

Washington State Department of Retirement Systems

Employee Retirement Benefits Board

Regular Board Meeting February 19, 2008 Minutes

Chair Sandy Matheson called the meeting to order at 9:30 am. Board members present: Claude Burfect, Michael Coleman, Dorothy Kiest, Robert Lenigan, Judi Owens, Al Symington, Brian Talbott, Staci Vesneske and Kathy Whitlock.

Staff/resource personnel present: Assistant Attorney General Lara Zimmermann, Kris Heurich, Joe Dear, Bill Kennett, Jeff Wickman, Cathy Cale and Wilma Eby. (Names of other attendees are not included in the minutes but are listed in the permanent record.)

A-1 Approval of Meeting Minutes - December 11, 2007

Robert Lenigan made a motion, seconded by Michael Coleman, to approve the December 11, 2007 meeting minutes as submitted. The motion passed unanimously.

Public Comment:

Ben Walker, Jeremy Houy and Bill Zehner from First Investors spoke to the board about their investment product and proposed that it be offered to Plan 3 participants.

Nyle Soper provided comments about the Plan 3 self directed investment program trading restriction and requested an example and explanation of the 30-day restriction. Mr. Soper also requested that the board consider easing the trading restriction on the Money Market fund to 10 or 15 days.

Status Reports

B-1 Record Keeping Program Update

Kris Heurich, Senior Vice President, ICMA Retirement Corporation (ICMA-RC) provided a status report of the record keeping and education services for the Plan 3 programs. Ms. Heurich reported a 16 percent increase in member contacts to ICMA-RC in 2007 compared to 2006 and a 6.2 percent increase in membership. The majority of the contact increase was via the Internet, and 87 percent of fund transfers in the self-directed program were completed online. Compared to 2006, she reported an increase of 15 percent in the number of fund transfers. The dollar impact of those transfers was approximately \$19 million moving into the International Fund, and an increase in the Bond Fund of approximately \$8 million. Approximately \$26 million moved out of the Small Stock Index and \$26.7 million moved from the self-directed program into the Washington State Investment Board (WSIB) Total Allocation Portfolio (TAP). She reported a 24 percent increase in the number of seminars held throughout the state with an 18 percent increase in attendance. Ms. Heurich also reported that due to the market volatility, ICMA-RC received over 1,000 more calls in January 2008 compared to January 2007 with nearly \$15 million moving between investment options.

B-2 Defined Contribution Plans Investment Performance

Joe Dear, Washington State Investment Board (WSIB) Executive Director, provided an investment report for the Plan 3 and Deferred Compensation programs for the quarter ended December 31, 2007. He reminded board members that although the fourth quarter saw lower returns, the investment programs offered by the WSIB are high quality portfolios built to weather the ups and downs of the market and should be viewed over the long term. He reported asset totals for the Teachers' Retirement System (TRS) in excess of \$4 billion, the School Employees' Retirement System (SERS) just over \$1 billion, the Public Employees' Retirement System (PERS) at nearly \$1.4 billion and the Deferred Compensation Program (DCP) at \$2.5 billion. Investment returns for the Plan 3 indexed funds are within a tracking error of performance and are performing as expected. The Social Balanced

Fund performance on a one year basis turned around significantly and is outperforming its benchmark. For DCP he reported significant underperformance by the Active Value Fund and the Active Core Fund.

Board member Staci Vesneske asked about the real estate market volatility and its impact on the TAP fund. Mr. Dear responded that both real estate and private equity support the value of the TAP fund. Although he expects the value to move, it won't move as fast because the assets are not valued every day. He stated the TAP fund has very little exposure to residential real estate but has apartments and manufactured housing community sites. He expects that those markets will do relatively well because manufactured housing and apartments are the affordable housing option for many people.

