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DEFERRED COMPENSATION PLAN BOARD REPORT 08-45



Date: November 12, 2008

To: Board of Deferred Compensation Administration

From: Staff

Subject: Stable Value Fund RFP/Third-Party-Administrator Role

Recommendation:

That the Board of Deferred Compensation Administration:

- (a) Cancel the August 22, 2008 Request for Proposal (RFP) for a Stable Value Fund manager and approve its immediate re-issuance; and
- (b) Establish that, to prevent the appearance of a conflict-of-interest and to promote the neutral and unbiased communication of investment options to Plan participants, any firm serving as the Deferred Compensation Plan Third-Party-Administrator (TPA) will not simultaneously be permitted to be a Plan investment provider.

Discussion:

On August 22, 2008, staff issued a Request for Proposal (RFP) for a Stable Value Fund manager. Responses were due October 24, 2008. Four firms submitted responses: Fidelity Investments, Galliard Capital Management, Great-West Retirement Services (Great-West), and Pacific Investment Management Company (PIMCO). Three of the four firms (all excluding Great-West) were found to be non-compliant with the City's Standard Provisions requirements. Specifically, all three failed the provisions relating to outreach to minority and women owned firms ("MBE/WBE"). This leaves only one viable firm.

Given the size of the asset pool under management and the importance of this mandate, staff believes that the Board should re-issue the RFP in order to obtain a larger pool of potential vendors to consider. The incumbent contracts with Galliard and Hartford Life Insurance do not expire until June 2009, so there is still sufficient time to re-issue the RFP, require a streamlined response period, and conduct a review. Staff is proposing that the RFP be re-issued November 19, 2008, with responses due December 19, 2008. An analysis and recommendation would be expected to be presented to the Board at its February 17, 2008 meeting.

Third-Party-Administrator Proposal – As indicated, Great-West was one of the respondents on the RFP. Great-West is the Plan's Third-Party-Administrator (TPA). When the Board "unbundled" the Deferred Compensation Plan in 1999 by separating the TPA contract from its investment provider relationships, one of the primary bases for doing so was to ensure that the TPA had no incentive to recommend any specific investment options offered in the Plan.

When staff became aware of the Great-West proposal, staff contacted the City Attorney's Office to see if there were any potential conflict-of-interest issues that might arise from the Board contracting with Great-West as an investment provider. Staff focused particularly on issues arising when Great-West Plan representatives discussed with participants an investment option from which they derived revenue, especially as compared to competing options in the Plan (e.g. the Plan's FDIC-insured option, Ultra-Conservative or Conservative funds, bond funds, etc.).

Staff initially spoke with Deputy City Attorney Richard Bobb, who in turn contacted Deputy City Attorney Renee Stadel, the City Attorney's ethics expert. Mr. Bobb stated that Ms. Stadel had indicated there is no direct conflict-of-interest issue given that Great-West cannot advise participants regarding where to invest their money. However, she further indicated that there could nevertheless be an appearance of conflict-of-interest and to avoid that the Board was free to, as a matter of policy, take a position that a TPA cannot be both a Plan administrator as well as investment provider.

The proposition that a TPA should not be both a Plan administrator as well as investment provider is a concept that informed the Plan's unbundling in 1999. It resulted from the Plan's prior dual-vendor, bundled design model that was in existence from 1983 through 1999. In that model, the two firms providing administrative services had incentives to market their particular investment products to participants. This provided a potential motivation or tendency to, in discussing these options with Plan participants, emphasize favorable aspects of their options while de-emphasizing unfavorable ones. This same dynamic could potentially exist if the Plan's TPA was also an investment provider. Even if it did not, as noted by the City Attorney, the appearance of conflict-of-interest could arguably be created in the minds of Plan participants which might inhibit their ability to assess their investment choices objectively.

The counter-argument to the concern about appearance of conflict-of-interest is that, given that this option will be branded under the Plan name and not with the provider, the appearance of a conflict-of-interest from the participant's perspective would be fairly remote (although not fully eliminated, because Plan literature would disclose the underlying providers for any City-branded option). Thus, it is possible that for the sake of the appearance issue the Board might close off consideration of a credible option.

On balance, however, and in the interest of consistency with prior Plan design considerations, staff recommends that the Board take position prohibiting a Plan TPA from simultaneously serving as an Plan investment provider. This would prevent the appearance of a conflict-of-interest and promote the neutral and unbiased communication of investment options to Plan participants

Submitted by:

Steven Montagna