

**DRAFT – PENDING BOARD APPROVAL**  
**STATE OF HAWAII**  
**DEFERRED COMPENSATION PLAN**  
**BOARD OF TRUSTEES**

**OPEN SESSION MINUTES**  
**MEETING # 434**

Date: February 7, 2020

Place: Department of Human Resources Development  
14<sup>th</sup> 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  
Kalbert Young, Employee Member  
Kalei Rapoza, Employee Member

Others: Pat Ohara, Deputy Attorney General  
Cynthia Akiyoshi, DHRD Staff  
Craig Chaikin, Segal Marco Advisors  
Kevin Malmud, Plan Administrator Staff (Prudential)/Honolulu Office  
Jeanne Kanai, Plan Administrator Staff (Prudential)/Honolulu Office  
Grace Baracao, Plan Administrator Staff (Prudential)/Honolulu Office  
Peter Eddy, Prudential Retirement  
Kapena Kim, Prudential Retirement  
Tom Kalili, Prudential Retirement  
Al Lee, Prudential Retirement  
Julie Klassen, Prudential Retirement  
Carol Blumenthal and Deborah Baran, Prudential Retirement – via  
conference call  
Wendy Carter, Segal Marco Advisors – via conference call

Absent: Randall Nishiyama, Deputy Attorney General

Call to Order: There being a quorum present, Chairperson Brian Moto called the meeting to order at 9:03 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. He noted that DAG Pat Ohara is representing DAG Randall Nishiyama who is

excused from today's meeting. Chairperson Moto stated that no one from the public was in attendance to offer testimonies.

Agenda

Item # 1: Approval of Minutes No. 433 for the October 28, 2019 meeting

**A motion was made by Trustee Wada and seconded by Trustee Rapoza to adopt Minutes No. 433, as prepared. The motion passed unanimously.**

Agenda

Item # 2: Discussion and Consideration on the Renewal of the Agreement for Investment Consulting Services with Segal Marco Advisors for an Additional 5-Year Period, upon the expiration date of June 30, 2020, and Potential Action Thereon

Chairperson Moto summarized that Segal's contract for the first five (5) year period will expire on June 30, 2020. Segal has prepared a letter for the Board's review and consideration on the extension of their agreement for an additional five-year period. Chairperson Moto stated that this next renewal period would be for the period July 1, 2020 to June 30, 2025. There is a last renewal period in their agreement which would be for the period July 1, 2025 to June 30, 2027, for an additional two years. The recommendation is to extend the current agreement with Segal Marco Advisors for the next additional 5-year period.

In response to Trustee Young's question on the fees for the next renewal period compare to the current fees, Ms. Akiyoshi stated the current annual fees are \$81,500.00, and the annual fees for the next renewal period would be \$90,000.00. She added that when the Board evaluated Segal's written proposal that was submitted during the 2015 investment consultant search and scoring of the finalists, the Board based its selection on Segal's bid for the total twelve (12) year period which was the lowest.

**A motion was made by Trustee Young and seconded by Trustee Yu to accept Segal's letter of interest and to extend their contract agreement for the next additional five-year period, from July 1, 2020 to June 30, 2025. The motion passed unanimously.**

Agenda

Item # 3: Discussion on the Authorization to Fund the New Position to Staff the Board, and Potential Action Thereon

Ms. Akiyoshi reported that DHRD has established a new position that would provide administrative support and be dedicated to the Board. The recruitment is ready to be initiated upon receipt of funds for the position. A Bill for Collection from DHRD is for the Board's consideration in the amount of \$43,180.00 which

includes the fringe benefit rate in accordance with the Department of Budget & Finance's memo. The anticipated funding amount is for the remainder of fiscal year 2020 and is for a Human Resources Specialist IV level which is the authorized funding level that DHRD initially proposed to the Board. Recruitment may be at a lower level to allow for growth potential. Any excess funds not expended will be returned to the Plan. Ms. Akiyoshi added that she is continuing to track the expenses in the Plan Budget & Expense Account and there are sufficient funds available in the Plan Expense Account to cover the funding of the position.

**A motion was made by Trustee Young and seconded by Trustee Yu to approve the payment of the funding to DHRD, for the special funded position, from the assets of the Plan in the amount of \$43,180.00 for the remainder of Fiscal Year 2020. The motion passed unanimously.**

#### Agenda

##### Item # 4: Status on the Established Process for an Alternate Competitive Bidding Process for Plan-related Investment Product Searches

Ms. Akiyoshi summarized that the Board adopted an alternate competitive bidding process at the August 5, 2019 meeting based on some best practices in the industry, which would be used in lieu of following the State Procurement Office process. A flowchart on the process was presented earlier and the process was finalized into a written formal process policy document which is for the Board's reference.

