



*Dale R. Folwell, CPA*

## INVESTMENT MANAGEMENT

To: North Carolina Supplemental Retirement Board of Trustees

From: Loren de Mey, Assistant Investment Director

Date: June 3, 2019

Subject: Discussion / Action: NC 401k and 457b Plans - Watch List Recommendation

### **Background**

Galliard was founded in 1995 by John Caswell (retired in 2017), Rich Merriam and Karl Tourville. At its founding, Galliard was a wholly owned subsidiary of Norwest Bank, now Wells Fargo Bank, after the banks merged in 1998. Galliard had operated independently from Wells Fargo since its inception. Given this independence, the Founding Managing Partners implemented succession planning for their own and other key leadership roles.

### **Firm Update**

On April 5<sup>th</sup>, staff received notice from Galliard of several upcoming retirements of senior members of the firm including the following: Richard Merriam, Founding Managing Partner, retiring at the end of 2019; Carrie Callahan, Managing Partner and Head of Client Service, retiring at the end of 2019; Karl Tourville, Founding Managing Partner, President and Chairman of the Operating Committee, retiring in June 2020; and Leela Scattum, Partner and Chief Value Strategist, retiring by year-end 2020.

Andrew Owen, currently Executive Vice President of Wells Fargo Asset Management, will be joining Galliard as President and a member of the Executive Operating Committee. Andrew has served as Chairman of Galliard's Board of Directors since 2013. Additionally, on January 1, 2020, Galliard's Operational Risk Management, Compliance, and Technology teams will get a direct reporting line into centralized Wells Fargo's risk management and technology groups. Those teams will continue to remain at Galliard.

### **Succession Planning**

With the announcements of retirement dates for the senior executives named above, Galliard has started to implement its succession plan for the key roles. In order to facilitate continuity, the implementation will occur in phases. The main components of the succession plan include the following:

- Carrie Callahan's roles will be assumed by Mike Norman, Partner. Mike has been with Galliard since 1996 and currently serves as Chief Administrative Officer.
- Karl Tourville will be stepping down from the Board of Directors and as the Chair of the Executive Operating Committee at the end of 2019. He and Rich Merriam will remain as Advisors to Galliard through the end of 2022. Andrew Owen will essentially be taking over Karl Tourville's responsibilities as President.



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- Nick Gage, Principal, will be assuming Leela Scattum's role. Nick has been with Galliard since 2008 and has been working with Leela on strategy and contract issuer management during his tenure at Galliard. Nick is currently a member of the Executive Committee and Chairman Elect of the Stable Value Investment Association (SVIA).

### Main Concerns

1. **Potential for Additional Turnover** - Historically, Galliard was mainly operationally independent of Wells Fargo. Although Galliard had always been a fully owned subsidiary of Wells Fargo, the recent announcements will represent an organizational change for Galliard. Wells Fargo and Galliard had historically maintained a revenue sharing agreement. With the upcoming retirements of Richard Merriman and Karl Tourville, that agreement will sunset at the end of 2019.

With the partners now retiring and essentially being bought-out, Wells may now opt to retain 100% of the revenues beginning in January 2020. With the revenue share going away, Wells Fargo has started to work on structuring a bonus pool for key investment professionals. The firm is currently working out the details of how this plan will be structured and is still working on retention bonuses for key investment professionals and others at the firm. There is the potential risk for additional turnover given the compensation and bonus pool structuring details have not been finalized. However, Wells has indicated to Galliard that there will not be any material changes to compensation levels for staff for the next few years.

Additionally, other than Ajay Mirza (contracted through 2022), who is a Managing Partner and Chair of the Investment Committee, no additional investment staff are currently under employment contracts. We will look for additional steps by Galliard over the next several months to ensure that the remaining senior investment professionals are incentivized to stay.

2. **Changes in Operational Reporting Structure** - Galliard's compliance, risk and technology teams will get an additional reporting line up through Wells Fargo beginning in 2020. Given the increased regulatory environment, it was determined to have all subsidiaries report in through Wells. Although there had always been a dotted line reporting to Wells, Galliard was the only remaining subsidiary that did not have these groups fully reporting up through Wells. Staff and Callan will be monitoring how Wells manages these groups and any changes to the teams as they begin reporting up through Wells and not Galliard.
3. **Potential Impact to Firm Culture or Morale** - With Wells Fargo now taking a more active role in managing the Galliard subsidiary, there could be potential impact to the firm culture or morale. Staff and Callan will monitor any potential impact.

### Mitigating Factors

Although the announced changes to the firm are significant, there are several mitigating factors to the concerns above including the following:

1. Richard Merriam and Karl Tourville will stay on as advisors for several years. Galliard had prepared for Mr. Merriam's eventual retirement through promoting Brandon Kanz to Head of Credit two years ago and to Vice Chair of the Investment Committee. So while this may have



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been a surprise to investors, internally at Galliard and Wells they have been preparing for these retirements for several years.

