

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

**OPEN SESSION MINUTES
MEETING # 361**

Date: April 19, 2012

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

Present: Scott Kami, Vice-Chairperson
Barbara Krieg, Ex-Officio Member
Kalbert Young, Ex-Officio Member
Neal Miyahira, Employee Member
Wesley Machida, Employee Member
Dennis Vanairsdale, Employee Member

Others: Rodney J. Tam, Deputy Attorney General
Cynthia Akiyoshi, DHRD Staff
Troy Saharic, David Williams, and Andrew Ness –
Mercer Investment Consulting – Via Conference Call
Melody Takacs, Grace Baracao, and Jeanne Kanai, Plan Administrator Staff
(ING)/Honolulu Office
Carol Cann, Kristine Matthews, Brian Merrick – ING/Boston Office – Via
Conference Call
Todd Egger – INVESCO
Harry Mattson, ING
Harriet Jacobs, Lisa Hoxha – Great West Retirement Services

Absent: Wayne Chu, Chairperson

Call to Order: There being a quorum present, Vice Chairperson Scott Kami called the meeting to order at 9:05 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.

Vice Chairperson Kami welcomed everyone and opened the meeting with introductions of Board members and ING staff present. Also introduced were attendees on the conference phone line from Mercer and ING, and guests.

Agenda

Item # 1: Approval of Minutes No. 359 and 360

Ms. Akiyoshi asked that this item be deferred since the minutes are not ready for review.

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Item # 2: Plan Administrator's Report for 1st Quarter 2012

Ms. Kanai reported the following highlights:

- a. Multi-Factor Authentication was implemented in January 2012 to heighten the security for computer accounts;
- b. Planning is underway for the Benefits Fair in May.
 - 1) Ms. Matthews reported that there are three (3) campaigns being developed for the Fair:
 - i. One is an Outreach campaign designed for DOE employees to communicate the benefits of the Plan. The local Plan Consultants will be doing additional outreach to the 30+ surrounding schools in the area. Will be monitoring participation from DOE relative to past Fairs.
 - ii. Another is a Diversification theme campaign designed to educate participants about the importance of diversifying their portfolios.
 - iii. Third is a Participant Feedback Survey on the Fund of Funds concept. Previously, the Board discussed this idea and indicated obtaining participant feedback. A brief overview will be given at the Fair workshops and surveys will be taken on this topic. Objective is to help the Board in its future planning.

Ms. Kanai reported on the Plan Updates:

- a. Plan assets grew to \$1.6 billion from \$1.5 billion at the end March 31, 2011.
- b. Total rollover contributions were just over \$5 million.
- c. There were 26 UEWs approved and processed for 1st Quarter 2012, for a total of \$388,301.
- d. There were 27 set-ups with TD Ameritrade for a total of \$723,619.

Ms. Takacs reported on the Local Office activities:

- a. 148 Group meetings were conducted.
- b. Enrolled 116 State and county employees into the Plan.
- c. 1,747 total one-on-one consultations held with employees.

Mr. Merrick reported on the follow-up activities:

- a. Lifecycle Funds Transfers as it relates to the economic cycles:

Mr. Merrick provided an analysis to show the net lifecycle transfers, total lifecycle earnings and the net stable value fund transfers to illustrate some trends by participants on the net transfers in and out of the Lifecycle Portfolios. The analysis showed that the net lifecycle transfers were stable in 2010, and then it trailed off in 2011 through the end of the year. In comparison to the net stable value fund transfers, there was a much larger net dollar flow swing within the Plan. It was noted that there much more assets in the Stable Value Fund than in the Lifecycle Portfolios.

The Lifecycle Portfolio earnings, compared to the percentage of assets in the Plan, saw fluctuations which dropped in the 2nd Quarter 2010, and then spiked in the 3rd Quarter 2010; compared to the net Lifecycle Portfolio transfers which had muted activity. It was difficult to draw a distinct correlation between the earnings and the net transfer activities. The net stable value fund transfers are much more muted than in the prior slide because of the comparison to the percentage of the assets.

