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Correspondence Memorandum

Date: February 8, 2021

To: Deferred Compensation Board

From: Shelly Schueller, Director
Wisconsin Deferred Compensation Program

Subject: Investment Option Recommendation: American Beacon Bridgeway Large Cap Value Removal

ETF recommends that the Board close the American Beacon Bridgeway Large Cap Value fund, replace it with a different large cap value option, and direct that balances remaining in American Beacon Bridgeway Large Cap Value after it is closed are reallocated to the new large cap value option.

The American Beacon Bridgeway Large Cap Value fund was added to the WDC core investment lineup in late 2017 to provide participants with a large cap value option. As of December 31, 2020, just over 15,000 WDC participants held approximately $18,768,000 in the option.

During 2017, the American Beacon Bridgeway Large Cap Value fund's performance was strong; it was in the top quartile for three-year percentile ranks when compared to peers for six months during calendar year 2017. Since then, however, the fund's investment returns have declined, and the Board has been carefully monitoring the American Beacon Bridgeway Large Cap Value fund. Since March of 2020, the fund has been "on watch" due to poor investment performance. As of the close of 2020, the fund's performance had not improved. Total return for this fund lags the Morningstar Large Cap Value Average benchmark over all periods reviewed (3 month, 1 year, 3 year, 5 year and 10 year) and lags the Russell 1000 Value Index benchmark over all but the most recent three-month period and the 10 year period. When reviewing three-year percentile ranks, the American Beacon Bridgeway Large Cap Value fund has been in the bottom quartile of performance for nine straight quarters.

ETF recommends the Board close the American Beacon Bridgeway Large Cap Value fund, replace it with a different large cap value option in the WDC core investment lineup, and direct that any balances remaining in the American Beacon Bridgeway Large Cap Value fund after it is closed are reallocated to a new large cap value option.

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

Matt Stohr Electronically Signed 2/24/21

Board	Mtg Date	Item #
DC	3.11.21	6A

As with other investment option closures, the Board can direct that remaining balances are reallocated to an option that is reasonably similar in terms of risk and rate of return to the option being closed. In the case of the American Beacon Bridgeway Large Cap Value fund, there is not currently a similar option. Thus, ETF is recommending that the Board begin the search process for a replacement.

If the Board takes no action on any remaining balances in the American Beacon Bridgeway Large Cap Value fund or does not add a different large cap value option to the WDC, then the Board's default fund policy would be put into effect. This would send participants' remaining American Beacon Bridgeway Large Cap Value fund balances to the Vanguard target retirement date fund appropriate for the participant's retirement age, using age 65 as the standard retirement age.

If the Board were to close and replace the American Beacon Bridgeway Large Cap Value fund, the following would occur:

- ETF would formally notify American Beacon Bridgeway of the decision.
- The investment option termination process found in Wisconsin Administrative Code Ch. ETF 70.08 would be followed. This states that the investment option termination process may begin on the first business day of the sixth month following the Board's decision. Participants have six months to cease deferring to the closing fund, then have another six months to move their remaining account balances from the fund. Thus, the timeline to close American Beacon Bridgeway includes notifying participants who are deferring funds to American Beacon Bridgeway as of September 1, 2021 that they must redirect existing deferrals before March 1, 2022, then further notifying any participant with a balance in the fund that they must move their balance to a different fund prior to August 1, 2022.
- The WDC would begin communicating this forthcoming change to participants via the WDC web site and on participant statements.
- Bill Thornton from Great West Investments would begin searching for a suitable large cap value option to add to the WDC, using criteria found in the Board's Investment Performance Statement as a starting point. He could present the results of his search to the Board at the June 2021 Board meeting.

Staff will be available at the meeting to answer any questions.

Attachment A: Deferred Compensation Board Default Fund Policy
Attachment B: Wisconsin Administrative Code Ch. ETF 70.08

Default Fund Policy

Adopted: unknown – perhaps at beginning of plan?
Last Revised: May 2008

The Deferred Compensation Board's Default Fund Policy is that the designated default fund will be the Vanguard Target Retirement Date Fund appropriate for the participant's retirement age, using age 65 as the standard retirement age.

Default Fund History
1983 - May 2008: Vanguard Money Market Fund
May 2008 – present: Vanguard Target Date Retirement Funds

Default Fund Procedure: When an investment option is removed from the Wisconsin Deferred Compensation Program (WDC), any remaining account balances will be swept to the Vanguard Target Date Fund closest to the participant's retirement date at age 65.

