

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

**OPEN SESSION MINUTES
MEETING # 437**

Date: December 15, 2020

Place: Department of Human Resources Development
14th Floor Director's Conference Room
235 S. Beretania Street, State Office Tower
Honolulu, HI 96813

Present via

Teams Link: Brian Moto, Chairperson
Ryker Wada, Ex-Officio Member
Robert Yu, Ex-Officio Member
Kalei Rapoza, Employee Member
Reiko Matsuyama, Employee Member
Ken Kitamura, Employee Member

Others via

Teams Link: Randall Nishiyama, Deputy Attorney General
Cynthia Akiyoshi, DHRD Staff
Craig Chaikin, Segal Marco Advisors
Wendy Carter, Segal Marco Advisors
Rob Luciani, Prudential Retirement
Kevin Malmud, Plan Administrator Staff (Prudential)/Honolulu Office
Julie Klassen, Prudential Retirement
Carol Blumenthal, Prudential Retirement
Deborah Baran, Prudential Retirement
Jeanne Kanai, Plan Administrator Staff (Prudential)/Honolulu Office
Grace Baracao, Plan Administrator Staff (Prudential)/Honolulu Office
Lawrence Chew, N&K, CPAs
Sarah Brown, N&K, CPAs
Judy Dang, B&F/Treasury Division

Absent: Kalbert Young, Employee Member

Call to Order: There being a quorum present, Chairperson Brian Moto called the meeting to order at 9:00 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.

Agenda

Item # 1: Welcome and Introduction of Incoming Board Member(s)

Chairperson Moto welcomed everyone and proceeded with introductions. He introduced the new incoming board member, Ken Kitamura, who is the Business Management Officer from the Department of Human Services and who previously served on the Board during his appointment at the Department of Budget and Finance. Trustee Kitamura provided some introductory remarks on his background. He continued with the introductions of the Board members, Board staff, and other guest attendees.

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Item # 2: Public Testimony Period

There was no one from the public in attendance to offer testimony. Chairperson Moto closed the public testimony period for this meeting.

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Item # 3: Approval of Minutes No. 436 for the August 4, 2020 meeting

There were no comments or changes offered by the Board members.

A motion was made by Trustee Rapoza and seconded by Trustee Matsuyama to approve Minutes No. 436, as presented. The motion passed unanimously.

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Item # 4: Independent Plan Audit Report for the section 457(b) Plan for the Plan Year ending June 30, 2019 by N&K CPAs, and Potential Action Thereon

Chairperson Moto stated that at the August 5, 2019 Board meeting, the Board authorized an independent audit be conducted for the Plan year ending June 30, 2019. Mr. Lawrence Chew and Ms. Sarah Brown presented the report.

Ms. Brown, the manager on the team audit, provided a summary of the financial statement audit, including:

- An explanation of the type of auditor's report that is issued which is in accordance with U.S. GAAP (Generally Accepted Accounting Principles).
- Statement that there were no material weaknesses.
- Statement that there were no material weaknesses found. There were two deficiencies that were identified in the report on internal controls over the financial reporting and on compliance and other matters. These are repeat findings from the last audit conducted for the plan year ending June 30, 2017. The two findings are: 1) to amend the Plan Document; and 2) to amend the Hawaii Administrative Rules.

- The responsibilities of the auditor as communicated in the engagement letter of August 22, 2019 and addendum. The addendum covers the supplementary information on Prudential Retirement's lost participants process and relevant participant data but which was not subjected to the auditing procedures, and no opinions were expressed or assurances provided on it.
- The significant accounting policies and the auditor's judgement about the quality of the accounting principles. The accounting policies were appropriate and consistent with GAAP. It was noted that there were no new accounting policies adopted and no transactions were entered into by the Plan during the year for which there is a lack of authoritative guidance or consensus.
- Accounting estimates are based on management's knowledge of current events. Disclosures on the fair value of investments are also provided and are neutral, consistent, and clear.
- It was noted that there were no difficulties encountered in the performance of the audit.
- Preparation of the management's representations.
- No new pronouncements to report as it relates to the Plan. GASB statement no. 95 was issued in response to the COVID-19 pandemic to provide relief to government and other stakeholders.

