SCFA RETIREMENT SUBCOMMITTEE
MINUTES OF MEETING
NOVEMBER 1, 2004

[In these minutes: Minnesota Life Annual Investment Review]

[These minutes reflect discussion and debate at a meeting of a committee of the University of Minnesota Senate or Twin Cities Assembly; none of the comments, conclusions or actions reported in these minutes represent the views of, nor are they binding on, the Senate or Assembly, the Administration or the Board of Regents.]

PRESENT: Daniel Feeney, chair, Gavin Watt, Barry Melcher, Jackie Singer, Chris Suedbeck, Gordon Alexander, Richard Goldstein, Kathryn Hanna, Dian Lopez, Michael Murphy, Herbert Pick

REGRETS: Jean Kinsey, Carol Siegel, Fred Morrison

OTHERS: Associate Vice President of Asset Management Stuart Mason; SCFA Chair Professor Morris Kleiner; Employee Benefits Director Dann Chapman, Minnesota Life Representatives Dick Manke, Lynne Mills, Laura Pierson and Greg Strong

I). At the request of Professor Feeney who was running late, Professor Mike Murphy called the meeting to order and asked those present to introduce themselves.

II). Minnesota Life provided members with an annual investment review. The following topics were covered:

- Rating agencies and Minnesota Life[1]s financial strength
- Advantus Update
- General Account Update
- Roth 403(b)
- Asset Allocation
- Service Update
- Plan Assets

Greg Strong provided members with a comprehensive review of the ratings environment and the activities of the four major rating agencies. Because financial analysis of insurance companies is complex and requires specialized knowledge, most individuals rely on rating agencies to determine the financial strength of the various insurance companies. However, investors should not simply rely on these ratings exclusively, but should read the reports on companies before he/she invests in a particular company or companies.

Rating agencies primarily conduct the following reviews when analyzing an insurance company[1]s financial strength:

1. A review of the company[1]s operations.
2. A review of the company[1]s financial performance.
3. A review of the industry.
4. A review of the company[1]s organizational structure.
5. A review of the company[1]s management.

While Minnesota Life has chosen to be rated by the four major rating agencies (Best[1]s, Fitch, Moody[1]s and S&P), not all companies choose to do so. Minnesota Life believes it is important for their markets, both its up-scale individual clients and corporate clients, to have its business subjected to all the viewpoints of the major rating agencies. Members were referred to an exhibit distributed earlier explaining the various ratings, which Mr. Strong proceeded to explain.

Other factors to consider besides ratings when determining which company to do business with include:

- Measures of financial strength e.g. ration of capital and surplus to liabilities, risk-based capital ratio.
- Quality of the company[1]s products.
- The company[1]s reputation in terms of how it treats its clients.

Minnesota Life has received a stable rating by each of the four major rating agencies. Mr. Strong noted, however, that S&P recently downgraded Minnesota Life from AA to AA-. This change is part of an overall industry trend that has seen 189 company downgrades by S&P over the last 21 months. Since May of 2002, more than 90% of S&P's rating changes have been downgrades. S&P attributes the lowered rating to "GAAP earnings below expectations and earnings quality, which are not expected to improve materially in the next 18 months due to exposure to equity market volatility."

Mr. Strong additionally shared information on how Minnesota Life compares to the rest of the industry and its liquidity.

What can Minnesota Life do to maintain and/or improve relative ratings?

- Continue to grow sales/revenue and convert this into earnings in all markets.

- Help the rating agencies refine their earnings expectations for group life, 401K and other products.

To conclude, Mr. Strong noted that Minnesota Life has:
- High ratings.
- Strong liquidity.
- Strong capital adequacy and investment quality.
- Solid relationships with only high quality businesses.
- A strong commitment to serving the needs of its customers and treating them fairly.

Questions/comments from members:
- Because much of the information shared today is based on fiscal year 2003 data, has Minnesota Life received any more recent information on its performance? According to Mr. Strong, Minnesota Life receives quarterly reports on its performance. Since 2003, capital ratios are up, Minnesota Life[1]s earnings through September 2004 are up by approximately 40%, Minnesota Life experienced an excellent year from a mortality standpoint, expenses are being controlled, sales are up, etc.
- What is Minnesota Life[1]s Weiss rating? Mr. Strong believes it is an A, but noted that Minnesota Life does not track its rating by Weiss. Weiss Ratings Inc. only use publicly available information.
- Are the rating agencies concerned that Minnesota Life has a significant fraction of its business divided among some large clients? The rating agencies are aware of Minnesota Life[1]s largest clients e.g. the University is Minnesota Life[1]s largest asset client. The rating agencies have not expressed any concerns around this fact.

