

June 9, 2014

Mr. Keven M. O'Neill  
Deputy Secretary  
U.S. Securities and Exchange Commission  
100 F Street, NE  
Washington, D.C. 20549-1090

Re: Investment Company Advertising: Target Date Retirement  
Fund Names and Marketing (File No. S7-12-10)

Dear Mr. O'Neill:

State Farm Investment Management Corp. ("SFIMC") appreciates the opportunity to provide comments on the recommendations of the Securities and Exchange Commission's ("SEC's") Investment Advisory Committee (the "Committee") relating to the development of a risk-based glide path illustration<sup>1</sup> as requested in the SEC's release reopening the comment period (the "2014 Release")<sup>2</sup> on its proposal, *Investment Company Advertising: Target Date Retirement Fund Names and Marketing*, released in 2010 (the "2010 Proposal")<sup>3</sup>.

SFIMC is the investment adviser for the five State Farm LifePath Funds. The LifePath Funds are target date funds that are designed to reach their asset allocation landing point as of the target date in the fund name. Each LifePath Fund seeks to achieve that goal by investing all of its assets in a corresponding series of the Master Investment Portfolio, a registered management investment company, each with substantially similar investment objectives, strategies, and risks. BlackRock Fund Advisors, a subsidiary of BlackRock Institutional Trust Company, N.A., is the investment adviser to the Master Investment Portfolio. The State Farm LifePath Funds held \$6.0 billion in net assets as of March 31, 2014.

As discussed in more detail below, SFIMC believes that (1) the 'average investor' has a limited understanding of the traditional risk measures utilized in modern portfolio theory; (2) the consequences of a risk measure based on a standard methodology would go beyond the intended marketing application and into a target date fund's operational aspects; and (3) illustrated risk measures in marketing materials could lead to unrealistic investment return expectations.

**1. Limited understanding of industry risk-based metrics could mislead the average investor.**

In modern portfolio theory, there are many different risk-based statistics that can be used to describe asset classes, as well as a glide path for target date funds. However, it is the opinion of SFIMC that the 'average investor' has a limited understanding of these metrics, such as standard deviation, beta, covariance, and value at risk.

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<sup>1</sup> *Recommendation of the Investor Advisory Committee: Target Date Mutual Funds* (Apr. 11, 2013), available at <http://www.sec.gov/spotlight/investor-advisory-committee-2012/iac-recommendation-target-date-fund.pdf>.

<sup>2</sup> *Investment Company Advertising: Target Date Retirement Fund Names and Marketing*, SEC Release Nos. 33-9570; 34-71861; IC-31004 (April 3, 2014), 79 FR 19564 (April 9, 2014).

<sup>3</sup> *Investment Company Advertising: Target Date Retirement Fund Names and Marketing*, SEC Release Nos. 33-9126; 34-62300; IC-29301 (June 16, 2010), 75 FR 35920 (June 23, 2010).

Furthermore, given that these statistics are backward looking (typically over a 3-year time period), they historically have had limited predictive power and could potentially lead investors to improper conclusions about the absolute and/or relative risk of their investment.<sup>4</sup> Given the frequency of allocation changes among the underlying asset classes within a particular target date fund glide path, it should also be noted that any illustration using industry risk measures would need to be continuously updated to incorporate the most recent data to capture new relevant measures of risk.

To illustrate the point that a metric such as standard deviation could mislead investors, we compare the standard deviations of 3 different asset classes in their respective ‘pre-bubble’ 3-year period vs. their respective ‘post-bubble’ 3-year period. As the table below shows, across all 3 asset classes, the ‘post-bubble’ standard deviation was much greater than the standard deviation of the ‘pre-bubble’ period (right column):

**COMPARISON OF STANDARD DEVIATIONS: POST vs. PRE-BUBBLE**

Asset Class	Years used for Comparison	Pre-Bubble	Post-Bubble	Pre-Bubble	Post-Bubble	Post- vs. Pre-Bubble
		Total Return	Total Return	Standard Deviation	Standard Deviation	Standard Deviation
S&P 500 Index - Technology Sector	Pre (1999), Post (2001)	79%	-41%	31%	55%	1.7x
FTSE NAREIT Equity REITs	Pre (2006), Post (2008)	35%	-38%	13%	46%	3.7x
MSCI Emerging Markets	Pre (2005), Post (2008)	34%	-53%	20%	37%	1.9x

Source: Morningstar Direct

The significant difference between the pre- and post-bubble standard deviations highlights the limited value of risk-based metrics. This outcome illustrates the potentially prejudicial nature of such illustrated metrics that could unduly influence an investor despite the presence of any offsetting disclosure meant to temper the strength of the illustration.

Finally, it is the opinion of SFIMC that the ‘average investor’ has limited understanding of the normal distribution curve, such that 68.27% of observable outcomes fall within ± one standard deviation and that 95.45% of observable outcomes fall within ± two standard deviations from the mean. Moreover, the ‘average investor’ has limited understanding of how tail-risk events, such as the 2008 financial crisis, can materially and immediately impact the volatility of backward looking risk measurements, such as standard deviation.

Therefore, the inclusion of traditional industry risk measures in target date fund marketing materials has the potential to mislead investors about the future risks of their investment choices since (1) these risk measures are backward looking and (2) the range of outcomes can vary widely, even over short periods of time. As an alternative, and as a supplement to the asset class glide path graphical illustration the SEC previously proposed and which we support, SFIMC suggests an illustration that depicts the annual ‘best/worst’ year performance, which we believe could be understood by the ‘average investor’ and would illustrate the potential variability in fund returns.<sup>5</sup> For those funds with limited history, such as a target date 2060 fund, or funds with new asset classes, a pro-forma illustration could be constructed using the proposed asset allocation mix and historical asset class returns.

