



# Board of Retirement Regular Meeting

## Sacramento County Employees' Retirement System

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### Agenda Item 16

**MEETING DATE:** March 17, 2021

**SUBJECT:** Enterprise Risk Tolerance Assessment

**SUBMITTED FOR:** \_\_\_ Consent      \_\_\_ Deliberation and Action       X  Receive and File

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### **RECOMMENDATION**

Staff recommends that the Board receive and file the Enterprise Risk Tolerance (ERT) assessment presentation by SCERS' general investment consultant, Verus Advisory.

### **PURPOSE**

This item represents a component of the asset liability modeling (ALM) study, which supports SCERS' Master Investment Policy Statement (IPS). The Master IPS calls for an ALM study to be conducted at least every five years.

### **DISCUSSION:**

Verus recently conducted an ERT survey with the SCERS Board. The primary objective of the assessment is to gauge Board member's understanding of risk considerations for the SCERS plan, as well as their and the plan's ability, willingness, and comfort in taking various types of risk in order to achieve SCERS' investment objectives. The assessment combines quantitative and qualitative considerations based on feedback from Board members. The feedback from the Board will play an important role in considering asset allocation mix options when conducting the asset liability modeling (ALM) study over the next several months.

A secondary objective of the ERT assessment was to gain insight and the Board's view across a number of peripheral topics, such as Board-staff governance, comfort levels with portfolio structure and underlying asset classes, environmental/social considerations, portfolio preferences related to complexity, use of active management, and investment management fees, as well as organizational and operational risks.

Verus will present the results of the ERT assessment for further discussion with the Board.

**ATTACHMENTS**

- Verus Enterprise Risk Tolerance Assessment presentation

Prepared by:

/S/

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Steve Davis  
Chief Investment Officer

Reviewed by:

/S/

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Eric Stern  
Chief Executive Officer



**PERSPECTIVES  
THAT DRIVE  
ENTERPRISE  
SUCCESS**



**MARCH 17, 2021**

Sacramento County Employees Retirement System (SCERS)

**Enterprise Risk Tolerance (ERT) Assessment**

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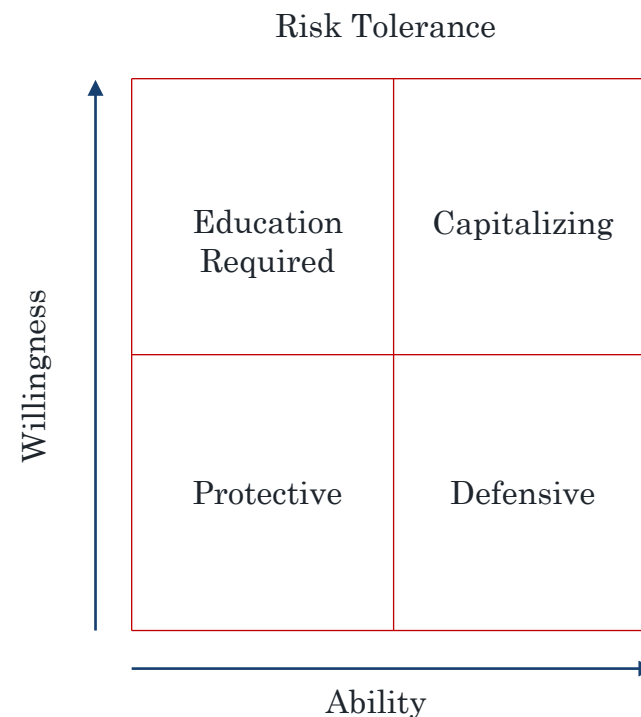
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# I. Introduction

