

# *California Secure Choice*

## **Secure Choice Retirement Savings Investment Board Meeting**

Comparison of  
Recommended Program Investment Vehicles

Sacramento, California

January 11, 2016

# Comparison of Recommended Program Investment Vehicles

## Overall Features



	Option 1: Dynamic Asset Allocation Auto IRA (DC)	Option 2: Pooled IRA (Reserve Fund)	Traditional Pension (DB) for comparison purposes only
<b>Income Replacement Range</b> <b>5<sup>th</sup> Percentile to Median<sup>1</sup></b> <i>(5% contribution rate; 42-year career)</i>	13% - 23%	2058 Cohort: 12% - 22% 2078 Cohort: 15% - 30%	Function of Career Income
<b>Who Bears Investment Risk</b>	Participant	Participants Collectively	Sponsor
<b>Sponsor Liability</b>	No Guarantees by Sponsor	No Guarantees by Sponsor	Explicit Obligation to Fund Shortfalls
<b>Fiduciary Responsibility<sup>2</sup></b>	Normal Especially on Product & Default Selection <sup>3</sup>	Elevated Fiduciary Responsibility Especially on Crediting Policy Unless Board Has No Discretion <sup>4</sup>	Normal
<b>Ease of Implementation</b>	High (no proprietary product) Moderate (proprietary product)	Moderate; Additional legal and actuarial services required, but recordkeeping will be simple	N/A
<b>Flexibility in Benefit Design</b>	Limited	Leaves Door Open to Private Investment Guarantee & In-Plan Annuity	N/A

### Notes

- 1-** N<sup>th</sup> Percentile means N% probability that result would be X% or lower. For example, there is a 5% probability that the income replacement rate for the AutoIRA option would be 13% or less. Conversely, this also means that there is a 95% probability of the income replacement rate exceeding 13%. Median means 50<sup>th</sup> percentile.
- 2-** A fiduciary duty is a legal duty to act solely in another party's interests. Parties owing this duty are called fiduciaries. The individuals to whom they owe a duty are called principals.
- 3-** The selection of investment products and, in particular, the default investments place a duty of care on the individual members of the board and program officials entrusted with making the selection.
- 4-** Members of the Reserve Fund board are likely to be deemed fiduciaries. As such they may not profit from their relationship with their principals (i.e., Secure Choice Participants) unless they have the principals' express informed consent. They also have a duty to avoid any conflicts of interest between themselves and their principals. A fiduciary duty is the strictest duty of care recognized by the US legal system. If the Board has discretion in setting the crediting rate of the Reserve Fund, then the utmost care has to be taken in avoiding conflicts of interest or favoring one group of participants over another. This burden can be mitigated if the crediting policy is strictly enshrined in legislation with little discretion left for the board.

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## Participant Experience



	Option 1 Managed Accounts	Option 1 Target Date Funds	Option 2 Pooled IRA with Reserve Fund
Income Replacement <i>5<sup>th</sup> Percentile to Median Range (5% contribution rate; 42-year career)</i>	13% - 23%	13% - 23%	2058 Cohort: 12% - 22% 2078 Cohort: 15% - 30%
Ease of Understanding	Moderate Participant sees allocation across several funds	<b>Easy</b> TDFs are intuitive	Easy-Moderate Savings bond concept is intuitive, but crediting policy may not be
Ability to Adjust Risk Profile	<b>Easy</b> Account interface can be designed to make this intuitive	Easy-Moderate Participants choose from among several different target dates	N/A No participant choice
<b><u>RISK/REWARD</u></b>			
Volatility in Account Balance	High (Low first 3 years)	High	<b>Low-Moderate</b> (Low first 3 years of operation)
Chance of Windfall <i>(benefit 33% higher than expected after full career)</i>	<b>~30%</b>	<b>~30%</b>	~20% in mature program (Less during startup)
Chance of Large Loss Near Retirement <i>(&gt;20% drop in balance)</i>	Significant (Insurance can mitigate, but will reduce benefits)	Significant (Insurance can mitigate, but will reduce benefits)	<b>Low</b> <b>in mature program</b> (Low-Moderate in early years)

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## Investment-Related Responsibilities of Board & Consultants



	Option 1 Managed Accounts	Option 1 Target Date Funds	Option 2 Pooled IRA with Reserve Fund
Board: Overall Investment Policy	Determine asset allocation for investment lineup; adjust when prudent		Determine appropriate asset allocation for single portfolio; adjust when prudent  <b>Determine prudent policies for reserve fund accumulation and interest crediting</b>
Board: Account Crediting	--	--	<b>Credit accounts in strict accordance with established policies</b>
Investment Consultants	Advise on investment/asset allocation policy, product creation/selection & vendor selection; supervise investment managers in tandem with staff		
Actuaries	Minimal - project average balances, plan demographics, retirement income		<b>Moderate</b> – help determine asset allocation policy, project system assets, help determine appropriate crediting policy
Legal	Oversee product creation		<b>Draft authorizing legislation and provide legal advice</b> to set up special purpose bond vehicle through which reserve fund can be implemented
Investment Managers	Day-to-day management of portfolio(s) in accordance with investment policy established and approved by Board		