin  
SECRETARY

Wisconsin Department  
of Employee Trust Funds  
PO Box 7931  
Madison WI 53707-7931  
1-877-533-5020 (toll free)  
Fax 608-267-4549  
etf.wi.gov

## Correspondence Memorandum

**Date:** August 8, 2018  
**To:** Deferred Compensation Board  
**From:** Shelly Schueller, Director  
Wisconsin Deferred Compensation Program  
**Subject:** Proposed Investment Policy Statement Revisions

**The Investment Committee and ETF recommend the Board revise the Investment Policy Statement as shown in the attached draft.**

The Deferred Compensation Board has one standing subcommittee, the advisory-only Investment Committee. One of the duties of the Investment Committee is a periodic review of the Investment Policy Statement (IPS). The Investment Committee reviewed the IPS on June 27, 2018, and recommends the following changes:

1. Page 1: Update “fixed income” to “capital preservation” to better reflect the intent of options offered in this investment category.
2. Page 2: Revise the sentence in “selection process” to
  - a. Update “fixed income” to “capital preservation” to better reflect the nature of these types of investment options; and
  - b. Indicate that capital preservation investments must meet the minimum criteria established by the Board in Attachment 1. This change would permit the Board to select fixed income/capital preservation investment options in a manner consistent with how other options are selected; and
3. Page 4: update the effective date of Attachment 2 to December 2018.
4. Page 5 (Attachment 1): Retitle the minimum criteria in the first section from “...Fixed Income Options” to “...Capital Preservation Options” to match change suggested above in 1 and 2a.
5. Page 6 (Attachment 2): Add the American Beacon Bridgeway Large Cap option and appropriate benchmarks.
6. Page 7 (Attachment 2):
  - a. Update the socially responsible offering to indicate the change to the Calvert U.S. Large Cap Core Responsible Index Fund and appropriate Large Cap blend benchmark;
  - b. Take the word “funds” out of the Vanguard Target Date listing; and

Reviewed and approved by Matt Stohr, Administrator, Div. of Retirement Services

Electronically Signed 9/11/18

Board	Mtg Date	Item #
DC	11.15.18	12

Proposed Investment Policy Statement Revisions

August 8, 2018

Page 2

- c. Update the note on the benchmarks to “investment provider” instead of “mutual fund advisor.”

Staff will be at the meeting to answer any questions.

Attachment: Investment Policy Statement (with proposed revisions shown in mark-up text)

**Wisconsin Deferred Compensation Program**  
**Deferred Compensation Board**  
**Investment Policy Statement**

*Approved by the Deferred Compensation Board November 1998*

Revised February 2005

Last Revised ~~June 8, 2017~~ [draft for November 2018 and effective December 2018](#)

***Objective***

The Wisconsin Deferred Compensation Program (WDC) will provide participants with the ability to invest retirement savings in a broad range of investment alternatives with diverse risk and return characteristics. The Deferred Compensation Board's goal is to ensure the WDC offers sufficient investment choices to meet participants' needs when establishing their personal retirement savings portfolio.

This Investment Policy Statement (IPS) describes a prudent investment process that the Board has determined is most appropriate for the WDC. The IPS is designed to allow for sufficient flexibility in the management oversight process, while also setting forth reasonable parameters to promote the exercise of reasonable prudence and care with respect to the investment options available in the WDC. The Board may amend the IPS from time to time, as it deems advisable.

***Investment Spectrum***

The Board recognizes that there is investment risk inherent in all investment options, and that individual participants each have their own level of risk tolerance. Accordingly, the Board will select and offer a broad array of investment options providing different levels of risk and historical return, and other financial characteristics as appropriate. The Board will maintain a core investment spectrum, normally between eight and twenty options, to ensure sufficient choices are available and are reasonable in number to allow the average participant to decide which options best meet their personal needs. The spectrum will be comprised of fixed options, publicly traded mutual fund options, and institutional investment products (examples: separate accounts, collective investment trusts) from the following categories:

1. ~~Fixed income/cash~~ [Cash preservation](#) investments - FDIC insured account option, stable value fund, or money market mutual fund.
2. Bond mutual funds - government or corporate bond funds, domestic or international, active or passive management.
3. Balanced mutual funds – combining equity and bond investments in one option.
4. Domestic large cap equity mutual funds – including both active and passive (index) investments; funds with investment objectives that may include: growth and income, growth, aggressive growth, value, and blend of growth and value, and active or passive management.
5. Domestic small and mid-cap equity mutual funds – growth, value or blend, and active or passive management.
6. International or foreign equity mutual funds – growth, value or blend, and active or passive management.

