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Correspondence Memorandum

Date: June 28, 2018
To: Deferred Compensation Board
From: Shelly Schueller, Director
 Wisconsin Deferred Compensation Program
Subject: Stable Value Fund: Proposed Contract Revisions

The Investment Committee recommends the Deferred Compensation Board (Board) approve the attached proposed revisions to Exhibit 3 of the Stable Value Fund contract with Galliard.

At the March 2018 meeting the Board heard an update from Mike Norman of Galliard Capital Management on the Stable Value Fund. Mr. Norman stated that by the end of 2018, Galliard will be removing the Wells Fargo Stable Return Fund allocation from its clients' separate account portfolios, including the portfolio Galliard manages for the Wisconsin Deferred Compensation Program (WDC).

Galliard is recommending revisions to Exhibit 3 of the Stable Value Fund contract, which will:

- 1) update the sector guideline allocations, increasing the Synthetic GIC (Guaranteed Investment Contract)¹ allocation to one hundred percent; and
- 2) standardize the WDC contract language to be consistent with other stable value fund portfolios managed by Galliard.

Sector Guideline Allocations

The Wells Fargo Stable Return Fund is currently part of the WDC Stable Value Funds liquidity buffer. When the Wells Fargo Stable Return Fund is removed from the portfolio, Galliard recommends revising the sector guidelines to permit increasing the maximum

¹ Synthetic GICs are "contracts with a bank or insurance company that guarantee a rate of return relative to a portfolio of assets held in an external trust. The rate of return, which is based on the actual performance of the underlying assets, is reset periodically. The participating plans own the assets. Typically, these contracts are commonly referred to as wraps or wrappers." Source: <https://www.dol.gov/agencies/ebsa/about-ebsa/about-us/erisa-advisory-council/2009-stable-value-funds-and-retirement-security-in-the-current-economic-conditions>

Reviewed and approved by Matt Stohr, Administrator, Division of Retirement Services

 Electronically Signed 9/11/18

Board	Mtg Date	Item #
DC	11.15.18	7

Stable Value Fund: Proposed Contract Revisions

June 28, 2018

Page 2

weighting for synthetic GICs from the current 95% to 100%. Without this change, the sector guidelines would require Galliard to allocate five percent (5%) to cash. Galliard suggests that keeping five percent in cash is not necessary and that five percent could work harder for participants if allocated to other sectors. Galliard believes that now is a good time to remove the Wells Fargo Stable Return Fund from the WDC's portfolio, as it would provide Galliard with more flexibility to manage the fund. In addition, the interest rate environment is good, meaning the balance in the stable return fund could be reallocated to a higher yielding option.

Standardizing Contract Language

Galliard also recommends cosmetic changes to Exhibit 3, which are intended to standardize the language used by Galliard across their stable value fund clients and to simplify the overall guidelines; each portfolio is managed and reviewed based on the portfolio's specific set of guidelines.

The revisions proposed by Galliard do not change how the WDC's Stable Value Fund will be managed. Rather, the changes update the contract to reflect the removal of the Wells Fargo Stable Return Fund and current Galliard contract language.

At the June 27, 2018, Investment Committee meeting, these changes were reviewed with Galliard and the Department of Employee Trust Funds (ETF). The Investment Committee and ETF concur with Galliard's request to revise and replace Exhibit 3 of the contract via an amendment to the existing contract.

Staff will be at the meeting to answer any questions.

Attachment: Third Amendment to the Amended and Restated Investment Advisory Agreement with Revised Exhibit 3

**THIRD AMENDMENT TO THE AMENDED AND RESTATED
INVESTMENT ADVISORY AGREEMENT**

This amendment (the "Amendment") is effective as of _____, 2018, by and between Galliard Capital Management, Inc. ("Advisor") and the State of Wisconsin through its Deferred Compensation Board (the "Board").

WHEREAS, Advisor and the Board entered into an Amended and Restated Investment Advisory Agreement effective June 16, 2015 (the "Agreement"); and

WHEREAS, Advisor and the Board now wish to amend the Agreement.

