

Washington State Department of Retirement Systems Employee Retirement Benefits Board

Regular Board Meeting September 22, 2009 Minutes

Chair Steve Hill called the meeting to order at 9:35 am. Board members present: Claude Burfect, Michael Coleman, Carol Jensen, Dorothy Kiest (by phone), Judi Owens, Staci Vesneske and Kathy Whitlock.

Staff/resource personnel present: Assistant Attorney General Anne Hall, Kris Heurich, Phil Paroian, Diana Will, Marcie Frost, Jeff Wickman, Cathy Cale, Brian Berghoff and Wilma Eby. (Names of other attendees are not included in the minutes but are listed in the permanent record.)

A-1 Approval of Minutes – May 26, 2009

Michael Coleman made a motion, seconded by Kathy Whitlock, to approve the May 26, 2009 meeting minutes as submitted. The motion passed unanimously.

Public Comment:

John Kvamme, representing School Principals and School Administrators, and Doug Nelson, representing Public School Employees of Washington/SEIU 1948 requested support from the board for another request to the Internal Revenue Service (IRS) to grant contribution rate flexibility for Plan 3 members of the Public Employees' Retirement System (PERS) and School Employees' Retirement System (SERS). In 2002, when Teachers' Retirement System (TRS) Plan 3 was submitted for plan qualification, the IRS approved an annual window for TRS Plan 3 members to change their contribution rate. However, a few years later the IRS did not grant the same flexibility for the PERS and SERS plans when those plans were submitted for plan qualification.

Mr. Nelson is currently meeting with Washington State congressional members to discuss a federal legislative effort. Board members Judi Owens and Staci Vesneske provided comments in support of another request for rate flexibility. Board member Dorothy Kiest commented that she is in opposition of the rate flexibility if it impacts plan qualification.

Jeff Wickman and Anne Hall responded that the department again discussed this issue with tax counsel Ice Miller when the plans were resubmitted for qualification. Tax counsel's advice was that they did not sense that the IRS position on granting flexibility has changed.

Judi Owens made a motion, seconded by Michael Coleman, that this board draft a memo to the Department of Retirement Systems asking them to submit a letter in support of the flexibility on our contribution rates for the SERS plan. The motion passed with six affirmative votes, one opposed.

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 services for the Plan 3 programs as of August 31, 2009. She reported a definite trend downward in contacts from Plan 3 members, most likely due to account fatigue and the fact that members who wanted to make account changes probably did so at the beginning of the market downturn. She noted that the most active time for internet activity by members is on Mondays between 6:00 and 7:00 a.m. For contacts to the Call Center, the average wait time for a phone call to be answered by an ICMA-RC customer service representative is 16 seconds. The top four topics are status of withdrawals, internet and password assistance, initiating program transfers and options for withdrawal. She noted that they get a few calls each month from members asking about contribution rate flexibility.

Ms. Heurich reported an increase in 2009 in money being transferred into the bond fund and moving from the money market fund to other funds. They are seeing an increase in dollars into the Retirement Strategy Funds. Approximately \$52 million moved from the TAP fund to the self directed program.

B-2 Defined Contribution Plans Investment Performance

Phil Paroian, Washington State Investment Board (WSIB) Senior Investment Officer of Public Equity, provided an investment performance report for the period ending June 30, 2009. He noted the second quarter 2009 is one where investors were cautiously relieved – with a sense that the markets turned at the end of March. The sharp decline in the last quarter 2008 and first quarter 2009, followed by one of the sharpest eight-week increases in the second quarter 2009 again confirmed the impossibility of timing markets.

Mr. Paroian noted that generally the Plan 3 equity and cash funds performed very closely in line with the market. While the Total Allocation Portfolio (TAP) underperformed for the quarter, the longer term performance for the TAP fund has been very strong. Diana Will, WSIB Senior Investment Officer - Asset Allocation, noted that the private market pricing in the TAP happens quarterly with a one-quarter lag. As a result, the fund may lag during rising markets because the private market portfolios do not yet reflect the most recent quarter's increase.