7. *Target Date funds – age-based portfolios for multiple time horizons.*
8. *Specialty Funds – may be offered for participants interested in a particular style of investment choice. Any specialty fund offered must remain true to its special criteria (e.g., socially responsible) and competitive to its specific asset class.*
9. *Self-Directed Brokerage Account (SDBA) – will offer a wide array of mutual funds that can be accessed by participants. The investment options in the SDBA will not be monitored by the Board. Participants electing the SDBA will be required to acknowledge that they are sufficiently sophisticated and knowledgeable about investing and that they are capable of making, managing and controlling their investment choices.*

### **Selection Process**

The Board may from time to time provide additional investment alternatives and may change the categories of funds offered to maintain a broad spectrum to address participants' changing needs or changes to the investment industry. The Board has established minimum criteria for selecting and evaluating the options offered by the WDC, as shown in Attachment 1.

~~Fixed income~~[Capital preservation](#) investments must meet minimum criteria established by the Board (see Attachment 1) ~~and are selected from a competitive request for proposal process.~~

Mutual fund options are selected from the universe of publicly traded funds through a comprehensive search process. For an option to be considered for the WDC, it must meet the established minimum requirements in regard to: asset size, years in operation, costs (expense ratio and sales fees), and historical performance. Once the initial screening has occurred, options are further analyzed based on criteria that includes, but is not limited to: short and long-term performance as compared to peer group average and benchmarks, risk/return measurements, manager tenure, and industry ratings (such as Morningstar).

### **Evaluation Process**

As required in Wisconsin Administrative Code ETF 70.08(9), to ensure options continue to be suitable for offering to WDC participants and are consistent with the established investment policy statement, the Board will complete a comprehensive evaluation each year. This evaluation will be accomplished using the minimum criteria stated in Attachment 1.

Performance benchmarks are specifically established for each investment option and include a comparison to their peer group average, an appropriate index measurement, and an internal benchmark identified by the fund manager. Volatility is also measured by an analysis of risk versus return. Benchmarks for each investment option are stated in Attachment 2.

The Board recognizes that an investment manager's performance can move in cycles over time and that investment option performance will not always be superior. As such, the Board will generally monitor selected investment option performance on a periodic basis.

While the primary analysis of investment options will be quantitative, the Board reserves the right to make decisions regarding investment options based upon other criteria that the Board believes will be in the best interests of the WDC and its participants.

### ***Underperforming Investment Options***

If the Board determines an option is underperforming or no longer acceptable for continued offering, the Board may close the investment to new participant elections or initiate the process to phase the option out of the WDC and require participants to move account balances to an alternate choice. The steps in the review process are as follows:

1. *The Board completes an investment performance review of all investment options. If an investment option is determined to be underperforming, the Board may:*
  - a) *Put the investment option on a formal “watch” list. While an investment option is on a “watch” list, no action will be taken to either close or replace the option. WDC participants will be informed of a “watch” decision. The investment option manager may be informed, and additional information may be gathered as to why the investment option is underperforming; or*
  - b) *Close the investment option to new elections and proceed with step 2; or*
  - c) *Initiate the phase out process to remove the investment option from the WDC. If this route is chosen, steps 2 and 3 will be skipped; go directly to step 4.*
2. *As a result of the next year’s investment performance review, if the option’s investment performance is determined to once again be acceptable, the investment option may be taken off the “watch” list and if necessary because the option was closed to new elections, the option will be re-opened to participant elections.*
3. *If improvements have occurred but the investment option is not completely meeting all established criteria and/or there are remaining questions about its performance, the option can be continued on a “watch” list or continue in its closed status for an additional year.*
4. *If the review demonstrates that the investment option continues to be unacceptable for offering, the Board can initiate the process to phase it out of the WDC over a minimum of a one-year period (as required in Wisconsin Administrative Code ETF 70.08(3)).*
5. *Participants are instructed to re-direct deferrals to an alternate choice within a period of not less than six-months from the original notification. If this action is not taken, deferrals being directed into the option being removed will automatically be redirected to an alternate option as designated by the Board.*
6. *Participants are instructed to transfer existing balances to an alternate choice within a period of not less than one year from the original notification. If this action is not taken, account balances not exchanged out of the option being removed will automatically be redirected to an alternate option as designated by the Board.*

