SETTING INVESTMENT POLICY

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SETTING INVESTMENT OBJECTIVES AND DIVERSIFICATION

The primary principle to observe in investing other people's money is to establish investment objectives. Managers have to consider the investment policy statement, which includes guidelines for investing, take appropriate courses of action, and monitor the portfolio. The process clearly implies the usage of an investment management consultant. The DOL virtually mandates investment objectives and the use of a consultant as seen in this excerpt from a 1999 interpretive bulletin.

It is generally established that if a money manager exceeds a percentage limitation in an investment style or securities class, the manager will be held liable.

CASES

In Dardaganis v. Grace Capital, the money manager ignored the trustee's refusal to raise the % limitation on investments, and exceeded that limitation. The principal, Grace, was found to be personally liable as he signed on to personally oversee and manage the portfolio.

Comment [JL1]: Citation Missing

In Laborers National Pension Fund v. Northern Trust Quantative Advisors, Inc., the money manager was hired to manage $170 million of a $1 billion portfolio. 6.5% was the fixed income component ($11 million) was invested in interest only bonds (I/Os). The fund guidelines said that:

Comment [JL2]: Citation missing

- ***Only holdings permitted under the prudent man rule were permitted***
- ***Bonds are limited to Federal or Agency or Corporate abb or better***

- ***No options, short sales, margin, letter stocks, private placement debt, commodities, venture capital, or foreign securities are permitted unless approved by the trustees***
- ***Diversification permitted mortgages as long as the goal is to preserve principle***
- ***The manager has full discretion***

The manager having established an account review committee considered the guidelines.

Since I/Os were not prohibited by the guidelines considering investments not in isolation but in the context of modern portfolio, the manager was found to be in compliance.

Finally, it fell to <u>GIW Industries v. Trevor Stewart, Burton and Jacobson</u> to hold a money manager liable for not inspecting the investment objectives of a fund. Trevor Stewart invested 75% of GIW's portfolio in long-term government bonds. GIW knew of TSBJ's investment philosophy but hired them with no restrictions. No one at TSBJ read plan documents, knew the plan history, their cash needs or the demographics of the participants. When Trevor was terminated, they had lost over $700,000 and collected fees of $17,031.54. The court said TSBJ subjected GIW to too much market risk and liquidity risk and failed to diversify the investments. They were fined $537,000 and had to rebate their fees. In prudent investing, then, no risk may be too risky given the financial circumstances and demographics of the client.

Comment [JL3]: Citation missing

<u>INVESTMENT PRINCIPLES</u>

Other investment principles for managers and consultants to observe include areas we previously discussed, including the following:

It is well established that every plan subject to fiduciary rules under ERISA, UPIA, UMIFA or other state and federal regulations must be maintained in a written document. Certain matters must be included in this document, such as:

- One or more named fiduciaries.
- A funding policy consistent with the objectives of the plan to determine short and long range financial needs such as liquidity and investment growth.
- A procedure for the allocation of responsibilities for operating the plan, including investing plan assets.

- Plan amendment procedures.
- Basis for contribution and payments.
- Responsibility, delegation and allocation, such as the appointment of investment managers.
- The naming or appointing of trustees.

In the absence of these allocation and delegation provisions in the plan documents, it will not be possible to engage in them. A trustee cannot appoint an investment manager unless there is a provision in writing permitting retention of a manager and unless that trustee has specifically been allocated authority to appoint a manager.

Plan documents include all documents which contain provisions which affect the operation of the plan, plan assets, participants' and beneficiaries' rights. The documents include contracts with service providers, plan rules and provisions, directors' resolutions and investment objectives.

Critical to the investment process is the funding policy. It enables administrators and trustees to evaluate and implement plan needs and investment policy. Since investment choices are dictated by the needs of the plan, short and long term financial requirements must be communicated by fiduciaries to those who invest plan assets. The funding policy is a crucial factor in the analysis to determine these needs.

