DRAFT

MINUTES

March 12, 2015

Deferred Compensation Board

State of Wisconsin

Location:

Department of Employee Trust Funds
801 West Badger Road (Mendota Room)
Madison, WI

BOARD MEMBERS PRESENT:

Ed Main, Chair
John Nelson, Vice-Chair
Gail Hanson, Secretary
Michael Gracz
Art Zimmerman

PARTICIPATING EMPLOYEE TRUST FUNDS (ETF) STAFF:

Bob Conlin, Secretary
John Voelker, Deputy Secretary
Division of Retirement Services: Matt Stohr, Administrator
Deferred Compensation Program: Shelly Schueller, Director
Legal Services: David Nispel, General Counsel
Office of the Secretary: Cheryllynn Wilkins, Board Liaison
Office of Trust Finance: Stefanie Pauls, Financial Management Supervisor

OTHERS PRESENT:

ETF Legal Services: Angel Johnson
ETF Secretary's Office: Tarna Hunter
Advised Assets Group (AAG):
Mike Burroughs
Bill Thornton
Empower Retirement:
Sue Oelke
Vanguard
Bob Lawler
Ed Saracino

Mr. Main, Chair, called the meeting of the Deferred Compensation Board (Board) to order at 1:00 p.m.

Board	Mtg Date	Item #
DC	6.16.15	2

ANNOUNCEMENTS

Ms. Schueller welcomed Art Zimmerman as a new Board member. Mr. Zimmerman, Ms. Hanson and Mr. Main were all confirmed by the State Senate earlier this year. ETF has contacted the governor's office with regard to Mr. Nelson's position, as he also submitted an application to be reappointed to the Board.

MINUTES

> ***MOTION: Mr. Nelson moved acceptance of the open and closed session minutes of the November 4, 2014, meeting as submitted by the Board Liaison. Ms. Hanson seconded the motion, which passed unanimously on a voice vote.***

ELECTION OF OFFICERS

Mr. Main asked for nominations for Board officers.

> ***MOTION: Ms. Hanson moved to elect Board officers for 2015 as follows: Ed Main as Chair, John Nelson as Vice-Chair and Gail Hanson as Secretary. Mr. Zimmerman seconded the motion, which passed unanimously on a voice vote.***

DEFERRED COMPENSATION INVESTMENT COMMITTEE UPDATE

Ms. Schueller provided an update on the February 11, 2015 Deferred Compensation Investment Committee ("Committee") meeting (see Attachment A).

INVESTMENT PERFORMANCE REVIEW AS OF DECEMBER 31, 2014

Mr. Thornton referred to the Investment Fund Performance Review report for the period ending December 31, 2014 (Ref. DC **|** 3.12.15 **|** 5). He reported that most funds have met or exceeded their benchmarks for the quarter, with the Calvert Social Equity Fund also rebounding from previous poor performance. The Federated U.S. Government Fund was trailing its peers slightly. The Fidelity Contrafund is also slightly below its peer group average for the year, but the fund's three year average is outperforming its peer benchmark group. The Vanguard target date funds continue to have solid performance.

The WDC has a total of 55,738 participants with an accumulated total of 245,925 accounts, which means the average participant is invested in 4.4 funds. The one year weighted return for the WDC as of December 31, 2014 was 7.60%. Much of this return can be attributed to the significant amount invested by WDC participants in the Fidelity Contrafund, which returned 9.56%.

VANGUARD TARGET RETIREMENT DATE FUNDS – COLLECTIVE TRUST OPTION

Mr. Lawler provided an overview of Vanguard and its corporate structure. He reviewed how Vanguard is different from other fund management companies and how participants benefit from Vanguard's approach to investing. Mr. Lawler discussed the expense ratio of Vanguard and that the low-cost investment savings are passed on to the customer.

Next, Mr. Lawler talked about target date funds (TDFs). There are three components to Vanguard's approach to TDFs. Vanguard seeks low cost, broad diversification and strategic asset allocations. The target date fund market has grown substantially over the past 10 years. Last year there were $55 billion dollars in net cash flow into these funds at Vanguard. Vanguard recently announced they will be adding institutional options for the TDFs. The institutional option could provide a significant savings to the WDC and its investors as instead of the 16 to 18 bps (basis points) per fund costs, the institutional funds will be priced at 10 bps.

Mr. Saracino provided a general overview for the Board regarding the structure of the Vanguard TDFs, reviewed the guide path of each fund based on retirement age and explained some upcoming changes. The TDFs will gradually increase global diversification in 2015 by increasing allocations to both international stocks and international bonds during the remainder of the year.

