STATE OF HAWAII
DEFERRED COMPENSATION PLAN
BOARD OF TRUSTEES

OPEN SESSION MINUTES
MEETING # 439

Date: May 7, 2021

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
Kalbert Young, Employee 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
Kevin Malmud, Plan Administrator Staff (Prudential)/Honolulu Office
Julie Klassen, Prudential Retirement
Carol Blumenthal, Prudential Retirement
Deborah Baran, Prudential Retirement
Grace Baracao, Plan Administrator Staff (Prudential)/Honolulu Office
Ata Azarshahi, National Life Group/Life Insurance Co. of the Southwest
Dan Grundman, National Life Group/Life Insurance Co. of the Southwest
Riley Fujisaki, House Finance Committee

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 Introductions

Chairperson Moto welcomed everyone and proceeded with the introductions of the Board members, Board staff, and other guest attendees.

Agenda 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.

Agenda Item # 3: Approval of Minutes No. 438 for the March 5, 2021 meeting

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

A motion was made by Trustee Yu and seconded by Trustee Young to approve Minutes No. 438, as presented. The motion passed unanimously.

Agenda Item # 4: Approval of Payment to DHRD for the Two Special Funded Positions for FY 2022

Ms. Akiyoshi reported that there are two bills for collection to fund the two positions to provide administrative support to the Board and the Plan for the Fiscal Year 2022. One is for the Human Resources Specialist V level position that she is currently in and the other is for the Human Resources Specialist IV level position which has been approved for filling. Recruitment is underway. The funding request is for both positions based on the current salary schedule for this fiscal year. The funding amount also includes the fringe benefit cost amount based on the revised interim rate for Fiscal Year 2021, per the February 18, 2021 memo from the Department of Budget and Finance. The funding to DHRD is from the assets of the Plan and is needed by June 30, 2021, before the start of the next fiscal year. Any excess amounts not used by the end of the fiscal year will be returned to the Plan.

Ms. Akiyoshi stated that the amount available in the Plan Expense Account is provided in Prudential's Plan report, under tab V which they will be providing shortly. The balance in the Plan Expense Account as of March 31, 2021 is approximately $1.5 million which also includes the communications budget allocations.

Trustee Wada commented that the funding is not only for Ms. Akiyoshi's position but for the new staff position. To summarize, the purpose for the new staff position is to assist Ms. Akiyoshi with the duties to support the Board and administer the Plan, and as a succession planning method to carry on and retain the institutional knowledge of the Plan. Trustee Wada added that he will refrain from voting on this agenda item.

In response to Trustee Young's question on the travel budget, Ms. Akiyoshi recapped that Prudential is responsible for setting aside amounts for the contractual items into the Plan Expense account. The travel budget is a contractual item in the contract with Prudential which Prudential periodically makes deposits and sets aside for related travel expenses. For the travel budget, if there are no expenses that are expended during the fiscal year then the amount continues to accrue and the balance carries over into the next fiscal year.

Ms. Klassen added that Prudential deposits $20,000 for each fiscal for travel expenses. In making the deposits into the Plan Expense Account for the contractual items, Prudential is neutral on which bucket the expenses are taken from within the Plan Expense account.

In response to Trustee Rapoza's question on the funding amount that is transferred to DHRD and whether the funds continue to accrue if the position is not filled during the fiscal year or if the funds are returned to the Plan, Ms. Akiyoshi responded that whatever excess funds are not used for the DHRD positions are returned back to the Plan at the end of each fiscal year. The funding amount that is being requested for the next fiscal year will be used for the salary amounts in the new fiscal year beginning July 1, 2021.

In response to Trustee Yu's question on the amount of travel expenses of $158,030.96, Ms. Akiyoshi explained that the total travel expenses are the total amounts expended over the past years, since the transition to Prudential. If there is a change in the TPA, the excess or remaining balance in the Plan Expense account carries over to the next TPA. The Board has custody/control over the expenditures within the Plan Expense account.

A motion was made by Trustee Rapoza and seconded by Trustee Yu to approve the funding to DHRD from the assets of the Plan for the HRS V level and the HRS IV level positions in the amount of $140,554.69 and $84,362.16, respectively for the Fiscal Year ending June 30, 2022. There were no objections and the motion passed with one abstaining vote by Trustee Wada.