DAG Ohara added that procurement of investments is exempt from the State Procurement Office process, so agencies that are exempt may choose to follow the State procurement because they like the structure but not necessarily use everything from the State's process. At the ERS, for the investments they choose, they have used their own process, while for some other procurements they have followed the State procurement process.

Trustee Yu asked for clarification on whether underlying changes in the investment fund that is a family of funds would warrant a search. Mr. Chaikin responded that he may or may not recommend a search, and that it would be dependent on the underlying change and the impact of a fundamental change on the fund.

#### Agenda

##### Item # 5: Discussion on the Proposed Timeline to Add the Roth 457 option to the Plan

Ms. Akiyoshi provided an overview on the features of Roth option, and a proposed timeline on the actions steps to implement and add the Roth option to the Plan:

- Discussions on the Roth features were held with Melanie Walker from Segal Marco Advisors, Mr. Chaikin, and DAG Nishiyama in November 2019 and in January 2020.
- Various resources were reviewed such as the IRS guidelines, NAGDCA brochure on the features of the Roth option, information and references from Prudential and other states.
- Some required amendments would include adding the post-tax contributions; and adding provisions that include establishing a Designated Roth Account, ensuring that contributions to the Designated Roth account are irrevocable, and that the total combined contributions of pre-tax and Roth deferrals cannot exceed the total annual contributions limit for 457(b) plans.
- Some proposed recommendations for the Board's consideration are to permit in-plan rollovers to the Designated Roth account, limit the in-plan rollovers to the Designated Roth account only upon a distributable event, and to not permit unforeseeable emergency distributions from the Designated Roth account since this type of distribution is not a qualified distribution under the Code.
- The current sub-accounts that are on Prudential's platform where rollovers are held in separate accounts include:
  - Pre-tax 457 account;
  - Non-457 rollover account;
  - ERS rollover account; and
  - Other 457(b) rollover account.
- Participant users that potentially would defer to the Designated Roth account could be:
  - Active participants electing to make payroll contributions to the Designated Roth account;
  - Active participants who may have rollover monies in the Plan from other outside qualified plans;
  - Terminated participants who do not have the age requirements to take distributions from their outside qualified plans; and
  - Terminated participants who meet age requirements to take distributions from their outside qualified plans.
- Rollover contributions to the Designated Roth account would be irrevocable, same as the payroll contributions.
- The incoming payroll contributions to the Plan for the pre-tax and the Roth 457(b) would be directed to the same investment options.

Mr. Malmud stated that he is aware of many plans that have start with limited provisions in the beginning, as the Roth options have a significant tax consideration. Mr. Chaikin commented that this is an important point that taxes on the rollover amount cannot come out of the rollover money. He added that the utilization of in-plan rollovers among the plans has been low.

Ms. Blumenthal commented that Prudential has surveyed the payroll jurisdictions, specifically the counties and they have responded to say that they would be able to add the Roth deductions to the payroll system and able to combine and track the pre-tax and Roth maximum contribution limits. In addition, they can format their data files to add the Roth deduction.

Ms. Akiyoshi reviewed the proposed timeline that includes the design phase to discuss the Roth features with the investment consultant and legal counsel; the development phase to discuss the program and system capabilities with the investment consultant, legal counsel, TPA and other affected agencies, in order to draft the necessary amendments to the Administrative Rules; and the rule-making phase in which the draft Administrative Rules would be sent through the required rule-making process steps and up to the Governor for approval of the final amendments sometime towards the end of 2021, with the education and rollout of the Roth option in the first part of 2022.

Ms. Akiyoshi explained that the proposed recommendations would be to keep the amendments and implementation as simple as possible as the amendments would need to go through the rule-making process, and to have a less complex structure that would avoid delays for the proposed implementation timeline. The proposed recommendations are in consideration of potential problems that could arise from miscommunications and payroll issues.

Trustee Wada stated that he has been giving the Governor updates on the decisions to add the Roth option to the Plan, as part of the Administration package during the 2019 legislative session, and will be giving updates on timelines for the amendments that will need to be made to the Administrative Rules.

Ms. Akiyoshi noted that this topic will be continued at the next meeting to allow time for the Board to review and consider the information and recommendations presented.