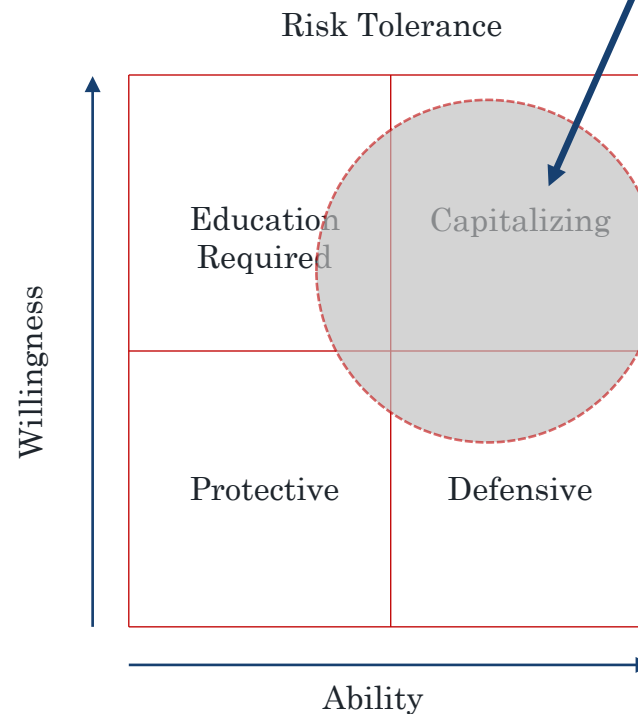
# Enterprise Risk Tolerance in Context

- Properly assessing enterprise risk tolerance (“ERT”) has important and practical implications for investment strategy development.
- Identifying the appropriate risk tolerance for a plan involves viewing risk in terms of the Plan’s willingness and ability to bear risk.
- The ability to bear risk depends on financial circumstances while the willingness to bear risk is generally based on investor’s attitudes and beliefs about investments.
- **In today’s session, we review SCERS willingness and ability to incur investment risk, based on our findings from recent Trustee interviews.**
- Although the SCERS Board’s duty is to the beneficiaries of the Association, assessing the County’s financial situation and ability to make contributions to the Pension is one component in evaluating the Plan’s ability to take on risk.
- An assessment of the financial health of the Plan sponsor will also be incorporated into the forthcoming 2021 asset/liability study.



# Summary Observations

- ERT interviews indicate a Trustee willingness to accept risk including
  - Not overly concerned about peer risk
  - Willingness to deviate from the herd
  - Confidence in governance structure
  - Willingness to consider new strategies with appropriate education/understanding
- Some potential opportunities to provide more summary level reporting



ERT Trustee interviews would imply SCERS is somewhere here

Trustees are comfortable with current level of risk/downside protection

Similar results to last ERT study conducted in 2016

Education needed to build comfort in new areas

# II. ERT Interview Process and Findings

- Mission and objectives
- Governance structure
- Plan sponsor strength
- Portfolio investment philosophy and risk assessment



# SCERS ERT Interview Objectives

## —Primary objectives:

- Assess the Trustees understanding of as well as ability, willingness and comfort in taking different types of risks to achieve the objectives of the SCERS mission
- Put current Trustee perspectives and views into historical context and incorporate into the 2021 asset/ liability study

## —Secondary benefit/opportunity:

- Validate the governance process and effectiveness among Trustees, board, staff and service providers
- Understanding and acknowledgement of what is working
- Identify potential opportunities for improvement across investment, operations and governance processes and practices

# SCERS ERT Interview Process

- ERT objectives, questions, and process prepared by Verus
  - Reviewed and conferred with SCERS senior staff
- Combined both a quantitative and qualitative assessment
- Questions were provided to Trustees in advance
  - A few questions included unfamiliar terminology and concepts
- One-hour phone/video interviews allowed for broader discussion
  - Clarification and explanation of topics/terminology to help ensure responses were based on a consistent understanding of the question
  - Provide constructive feedback as well as acknowledgement and praise
  - Discussion of areas indirectly related to asset/liability study
- Verus compiles, consolidates and summarizes data, key findings and relevant comments

Conducting an interview combined with a questionnaire allowed for clarification and consistency in understanding and responding to questions.

Interview process also allowed for more detailed discussions on opportunities in other areas.

# Mission and Objectives

*“How would you describe SCERS mission and objectives, and do you prioritize any objectives over others? “*

*“Diversified well performing investments and making certain that obligations are met for beneficiaries in a most efficient and timely manner. “*

*“Provide benefits to participants”*

*“Performing at an optimal level, addressing rates of return and safety factor, willing to invest longer term/riskier with short term investments for short term benefits.”*

*“Look after the assets of the Employers and make sure benefits are going to be there as promised “*

*“Be able to produce the checks and stay out of danger, understand who ultimate audience is”*

*“Still working on it, struggling with it. It's hard to keep it short and sweet”*

*“With Eric it's been good to review the Mission statement, and updating”*

*“Prioritize ability to meet benefits, that's the purpose of the Board”*

*“Responsible for being fiduciaries to manage benefits portfolio to pay benefits. They also have a duty to service to beneficiaries, , it's the strategic planning process that matters and we haven't gone through that yet”*

*“Our job is to make the benefit payments approved by others, invest responsibly to meet benefits and ensure diversification”*

*“Service side isn't properly represented in the Mission.”*

*“Ensure employees when they retire have a secure source of income, make investments and have money to pay benefits”*

*“Goal is to provide lifetime benefits for the employees, customer service to the employees (responsive to their needs) “*

There is broad agreement on SCERS overall Mission, objectives and priorities

Changes to specific language remains under discussion/consideration ....

