

# PERAC

COMMONWEALTH OF MASSACHUSETTS | PUBLIC EMPLOYEE RETIREMENT ADMINISTRATION COMMISSION

PHILIP Y. BROWN, ESQ., *Chair*JOHN W. PARSONS, ESQ., *Executive Director*

Auditor DIANA DIZOGGIO | KATHLEEN M. FALLON | KATE FITZPATRICK | JAMES J. GUIDO | RICHARD MACKINNON, JR. | JENNIFER F. SULLIVAN, ESQ.

## MEMORANDUM

TO: All Retirement Boards

FROM: John W. Parsons, Esq., Executive Director

RE: Outsourced Chief Investment Officer (OCIO) Policy

DATE: November 2, 2023

The Commission has seen a number of retirement systems look at the possibility of using an Outsourced Chief Investment Officer (“OCIO”) as a method of investing. This has raised concerns regarding how such an arrangement can be in compliance with the procurement provisions of Chapter 32 as well as whether such arrangements are in the best interests of the retirement system. This memo will discuss the use of an OCIO and what is necessary for a system to be compliant with Chapter 32 in the selection of an OCIO.

Currently, per statute, boards can invest fully with PRIM, partially with PRIM and partially on their own, or fully on their own. In cases where boards invest on their own, nearly all employ an investment consultant. If the Board is investing on their own, they must follow the provisions of G.L. c. 32, § 23 and §23B.

Section 23 of Chapter 32 Management of funds governs the investment of system assets. G.L. c. 32, §23(2)(b)(ii) states that “in investing funds the board shall employ an investment manager or investment managers who shall invest the funds of the system;”. G.L. c. 32, §23(2)(c) states:

**c) No investment of funds shall take place until the board has received from the commission an acknowledgement of receipt of the following: (i) certification that, in making the selection, the board has complied with the process established in section 23B; (ii) a copy of the vendor certification required under section 23B; (iii) copies of disclosure forms**



MEMORANDUM - Page Two

TO: All Retirement Boards  
FROM: John W. Parsons, Esq., Executive Director  
RE: Outsourced Chief Investment Officer (OCIO) Policy  
DATE: November 2, 2023

submitted by the selected vendor; (iv) a certification that the investment is not a prohibited investment as set forth in regulations of the commission; (v) if the board has retained a consultant, a copy of the consultant reports pertaining to the investment and the selected vendor; and (vii) a copy of the board certification required under section 23B. (Emphasis added).

This provision requires that when a board wishes to make an investment, they must comply with the procurement provisions of G.L. c. 32, § 23B. Section 23 also invests PERAC with the authority to withhold the acknowledgement if PERAC determines that the investment is not in the best interest of the retirement system. Section 23 (2)(c) provides:

The commission may withhold the acknowledgement if it determines that it is in the best interest of the retirement system; provided, however, that it must so notify the board within 10 days of receipt of completed documents as required by this section.

PERAC reviews all procurements to determine if the provisions of Section 23 and 23B have been complied with by the Board and if the investment is in the best interest of the system. Retirement Boards selecting an OCIO must comply with the provisions of Chapter 32, Section 23(2)(b), Section 23B and other relevant provisions of law and regulation, as well as meet the fiduciary duty set forth in Section 23(3) of Chapter 32.

**Two types of OCIO arrangements**

The Commission has determined that two types of OCIO arrangements can be in compliance with Chapter 32. For purposes of this memo we will refer to them as a “Proprietary OCIO” and a “Full OCIO”. In a Proprietary OCIO the OCIO has a set of funds that they control and in which they invest the assets of the retirement system based upon an agreed upon asset allocation and investment strategy. If a Proprietary OCIO recommends any investments outside of their own funds then a complete Section 23B search process must be completed. In a Full OCIO, the OCIO acts as an investment manager and does a due diligence search for other managers in which to invest the assets of the retirement system based upon an agreed upon asset allocation and investment strategy.

MEMORANDUM - Page Three

TO: All Retirement Boards  
FROM: John W. Parsons, Esq., Executive Director  
RE: Outsourced Chief Investment Officer (OCIO) Policy  
DATE: November 2, 2023

The process for selecting an OCIO and the requirements of the OCIO will be the same for both models. The procurement process to select an OCIO is the same as that for selecting an investment manager under Chapter 32.

**Limitations on the Use of an OCIO**

The Commission has determined that it is not in the best interest of retirement systems to allocate the entirety of their assets to a Full OCIO and has determined that systems that wish to use the Full OCIO model are limited to investing 10 percent of their assets with said OCIO. If the Boards are selecting a Proprietary OCIO then asset percentage restrictions are not applicable.

There are other specific requirements, in addition to the requirements specifically required under PERAC regulations and Chapter 32 Section 23B, that must be met if an OCIO is used by a Board.

1. All investment managers selected by the OCIO must be registered with either the Secretary of State or the SEC.
2. All contracts with the selected investment managers must be between the Board and the manager and not with the OCIO and must meet the requirements of Chapter 32 and any and all applicable PERAC regulations and policies.
3. All fee arrangements with the OCIO must be in compliance with Chapter 32 and must be based upon a flat fee and not a percentage of assets.
4. All investment managers selected by the OCIO must complete all of the required disclosures and compliance documentation as if they were selected directly by the retirement board following a section 23B search. All such information must be submitted to the Board and the Commission.
5. The Board must be apprised of all manager selections that the OCIO intends to make prior to the selection. The Board must adopt a policy, that will be included in the contract with the OCIO, detailing a process that will be followed which will allow the Board appropriate time to review manager selections and raise any objections.
6. The OCIO must submit to the Board and PERAC a detailed review of the due diligence process it follows in selecting, retaining and monitoring investing managers.
7. The OCIO must agree that it is a fiduciary with respect to the funds which are invested on behalf of the retirement board.
8. The OCIO must agree that it shall not be indemnified by the retirement board.

MEMORANDUM - Page Four

TO: All Retirement Boards  
FROM: John W. Parsons, Esq., Executive Director  
RE: Outsourced Chief Investment Officer (OCIO) Policy  
DATE: November 2, 2023

9. The OCIO is subject to all of the mandatory contract requirements and disclosures that are required by Chapter 32 and PERAC regulations and policies.

The retirement board shall assess each prospective Full OCIO's due diligence process and incorporate that assessment into the evaluation criteria used to select an OCIO. Such a process is as follows:

- (1) The OCIO process must be open in that new managers/funds can gain entry to the platform;
- (2) The evaluation criteria used by the OCIO as part of the selection, retention and monitoring process must be independent and objective;
- (3) The evaluation criteria that will be utilized in those circumstances by the OCIO must be clear and available to prospective investing managers; and
- (4) The evaluation of investing managers shall be based solely on those criteria.

**Memorandum 18 of 2014**

Memorandum 18 of 2014 is superseded with respect to the selection of Discretionary Managers, otherwise referred to herein as OCIO's, and otherwise remains in effect.