In response to Trustee Matsuyama's question on the length of time in conducting and reporting on the audit, Ms. Brown stated that there were some delays in completing certain testing due to the pandemic and remote testing.

A motion was made by Trustee Yu and seconded by Trustee Matsuyama to accept the independent audit report prepared by N&K CPAs, as presented, for the Plan Year ending June 30, 2019. The motion passed unanimously.

Mr. Chew thanked and acknowledged the assistance of everyone in the preparation of the audit.

Agenda

Item # 5:

Discussion and Consideration on the Renewal of the Contract Agreement with Prudential Retirement for an Additional 2-Year Period upon the Expiration date of June 30, 2021, and Potential Action Thereon, including but not limited to:

a. Review of the Prudential Retirement Performance Scorecard

Ms. Akiyoshi provided a background summary on the current agreement with Prudential which covers an initial 5-year period, plus four (4) additional renewal periods. The current period that expires on June 30, 2021 is the first renewal period which was for three (3) years. The second renewal period is for two additional years which would expire on June 30, 2023. The two (2) renewal periods thereafter are for 2-year periods. Prudential has provided their letter of interest in extending the contract for the additional 2-year period.

Ms. Klassen provided and summarized the letter of interest:

- Reviewed the highlights and accomplishments since the start of the Plan administration, such as:
 - Providing counseling sessions through both individual and group meetings.
 - Providing services that resulted in national awards from NAGDCA, including two (2) awards in 2020.
 - Partnering to create the first-ever ISP virtual benefits fair in 2020.
 - Providing a custom website and online digital tools and resources.
 - Seeing the increases in enrollments, Plan participation rate, and improvements in Plan asset allocations.
- Plans for continuing to provide enhancements to the mobile app and website.

Ms. Klassen reviewed and noted deficiencies in two categories in the Performance incentives scorecard. In the category of the call center's responsiveness to incoming participant calls, Prudential did not meet the expected standard due to a higher volume of calls related to the COVID-19 pandemic that generated higher number of questions on market volatility and the relief provisions under the CARES Act. She added that the participant satisfaction remains high, over 90%. The second category that Prudential did not meet the expected standard was related to the goals of 630 group educational meetings. Due to COVID-19 pandemic and the quarantine restrictions, the Prudential team was unable to hold the established number of group meetings for the Plan year ending June 30, 2020, at the department's locations. Since Prudential was able to launch the virtual counseling meetings prior to COVID-19 pandemic, individual meetings were able to continue through virtual appointments, the virtual Benefits Fair, and the webinars.

Mr. Malmud added that Prudential was able to transition to a virtual environment prior to the pandemic and are ahead of the individual meetings. Group meetings are meetings held at departmental locations and became more difficult to schedule during the pandemic and stay-at-home environment. However, through the virtual Benefits Fair, group sessions and webinars were able to be scheduled. An email communication chain with human resource offices has been set up to offer both individual and group sessions to promote their availability.

Ms. Akiyoshi stated that the independent plan audit report has been presented and is available for the Board's use in the deliberation of the extension of the contract agreement for an additional 2-year period, along with Prudential's performance scorecard through the Third Quarter 2020 which looks at the measurements and goals identified in the contract for each quarter.

A motion was made by Trustee Wada and seconded by Trustee Rapoza to accept the letter of interest from Prudential to continue the contract agreement and to prepare a notice to Prudential on the renewal of the contract agreement for an additional 2-year period which would expire on

June 30, 2023. The motion passed unanimously.

Chairperson Moto stated that Board staff will prepare a letter to Prudential to confirm the extension of the contract agreement for an additional 2-year period through June 30, 2023.

Mr. Malmud and Mr. Luciani expressed their appreciation of being able to continue the partnership with the State of Hawaii.

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Item # 6: Plan Administrator's Report:

- a. Identity Fraud Case Activities within the Plan
- b. Plan Highlights
- c. Reporting on the CRD Withdrawals and RMD Waiver Options

Ms. Klassen opened with a report on some identity fraud cases that were occurring in the Plan and the fraud loss protection policy that is in place by Prudential. She explained that there were 6 attempts made since September 21, 2020, but no new incidents since October 1, 2020. There were 3 successful attempts whereby funds were withdrawn. These participants were made whole. She reviewed the protocols that are in place to mitigate fraud activities and added that the incidents most appear when participant accounts are not registered with Prudential. Prudential is doing outreach to the participants who have not registered their accounts. A proposed education plan was outlined to continue the outreach. Local law enforcement has been in contact with Tom Kalili regarding the incidents, especially those related to the incidents with participants on Hawaii Island.

