DEFINED CONTRIBUTION PLANS TRUSTEE MEETING MINUTES
Friday, June 30, 2017

The Defined Contribution Plans 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 1:06 p.m. by Tracy McCraner.

Trustees Present:	Robert Davis, Mark Hovey, Tracy McCraner Julio Canizal arrived at 1:07 p.m. Gail Granewich arrived at 1:08 p.m.
Staff present:	Tom Brady, Estella Montoya, Nancy Stadille, Quennelle Allen, Gilda Smith
Presenters:	Denise Jensen (Wells Fargo IRT) Bill Cottle (Milliman) Jeff Nipp (Milliman)

1. ACTION ITEMS

A. Dispense with the reading and approval of the minutes of April 26, 2017.

MOTION TO ACCEPT THE MINUTES OF APRIL 26, 2017: Mark Hovey
SECOND: Robert Davis
Approved (3-0, 2 absent)

B. Review and approve FY 2018 Trustee Board Budget.

Ms. Montoya informed the Board the budget for FY 2018 is $438,760. This is a decrease of $20,971 from FY 2017. The decrease is due to a reduction in personnel and data processing expenses. Mr. Hovey asked for clarification regarding the budgeted amount for training. Ms. Montoya confirmed the budgeted amount is available for use by the Trustees and has not been fully utilized. Mr. Hovey encouraged fellow Trustees to utilize the training resources. Ms. McCraner asked for clarification regarding potential conflict of interest. Ms. Montoya stated Wells Fargo provides the accommodations for their Sponsor Advisory Council meeting and the attendee would be responsible for travel expenses. She further stated the City would be able to pay for the cost of the accommodations to avoid conflict of interest. Ms. McCraner asked staff to notify the Trustees of upcoming training opportunities. Ms. Montoya informed the Trustees the City is a member of the National Association of Governmental Defined Contribution Administrators (NAGDCA). NAGDCA offers a menu of educational seminars.

Approved (5-0)

C. Discuss and approve implementation of Wells Fargo's Retirement Investment Advice.

Ms. Jensen directed the Board to Section 3 of the Wells Fargo quarterly report located under the Informational Items tab. Ms. Jensen informed the Board Wells Fargo offers two tools; Retirement Guidance and Retirement Advice fueled through Morningstar. These tools are offered with no additional cost. Ms. Jensen informed the Board these tools have been available for many years. These were initially offered with an additional cost and the Board was not interested. With different negotiations through the years, these tools are now available with no additional cost to participants or plan sponsors.

The Guidance and Advice are the same exact tool with Advice actually giving recommendations on specific funds within the plan where Guidance would provide asset allocation suggestions. Through the participant website, Advice will tell the participant how to invest based on their risk tolerance and time horizon to retirement. If the City would like to implement this tool, Wells Fargo would amend the service agreement. Ms. Jensen informed the Board Wells Fargo will not solicit their products within these tools. Within the Wells Fargo book of business, less than 2% utilize Guidance and less than 29% utilize Advice. Not all plans utilize these tools because other tools are utilized.

Ms. McCraner asked if there are fiduciary concerns regarding this tool. Ms. Jensen stated the advice is from Morningstar back engine. Morningstar is the fiduciary on the tool. Mr. Hovey asked if there are downsides, such as confusion for participants, to this tool and what would be the rollout plan. Ms. Jensen replied the downside would be additional communication. The biggest downside is the participant would not be able to change their contribution amount on the Wells Fargo website. The City directs contribution activity through Self-Services. Mr. Hovey asked if the Board would be involved in the communication. Ms. Jensen stated she will coordinate with staff to implement. Their back office can turn on the tool within 7 to 10 business days. Communication to participants would be timed where the tool is live when the communication is received. Mr. Hovey deferred to staff to implement.

MOTION TO APPROVE IMPLEMENTATION OF RETIREMENT ADVICE: Gail Granewich
SECOND: Julio Canizal
Approved (5-0)

D. Request to approve informational meetings from fund managers.

MOTION TO APPROVE INFORMATIONAL MEETINGS FROM FUND MANAGERS: Julio Canizal
SECOND: Mark Hovey
Approved (5-0)

2. STAFF REPORTS AND INFORMATIONAL ITEMS

- <u>Trustee Education-Fiduciary Responsibility</u>

Mr. Brady began his presentation by providing an overview of fiduciary duties. He stated the Employee Retirement Income Security Act of 1974 (ERISA) governs all private sector retirement plans. ERISA specifically excludes government plans. The duties of a public retirement board are governed under Article XVI, § 17 of the California Constitution, specifically Government Code § 53609.