Next, Lynne Mills provided members with an Advantus/General Account update. She highlighted the following:
- It is likely Advantus will set a new sales record in terms attracting new assets this year. Year to date, Advantus has added an excess of $500,000 million in new assets.
- Advantus is very satisfied with its current staffing. Most of its key positions are filled.
- Advantus[1] performance has been very strong in terms of its core products: real estate, bond and mortgage securities.

Ms. Mills referred members to a handout, which provided the following information:
- Summary of investments in the General Account. The General Account is valued at $10.8 billion.
- Bond portfolio quality.

- Internal Œwatch list[1].
- Asset quality measures.

Roth 403(b) highlights: Currently, Faculty and P&A have the ability to invest in two optional retirement plans, the Optional 403(b) and the 457. Recent legislation would permit the University to add another type of contribution to the Optional 403(b), a Roth 403(b). This option goes into effect until January 1, 2006 should the University decide to offer it.

A Roth 403(b) is very similar to a Roth IRA (Individual Retirement Account) at an employer level. However, there are two main differences between a Roth IRA and a Roth 403(b):

1. The contribution limit is three times higher for a Roth 403(b). The Roth 403(b), however, would be viewed as another component to the University[1]s existing Optional 403(b) plan. Therefore, participants would not be able to invest $15,000 is the Optional 403(b) plan and another $15,000 in the Roth 403(b) plan.
2. There is no income limit on one[1]s eligibility to make contributions into a Roth 403(b).

A major difference between the Roth 403(b) and the Optional 403(b) is the tax treatment. In exchange for giving up the tax deduction at the time of contribution, withdrawals from a Roth 403(b) are tax-free both at the State and Federal level for all qualifying distributions. Another provision of the Roth 403(b) is that contributions into the plan are scheduled to expire in 2010.

Ms. Singer noted that because the Optional 403(b) plan and the Roth 403(b) will require a coordinated limit there are PeopleSoft implications.

In closing, members were referred to the written material provided by Minnesota Life describing the advantages and disadvantages of offering a Roth 403(b) and the key features of the Option 403(b), Roth 403(b) and a Roth IRA.

In the interest of time, Dick Manke requested members review on their own the service update information and the plan assets information in their three ring binders.

Mr. Manke then mentioned the Spitzer subpoena Minnesota Life received. He directed members to the executive summary on the topic of [3]tying[2]. He noted that an insurance broker is involved in [3]tying[2] when the sale of one product is contingent on the purchase of another. Mr. Manke emphasized that Minnesota Life is not involved in ^{3}tying^{2}, has not been accused of any wrongdoing with respect to ^{3}tying^{2} and is unaware of any insurance brokers that are involved in ^{3}tying^{2}.

The remaining minutes of the meeting were spent discussing asset allocation. Asset allocation is the process of dividing your savings into different categories e.g. domestic equities, international, fixed income, guaranteed accounts. Many financial planners today belief that asset allocation is more important than the fund an investor chooses. Asset allocation helps investors persevere through adverse market conditions and achieve their asset allocation goals. Basically, there are three components that factor into an investors^{1} asset allocation decisions:

1. The time horizon until retirement
2. Risk tolerance
3. Financial goals

Minnesota Life is currently providing the University of Minnesota with free asset allocation training/education.

Professor Feeney distributed samples of Minnesota Life^{1}s quarterly statements to members. The goal is for the University of Minnesota in conjunction with Minnesota Life to have all its communication pieces use clean, common terminology and to promote an understanding of the importance of asset allocation.

III). Professor Feeney reminded members that the next Retirement Subcommittee meeting is on Monday, November 8th. Members were encouraged to let Professor Feeney know if they did not like the format of today^{1}s meeting.

For anyone interested, Jackie Singer will provide SCFA with an update tomorrow, November 2nd, on employees hired in the past two years under the waiver period. So far this year, approximately 10% of the employees hired took the waiver. Ms. Singer distributed a handout with additional information on this subject.

IV). Hearing no further business, Professor Feeney adjourned the meeting.

Renee Dempsey
University Senate