

FLORIDA RETIREMENT SYSTEM

Public Employee Optional Retirement Program Investment Policy Statement

I. PURPOSE

The Public Employee Optional Retirement Program Investment Policy Statement (IPS) serves as the primary statement of Trustee policy regarding their statutory responsibilities and authority to establish and operate an optional defined contribution retirement program for members of the Florida Retirement System. The IPS shall serve as a guiding document pertaining to investment matters with respect to the Public Employee Optional Retirement Program. The Trustees will strive to make investment decisions consistent with this IPS. Section 121.4501(14), Florida Statutes, directs the Trustees of the State Board of Administration to approve the IPS. The IPS will be reviewed annually and will be revised or supplemented as policies are changed or developed.

II. DEFINITIONS

- A. **Participant** – An employee who enrolls in the Public Employee Optional Retirement Program (PEORP), a participant-directed 401(a) program, in lieu of participation in the defined benefit program of the Florida Retirement System.
- B. **Investment Product** – The result of a process that forms portfolios from securities and financial instruments in order to produce investment returns.
- C. **Investment Manager** – A private sector company that provides one or more investment products.
- D. **Investment Funds** – One of the investment options that may be chosen by participants. A Fund may be an aggregate of one or more investment products.
- E. **Bundled Provider** - A private sector company that offers investment products, combined with recordkeeping and trading services, which are designed to meet individualized needs and requirements of plan participants, so as to afford value to participants not available through individual investment product.
- F. **Passively Managed Option** – An investment management strategy that intends to produce the same level and pattern of financial returns generated by a market benchmark index.
- G. **Actively Managed Option** – An investment management strategy that relies on security return predictions in an effort to out-perform the financial returns generated by a market benchmark index.
- H. **Performance Benchmark** – A market benchmark index that serves as the performance measurement criterion for investment options.

- I. **Third-Party Administrator or Recordkeeper** – A private sector company that provides administrative services, including individual and collective recordkeeping and accounting, IRC limit monitoring, enrollment, beneficiary designation and changes, disbursement of monies, and other centralized administrative functions.

III. OVERVIEW OF THE PEORP AND STATE BOARD OF ADMINISTRATION

- A. The PEORP is a participant-directed 401(a) program selected by employees in lieu of participation in the defined benefit program of the Florida Retirement System. PEORP benefits accrue in individual accounts that are participant-directed, portable and funded by employer contributions and earnings. In accordance with Section 121.4501(15)(b), Florida Statutes, participants and beneficiaries bear the investment risks and reap the rewards that result when they exercise control over investments in their accounts. Fluctuations in investment returns directly affect participants' benefits.
- B. The State Board of Administration (Board), Division of Retirement and affected employers administer the PEORP. The Board designs educational services to assist employers, eligible employees, participants and beneficiaries. The State Legislature has the responsibility for setting contribution levels and providing statutory guidance for the administration of the PEORP.

IV. THE BOARD

- A. The Board consists of the Governor, as Chairman, the Chief Financial Officer, as Treasurer, and the Attorney General, as Secretary. The Board shall establish an optional defined contribution retirement program for members of the Florida Retirement System and make a broad range of investment options, covering most major market segments, available to participants. The Board makes the final determination as to whether any investment manager or product, third-party administrator, education vendor or advice vendor shall be approved for the program.
- B. The Board shall discharge its fiduciary duties in accordance with the Florida statutory fiduciary standards of care as contained in Section 121.4501(15)(a), Florida Statutes.
- C. The Board delegates to the Executive Director the administrative and investment authority, within the statutory limitations and rules, to manage the PEORP program. The Board appoints a six-member Investment Advisory Council (IAC). The IAC reviews the IPS and any proposed changes prior to its presentation to the Board of Trustees. The Council presents the results of its review to the Board of Trustees prior to the Trustees' final approval of the statement or any changes.