The Constitution states the specific standards on responsibilities are the duty of prudence, the duty of loyalty, and (particular to California) the duty to diversify investments to minimize the risk of loss and to maximize the rate of return. ERISA does not govern governmental plans, but ERISA is a good place for guidance regarding the Board's fiduciary responsibility. There is not much case law in California. All is guidance is from the DOL or IRS.

Mr. Brady proceeded to inform the Board about the duty of prudence on page 7. There is a two-prong approach; substantive and procedural. On substance, trustees need to know a lot about investments and how retirement plans work in order to make a proper decision. Then there is a process with how the relevant information is evaluated. The information needs to be evaluated appropriately to reach a reasonable decision. The decision may produce a poor return, but document the process. The result does not always matter; it is the process followed. Page 8 discusses prudence involved in selection of service providers. The service provider and the client service team should be knowledgeable about government plans. Trustees should be aware of the fee structure. Mr. Brady proceeded to recommend periodic requests for proposals to identify trends in fees and if fees paid are appropriate. Ms. Montoya confirmed Risk Management complies with City of San Diego guidelines of five years. Mr. Brady stated private sector files Form 5500. Reviewing fees indicated on Form 5500 can assist in determining whether fees are appropriate. He informed the Board recent litigation has caused fees to be significantly reduced.

Mr. Brady reviewed the duty of loyalty on pages 10-12. The California Constitution specifically states the duty of loyalty is most important. Trustees are required to avoid conflicts of interest, misrepresentations to participants, and misuse of plan assets. Fiduciaries may not put anyone's interest ahead of the interests of plan participants. Mr. Brady also encouraged the Trustees to attend as many education opportunities possible. He states there is a trend where board members are required to attend a certain number of conferences. The DOL is looking at whether trustees are knowledgeable in administering their plan. Mr. Hovey stated pension boards have a practice that encourages conference attendance. Ms. McCraner stated the City's CFO has a continuing education requirement for her staff and trustee education may support the CFO's requirement. Mr. Brady acknowledges it may be difficult to attend conferences. He suggested the Trustees can identify areas of interest and the City Attorney's office can provide the training. Mr. Hovey asked if the Defined Contributions Board have a fiduciary education policy. He stated SDCERS has fiduciary education every two years. Ms. Montoya confirmed there is not an official policy, however education materials are available. Ms. Montoya asked if the Board is interested in establishing an education policy. Ms. McCraner requested Trustee Education to be placed on the next agenda for further discussion.

Fiduciary duty regarding investments begins on page 13. Mr. Brady stated the Board is ahead of the game by having an established investment policy statement, monitoring investments, and providing a default investment option. Mr. Canizal asked how often the investment policy statement should be reviewed. Mr. Brady replied annually. Ms. Montoya confirmed the investment policy statement is reviewed annually. Mr. Brady reviewed the best practices in selecting investment options on page 15. Mr. Hovey asked for clarification on when Qualified Default Investment Alternatives (QDIA) were required. Mr. Brady replied with the Pension Protection Act of 2006. The City is not required but it is good practice to follow. Mr. Hovey stated Ms. Stadille had previously confirmed the City had a default fund prior to 2006. In 2007 the default fund was switched to the current default life strategy fund. California law provides a safe harbor for plan sponsors if participants exercise control over their investment options. However the Board still has a duty to continuously monitor the investment options; that fees are reasonable and funds are performing well.

Mr. Brady informed the Board fiduciary litigation is increasing. Most cases have been against large Fortune 500 companies. However, more recently there have been suits filed against non-profits and inevitably it will include public sector plans. The message of the cases is to always monitor the investment line up; that fees are reasonable and the returns are good compared to their competitors.

