

**STATE OF HAWAII
DEFERRED COMPENSATION PLAN
BOARD OF TRUSTEES**

**OPEN SESSION MINUTES
MEETING # 403**

Date: August 2, 2016

Place: Department of Human Resources Development
14th Floor Merit Appeals Board Conference Room
235 South Beretania Street, State Office Tower
Honolulu, HI 96813

Present: Brian Moto, Chairperson
James Nishimoto, Ex-Officio Member (arrived at 9:45 a.m.)
Wesley Machida, Ex-Officio Member
Roderick Becker, Employee Member
Kanoë Margol, Employee Member

Others: Rodney J. Tam, Deputy Attorney General
Cynthia Akiyoshi, DHRD Staff
Jeanne Kanai, and Grace Baracao, Prudential Honolulu Office
Julie Klassen, Prudential Retirement
Carol Blumenthal, Deborah Baran, Prudential Retirement – via conference call
Glenn Ezard, Segal Rogerscasey

Absent: Kenneth Villabrille, Employee Member

Call to Order: There being a quorum present, Chairperson Brian Moto called the meeting to order at 9:07 a.m.

Agenda: The agenda for this meeting was filed with the Office of the Lieutenant Governor, as required by Hawaii Revised Statutes section 92-7.

Chairperson Moto welcomed everyone and started the meeting with introductions. He opened with an introduction of himself as the Board Chairperson and introductions of Board members, staff, and guests in attendance, followed by attendees participating via conference line. No other guests were in attendance.

Chairperson Moto proceeded to Agenda Item # 1.

Agenda
Item # 1:

New Business

a. Approval of Minutes Nos. 401, 401-ES, and 402

The Board took a few minutes to review Minutes Nos. 401, 401-ES, and 402 for the April 28, 2016 and May 13, 2016 meetings.

A motion was made by Trustee Becker and seconded by Trustee Margol to adopt Minutes Nos. 401, 401-ES, and 402 as presented. The motion passed unanimously.

b. JP Morgan's Notice to the Shareholders of the JP Morgan Diversified Real Return Fund Regarding Proxy Voting on Proposed Changes and Ratification of Chairperson's Decision on Submittal of Proxy Voting

Ms. Akiyoshi reported that a notice of a proxy voting to all shareholders was received from J.P. Morgan. The vote was for proposed changes that would allow J.P. Morgan to have more flexibility in its portfolio construction and would decrease the share price from 81 basis points to 76 basis points. As the changes affected the Fund, the Plan's consultant was contacted to provide his recommendations on the vote.

Mr. Ezard remarked that given the changes in the commodities over the past years, J.P. Morgan did not feel that they could meet their objectives. He added that it would remove the requirement to go into inflation hedging asset classes, and may cause J.P. Morgan to be less inflation hedged. Changes were in effect as of July 1, 2016. Although the changes do not go outside of the Board's Investment Policy, the change is that the focus is not on inflation hedging.

Ms. Akiyoshi added that the reason for raising and presenting this issue with the Chairperson was because of the deadline to respond to the proxy vote which was on June 21, 2016.

They will use the same benchmark but would use an additional benchmark as well. The benchmark doesn't change but its category would slightly differ and look like a global balanced strategy.

A motion was made by Trustee Margol and seconded by Trustee Machida to ratify the Chairperson's decision to submit the proxy vote in favor of J.P. Morgan's proposed changes to the J.P. Morgan Diversified Real Return Fund, based on the recommendations presented by Segal Rogerscasey. The motion passed unanimously.

c. Board's Delegation of Authority to Staff for Upcoming Proxy Voting on Proposed Changes within the Schroders Funds

Ms. Akiyoshi reported that Schroders informed her of an upcoming proxy notice to be sent to shareholders on proposed changes that would move the responsibility for the distribution, oversight, and administration to Hartford Funds. Hartford Funds would adopt 10 of the Schroders' existing mutual funds and be advised by Hartford Funds, sub-advised by Schroders, and renamed the Hartford Schroders Funds. Ms. Akiyoshi requested delegation of authority to staff to respond to the proxy vote in favor of the proposed changes. Mr. Ezard commented that there is no material change to the strategy and it is expected that the fees should decrease at some point due to the economies of scale.

A motion was made by Trustee Margol and seconded by Trustee Becker to delegate authority to the Board's staff to respond and submit a proxy vote on the upcoming proposed changes within the Schroders Funds. The motion passed unanimously.

Ms. Akiyoshi added that the changes to the naming convention will be coordinated with Prudential and communications will be prepared to notify participants.

Agenda

Item # 2:

Ongoing Business

a. Performance Evaluation Report by Segal Rogerscasey for First Quarter 2016, Period Ending March 31, 2016, including but not limited to:

- i. Overview of Funds Currently on the Watch List: MainStay Large Cap, Victory Institutional Diversified Stock Fund, and PIMCO Total Return Fund

Mr. Ezard presented some highlights of the First Quarter 2016, summarizing the reported on the assets in the individual funds, with the Stable Value Fund having the largest portion of the total Plan assets. He noted that the annual crediting rate for the Stable Value Fund, relative to other stable value plans, remains attractive.