Ms. Klassen continued with comments and an overview of the Plan highlights:

- In December, implementing new features to enhance the digital security protocols to secure registration and the authentication of account information via mobile phones.
- Pursuant to the CARES Act, RMDs were not required for 2020. 3,287 individual RMDs were suppressed. Those participants who received distributions prior to the effectiveness of the CARES Act waivers were sent mailings. To date, 444 participants of the 3,287 responded that they still wanted their RMDs.
- The CRD option will expire in December 2020.
- It is anticipated that further legislation is possibly being developed and proposed under the SECURE Act to raise the RMD requirement to age 75.
- CRD activity through October 2020 revealed 567 withdrawals, representing over \$13 million in assets.
- Reports on the cash flows for distributions, contributions and the net cash flow.

- Report on activities related to participation rates and use of asset allocation tools. Expect further discussions on enhancements to the online capabilities and tools that would help provide participants looking to draw down assets as they entire into retirement.

Ms. Baran reported on the communication campaigns since the virtual Benefits Fair:

- Introduced virtual Lunch-n-Learn webinar series and were beneficial for those that did attend. The attendance at the sessions were lower than previous years but this may be due the same sessions being repeated and replayed from the Fair. The Plan website also has uploaded the replays of the sessions for an expanded venue for viewing.
- Plan newsletters that reported on the various campaign events and activities.
- A target letter to the participants who have not registered their accounts was prepared and distributed for the fraud campaign.
- The Plan website has new tools to set up virtual appointments which allows for more hand-held interactions.
- Upcoming discussions and planning of future newsletters to include the registration of accounts related to the fraud campaign, and options for the next Benefits Fair.
- Plans to look at preparing a submittal to NAGDCA on the virtual Benefits Fair that was held in June 2020, as it did not appear that there were similar events held at that time that was of that magnitude as the Benefits Fair.

In response to Trustee Matsuyama's question on what changes would be anticipated in communications and secondly what trends or changes are expected in habits for employees who may possibly be furloughed, Ms. Baran remarked that employees still will have access to the Prudential team. Prudential will look at the demographics to determine the need for any additional communications.

Mr. Malmud added that an increase in the UEW (unforeseen emergency withdrawal) distributions could be possible as seen in 2008, so the Prudential team will make the process as smooth as possible. Mr. Malmud continued with the local office activities:

- Continuing with call out campaigns to participants who are terminated and recently retired to explain the benefits of the Plan.
- Engaging with union contacts, especially with the UH lump sum payout payments.
- The retirement of Al Lee from the local office in September; have interviewed candidates and will be filling his position in January.
- Working with a Human Resource email list to communicate to departments on recent developments and market volatility updates.
- Worked with HGEA to coordinate information and instructions to employees on deferring pay increases to Plan that included links to the Plan's forms.

There were no other questions from the Board. Trustee Yu was excused from the meeting at 10:10 a.m.

Chairperson Moto called a break at 10:25 a.m. The meeting resumed at 10:37 a.m.

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Item # 7: Performance Evaluation Report for the Third Quarter 2020 by Segal Marco Advisors:

Mr. Chaikin provided remarks and an overview of the Third Quarter 2020:

- We can expect changes in 2021 but it will be an uphill climb for moving things forward.
- The U.S. Department of Labor provided guidance for ERISA plans on requirements for Plan Sponsors to show lifetime income disclosures on an annual basis. In following best practices of ERISA plans, this would be beneficial for participants to see the impact on their retirement savings. May want to consider partnering with ERS to show retirement projections. Ms. Blumenthal added that Prudential will be implementing for plans across the board.
- U.S. Department of Labor issued guidance regarding proxy voting, to allow for proxy voting only if there is a tangible benefit to participants.
- In recent guidance regarding ESG, plans are advised to evaluate investments choices on pecuniary factors or those with financial issues. Risk and return factors are the primary metrics. Other factors with ESG are if plans can prove that all else is equal. The U.S. Department of Labor could change its guidance again on this.
- Performance results through September 30, 2020:
 - With the news of a vaccine, the U.S. markets have done well through November 2020, up at 10.2%.
 - Markets were up 7% during the week of November 2020, while waiting for the election results.
 - Market shifts in volatilities resulted in Russell 1000 large cap growth equities and Russell 1000 large cap value equities showing its largest discrepancy in history, and reflecting poor returns against the benchmark. Russell 2000 small cap equities rallied in recent months.
- The Plan's assets were at \$2.7 billion through the Third Quarter.
- The AMCAP Large Cap fund struggled during the Third Quarter due to an underweight to tech and healthcare stocks, likely due to the expectations that the vaccines may not likely be ready.
- Also struggling was the MainStay Large Cap fund due to an underweight to Apple and Tesla stocks, as these were extremely strong.
- The MFS value fund was up 7% relative to the benchmark for the Third Quarter.

- The expense fees continue to be competitive relative to the available investments out in market.
- The SSGA Real Asset Return fund had a good return relative to its benchmark but not necessarily against its peer group universe.
- The Vanguard Target Date funds will trail the benchmark because of its passive implementation. This does not mean anything is wrong with the management of the underlying holdings.

Mr. Chaikin noted that given the market environment, there were no recommended changes or watch list recommendations.

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Item # 8:

Report on Payroll Wire Delay from State for the July 2, 2020 Pay Date, and Potential Action Thereon

Ms. Akiyoshi noted that Ms. Judy Dang from the Treasury Division of the Department of Budget & Finance was available to join today's meeting.

Ms. Akiyoshi reported that there was a payroll wire delay from the State to Prudential. She explained how the payroll files and wires are normally handled every pay date and that she monitors the payroll transmissions for every pay date. For the July 2, 2020 payroll:

- Payroll interface files were timely sent by the State to Prudential Retirement, three to four days prior to pay date. For the State's payroll, the DHRD's Employee Assistance Office pulls the State file for the contributions to review.
- On July 1, 2020, Prudential reviewed and sent an acknowledgement that the files were in good order. Ms. Akiyoshi ensures that the payroll amounts match the State's files and looks for any discrepancies.
- On July 2, 2020, the Treasury Division sent a confirmation of the wires that were sent to the First Hawaiian Bank. Ms. Akiyoshi checks to make sure that the wire amounts match the State payroll files and Prudential's report. At this point in the process, all the actions were timely.
- On July 8, 2020, Prudential office notified Ms. Akiyoshi that the wire was not received on Thursday, July 2, 2020 but instead on Monday, July 6, 2020. Therefore, the contributions were posted to participant accounts one business day late.
- The Treasury Division was informed that the wire from the First Hawaiian Bank was received on July 6, 2020 and not on July 2, 2020. The Treasury Division said that they would check with the bank.
- On July 9, 2020, the First Hawaiian Bank provided a response:
 - The First Hawaiian places the wires received the day before into a specific folder.
 - The morning team confirms that there is a sufficient balance in the account and recommends the release of the wire.

- In this instance, the wires were not placed in the correct folder and the morning team was unaware of the wires.
- The Treasury Division reported that the bank sent the wires after 11:00 a.m. HST which is after the 4:00 p.m. Eastern time closing of the U.S. markets.
- There were lost earnings due to the delayed posting to participants' accounts.
- In 2005, the Board established a policy to handle situations when the payroll files are received by the third-party administrator after the designated time. It states that in the event that the reprocessing of the payroll results in a loss to the Plan, the responsible agent/entity will reimburse the Plan for the full amount of the loss.
- Considerations on action steps were presented for discussion. One option is not to take actions as it could be costly and labor-intensive to recover the lost earnings and an administrative burden for the record keeper to calculate the individual de minimus adjustments to each affected account; the other is to follow the Board policy and recover the lost earnings and recalculate and make the applicable adjustments.
- Prudential reported that in following the best practices under the EPCRS (Employee Plan Compliance Resolution System) to make participants whole, the amount to restore the lost earnings had the contributions been posted timely would total \$30,167.98. There were 11,521 participants' accounts affected but 97 accounts did not have any difference in their accounts that resulted from the delay. For the majority of the remaining participants, the loss represented less than ten dollars of an earnings adjustment.

