

DEFINED CONTRIBUTION PLANS TRUSTEE MEETING MINUTES
Wednesday, February 22, 2017

The SPSP/401(k) Trustee Board of the City of San Diego held its regularly scheduled meeting in the SDCERS Boardroom. Location: 401 West A Street, 3rd Floor Boardroom, San Diego, California. The meeting was called to order at 1:39 p.m. by Estella Montoya.

Trustees Present: Julio Canizal, Robert Davis, Mark Hovey, Tracy McCraner
Trustees Absent: Gail Granewich
Staff present: Bill Gersten (left meeting at 3:00 p.m.), Estella Montoya, Gilda Smith, Nancy Stadille
Presenters: Chad Breunig (Wells Fargo IRT)
Denise Jensen (Wells Fargo IRT)
Jonathan Scharmer (Wells Fargo IRT)
Bill Cottle (Milliman)

1. ACTION ITEMS

- A. Dispense with the reading and approval of the minutes of December 14, 2016.

MOTION TO ACCEPT THE MINUTES OF DECEMBER 14, 2016: Mark Hovey
SECOND: Julio Canizal
Approved (3-0, Ms. McCraner abstained)

- B. Approve revised Investment Policy Statement.

Mr. Canizal commented the error on page 1, last paragraph needs to be corrected.

MOTION TO ACCEPT THE INVESTMENT POLICY STATEMENT WITH CORRECTION:
SECOND: Mark Hovey
Robert Davis
Approved (4-0)

2. STAFF REPORTS AND INFORMATIONAL ITEMS

- Wells Fargo Regulatory Compliance Program

Mr. Breunig introduced himself as the Senior Vice President, Director of Fiduciary and Regulatory Support Services. Mr. Breunig reports to Joe Ready. He began his presentation on page 3 stating there are four areas of risk management. The first area, line of business risk management teams, works with day-to-day processes to protect Wells Fargo, follow policies and procedures, and provide credible challenge. They have a seat at the table for every business decision that gets made. Compliance is the second area. The first line audit reviews 40-50 samples. Compliance pulls 90-100 samples. Office of the Comptroller of the Currency (OCC) is their regulatory agency. They interpret policies and procedures and help draft policies. The group operational risk management team is focused on privacy, record retention, and external and internal information security. Plan participants are not the customer, they are beneficiaries of the trust. The plan sponsor is the customer. Lastly, investment risk management looks at following investment guidelines.

Mr. Breunig proceeded to page 4 and reviewed the Wealth and Investment Management (WIM) risk structure. He stated FLoD and SLoD are the acronyms for first line of defense

and second line of defense, respectively. There are a myriad of controls; no one individual can move money, distribute money, or change investments. The third line of defense is audit. Regulatory compliance risk management are corporate committees that set forth policy and procedures for the organization. They ensure adherence to enterprise-wide regulatory compliance framework policies and procedures. There are corporate committees that set forth the policies for the organization. There are areas where the law may allow but Wells Fargo does not want to do business. For example, there are areas where marijuana is legal. However, Wells Fargo has a policy where they do not do work with companies that have any involvement with the marijuana industry. There are business that support businesses in the marijuana industry. For example there are mortgages or 401(k) plans for companies that own strip malls that lease property to marijuana selling businesses in legal states. That gets to be a very difficult situation for these Wells Fargo committees to navigate.

Mr. Breunig continued to inform that each line of business has dedicated and independent compliance and risk. OCC reviews various aspects of their business on a regular basis. Wells Fargo is on a first name basis with the OCC. The OCC is consistently reviewing their processes. Page 7 displays the various committees of retirement. If Wells Fargo wanted to introduce a new product, for example an advice product within 401(k) plans, it would first have to be approved by the Product Steering Committee. The committee is made up of individuals from risk, compliance and the business. If approved, then up through the chain to the IRT Trust Oversight & Risk Committee which is staffed with more senior levels of risk and compliance, legal, and audit. Ultimately it must be approved by the Compliance and Operations Risk Committee. This committee is exclusively risk and compliance; there are no business folks on the committee.