### ***Other Considerations***

The Board may conduct informal reviews and evaluations of an investment option at any time. The Board may place an investment option under formal review or terminate an investment option for any reason, including but not limited to the following:

1. The investment option has changed managers, or such a change appears imminent.

2. The investment option has had a significant change in ownership or control.
3. The investment option has changed its investment mandate or has experienced style drift, departing from the investment objectives or parameters in its prospectus.
4. The investment option has experienced substantial portfolio turnover.
5. The investment option has violated an SEC rule or regulation.
6. The investment option has experienced difficulty in transacting trades, fund transfers or pricing.
7. The investment option has experienced other changes or problems in its procedures, operations, investing or reporting or a lack of employee participation, which in the Board's view has detracted from our could detract from the WDC's objectives.
8. Any other circumstance regarding the investment option that the Board determines is in conflict with this IPS or may be detrimental to the WDC, such as involvement in a scandal process.

### ***Responsibilities***

Deferred Compensation Board – The Board is responsible for selecting appropriate investment options for offering by the WDC and monitoring the selections to ensure they continue to be acceptable for long-term retirement savings.

Investment Providers – The companies contracted to provide an investment option to the WDC are responsible for following the investment objectives that were either, identified during the competitive bid process (for fixed income options or institutional investment products) or stated in their fund prospectus (for mutual funds).

Department of Employee Trust Funds and Administrative Services Provider Staff – Staff is responsible for completing the annual evaluation to monitor the WDC investment choices and providing sufficient analysis and information on which the Board can base decisions regarding maintaining, removing or adding investment options to the WDC. Staff is also responsible for providing sufficient information about the available investment choices and how to structure a retirement savings portfolio to enable participants to make informed decisions.

Participants – Investment decisions are the full responsibility of participants and their beneficiaries. Although the Board monitors the options that are being made available, participants are responsible for deciding which, if any, of the available choices are the most appropriate for their supplemental retirement savings needs.

Attachment 1: Minimum Criteria for Selecting and Evaluating Investment Options

Attachment 2: Benchmarks for Evaluating Investment Options (effective [November 2014](#)[December 2018](#))

**Attachment 1**

<b>Minimum Criteria for Selecting and Evaluating Fixed Income <u>Cash Preservation</u> Options</b>	
Bank Option	<ul style="list-style-type: none"> <li>• FDIC insured</li> <li>• Capital ratio as required by US government to maintain FDIC coverage</li> <li>• Minimum size - \$1 billion in assets</li> </ul>
Insurance Option	<ul style="list-style-type: none"> <li>• Top rating received by at least 2 rating agencies</li> <li>• No rating below a Double A or equivalent</li> <li>• Total capital (equivalent to total assets minus total liabilities) equal to at least 5% of invested assets</li> <li>• High risk assets (non-investment grade bonds and non-performing real estate loans and investments) under 200% of total capital</li> <li>• Performance returns compared to blended 5-year Treasury rates, or other index as appropriate and approved by Board</li> </ul>
Stable Value Fund Manager	<ul style="list-style-type: none"> <li>• Minimum five years experience managing stable value assets</li> <li>• Minimum \$2 billion in discretionary assets under management</li> <li>• Investment guidelines and performance benchmark as approved by Board</li> </ul>
<b>Minimum Criteria for Selecting and Evaluating Mutual Fund and Institutional Investment Product Options</b>	
<b>Selection Criteria:</b> <i>Requirements apply to all unless specifically waived</i>	<ul style="list-style-type: none"> <li>• Minimum 5-year operating history – may be waived for index funds</li> <li>• Manager Tenure not less than 3 years</li> <li>• Expense ratio [internal expense charge plus any 12(b)1 fee] not greater than the mean for the appropriate peer group</li> <li>• 5-year rolling average performance must equal or exceed appropriate benchmark or index</li> <li>• Minimum total asset size of \$400 million – may be waived for certain categories of funds</li> <li>• Anticipated WDC assets not greater than 5% of total fund (determined by comparing current WDC asset levels in a comparable fund)</li> <li>• No loads or sales charges unless they are waived for the WDC</li> <li>• Not a sector fund</li> </ul>