As has already been seen, the only prudent course of action a fiduciary can take is to document his responsibilities and the responses to them. Since the Regulators clearly dictate that a document which governs a plan must be in place in order to establish some sort of rationale against which subsequent judgments can be made and evaluated, these investment objectives must be in writing. If the investment program is spelled out, then actions can be justified later as part of the overall strategy.

On a panel discussion some years ago, Jim Hutchinson, a drafter of ERISA, said, "Take the plan, look at its needs and objectives in terms of required return, and the alternative means of achieving the objectives. Choose one course of action, and document the rationale for that choice."

An investment policy may be appropriate or not, but regardless, it is defensible if it is properly documented. The minimum requirements for such documentation should include:

- The method for selection, monitoring, evaluating, retaining, and firing investment managers
- A policy for supervising investment performance and for making this information available to participants and beneficiaries
- There is no other way that a prudent fiduciary can meet his obligations unless the investment policy is clearly set down consistent with the fund's documents and instruments. If the objectives are designed carefully, clearly enunciated and set down in well-thought-out investment policy, then the fiduciary will be able to defend all

future actions relating to the investment of those funds as long as they are consistent with the policy.

- The specifics of setting objectives goes deeper than preservation of capital or beating an index. It is, after all, the participants' money and the purpose of the plan is to provide assets for payment to the participants when it is required. Therefore, investment objectives should be made considering return, time period, levels of risk, liquidity and income requirements evaluated in terms of the particular requirements of the plan in question. ERISA case law discussed in the prudent investment section, clearly states that each plan stands on its own facts. Different plans will have different objectives depending on the type of plan, age of participants, financial condition of the company, expenses, liabilities, economic and industrial factors, actuarial assumptions, cash flow and liquidity requirements, and fund planning conclusions. The administrator, trustee or fiduciary should expect to respond to a lengthy questionnaire if he selects professional help to establish these objectives. Unless specific questions are addressed, a prudent investment policy cannot be maintained.

Once all the above considerations have been addressed, the critical factor in selecting a prudent investment course of action lies in defining the appropriate level of risk with regard to the returns desired. Since the Department of Labor evaluates individual investment prudence as a component of the entire portfolio, whether one investment loses money or not is not a significant question. The risk-return analysis is examined in a later chapter.

INVESTMENT OBJECTIVES STATEMENT

A simple statement of investment objectives for a fund with a relatively old work force where 50% are expected to retire in the next 10 years will require liquidity and income perhaps with a compounding effect. Security and preservation of capital will be paramount with strong incentive to keep costs low and stable. It may look, in part, like this:

ABC Corporation wishes preservation of capital as its primary investment objective. Investments should provide stable returns with high current income. Capital appreciation and high growth of principal are secondary to maintaining liquidity and consistency. A long term (10 year) total time and dollar return of 8.5% is desired with a preferable asset mix per year of:

	Maximum	Minimum
Equities	30%	0%
Fixed Income	80%	40%

Cash Equivalents	100%	20%

The desired return should exceed by 2.5% per year the actuarial assumptions set by independent counsel. Given the current economic conditions and the long term expectancy for inflation to remain moderate to low, this should warrant relatively low volatility in terms of return.

[Add a procedure for selecting investment managers, a review and evaluation process, and a method to amend the objectives and, in a few pages, a relatively defensible statement of investment policy can be achieved.]

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COMPONENTS OF INVESTMENT POLICY

Before a broker/consultant can consider assisting a fund develop written investment objectives, there are several things that must be considered.

You must know the nature of the plan and the purpose of the assets. Evaluate the current and future financial prospects of the sponsor (e.g., for a multi-employer plan, is the industry growing or in decline), ask what is the current financial condition of the plan sponsor, what is the type of plan (defined benefit versus defined contribution, foundation, endowment, trust, etc.), what are the sponsor's objectives for the plan (is it intended to fund primary retirement or is it a supplemental savings plan). All must be weighed in developing a rational approach to overall investment policy.