Page 9 discusses how within the line of business there is training for each employee to raise their hand if there is an area of risk. With the concerns on the banking side people have raised their hands with concerns about the IRT's sales practices. Mr. Breunig stated the good news is within reviewing their structure, it was pretty good but there were areas of improvement and modifications were made. Mr. Hovey asked Mr. Breunig, based on the recent concerns on the banking side, what changes have recently taken place? Mr. Breunig replied, for example Wells Fargo provides distribution consulting when a participant calls the Retirement Service Center. It used to be when a participant wanted to talk about an IRA rollover, the participant was handed over to Wells Fargo advisors and the service representatives were compensated on referrals. Though legal, it doesn't look right. Wells Fargo IRT changed their compensation structure. The compensation structure has changed for the people selling IRAs. Wells Fargo wants to move away from the perception of pushing products and increase perception of getting participants to the right place and it may not be a rollover to an IRA. Mr. Hovey stated banking was incentivized to do what they did. Mr. Breunig replied in community banking there was an overwhelming pressure to do what they did.

Mr. Hovey asked if the organizational structure has changed due to the community banking situation or has this structure been in existence. Mr. Breunig stated Wells Fargo started a complete review of the risk management and compliance structure a year and half ago. The community banking situation probably accelerated some of it. Ms. Stadille informed the Board that City participants are not directed to advisors for IRAs. Mr. Breunig agreed with Ms. Stadille and advised that City plan participants are not customers and therefore without explicit direction from the plan sponsor, they are unable to sell products to the employees. Mr. Breunig stated that about half of Wells Fargo clients want employees to be directed to advisors for distribution consulting. He explained that the call center staff was unable to answer difficult questions about tax implications. So, they

wanted to develop an expertise group to answer the difficult questions instead of sending those employees to advisors. They are going to do more dialogue within the retirement group and veer away from discussing IRAs. Unless the participant specifically states they want to discuss IRAs. There is a lot of movement. The changes are in part due to community banking, the evolution of business, and also legislation and regulations that keep altering. Ms. McCraner wanted confirmation from Mr. Breunig that City plans are a part of the Wealth and Investment Management and not Community Banking. Mr. Breunig confirmed the City is a part of Wealth and Investment Management and he explained that Community Banking is completely separate from Wealth and Investment Management. Ms. McCraner inquired if Community Banks and Wealth and Investment Management used the same structure. Mr. Breunig stated he was unable to speak for Community Banks. He speculates they are similar but is unsure.

Ms. McCraner asked if the internal audit group that comes in after compliance are truly the Wells Fargo structure. Mr. Breunig stated that they are the audit group and they are a part of a corporate audit team that is not in the business. Ms. McCraner asked Mr. Breunig if he had KPMG or OCC audits. Mr. Breunig stated that KPMG comes in every year and does the SSAE 16 report. The people that can review the same function are called the second line of compliance testing group. They test their controls, internal audit test their controls, the OCC test their controls, and the KPMG group tests their controls, and on occasion the Department of Labor will come in and test their controls. The Department of Labor doesn't focus on the operations of recordkeeping like everybody else. The Department of Labor looks for fiduciary activity, investments, how is the money held, and reviews if they are doing the right thing.

Mr. Breunig stated that the conflict of interest rule (page 11) has been in the news a lot. He continued to advise that it is supposed to be enforced on April 10, 2017. Once the rule is final there needs to be additional rule-making, legislation or legal action to repeal. The Department of Labor introduced a proposed rule, sent it to the OMB (Office of Management and Budget) with a delay. No one knows what the delay is and the OMB can take up to 90 days to decide. Wells Fargo IRT is already dealing with ERISA and they are moving forward with the rule in place. This rule caused Wells Fargo IRT to revisit what information they tell the participants and how they educate them. This rule expanded investment education, such as identifying funds that fit asset allocation categories. Mr. Breunig explained they will only offer advice when hired by the plan sponsor to do so. There are minor changes to sponsor interaction. Plan sponsors with more than \$50 million in AUM (assets under management) are excluded from the rule, they can provide broad reaching investment consulting services, and they must comply with certain disclosures and agreements. Plan sponsors with less than \$50 million in AUM that have engaged an investment fiduciary are excluded from the rule. They can also work with investment consultants to provide services and they must comply with certain disclosures and agreements. Plan sponsors with less than \$50 million in AUM and no investment fiduciary have a limited investment service offered, broader assistance with fund placement dialogue, and fiduciary services are available for a fee. The good news is that the Department of Labor recognizes that plan sponsors are not implicated by the rule. The bad news is that it makes it easier for participants to sue for breach of fiduciary duty. ERISA fiduciary standard of care is the highest under the law. Mr. Breunig advised that it is important for plan sponsors to know who their providers are and what they are agreeing to provide.

