

Deferred Compensation Plan BOARD REPORT 14-40

Date: October 8, 2014
 To: Board of Deferred Compensation Administration
 From: Staff
 Subject: Active Investment Manager Search Update

*Board of Deferred
 Compensation Administration
 Eugene K. Canzano, Chairperson
 John R. Mumma, Vice-Chairperson
 Cliff Cannon, First Provisional Chair
 Tom Moutes, Second Provisional Chair
 Michael Amerian, Third Provisional Chair
 Ray Ciranna
 Mary Higgins
 David Luther
 Robert Schoonover*

Recommendation:

That the Board of Deferred Compensation Administration receive and file staff's update regarding the status of the active investment manager searches.

Background:

At its February 18, 2014 meeting, the Board adopted revisions to the Plan's Investment Policy Statement (IPS) incorporating the option for a mutual funds search process for filling certain investment manager mandates as approved by the Board, and further approved a proposed search schedule for the Plan's various investment options as recommended by staff.

At its March 18, 2014 meeting, the Board further approved specific search criteria for each asset category such that the Board's investment consultant, Mercer Investment Consulting ("Mercer"), could initiate its search processes and present findings to the Board's Investments Committee for the purpose of the Investments Committee generating final recommendations to the full Board. The Investments Committee is chaired by Gene Canzano and includes Michael Amerian, Mary Higgins and Tom Moutes.

The Board's approved searches for 2014 include the following mandates:

	Investment Menu Option	Fund Sub-Category	Presently Filled?	Incumbent Provider	Incumbent Fund	Assets	Adopted Search Vehicle
Search Year - 2014							
ACTIVE MANAGERS	DCP Small-Cap Fund	Active Small-Cap Growth	No	n/a	n/a	\$105 million	Mutual Fund
	DCP Small-Cap Fund	Active Small-Cap Value	No	n/a	n/a	\$105 million	Mutual Fund
	DCP Mid-Cap Fund	Active Mid-Cap Growth	No	n/a	n/a	\$68 million	Mutual Fund
	DCP Mid-Cap Fund	Active Mid-Cap Value	No	n/a	n/a	\$68 million	Mutual Fund
	DCP Intl Fund	Active Intl Developed Mkts	Yes	Fidelity	n/a	\$214 million	Mutual Fund
	DCP Intl Fund	Active Intl Emerging Mkts	No	n/a	n/a	\$58 million	Mutual Fund
	DCP Intl Fund	Active Intl Small-Cap	No	n/a	n/a	\$58 million	Mutual Fund
	DCP Bond Fund	Active Bond	Yes	PIMCO	Total Return Fd	\$179 million	Mutual Fund

The Investments Committee established a review process involving a series of meetings during which the Committee reviews the fund search results in a designated order, reduces the search results to a smaller number of finalists, and then at a subsequent meeting considers the finalists in greater detail in order to develop a recommendation to the full Board.

On August 28, 2014, the Investments Committee met to review the search results for the Active Bond, Active Small-Cap Value, and Active Small-Cap Growth fund categories. The Committee established a list of finalists for further review of each category.

On September 29, 2014, the Investments Committee reviewed a subsequent report from Mercer providing more detailed findings regarding the finalists in each category and made selections in each category to recommend to the full Board.

Discussion:

ACTIVE CORE BOND: SELECTION UPDATE

Subsequent to the Investments Committee meeting on September 29th, a special meeting of the Board was convened on October 2, 2014 in order to expedite consideration of replacing the current active core bond fund, PIMCO's Total Return Fund.

On September 26, 2014, PIMCO announced that Total Return Fund manager William Gross would be leaving the firm. This management change is deemed significant by industry observers and the Board's investments consultant because of Mr. Gross' longstanding and prominent role in managing the Total Return Fund. There is a significant possibility that a substantial amount of assets could leave the Fund in the coming weeks and months. Although PIMCO has indicated that it will maintain sufficient liquidity to honor all redemption requests, mutual fund companies have the ability to restrict fund outflows if they deem it necessary. In addition, a significant level of ongoing redemptions may serve as an immediate distraction to the portfolio management team and over the longer-term, depress returns.