#### Agenda

##### Item # 6:

#### Plan Administrator's Report

##### a. Plan Highlights for the Fourth Quarter 2019

Ms. Klassen provided highlights on the enactment of the SECURE Act and for the Fourth Quarter:

- President Trump signed the SECURE Act which:
  - Moved the Required Minimum Distributions age from 70½ to 72 years old which is effective in 2020. In general, most participants are not waiting until the required minimum age to take the required amount and are taking more than the minimum, but for those who are taking the required RMD amounts it would affect them as people are living longer;

- Provides a provision for penalty-free withdrawals up to \$5,000 in the case of birth or adoption of a child;
- Prudential is seeking guidance from the IRS in terms of plan amendments that would be required;
- Provides a provision that would reduce the minimum age to allow in-service withdrawal requirements to 59½ if they are still working;
- Addresses Life-time income disclosures which Prudential currently is doing. Prudential is seeking guidance on to determine any further disclosures; and
- Addresses draw-downs for designated non-spousal beneficiaries, with some exceptions.

Ms. Klassen reported on the cash flows within the Plan: of the \$375,809,794 allocation which is comprised of the Vanguard Institutional Target Retirement funds, State Street Real Asset fund, and the Vanguard Wellington fund, approximately \$150 million represents the Vanguard Institutional Target Retirement funds; Goalmaker has about \$257 million; and the managed accounts are close to \$150 million. The total assets in the Plan through December 2019 total approximately \$2.6 billion and about \$116 million are attributed to market gains in the Fourth Quarter 2019.

Ms. Klassen remarked that Prudential has been sponsoring the spirit of community awards in conjunction with the National Association of Secondary School Principals with 102 students across the country who have won awards. There have been 2 students from the State of Hawaii who received awards, which can involve scholarships, for their volunteerism.

Mr. Malmud discussed the activities at the local office:

- With the help of counselor-assistance, rollover assets totaled over \$9 million.
- There were over 20,000 participant interactions through individual counseling sessions, group sessions, and phone contact.
- The local office counselors will be participating in the upcoming Teachers' Institute Day which will be held throughout the islands, and in a HGEA event.

Ms. Klassen added that an announcement was made by New York Life/MainStay Funds that the name of the fund will change to MainStay Winslow Large Cap Growth Fund, so Prudential is currently working on the updating the website and materials.

Mr. Chaikin asked about the status of the outreach to individual participants with multiple target date funds. Mr. Malmud reported that there is no data yet but they are working on reaching out to those participants on how and why they are allocated. The numbers so far have been low on the changes and actions taken.

The counselors are also reaching out to those participants who have terminated, approximately 300, to review options on staying in the Plan.

In response to Trustee Rapoza on the progress of the outreach initiatives with DOE, Mr. Malmud reported that discussions with DOE have started and have led to meetings with DOE staff. As a result, discussed possible initiatives such as holding workshops for DOE employees within the DOE districts and the coordination by DOE on distribution of internal emails to employees to publicize the workshops, in addition to working with UH on similar email distribution. Locations of the workshops would be outside of the school complex but within each of the school districts. Mr. Malmud shared some of the distinctions between the 403(b) plan and the 457(b) plan.

There were no other questions.

#### Agenda

Item # 7: Performance Evaluation Report for the Fourth Quarter 2019 by Segal Marco Advisors, including but not limited to:

- a. Overview of Funds Currently on the Watch List: Wellington Management Research Value Fund
- b. Management Changes Related to the Vanguard Wellington Fund

Mr. Chaikin presented a commentary on the market and performance evaluation of the funds through the Fourth Quarter 2019, in addition to some commentary on updates on defined contribution market updates, legislation, and litigation:

- Can expect to see industry innovations on the income front, as safe harbor provisions will make it more attractive for the industry to develop solutions and bring to the marketplace.
- There are ongoing industry litigations on issues and suits. The issues and suits relate to what the Plan is already doing and have in place to address such issues (e.g., related to fees, monitoring performance, changes to underlying fund managers).
- There is a new suit related to Cyber fraud and fiduciary liability. There are certain plan vulnerabilities that are introduced to plans with the shift to online activities. In general, the suits are saying that plan sponsors do have liabilities or responsibilities when it comes to having procedures in place that ensure participant data is protected.
- The S&P 500 was up at 31.5% at the end of 2019, and 9% was added in just the Fourth Quarter.
- The driving factors have been due to the interest rates. In 2018 the Federal Reserve raised the rates due to trade concerns with China and the potential slowdown in the economy; in 2019, the Federal Reserve lowered the rates three times during the year and the market reacted favorably.