- Fourth Quarter Activity Report–Wells Fargo

Ms. Jensen began by providing a brief overview. She advised there was positive plan growth from December 31, 2015 through December 31, 2016. The Plans are above the billion dollar mark. There is a decrease in outstanding loans and outstanding loan amounts. There has been a significant increase in plan-to-plan transfers in 2016. A little over \$5.5 million in assets went over to SDCERS. The average balances in all four plans has increased year over year. The participant headcount increased in the 401(k), 401(a), and the SPSH-H. The participant head count has decreased in the SPSP. Ms. Jensen stated that the plan change that allowed terminated participants to rollover funds into the 401(k) was a positive change. She explained that two participants took advantage of the new policy and rolled funds from SDCERS into the 401(k). Those plan transfers are bringing more money into the plan which gives the City more leverage from an investment and vendor perspective.

- Education update–Wells Fargo

Mr. Scharmer went over the current state of the savings plans (page 19). He advised that he changed the metrics to include three years of results for all of the metrics that he is reporting. He explained that it is powerful to see the trending and everything is moving in a positive direction. Mr. Scharmer advised the City had about 36 average logins and their book of business ranges from four to 52 with an average of 19 logins. This shows that City participants are more digitally engaged than the average plan. The number of participants that elected to receive e-statements has increased to 11,234, which is a 27% increase in 2 years. The 401(k) plan participation has grown, there is an 8% increase. The beneficiary designation continues to increase on the Wells Fargo side. Mr. Scharmer stated that all participants may also add beneficiaries through SAP Self-Services and he does not have the information. Diversification continues to grow which is good. Mr. Scharmer highlighted the average contribution amounts that the participants contributed into each plan. Ms. McCraner asked for verification and Mr. Scharmer provided an example: 30% of the 401(k) contributions are going into the Managed Income Fund. He explained that the amount of funds in the Managed Income Fund is trending down. Mr. Scharmer advised that diversification means that the participant is in the Vanguard Lifestyle Fund or in three separate individual mutual funds in the plan.

Mr. Scharmer advised they continue to host a monthly webinar and virtual events. He explained that last year 107 employees attended those. He advised they are continuing to promote the webinars internally, sending emails, and promoting on the website. There was a campaign that promoted designating beneficiary designations which engaged about 1,900 city employees. Mr. Scharmer advised there were about 52,000 engagements with the participants which includes, emails, personalized communications, that is targeted based on the information they know about the participant and the events that are taking place throughout the year. There was a 19% open rate for those communications. A new goal for 2017 is increasing satisfaction and trust with Wells Fargo. Mr. Scharmer advised that if City employees' value and trust Wells Fargo IRT they will be more likely to read communications, value and take note of communications, and ultimately take action. Mr. Scharmer went over the steps that Wells Fargo IRT does to help drive and shape that strategy. They compile data from annual surveys (retirement surveys, consumer confidence survey, millennial survey) and segmented studies. They all help in understanding what Americans are looking for, struggling with, how they want to be interacted with. All of that knowledge shapes the direction Wells Fargo IRT takes with education.

Mr. Scharmer explained they also speak to internal team members that do education sessions, relationship managers, and clients to see what is happening in their businesses. Ultimately, this shapes when, where, and how they communicate with participants. One of the things that came from this was the triggered communications. Those are the engagements that are sent while the participant is taking actions within the plan. Mr. Scharmer advised that they know from their millennial studies that millennials like to have confirmation of their decisions and part of the studies shows that they are more likely to take action. Ms. McCraner inquired if Mr. Scharmer knew how many millennials were contacted to participate in the survey and how many of them responded. Mr. Scharmer advised it was 1,000 or more, and they also have focus groups. He stated that he did not have the exact numbers but he would be able to provide them at a later date. He explained they will continue with the webinars because they have been successful and they are going to broaden them with additional virtual events. A couple webinars will have chat rooms where questions can be asked to experts, and work with resource groups, as well as download learning materials to their laptop or tablet.