Agenda Item # 5: Deep Dive Presentation by Segal Marco Advisors

a. NAGDCA Survey Presentation on Public Sector Plans
b. ERS Presentation on Employee Retirement Benefits
c. Presentation on Retirement Income Gap Analysis by Prudential

Ms. Carter stated that NAGDCA has a new approach for gathering their survey data. In partnership with EBRI (Employee Benefit Research Institute), data was compiled through a NAGDCA survey process. Ms. Carter remarked that this information is beneficial in looking at what is happening within the industry. The survey universe is comprised mainly of state plans. She provided an overview of Hawaii's plan compared to the NAGDCA PRRL (Public Retirement Research Lab) study:

- In regards to Plan participation rates, the comparative data shows that the middle ground, around age 40 years old, stays consistently equal.
- Some aspects that impact the comparative data results are:
  - Hawaii's life expectancy is the longest in the United States. The average life expectancy is 82.3 years old.
  - Longevity in Hawaii affects workforce patterns, as compared to the overall data results.
  - Given the cost of living and longevity, observations on the average accounts show the low end of the account balances are among the 20-year old population versus the higher account balances are among the 60-year old population.
- Contributions are higher for the Hawaii plan against the NAGDCA universe. The patterns are consistent and show contributions increasing as the age group increases. Ms. Carter and Mr. Malmud commented that despite the higher cost of living in Hawaii, participants in Hawaii seem to be more engaged and motivated to find ways to save, and that the cost of living does not appear to be a dramatic impact.
- In looking at the asset weighted allocations, there is a higher allocation to equities. One reason for the higher allocation in the Hawaii plan is due to the higher participation levels in the GoalMaker asset allocation tool as opposed to other programs that do not utilize GoalMaker. Patterns show that the younger population contributed up to 80% of assets to equities and 20% to Stable Value, compared to the same universe in the NAGDCA survey which is at 24% invested in equities.
- Study of the age 20 population shows in the NAGDCA survey that 62% are invested in target date funds compared to Hawaii which has 8% invested in target date funds, but this is masked because of GoalMaker does not show up in the suite of funds.
- Many of the large plans in the study do have automatic enrollment which does create a difference in the asset allocations.

Mr. Williams presented an overview on the ERS pension comparisons among its members and retirants. He stated that he has observed that the younger employees tend not to save at the same rates as the participants in the survey.

- One characterization of the changes that have occurred with the ERS pension is that the value of the plan has been modestly reduced for new employees who were hired after July 1, 2012. The value is down about 12.5% and so there is a potential gap that is created relative to the older employees. These employees should take the opportunity to fill the gap and save as early as they can through participation in the deferred compensation plan.

- Types of programs include the Non-Contributory plan for the earliest employee members, two other hybrid programs. One is from July 2006 to 2012. There is also the Tier II for new employees beginning July 2012 through present. The plans result in different benefit structures and different replacement ratios.
- The ERS membership was broken down from approximately 148,000 employee members among the active, retirees and beneficiaries, inactive vested and inactive non-vested. There is a 1:3 relationship of active to retiree ratio which illustrates a mature plan. The ERS pays out about $1.4 billion in benefits per year and intakes about $1 billion in contributions. The rest has to be made up through investments on the assets.
- In 2013, there was a big jump following the introduction of Tier II when the benefit formula was lowered and vesting period increased.
- The number of retirees has steadily increased year after year. In December 2020 there was about an 18-20% increase in the number of retirees which may be due to reasons such as COVID-19, attrition, or budget reductions.
- The unfunded actuarial liability as of June 30, 2020 is $14.6 billion. The gap difference between the actuarially accrued liabilities and the total funded assets is mainly due to a diversion of contributions away from the ERS for about 3 decades which ceased in 2005.
- The new hire contribution rates have resulted in a funding period of 26 years at which time the ERS expects to be fully funded. The ERS investment program has not been a factor in the low funded ratio but helps to offset the unfunded liability.
- The breakout of the total membership is about 16.8% of the membership in the Non-Contributory program and 74% in the Hybrid program (Tiers I and II). The gap is made up of legislators and police and fire.
- The most popular retirement options for those employees who elected benefits solely for themselves and the maximum benefit allowance were reflected as 52% that are represented under the Non-Contributory program and 36% represented under the Hybrid program. The second most popular retirement option is the survivor benefit option, leaving benefits to a spouse.

Mr. Williams reviewed the benefit features such as the employee contribution rate, employer contribution rate, interest rate, the age requirements for full retirement, the pension formula and the post-retirement increase for the Non-Contributory program and the Hybrid programs (Tier I and II). He noted that the vesting period under the Non-Contributory program is 10 years, 5 years for Tier I, and 10 years for Tier II. So it is important for younger employees to participate in a deferred compensation plan because those employees are not assured of any benefits in the first ten years from the retirement system. He further reviewed some scenarios of the pension comparisons based on employee contributions before and after July 1, 2012, for the Hybrid programs for Tiers I and II.