Ms. Dang added that the State Central Payroll Office provides a certified payroll report and the checks the day before the pay date. The checks for the employee deductions are then wired to Prudential. The process is to input the wire information the day before for the wires to be sent by the bank on pay day. She noted that the First Hawaiian Bank recently did a reorganization of that section and has been putting updated processes in place to prevent future occurrences. They are also working with DAGS to be able to send out an ACH file instead of a wire as a long term solution in preventing future incidents.

Trustee Kitamura stated that a legal process would be onerous given the small amount of the losses and raised whether there is an administrative remedy in the contract between the Department of Budget & Finance and the First Hawaiian Bank.

Chairperson Moto stated that as fiduciaries, we should look at taking appropriate steps. The error seems to be at the bank but the Plan or the Board does not have a contract with the bank. The Board discussed considerations and is asking for a letter to be prepared to the Department of Budget & Finance to notify them of the Board's understanding of the events and that some participants were impacted and had lost earnings, and to also ask how the participants can be made whole. Trustee Wada remarked that at least it would demonstrate that action was attempted and to ensure that this would not set a precedent.

A motion was made by Trustee Wada and seconded by Trustee Kitamura to have a letter prepared to the Department of Budget & Finance to notify them of the issue of the late posting of payroll contributions that occurred on July 2, 2020 and the resulting lost earnings to participants, and ask whether there would be remedy to reimburse the Plan and make participants whole. The motion passed unanimously.

Trustees Rapoza and Matsuyama stated their agreement that as a policy the Board should take some steps to follow-up. Trustee Wada was excused at 11:18 a.m.

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Item # 9:

Discussion and Consideration on Optional Provisions for In-service Distributions under the SECURE Act, and Potential Action Thereon:

Ms. Akiyoshi reported that Prudential has prepared a summary description on the two optional provisions under the SECURE Act. The IRS issued guidance on September 2, 2020 on the optional provisions. One is on the qualified birth or adoption distributions and the second is on the in-service distributions at age 59-1/2. These are optional and plans are not required to adopt the provisions.

Over the years, the Board has expressed concern about the sources of the leaks from the Plan, and these options would add to the sources of the leaks.

The consideration that is being proposed is to defer the adoption of the optional provisions.

- The distribution options would make monies from the Plan more easily accessible.
- Saw that with the adoption of the CRDs in 2020 due to the COVID-19 pandemic, it provided an opportunity for participants to access their retirement monies. It was a unique event that provided relief for many employees; however, it does have a consequence in that their retirement savings, even if they choose to repay that portion within the three years, it would take them longer to recover the amount withdrawn as they would lose the compounding effect accumulated during that period and have less saved. In looking ahead, should another crisis occur during their retirement years, they may not have enough saved. There were about a dozen participants who took the maximum CRD withdrawal amount.
- For those wishing to take distributions at age 59-1/2, they would likely retire in the next five to six years, so rather than taking the funds early, they could be saving that amount for when they may need it during their retirement years, especially if faced with another crisis in the future. They will also no longer be actively contributing and will not have those contributions to depend on to add more monies into their retirement account.

- In July 2020, Segal provided IRS guidance on additional mandatory changes that would be required when amending the Administrative Rules which need to be incorporated into the draft Rule amendments. The addition of these changes and adding any potential adoption of the optional provisions would further push the completion time for the drafting of the Rules amendments.

As Prudential reported earlier, Congress is looking at developing more legislative changes and the September 2020 IRS guidance on the optional provisions are examples of the trend that there will be more provisions coming. Therefore, the request is, rather than to stop now to look at the optional provisions, move forward with the amendments that need to be done and to defer the optional provisions that were issued in the until a later date. In this way, it would not further impact the completion of the Rules amendments at this time.

Chairperson Moto stated that his preference would be in favor of adopting the provisions, in particular to allow in-service distributions at age 59 1/2, since this is currently allowed in the 403(b) plans and would be consistent with the intent of Congress. He noted that it would lessen the anxiety for participants if they know they can access their monies and would benefit in promoting the Plan.

