

SCFA RETIREMENT SUBCOMMITTEE
MINUTES OF MEETING
NOVEMBER 7, 2005

[In these minutes: Revised Retirement Plan Fiduciary Committee Bylaws, Benchmark Review, FRP Investment Performance Results for Period Ending September 30, 2005, Draft of *Faculty and Staff Retirement Programs Annual Report* for Fiscal Year Ending June 30, 2005, TIAA-CREF Concerns and Discussion]

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

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

REGRETS: Michael Murphy, Burt Sundquist

OTHER: Michelle Johnson

GUESTS: TIAA CREF representatives Lisa Stitzel, relationship manager and John Wilcox, senior vice president and head of corporate governance

I). Members reviewed the revised Retirement Plan Fiduciary Committee bylaws. Comments/questions from members regarding these bylaws included:

- A member asked whether serving on the Retirement Plan Fiduciary Committee and being a beneficiary of the Faculty Retirement Plan (FRP) would pose a conflict of interest. Mr. Suedbeck stated that to the best of his knowledge, this should not be a problem, but will check into this question to verify. He noted that it is not uncommon for a trustee of a public pension plan to serve on the plan's advisory board. Ms. Singer added that it is also common in the private sector to have employees of a company serve on its compensation committee.
- The wording of Section V Subd.1 is awkward. It was agreed that the wording of the second sentence in this section would be reviewed for possible rewording.

Members voted to unanimously approved the bylaws, which will be forwarded to SCFA for endorsement, and then onto the FCC. Simultaneous with this process, conversations around indemnification issues will occur with the Office of the General Counsel and Gray Plant Mooty.

II). The subcommittee fulfilled its limited fiduciary responsibility by reviewing the benchmark data provided by Securian. Members agreed that monitoring this information is one way to ascertain whether the FRP is being paid a comparable interest rate in the market.

III). Jackie Singer shared FRP investment performance results for the period ending September 30, 2005. Ms. Singer reported that overall the University's investments are doing very well. The two accounts that are underperforming their benchmarks include: CREF Growth Account and the CREF Global Equities Account. While the performance on these accounts is somewhat troublesome, it is not to the point where any action needs to be taken.

Members briefly expressed concern over whether the benchmarking on the University's various accounts was being done accurately. Ms. Singer and Chris Suedbeck volunteered to explore whether the benchmarks are being done correctly for the December 31, 2006 statement.

IV). Ms. Singer distributed a draft copy of the *Faculty and Staff Retirement Programs Annual Report* for fiscal year-ending June 30, 2005. The report is in the same format as last year, but naturally contains updated information. Once input from this subcommittee, CAPA Benefits and Compensation Subcommittee and the Civil Service Committee have been garnered the document will be published and widely distributed. Ms. Singer asked that members send their comments regarding this report to her via email at singe020@umn.edu.

V). Before today's guests arrived, Professor Morrison briefed members on the issues he intended to ask them to respond to. Professor Feeney then welcomed TIAA-CREF representatives Lisa Stitzel, relationship manager, and John Wilcox, senior vice president and head of corporate governance. Members and guests went around the room and introduced themselves.

Professor Morrison outlined the five areas of concern that the committee would like TIAA-CREF to respond to:

1. TIAA-CREF's governance structure and recent governance problems involving TIAA-CREF's auditors, Ernst and Young.
2. The leave of absence by TIAA-CREF CFO Elizabeth Monrad, and, on a semi-related note, the departure of TIAA-CREF's compliance officer, Carol Baldwin Moody.
3. TIAA-CREF's investment in Refco.
4. Abandonment of businesses e.g. long-term care, foreign educational institutions.
5. Recordkeeping concerns.

With respect to the first issue stated Professor Morrison, the improper relationship between two TIAA-CREF trustees and TIAA-CREF's auditor, Ernst and Young, it appears that TIAA-CREF attempted to suppress details about this indiscretion rather than be forthcoming with the facts. What does this say about the culture of TIAA-CREF? How can the University of Minnesota be assured that TIAA-CREF is investigating the issues it needs to be investigating when they arise?

Mr. Wilcox stated that he is the senior vice president in charge of all of TIAA-CREF's governance activities, which he described in a fair amount of detail. It is Mr. Wilcox's understanding related to the TIAA-CREF/Ernst and Young governance controversy that two of TIAA-CREF's trustees failed to report on their annual disclosure statement that they had a business relationship with TIAA-CREF's auditors, Ernst and Young. In Mr. Wilcox's opinion the problem escalated because no one took it seriously enough, and thought it to be of minimal

concern. He emphasized that it was not the Wall Street Journal's investigation into this matter that prompted TIAA-CREF to contact the SEC.