The regulators say four factors must be addressed:

1. Understanding and minimizing risks relating to all investments
2. Generating favorable return without undue compromise of policy guidelines
3. Provide for adequate liquidity
4. Ensure the ability to meet funding requirements (pay retirees)

To evaluate these factors, you should answer the following questions:

- What type of credit analysis is required?
- When to use investment ratings?
- Specific instruments allowable?
- Acceptable liquidity?
- Diversification desired?
- Investment authority/delegation?
- Performance reporting requirements (frequency and content)?
- Trading guidelines?
- Definition of speculative activities?
- Internal controls?
- Custody?

Ask the trustees to consider the following questions.

- What are the risks of a short-term adverse outcome like October, 1987 or the current crisis?
- What will your emotional reactions be?
- How knowledgeable are the trustees about the risk and return characteristics of the capital?
- What are the consequences of interim fluctuations of the value of your assets?
- What are the legal and accounting issues that might affect your decision making?

- **The International Foundation of Employee Benefit Plans suggests the following questions should be addressed for all employee benefit plans:**

- Are the trustees familiar with the fundamentals of investing money? Do they understand investment terminology? Do the trustees understand the alternative types of investment vehicles available to the fund? Do the trustees understand investment management?
- Does the trust fund regularly measure the investment performance of its portfolio?
- Is the performance of the portfolio measured against other funds and market indices?
- Has the board of trustees reviewed the implications of the fiduciary standards under ER1SA?

- Has the trust fund established specific investment objectives in writing?
- Has the board of trustees recognized the importance of the asset allocation decision?
- Does the board of trustees regularly communicate with their investment managers to review performance vs. objectives?
- Has the board of trustees specifically discussed such matters as risk definition and the trustees' attitude toward risk?
- Has the board of trustees discussed the ways in which the fund might wish to diversify assets?

After all these factors are considered, then and only then can the broker/consultant begin to assist drafting an investment policy statement.

ESTABLISHING INVESTMENT POLICY

Establishing sound investment policy itself is a simple five-step process.

1. Identify the plan needs
2. Determine an acceptable risk level for the fund
3. Determine an appropriate asset allocation to satisfy the risk tolerance
4. Select an investment management strategy and style to fit each asset class selected
5. Hire the appropriate money managers.

Where most Employee Benefit Funds fail is in going to step five first without considering the other four. Plan sponsors or their trustees often believe they satisfy their fiduciary responsibilities by hiring a money manager, but that simply does not work unless the entire process is followed. Let's look at each component more closely.

1. Identify Plan Needs

- The needs of a defined benefit plan differ from those of a defined contribution plan, from those of a foundation, etc.
- For a defined benefit plan, a trust, or a foundation or endowment, you might analyze cash flow requirements and examine funding status.

- For a defined contribution plan, such as a 401(k) or 403(b) plan, consider the importance of low volatility. An objective might be to preserve principal or get a real return.

2. ***Determine Acceptable Risk Level***

- For a defined benefit plan or trust, look at financial condition of sponsor or grantor. Standard deviation, BETA, downside movement might be important to consider before investing.
- In a defined contribution plan, the loss of principal or loss of buying power may be a significant factor. Probability of not meeting the anticipated return might be the most significant investment risk.

> For example, a fund earns 8% for three years. During the fourth year, it loses 8%. A 26.7% return during the fifth year must be achieved if the fund is to have an 8% compound return for the five year period.
>
> You have to define: What is risk? Trustees must understand capital markets, examine volatility/standard deviation, liquidity, consider holding periods.

3. ***Determine Asset Mix***

- What are the needs of the plan?