- Corporate earnings have been good; the GDP has remained relatively strong during the Fourth Quarter.
- Unemployment rates have remained low; from the economic perspective things look strong.
- In 2020, the S&P started out flat; and small caps and emerging markets were down. Bond yields have decreased significantly, and bond returns have been good.
- Interest rates have been low, for historical norms.
- As summarized in Segal's February 7, 2020 memo, the Vanguard had announced in 2019 that two lead portfolio managers for the Vanguard Wellington Fund will be retiring – Mr. Edward Bousa and Mr. John Keogh. Both are lead portfolio managers who developed the portfolio teams that supported them. The announcements were made in advance so there are no surprises. Segal feels that Vanguard is a strong, well-resourced firm; therefore, Segal does not have any recommendations for changes.
- The performance of the Wellington Research Value Fund has been challenged relative to the benchmark. The performance has been strong in 2019 and has been strong for the past five quarters. The fund was placed on the watch list in December 2018, and now the numbers are back in line with what the expectations should be.
- Segal recommends that the Wellington Research Value fund be removed from the watch list.

**A motion was made by Trustee Wada and seconded by Trustee Yu to remove the Wellington Research Value Fund from the Watch List.**

Discussion: Mr. Chaikin added that the fund trailed for the Fourth Quarter; however, has outperformed by 158 basis points over the past year and ranked ahead of its peer median. And, over the past five quarters, the overall performance results have been more consistent with expectations.

**The motion passed unanimously.**

Chairperson Moto called a short break at 10:43 a.m. Trustee Wada was excused. The meeting resumed at 11:00 a.m.

Agenda

Item # 8:

PTS Plan:

- a. Approval of Report on Funds Not Deposited in the State/County Treasuries for the Periods Ending June 30, 2019 and September 30, 2019
- b. Quarterly Management Reports for Periods Ending June 30, 2019 and September 30, 2019

Ms. Akiyoshi presented the Plan asset report for the periods ending June 30, 2019

and September 30, 2019. The total assets are the combined assets for the State and the County of Kauai. The corresponding quarterly management report for the periods ending June 30, 2019 and September 30, 2019 are included.

**A motion was made by Trustee Rapoza and seconded by Trustee Yu to accept the Report of Funds Not Deposited in the State/County Treasuries for the PTS Plan for the periods ending June 30, 2019 and September 30, 2019. The motion passed unanimously.**

- c. LSW's Annual Letter on the Reimbursable Amount Available in the PTS Plan Expense Account for 2020
- d. Notification on New Interest Rates for the PTS Plan Effective January 1, 2020

Ms. Akiyoshi reported that LSW has prepared their annual letter to report the amount that is available in the PTS Plan Expense Account for Plan Year 2020. There were no expenditures for the calendar year 2019. For 2020, the amount that is available for reimbursement is \$66,209.67.

The new crediting rate for the PTS Plan beginning January 1, 2020 is 2.40%.

#### Agenda

##### Item # 9: Staff Administrative Report

Ms. Akiyoshi presented highlights of the ongoing monthly activities during 2019:

- Act 86, SLH 2019, was passed to add a Roth option. Researched and gathered information and have been discussing and working with Segal and DAG Nishiyama to prepare the amendments.
- Worked with DHRD on an additional position with DHRD which was approved by the Legislature to support the Board. The position has been established and is ready to go out for recruitment.
- Facilitated the replacement and transition from the LifeCycle Funds to the Vanguard Institutional Target Retirement Funds which were launched in April 2019.
- The Committee on Operations was established to support the Board between regular Board meetings.
- A modified competitive bidding process was developed for use in lieu of the State Procurement Office process which the Board adopted in April 2019.
- The Board requested an independent audit of the Plan be conducted for the Plan Year ending June 30, 2019. N&K CPAs was engaged by Prudential and they are currently conducting the audit and are expected to be completed soon.