VANGUARD TARGET RETIREMENT DATE FUNDS – INSTITUTIONAL SHARE CLASS OPTION AND GLOBAL ALLOCATION CHANGE

The Board discussed the information provided by Mr. Lawler and Mr. Saracino as outlined in the memo (Ref. DC | 3.12.15 | 6A). The Board deliberated on the trade-offs with collective trusts that includes potentially lower expenses of 8.25 bps but also reduced transparency and regulatory oversight. The Board determined that paying a slightly higher cost for the institutional funds (10 bps) with greater transparency was a better option than moving to collective trusts.

> ***MOTION: Mr. Nelson moved to authorize changing the Vanguard Target Date Retirement Funds from retail to institutional options when they are available. Ms. Hanson seconded the motion, which passed unanimously on a voice vote.***

PLAN AND TRUST DOCUMENT REVISIONS

Ms. Schueller recognized the work Mr. Nispel and Ms. Johnson did in preparing two revisions to the Plan and Trust document for Board consideration (Ref. DC | 3.12.15 | 7). The first change applies to the beneficiary sequence and involved revising the existing beneficiary language in the Plan and Trust document to better match the beneficiary explanation and format used with other benefit programs administered by the

Department. This simplifies the language and puts grandchildren on their own line in the list of beneficiaries.

> ***MOTION: Mr. Zimmerman moved to approve the proposed changes to the Plan and Trust document which will ensure the beneficiary sequence is identical to that used for other benefits administered by the Department. Mr. Gracz seconded the motion, which passed unanimously on a voice vote.***

The second recommended change explored language regarding how the WDC may administer local employers' 457 plans that come to the WDC with existing participants loans, if these employers wish to convert from other s. 457 plans to the WDC. In discussions with Empower Retirement, Empower has stated they could administer these loans. Empower Retirement's loan group could take over the loan processing. There would be no cost to the WDC for administering these "grandfathered" loans. The difference would be that instead of a payroll deduction to pay back the loans, these individuals would have a traditional coupon payment book.

Empower Retirement recommended that if the Board would like to pursue this, then the Plan and Trust document should include language clarifying that the WDC does not permit loans, but would allow for grandfathered loans from local public employer plan conversions with loans. This would allow public employers in Wisconsin currently offering programs with loans the option of moving to the WDC.

Ms. Oelke explained the current challenge: Many public employers have learned about their fiduciary responsibilities for offering a s. 457 plan, and because they do not want the fiduciary oversight responsibility, they would be interested in joining the WDC. However, because their current plans have loans, they cannot join the WDC. If a plan converts to the WDC except for accounts with loans, the employers would be running two plans and still have the fiduciary responsibility for the original plan.

If the Board decided to permit grandfathered loans for incoming new public employers, an administrative contract change would not be necessary, but a Plan and Trust document change and a Loan Policy or letter of agreement would be requested from Empower Retirement.

The Board discussed this concept and tabled the item. They have questions regarding their fiduciary responsibility with regard to s. 457 plans converted from other programs to the WDC by public employers that offer loans and the risks associated with doing so. Mr. Nispel will make a presentation at the June Board meeting regarding any potential complications or other concerns regarding permitting local employers with existing loan provisions to become part of the WDC.

ALLOCATION OF INVESTMENT OPTION REIMBURSEMENTS: Proposed Policy, Possible Impacts and Potential Implementation Timeline

Ms. Schueller reviewed the board memo (Ref. DC | 3.12.15 | 8) which discusses the reallocation of fund house share class reimbursements and its possible effect on participant administrative fees. A draft policy was also prepared and presented for the Board's consideration. Ms. Pauls reviewed the anticipated administrative fee changes tied to possible implementation dates, which included delaying reimbursements directly to the participants in the funds providing the reimbursements until the Board's administrative account reaches its target balance of 100% of annual plan expenses, or implementing participant reimbursements effective January 1, 2016. She also suggested that the Board may wish to expand the fee structure, which currently tops out with those account balances of $100,001 or greater paying $66 per year.

Historically, participant administrative fees are reviewed annually at the March or June Board meeting for the following year. Changes to the fee structure were last made in 2008 and staff anticipates this topic will be part of the next Board meeting in June 2015.

The Board requested that Ms. Pauls return with an expanded fee structure proposal using an anticipated implementation date of January 1, 2016. An effective goal date of January 1, 2016 for an upcoming administrative fee changes, would provide Empower Retirement with six months to execute a communication plan and discuss any fee changes with participants.

