

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

**OPEN SESSION MINUTES
MEETING # 430**

Date: April 16, 2019

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
Ryker Wada, Ex-Officio Member
Robert Yu, Ex-Officio Member (arrived at 9:09 a.m.)
Kalei Rapoza, Employee Member
Kalbert Young, Employee Member

Others: Christopher Leong, Deputy Attorney General
Cynthia Akiyoshi, DHRD Staff
Craig Chaikin and Wendy Carter, Segal Marco Advisors
Jeanne Kanai, Plan Administrator Staff (Prudential)/Honolulu Office
Grace Baracao, Plan Administrator Staff (Prudential)/Honolulu Office
Julie Klassen, Prudential Retirement
Kevin Malmud, Plan Administrator Staff (Prudential)/Honolulu Office – via
conference call
Carol Blumenthal and Deborah Baran, Prudential Retirement – via
conference call

Call to Order: There being a quorum present, Chairperson Brian Moto called the meeting to order at 9:01 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 proceeded with introductions. It is noted that no one from the public was in attendance to offer testimonies.

Agenda

Item # 1: Approval of Minutes No. 429 for the March 8, 2019 meeting

A motion was made by Trustee Young and seconded by Trustee Rapoza to adopt Minutes No. 429, as prepared. The motion passed unanimously.

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Item # 2: Discussion of the Board's Standing Committee on Operations and Adoption of the Resolution to Authorize the Committee's Responsibilities and Authorities

Chairperson Moto stated that a Standing Committee was established at the last Board meeting. The Committee consists of Trustees Young and Rapoza.

DAG Leong stated that a resolution outlining the Committee's proposed scope, responsibilities and authorities has been drafted and is in progress but is still under review.

Chairperson Moto stated that this item will be deferred until the next meeting to allow legal counsel and committee members to refine the draft. There were no objections to deferring this item.

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Item # 3: Discussion on the Planning and Scheduling of an Independent Plan Audit for the section 457(b) Plan for the Plan Year Ending June 30, 2019 or for the Plan Year Ending June 30, 2020

Ms. Akiyoshi reported that this discussion item is being presented in order to make some pre-planning arrangements for the next audit of the Plan.

Ms. Akiyoshi stated that:

- Prudential's first extension renewal will expire on June 30, 2021.
- When the Board discussed Prudential's first renewal extension, the Board expressed that more time is needed in advance of the expiration period to discuss the options to either extend the renewal period or consider a TPA solicitation.
- The question before the Board is whether the Board would like to have the audit reports available when the Board discusses Prudential's next extension renewal.
- The last audit was for the Plan Year ending June 30, 2017 and the report was presented at the September 2018 meeting.
- Plan audits have been conducted every three years, so the next planned audit would be for the Plan Year ending June 30, 2020 and the report presented in 2021.
- A discussion would need to start during the second half of 2020 on Prudential's next extension renewal or to consider a TPA solicitation. The next extension renewal would be for a two-year period that would begin on July 1, 2021.

Ms. Akiyoshi presented two options:

- Option to conduct an audit for the period ending June 30, 2019, if the Board foresees needing a report to evaluate Prudential's second additional two-year renewal period. This audit report would be completed in 2020.
- Or, the option to conduct an audit for the period June 30, 2020. This audit report would likely be completed and presented in 2021 but may not be in time for the discussion on Prudential's contract. The audit, however, would coincide with the regular timeframe of the audit schedule.

Ms. Akiyoshi stated that the cost of the audit expenses is covered under the TPA's contract agreement. The Board stated its preference for an audit for the Plan Year ending June 30, 2019, in time for the evaluation of Prudential's next renewal period. Ms. Akiyoshi noted that this item will be placed on the upcoming Board meeting agenda for the Board's action.

Chairperson Moto proceeded to Agenda item #4.

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Item # 4:

Annual Deep Dive Plan Analysis by Segal Marco Advisors

Ms. Carter stated that the focus of this analysis is on creating retirement income within voluntary savings plans along with an overview of the legal and regulatory updates. She commented that one of her observations at the Benefits Fair is that employees appear to have little awareness about managing their monies once they reach retirement.