V. THE EXECUTIVE DIRECTOR

- A. The Executive Director is responsible for managing and directing administrative, personnel, budgeting and investment-related functions, including the hiring and termination of investment managers, bundled providers and products.
- B. The Executive Director is responsible for developing specific investment objectives and policy guidelines for investment options. The Executive Director is responsible for developing policies and procedures for selecting, evaluating, and monitoring the performance of investment managers and products to which employees may direct retirement contributions under PEORP, and providing the Board with monthly and quarterly reports of investment activities.
- C. The Executive Director is responsible for maintaining diversified investment options, and maximizing returns with respect to the performance benchmarks of individual investment options, consistent with appropriate risk constraints. Each investment option will avoid excessive risk and have a prudent degree of diversification relative to its broad market performance benchmark.
- D. The Executive Director shall adopt policies and procedures designed to prevent excessive participant trading between investment options from negatively impacting other participants.
- E. The Executive Director is responsible for periodically reviewing this IPS and recommending changes to the Board of Trustees when appropriate.

VI. INVESTMENT OBJECTIVES

- A. The PEORP investment program shall seek to achieve the following long-term objectives:
 - 1) Offer a diversified mix of low-cost investment options that span the risk-return spectrum and give participants the opportunity to accumulate retirement benefits.
 - 2) Offer investment options that avoid excessive risk, have a prudent degree of diversification relative to broad market indices and provide a long-term rate of return, net of all expenses and fees that seek to achieve or exceed the returns on comparable market benchmark indices.
 - 3) Offer participants meaningful, independent control over the assets in their account with the opportunity to:
 - a) Obtain sufficient information about the plan and investment alternatives to make informed investment decisions;
 - b) Direct contributions and account balances between approved investment options with a frequency that is appropriate in light of the market volatility of the investment options;
 - c) Direct contributions and account balances between approved investment options without the limitation of fees or charges; and

- d) Remove accrued benefits from the plan without undue delay or penalties, subject to the contract and all applicable laws governing the operation of the program.

VII. PARTICIPANT CONTROL AND PROGRAM FIDUCIARY LIABILITY

- A. This IPS is structured to be consistent with the Legislature's intent to assign liability for participants' investment losses to participants and provide a safe harbor for program fiduciaries.
- B. In Sections 121.4501(8)(b)4. and 121.4501(15)(b), Florida law incorporates the federal law concept of participant control, established by regulations of the U.S. Department of Labor under section 404(c) of the Employee Retirement Income Security Act of 1974. The PEORP investment program shall incorporate these concepts by providing program participants the opportunity to give investment instructions and obtain sufficient information to make informed investment decisions. The PEORP program shall, in accordance with the 404(c) regulations and Florida law, provide participants an opportunity to choose from a broad range of investment alternatives.
- C. If a participant or beneficiary of the PEORP exercises control over the assets in his or her account, pursuant to section 404(c) regulations and all applicable laws governing the operation of the program, no program fiduciary shall be liable for any loss to a participant's or beneficiary's account which results from such participant's or beneficiary's exercise of control.
- D. The default option for FRS Investment Plan participants that fail to make a selection of investment options shall be the Moderate Balanced Fund, which otherwise meets the requirements of a qualified default investment alternative pursuant to regulations issued by the U.S. Department of Labor. The default option for FRS Pension Plan DROP participants who rollover funds from their DROP account to the PEORP as permitted by section 121.4501(21), Florida Statutes, and fail to make a selection of investment options shall be the FRS Select Money Market Fund.

VIII. PARTICIPANT EDUCATION AND INVESTMENT ADVICE

- A. The education component of the PEORP program shall be designed by the Board to assist employers, eligible employees, participants, and beneficiaries in order to maintain compliance with section 404(c) regulations and to assist employees in their choice of defined benefit or defined contribution retirement programs. Educational services include, but are not limited to, disseminating educational materials; providing retirement planning education; explaining the differences between the defined benefit retirement plan and the defined contribution retirement plan; and offering financial planning guidance on matters such as investment diversification, investment risks, investment costs, and asset allocation. The following items must be made available to participants in sufficient time to allow them an opportunity to make informed decisions: -
 - o A description of all investment funds including: general investment objectives, risk and return characteristics, and type and diversification of assets.