B-3 Defined Contribution Plans Activity Report

Jeff Wickman, Department of Retirement Systems (DRS) Assistant Director of Policy and Strategic Initiatives, reported that the department completed the evaluation of bids for third party record keeping services for both Plan 3 and the Deferred Compensation Program (DCP), held interviews with companies recommended by the evaluation team, and is now conducting site visits. The department determined in the evaluation process that a separate vendor will be hired for each program. The date for announcing the apparently successful respondents is September 28, 2009. The projected effective date for new contracts is January 2010.

Mr. Wickman also reported that the department is working with the State Investment Board and AllianceBernstein to add a 2055 Retirement Strategy Fund effective January 2010. When the original Retirement Strategy Funds were implemented, they included 11 funds or vintages in five year increments beginning with the 2000 fund and ending with the 2050 fund. This approach was

based on the demographics of the Plan 3 and DCP membership. The 2055 fund will be appropriate for Plan 3 members and DCP participants born in 1988 or after. Although no one will be automatically mapped to the new fund, the department will communicate directly with individuals who may fit the demographic for the fund.

Presentation

C-1 Plan 3 and DCP Lower Risk Investment Options

Phil Paroian provided information on the lower risk investment options available for Plan 3 members and DCP participants. Plan 3 offers a money market fund, DCP has the savings pool and both plans offer the bond fund. The presentation was made to the board in response to a DCP participant's request for a Treasury Inflation-Protected Securities (TIPS) investment option.

Money market funds invest in lower-risk securities such as commercial paper, government securities and certificates of deposit. Money market funds are not insured, but are closely regulated by the Securities and Exchange Commission and are generally considered very safe investments. In line with lower risk, longer term returns on money market funds are usually modest when compared to other types of investments.

The Savings Pool has interest-bearing contracts (GICs) bought from insurance companies. The contracts have a guarantee, by the insurance company, that the principal and interest payments will remain stable for a certain amount of time, regardless of market conditions. While the GICs are not insured, they are first in line to get money back should one of them go into bankruptcy. The goal of the savings pool is to earn a return similar to intermediate fixed income bonds but without the market volatility.

The Intermediate Bond Fund primarily invests in corporate bonds, but has the ability to invest in U.S. government bonds. The fund is not insured and has interest rate risk (as interest rates rise, bond prices usually fall), the risk of issuer default and inflation risk. The fund is designed to provide higher returns than money market funds, but bears less risk than long-term bond funds.

TIPS are marketable securities, where the principal is adjusted by changes in the Consumer Price Index. The coupon is a fixed rate and the principal grows or decreases with inflation. The bonds have the full backing of the U.S. government, but most funds are not insured and still have interest rate risk. Over the long run, TIPS are expected to offer a lower return than credit bonds. Mr. Paroian noted that most people don't realize that they will not earn inflation plus a fixed spread on a year-to-year basis. The market value fluctuation is higher in TIPS than the Daily Bond Fund. In the DCP the GIC's normally have a non-compete clause and would mandate a 90-day equity wash if a TIPS fund was added.

Mr. Paroian reported that at the end of 2009 and into 2010, the WSIB will do a comprehensive review of the investment options for Plan 3 and the Deferred Compensation Program. The review includes the number and type of options, along with the managers and fund structure. For anyone interested in the subject of the optimal number of investment options to offer, how to design a menu of options and the field of behavioral economics, Chair Hill recommended reading the book *Nudge: Improving Decisions About Health, Wealth and Happiness*, by Richard Thaler and Cass Sunstein.

New Business

D-1 Board Operations Policy

Chair Hill presented the draft Board Operations Policy. As a result of the quorum issue raised at the May meeting, Assistant Attorney General Lara Zimmermann recommended development of an operations policy that includes specifics about the quorum.

Judi Owens questioned whether the votes of members attending by conference call are counted in the total for quorum purposes. Assistant Attorney General Anne Hall responded that members may attend in person or by electronic means.

Judi Owens made a motion, seconded by Claude Burfect, to approve the Board Operations Policy. The motion passed unanimously.

Board Report

E-1 December 8, 2009 – Tentative Agenda

Chair Steve Hill reviewed the proposed agenda for the December 8, 2009 meeting. He noted that he will give consideration to the December meeting being an electronic meeting. With no further business, the meeting adjourned at 10:40 a.m.

Approved:

Steven R. Hill
Chair