The Katzenbach Report outlines in depth TIAA-CREF's internal problems, which are a result of its governance structure. Mr. Wilcox briefly described TIAA-CREF's complex governance structure. With this said, he added that TIAA-CREF is a very special kind of financial services company in that it does not encounter the same kinds of conflicts of interest that afflict many other firms, which in large part can be attributed to its not-for-profit charter and long-term outlook of its client base.

After reviewing the Katzenbach Report, TIAA-CREF decided that it would not be feasible to change its governance structure. However, in response to the report, TIAA-CREF rewrote its corporate governance guidelines. These guidelines go into great detail outlining the importance of shared responsibilities within the organization, and how communication needs to be improved amongst members of the company's various boards. Mr. Wilcox offered to provide the committee with a copy of the document that explains how TIAA-CREF has handled the problems, which led to the TIAA-CREF/Ernst & Young scandal.

Professor Morrison stated that the University's concern is not about TIAA-CREF's structure, but whether TIAA-CREF has a culture, which attempts to cover up problems. Mr. Wilcox stated that he does not believe TIAA-CREF ever intended to cover up the TIAA-CREF/Ernst & Young problem because it was determined that there had been no compromises to the audits that had been conducted. Professor Morrison added that there is also the issue of the lack of compliance on the part of the two TIAA-CREF trustees to not contract with the auditors. Mr. Wilcox agreed this information should have been disclosed in the trustees' annual disclosure statements; however, he added that when these trustees were questioned about the matter, they explained the nature of the conflict, and it was deemed to be a minimal infraction. Mr. Wilcox does not believe there was ever any intent to conceal the issue because the internal investigation concluded that there was no significant issue affecting the financials or the audit. Professor Morrison noted that obviously it was a significant enough issue if Ernst and Young felt it necessary to report the incident to the SEC. Mr. Wilcox replied that Ernst and Young operate under a very different set of rules than does TIAA-CREF's trustees. Ernst and Young has its own obligations as an auditor, and it was judging the situation from that viewpoint.

A member asked that simply because the audit was not found to be compromised, does TIAA-CREF take the position that an arrangement between its trustees and its outside auditing firm is acceptable? Mr. Wilcox stated absolutely not. With respect to the question regarding whether TIAA-CREF should have explained and publicly disclosed this information or simply terminated these trustees, TIAA-CREF chose to remove the trustees. In Mr. Wilcox's opinion, the University and TIAA-CREF have no difference in terms of their values. The reason behind why these two trustees failed to disclose their relationship with Ernst and Young is a mystery and will likely remain so. Unfortunately, their failure to disclose this information created a serious problem for TIAA-CREF and damaged its reputation.

A member asked whether the rewriting of TIAA-CREF's governance guidelines was a reaction to this matter, or was it something TIAA-CREF planned to do anyway. Mr. Wilcox stated that

the Katzenbach Report spurred TIAA-CREF to review and revise its corporate governance guidelines. The delay in failing to come forward sooner with information concerning this problem can be attributed in large part to the fact that the responsibility to do so was dispersed between the trustees and the Board of Overseers. In its revised corporate governance guidelines, TIAA-CREF clarifies who is responsible for what, and who communicates with who, etc.

Moving on to the next issue, Professor Morrison asked whether Ms. Monrad was still on leave. Yes, stated Mr. Wilcox. Professor Morrison noted that prior to working for TIAA-CREF, Ms. Monrad was employed by General Re Corporation (Gen Re), which is deeply involved in the AIG insurance scandal. Ms. Monrad was placed on leave from TIAA/CREF when she received a Wells notice from the SEC related to her possible involvement into questionable insurance activities. Does TIAA-CREF investigate the background of the people it hires, or are hiring decisions simply a bottom-line decision? Mr. Wilcox stated that naturally background investigations are conducted on individuals that are being considered for employment opportunities at TIAA-CREF. He added that he does not believe that TIAA-CREF could have uncovered information about these allegations prior to hiring Ms. Monrad who is a very highly regarded financial executive. It is unfortunate that there is this blemish on her reputation.

Regarding the departure of TIAA-CREF's compliance officer, Carol Baldwin Moody, why was there so little information in the press release concerning her departure? Mr. Wilcox stated that Ms. Moody's mother is desperately ill, and that she chose to leave to help care for her mother. Ms. Moody did not want these personal details put in the press release.

Next, Professor Morrison asked why TIAA-CREF chose to invest in Refco despite the fact that the company's prospectus clearly mentioned that it was being investigated by the New York Attorney General's Office as well as the SEC, etc. Before TIAA-CREF invests in a company, is an analyst responsible for reading that company's prospectus? Mr. Wilcox stated that many of TIAA-CREF's portfolios are indexed, and this indexing strategy requires TIAA-CREF to invest in every IPO that is in the Russell 3000. In TIAA-CREF's actively managed funds, it looked closely at Refco, but, unfortunately, followed the lead of Thomas H. Lee and others that had been trading with this company for many years. While Mr. Wilcox cannot speak for TIAA-CREF's analysts' actions, he believes that they did their due diligence when investigating this company. This same question can be asked of others on Wall Street who invested in Refco.