- An explanation of how to give investment instructions and any limits or restrictions on giving instructions.
- A description of any transaction fees or expenses that are charged to the participant's account in connection with purchases or sales of an investment fund.
- Investment fund profiles as defined at Sections 121.4501(15)(c).
- Descriptions of the annual operating expenses for each investment alternative, such as investment management fees.
- The value of shares of all investment funds and a quarterly participant statement that accounts for contributions, investment earnings, fees, penalties, or other deductions.
- Information concerning the past investment performance of each investment fund, net of expenses, and relative to appropriate market indices.

- B. Consistent with Sections 121.4501(8)(b)3. and 121.4501(10)(b), Florida Statutes, the education component shall provide system members with impartial and balanced information about program and investment choices. In addition, the approved education organization shall not be an approved investment provider or be affiliated with an approved investment provider. Educational materials shall be prepared under the assumption that the employee is an unsophisticated investor and all educational materials, including those distributed by bundled providers, shall be approved by the Board prior to dissemination. Participants shall have the opportunity to choose from different levels of education services, as well as a variety of delivery methods and media. All educational services offered by investment product providers shall be provided on a fee-for-service basis.
- C. The Board shall contract for the provision of low-cost investment advice to participants that is supplemental to educational services and that is paid for by those receiving the advice. Investment advice shall consist of impartial and balanced recommendations about investment choices consistent with Rule 19-13.004, FAC. Participants shall have the opportunity to choose from different levels of customized investment advisory services, as well as a variety of delivery methods and media.
- D. Bundled provider(s) selected to provide investment products for PEORP participants shall not provide any participant education services aimed at influencing the choice between the defined benefit and defined contribution programs of the Florida Retirement System. This initial education program will only be provided by the neutral education vendor hired to do so by the Board.

IX. ROLES OF THIRD-PARTY ADMINISTRATOR AND BUNDLED PROVIDER

- A. The Board selects a single private party to serve as the third-party administrator for PEORP. The Board makes the final determination as to whether any third-party administrator shall be approved for the program. Administrative services such as individual and collective recordkeeping and accounting, IRC limit monitoring, enrollment, beneficiary designation and changes, disbursement of monies, and other centralized administrative functions shall be provided by the single third-party

administrator selected by the Board. The SBA retains the right to delineate through the contract the specific administrative services to be provided by the Bundled Provider. The SBA also retains the right, consistent with Section 121.4501(8)(b)1., Florida Statutes, to enter into a contract with the Department of Management Services for certain administrative services.

- B. Bundled provider(s) selected to provide investment products to the participants will provide administrative services that are uniquely relevant to the bundled provider mandate. The SBA shall specify the administrative services to be provided by the single third-party administrator and the bundled provider in the solicitation documents and contracts for services.

X. PEORP INVESTMENT OPTIONS AND PERFORMANCE BENCHMARKS

- A. The authorized categories of PEORP investment options are contained in IPS-Table 1. The default option for participants that fail to make a selection of investment options shall be the Moderate Balanced Fund. The number of investment options shall not exceed the “Maximum Number of Options” listed in IPS-Table 1 for each category, except to the extent that
- 1) Multiple investment options within the same category are simultaneously offered to facilitate a transitional mapping of contributions and account balances from a terminating option;
 - 2) An investment option is temporarily closed to new contributions and account balance transfers.

IPS-Table 1: Authorized Investment Option Categories and Representative Performance Benchmarks and Retiree Annuities

Investment Option Categories	Maximum Number of Options	Representative Performance Benchmarks
Tier I: Core Investment Options		
Money Market	1	Money Fund Report Institutional Average (Tax.)
Inflation-Protected Bond	1	Barclays Capital U.S. Treasury Inflation Note Index
U.S. Bond	2	Barclays Capital Aggregate Bond Index
U.S. Core Stock	2	Russell 3000 Index
U.S. Small/Mid Stock	2	Russell 2000 Index
Foreign Stock	2	MSCI World, excluding U.S., Index
Tier II: Balanced Investment Options		
Conservative Balanced Fund	1	Weighted-Average of Constituent Fund Benchmarks per Table 2
Moderate Balanced Fund	1	Weighted-Average of Constituent Fund Benchmarks per Table 2
Aggressive Balanced Fund	1	Weighted-Average of Constituent Fund Benchmarks per Table 2
Tier III: Specialty Investment Options		
U.S. Large Value Stock	1	Russell 1000 Value Index