Trustee Vanairsdale noted that based on the dollar amounts, the Lifecycle Portfolio earnings went down in 2010 in 2nd quarter 2010, and the net Lifecycle Portfolio transfers were negative; then it goes up in 3rd quarter and transfers go up; it indicates that there is some reaction by participants to sell after the market drops and buy when it goes up. For participants closer to retirement, if there is a more conservative allocation within the mix of the Lifecycle Portfolios and it reacts less in a downturn, then participants may be less likely to bail.

- b. UEW Analysis

In a follow-up to the inquiry on the comparison to other government plans, when compared to other large government plans, Hawaii is not overly numerous. In comparison in dollar amounts, Hawaii is a little higher than others. In comparison to 1,000 participants, Hawaii starts to stand out more. In relation to the number of UEWs processed, Hawaii does not really stand out, but in relation to the dollar amount, Hawaii is highest. Some reasons could be due to the larger average account balance or larger hardship needs.

Trustee Young questioned whether the Hawaii Plan is more liberal in processing the requests since the amount is so much higher. Mr. Merrick responded that he will look for some trends on the UEW processing procedures to see if there is anything unique to Hawaii.

Mr. Ness added that another reason could be because other plans may have a loan provision which is a lot easier to get and the Hawaii Plan does not.

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Item # 3: INVESCO's Request to Retain Wrap Contract Providers with Lower Guideline Ratings:

Ms. Akiyoshi reported that a letter was received from INVESCO, to explain the situation occurring within the stable value fund wrap provider market, the guidelines for the credit quality ratings that they follow and what they must maintain at a minimum, and that they have two (2) wrap contract providers that have fallen below the credit quality ratings. INVESCO is asking for a temporary exception to retain the wrap providers until the current situation in the market changes.

Mr. Egger stated that the guidelines reference S&P and Moodys. INVESCO looks at S&P, Moodys, Fitch, and its own internal criteria. Both S&P and Moodys have downgrade below the stated minimum threshold. The reasons for the downgrade appear to be a knee-jerk reaction coming out of the financial crisis resulting in the reviews of banks. INVESCO does not anticipate this happening again in the near future. As they monitor, INVESCO gives them, on an ongoing basis, an internal rating separate from the rating agencies.

Trustee Machida asked what the total number of wrap providers are out in the market. Mr. Egger responded that of the number of approved wrap providers that INVESCO utilizes and of those issuing wrap contracts, the number is severely reduced. So another reason for the request is because there is not an opportunity to make a change now. Besides doing away with the wrap, there does not appear to be any other alternative.

Mr. Saharic added that there has been a limited supply of wrap providers, and there have been a number of wrap providers exiting the market including large banks due to the federal legislation surrounding wrap contracts needing to be treated as swaps which has not been formally approved. He feels that need to have some flexibility so that can have the wrap coverage.

A motion was made by Trustee Vanairsdale and seconded by Trustee Miyahira to approve the request from INVESCO for a temporary period.

Trustee Young asked what period of time it took for the ING downgrade to fall three (3) notches in the rating levels. Mr. Egger responded that with Pacific Life, the rating level dropped one notch; and responded that since there are multiple ratings over the past year and a half ING was downgraded by one agency, was rated high enough by another to qualify, and did not get a three (3) notch downgrade at one time. They were downgraded by one agency but still having a qualification by the other agency.

The Board wanted to get a better idea of the market and default risk and the ratings of all the providers and what the trend has been.

Trustee Machida asked at what point in time did they get out of compliance and why is the Board only now being informed. Mr. Egger responded that he would need to go back and do some research on the dates of the downgrade.

Mr. Egger added that there are no other wrap providers issuing contracts that they can place in this fund at this time. The Board discussed how far below the current minimum rating levels the Board would accept.

Mr. Egger stated that they can provide a listing of the wrap providers that are available, their credit ratings, and an internal analysis of an outlook for those providers to determine the right level. Trustee Miyahira noted that if it is put too out of line from the market reality, we could close off the option of wraps.