> The allocation reflects the needs of the plan (e.g., cash flow for benefit payments), the sponsor's financial status and future business prospects (growing, maturing or declining company or industry) and the other factors that determine an acceptable risk level (for example, the historical behavior of asset classes). If the plan sponsor believes that future market conditions can be predicted with reasonable reliability, the sponsor may use market timing or continual reapportionment among the asset classes in anticipation of such changes. If the plan sponsor is not certain of the predictability of market conditions, the sponsor may elect to allocate plan assets within a static framework or devise an investment policy that incorporates fluctuations in asset allocation within limited guidelines.
>
> Determine the Investment Management Style (For each asset class selected) Goals for each must be selected such as:

- Outperform the market
- Approximate the market
- Underperform bull, outperform bear markets

> ASK: Can the market be outperformed and can a manager add value? Ideally the process will culminate in a thoughtful, written policy with specific principles that the plan sponsor will use in selecting investment managers, in communicating to each manager the investment guidelines

the manager is to observe and the objectives he or she is to accomplish, and in evaluation the manager's performance.

4. ***Pick a Manager***

5. ***Components***

A sound investment policy results from the plan sponsor evaluating the plans's objectives, analyzing the characteristics of various classes of assets and assessing what realistically may be expected from investments in each class. Each of the different investment management styles must be evaluated and the trustees must decide whether it is possible to outperform the market indices- all as a means of devising an investment policy for the plan, which the investment manager is expected to carry out.

MORE ON COMPONENTS OF AN INVESTMENT POLICY STATEMENT:

The role of the investment policy statement is to facilitate internal and external communication of investment policy, ensure continuity of policy during periods of turnover within a sponsor's organization, and provide a clear baseline against which to review proposed policy changes. It should contain four basic elements:

1. An overview of a plan's delegation of authority and responsibility among its various decision-making groups, including trustees, staff, actuary, administrator, consultant, money managers. It defines the roles of the various parties.
2. The sponsor's definition of the primary investment policy components, i.e., cash flow requirements, asset allocation, diversification.
3. A description of the sponsor's strategy with respect to each investment policy component, i.e., % equities, % bonds, the investment objectives, the guidelines to the managers.
4. An explanation of the sponsor’s rationale underlying the choice of investment strategies and he reason whey each was chosen.

There are 13 specific components of a sound policy statement:

1. Background information on fund

2. Identification of fiduciaries
3. Organizational structure
4. Cash flow requirements
5. Lines of authority and delegation
6. Diversification of the portfolio
7. Active/passive strategies
8. Definition of assets
9. Performance objectives
10. Guidelines
11. Brokerage
12. Voting of proxies
13. Trusteeship/custodianship

Each manager selected should be given:

1. Background information on the fund
2. Future fund and cash flow projection
3. Specific investment objectives
4. Policies related to the voting of proxies
5. Portfolio guidelines
6. Reporting requirements and review
7. Evaluation and modification methodologies

The factors that influence decisions on portfolio guidelines and constraints :

1. Policy and strategy
2. Asset allocation
3. Volatility
4. Quality
5. Diversification

When defining manager portfolio performance objectives, it is not sufficient to simply use a standardized index. Rather composite benchmarks customized to fit the asset allocation and investment strategy of each fund should be employed.

Some types of return objectives include:

1. Inflation rate +_%
2. A published index, including income +_%
3. Special index reflecting a chosen risk/reward preference
4. An evaluation comparable to other accounts having similar objectives
5. A minimum of_%
6. A goal to preserve portfolio value sufficient to avoid a plan deficit
7. A total return sufficient to stabilize contributions at _% of payroll

Some combination of several of the above can work adequately.

HOW TO USE THIS MATERIAL

It is estimated that 80 percent of smaller plans (under $3 million) do not have written investment objectives. Over 25 percent of the larger funds do not have written investment objectives. While this failure will not assure a violation of Federal or State laws, it is clearly not the prudent course of action. None of the required functions in the investment process such as investment monitoring and evaluating can be completed unless the plan's objectives are set down in writing. This function alone will enable many broker/consultants to capture assets, particularly those of the smaller plans. Furthermore, it is apparent that acceptable investment practices of a few years ago are no longer acceptable. Investment objectives need to be dynamic. Once objectives are set, they must be reviewed and re-reviewed to assure they meet fund requirements. Without considering anything else, this is sufficient to warrant hiring an investment consultant.