Given this, the Investments Committee, the Plan's investments consultant, and staff deemed it prudent to execute the fund transfer from PIMCO as soon as practicable as the Investments Committee was recommending a new selection for the active core bond fund provider. Thus, in a special meeting held on October 2, 2014, the Board approved the Investments Committee's recommendation to select the **Loomis Sayles Core Plus Bond Fund N** ("Loomis Fund," ticker symbol NERNX) as the new Active Bond fund component of the Deferred Compensation Plan (DCP) Bond Fund. The Loomis Fund was recommended for its strong results within a range of criteria applied to this fund search, including long-term performance, management team depth, personnel stability, portfolio construction, competitive fees, performance in different market environments, risk-adjusted returns, and other criteria reviewed by the Committee and detailed in the attached consultant report. The Board further approved the Committee's recommendation to execute the transfer as quickly as administratively feasible.

At the time of the writing of this report, the transfer of funds from PIMCO to the Loomis Fund is anticipated to have taken effect on **October 14, 2014**. Based on June 30, 2014 values, the estimated size for the active allocation of the fund is approximately \$179 million (including assets invested in the risk profile portfolios). The active core bond category makes up 50% of the underlying allocation for the DCP Bond Fund (the other half of the DCP Bond Fund is an index fund managed by Vanguard).

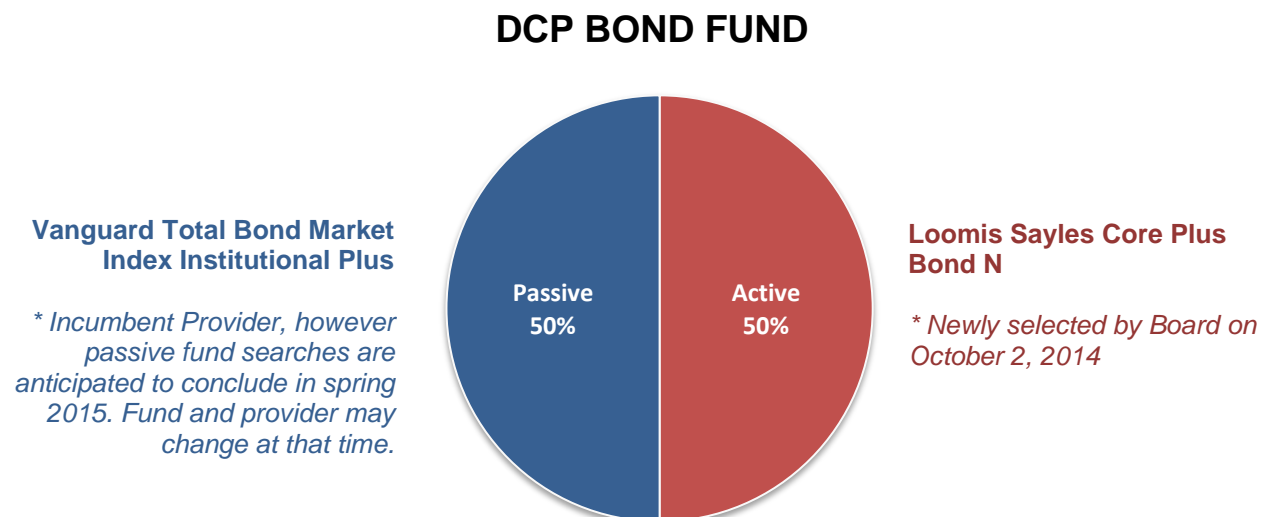
PLAN INVESTMENT MENU - NEXT STEPS

Staff anticipates the active manager searches will conclude in December 2014 with the selection of the active international funds. The Board has already selected the active core bond manager and will be considering the small-cap recommendations in a subsequent report at this meeting; mid-cap recommendations are anticipated in November.

Once these selections are complete, staff will work to implement the fund changes. For the DCP Bond Fund and the DCP Mid-Cap Funds, the underlying fund allocations will be updated with the new active fund component. The DCP Bond Fund already has an existing active allocation, but the DCP Mid-Cap Fund will have the new active component blended in.

It should be noted that the small-cap and international asset class funds in the Plan's core investment menu have yet to be Plan branded and currently consist of standalone options. Once the active manager searches have been completed, staff can begin to take steps to introduce the DCP Small-Cap Fund and the DCP International Fund and complete the re-branding of the Plan's core investment options menu. Implementation will include development of strategy and timeline for communication of these changes, as it will involve elimination of three standalone investment options: the SSgA Russell Small Cap Index Fund (NL Series S), the DWS EAFE Equity Index Institutional Fund, and the Fidelity Diversified International Fund.