<p><b>Monitoring Criteria:</b> <i>Requirements apply to all unless specifically waived</i></p>	<ul style="list-style-type: none"><li>• Performance must meet or exceed one or more of established benchmarks – benchmarks used include but are not limited to 1) peer group average, 2) appropriate index as determined by Board, and 3) internal benchmark assigned by fund manager.</li><li>• For specialty funds selected for reasons other than performance (e.g., socially responsive funds or target date funds), performance will only be evaluated based on a comparison to the funds peer group of funds with same specialty objective. [Participants will be fully advised when a fund is selected for reasons other than investment returns.]</li><li>• WDC assets in fund no greater than 10% of the total mutual fund assets</li><li>• After 5 years in the WDC, minimum of 3% of participants or 3% of assets.</li></ul>
--	---

**Attachment 2**  
**Benchmarks for Evaluating Investment Options**  
(effective ~~November 2014~~ December 2018)

**Investment Product**

**Benchmarks**

<a href="#">American Beacon Bridgeway Large Cap Value</a>	<ul style="list-style-type: none"> <li>• <a href="#">Morningstar Large Cap Value Average</a></li> <li>• <a href="#">Russell 1000 Value Index</a></li> </ul>
American Funds EuroPacific Growth R6	<ul style="list-style-type: none"> <li>• Morningstar Foreign Large Blend Average</li> <li>• MSCI EAFE Index</li> <li>• MSCI ACWI ex U.S.</li> </ul>
DFA U.S. Microcap Portfolio	<ul style="list-style-type: none"> <li>• Morningstar Small Cap Growth Average</li> <li>• Russell 2000 Index*</li> </ul>
FDIC Option (Nationwide Bank)	<ul style="list-style-type: none"> <li>• 50% 3-Month LIBOR / 50% 12-Month LIBOR</li> </ul>
Federated U.S. Government Securities Fund 2-5 Years Institutional	<ul style="list-style-type: none"> <li>• Morningstar Short Government Average</li> <li>• Barclay's US Treasury/Agency 3-5 Year</li> <li>• BofA Merrill Lynch US Treasury 3-5 Year</li> </ul>
Fidelity Contrafund	<ul style="list-style-type: none"> <li>• Morningstar Large Cap Growth Average</li> <li>• Russell 1000 Growth Index</li> <li>• S&amp;P 500 Index</li> </ul>
Stable Value Fund (Galliard)	<ul style="list-style-type: none"> <li>• Five Year Constant Maturity Treasury Rate</li> </ul>
Vanguard Admiral Treasury Money Market Fund	<ul style="list-style-type: none"> <li>• Morningstar Taxable Money Mkt Average</li> <li>• U.S. Treasury 90-Day T-Bill</li> <li>• iMoneyNet Money Fund Report Average 100% Treasury Fund</li> </ul>
Vanguard Long-Term Investment Grade-Fund Admiral	<ul style="list-style-type: none"> <li>• Morningstar Corporate Bond Average</li> <li>• Barclay's LT Corporate A*</li> </ul>
Vanguard Wellington Fund (Admiral Shares)	<ul style="list-style-type: none"> <li>• Morningstar Moderate Allocation Average</li> <li>• Composite 65% S&amp;P 500 / 35% Barclay's U.S. Credit A or Better Index</li> <li>• Composite 65% S&amp;P 500 / 35% Barclay's Aggregate</li> </ul>

## INDEX FUNDS

Blackrock EAFE Equity Index Fund	MSCI EAFE
Blackrock MidCap Equity Index Fund	S&P MidCap 400 Index
Blackrock Small Cap Equity Index Fund	Russell 2000 Index
Blackrock U.S. Debt Index Fund	BarCap Aggregate Index
Vanguard Institutional Index Fund (Plus Shares)	S&P 500 Index

## SPECIALTY FUNDS

Calvert <a href="#">U.S. Large Cap Core Responsible Index Social Investment Equity Fund - Institutional Class</a>	<ul style="list-style-type: none"> <li>• Morningstar Socially Responsible Large Cap Average **</li> <li>• Morningstar Large Cap <a href="#">Growth Blend</a> Average</li> <li>• S&amp;P 500 Index</li> </ul>
Vanguard Target Date <a href="#">Funds</a>	<ul style="list-style-type: none"> <li>• S&amp;P Target Date Indexes**</li> <li>• Composite benchmarks based on asset allocation of funds</li> </ul>

\* Benchmarks that are used by both the Wisconsin Deferred Compensation Board as well as the [mutual fund advisor/investment provider](#).

\*\* Per the Board's Investment Policy Statement, Specialty Funds (funds chosen for reasons other than performance) are measured only against their peer group.

*Other benchmarks may be included to provide additional monitoring criteria.*