

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

**OPEN SESSION MINUTES
MEETING # 404**

Date: September 14, 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 11:00 a.m.)
Wesley Machida, Ex-Officio Member
Kanoë Margol, Employee Member
Kalei Rapoza, Employee Member

Others: Rodney J. Tam, Deputy Attorney General
Cynthia Akiyoshi, DHRD Staff
Kevin Malmud, Jeanne Kanai, and Grace Baracao, Prudential Honolulu Office
Julie Klassen, Prudential Retirement
Glenn Ezard, Segal Rogerscasey
Wendy Young Carter, Segal Rogerscasey – via conference call
Patrice Sumikawa and Lawrence Chew, N&K CPAs

Absent: Roderick Becker, Employee Member
Kenneth Villabrille, Employee Member

Call to Order: There being a quorum present, Chairperson Brian Moto called the meeting to order at 9:06 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 introduced himself as the Board Chairperson. He noted that Trustees Becker and Villabrille are excused from today's meeting. He followed with introductions of Board members, staff, guests in attendance, and attendees participating via conference line.

Chairperson Moto proceeded to Agenda Item # 1.

Agenda

Item # 1: New Business

a. Welcome and Introduction of Incoming Trustee

Chairperson Moto officially welcomed a new incoming trustee to the Board from Hawaii Island, Kalei Rapoza, who joins today's meeting. A lei was presented to Trustee Rapoza. Trustee Rapoza provided a brief summary of his background, and stated that he currently works at the University of Hawaii Hilo in the Human Resources Department.

b. Approval of Minutes Nos. 403 and 403-ES

The Board took a few minutes to review Minutes Nos. 403 and 403-ES, for the August 2, 2016 meeting.

A motion was made by Trustee Machida and seconded by Trustee Margol to adopt Minutes Nos. 403 and 403-ES, as presented. The motion passed unanimously.

c. Presentation by N&K, CPAs and Approval of the Independent Audit Report for the Plan Year July 1, 2013 to June 30, 2014

Chairperson Moto thanked Mr. Lawrence Chew and Ms. Patrice Sumikawa for attending today's meeting to present the report prepared by N&K CPAs for the Plan Year July 1, 2013 to June 30, 2014, and for their service they have provided over the years. Mr. Chew introduced himself and stated that the auditor's report covers the first year after the transition of the Plan to Prudential Retirement from the prior Third Party Administrator, ING/VOYA.

Mr. Chew stated that the report provides a stated opinion that includes financial report and notes. There were no internal control findings and no material weaknesses were identified.

Mr. Chew noted under compliance findings there are provisions that need to be updated and amended within the Plan Document to conform with federal and State laws. DAG Tam added that staff is working with Prudential on revising the Plan Document. Mr. Chew added that the Administrative Rules also need to be updated and amended.

Mr. Chew and Ms. Sumikawa expressed that, with the assistance of Ms. Jeanne Kanai from Prudential, there were no difficulties in conducting the audit of Prudential's initial year in the administration of the Plan.

There were no further questions from the Board and the report was accepted with no objections.

Agenda

Item # 2: Ongoing Business

a. Performance Evaluation Report by Segal Rogerscasey for Second Quarter 2016, Period Ending June 30, 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 provided an overview of the Second Quarter 2016 and some commentary:

- The Second Quarter returns were positive.
- Drivers for the Second Quarter were mainly due to the conundrum by Federal Reserve in setting interest rates.
- Saw low yields on bonds, so both stocks and bonds were up.
- S&P 500 was up, so returns were good.
- The Russell 3000 was up at 3.5%; emerging markets had a strong recovery.
- Low volatility seen during the Second Quarter.

Overview of the Plan's assets as of June 30, 2016:

- Stable Value Fund still holds the largest portion of the Plan's assets.
- Expense ratios are generally under the median.
- LifeCycle portfolios tend to be a little higher but overall the weighted fees are still good.

The funds on the watch list:

- PIMCO continues to underperform relative to the benchmark and peers. Comparison on the 5-year universe is better, but is still under the index.
- The MainStay Large Cap Growth is still underperforming and 1-year period has been weak. He recommends giving MainStay more time to monitor any improvement and evaluate the performance consistency.
- Victory Institutional Diversified Stock Fund is underperforming relative to its peers and the benchmark. The

Fund has not recovered during the recent quarter and returns have been weak. The indicators reflect that their risk has been higher and their returns have been lower. The Board has decided to look for alternative options to replace the Fund through the competitive sealed proposal process.

Other comments:

- The J.P. Morgan Fund saw a significant rebound due to commodities performing well.
- The performance for the Schroder Emerging Market over the 1-year period has performed well compared to the benchmark due to weakening of the dollar against other currencies and anticipated easing of the monetary policy.

b. Other Investment Fund Updates

i. Discussion on Request to Victory for Revenue Sharing

Ms. Akiyoshi provided a background and summary of the events and the numerous discussions with Prudential and Victory on the discovery of the revenue sharing available from the Victory Funds, and Victory's position that they are not willing to provide retroactive revenue sharing.