Mr. Williams confirmed that because the option of transferring from the Non-Contributory to the Hybrid Tier I was offered only one time in 2006, the ERS provided an actuarial present value of the contributions that every member would need to make up in the plan only at that time. It is not done on an ongoing basis. The Non-Contributory program is no longer available to new employees.

He also confirmed that new employees and returning employees are not offered a choice but are placed in the Hybrid Tier II program.

Mr. Malmud discussed the educational approach for participants by having them look at the retirement income benefits that they will receive and what they will need to maintain a standard of living in retirement. He explained that the common amount of income that is generally needed to maintain a standard of living in retirement is about 80% of the employee's pre-retirement income. He explained that the education covers the major sources of income during retirement such as what is expected from the Social Security Administration and from the ERS. He illustrated some of the expected benefits under the different ERS programs. For the Non-Contributory the multiplier is 1.25%, the Hybrid Tier I the multiplier is 2%, and for Tier II the multiplier is 1.75%. He stated that they point employees to the ERS website to log-in and review their benefits.

Mr. Malmud described the Retirement Income Calculator that is available through the Plan. The Retirement Income Calculator shows the goal amount that they are targeting and are projected to need. Participants would add in their estimated ERS pension benefits, Social Security and outside savings, along with the amount of contributions to the Plan.

Agenda
Item # 6: Plan Administrator's Report for the Fourth Quarter 2020 and First Quarter 2021, including but not limited to:

a. Plan Highlights

Ms. Klassen summarized some comments and highlights:

- Legislation that may impact the Plan is related to further increases to the RMD ages, increases in catch-up amounts, and additional EPCRS (Employee Plans Compliance Resolution System) guidance for self-corrections for plans.
- Utilization of the Retirement Income Calculator (RIC) during the First Quarter 2021 resulted in 928 completions. The RIC encourages good retirement readiness behavior. For RIC users who inputted data related to the pension and the deferred compensation plan contributions, the average income replacement ratio is 62%.

  Ms. Klassen confirmed that the gap shown in the RIC is the gap to get to the employee's goal. The gap analysis is based on the employees' assumptions and how aggressive they are towards reaching their goals.

- The web activity on the home page of the website resulted in over 103,000 log-ins into the Prudential platform during the First Quarter 2021. Of that total, there are over 7,000 unique visitors.
- Prudential is continuing to monitor web account registrations and efforts to monitor cyber security. 59% of Plan participants are web-registered.
- The greatest allocation of Plan assets is in the Stable Value Fund and U.S. large cap equities.

Ms. Klassen commented that as of yesterday, the Plan assets exceeded $3 billion.

Chairperson Moto called a break at 10:35 a.m. The meeting resumed at 10:52 a.m.

Agenda Item # 7: Interim Performance Evaluation Report for the First Quarter 2021 by Segal Marco Advisors

Mr. Chaikin remarked that the report was for information only and reporting will be at a future meeting. There were no questions from the Board at this time.

Agenda Item # 8: Status on Payroll Wire Delay from State to the section 457(b) Plan for the July 2, 2020 Pay Date

Ms. Akiyoshi summarized that the payroll wire for the July 2, 2020 pay date was delayed from the State to Prudential which resulted in the contributions being posted on the next business day of July 6, 2020. There was a difference in the market prices between July 2, 2020 and July 6, 2020 that represented a loss to participants. She reported that since the last Board meeting, Prudential did provide the additional information to the Department of Budget & Finance (B&F) which they relayed to the First Hawaiian Bank. B&F did receive the entire funding from First Hawaiian Bank and the funding was received by Prudential. Prudential has completed the posting of the earnings allocations to participants' accounts as of March 19, 2021.

She remarked that the earnings adjustments were posted to individual accounts, and there was no separate messaging that was posted.

Chairperson Moto asked that letters be prepared and sent to DHRD and B&F and to acknowledge the receipt of the funding and to express appreciation for their assistance.

Agenda Item # 9: Discussion and Consideration on the Renewal of the Contract Agreement with Life Insurance Company of the Southwest upon the Expiration date of June 30, 2023, and Potential Action Thereon, including but not limited to:

a. Presentation on Projected Interest Rates for a 5-Year and 10-Year Periods
b. Election of a 5-Year or 10-Year Renewal Period
c. Minimum of a Guaranteed Annual Effective Interest Rate
d. Asset Management Fee

Mr. Azarshahi and Mr. Grundman, from Life Insurance Company of the Southwest, reminded the Board that renewal for the contract expires on June 30, 2023, and that LSW needs advance notification of about 18 months whether the Board intends to renew the contract for a 5-Year or 10-Year period, or to conduct a search. They presented an overview on the projected interest rate difference for either a 5-Year or a 10-Year renewal period. Overview presented included comments and information:

- The PTS Plan assets as of March 31, 2021 were approximately $142 million in account value.
- The assets are invested in National Life's Fixed Interest Annuity asset-segment for fixed interest annuities.
- Within that asset-segment, the PTS Plan assets of $142 million make up a portion of the larger asset-segment, thereby, the PTS Plan is benefiting from the larger pool of assets. The credited rate is based on a portfolio rate and less the spread, and the remainder is passed to the participants.
- Investments are in investment grade bonds rated NAIC 1 and 2. Most are corporate bonds. The only portions that are not investment grade are the corporate high yield and a small portion of private corporate bonds.
- The portfolio has about $544 million in assets; National Life has about $30 billion in total assets.

Mr. Azarshahi explained the cash flows in the Plan on a quarterly basis, such as the contributions, distributions, interest and assets that are rolled over. Total reinvestment is about $8.8 million to $16.9 million in current assets.

Mr. Azarshahi reviewed the interest rate levels as of April 7, 2021 for the 5-Year Treasury and the 10-Year Treasury. He provided the 5-Year and the 10-Year corporate spreads. He explained what the difference amounts to between the 5-Year and the 10-Year periods and what the new rates would be for the instruments. The portfolio earning rate for the past quarter was at 4.08%, less the spread of 195 basis points, resulting in the credited rate of 2.13%.

He illustrated the potential credited rates through the Fourth Quarter 2022. He stated that National Life is willing to reduce the spread by 5 basis points, from 195 basis points to 190 basis points if the contract is renewed for a 10-Year period. He further explained the impact if the spread were to be reduced by the 5 basis points.

He added that if a decision is made sooner than later, LSW would be in a better position.

Trustee Rapoza stated that he had raised his concerns committing to a 10-Year renewal period at the last Board meeting; however, at this time he is ready to support a 10-Year renewal of the contract if that is the desire of the Board. He expressed his appreciation for the information in the presentation and added that his concerns at that time were not based on the performance by LSW.

In response to Trustees Matsuyama and Young, with respect to the projection of interest rates, LSW has a view on the movement of the interest rates based on their perspective of the economy. Contrary to the mutual fund space, LSW actually buys and guarantees the rates and the spreads. In the fixed income bucket, LSW ensures that the duration remains as close to the liability. With the economy growing stronger, he feels that interest rates will slowly get better and offset inflationary factors.

A motion was made by Trustee Yu and seconded by Trustee Rapoza to authorize the renewal of the contract agreement with Life Insurance Company of the Southwest for a ten (10) year period that expires June 30, 2033. The motion passed unanimously.

<u>Agenda</u>
<u>Item # 10:</u> <u>PTS Deferred Compensation Retirement Plan for Part-time, Temporary and Seasonal/Casual Employees (PTS Plan):</u>

a. <u>Annual Management Report for Plan Year Ending December 31, 2020</u>
b. <u>Notification of New Interest Rates for the PTS Plan, Effective April 1, 2021</u>

Ms. Akiyoshi reported that the quarterly PTS Plan asset reports through December 31, 2020 were previously presented at the last Board meeting. The Plan asset report presented today is a summary report for the Plan Year ending December 31, 2020, to provide a recap for the year. No action is required for these reports.

The total combined assets as of December 31, 2020 totaled $143,815,346.84. The corresponding annual management report for the year is provided for the Board's review and information.

Ms. Akiyoshi reported that the interest rate for the PTS Plan effective April 1, 2021 is 2.13%.

There were no questions from the Board.

<u>Agenda</u>
<u>Item # 10:</u> <u>Other Business/Announcements</u>

a. <u>2021 Legislative Session</u>

Ms. Akiyoshi reported that Trustee Kitamura's appointment has been confirmed by the Senate for a term to expire June 30, 2025.

There were a couple of other legislative bills being monitored which did not make it through the session for the Board's information. One was a resolution to urge retirement plans to offer a Roth option; and there was another bill to urge Boards and Commissions to provide orientation to incoming members and provide training to members on an annual basis.

Trustee Wada added that for the resolution pertaining to the Roth option, the push was from Senator Chang. He commented that he did have a conversation with Senator Chang, to give an update and timeline on where the Deferred Compensation Plan was in offering this option.

There were no further questions from the Board. Chairperson Moto acknowledged Segal Marco Advisors for hosting the meeting and for everyone's participation in the meeting and the presentations.

Chairperson Moto thanked everyone for attending today's virtual meeting and reminded everyone that the next regular meeting is scheduled for June 25, 2021. He adjourned the meeting at 11:32 a.m.

(NOTE: Signed copy on file.)