

# **Investment Objectives and Policy Statement**

## **City of Fresno Deferred Compensation Plan**

(Adopted by the Deferred Compensation Board February 9, 2006)

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# Investment Objectives and Policy Statement

## City of Fresno Deferred Compensation Plan

### Foreword

This Investment Objectives and Policy Statement is intended to summarize the underlying philosophy and processes demonstrating care, skill, prudence and diligence in the selection and monitoring of investment options of the City of Fresno Deferred Compensation Plan (the Plan) as an eligible deferred compensation plan within the meaning of Internal Revenue Code Section 457(b). The Plan allows employees to voluntarily invest a portion of their compensation before it is considered taxable. The amount invested, plus any accumulated gain, is available to the employee (or beneficiary) at a future date.

This statement contains:

- A summary of the Plan's structure and underlying philosophy;
- Performance objectives and other criteria to be used by the Deferred Compensation Board (Board) and the Plan Administrator to review and evaluate the investment results of the Plan's investment options; and,
- Responsibilities of the Board, the Plan Administrator and the Third Party Plan Administrator (Trustee).

The guidelines contained in this statement will be revised and modified as appropriate on a periodic basis to reflect such factors as changes in the investment environment, manager performance, participant objectives and the Board's expectations.

### Plan Structure

#### 457(b)

The Plan constitutes an "eligible deferred compensation plan" within the meaning of Internal Revenue Code §457(b). In accordance with the Plan Document adopted by the City Council on August 15, 2006, the Plan permits the City's Eligible Employees to defer portions of their Compensation until Severance from Employment. The Plan is a long term retirement savings vehicle and is intended to be used as a source of retirement income for eligible participants. Therefore, employees are encouraged to participate in the Plan.

The Plan structure establishes and operates a "retirement system" satisfying the requirements of §3121(b)(7)(F) of the Internal Revenue Code of 1986, as amended from time to time (the "Code"), §31.3121(b)(7)-2 of the Income Tax Regulations promulgated there under.

## **Investment Objectives**

The Plan's investment objective is to make available a broad range of diversified investment options that have varying degrees of risk and return. The selection is intended to make it possible for the individual participant to achieve a balanced portfolio consistent with modern portfolio theory.

## **Risk Tolerance and Rates of Return Expectations**

Individual participants vary in their level of risk tolerance. Because participants direct their own investments, the plan will offer a wide spectrum of investment options, including a variety of Mutual Funds, Life Style Funds and a Self-Directed Brokerage Account (SDBA), all with varying levels of risk and return.

Risks associated with the investment options can vary significantly within each investment category and the relative risks of categories may change under certain economic conditions. The third party Administrator will provide participant education and counseling, including investment advice to guide participants in their selection of investment options. Participants may design an investment plan from those options that best meets their individual needs.

## **Investment Options**

The plan seeks to offer a diversified portfolio by making available several investment options in each of the following investment categories:

- Managed Income/Stable Value
- Bonds
- Balanced/Hybrid
- Domestic Equity (Large/Mid/Small – Value/Blend/Growth – Index)
- International/Global Equity

### **– Mutual Funds**

The Plan offers a wide variety of Mutual Fund investment choices that:

- Cover a risk/return spectrum of appropriate investment classes;
- Are distinguishable and have distinct risk/return characteristics;
- Are well diversified and professionally managed;
- Provide, in aggregate, the participant with the opportunity to structure a portfolio with risk and return characteristics at any point within a normally appropriate range of investments; and,
- Charge fees that are reasonable for the asset class and investment style.

In addition, the Plan also offers investment choices in Life Cycle Funds and a Self-Directed Brokerage Account.

## **Life Cycle Funds**

Participants who do not wish to actively manage their own asset allocation strategy may choose a lifestyle fund in which the objective is to provide a composite rate of return from current income and capital appreciation which is appropriate for a given state of an individual's investment life cycle. These funds:

- are designed for employees who lack the time or investment knowledge needed to actively make investment choices.
- help participants by turning over asset allocation decisions to investment professionals managing the fund.
- include automatic rebalance to maintain the right investment mix based upon age-appropriate diversification within a single "fund of funds".

## **Self-Directed Brokerage Account (SDBA)**

Another investment options under the Plan is the Fidelity, self-directed brokerage account, BrokerageLink. BrokerageLink offers a broad range of investment options for participants who want to more actively manage their investment choices. The account is neither a mutual fund nor is it managed by any of the Fidelity Investments group of companies. Participants alone decide how to invest the assets in the BrokerageLink account. Available investments include:

- most listed stocks, corporate bonds, zero-coupon bonds, US Treasury securities, mortgage securities and US government agency bonds, certificates of deposit, unit investment trusts, and foreign securities.
- Mutual funds beyond those available through the standard Plan mutual fund options.
- may include additional fees such as transaction-based fees and commissions.