Mr. Ezard provided an overview of the Second Quarter 2016 and some comments:

- Most asset classes were up during the Second Quarter. Foreign equities (developed markets) were down during the Second Quarter 2016; emerging markets saw a better performance.
- Towards the end of the quarter, the BREXIT vote resulted in Europe's and Japan's economies lagging.
- At the end of the quarter, especially in the U.K., there was a

drop in the equity markets but which reversed after, and now seeing the markets back to normal. Economy in the U.K. will be disrupted for a while going into new treaties and trade. May see an impact in two years and see EU growth be even slower.

- Through July, the returns have been up and generally positive.

The funds on the watch list:

- PIMCO continues to underperform. The RFP is out and this issue on the underperforming fund is being addressed by the Board. PIMCO has been undergoing significant changes in its management, and now is having a new CEO coming aboard, as of about 2 weeks ago, who has a history of re-structuring personnel.
- The J.P. Morgan Diversified Real Return fund had a surge in the returns, but looking at the risk metrics, it indicates that the Fund is taking greater risk than their peers and getting less return. The Plan has a significant weighting in this Diversified Real Return Fund. The Fund is not on the watch list but Segal is monitoring their volatility.
- Victory Institutional Diversified Stock Fund is trailing its benchmark for the quarter and the underperformance has been persistent. The Fund's assets have seen a decline, and Victory has made some staffing changes. The pattern of what has been happening present some concerns and the Board may need to make some decisions on this Fund.
- MainStay Large Cap Growth Fund has had a weak year-to-date performance. The Fund has had periods of good performance. The Fund is taking more risk than peers, and its volatility is a bit higher. Winslow Capital Management, the subadvisor, has been doing a good job lately in the stock selection and suggested giving more time to monitor this Fund.

b. Other Investment Fund Updates

i. Follow-up Report on U.S. Dept. of Labor's Investigation on the INVESCO ISTIF

Mr. Ezard summarized Invesco's report on the investigation by the U.S. Department of Labor on their ISTIF. The conclusion of the investigation noted that Invesco did not adequately make disclosures to investors, and made recommendations that Invesco make payments to its clients for lost income during the period.

ii. Follow-up Report on Request to Victory on Revenue Sharing

Ms. Akiyoshi provided a summary on the discovery of revenue sharing by the Victory Funds, the authorization given to Victory to begin revenue sharing payments that became effective in April 2016, and provided a review of the request made to Victory for retroactive revenue payments, including the formal follow-up letter of July 12, 2016 letter to Victory to ask Victory to consider their position on the retroactive payments.

The Board discussed Victory's non-response to the request and the current performance status of the Victory Fund, and agreed to go into Executive Session to confer with legal counsel on questions and options related to possible actions with respect to the Fund and the collection of the retroactive revenue sharing payments.

A motion was made by Trustee Nishimoto and seconded by Trustee Machida to move into Executive Session at 10:17 a.m. to confer with legal counsel on questions and issues pertaining to the Board's powers, duties, privileges, immunities, and liabilities with respect to addressing Victory's position on the revenue sharing payments. The motion passed unanimously.

All guests were excused, with the exception of the Plan's consultant and Ms. Klassen.

EXECUTIVE SESSION

Meeting

Reconvened: **A motion was made by Trustee Machida and seconded by Trustee Nishimoto to move out of Executive Session at 10:55 a.m. The motion passed unanimously.**

All guests rejoined the meeting. Chairperson Moto called a short break. The meeting resumed at 11:01 a.m., and continued with Agenda item 2.ii.

ii. Follow-up Report on Request to Victory on Revenue Sharing

Mr. Ezard stated that since the performance of the Victory Institutional Diversified Stock Fund has been underperforming for a while, he recommended that the Board consider exploring alternative options to replace the Fund.

A motion was made by Trustee Machida and seconded by Trustee Becker to begin the search process for alternative options to replace the Victory Institutional Diversified Stock

Fund, and allow Victory to rebid. The motion passed unanimously.

c. Plan Administrator's Report

i. Plan Report for the 2nd Quarter 2016

Ms. Klassen announced that the Plan will be receiving a Leadership Award at the upcoming NAGDCA conference, for the education of participants during the 2015 Benefits Fairs. The outreach events resulted in 48% of the attendees taking action at the Fairs during 2015.