NOW THEREFORE, the parties agree as follows:

AMENDMENT

1. Exhibit 3 of the Agreement is hereby deleted and replaced with the Exhibit 3 attached to this Amendment.
2. Except to the extent modified by this Amendment, the remaining provisions of the Agreement shall remain in full force and effect. In the event of a conflict between the provisions of the Agreement and those of this Amendment, the Amendment shall control.
3. This Amendment may be executed in two or more counterparts, each of which shall be an original, but all of which together shall constitute one and the same agreement. Delivery of an executed counterpart of this Amendment by facsimile, including, without limitation, by facsimile transmission or by electronic delivery in portable document format (".pdf") or tagged image file format (".tiff"), shall be equally effective as delivery of a manually executed counterpart thereof.

State of Wisconsin Deferred Compensation Board

By: _____

Name: _____

Its: _____

Galliard Capital Management, Inc.

By: _____

Name: _____

Its: _____

EXHIBIT 3

Investment Objective & Guidelines State of Wisconsin Deferred Compensation Plan – Stable Value Fund

Effective: _____, 2018

INVESTMENT OBJECTIVE AND BENCHMARK

The primary investment objective of the Account is preservation of principal. The secondary objective is to provide a stable crediting rate with an average yield that is consistent with the 3-year Constant Maturity Treasury yield over a full interest rate/market cycle.

Advisor cannot guarantee that these objectives will be achieved.

I. ACCOUNT BOOK VALUE INVESTMENT GUIDELINES

A. PERMITTED BOOK VALUE INVESTMENTS

Permitted investments will be limited to GICs, synthetic GICs, separate account GICs, stable value collective funds* and fixed income collective funds wrapped by synthetic GICs, cash equivalents, short-term investment funds and/or money market funds.

**The Account will maintain a holding of units of the Wells Fargo Stable Return Fund until on or about 12/1/2018.*

B. SECTOR GUIDELINES

<u>Account Level</u>	<u>Maximum Weighting</u>
Liquidity Buffer*	50%
Guaranteed Investment Contracts (GICs)	10%
Separate Account GICs	50%
Synthetic GICs	100%

**The Account's Liquidity Buffer may consist of short-term money market instruments, money market mutual funds, and/or collective investment trusts seeking to maintain a constant unit value of \$1.00, and/or stable value collective funds.*

C. DIVERSIFICATION GUIDELINES

No more than 3% of the aggregate Account will be invested in traditional GICs from any one contract issuer, measured at the time of purchase or at the time of the last deposit to the contract.

Exposure to any one separate account GIC issuer shall be limited to not more than 25% of the Account's assets, measured at the time of purchase or at the time of the last deposit to the contract.

Exposure to any one synthetic GIC issuer shall be limited to not more than 35% of the Account's assets, measured at the time of purchase or at the time of the last deposit to the contract.

In the event a contract issuer is terminated, it will not be deemed a violation to the guidelines if the remaining issuers exceed the limit. Galliard will replace the terminated issuer within 180 days or obtain client approval for an extension.

D. QUALITY GUIDELINES

The minimum quality rating of traditional GIC, separate account GIC and synthetic GIC issuers must be A- or equivalent by at least one Nationally Recognized Statistical Rating Organization ("NRSRO"), measured at the time of the initial placement. In the case of a split rating, the higher rating shall apply.

II. DURATION GUIDELINES

The total duration of the securities held in the Account (including the Liquidity Buffer and cash/cash equivalents) shall be limited to a maximum of 3.5 years. Duration will be calculated using a contract value weighted average duration.

III. SECURITIES AND INVESTMENTS UNDERLYING THE SYNTHETIC GICS AND SEPARATE ACCOUNT GICS OWNED BY THE ACCOUNT

A. PERMISSIBLE SECURITIES AND INVESTMENTS

Under normal circumstances the securities and investments underlying the synthetic GICs and separate account GICs owned by the Account will be invested in the following investment vehicles and securities:

- Asset backed securities
- Collective investment funds and pooled separate account GICs (herein "Pooled Vehicles") – Pooled Vehicles will be governed exclusively by the investment guidelines of the Pooled Vehicle but will primarily consist of securities and investments listed herein
- Debt obligations of corporations, financial institutions, or non-corporate credit issuers, including both domestic and foreign issuers
- Direct obligations of a Government Sponsored Enterprise (GSE) and issues or loans guaranteed by a GSE
- Commercial mortgage-backed securities