For the legal and regulatory updates:

- One take-away is that Congress appears to be interested in retirement security but has not been unified in accomplishing a lot. Momentum is growing so will expect to see more in future.
- The Bipartisan Budget Act of 2018 did result in some changes to the hardship withdrawal rules. Most changes do not apply to the Plan. Ms. Klassen added that the practice within the Plan is to stop contributions when applying for hardship reasons. They are looking at general standards for defining financial hardships.
- Student loan debt is an increasing financial burden. Private letter rulings (PLR) were issued related to student loan repayments in response to written requests. The PLR does not have authority beyond the company that made the request. Ms. Klassen added that information on a student loan assistance is available on the financial wellness platform and Prudential is able to offer additional advisory services should the Board desire.

- The proposed Secure Act which would affect IRAs and automatic enrollment features did not pass.

Commentary on creating retirement income:

- The concerns and challenges for retirees are on spending down and making the savings last for their entire lifetime.
- The rate of employees reaching age 65 years will increase every day until year 2030. Hawaii is number 1 in terms of longevity. 20% of people living in Hawaii are retiring earlier than expected but 80% of those retiring early are doing so because of health care and family issues.
- With inflation, those who retire will lose 50% of purchasing power over 30 years.
- Other challenges, there are many retirees who:
 - Are working during retirement and overestimate income from post retirement employment;
 - Neglect to run the numbers. They may have access to the information but do not necessarily use the information.
 - Are not maximizing social security benefits. The many strategies can be overwhelming to choose from. 75% of retirees will claim benefits within 3 months of turning 62 years of age.
- Observations on general participant behaviors:
 - Many under select annuities and do not set up income streams.
 - Millennials are more interested in selecting annuities than preceding generations.
 - Are not utilizing employer-provided educational resources.

Some ways that retirement plans can raise participants' awareness on the importance of retirement savings are the use of retirement income statements that includes the defined benefit and defined contribution projected incomes but it would be a big data undertaking and there are logistical concerns on sharing of confidential information; holding Benefits Fairs to promote the benefits of the retirement plans; and use of the Plan's Retirement Income calculator that is available on the Plan website to input their defined benefit monthly income to estimate monthly projected retirement benefit incomes.

Some impediments to retirement and variety of retirement plan risks are:

- longevity risks and outliving retirement savings; and
- conversion risks and knowing how to take their monies and turning it into supplemental income.

Ms. Klassen commented that Prudential would make sure that assistance is provided to employees to address such issues. Prudential is looking at and

utilizing various resources that will engage participants so as to reduce some of the confusion. Ms. Carter added that the educational efforts and resources that are being provided are to help participants overcome their inertia.

- Surveys have shown that those who prefer annuities believe they may live a long time and gives them piece of mind.
- There is a consensus that participants need help to create an income stream. 60% of men and 43% of women have not seen a retirement income projection.
- Annuity usage for section 457 plans is generally low. Other solutions are QLACs which is buying a deferred annuity to protect at the tail-end of the spend down period. This has shown little uptake because few people will give \$50,000 for use and to get an income stream later at age 85 years. There has been little traction on this option.
- Retirement income solutions have benefits to protect when drawing down but there are also consequences in terms of fiduciary liability. The SECURE Act provides portability for the accumulated benefits to be moved and provides for some relief and provides for minimal protection for Plan fiduciaries.
- Guaranteed income products include traditional annuities such as those available through the Plan's annuity shopping service, QLACs, and guaranteed minimum withdrawal benefits such as in-plan offerings or a component of the plan.

Mr. Chaikin added that for this Plan, developing a consistent retirement income stream may be less of a priority since employees do have a defined benefit plan that already provides a base level of a guaranteed income stream upon retirement along with social security.

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Item # 5: Follow-up Discussion on the Design of the Investment Menu Line-up Structure

Mr. Chaikin presented follow-up information from the last meeting related to the investment line-up structure, and the potential cost impact for the alternatives, if using the existing investment line-up:

- Alternative #1 and #2 have similar structures with stand-alone investment options. Alternatives #3 and #4 use a fund-of-funds or white label fund approach.
- The move from the LifeCycle portfolios to the Vanguard Target Retirement series on April 2, 2019, did decrease the expense ratios, from an overall weighted average of 31 basis points resulting in approximately \$7.4 million in total estimated investment costs to 29 basis points with the

change to the new Vanguard funds. The change resulted in savings of about \$450,000.