U.S. Large Growth Stock	1	Russell 1000 Growth Index
U.S. Small/Mid Value Stock	1	Russell 2000 Value Index
U.S. Small/Mid Growth Stock	1	Russell 2000 Growth Index
Global Stock	1	MSCI World Index
U.S. Short/Intermediate Bond	1	Barclays Capital Intermediate Aggregate Bond Index
High Yield Bond	1	Barclays Capital High Yield Index

Tier IV: Retiree Annuity Options (Section 121.591(1)(c), Florida Statutes)

Immediate and Deferred Annuities	Not Applicable	Specified by the Executive Director
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- B. Investment options and investment products (i.e., that support Investment Funds that are composed of an aggregate of one or more investment products) may be provided by investment managers or bundled providers. Pursuant to Section 121.4501(9)(a), Florida Statutes, the Board shall select one or more providers who offer multiple investment products when such an approach is determined by the Board to afford value to participants otherwise not available through individual investment products.

- C. Investment options may have performance benchmarks other than the “Representative Performance Benchmarks” listed in IPS-Table 1, but any alternative performance benchmark must be identified in the investment guidelines required under Section XI of this IPS and provide substantial coverage of the financial market segment defined by the corresponding Representative Performance Benchmark.

- D. Balanced funds are only available as a weighted average of Tier I and III options. The Board shall establish procedures for initiating rebalancings per approved investment guidelines.

- E. With IAC review and input, the Executive Director shall periodically recommend changes to the authorized investment option categories in IPS-Table 1, as modifications are appropriate. Any recommended modifications must be justified in terms of the incremental costs and benefits provided to participants.

XI. GENERAL INVESTMENT OPTION GUIDELINES

- A. The Executive Director is responsible for developing specific investment policies and guidelines for investment options, which reflect the goals and objectives of this IPS. In doing so, he is authorized to exercise and perform all duties set forth in Section 121.4501(9), Florida Statutes, except as limited by this IPS or Board Rules. General guidelines are as follows:
 - 1) The Money Market fund seeks high current income consistent with liquidity and capital preservation. The fund will be actively managed and will primarily invest in high quality, liquid, short-term instruments to control credit risk and interest rate sensitivity. The fund’s sensitivity to interest rate changes will approximate that of the performance benchmark.

- 2) The U.S. Bond funds seek high current income consistent with capital appreciation. The funds may be passively or actively managed and will primarily invest in securities contained in the benchmark, although other fixed income instruments which fit the funds' objectives may be selectively used to generate excess return, such as non-investment grade securities or securities issued by foreign entities. The funds' sensitivity to interest rate changes will closely approximate that of the performance benchmark.
- 3) The U.S. Large Stock funds seek capital appreciation and current income. The funds may be passively or actively managed and will primarily invest in equities contained in the benchmark. Other securities which fit the funds' objectives may be selectively used to generate excess return. The funds' investment process will not have a persistent bias toward the selection of securities that are predominantly in the growth or value style categories.
- 4) The Foreign Stock funds seek capital appreciation and current income. The funds may be passively or actively managed and will primarily invest in equities contained in the benchmark, although other securities which fit the funds' objectives may be selectively used to generate excess return, such as equity securities issued by corporations domiciled in emerging economies.
- 5) The Balanced Investment funds are diversified balanced portfolios designed to provide participants with pre-packaged asset allocation vehicles. The funds seek favorable long-term returns through investments in the Tier I and III Options according to the risk levels identified in IPS-Table 2. Asset allocations will generally be held within 5 percentage points of the optimal shares for their respective risk target, but short-term deviations may occur. Optimized asset allocations for the balanced funds shall be established using methodology consistent with the guidance rendered by the PEORP's education/advice vendor.