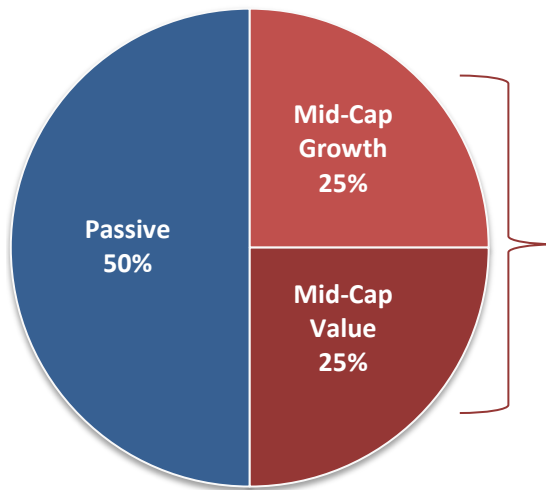
Here is a general overview of what the updated funds will look like, along with a tentative timeline for implementation and communication:



DCP MID-CAP FUND

Vanguard Mid-Cap Index Fund Institutional Plus Shares

** Incumbent provider, however passive fund searches are anticipated to conclude in spring 2015. Fund and provider may change at that time.*

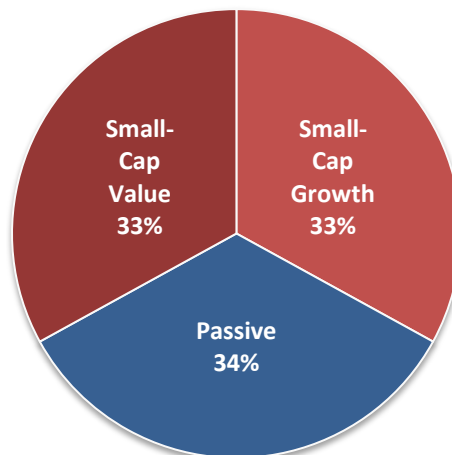


** Funds to be determined; to be reviewed by the Board in November 2014.*

DCP SMALL-CAP FUND

DFA U.S. Small Cap Value Portfolio

** Subject to Board approval on October 21, 2014*



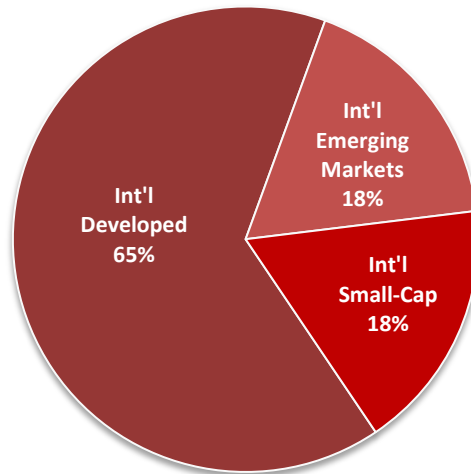
Hartford Small Cap Growth HLS Fund

** Subject to Board approval on October 21, 2014*

SSgA Russell Small Cap Index Fund NL Series S

** Incumbent provider, however passive fund searches are anticipated to conclude in spring 2015. Fund and provider may change at that time.*

DCP INTERNATIONAL FUND



** Funds to be determined; to be reviewed by the Board in December 2014.*

TENTATIVE IMPLEMENTATION TIMELINE

TASK	TO BE COMPLETED
<i>Selection of active core bond manager</i>	<i>Completed 10/2/2014</i>
Selection of active managers for the DCP Small-Cap Fund	October 21, 2014
Selection of active managers for the DCP Mid-Cap Fund	November 18, 2014
Selection of active managers for the DCP International Fund	December 16, 2014
Communication to Plan Participants (Newsletter – 4 th Quarter 2014)	Mailed at end of month in January 2015
Implementation of New DCP Small-Cap and International Funds	March 1, 2015 (tent.)
Selection of passive managers (bond, large-cap, mid-cap, small-cap) <i>* The small-cap passive manager search will be addressed first to time with DCP Small-Cap Fund re-brand.</i>	First quarter 2015

Submitted by: _____
Esther Chang

Approved by: _____
Steven Montagna