SCFA RETIREMENT SUBCOMMITTEE
MINUTES OF MEETING
MAY 7, 2012

[In these minutes: P&A Senate Requests, Vice President for Human Resources Kathryn Brown, Discussion with Securian about General Account and General Account Limited Interest Rates, Monte Carlo-Type Simulation Demonstration, 2011 Retirement Plan SOC 1 Report Summaries, Full Fee Disclosure Analysis]

[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, Thomas Schenk, Nancy Fulton, Joe Jameson, Barry Melcher, Jackie Singer, Murray Frank, Kathryn Hanna, Andrew Whitman, Vernon Eidman

REGRETS: Wendy Berkowitz, Jane Carlstrom, Chris Suedbeck, Vernon Cardwell, James Cotter, Harvey Keynes

OTHERS ATTENDING: Rosalie O'Brien, counsel to the committee

GUESTS: Vice President Kathryn Brown, Office of Human Resources
Dick Manke, vice president, Securian Retirement
Blake Reigert, manager, U of M Retirement Plans

I). Professor Feeney called the meeting to order and welcomed those present.

II). Members unanimously approved the April 2, 2012 minutes.

III). Professor Feeney called on Mr. Schenk to share feedback from a recent Academic Professionals & Administrators Senate (P&A Senate) meeting. According to Mr. Schenk, the P&A Senate has requested that the Retirement Subcommittee look into renaming the Faculty Retirement Plan (FRP) the Academic Retirement Plan to more accurately reflect who is covered under the plan. Additionally, noted Mr. Schenk, the P&A Senate also requested that consideration be given to eliminating the two-year waiting period for P&A employees to be covered by the plan similarly to when the University eliminated the waiting period for faculty.

Professor Feeney asked Ms. Dempsey, Senate staff, to start a list of issues for next year and to put these two items on that list. The Retirement Subcommittee will take these up next year.

IV). Professor Feeney welcomed Vice President Kathryn Brown from the Office of Human Resources, and called for a round of introductions.

By way of background information, Professor Feeney stated that over the years, the committee has considered ways to better serve retirement plan participants. As coverage of the FRP has increasingly become more comprehensive, the committee has discussed whether a tiered structure might better serve participants because of the broad range of approaches taken by them in managing their accounts. In essence, the proposed plan would offer different options for plan participants: 1). target date funds, 2). an array of pre-screened core funds (similar to the current plan but with fewer funds), and 3). a self-directed brokerage account. In addition to this discussion, the committee has also been talking about adding a global bond fund, a managed small cap fund and a Roth 403(b). With that said, Professor Feeney stated that these additions/changes have been put on hold pending the Strategic Directions work that is being undertaken by the Office of Human Resources as well as the PeopleSoft upgrade. He asked Vice President Brown about the timeline for possibly moving forward with these plan changes and whether the Office of Human Resources has any sense about expected utilization of a structured brokerage type account.

Vice President Brown thanked Professor Feeney for the background information. She then went on to share what has been happening in the Office of Human Resources in order to put the conversation in context. Vice President Brown stated that after she assumed her role as Vice President of Human Resources last July, the office began a strategic planning exercise. The Office of Human Resources is committed to both the employee in terms of making sure the work experience is good and to the employer in terms of making sure the institution's needs are met. As the strategic planning exercise was being rolled out, it became clear that before a number of other efficiency changes could be made that the Human Resources enterprise system (PeopleSoft system) needed to be upgraded. The current system has been in place since 1997, and the University of Minnesota was an early adopter of the system, which over the years has had a number of modifications to meet the institution's business needs. These modifications have become unsustainable. PeopleSoft has informed the University that given the age of the system, it will no longer be able to provide technical or legal support. Because structural changes to the retirement plan need to be incorporated in the enterprise system, it simply does not make sense to make them before the new system is in place.

The enterprise system upgrade is expected to be completed sometime in the first half of 2014, but this is subject to change. Therefore, Vice President Brown stated that she cannot give the Retirement Subcommittee a firm completion date at this time. Conceptually and philosophically, she stated that she is supportive of the changes to the retirement plan that the committee has proposed.

Professor Feeney stated that based on Vice President Brown's statements, it is not likely that a tiered retirement plan can be implemented for at least a year. Vice President Brown stated that that is correct and a realistic estimate. Professor Feeney suggested that given the timeline is fairly far out that it would make sense for the Retirement Subcommittee in conjunction with the Retirement Plan Fiduciary Advisory Committee (RPFAC) to explore adding a global bond fund, and a managed small cap fund to the current plan. He added that the Retirement Subcommittee would also like to request that the new PeopleSoft system have the programming capabilities so that at some point the University can offer not only a tiered retirement plan but also a Roth 403(b). Vice President Brown acknowledged his request and noted that the Office of Human Resources will need to explore the costs and benefits of all proposed changes in order to make sure the retirement program is cost effective.