## **Review Criteria**

### **- Investment Options**

The Plan Administrator and Third Party Plan Provider will track performance of the Investment Options on a quarterly basis and fully review these options at least annually. The annual review will include, but not be limited to, evaluations of the following:

- Historical return and risk results versus the appropriate benchmarks;
- Any changes in process, philosophy, and/or personnel; and,
- Fees and expense levels.

Fund performance continues to be compared using quantifiable measures:

- Sharpe Measures
- Fund Returns
- Morningstar Ratings: The Board has determined that the use of the “category” rating would be of value to interested plan participants. The category rating compares funds to their peers within the specific asset class, giving a more “apples to apples” comparison.

The Benchmark is the 50th percentile of retail funds in the asset class on the Morningstar database.

The performance of each fund is classified as being in one of three categories:

- Above Benchmark
- Below Benchmark
- Neutral (This category has been added to indicate both above and below benchmark measurements within evaluation period)

There are four levels of fund evaluation analysis:

I. Performance Measurement Period

Funds with more than three years’ history will be analyzed to determine if performance is above or below benchmark.

II. Sharpe Measure Analysis

- Sharpe measure indicates the return per unit of risk.
- Sharpe measure equals:  

$$\frac{\text{Fund Rate of Return} - \text{Risk Free Rate of Return (90 day T-bill)}}{\text{Standard Deviation of the Fund's Returns (i.e. risk)}}$$
- The higher the Sharpe measure, the better the performance.

III. Funds Returns Analysis

Funds with performance greater than the 50th percentile for two or more measurement periods are classified as above benchmark performers.

IV. Morningstar 3 to 5 Star Analysis

- Funds with a Morningstar rating of 3 to 5 stars are classified as above benchmark performers.
- Funds with a 1 or 2 star rating are classified as below benchmark performers.

The policy of the Board is to review all of our investment options on an annual basis. Each fund is measured opposite the benchmarks and objectives that have been established. As a result of the review each year, conclusions are reached

with respect to each current investment option and consideration given for new options:

1. The fund will be retained for the next twelve months.
2. The fund will be placed on a “watch list” when the overall fund rating is “at” or “below” benchmark. A fund on the “watch list” may be put on probation at any time in the future.
3. The fund will be placed on probation when the overall fund rating is below benchmark.
4. The fund will be closed to new contributions because it no longer meets the investment criteria.
5. New funds will be added for two reasons:
  - a. To replace a closed fund, or
  - b. To provide additional choices for participants.

A change in fund manager or other unusual situation may require a special review. The Board will publish the results of the investment review annually for all plan participants.

Each investment option will be compared to recognized, appropriate indices and within universes of mutual funds and investment options with similar styles. Performance will be considered over a full market cycle of a three-to-five year period.

In general, each investment alternative should outperform median returns for similar investment alternatives as shown by Morningstar Category.

## **Responsibilities**

### **Plan Administrator:**

The duties and responsibilities of the Plan Administrator include:

- Present any necessary revisions to the Board’s Investment Policy Statement to the Board for their consideration,
- With assistance of the Third Party Plan Administrator, develop, review, and revise the Investment Policy Statement,
- Evaluate and measure investment alternatives,
- Notify the Board of any issue that may impact the investment of Plan assets, e.g., change in ownership, professional staff, investment philosophy and/or process,
- With assistance of the Third Party Plan Administrator, evaluate and recommend investment alternative changes, and
- Communicate with and report to the Board on a regular basis.

## **Board:**

The duties and responsibilities of the Board include:

- Approve Plan Investment Policy Statement,
- Approve addition/deletion of investment options, and
- Review and approve of reports provided by the Plan Administrator and Third Party Plan Administrator.

## **Third Party Plan Administrator:**

The duties and responsibilities of the Third Party Plan Administrator include:

- Communicate with and report to the Plan Administrator and the Board on a regular basis,
- Communicate with and report to the participants on a regular basis,
- Notify the Plan Administrator and the Board of any issue that may impact the investment of Plan assets, e.g., change in ownership, professional staff, investment philosophy and/or process, and
- Assist Plan Administrator, in developing, reviewing, and revising Plan Investment Policy Statement
- Offer investment education and advice to participants,
- Notify the Plan Administrator and the Board of any issue that may impact the investment of Plan assets, e.g., change in ownership, professional staff, investment philosophy and/or process, and
- Monitoring Plan assets with the care, skill, prudence and diligence that an investment professional should exercise in the investment of those assets.