While the written documents need not be extraordinarily lengthy or sophisticated, they need to be specific enough to clearly meet plan needs. There would appear to be a problem with prototypes, so the consultant who offers only tailored objectives written in concert with the trustees or the investment committee will have a decided edge. He will be able to offer assurances to the plan fiduciaries that his services will meet the prudence requirements, not put them on the verge of a breach.Reviewing investments needs to begin face to face and probably is best followed by a written questionnaire completed by plan officials and then finalized and crystalized in a series efface to face conferences. It must represent a meeting of the minds, not a fill-in-the-blanks page from a form book.

It cannot be emphasized strongly enough to the prospective client that this document will represent the keystone of his compliance with his fiduciary responsibilities. A sound investment policy without supporting written documentation is a penguin—it will not fly.

Even the smallest employee benefit plan such as a three person Keogh sponsored by Dr. Smith falls under the fiduciary responsibility rules. This plan needs written investment objectives. So it becomes a matter of education for the broker/consultant to undertake. First the plan sponsor from very small to very large needs to know he has to comply with ERISA and then he needs to have specific guidance on how to comply best. The plan sponsor needs this education and the consultant who provides it objectively will be best serving the needs of the employee benefit plan marketplace.

Each question to ask Trustees or Fiduciaries leads to a solution for you, the investment consultant to offer. Take the questions the IFEBP asks you to have trustees consider and reply, "If not,…."

Following is a sample investment objective questionnaire, and a sample Investment Policy Statement. They are samples only, and may not be used as prototypes. Each Investment Policy Statement should be customized for each client.

SAMPLE INVESTMENT OBJECTIVE QUESTIONAIRE
Please complete all of the following questions by circling your responses.

1. In general, what is your attitude towards the U.S. economy over the next three to five years?
(A) Very negative
(B) Somewhat negative
(C) Neutral
(D) Somewhat positive
(E) Very positive

2. In determining your needs and setting your investment objectives, please choose one primaryand one secondary objective after reading the seven objectives listed below.

A. Liquidity — The ability to convert cash and/or to achieve or exceed on an ongoing basis a return on short-term money market instruments.
B. Current Income to Meet Financial Requirements — Generate sufficient income to meet ongoing withdrawal needs, such as monthly income for benefit payments.
C. Annual Return Sufficient to Meet Specific Requirements — Meet or exceed a specific return, for example an actuarial rate of return.
D. Preservation of Purchasing Power — Equal or exceed rate of inflation over the investment time horizon, i.e., being able to purchase the same amount of goods with your fund next year that you are able to purchase with it now.
E. Stability of Returns — Obtain a fairly consistent annual return, e.g., a bank passbook savings account consistently receives 5% each year.

F. Growth of Capital — Obtain above-average total return, i.e., forego receiving some income with the expectation that the assets will grow through appreciation.
G. Aggressive Growth of Capital — Achieve maximum total return even though it may entail taking substantial risk, i.e., take greater risk of losing your money with the expectation of being able to obtain greater rewards. (Bet on higher stakes for chance to receive bigger jackpot.)

2a. From the seven objectives listed above, which objective is your primary objective?
(Circle only one) A B C D E F G

2b. From the seven objectives listed above, which objective is your secondary objective?
(Circle only one) A B C D E F G

3. The time frame you establish to meet your goal(s) will affect your ability to do so. The longer the time frame, the better the chance that up and down market cycles will average out and the more likely you are to meet that goal. How long are you willing to wait to reach your goal?
( ) Less than three years ( ) Three to five years
( ) Five to ten years ( ) Ten or more years

4. Often an advisor has complete discretion over the asset mix of a portfolio. In other instances, either trustees or individuals have a predisposition to the balance among stocks, bonds and cash. Which best describes your sentiments?