# Governance Structure

*“Are you comfortable with the current monitoring process of delegated responsibilities? “*

- Are there areas where you believe there should be additional delegated authority?
- Do you feel you have sufficient information/transparency for proper oversight?
- Thoughts on improvement? On what topics is too much or too little of the Board’s time spent?

There was broad Trustee comfort with both the current governance structure and delegations.

There was acknowledgement by some Trustees that they were open to considering changes to governance/delegation structure if a specific proposal were brought forward articulating the rationale.

# Governance Structure

*“Would be nice to have self education modules that they can do at home not during a long Board meeting.”*

*“We receive a lot of detail on fees but there's no real summary”*

*“Would like more information on operations and service”*

*“Sometimes get too much detail, want high level summary reports”*

*“Makes me wonder whether I know everything I should know”*

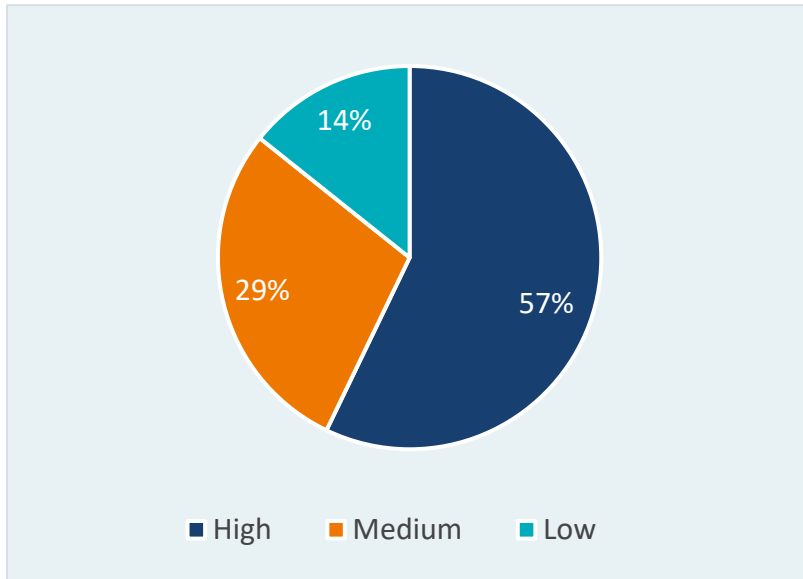
*“Out of touch with portfolio, now there are too many managers to review each one, want top level view and better top level reports”*

*“Comfortable CEO is making improvements as needed”*

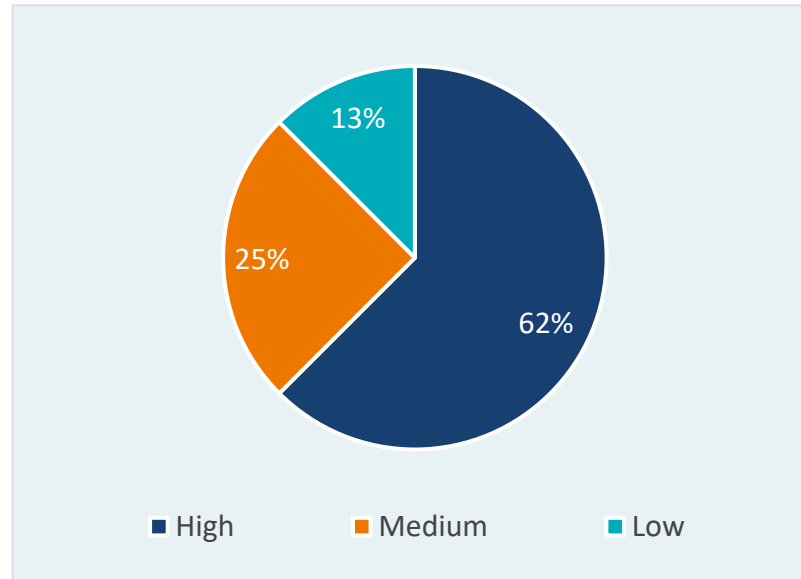
There were several Trustee comments requesting summary level reporting.