IPS-Table 2: Target Risk Levels of Balanced Investment Funds

	Conservative Balanced Fund	Moderate Balanced Fund	Aggressive Balanced Fund
All asset classes shall be included for optimization of each balanced fund to the risk levels indicated. Actual Tier I and III investment funds included in the balanced funds and their respective weightings shall be reported to the Trustees and communicated to participants.	A risk level equivalent to that of an all bond portfolio	A risk level equivalent to that of the average U.S. investor	A risk level approximately mid-way between that of an all equity portfolio and the Moderate Balanced Fund

- 6) The Inflation-Protected Bond fund seeks long-term total returns that keep pace with inflation in order to protect the purchasing power of accumulated participant benefits. The fund may be passively or actively managed and will primarily invest in the U.S. Treasury's inflation-indexed securities. The fund's sensitivity to interest rate changes will closely approximate that of the performance benchmark.
- 7) The High Yield Bond fund seeks high current income consistent with capital appreciation. The fund will be actively managed and will primarily invest in non-investment grade securities contained in the benchmark, although other fixed income instruments which fit the funds' objective may be selectively used to generate excess return, such as non-rated securities or securities issued by foreign entities. The fund's sensitivity to interest rate changes will closely approximate that of the performance benchmark.
- 8) The U.S. Large Value Stock fund seeks capital appreciation, and to a lesser degree, current income. The fund will be actively managed and will primarily invest in equities contained in the benchmark, generally characterized by lower price-to-book ratios and lower projected earnings growth than the overall U.S. equity market averages. Other securities which fit the funds' objectives may be selectively used to generate excess return.
- 9) The U.S. Small/Mid Stock funds seek capital appreciation. The funds may be passively or actively managed and will primarily invest in equities contained in the benchmark, although other securities which fit the funds' objectives may be selectively used to generate excess return. The funds' investment process will not have a persistent bias toward the selection of securities that are predominantly in the growth or value style categories.
- 10) The U.S. Large Growth Stock fund seeks capital appreciation. The fund will be actively managed and will primarily invest in equities contained in the benchmark, generally characterized by higher price-to-book ratios and projected higher earnings growth than the overall U.S. equity market averages. Other securities which fit the funds' objectives may be selectively used to generate excess return..
- 11) The U.S. Small/Mid Value Stock fund seeks capital appreciation, and to a lesser degree, current income. The fund will be actively managed and will primarily invest in equities contained in the benchmark, generally characterized by lower price-to-book ratios and lower projected earnings growth than the overall U.S. equity market averages. Other securities which fit the funds' objectives may be selectively used to generate excess return.
- 12) The U.S. Small/Mid Growth Stock fund seeks capital appreciation. The fund will be actively managed and will primarily invest in equities contained in the benchmark, generally characterized by higher price-to-book ratios and projected higher earnings growth than the overall U.S. equity market averages. Other securities which fit the funds' objectives may be selectively used to generate excess return.
- 13) Each investment option must:

- (a) Have a prudent degree of diversification relative to its performance benchmark;
- (b) Be readily transferable from a PEORP account to another PEORP investment option or to a private-sector or public-sector defined contribution plan accounts and self-directed individual retirement accounts;
- (c) Allow transfers of participants' balances into and out of the option at least daily;
- (d) Have no surrender fees or deferred loads/charges;
- (e) Have no fees or charges for insurance features (e.g. mortality and expense risk charges);
- (f) To the extent allowed by law, notwithstanding failure to meet one or more of the IPS Section XI(13)(b),(c)-(f) requirements, an option may be authorized if: (i) it produces significant and demonstrable incremental retirement benefits relative to other comparable products in the market place and comparable Tier I, Tier II, or Tier III options; and (ii) the incremental benefits are sufficient to offset all associated fees, charges and the expected economic cost of the variance(s) with the IPS Section XI(13)(b),(c)-(f) requirements. Comparability shall be based on the option's underlying investments within the broad categories of Money Market, U.S Fixed Income, U.S. Equities and Foreign Equities.