Mr. Scharmer explained that messages need to be more holistic and include more than just retirement information. There will be a powerful webinar in May (Credit: The good and the bad). The reason being, so few people know how impactful their FICA score is. If they don't know what their score is or don't know how to influence it or if they don't know how it impacts them, they are missing out on a lot of information that is going to drive not just retirement but financial wellbeing. Throughout the year participants will see the mailer components. Early in the year, they will try to influence 401(k) participation with a drip campaign. He advised first they will send information about a pre-tax benefits. They will send a second communication about starting to save for retirement early and the impact of early retirement savings. Once someone enrolls into the 401(k), they are pulled out of the drip campaign. Mr. Canizal inquired on the effectiveness of the drip campaign. Mr. Scharmer advised that he can see when someone enrolls in the 401(k) and he will be engaging the participants that are not enrolled and measure what percent of them started contributing into the 401(k). Mr. Canizal inquired if that information can be provided to the Board. Mr. Scharmer confirmed that he will provide the percentage of the participants who began contributing to the 401(k). Mr. Scharmer advised that if this campaign was successful the City may want to begin engaging the low 401(k) contributors and help influence a larger contribution rate. Ms. Stadille advised that before, the City had limited Wells Fargo's access to campaigns but now we are allowing Wells Fargo to proceed with campaigns. Mr. Scharmer advised that because the amount of loans and loan balances are going down, this shows that this is a good time to save. Mr. Scharmer stated they also want to help participants that are SDCERS eligible and how to input that information into the website dashboard and utilize the tools.

- Fourth Quarter Investment Report-Milliman

Mr. Cottle began by advising that the Boston Trust CEO has stepped down and relinquished his CEO responsibilities. The position will be filled by a three person executive committee, which will be comprised of Kenneth Scott, Bill Apfel, and Stephen Amyouny. Mr. Cottle advised this is a positive change for the firm.

Mr. Cottle reviewed the performance report beginning on page 1. Domestic equities continue to do to well. The domestic equities with higher risk levels had a great return. International equity did not do well. Bonds did not do well. Mr. Cottle referenced page 5, and discussed asset allocation. He confirmed the plans are over the billion dollar mark. Total assets at the beginning of the quarter was \$1,008,928,150. The quarter ended with \$1,031,542,230. The increase is made up of contributions of about \$7 million. Investment

gains is made up of about \$16 million. The level of loans declined. Asset allocations did not change significantly. On a percentage basis the Managed Income Fund came down. Mr. Cottle discussed page 7, the watch list. He advised that the Boston Trust Small Cap has been on watch for a long time and he believes it is appropriate to leave them on watch. Mr. Cottle explained that in the quarter there was a substantial return and it matched the benchmark. Oakmark Equity and Income Fund was put on the watch list and other organizations terminated them but he believes keeping them on watch was a good idea. He stated that Oakmark had an excellent quarter and the one-year return is above benchmark. BlackRock TIPS was put on watch and slightly outperformed in the quarter. Principal Mid Cap underperformed by about 2.5%. In reviewing their long term results, generally they are above the benchmark. Invesco outperformed and Dodge & Cox underperformed. Oakmark outperformed by 4% and the return was by 5%. The markets continue to do well domestically on the equity side. Mr. Cottle advised in his personal opinion, he believes that allocating more money internationally would be a smart decision. Mr. Cottle advised that it was a decent quarter even though some markets did not perform particularly well. Ms. McCraner asked Mr. Cottle why BlackRock was on watch. Mr. Cottle advised that they were placed on the watch list due to underperformance. They continuously underperformed and he thought it was appropriate to place it on watch. Mr. Canizal inquired for how long was BlackRock underperforming? Mr. Cottle referenced page 54 and went over BlackRock's annualized excess performance. He explained that we want the yellow line (annualized excess performance) above zero and trending upward. Recently, it has done ok, slight outperformance but for about two years it was poor. Mr. Hovey stated that BlackRock is in a good place going forward; inflation is picking up, Federal Reserve indicating rate increases. Mr. Cottle informed the Board there is a new member to the Milliman team, Mr. Jeff Nipp. Mr. Nipp will help Mr. Cottle with his future presentations.

- Disclosure of Economic Interests (Form 700)

Ms. Stadille reminded the Board that they need to complete the conflict of interest if they haven't done so already. She advised that because April 1st, falls on a Saturday the deadline has extended to Monday, April 3rd. All trustees need to submit a conflict of interest form for their position but they also have to include that their trustee role on the Deferred Compensation Plans Board.