A member asked whether TIAA-CREF made investments in Refco after its problems were revealed. Not to Mr. Wilcox's knowledge, however, he admitted not having spoken with the analysts about the Refco purchase. Mr. Wilcox is under the impression that TIAA-CREF purchased Refco at the time of the IPO. TIAA-CREF has since sold its positions in Refco. Mr. Wilcox agreed to provide the committee with more information on the Refco transactions. Professor Morrison agreed that this would be helpful. Ms. Stitzel stated that while she does not want to downplay this issue, the Refco purchase represented less than half of a basis point of TIAA-CREF's overall portfolio. Professor Morrison stated that he understands the Refco purchase represents a trivial amount, but it raises the question of whether anyone is analyzing investments before they are made.

This committee is also concerned over what it perceives to be TIAA-CREF's decision to abandon or remand its 529 college savings plans business, foreign educational institution business, long-term care insurance, etc. The University needs to decide whether it wants to do business with a company that abandons or remands business relationships after short periods of time. Professor Morrison used a personal example to highlight his concern over this issue. Ms. Stitzel responded to Professor Morrison's example by noting that TIAA-CREF sold long-term care insurance for approximately 13 years, but due to changes in the marketplace, it became apparent that TIAA-CREF would be unable to continue to offer this type of insurance coverage and remain competitive. Therefore, a decision was made to get out of this line of business. TIAA-CREF realizes that many of those that purchased long-term care insurance through TIAA-CREF did so because of its reputation. With respect to Professor Morrison's less than satisfactory transition experience to a new long-term care insurance carrier, Ms. Stitzel was apologetic. Mr. Wilcox asked that Professor Morrison provide TIAA-CREF with the correspondence around his experience so that TIAA-CREF can investigate the matter further.

In response to the committee's concern over TIAA-CREF's lack of commitment to long-term business relationships, Mr. Wilcox stated that this is absolutely not the case. One of the qualities that Mr. Wilcox finds most admirable about TIAA-CREF is its reputation, lack of conflicts of interest as described earlier, and its commitment to long-term performance. Today many organizations have a philosophy, which focuses on short-term results. TIAA-CREF is not a hedge fund, an arbitrageur or a short-seller, and, therefore, the culture of TIAA-CREF is infused with a commitment to long-term performance. Mr. Wilcox and Ms. Stitzel both shared examples of TIAA-CREF's commitment to long-term investments. Mr. Wilcox added that the TIAA-CREF charter requires it to be a long-term investor.

A member asked whether TIAA-CREF's restructuring strategy includes plans to move to a for-profit platform. Yes, stated Mr. Wilcox. This member then asked how this strategy squares with an earlier statement, which indicated that TIAA-CREF's not-for-profit status was what made it different from all the other financial services firms on Wall Street. Mr. Wilcox stated that TIAA-CREF's decision to move to a for-profit basis did not include having conflicts of interest. TIAA-CREF is infused with the values of a not-for-profit organization, and has high fiduciary standards.

Lastly, Professor Morrison raised the issue of the high number of inaccurate FRP transfers that TIAA-CREF is responsible for. Ms. Singer stated that while the financials for third quarter have not yet been reconciled there appears to be a significant improvement in the third quarter numbers thus far. Professor Feeney added that the University has been postponing its decision to permit rollovers into its retirement plans due to the high number of inaccurate transfers, of which a majority are attributable to TIAA-CREF.

In response, Ms. Stitzel stated that TIAA-CREF does not strive to be a poor performer in terms of processing transactions. There have been a myriad of reasons why these inaccuracies have occurred, which include mistakes by TIAA-CREF to participants filling out wrong forms, etc. Ms. Stitzel stated that in response to the high number of transaction errors, TIAA-CREF has instituted a procedure for contacting participants or former vendors if a transaction does not look right in order to ensure the intention of the employee and the correct processing of the

transaction. Additionally, probably the most important factor contributing to TIAA-CREF's high number of errors has been its complex, participant-based recordkeeping system. This weekend the University of Minnesota account will be transferred onto TIAA-CREF's new plan level-based recordkeeping system. The new platform is expected to make it easier for TIAA-CREF to process transactions e.g. transfers between vendors, processing rollovers, etc. Ms. Singer hopes that with the move to the new platform, TIAA-CREF will focus not only on individual participants as clients, but plan sponsors as well. Ms. Stitzel recognized the role the University has played in helping TIAA-CREF move in this direction.

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

Renee Dempsey
University Senate