

How are investment options chosen for the Plan 3 and Deferred Compensation programs?

Objective

The Washington State Investment Board (WSIB) is responsible for establishing investment policy, developing participant investment options, and managing investment funds of the self-directed retirement and savings programs (RCW 43.33A.135). In carrying out that role, the WSIB seeks to offer a set of options that offer an opportunity for the majority of participants to achieve the plan goals: long-term financial and retirement security.

Investor behavior

In the course of selecting offerings for the self-directed retirement and savings programs, the WSIB reviewed research on investment behavior. Key conclusions that influenced the menu of options offered include:

- Too many options can cause confusion and lead participants to make uninformed investment decisions or to not participate in the program at all.
- Over 60% of the participants in a typical plan need or want investment help and less than 10% are active investors.
- The majority of participants will infrequently change or rebalance their investment allocation.
- The typical participant uses between three and four options.

The WSIB is also very aware there is no such thing as a neutral menu of options. Regardless of how the menu is designed, it will influence participant behavior. The WSIB strives to offer a simple set of options that influence behavior toward plan objectives.

Keep it simple

For the vast majority of participants, simpler is better because it makes it easier for participants to manage their investment portfolios.

Most members have neither the time nor the desire to manage their investments. They do not have experience managing investments, and they are not comfortable with the task. For them, there are “One-Step” investment options that are well diversified, rebalanced, and designed for the participant who wants to spend a minimal amount of time on their portfolio.

For those who want to be more actively involved in managing their portfolios, there is a “Build and Monitor” menu of options that allows participants to invest across the risk spectrum but is still limited enough to maintain ease of use.

Why are options limited?

Some members have expressed a desire to have additional options added.

These members would like to see more or different options. Some want lower-risk options (like Certificates of Deposit) and some want higher-risk options (including niche strategies like a green technology/biotech fund or a gold fund). When considering these requests, WSIB asks the following questions:

- Would it benefit the majority of plan members?
- Is it a basic building block required to build an appropriately diversified investment program?
- Does it serve some purpose that is not already served by an existing option?
- Is it liquid—would members be able to move their money in or out with little or no restriction?
- Is the appeal of the potential option long-term, or transitory and cyclical?
- Is it feasible for a program such as ours?
- If adding a new option would result in logistical challenges and/or higher fees, are the benefits compelling enough to justify the change?
- All studies show that increasing the number of options results in less beneficial outcomes for the majority of members because the program becomes more complex. Are the benefits of adding a new option worth the increased complexity?

If careful study shows that the answer to all of the above questions is “yes,” the WSIB will discuss with the Department of Retirement Systems and with the WSIB Board of Trustees whether such an option should be added. However, studies of member behavior have shown that continual change can be confusing and counterproductive so menu redesign should not be done too frequently.

The investment options in the Plan 3s and DCP may not satisfy everyone. Not every participant’s desire or request can or will be met. Participants’ needs for specific funds or focused investment strategies are best met through their own personal investments.

Conclusion

The self-directed investment options for the Plan 3s and DCP are carefully chosen to provide the best results for the majority of plan participants while keeping it as easy and straightforward as possible.