- Alternative #1 would streamline the core line-up and would result in a projected cost of 26 basis points. This alternative proposes to:
 - eliminate and move assets from the SSGA Real Asset fund and the Vanguard Wellington fund to the Vanguard Target Date funds;
 - eliminate and move assets from the Hartford Schroder Emerging market fund and the MFS International Value fund to the American Funds EuroPacific Growth fund;
 - eliminate the Harbor Small Cap Value fund and the William Blair Small/Mid Cap Growth fund to an added active Small/Mid Core fund.
- Alternative #2 would eliminate growth and value core funds in large cap asset class and growth and value core funds in SMID cap asset class and would move \$344 million in assets from the S&P 500 index fund to the MainStay Large Cap Growth fund and to the Wellington Research Value fund. The core funds would be mapped 50% to growth and 50% to value funds.

Mr. Chaikin provided some investment options structure line-up comparisons with other plans. Since, the Board previously discussed looking at possibly reducing the number of options, the alternatives are for consideration for the Board in lieu of adding additional asset classes.

There were no other questions. Chairperson Moto proceeded to Agenda item #6.

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Item # 6:

Discussion on a Proposal to Establish an Alternative Competitive Bidding Process for Plan-related Investment Product Searches and Potential Action Thereon

Mr. Chaikin summarized that legal counsel had concurred that the Board could move away from the State's procurement process for selecting investment options in the Plan, and the Board made a decision to establish a competitive bidding process that would be handled by the investment consultant. Discussions to develop a separate competitive bidding process were held with legal counsel and Board staff. Mr. Chaikin reviewed the flowchart of the proposed competitive bidding process:

- The Board, along with the investment consultant, determines a need for a new investment product. The investment consultant would propose the minimum criteria and qualifications.
- A notice is posted on the NAGDCA website for public viewing.
- This process would allow investment companies to contact the investment consultant and ask to be considered for selection. Segal would reach out

to the companies for data, and then Segal would provide an analytical report to the Board with basic information on all companies that had expressed interest.

- The investment consultant identifies five potential product providers. The Board holds interviews with at least two product providers to discuss the offer and makes a selection. Finalists would be asked to bring their best and final offer.
- The award would be made to the selected product provider.

Trustee Rapoza commented that he realized from the past competitive searches that were conducted and the amount of information that was provided for Board members' review that Segal has more exposure and knowledge of the interested investment companies than Board members. He feels that the Board contracted with the investment consultant to rely on their expertise. Based on their knowledge and the criteria used by the Board in past searches, this would streamline the search and evaluation process and serve as guidance in handling the competitive bidding process. Mr. Chaikin added that for this proposed process, there were some steps from the State Procurement process that were retained.

DAG Leong remarked that the Board is empowered to develop a process on a statutory level, under chapter 88E-9, HRS, through a competitive bidding process based on the specifications and consideration deemed appropriate by the Board, and therefore, would not need to go through the normal procurement process. Mr. Chaikin added that in most states, the state procurement process is not set up for procuring investment products.

A motion was made by Trustee Yu and seconded by Trustee Wada to adopt the proposed alternate competitive bidding process for conducting investment product searches in lieu of using the State procurement process, under Chapter 103-D, HRS, and where all investment searches will be handled by the Plan's investment consultant for the Board's consideration.

Discussion: The Board discussed and agreed that the Board will not be formally scoring offerors' proposals in the proposed investment search evaluation process, as has been done in past search processes. The selection would be based on the Board's discussion.

The motion passed unanimously.

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Item # 7:

Investment Fund Updates and Performance Review by Segal Marco Advisors, including but not limited to:

- a. Discussion on Subadvisor IGT Manager Changes by INVESCO to the

- Stable Value Portfolios and Potential Action Thereon
- b. Status on the Transition and Launch of the Vanguard Target Date Retirement Series

Mr. Chaikin provided comments on the First Quarter 2019, which was a good quarter for equities in the marketplace. The Federal Reserve did not raise rates, and this was received favorably.

For the transition to the Vanguard Target Date Retirement funds, the transition took place on April 2, 2019. Prudential did provide reconciliation of the fund transfers. Ms. Akiyoshi added that the amount of assets transferred to the Vanguard Target Date Retirement funds totaled \$130,448,125.97.