A motion was made by Trustee Machida and seconded by Trustee Margol to move into Executive Session at 9:54 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 the request to Victory 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 Margol to move out of Executive Session at 10:33 a.m. The motion passed unanimously.**

All guests rejoined the meeting. Chairperson Moto called a short break. The meeting resumed at 10:36 a.m. There were no actions taken related to Agenda

item 2.b.i., and Chairperson Moto moved to Agenda item 2.c.ii.

c. Plan Administrator's Report

ii. Discussion on Policy Regarding the Handling of Gains and Losses Due to Processing Errors

DAG Tam explained the Board's current policy when an error that is caused by processing errors or delays which can result in a gain or loss to a participant. He stated that the Board's position is that the party that caused the loss situation is responsible for making the participant whole, and if there are any gains, the party that caused the error would not keep the gains. Those gains would instead go back to the Plan and be used for Plan expenses. This policy is based on the Board's position that participants should be placed in the same position they would have been in had the error not been made. The participant should not be any better or worse off due to the error. DAG Tam stated that the gains are held in a separate "Mr. Gains" account with Prudential.

Prudential has requested to revisit the current policy because they interpret their Master Agreement with the Board differently. Prudential believes that unintended gains should be used to offset the unintended losses. Prudential is requesting to establish and keep a separate bucket to hold any gains resulting from errors that are caused by Prudential. When the error is caused by Prudential and results in a loss Prudential, would use monies from that bucket or account to offset any of their losses. A separate account would be set-up in the Plan expense report to track gains and loss for errors not caused by Prudential (e.g., employers, participants).

The Board requested an executive summary from Prudential, and a proposal be prepared for discussion at a future meeting.

Chairperson Moto called for a lunch recess at 10:57 a.m. The meeting resumed at 11:43 a.m. Chairperson Moto stated that Agenda item 2.c.i was taken out of order and will be taken up now for discussion.

Meeting

Reconvened: c. Plan Administrator's Report

i. Plan Highlights

Ms. Klassen provided a summary of the Plan's assets and highlights as of August 31, 2016:

- The Plan assets total \$2.086 billion.
- The overall average participant account balance has increased to \$75,616.00.
- The inflows into the Plan are positive.

Mr. Malmud reported on the initiatives by the local office:

- Video that was produced for DOE and which will be presented at a later meeting.
- The local office will be participating in a joint labor-management meeting.
- Conducting mini fairs and the next one will be at the UH Hilo campus.
- Planning to do webinars for the National Retirement Security Week, along with a payroll message that will be on the October 20, 2016 pay statement and open house events.

d. Staff Administrative Report to the Board

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

- Overseeing various outreach projects: Development of a video for DOE employees along with a supplemental flyer which complements the video; a short video on Plan orientation for employees who are new hires or new enrollees; a video on the Plan Overview; and a video on pre-retirement for pre-retirees. Videos are being posted on DHRD website and the Island Savings Plan website.
- HHSC Transition to Kaiser where vacation payout requests were received are pending and on hold.
- N&K audit project has been completed.
- Vacation Payout Deferral issue with DLIR that has been outstanding since the initial memo in 2014, will resume with another follow-up memo to seek recovery of the amount of the loss to the reversal and redeposit action by the department.
- Discussions have been taking place with Victory and Prudential regarding the revenue sharing matter.
- For the Schroders proxy voting, still awaiting the proxies to come in.
- Preparations and coordination underway for the Semi-Annual meeting and Benefits Fair on Kauai.
- For the PTS Plan, an escrow account is set-up to cover the Plan's assets. An amended agreement is needed in order for LSW to add additional monies. Staff has been reviewing the amended agreement,

and the amendment has been executed.

- A conference call was held with County of Kauai to discuss the transitional activities necessary to add Kauai County PTS employees into the PTS Plan. The target rollout date for Kauai County to join the Plan is tentatively set for January 2017.
- The amendments to the Administrative Rules is moving along.

Agenda

Item # 3: PTS Plan Ongoing Business

- Approval of Report on Funds Not Deposited in the State/County Treasuries for the Period Ending June 30, 2016
- Quarterly Management Report for Period Ending June 30, 2016

Ms. Akiyoshi presented the Report on Funds Not Deposited in the State/County Treasuries for the period ending June 30, 2016, and the Quarterly Management Report for the period ending June 30, 2016.

A motion was made by Trustee Nishimoto and seconded by Trustee Margol to accept the Report on Funds Not Deposited in the State/County Treasuries for the period ending June 30, 2016. The motion passed unanimously.

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

Item was discussed earlier.

Agenda

Item # 4: Other Business/Announcements

- Upcoming Board Meetings

Ms. Akiyoshi stated that the next upcoming Board meetings are scheduled for October 5, 2016 and October 17, 2016.

- Fall Semi-Annual Meeting and Employees' Benefits Fair

As mentioned earlier, the Semi-Annual meeting will be held on October 31, 2016 and the Benefits Fair will follow on November 1, 2016.

Chairperson Moto thanked Prudential for the reports and highlights; Prudential was excused for the next agenda item.

Agenda

Item # 5: Status of RFP for an Active Cord Fixed Income Investment Option

A motion was made by Trustee Nishimoto and seconded by Trustee Margol to move into Executive Session at 12:04 p.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 1:18 p.m. The motion passed unanimously.

There was no other business.

A motion was made by Trustee Machida and seconded by Trustee Nishimoto to adjourn the meeting at 1:18 p.m. The motion passed unanimously.

(NOTE: Signed copy on file.)