The Board also asked the Department to reexamine the reserve target for the Board's administrative account as to what is adequate and ETF's historical experience. The Board would consider changing the 100% funding target for administrative fees to a different goal, and requested estimates for 50% funded and 75% funded. Currently, the account is at 71% funded.

No Board action was taken at this time. Revising the policy target goal to state that the Board's goal is to have 100% annual expenses in the account was also deferred pending additional analysis.

POLICY PROPOSALS

Ms. Schueller referred the Board to the memo (Ref. DC | 3.12.15 | 9) presenting two policy proposals for discussion and consideration. Upon approval, these documents will be included in the *Deferred Compensation Board Governance Manual*.

1. Conduct of Board Meetings
2. Vendor Procurement Appeals

> ***MOTION: Ms. Hanson moved to approve the proposed policies as presented. Mr. Nelson seconded the motion, which passed unanimously on a voice vote.***

2014 PLAN ENHANCEMENT PROGRAM (PEP) YEAR IN REVIEW AND 2015 ADMINISTRATIVE FEE CHANGE

Ms. Schueller presented a recommendation to increase the annual fee paid to Empower Retirement of 3.7%. (Ref. DC | 3.12.15 | 10) Empower Retirement has met all the goals in the 2014 PEP and did very well in adding participants and new employers.

Ms. Oelke reviewed and discussed the final results of the 2014 PEP scorecard. In 2014, goals were established for four PEP areas: participation, asset allocation, education and learning and retiree outreach. As outlined in the Administrative Services Contract, if WDC participant growth is greater than 3.0%, the fee increases 3.0%. The number of participating employees increased by 4.1% which was above the goal for increasing the number of participants. The goal of adding 8 new employers was also exceeded with 18 new employers adopting the WDC in 2014. The additional 0.7% increase was achieved by Empower Retirement meeting all the Board's objectives as defined in the annual PEP.

> ***MOTION: Mr. Nelson moved to approve a 3.7% increase in the annual administrative fee paid to Empower Retirement. Ms. Hanson seconded the motion, which passed unanimously on a voice vote.***

STABLE VALUE FUND

Ms. Schueller discussed the possible Stable Value Fund trustee fee increase by Wells Fargo, as presented at the November Board meeting by Galliard Capital Management (Ref. DC | 3.12.15 | 11). After a review of the existing contract, the Department and Galliard agreed that the trustee fee could not be implemented as originally proposed. ETF's legal and procurement staff are working with Galliard to revise and update the contract. It will be presented to the Board for review at a future meeting.

SOCIALLY RESPONSIBLE FUND OPTION REVIEW

Ms. Schueller discussed the socially responsible fund review that Bill Thornton provided for the investment committee outlined in the memo (Ref. DC | 3.12.15 | 12). Mr. Thornton detailed his fund search based on the criteria of the Board's Investment Policy Statement. The challenge in the socially responsible arena is that investment fund performance is generally compared to a fund's peer group, in this case other socially responsible funds. There are 20 funds that would pass the criteria of the Socially Responsible Fund. Mr. Thornton will do more research in this area for the next investment committee meeting. The Board needs to consider various details, such as whether they would like to offer an index fund or an actively managed fund. Both Calvert funds discussed at the meeting (active and index) have the same social screening standards but the index fund costs less.

DC BOARD GOVERNANCE MANUAL UPDATE

Ms. Schueller referred Board members to the memo (Ref. DC | 3.12.15| 13) that provides the list of the *Deferred Compensation Board Governance Manual* materials recently-updated. Electronic copies are available on the Department of Employee Trust Funds' website and paper copies will be available upon request.

OPERATIONAL UPDATES

Ms. Schueller referred Board members to the materials under the "Operational Updates" section in the meeting materials for routine reports and additional information and news from the WDC's investment providers. (Ref. DC | 3.12.15| 14).

FUTURE ITEMS FOR DISCUSSION

With regard to the Financial Statements Auditor Procurement, ETF is still waiting to hear from the CPA Review Board regarding a question with the lowest cost bidding firm. The 2014 audit is underway and Ms. Schueller expects that the auditing firm will have the draft report available for the Board's consideration in June.

In June, the Board will also be reviewing the Administrative Services Contract. The current contract runs through November 2015.

Ms. Hanson complimented the Board on its selection of investment options. She noted that in her experience, it is highly unusual when a board does not have to change a fund due to poor performance. Mr. Thornton also recognized the Board for its careful and regular reviews of performance because on a weighted basis, the WDC is one of the lowest cost plans in the country.