Ms. Klassen provided a summary and highlights:

- The overall Plan participation rate:
 - The rate during the 2nd Quarter 2016, excluding DOE and UH, was at 47.33%.
 - The rate during the 2nd Quarter 2016, that includes all departments, was at 27.7%.
 - The rate for all actives was at 31%.
 - Active deferrals totaled 16,028 participants.
- Participant using the RIC reflected participants having beneficial results. The average participation is greater when using the RIC.
- The higher allocation to the Stable Value Fund is due to a maturing age group, especially over the ages of 55 years.
- From the deep dive analysis, the focus will be on those coming into the Plan and those newly coming into employment.
 - Future initiatives, such as quasi-enrollment, will be explored. Online enrollment does require indicative data which can be problematic for some plans.
 - More online tools to increase outreach, but will not lessen the focus for on one-on-one meetings.

Ms. Baran reported that they are working with DOE and UH on online videos to reach those employees who were starting State employment. As a way to reach the millennials, a video for DOE to use and an e-mail to introduce the Plan that would have links to Prudential's Educational Retirement counselors.

- The average account balance is \$73,752.00.
- Contribution rate increases have had good results and indicating that participants are taking right steps.
- Ms. Klassen and Ms. Baran provided highlights of the Benefits Fair in May 2016:
 - Attendance totaled over 1,000 employees.
 - Approximately 10% of the attendees took action.
 - Surveys went digital for the first time, eliminating the need for paper surveys. 61% did digital surveys.
 - The workshops on Plan topics were well attended.
 - Planning for the Benefits Fair on Kauai is in progress.
 - Working on posting workshop schedules and to be able to schedule appointments through the easy scheduler.
 - Over 90% of the surveys posted comments that the information has been of value.

d. Staff Administrative Report to the Board

Ms. Akiyoshi provided a summary of the ongoing monitoring and oversight of the Plan's administrative activities:

- Monitoring the activities on the HHSC transition to Kaiser and the vacation payouts that are pending outcome of the transition.
- N&K audit should be closing soon.
- Following up on the Victory revenue sharing matter.
- Worked with the Consultant on follow-up to clarify proposed changes raised in the J.P. Morgan and Schroders proxy voting.
- Monitoring of INVESCO's reports on the wrap provider rating changes.

Agenda

Item # 3: PTS Plan New Business

a. Approval on Amendments to PTS Plan Administrative Rules

Ms. Akiyoshi reported that the applicable sections of the Administrative Rules for the PTS Plan have been amended to expand the references to include and reflect the ability for counties to participate in the Plan. Preliminary review was completed by DAG Tam.

A motion was made by Trustee Nishimoto and seconded by Trustee Margol to approve the amendments to the PTS Plan Administrative Rules, as presented. The motion passed unanimously.

Agenda

Item # 4: PTS Plan Ongoing Business

- a. Approval of Report on Funds Not Deposited in the State/County Treasuries for the Period Ending March 31, 2016
- b. Quarterly Management Report for Period Ending March 31, 2016
- c. Effective Interest Rate Beginning July 1, 2016

Ms. Akiyoshi presented the Report on Funds Not Deposited in the State/County Treasuries for the period ending March 31, 2016, and the Quarterly Management Report for the period ending March 31, 2016. She announced that the effective rate for the current quarter beginning July 1, 2016 is at 2.70%.

A motion was made by Trustee Machida and seconded by Trustee Nishimoto to accept the Report on Funds Not Deposited in the State/County Treasuries for the period ending March 31, 2016. The motion passed unanimously.

- d. Status on County of Kauai's Transition to the PTS Plan

Item was not covered.

Agenda

Item # 5: Other Business/Announcements

- a. 2016 NAGDCA Conference

Chairperson Moto announced that 2 Board members and Board staff have expressed their availability and interest in attending 2016 NAGDCA conference, and asked that any other interested members inform Ms. Akiyoshi. The Board members and staff will be in attendance to also receive this year's conference Leadership Award that will be presented.

- b. Next Board Meeting

Ms. Akiyoshi stated that the upcoming Board meetings have been confirmed for September 14, 2016 and October 5, 2016.

Mr. Ezard also announced an educational summit that Segal Rogerscasey will be hosting in Arizona on October 19-22, 2016, for their clients that will cover Plan year highlights and an outlook for the future. Chairperson Moto asked that interested Board members let Board staff know.

Agenda

Item # 6: Status of RFP for an Active Cord Fixed Income Investment Option

A motion was made by Trustee Machida and seconded by Trustee Nishimoto to move into Executive Session at 11:42 a.m. to confer with legal counsel on procurement matters. The motion passed unanimously.

All guests were excused, with the exception of the Plan's consultant, Segal Rogerscasey.

EXECUTIVE SESSION

Meeting

Reconvened: **A motion was made by Trustee Machida and seconded by Trustee Nishimoto to move out of Executive Session at 11:50 a.m. The motion passed unanimously.**

All guests rejoined the meeting.

There was no other business.

A motion was made by Trustee Machida and seconded by Trustee Nishimoto to adjourn the meeting at 11:50 a.m. The motion passed unanimously.

(NOTE: Signed copy on file.)