( ) I have no preference regarding the balance of stocks, bonds and cash and will leave the determination to my advisor.
( ) I have a preference for the mix of assets. However, these preferences need not be rigidly observed.
( ) I have preferences for the asset mix which must be rigidly observed.

5. What asset mix would you feel most comfortable with?
( ) 100% Fixed Income or Cash Equivalents and 0% Equity
( ) 75% Fixed Income or Cash Equivalents and 25% Equity
( ) 50% Fixed Income or Cash Equivalents and 50% Equity
( ) 0% Fixed Income or Cash Equivalents and 100% Equity

6. Please indicate your opinion of the following asset class and individual security characteristics:

	Positive	Neutral	Negative
A. Young or emerging companies	( )	( )	( )
B. Stocks with high dividends	( )	( )	( )
C. Stocks with no or low dividends	( )	( )	( )
D. Stocks with high price earnings multiples	( )	( )	( )
E. Bonds with intermediate and maturities	( )	( )	( )
F. Unfamiliar Companies	( )	( )	( )
G. Foreign Stocks	( )	( )	( )

H. Foreign Bonds ( ) ( ) ( )
I. Real Estate ( ) ( ) ( )

7. Given the funding status of your plan, how would you like your fund to be managed.
( ) Conservatively — take very little risk, so as to obtain stable returns.
( ) Moderately Conservative — take little risk in order to receive average returns.
( ) Moderately Aggressive — take chance of losing part of your money with expectations toreceive better than average returns.
( ) Aggressively — assume chance of losing most of your money, but expect to be able to receive maximum returns.

8. Your investment loses 20% of its value in one month. Assuming that none of the fundamentals have changed, do you:
( ) Wait for it to go back up.
( ) Sell it.
( ) Buy more—it looks even more attractive.

9. Investment "risk" can be reflected in different ways. Please mark an (X) next to the single item that best describes how you tend to view risk.
( ) The possibility of not achieving an established target rate of return.
( ) Erosion of purchasing power; not keeping pace with inflation.
( ) Long-term erosion of capital; gradual loss of original investment
( ) Total portfolio value bouncing up and down even if it is essentially in phase with general market fluctuations.
( ) Chance of significant loss of overall portfolio.
10. Please circle the letter of the portfolio whose five-year investment average is most in keeping with your own preference and expectations.
5-Year

	Year1	Year 2	Year 3	Year 4	Year 5	Average
(A) Portfolio A:	+8%	+5%	+8%	+7%	+6%	+7%
(B) Portfolio B:	+27%	-4%	+22%	+18%	-5%	+11%
(C) Portfolio C:	+37%	-9%	+39%	+32%	-10%	+16%

11. If risk is measured on a scale of 1 to 10, 1 being most conservative and 10 being the most aggressive, where on this scale would you feel most comfortable? (Circle one number)

Less Risk More Risk
1 2 3 4 5 6 7 8 9 10
More Conservative More Aggressive

12. Where on the scale is the highest or maximum level of risk that you are willing to assume?
The answer indicated should be at least as high as your answer to question 11.
(Circle one number)

Less Risk More Risk

1 2 3 4 5 6 7 8 9 10
More Conservative More Aggressive

Sample Statement of Investment Policy

The following asset allocation policy shall govern the overall equity commitment of the plan

Acceptable Ranges of Equity Commitment

Minimum	**Target**	**Maximum**
45%	55%	65%

Guidelines describing permissible types of equities and non-equities, or fixed income, are provided in the Diversification and Risk sections that follow.

OBJECTIVES

Based on extensive analyses of the capital markets and the emerging needs of the system, this policy has been adapted to achieve the following objectives:

1) Achieve a rate of return on investments that
exceeds inflation by at least 5%.