2. Nick Gage has been serving as the de facto head of the Stable Value and contract team for several years as Leela Scattum has been transitioning her duties over time.
3. Galliard has exhibited a strong company culture and has been a stable organization over time.
4. As a member of Galliard's internal board of directors, Andrew Owen has served as an intermediary between Galliard and Wells Fargo since 2013. Additionally, he had also worked closely with Messrs. Merriam, Tourville, and Caswell as the CFO of Norwest upon the founding of Galliard, so he is well known to the Galliard team.

### Recommendation

Given the lack of clarity with Galliard's ability to retain and incentivize their investment team and the changes with Wells Fargo taking a more active role in the management of the firm, staff and Callan recommend placing Galliard on watch status until there is greater clarity on these issues and they are able to demonstrate that they can maintain stability at the firm.

Stable Value Fund: Total assets in NC 401(k)/457 Plans: \$2,076,445,357, representing 17.15% of total Plan assets (as of 4/30/19)

### Trailing Performance (net of fees, ending 4/30/19):

	YTD	1-YEAR	3-YEAR	5-YEAR	SINCE INC*
Galliard	0.74	2.32	2.12	2.01	2.27
3-yr Constant Maturity Tsy	0.80	2.64	1.89	1.53	1.15
US 3-month Tsy Bill Index + 150 bps	1.29	3.72	2.78	2.30	2.02

\*Galliard inception: December 1, 2010

### Calendar Year Performance

	2011	2012	2013	2014	2015	2016	2017	2018
Galliard	3.27	2.75	2.15	1.80	1.87	1.95	2.00	2.28
3-yr Constant Maturity Tsy	0.75	0.38	0.54	0.90	1.03	1.01	1.58	2.63
US 3-month Tsy Bill Index + 150 bps	1.61	1.62	1.58	1.55	1.56	1.84	2.38	3.41

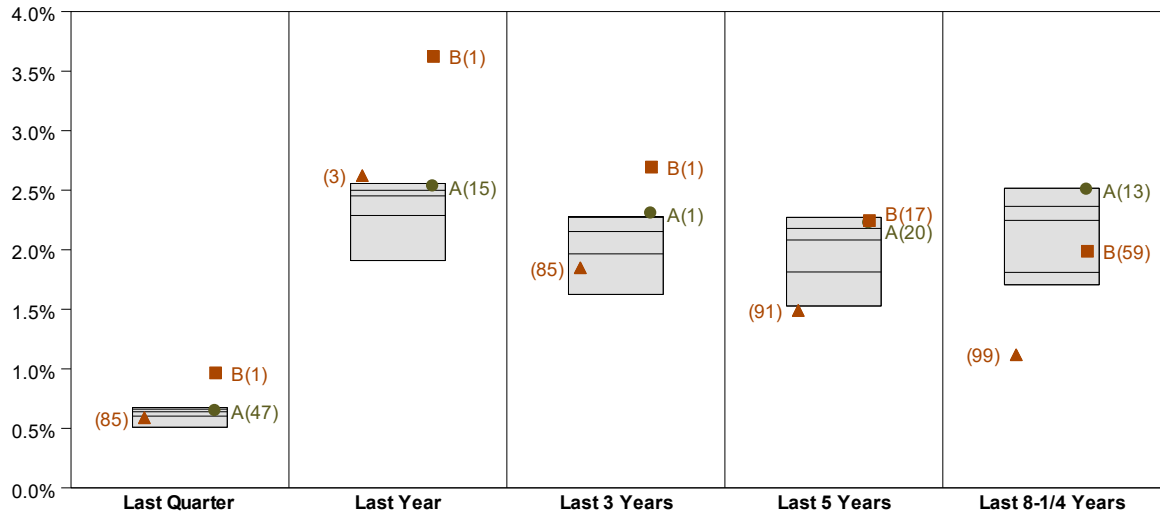


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### Performance Versus Peers (gross of fees, ending 3/31/19)

#### Performance vs Callan Stable Value SA (Gross)



	Last Quarter	Last Year	Last 3 Years	Last 5 Years	Last 8-1/4 Years
10th Percentile	0.67	2.56	2.28	2.27	2.52
25th Percentile	0.66	2.50	2.27	2.18	2.36
Median	0.64	2.45	2.15	2.08	2.25
75th Percentile	0.60	2.29	1.97	1.81	1.81
90th Percentile	0.51	1.91	1.62	1.53	1.71
Galliard Stable Value ● A	0.64	2.53	2.30	2.22	2.50
T-Bill + 1.5% ■ B	0.97	3.62	2.69	2.24	1.99
3 Yr Constant Maturity Yield ▲	0.59	2.62	1.85	1.49	1.12