Lastly, Mr. Brady reviewed plan document compliance on page 22. There is a duty to keep the plan document in compliance with the Code for tax qualification purposes. If the Plan were to lose its' tax qualified status there would be tremendous negative tax consequences for the employees. The IRS recently announced they will no longer provide a determination letter. If audited the Plan cannot rely on the letter for compliance purposes. Every year the IRS provides a list of changes for plan amendments. Mr. Brady recommends the Trustees review the plan document every year and update according to IRS changes. Mr. Canizal asked how the Board would receive this information. Ms. Montoya replied, staff would rely on advice from the investment consultant or City Attorney. In the past the City Attorney would update the plan document accordingly. Ms. Granewich asked if the information was presented to the Board. Ms. Montoya replied the plan documents were presented to City Council for approval and presented to the Board as an information item. Ms. Granewich asked if the information would be presented to the Board before the document is presented to Council. Mr. Canizal asked for review of the latest IRS changes. Mr. Brady replied the IRS changes will be reviewed with outside tax counsel and the City Attorney will provide an update at the next quarterly meeting. Ms. McCraner and Ms. Granewich suggested the Trustees should reviewed plan documents annually. Mr. Hovey informed the Board that SDCERS engages a third party to perform a tax compliance audit every three years. He is not recommending this to the Board to perform often because it is an expensive option. He believes SDCERS is leading the pack in terms of ensuring compliance. Ms. Granewich stated the Board has a duty to follow-up on compliance. Ms. Stadille informed the Board the Plan Documents were recently updated. They were submitted and receive determination letters.

- First Quarter Activity Report-Wells Fargo

Ms. Jensen began by providing a brief overview on page 2 of the Wells Fargo presentation. She advised there was positive plan growth from March 31, 2016 through March 31, 2017. The Plans are above the billion dollar mark. Plan to plan transfers are trending back down. There were no reverse plan to plan transfers so far in 2017. All participant access activities have an uptick in distinct users. All plans have an increase in the average account balance. Headcount increased in the 401(k), 401(a), and the SPSH-H. The participant headcount decreased in the SPSP. Plan diversification is trending up. Mr. Hovey stated he anticipates diversification will continue to trend up as the SPSP-H population with the QDIA grows. However he thinks the SPSP participants are stuck; it has not done much for a long time. Ms. Stadille confirmed diversification communications have been sent to SPSP participants. SPSP participants are aging. When the Plans were transitioned to a third party administrator, at that time it was emphasized the Managed Income Fund (MIF) is where to be as a safe investment option. Mr. Hovey stated it may have been the emphasis back then but it may not be the emphasis now. Ms. Montoya further confirmed diversification information is provided to participants with each communication opportunity.

Ms. Jensen provided follow-up on questions from previous meetings. During the February 22, 2017 meeting Jon Scharmer discussed trigger emails sent to participants to take action. Jon informed the Board of the emails sent, there was a 49% open rate. Of those opened 70% took action. Millennials had a 53% open rate but only 14% took action. Individuals in the 50-65 age range had a 32% open rate with 37% of those took action. Wells Fargo research indicates millennials like to receive information electronically, but when taking action they want to talk with someone.

Mr. Canizal had previously asked about trigger emails for those who have not enrolled. Ms. Jensen stated currently their trigger based communications do not involve those who are not enrolled, but will roll out moving forward. The issue is Wells Fargo needs to have the email address. Wells Fargo does not have an email address if the participant did not provide it. If the City had the appetite to share City email addresses Wells Fargo would be able to get better traction on those who are not in the plan.

During the March 27, 2017 meeting Mr. Hovey asked about government employers who sponsor auto escalation of employee contributions. Within the Wells Fargo book of business they have 22 government plans. Two have employer forced auto escalate; one escalates 1-6% annually, the other 1-8% annually. Ms. Jensen also looked at their plans that have over $1 billion, of those 25% use employer forced auto escalate, primarily 1-6% annually. There is a plan sponsor that goes up to 10%.

Ms. Jensen reviewed the 2016 fee summary under Section 2. The recordkeeping fee paid by participants is 11 basis points, charged annually. This does not include fund expense. Funds that have revenue share are rebated back to the participants that are utilizing those funds. The only other participant fee is the loan set-up fee. The total administrative fee paid is just under $1.2 million. Comparatively to 2015, there is a reduction of almost $182,000. Ms. Jensen reminded the Board in 2015, first quarter fee was 16 basis points, last three quarters were 12 basis points. There is a reduction in the amount of loans taken. The required fee disclosure to all employees will be included with the June 30th quarterly statement. The disclosure will also be posted on the intranet. The required QDIA notice will be included in the September 30th statement.