Mr. Malmud remarked that before this recent legislation, although 401(k) plans did have the ability to allow distributions at age 59 1/2, there are those plans that were more restrictive than the law and did not offer that distribution option. Only governmental plans were not permitted distributions at 59 1/2.

Trustee Rapoza commented that these provisions could have an impact on the Plan as the leaks are valid, and we would want to keep the leaks to a minimum; therefore, prefers not to make the change right now. He noted that Prudential is doing their best on the education and promotion of the Plan. Ms. Carter remarked that NAGDCA does member survey of what other plans are doing. She can ask the committee about a survey.

The Board had no further objections to delaying any action until more information can be gathered.

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Item # 10: Status and Discussion on the Proposed Draft Amendments to the Administrative Rules to Add the Roth 457 option to the Plan:

Ms. Akiyoshi reported that as mentioned in the prior agenda item, due to the additional guidance issued by the IRS in July 2020, the mandatory changes are being incorporated into the draft Rules and has caused a delay and edits are still being review.

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Item # 11: Status on the Establishment of a New Position to Staff the Board of Trustees

Ms. Akiyoshi reported that there has been no further word on the status and the review is still with the Department of Budget & Finance analyst. DHRD is looking into the status.

There were no additional questions from Board members.

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Item # 12: PTS Deferred Compensation Retirement Plan for Part-time, Temporary and Seasonal/Casual Employees (PTS Plan):

- a. Approval of Report on Funds Not Deposited in the State/County Treasuries for the Periods Ending June 30, 2020 and September 30, 2020
- b. Quarterly Management Report for the Periods Ending June 30, 2020 and September 30, 2020

Ms. Akiyoshi reported that the Plan asset reports for the PTS Plan, for the periods ending June 30, 2020 and September 30, 2020, are presented for the Board's review and action.

The total combined asset balance in the PTS Plan as of September 30, 2020 has grown to \$142,508,539.26 since December 31, 2019. For the amount of CRD withdrawals taken as of September 30, 2020, by participants, totaled approximately \$430,000.

The corresponding quarterly management reports for these periods are also provided for the Board's review and information.

A motion was made by Trustee Rapoza and seconded by Trustee Matsuyama to accept the Report on Funds Not Deposited in the State/County Treasuries for the periods ending June 30, 2020 and September 30, 2020. The motion passed unanimously.

- c. Notification on New Interest Rate for the PTS Plan, Effective July 1, 2020

Ms. Akiyoshi reported that the new interest rate effective October 1, 2020 is 2.31% which is down from 2.37% during the Third Quarter 2020 period.

There were no additional questions.

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Item # 13: Other Business/Announcements:

- a. 2020 Annual NAGDCA Conference:

Ms. Akiyoshi stated that the NAGDCA was held virtually due to the challenges presented by COVID-19 pandemic. There were some interesting speakers at both the general and the breakout sessions. Some topics covered this year included turbo charging your program and a need to keep in mind the changing age demographics, and on fraud and cybersecurity. The sessions bring awareness of how to administer a plan so the sessions were very informative.

Chairperson Moto added that the conference was easier to follow because it was online, and he thought the legislative sessions were interesting. Board members may want to consider attending future NAGDCA conference sessions.

b. Updates and Highlights of Virtual Benefits Fair:

Ms. Akiyoshi presented considerations for 2021 events and proposed planning of another virtual Benefits Fair in 2021 since many states are tightening their travel restrictions, have seen the latest COVID-19 surges across the nation, and have seen a lockdown in some states. In keeping with health and safety practices, a mid-year fair could be tentatively planned.

A second consideration that could be explored is arranging for a virtual meeting with the Plan's fund managers and have some educational forums with them.

Trustee Rapoza remarked that he would prefer a virtual fair until such time that there is confidence in travelling safely again. Trustee Matsuyama agreed since there was a high level of participation at the last virtual fair. With the current environment, we may not likely see a lot of changes to having gatherings in 2021.

There were no additional comments on the virtual fair from Board Trustees and no objections on holding virtual events in 2021.

Chairperson Moto thanked everyone for attending today's virtual meeting and adjourned the meeting at 11:48 a.m.

(NOTE: Signed copy on file.)