Mr. Dear provided information on the selection of a target date fund manager. He reported that the State Investment Board will likely accept the recommendation from the Public Markets Committee at the next board meeting for Alliance Bernstein as fund manager for the target date funds. Studies show that on a national average 80 percent of defined contribution participants do not make changes to their investment strategy after making their initial investment decision. Target date funds allow for automatic rebalancing and changing the asset mix as the individual moves closer to retirement. An important part of the fund change is participant education. If participants don't change as a result of this new option, they won't realize the benefit. Mr. Dear stated the WSIB is deferring to DRS for participant education and the initiation date of the target date funds.

B-3 Defined Contribution Plans Activity Report

Jeff Wickman, Senior Assistant Director of Policy at the Department of Retirement Systems (DRS), reported that the gain sharing payments were posted to Plan 3 member accounts on January 2, 2008. 120,716 Plan 3 members and retirees received a gain sharing payment with the average payment equaling approximately \$2,647 per person.

He also reported that in January, during the extreme market fluctuations, DRS received some inquiries from Plan 3 members, DCP participants and Legislators about the trading restrictions DRS and the Washington State Investment Board adopted in 2006. DRS responded to these questions by reminding members and participants of the value of investing for the long term. In particular, it's time in the market, rather than timing the market, that can allow investors to benefit from and avoid the risks of the stock market. Director Sandy Matheson distributed a memo to ERBB members about the history, decision process and reasons why the trading restrictions were implemented.

B-4 Plan 3 Pension Legislation Report

Jeff Wickman also provided information about proposed pension legislation impacting the Plan 3 programs.

- HB 3024/SB 6656 - TRS Out of State Service Credit. A TRS Plan 2 or Plan 3 member can currently purchase up to seven years of service credit for public education experience earned outside the Teachers' Retirement System (TRS). To make the purchase the member must have five service credit years in TRS. This legislation reduces the number of service credit years from five to two years in order to be eligible to purchase the out of state service.
- HB 3005/SB 6655 - PERS to SERS Auto Transfer. Beginning September 1, 2000, Public Employees' Retirement System (PERS) Plan 2 members hired into a position eligible for membership in the School Employees' Retirement System (SERS) have their PERS service automatically transferred to SERS. This legislation ends this automatic transfer for members employed in an eligible SERS position on or after July 1, 2008. From September 1, 2008 through November 30, 2008, members and former members of PERS Plan 2 who had service credit transferred to SERS Plan 2, may request, in writing, to have that service credit transferred back to PERS Plan 2 if; 1) The member or former member did not earn service credit with a school district or educational service district before the transfer; and 2) The member or former member has not transferred to SERS Plan 3 or PERS Plan 3.
- HB 3019/SB 6654 - TRS and SERS 2/3 Half-Year Contracts. This bill grants six months of service credit to members of Teachers' Retirement System (TRS) and School Employees' Retirement System (SERS) Plan 2 and 3 who work for at least five months of a six-month period, from September through August, and earn 630 hours or more within that six-month period.

Additional information about pension legislation is available at www.drs.wa.gov/legislative/.

Presentation

Bill Kennett, WSIB Fixed Income Senior Investment Officer, provided an overview of the Fixed Income investment program. He reported approximately \$26 billion in assets under management. The program unit has 10 staff members including portfolio managers and traders, credit and securitized analysts and database and risk management. Fixed income is debt obligation in the form of a security; the borrower pays interest and promises to pay back the debt at maturity. The WSIB manages Fixed Income portfolios for retirement, Labor and Industries, the Deferred Compensation Program, the Guaranteed Education Tuition Program and the Developmental Disabilities Endowment Fund. Mr. Kennett reported that Fixed Income risk components include interest rate risk - a change in interest rates means a change in market value, credit risk – change in spread changes market value, and structure risk – change in when payments are received changes market value and changes duration. He stated that the greater a bond's duration, the more its price will change for a given change in yield. Fixed income return components are price return, coupon return and paydown return. The Fixed Income goal for the retirement funds is to meet or exceed the performance of the Lehman Universal Index and to provide diversification.

Board Report

D-1 May 27, 2008 – Tentative Agenda

Chair Sandy Matheson reviewed the proposed agenda for the May 27, 2008 meeting.

With no further business, the meeting adjourned at 11:15 a.m.

Approved:

Sandra J. Matheson