ADJOURNMENT

> ***MOTION: Mr. Nelson moved to adjourn. Ms. Hanson seconded the motion, which passed unanimously on a voice vote.***

The Board adjourned at 2:35 p.m.

Date Approved: ___________________________

Signed: ___________________________________
Gail Hanson, Secretary
Deferred Compensation Board

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CORRESPONDENCE / MEMORANDUM

DATE: February 11, 2015

TO: Deferred Compensation Board Members

FROM: Shelly Schueller

SUBJECT: February 10, 2015 Investment Committee Meeting Notes

1. Bob Lawler of Vanguard joined the Investment Committee by teleconference to discuss a new investment class option for the Target Date Retirement Funds. The WDC could move from the existing mutual fund options to collective trusts options. The collective trusts offer the identical investment approach as the Vanguard Target Date funds (including glide path and target allocation). The appeal of changing to collective trusts is the lower cost than mutual funds. The Vanguard Target Retirement Date Funds offered through the WDC have expense ratios ranging from 16 to 18 bps (basis points). If the Target Retirement Date funds were converted to collective trusts, the expense ratios would drop to 8.25 bps.

   Although moving to collective trusts would eliminate some transparency currently provided by offering the retail mutual fund versions of the Target Date funds, this change would be consistent with the Board's policies regarding offering low-cost options and should result in better returns for participants.

   The Investment Committee asked several questions of Vanguard, including requesting that Vanguard make the annual audited financial statements for the collective trusts available for posting on the WDC website. Vanguard agreed to provide this, along with performance information, on a regular basis.

   The Investment Committee requested certification or documentation from Vanguard that the Target Date collective trusts are subject to compliance regulations similar to those under which the mutual funds operate, and also requested a statement regarding the level of risk in collective trusts relative to the mutual fund versions of the target date funds. The committee is interested in learning where compliance requirements are different and how Vanguard addresses these differences. Vanguard agreed to follow-up on these requests and report back to the Board.

   If Vanguard can provide documentation or certification indicating the regulatory compliance requirements and risk of the target date collective funds are similar to the mutual fund versions, and this information can be included on the WDC website for participants, then the Investment Committee will recommend the Board consider changing the Vanguard Target Date offerings from mutual fund options to collective trusts.

2. The Investment Committee discussed the investment performance results as of December 31, 2014, with Bill Thornton of Advised Assets Group. The Investment Committee heard from Mr. Thornton that the performance of the Calvert Social Investment Equity Fund improved during the last quarter of 2014. Mr. Thornton also noted that the Fidelity ContraFund three year quartile performance during the last quarter of 2014 can be viewed as an anomaly, because of how Morningstar calculates mean and median between categories. Mr. Thornton said he was not concerned with the performance of either of these funds, or the other funds in the WDC's core lineup. No changes to the status of the current lineup of investment options were recommended. Mr. Thornton noted that the WDC has an extremely low asset-weighted average expense ratio of 0.29%, which could be further lowered if the Board decides to change to the Vanguard Target Date collective trusts. Finally, Mr. Thornton pointed out a new page in the review book (page 41), which is a graphic illustration of the target date funds' glide path, equity diversification and fixed income diversification relative to the industry max/min and average.

3. The Investment Committee reviewed a presentation by Mr. Thornton regarding potential replacement options for the WDC's socially responsible offering (Calvert Social Investment Equity Fund, ticker symbol CEYIX). The CEYIX fund meets the Board's investment policy statement criteria, but its performance has lagged over the past 18 months. Mr. Thornton's analysis included a review of the non-economic principles used by most firms offering socially responsible investments, a review of the socially responsible funds in the Morningstar database and the Board's Investment Policy Statement criteria that pertain to fund searches. The results of this are that approximately 20 funds might be appropriate replacement options, including a Calvert Social Index fund.

   The Investment Committee requested additional detail regarding the differences between the CEYIX and Calvert Social Index fund holdings and level of social responsibility, which Mr. Thornton will research and provide. The Investment Committee also asked for continued monitoring of the CEYIX fund's performance, but determined that no changes to the WDC's socially responsible fund option are necessary at this time.

4. Staff noted the January 2015 Galliard Update regarding PIMCO was provided for information only. Galliard continues to monitor the personnel changes and performance at PIMCO as PIMCO remains on Galliard's "watch" list, but Galliard is not expecting any changes at this time.