Trustee Young stated that the Board needs to be clear in its direction of where the Board is going with respect with wrap contracts. Mr. Egger noted that since they are out of compliance, the simplest remedy is a temporary exception until such time there are amendments made to the contract.

Since there are some legal concerns, Vice Chairperson asked to go into Executive Session to discuss with Legal Counsel.

A motion was made by Trustee Vanairsdale and seconded by Trustee Young to move into Executive Session at 10:05 a.m. The motion passed unanimously.

ING staff and guests were excused from the meeting, and conference line was placed on hold.

EXECUTIVE SESSION

Meeting

Reconvened: **A motion was made by Trustee Machida and seconded by Trustee Krieg to**

move out of Executive Session at 10:28 a.m. The motion passed unanimously.

Guests and the conference line attendees rejoined the meeting.

Trustee Vanairsdale stated that he withdraws his earlier motion on INVESCO's request.

DAG Tam summarized that the Board has decided not to take action on the request at this time; the Board is not waiving any of its rights under the agreement, and the Board has requested for additional information:

For INVESCO, the Board asked for the following information:

- Chronological history of when the ratings of the wrap providers decreased and how long has INVESCO been out of compliance;
- A list of available wrap providers offering wrap protection and its respective ratings;
- A list of alternatives, if the Board does not approve the request, alternatives that INVESCO will seek under the contract.

For Mercer, the Board asked for the following information:

- An analysis on the current situation of the stable value market and an opinion on if INVESCO's request is reasonable;
- An analysis of wrap market and the trends on ratings;
- Alternatives if the Board doesn't approve the request (e.g., like other types of products);
- Look at whether Prudential is currently in compliance.

Vice Chairperson Kami stated that Agenda Items Nos. 6 and 7 will be taken out of sequence, if there are no objections from the Board.

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Item # 6:

PTS Plan Quarterly Crediting Rate Effective April 1, 2012

Ms. Akiyoshi announced that the quarterly crediting rate beginning April 1, 2012 is at 3.78%.

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Item # 7:

Other Business/Announcements

a. 2012 Legislation Updates:

1. HB 2404, HD1, SD1, Related to Public Information. Ms. Akiyoshi reported that this bill is intended to require the posting of the agenda and the minutes online, in which both are currently being done. The minutes are currently posted on the Plan's website. The bill also would require any additional written materials to be posted online. The amount of materials to be posted could be voluminous; and there are other non-Plan related items such as the PTS Plan reports which do not relate to the Plan but would now be posted on the Plan website. Ms. Akiyoshi noted that she explored posting Board materials on the DHRD website and the concern raised by the IT administrator was volume capacity. However, there could be a link posted that would be on the DHRD website that takes the viewer to the Plan website.
2. Resolution on Report on Socially Responsible Investing that requires boards to encourage practices of SRI and adopt principles in its investment decision making. Ms. Akiyoshi relayed that an option is to have Mercer provide some education on this topic to increase the Board's awareness on SRI. Trustee Krieg mentioned that this has been raised at the EUTF meetings, so it is an issue that is making its way.

b. Board Appointments Expiring on June 30, 2012

Ms. Akiyoshi reported that there is one board appointment that is expiring on June 30, 2012. The Boards and Commissions Office has informed us that that appointee will be a holdover trustee.

c. Upcoming Scheduled Board Meeting(s) – The next meeting is scheduled for May 10, 2012.

A motion was made by Trustee Krieg and seconded by Trustee Miyahira to move into Executive Session at 10:40 a.m. The motion passed unanimously.

EXECUTIVE SESSION

Agenda

Item #4:

Status Report on Contract Award for RFP Nos. DCP-11-1, DCP-11-2, and DCP-11-3

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Item #5:

Review and Approval of Draft RFP for Third Party Administration Services

Trustee Krieg was excused at 11:15 a.m.

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Meeting

Reconvened: **A motion was made by Trustee Young and seconded by Trustee Miyahira to move out of Executive Session at 11:48 a.m. The motion passed unanimously.**

Vice Chairperson Kami adjourned the meeting at 11:48 a.m.

(Note: Signed copy on file.)