# Plan Sponsor Support

WILLINGNESS TO SUPPORT



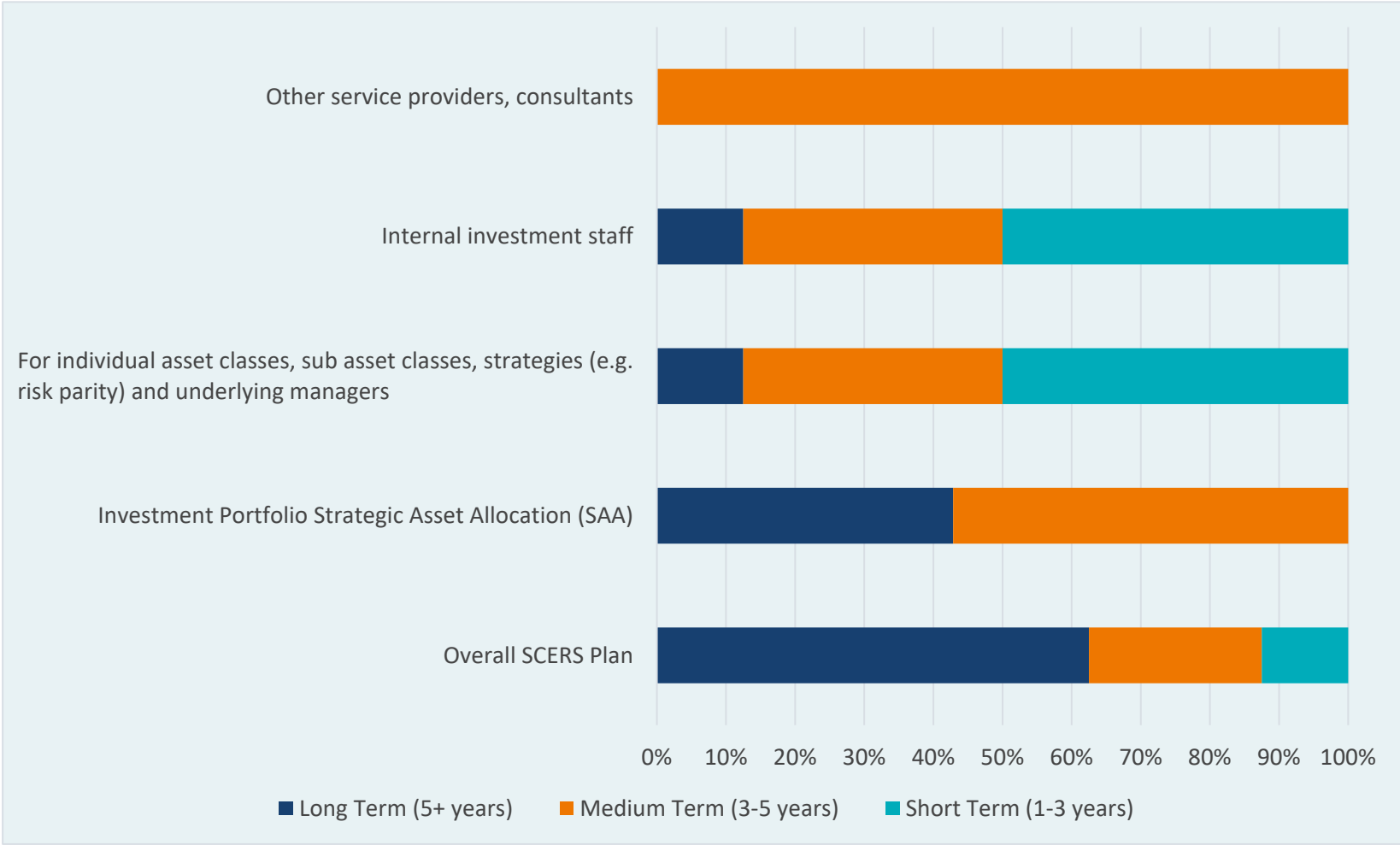
ABILITY TO SUPPORT



High level of Trustee confidence in both willingness and ability to support SCERS.