Mr. Chaikin reported on fund updates:

- INVESCO announced changes to the subadvisor IGT managers. INVESCO notified BlackRock of the plans to terminate and the replace the BlackRock Intermediate and core portfolios. Within the Stable Value Fund, the allocation to BlackRock intermediate mandates is 6.7%, and 8.87% to core mandates. INVESCO has the discretion to make selection of their underlying managers. INVESCO expressed concerns on BlackRock's ability to add strong risk-adjusted returns going forward. Loomis Sayles has a deep fixed income team and will assume responsibility in May 2019. Segal does not have any concerns with the change.

There were no objections to INVESCO's changes by the Board.

- The performance of the managers was good. Wellington Research Value fund outperformed the benchmark and performance was positive at 12.5% versus the benchmark at 11.9%.

Mr. Chaikin stated that Segal does not have changes at this time and recommends keeping the Wellington Research Value fund on the watch list.

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Item # 8: Notification on New Interest Rates for the PTS Plan, Effective January 1, 2019 and April 1, 2019

Ms. Akiyoshi reported that the interest crediting rate effective January 1, 2019 was 2.61%. The interest rate effective April 1, 2019 will also be 2.61%. The rates have remained status quo over the past year.

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Item # 9: Staff Administrative Report

Ms. Akiyoshi provided some brief highlights of the monthly activities:

- Worked with the members of the Operations committee that was established at the March 8, 2019 meeting, to discuss the scope, responsibilities and authorities.
- As a result of the transition to the Vanguard Target Retirement funds, worked with legal counsel on amendments to Prudential's TPA service and trust agreements related to the removal of the responsibilities involving the custody of the LifeCycle portfolios.
- Worked with legal counsel to prepare testimonies for the Board's legislative initiatives related to the addition of the Roth option and the establishment of a second support position for the Board.
- Continuing to track the Plan-related expenses, pending the appointment of new sub-committee members.
- Worked with Prudential on the transition of the LifeCycle portfolios to the new Vanguard Target Date funds, including review of Prudential's authorization forms to make the changes on Prudential's platform, fund change announcements, updates to the contents in the written materials and website, and article for the quarterly newsletter.
- Worked with Prudential on the development of communications for a new Go-Green initiative to encourage employees move to e-delivery and receive communications electronically.
- Worked with Prudential on subsequent written communications via emails and mailers for the Financial Wellness campaign.
- Working with Prudential on planning preparations for the upcoming Spring Employees' Benefits Fair and Semi-Annual meeting.

Ms. Akiyoshi added that there are some HawaiiPay situations related to pay and employment transfers that are affecting participant accounts, so these issues are being researched and addressed. Ms. Blumenthal stated that there are a few payroll deferral and vacation payout deferral issues that have occurred when employees have transferred between departments. Contributions are not coming over with the transfers. They are having ongoing discussions with ETS.

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Item # 10: Other Business/Announcements

- a. Review of Bills for 2019 Legislative Session
 - i. HB 1007, SD1, Relating to Adding the Roth Option

The latest version of the bill shows the amendments that were made and has been moving. Testimonies were prepared and have been

submitted to support the bill. Trustee Wada noted that a request was made to the WAM chair for inclusion on a last-minute hearing agenda to keep the bill alive. He added that the bill would just give the State the ability to create the option for inclusion in the Plan.

- ii. HB 1344, HD1, SD1, Relating to DHRD Operating Budget
Trustee Wada stated that this has been sent to the Governor and is now Act 005. The DHRD is waiting on further guidance on funding but could begin making arrangements to recruit and fill the support position for the Board and Plan.

b. 2019 Annual NAGDCA Conference

Ms. Akiyoshi stated that the 2019 NAGDCA conference will be held on September 8 through 11, 2019, in New Orleans, Louisiana. The Board has established that the NAGDCA conference provides excellent education for the Board as it is specific to section 457 plans. Agenda for the conference has been provided.

A motion was made by Trustee Rapoza and seconded by Trustee Yu to authorize travel for interested Trustees and Board staff members to attend this year's NAGDCA conference on September 8-11, 2019.

Discussion: DAG Leong added that he will check on sunshine law provisions for board members travelling to attend such events outside of the public meetings.

The motion passed unanimously.

c. Upcoming Scheduled Meetings and Events for 2019

Ms. Akiyoshi stated that the next Board meeting is the Semi-Annual meeting that is scheduled for May 30, 2019. The Benefits Fair will be held at the Oahu Veteran Center on May 29, 2019.

There was no other business. Chairperson Moto thanked everyone for attending today's meeting and adjourned the meeting at 11:20 a.m.

(NOTE: Signed copy on file.)