<sup>4</sup> Notwithstanding the limited predictive power of a risk-based metric, the underlying assumptions incorporating historical performance within traditional risk metrics indicate that a risk-based glide path requiring risk assessment disclosure of future fund holdings may not comply with SEC and FINRA rules prohibiting communications that predict or project performance. See SEC Rule 156(b)(2)(ii) and FINRA Rule 2210(d)(1)(F).

<sup>5</sup> This type of illustration would be similar in concept to the disclosure of a fund’s highest and lowest return for a quarter during the 10 years or other period shown on the bar chart and required to appear in the fund’s prospectus pursuant to Form N-1A, Item 4(b)(2)(ii).



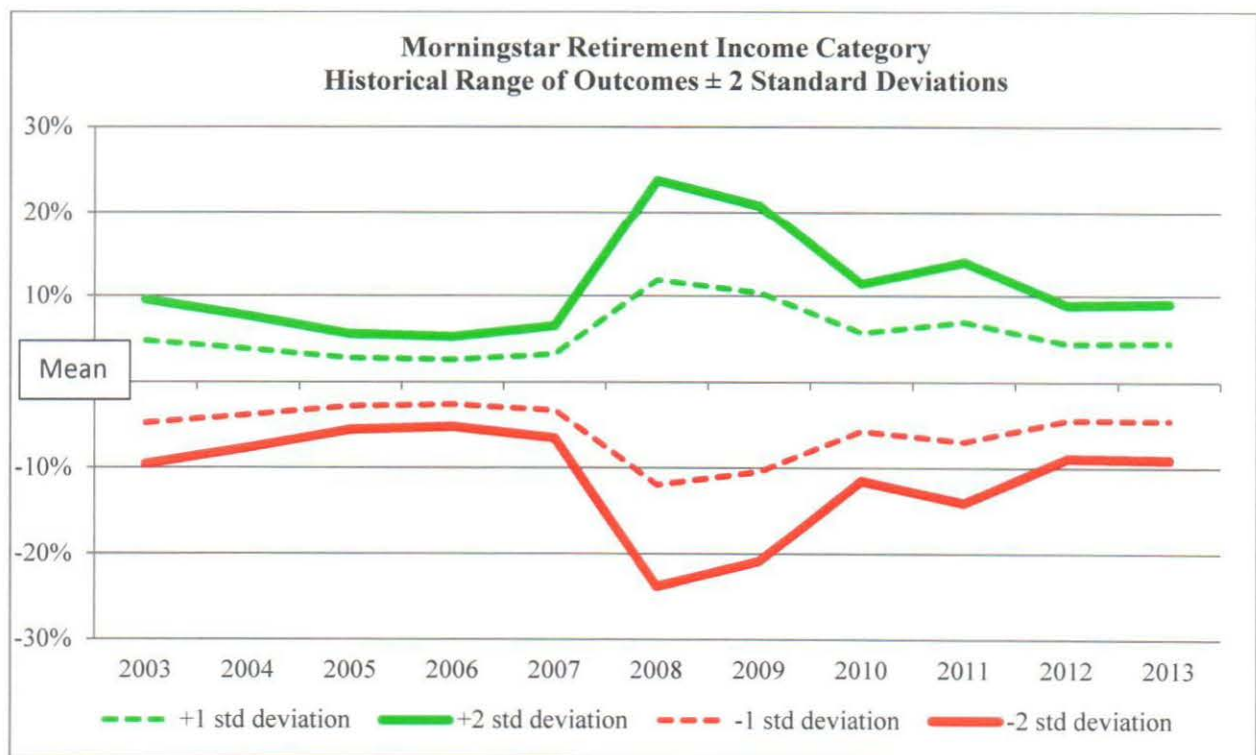
**2. A risk-based illustration based on a standardized methodology could stifle target date fund innovation.**

SFIMC believes that a risk measure based on a standardized methodology would unduly cause target date fund offerings to conform to the SEC-established risk standard. Fund offerings would become less differentiated, essentially stifling each firm's investment thesis or view of the economic environment. The standard methodology would thus reach far beyond just the intended marketing application and into the operational aspects of target date funds; a result the SEC may not have desired.

**3. Investors may have unrealistic investment return expectations based on illustrated risk measures and risk-based glide paths.**

It is the opinion of SFIMC that the majority of modern portfolio theory risk measures would confuse the 'average investor' and potentially create an improper expectation of risk and return since these risk measures are backward looking (typically over a 3-year time period) and are subject to significant volatility over time.

As illustrated in the table below, the standard deviation of the Morningstar Retirement Income Category varied significantly from 2003 to 2013. Specifically,  $\pm$  two standard deviations from the mean ranged from  $\pm$  5% in 2006 to  $\pm$  24% in 2008. Assuming an investor in the fund invested in the Morningstar Retirement Income Category in 2006 on the basis of a  $\pm$  5% two standard deviation expectation, the realized outcome just two years later in 2008 of an -18% annual total return for the Morningstar Retirement Income Category would likely have not been expected given the reported standard deviation risk measure that potentially could have been advertised at the time of initial purchase in 2006.



Source: Morningstar Direct

In addition, the creation of a universal, or standardized, definition of risk does not in and of itself limit risk. On the contrary, it may actually contribute to risk if investors misinterpret that the stated risk measures define the range of outcomes they could expect, rather than understanding that these risk measures represent only the range of outcomes historically observed over a defined time period.

SFIMC appreciates the opportunity to provide these comments. Please feel free to contact me if you should have any questions about this comment letter.

Sincerely,



A handwritten signature in black ink, appearing to read "Joe Monk", is written over a solid horizontal line. The signature is stylized and cursive.

Joe Monk  
Senior Vice President  
State Farm Investment Management Corp.