Background: Selecting a default fund option when removing or replacing an investment option is a fiduciary duty, since the Board is making an investment decision for participants instead of the decision being directed by the participant.

Section ETF 70.08 (3), Wisconsin Administrative Code, states that after the Deferred Compensation Board (Board) has determined that an investment option is no longer acceptable for inclusion in the Wisconsin Deferred Compensation Program (WDC), the Board is required to tell the WDC's third party administrator to which other WDC investment option any remaining participant account balances from the closed fund should be automatically moved or "swept." The administrative rule does not specify to which investment option the money is to be swept; that decision is left to the Board.

Selected References:

1) ERISA. The preamble to section 404(c) of the Employee Retirement Income Security Act (ERISA) states that "plan fiduciaries will not be relieved of responsibility for investment decisions under an ERISA section 404(c) plan unless those [investment] decisions have affirmatively been made by participants..." Like other public retirement plan sponsors, the WDC is not directly subject to ERISA. However, in practice most public plan sponsors, including the WDC, seek to abide by ERISA regulations as the ERISA regulations provide guidance on federal interpretations of situations that are also experienced by public plan sponsors.

2) PPA. The Pension Protection Act of 2006 (PPA) included language creating ERISA s. 404 (c)(5), which alleviates fiduciary liability for plan sponsors who meet specific conditions regarding assets invested in a plan's default fund. The PPA also directed the federal Department of Labor (DOL) to issue guidance that plan sponsors could follow when selecting a default fund. In October of 2007, the DOL issued Qualified Default Investment Alternative (QDIA) regulations. Employers following QDIA regulations have no legal liability for market fluctuations when providing a QDIA for employees who fail to select their own investment options. Target date retirement funds are considered appropriate QDIAs.

ETF 70.08 Investment providers.

(1) Investment providers offering an investment product through the primary plan or an alternate plan shall be selected by the board based on the investment product categories and criteria established under s. ETF 70.03 (8) and (9). All contracts with investment providers of the primary plan or an alternate plan shall be approved by the board and signed by the board chair or designee.

(2) Investment providers shall not be allowed to assess any direct or indirect costs to members.

(3) Based on the board's review required under s. ETF 70.03 (10), the board may determine that an investment product offered by the primary plan or an alternate plan is no longer acceptable for inclusion in the program. If the board decides to remove an investment product from the plan as a result of the product's failure to meet the criteria as established under s. ETF 70.03 (9), the product shall be phased out of the primary or alternate plan in a 2-step process over a 12 month period that shall commence on the first business day of the sixth month following the board's decision, as follows:

(a) Phase 1 of the investment product termination process shall last for 6 months during which time current members and employees newly enrolling in the primary or alternate plan shall be informed in writing that the terminating investment product does not meet board's evaluation criteria and that this *investment product is not open to new enrollments.*

1. Any members already deferring to the terminating investment product shall be informed in writing that they need to redirect future deferrals from this product to an alternative investment product offered by the primary or alternate plan by notifying the administrator of their new investment choice.

2. At the end of the 6-month period, the board shall instruct the administrator to automatically redirect any member's deferrals that have not been redirected to an alternative investment product from the terminated product into a board designated alternative investment product offered by the primary or alternate plan.

3. Existing member account balances shall be allowed to remain in the terminating investment product during this period.

(b) Phase 2 of the investment product termination process immediately follows the first 6-month period and provides an additional 6-month period during which time members shall transfer existing balances from the terminating product to another investment product offered by the primary or alternate plan.

1. If at the end of the 6-month period, any member has failed to move a remaining account balance from the terminated fund, the board shall instruct the administrator to automatically move that member's account balance into a board designated alternative investment product offered by the primary or alternate plan.

2. During the phase out process and at any time prior to the end of the second phase, the board may re-examine the performance of the terminating investment product to determine if continued plan participation is justified.

History: Cr. Register, June, 1992, No. 438, eff. 7-1-92; CR 08-016: am. (3) (intro.) Register August 2008 No. 632, eff. 9-1-08; correction in (1), (3), made under s. 13.92 (4) (b) 7., Stats., Register July 2012 No. 679, eff. 8-1-12.