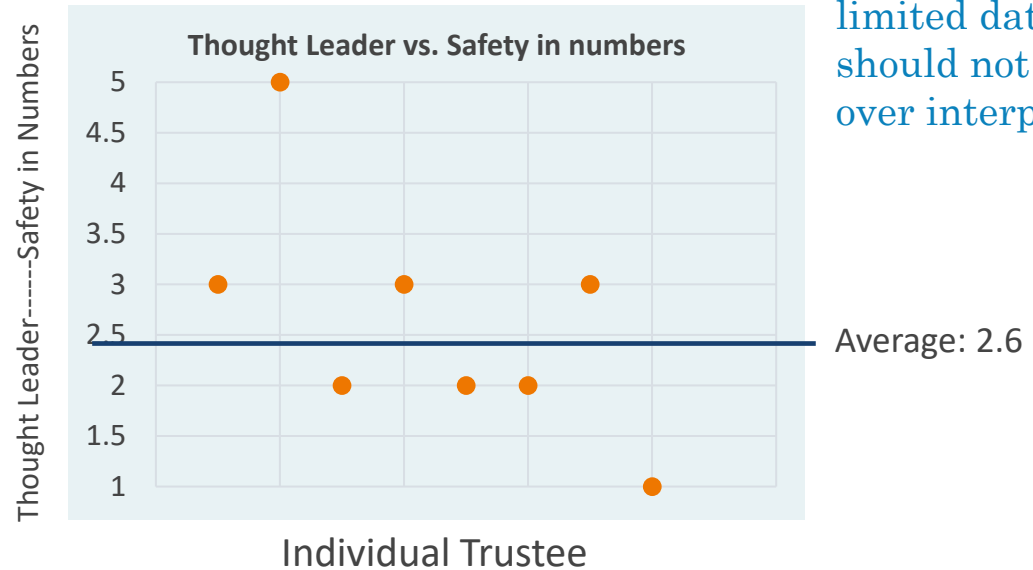
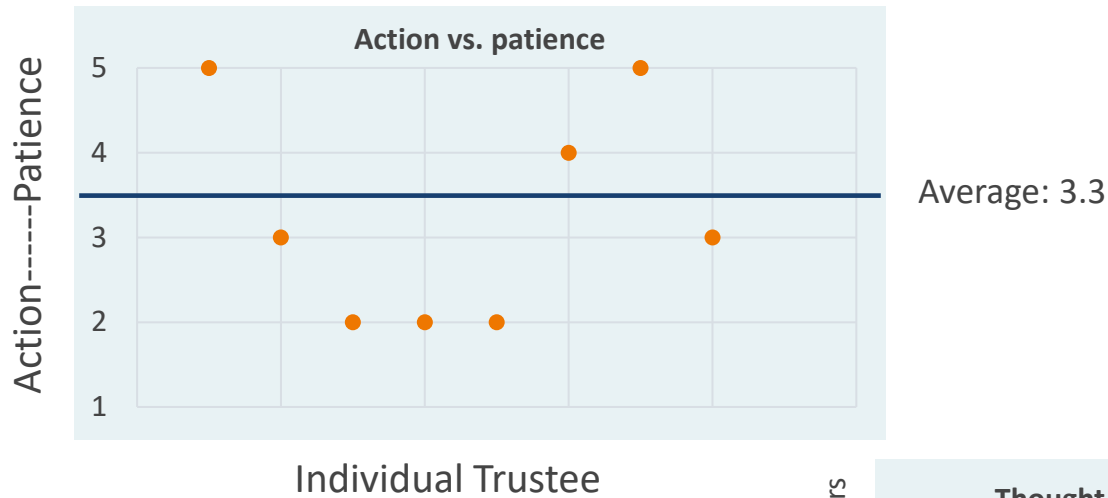
Improved transparency/communication was mentioned by some trustees as a factor leading to their increased confidence in plan sponsor support.

# Evaluation Period



Trustees are focused on appropriate evaluation periods based on the type of strategy, asset class or service being performed.