2) Maintain or reduce the combined (employer

plus employee) contribution rate of the system
over time. The combined rate for 2000
is 16% of payroll.

3) Maintain 120%, or higher, funding of the system's pension benefit obligation over time.

PHILOSOPHY

Since (a) assets are sufficient to pay current accrued obligations, (b) a net cash outflow is expected for the next decade, and (c) the Trustees hope to enrich* the plan through investment returns rather than from future contributions, a moderately aggressive investment posture is warranted. Median equity commitments of employee benefit plans were approximately 50% when this policy was adopted. A 55% allocation to equities is moderately aggressive in this context. All allocations are at market value. As discussed in the following section on diversification, equities include U.S. and international stocks, as well as U.S. equity real estate. This diversification should result in above average returns for the risks that are taken.

In addition to the guidelines and procedures set forth herein, rigorous compliance with all applicable statutes shall be maintained.

DIVERSIFICATION

The system's assets will be well diversified to reduce the risks of large losses. To achieve this diversification, the following policies have been adopted: Each asset class, such as stocks and bonds,will be broadly diversified to be similar to the market for the asset class. The market for stocks shall be represented by the Wilshire 5000. The market for bonds shall be represented by the Lehman Corporate/Government Bond Index.

Equity portfolio holdings may include diversifying alternative investments, such as international stocks and equity real estate. Short-term fixed income investments, defined as fixed income issues maturing in less than one year, will be managed to add value. Credit risk will be avoided in these investments since the intent is to dampen overall volatility. Multiple managers will be employed. Allocations among the managers will be controlled by the Trustees to maintain both diversification and policy guidelines. Permissible allocations may be summarized as follows:

Acceptable Ranges of Commitment

	Minimum	**Target**	**Maximum**
U.S. Stocks	40%	50%	60%
Equity Real Estate	0	5	15
International Stocks	0	0	10
Total Equities	45	55	65
Short-Term Bonds	0	5	35
Long-Term Bonds	20	40	55
Total Fixed Income	35	45	55

BOND AND STOCK RISK
The average quality of the total bond portfolio will be maintained at A or better. No more than 10% of the portfolio may be in issues rated Baa by Moody's, or BBB by Standard & Poor's, or below. Total average duration should not exceed 120% of the bond market's duration, where the bond market is represented by the Lehman Corporate/Government Bond Index. Equity investments should emphasize high quality, income-producing companies with good marketability. No individual issue shall constitute more than 10% (at cost) of the total equity portfolio.

LIQUIDITY
Benefit payments will probably exceed contributions starting in 2003. Accordingly, the core manager should be prepared to provide assets to meet these liquidity requirements as they arise.

POLICY REVIEW
The various policies and objectives of the system will be reviewed periodically. These reviews will focus on the continued feasibility of the objectives
and the continued appropriateness of the investment policies for achieving the objectives. It is not anticipated that objectives and policies will be altered frequently.

PERFORMANCE REVIEW
It is expected that the total fund will perform in the top one-third of plans with similar risk over a complete market cycle. Progress toward achieving performance objectives will be reviewed quarterly. These reviews will focus on adherence to policy and the opportunities available in the investment markets. Particular attention will be directed to reviewing performance relative to the risks; this will be achieved by comparing performance with that of plans with similar risk. It is believed that the performance expectation set forth in the statement of investment policy is reasonable and consistent over the long-term. Adherence to policy means conforming to the asset allocation, diversification, and risk guidelines set forth in the policy statement; this will also be reviewed quarterly. In regard to the individual managers, their performance
and adherence to policy will also be reviewed quarterly. Each manager will have separate policies and objectives, as established by the Board. Manager reviews will focus on adherence to policy, progress toward achievement of objectives, and performance relative to opportunities. Each manager is expected to perform
in the top one-third of managers with a similar style over a market cycle.