- <u>First Quarter Investment Report-Milliman</u>

Mr. Cottle began by providing a performance summary as of June 28 since it was close to the end of the second quarter. The domestic equity market is up about 3.8%. International equity up about 7.5%; it has been extremely volatile. Bonds up reasonably a little over 1% and REITs are up about 3%.

Mr. Cottle reminded the Trustees Milliman has provided a Quarterly Performance Reference Sheet to assist with the review of their report. He reviewed the Q1 performance report beginning on page 1. Domestic and international equities continue to do to well. Almost every segment of the equity market performed well. Mr. Cottle reviewed the changes in market value of assets on page 5. Total assets increased from $1,031,542,230 at the beginning of the quarter to $1,066,974,689 at the end of the quarter. Ms. McCraner asked about the withdrawal amount from the MIF. Ms. Smith replied the large withdrawal amount may be due to SPSP participants taking advantage of the annual in-service withdrawal option. Mr. Hovey referred to Wells Fargo's quarterly report, page 39, Cash Flow for the SPSP. He stated SPSP continues to have more distributions than contributions coming in.

The watch list on page 7 was reviewed. Mr. Cottle informed the Board he met with Boston Trust recently. They have had a difficult year, but surpass their benchmark at the 2-year performance period. Oakmark has been good over the past year, and expected to continue. BlackRock TIPS performed well over the past year and adding value over each of the last four quarters. Generally there has been improvement in the funds on watch.

Mr. Cottle proceeded to review cumulative performance data on pages 12-13. He reminded the board the data is net of fees. Vanguard Growth, Vanguard Value, and BlackRock Equity funds matched their benchmark for the quarter. Principal Mid Cap has out-performed and has since the fund was hired. Vanguard Mid Cap matched their benchmark. Boston Trust performed slightly below the benchmark. However, at 2-years they are above the benchmark. The longer period they are still trailing their benchmark and the fund remains on watch. Invesco has been trailing and has trailed over most of the time period.

Milliman will perform additional research on Invesco. Dodge & Cox International Equity out-performed and has out-performed historically. Oakmark continues to out-perform in recent periods. All three of the life-strategy funds out-performed by a small amount. The MIF matched its' benchmark. The TIPS has been out-performing. T. Rowe Price has been a problem child for the quarter and longer. Milliman will speak with T. Rowe Price and they may recommend the fund be placed on watch.

- Mr. Nipp updated the Board on his March 8, 2017 visit with BlackRock regarding their TIPS fund. He informed the Board of BlackRock's organizational changes. He confirmed their strategy has not changed. In March, BlackRock's view was there will be more inflation than what the market is expecting. Since then inflation has come in lower. Mr. Nipp stated with BlackRock's strategy in the very low volatility environment, low inflation, there is not a whole lot they can do with that. It is hard to get value when the market is not providing the opportunities. In his opinion, until there is an environment with more volatility, more inflation, more opportunities to add value, there will not be dramatic swings in relative performance one way or the other.

- Mr. Cottle reviewed the June 23, 2017 memo regarding their review of Wells Fargo's SSAE 16 and Code of Ethics & Business Conduct. Milliman submitted additional questions to Wells Fargo. The responses received from Wells Fargo were adequate.

- Mr. Cottle reviewed the June 26, 2017 memo regarding their review of Wells Fargo's Sales Practices Investigation Report. Milliman submitted additional questions to Wells Fargo. Wells Fargo's responses confirmed Institutional Retirement Trust has no relationship with community banking activity and there was no impact to the City of San Diego. Mr. Cottle informed the Board Wells Fargo has a new Office of Ethics, Oversight, and Integrity. There is an elimination of product sales goals. Mr. Cottle stated again there was no impact from the sales practice issue relative to the City of San Diego's retirement savings plans.

3. COMMENTS FROM TRUSTEES, STAFF, ADMINISTRATOR, ATTORNEY

- Ms. Montoya reminded the Trustees Ms. Stadille will be retiring on August 4, 2017. Ms. Quennelle Allen will be Ms. Stadille's successor. Ms. Granewich thanked Ms. Stadille for her service to the Board and welcomed Ms. Allen. Ms. McCraner thanked Ms. Stadille as well. Ms. Stadille shared the recognition with the staff assigned to the Defined Contribution Plans Trustee Board.

4. PUBLIC COMMENT

None

The next meeting is scheduled for July 24, 2017.

Meeting adjourned at 2:38 p.m.

Backup documentation is available at Risk Management.