# How Active Should SCERS Be?

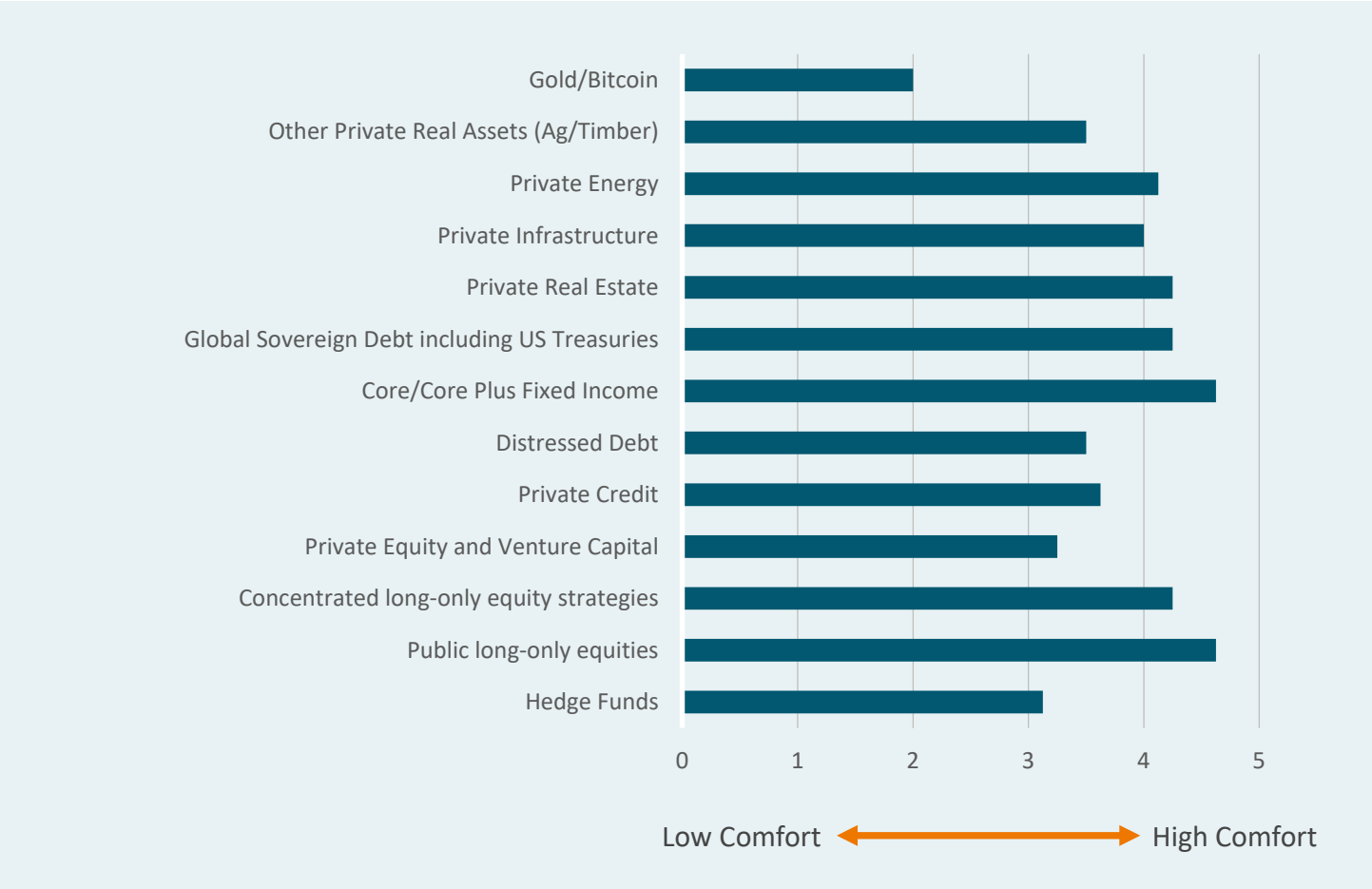


Trustees did not express any views on average that would preclude SCERS from considering portfolio strategies based on SCERS mission and objectives, however, the limited data should not be over interpreted.



# Comfort With Asset Classes

COMFORT WITH ASSET CLASSES (AVERAGE)



There was high trustee comfort investing in both traditional and alternative investments.

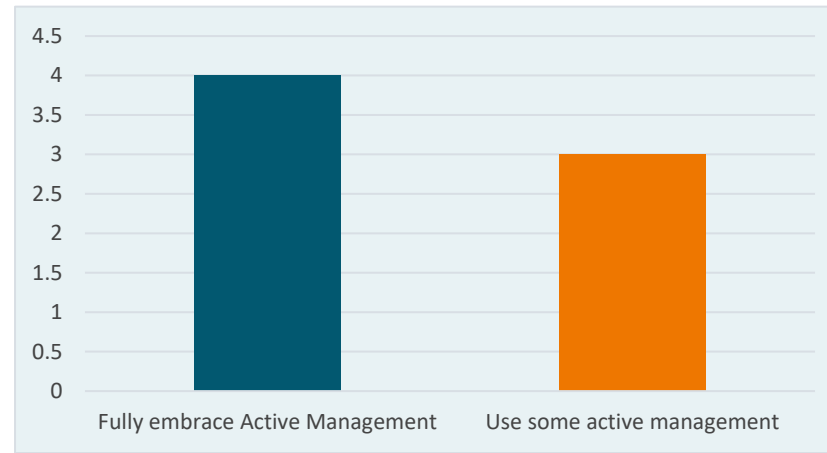
There was no real interest in investing in gold/Bitcoin but there was some acknowledgement that it could be considered if the investment case was made and supported it.