- An award was presented to the Plan by NAGDCA at the 2019 annual conference in September 2019.
- Coordination of the 2019 Spring and Fall Benefits Fairs; both fairs were well attended.
- Worked with Prudential in scheduling meeting with DOE to discuss strategies on promoting Plan information to DOE employees. Workshops are being planned within the DOE districts, with assistance from DOE staff.
- The HI Pay Modernization project which migrated to the new payroll system in 2018 resulted in several payroll issues. In 2019, within the Plan there was one missed vacation payout, 10 ineligible contributions, and 13 missed contributions. The ineligible contribution issues appear to be related to the employees' employment and eligibility status and the missed contributions appear to be due to deferral rates that are not carried over with the employee or timing of reinstated deferrals due to LWOP. ETS has been working with a Benefits Eligibility Group to analyze and find solutions.
- Worked with Prudential on various communication campaigns related to the rollout of the Vanguard Institutional Target Retirement Funds, the new Go-Green campaign, and additional brochures (e.g., guide) to support Financial Wellness to help employees build their financial plans.
- Assisted Prudential in the coordination of the 2019 Summer Lunch-n-Learn sessions which were expanded to the neighbor islands.
- Review of the Plan Asset Reports through Fourth Quarter 2019 which were distributed to affected parties.
- Continuing to monitor INVESCO's portfolio reports. There have been no changes to the wrap contract providers' ratings. As of December 31, 2019, the total market to book ratio remains above book value at 100%.
- The PTS Plan monthly distribution reports have been reviewed and approved for processing through December 2019.
- The independent audit of the PTS Plan for the period January 1, 2017 to December 31, 2017 was completed and presented at the March 2019 meeting.

Agenda

Item # 10: Other Business/Announcements

a. 2019 Annual NAGDCA Conference Highlights and Summary

Ms. Akiyoshi noted that an award was presented to the Plan at the 2019 annual NAGDCA conference in the category of National Retirement Security Week for the Maui Employee Benefits Fair event and activities.

Some interesting sessions and topics covered were on:

- Strategies for organizational change through storytelling to promote and provide encouragement in finding ways to make even impossible changes, or ways to increase employee engagement.
- Successful communication campaigns that would help participants visualize needs in a way to capture their interest. Missouri State Plan shared stories of their plan transitioning their field reps from their recordkeeper to their office.

Chairperson Moto added that the conference sessions were very worthwhile and educational.

b. Review of Bills for 2020 Legislative Session

i. HB 2405, Relating to Socially Responsible Investing

Ms. Akiyoshi reported that HB 2405 was introduced with the intent to incorporate socially responsible investing in the investment decision-making of endowment, trust, or investment funds established by statute or maintained by state agencies or offices. The Plan, as established by statute, could be impacted; however, it is not clear if there is any intent that this would be directed to our Plan. There is no specific reference to this Plan.

Ms. Akiyoshi stated that this was reviewed and discussed with legal counsel and was felt that the Board should be made aware of this bill. Staff plans to only monitor this bill as it moves through the session. There is a companion bill, SB 3085.

Trustee Young stated that in his review of SB 3085, it could target all government investments and that for the University, its position would probably be to oppose this bill. He noted that the bill provisions seem to require that all government investments must conform to the bill's specific investment parameters, and not that investment choices must be generally socially responsible. The exclusionary investments listed seem overly prescriptive, and there would be no way that the University endowment would easily manage those other exclusionary investments.

Mr. Chaikin commented that when the Board discussed ESG in 2018, the discussion included characteristics of ESG, and there are certain characteristics that could be implemented such as looking at companies that have positive attributes. The exclusionary investments covered in the bill would be extremely problematic.

The Board had no objections on monitoring the bill for now.

c. Board Appointment/Reappointment(s)

Ms. Akiyoshi reported that the County of Finance Director on Kauai, Reiko Matsuyama, has applied for this Board's vacancy and the status of her nomination is pending. Trustee Rapoza's term will expire on June 30, 2020, and he is interested in serving a second term. The DHRD director's office is tracking and monitoring the status of both appointments.

Ms. Akiyoshi added that she is working with the director's office on the filling of the remaining vacancy on the Board.

d. Scheduled Meetings and Events for 2020

i. Updates on Spring Semi-Annual Meeting and Benefits Fair

Ms. Akiyoshi stated that the date for the Semi-Annual Board meeting is confirmed for Wednesday, May 27, 2020 in Hilo.

The rotation of the Benefits Fair will be on the Big Island, one fair is planned in Hilo and the second fair in Kona. Prudential is working to confirm and secure the sites in Hilo at the Imiloa Astronomy campus on Tuesday, May 26, 2020, and the other in Kona on Thursday, May 28, 2020.

There were no questions or objections on the proposed locations for the events.

The next regular meeting is confirmed for April 23, 2020.

There was no other business. Chairperson Moto thanked everyone for attending today's meeting and adjourned the meeting at 11:36 a.m.

Taken and recorded by:

Reviewed and approved by:

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Cynthia Akiyoshi  
Board Staff

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Brian T. Moto  
Chairperson