- Foreign government debt obligations denominated in U.S. dollars, including sovereigns, foreign agencies (government-guaranteed and government-sponsored), foreign local governments, and supranationals
- Municipal securities
- Private placements, including but not limited to securities issued under 144A and Regulation S
- Residential mortgage-backed securities
- Money market mutual funds, short-term money market instruments, including but not limited to CDs, time deposits, bankers acceptances, commercial paper, repurchase agreements, money market mutual funds or short-term investment funds operating pursuant to 12 CFR 9.18
- U.S. Treasury securities, U.S. Agency securities, and issues or loans guaranteed by the U.S. Government or its Agencies
- Derivative usage shall not introduce risk that is inconsistent with other aspects of these guidelines including, but not limited to, exposure to unexpected asset classes, leverage and illiquidity. Derivatives are generally expected to be used such that they hedge or mitigate market risk and to gain exposure to asset classes that are consistent with these investment guidelines. The Derivatives that may be used in the Fund include the following:
 - Futures Contracts, including Eurodollar futures, interest rate futures, and Treasury futures
 - Options and Swap agreements, including caps and floors, total return swaps, credit default swaps, options on interest rate futures, and options on MBS.
 - Rights and warrants, if received as the result of a corporate action or ownership of a permissible security or investment
 - TBA securities, forward purchase agreements and mortgage dollar rolls on Agency MBS and Agency CMBS subject to the following:
 - The net value of TBA securities and forward purchase agreements shall be backed by cash (including STIF) and cash equivalents (defined as investment grade fixed income securities with an effective duration of one year or less.) and
 - Net sales of TBA positions shall be covered by like securities deliverable into these positions;

B. PROHIBITED SECURITIES AND STRATEGIES

Under normal circumstances, the securities and investments underlying the synthetic GICs and separate account GICs owned by the Account shall not invest in the following prohibited securities and strategies:

- Equity securities (except equity or equity-like securities received as the result of a corporate action associated with a permissible security or investment)
- Investments used for leverage

- Non-U.S. dollar denominated securities
- Short sales (except mortgage TBA sales where the portfolio holds sufficient deliverable securities to cover the net TBA sale or intra-day short sales of Treasury securities to facilitate trading that are covered by close of the same business day)
- Writing of uncovered call options and uncovered put options

IV. POOLED INVESTMENT VEHICLE SELECTION CRITERIA

Section IV sets forth the requirements with respect to the investment vehicles utilized in the Account, other than the assets of the Account invested in the Account's Liquidity Buffer.

GICs and the Account's Liquidity Buffer are not subject to the requirements of this Section IV. The Account's Liquidity Buffer shall be categorized as Cash and Cash Equivalents.

A. DIVERSIFICATION GUIDELINES

Each collective investment trust underlying the synthetic GICs and any separate account GICs held by the Account shall require that no more than 5% of the Account will be invested in any single asset backed or non-government mortgage backed issuing trust and no more than 3% of the Account will be invested in the securities of any other single issuer. For purposes of this limitation, the trust or special purpose corporation that holds the associated collateral shall be deemed the issuer for any non-agency RMBS, non-agency CMBS or asset-backed security. U.S. Government debt obligations, agency RMBS (including TBAs), and agency CMBS are exempt from these issuer maximums.

B. QUALITY GUIDELINES

Each collective investment trust underlying the synthetic GICs and any separate account GICs held by the Account shall require that all securities will be rated investment grade (BBB- or equivalent) or better by at least one Nationally Recognized Statistical Rating Organization ("NRSRO") at the time of purchase. Securities that are downgraded below investment grade (BBB- or equivalent) may be held in Advisor's discretion.

In addition, each collective investment trust and separate account GICs shall require that the weighted average credit quality of the securities held by the Account shall be maintained at a minimum rating of AA- or equivalent. In the case of a split rating on a security, the higher rating shall apply.

For purposes of this Section IV.B, unrated securities which rank pari passu with a rated security of the same issuer will be considered to have the same rating as the rated security. For securities guaranteed by another entity, the guarantor's rating may be used in cases where a security does not carry its own rating.

C. PROVISION OF UNDERLYING PORTFOLIO GUIDELINES

On an annual basis, Advisor will furnish Principal with a current copy of the investment guidelines of any fixed income collective investment trust or separate account GIC held by the Account.

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