# Portfolio Preferences

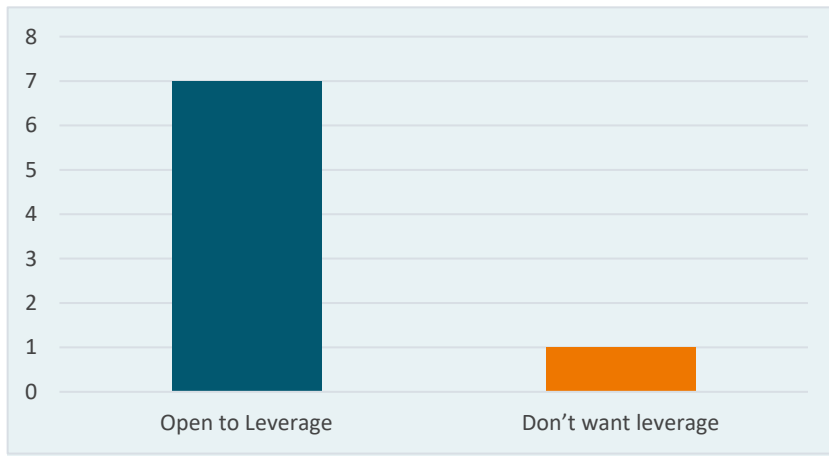
## COMPLEXITY



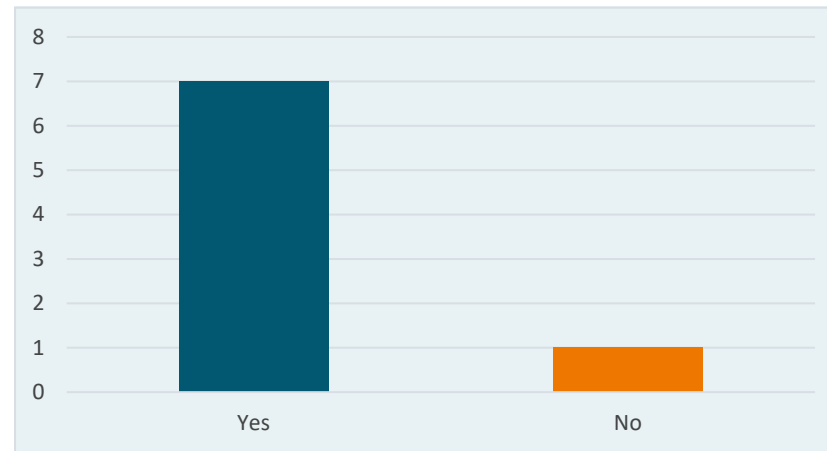
## ACTIVE MANAGEMENT



## LEVERAGE



## ARE FEES UNDERSTANDABLE/DO YOU NEED MORE INFORMATION REGARDING FEES



Trustees are aware of the benefits and potential risk of these approaches and broadly support the use or potential consideration of them as an essential part of trying to achieve the overall objectives.

Further education on newer /complex areas was mentioned as a prerequisite.