14) The investment product supporting any annuity option offered in Tier IV must have a prudent degree of diversification relative to its performance benchmark and, where applicable, providers shall have high independent ratings for financial strength and stability. Tier IV options may include allocated or unallocated immediate annuities with combinations of some of the following features:

- (a) Single or flexible premium.
- (b) Life or fixed period payouts.
- (c) Single or joint life (survivors with an insurable interest).
- (d) Complete or partial survivor benefits.
- (e) Cash refund, installment refund or period certain features.
- (f) Variable or fixed payments, non-participating, or income payable features.
- (g) Deferred payments.

B. The long-term performance of each actively managed investment option is expected to exceed the returns on their performance benchmark, net of all fees and charges, while avoiding large year-to-year deviations from the returns of the performance benchmark. The long-term performance of each passively managed investment option is expected to closely approximate returns on the performance benchmark, net of all fees and charges. Investment managers are authorized to prudently use options, futures, notional principal contracts or securities lending arrangements, in accordance with the fiduciary standards of care, as contained in Section 121.4501(15)(a), Florida Statutes, investment guidelines and related policies.

XII. INVESTMENT MANAGER SELECTION AND MONITORING GUIDELINES

- A. The Executive Director shall develop policies and guidelines for the selection, retention and termination of investment managers, bundled providers and products, and shall manage all external contractual relationships in accordance with the fiduciary responsibilities of the Board, this IPS and provisions of Section 121.4501(9)(c), Florida Statutes.

When the Executive Director decides to terminate an investment fund in the PEORP, participants will be granted an opportunity to direct their assets to other PEORP investment fund options prior to the investment fund termination. Assets that are not directed by participants will be transferred or “mapped” to the investment fund(s) that the Executive Director deems appropriate. The mapping factors that the Executive Director will consider include, but are not limited to, alignment of investment fund type (e.g., asset class, capitalization and style) and investment strategy (e.g., objectives, market focus, and implementation tactics).

- B. In the selection of investment managers, investment products or bundled providers, consideration shall be given to their effectiveness in minimizing the direct and indirect costs of transferring the total present value of accumulated benefit obligations for existing employees that choose membership in PEORP from the defined benefit trust to the PEORP trust.
- C. In the selection and monitoring of products from bundled providers, each proposed product will be evaluated on a stand-alone basis, pursuant to the requirement in Section 121.4501(9)(c)9., Florida Statutes. The cost-effectiveness of the levels of non-investment services supporting the products will also be evaluated relative to their benefits.
- D. In the selection, retention and termination of bundled providers and their proposed products and services, value afforded, as that term is used in Section 121.4501(9)(a), Florida Statutes, shall be evaluated based on the value added to the process of accumulating retirement benefits for participants. This evaluation shall consider the following factors in arriving at any staff recommendation:
- 1) Additional products or services that are not otherwise available to the participants within the program;
 - 2) The type and quality of investment products offered;
 - 3) The type and quality of non-investment services offered; and
 - 4) Other significant elements that provide value to participants, consistent with the mandates of Section 121.4501, Florida Statutes.
- E. On at least an annual basis, a review will be conducted of the performance of each approved investment manager and product and related organizational factors to ensure continued compliance with established selection, performance and termination criteria, Board policy and procedures and all contractual provisions. The performance and termination criteria for each provider and investment product will be reflected in each employment contract.

- F. In addition to reviewing the performance of PEORP's investment managers/options, the Executive Director will periodically review all costs associated with the management of PEORP's investment options, including:
- 1) Expense ratios of each investment option against the appropriate peer group; and
 - 2) Costs to administer the Program, including recordkeeping, account settlement (participant balance with that of investment), allocation of assets and earnings, and (when applicable) the proper use of 12b-1 fees to offset these fees.

XIII. REPORTING

- A. The Board directs the Executive Director to coordinate the preparation of quarterly reports of the investment performance of the PEORP by the Board's independent performance evaluation consultant.
- B. The following formal periodic reports to the Board shall be the responsibility of the Executive Director: an annual investment report, an annual financial report and a monthly performance report.

XIV. IMPLEMENTATION SCHEDULE

This IPS is effective upon approval of the Board.