- Follow-up on review of Wells Fargo SSAE 16/SOC1

Ms. Montoya reviewed a follow up item from the previous meeting. The SSAE 16 report was emailed to the trustees in December. Ms. Montoya stated the last meeting the Trustees were to consider any questions the Trustees might want to have regarding the SSAE 16 report. However at that point the Trustees requested additional time to review the report. This action item was included in this meeting because if the Trustees have any questions on the SSAE 16 report this would be their chance to get those questions answered. Mr. Cottle began by asking for additional information such as, Wells Fargo's ethics policy, subservice organizations and functions provided to Wells Fargo. Mr. Cottle advised it would be useful for him to know what their (subservice organizations) input is for this plan in particular. Mr. Cottle confirmed he had no issues but wanted more information. He stated that this information would also be helpful for the Board. Ms. McCraner asked Ms. Montoya if she could work with Wells Fargo and get the information Mr. Cottle requested. Ms. Montoya confirmed she would be able to provide that information from Wells Fargo IRT for the next quarterly meeting.

Ms. Montoya advised that they spoke to Macias and Gini about their input into the Comprehensive Annual Financial Report (CAFR) that relates to the deferred compensation

plans. Macias and Gini does not perform a full audit; they provide a high level material analysis. They compare balances from current to prior years to see if there are any material changes. Ms. Montoya asked the Board if they would like additional information on the other audits that can be done and that are more detailed. Ms. McCraner inquired if those audits were done by the City's outside audit firm. Ms. Montoya advised that the audits are done by Macias and Gini, an outside audit firm. Ms. Montoya stated that they looked at other entities that have savings plans and some other entities have independent single audits for their plans. Ms. McCraner recommended to have staff present information for the Board to review. Ms. McCraner inquired if Ms. Montoya could get a pricing schedule from Macias and Gini to identify the fees applicable with additional audit services. Ms. Montoya confirmed that any cost that are incurred as a result of an additional audit services related to the plans would be owned by Risk Management.

Mr. Breunig addressed Mr. Cottle's questions regarding Wells Fargo's subservice organization. He advised that the NSCC (National Securities Clearing Corporation) does all of the clearings for trades. All of the automated trades are collected and bundled through the NSCC that interfaces with the companies and that touches the City participants. Genpact India is Wells Fargo's offshore organization. They do a lot of back house functions such as reconciliations, so there is a lot of back door processing that occurs in India. Ms. Stadille inquired what participant information Genpact India would have access to. Mr. Breunig confirmed Genpact India does have access to view participant information but no data is stored there. Ms. McCraner inquired if the Board could get a detailed list of functions and how they impact the City participants. Mr. Breunig advised he would be able to provide a report. He explained that SunGard (InvestOne) is a valuation feature that values assets for securities that may not be publicly traded. VMS (Vertical Management Systems) is a trading link that facilitates trading activity with the mutual fund companies. State Street and Galliard does custody work for the collective investment funds and NAV calculations for the assets they manage. Wells Fargo Trust Operations is the internal group that ensures the assets are there and accounted for. Wells Fargo First Clearing, outside the mutual funds space and dealing with unique assets, especially executive benefits, need to go through a clearing desk, that's Wells Fargo First Clearing. Infosys McCamish Systems, for the executive benefits non-qualified plans, Wells Fargo does not have their own record keeping platform. Infosys builds and manages the system.

3. COMMENTS FROM TRUSTEES, STAFF, ADMINISTRATOR, ATTORNEY

- Mr. Canizal explained they had discussed in a previous meeting about having a Board member attend the Sponsor Advisory Council (SAC) meeting that is scheduled for March 7 and 8. After review, and looking at the City policy, due to the conflict of interest, it is very likely that Board members will not be able to attend the event. Mr. Canizal wanted to know if Wells Fargo can provide a summary of the event to the Board. Ms. Jensen advised that she will be attending. She will summarize the events and share the presentation materials. Ms. McCraner was not familiar with SAC. Ms. Jensen advised that the SAC is a council that is made up of about 50 to 60 of Wells Fargo clients that meet on an annual basis and they are asked to attend 2 or 3 years in a row. She advised that it is a way to talk about industry trends, regulatory updates, and exchange ideas. Mr. Breunig advised that it is an opportunity for Wells Fargo to find out from plan sponsors what is working and what needs improvements.

4. PUBLIC COMMENT

None

The next meeting is scheduled for March 27, 2017.

Meeting adjourned at 3:26 p.m.

Backup documentation is available at Risk Management.