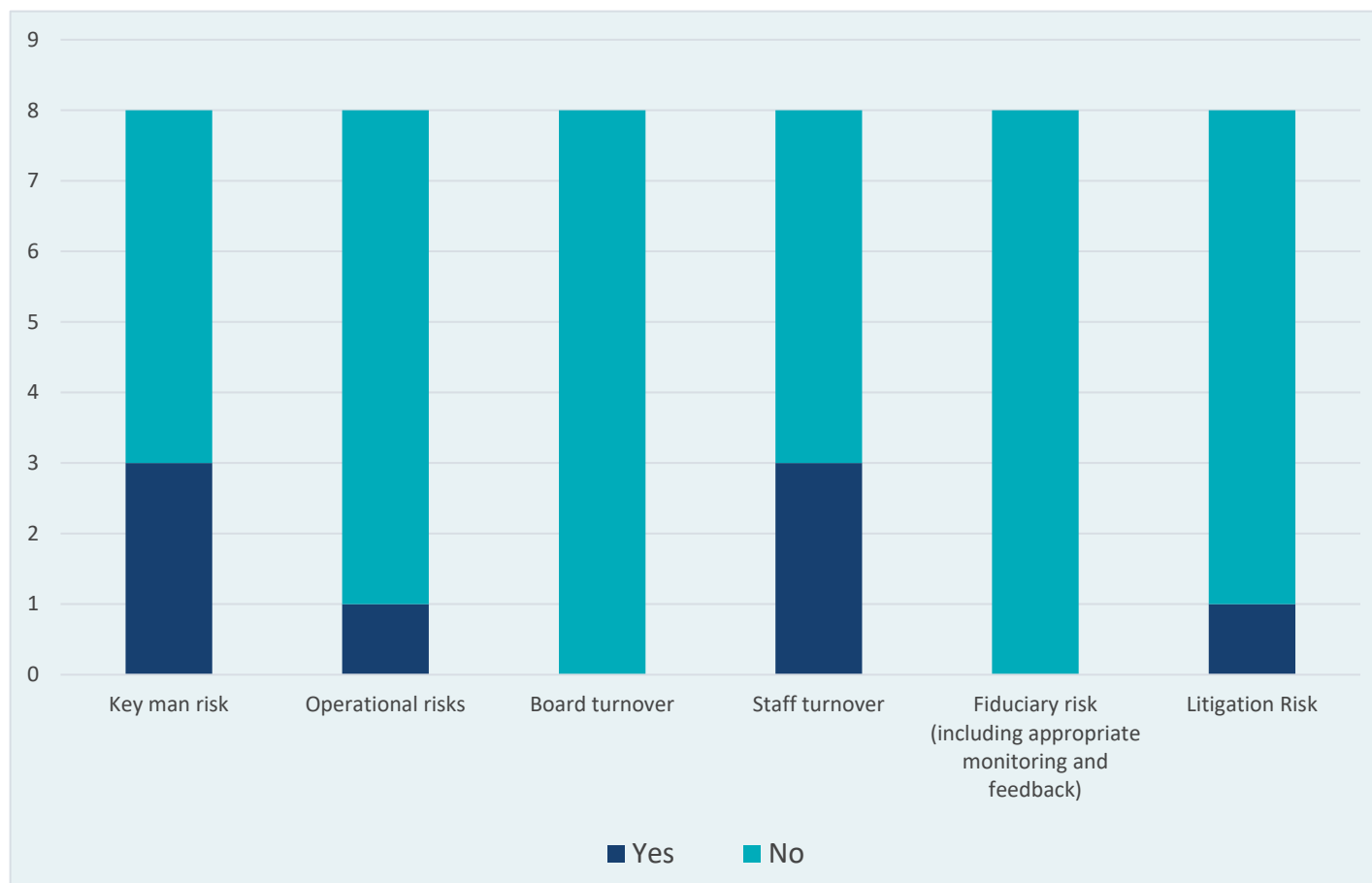
# Operational, Organizational and External Risks

*“How important are these external risks to SCERS and to what extent do you believe the Board should take them into consideration?”*

- Peer risk
- Headline risk
- Constituents
- Regulatory risk

Trustees are aware and are informed of risks in these areas but did not indicate a level of concern or a level of consideration that could adversely impact the management of the SCERS plan.

# Operational, Organizational and External Risks



Maintaining continuity of CEO/CIO and current staff was mentioned by a couple of Trustees as a potential risk area for monitoring/management.

Overall trustees indicated that they are comfortable with these organizational and external risks.

# ESG and Sustainability

*“What is your perspective on ESG policies/initiatives which are implemented and governed at the Plan level versus ESG considerations and implementation at the investment manager level?”*

*“How do you feel about maximizing portfolio returns at the expense of ESG risks /considerations – exclusionary screening?”*

There was broad understanding among Trustees of the role(s) that ESG can/will play and are comfortable incorporating ESG as long as it is consistent with Plan objectives and fiduciary responsibilities.

# III. Next Steps

# Next steps

Results from the ERT interview will be incorporated into an overall ERT assessment for SCERS and incorporated into the modelling of different potential long-term strategic asset allocation portfolios for evaluation and consideration in the upcoming asset/liability study.