Professor Hanna informed Vice President Brown that the Retirement Subcommittee had previously formed an ad hoc committee and explored the feasibility of adding a Roth 403(b) to the University's retirement plan, and asked if she would be interested in receiving a copy of this report. Vice President Brown indicated she would be interested in seeing the report. Professor Feeney asked Ms. Dempsey to send the report to Vice President Brown as well as committee members. The goal, stated Vice President Brown, will be to identify a common ground that will address the majority of peoples' needs. The Board of Regents and the administration's philosophy on compensation is that the University needs to be competitive in the marketplace. As an employer of this size, the University should provide competitive retirement program benefits and compensation.

Ms. Singer noted that a positive outcome of the PeopleSoft upgrade is that the Office of Human Resources is using this opportunity to streamline its processes related to the retirement program. Vice President Brown stated that she is hopeful that the Office of Human Resources' strategic planning exercise will translate into better service for employees. The goal will be to make the new system as efficient and effective as possible with a real service-oriented element.

Professor Hanna asked whether there are any items in the new PeopleSoft upgrade that relate to the retirement program. Ms. Singer stated that she has requested that the catch-up contributions in the 457 plan for participants who are pre-retirement age be automated if possible. Currently, this is a manual, labor-intensive process. She added that this is just an example of the types of enhancements that are currently being looked at.

Professor Feeney thanked Vice President Brown for meeting with the committee. In turn, she thanked the committee for their time and for serving on the committee.

V). Next, Professor Feeney welcomed Dick Manke and Blake Reigert from Securian and noted that they had been invited to provide a Monte Carlo-type simulation demonstration as well as to have a discussion with the committee about the General Account and General Account Limited interest rates. Regarding the interest rates of the General Account and General Account Limited, the issue, noted Professor Feeney, is that the interest rates are converging and the guaranteed floor for both accounts is the same. This is somewhat troublesome in light of the fact that there are a greater number of restrictions on the General Account Limited than the General Account.

To facilitate the discussion, Mr. Manke distributed an exhibit to inform members about the differences between the General Account and General Account Limited. He took a few minutes and walked members through the handout. He noted that the General Account is unrestricted and operates much like a money market account. The General Account Limited, on the other hand, has withdrawal restrictions.

Mr. Manke noted that Securian is currently paying interest on the General Account above market rates by honoring the 3% crediting rate. The difference today is more than the 50 basis points or ½% on the General Account and General Account Limited. As interest rates continue to stay low there is the possibility that the General Account Limited crediting rate could go down. When the General Account Limited was introduced in 1995, no one could have ever guessed the current rate environment. The goal has always been to credit the General Account Limited more than the General Account, but as the rates go down the reality is that the interest rates are converging. Mr. Manke then cited some personal reasons for why he believes it would be advantageous to invest in the General Account Limited versus the General Account despite the fact that the rates are converging.

In light of this situation, Securian's actuaries have suggested that the committee may want to think about making the minimum guarantee on the General Account Limited 3.5% (currently 3%) and making the minimum guarantee on the General Account 2.5% (currently 3%). He added that even if the committee fully endorses this proposal, it would still require the approval of the State of Minnesota to make this change. If this change were made, stated Mr. Manke, a communication plan would be crucial in order to get the information out to plan participants.

Professor Feeney opened up this proposal for discussion and asked members to share their thoughts. Members' questions/comments included:

- Would this change only affect new money or money already invested? This would affect all monies, stated Mr. Manke. He added that while he does not know for sure, Securian may be willing to consider gradually lowering the General Account crediting rate, e.g., 10 basis points per quarter.
- There would be a lot of unhappy people if the General Account's minimum guarantee were lowered from 3% to 2.5%.
- Given that there may currently be the perception on the part of some plan participants that the minimum guarantees for the General Account and General Account Limited are different, it might make sense to make a distinction and actually make the minimum guarantees different.
- There should be a difference in the minimum guarantees of the two funds.

Before moving on to the Monte Carlo-type simulation demonstration, Professor Feeney asked members to give this matter more thought and that the committee will continue this discussion in the fall. He reminded members that the committee has the option of recommending that the University keep both minimum guarantees at 3%, pursue Securian's proposal to differentiate the minimum guarantees on the two accounts, or consider alternative options. Mr. Melcher noted that this issue should be brought to the RPFAC for discussion as well and Professor Feeney completely agreed.

Rosalie O'Brien, counsel to the committee, noted the importance of distinguishing between stated intentions and contractual obligations. Mr. Manke stated that the goal has always been for the General Account Limited to pay more given a reasonable interest rate climate. The current interested rate climate is unprecedented.

Professor Hanna asked whether, if there were parity in the General Account and General Account Limited rates, it would be possible to reduce the restrictions on the General Account Limited fund. Mr. Manke admitted not knowing where interest rates are going, but stated that they would need to stay at the current level for quite a while before there would be parity in the rates. He reminded members that the General Account Limited fund is being invested longer term so based on that he believes there will always be at least some difference in the rates. Mr. Manke stated that he would take this question back to Securian for further discussion.

Professor Frank stated that it is not inherently necessary to tie the minimum rate guarantees together. For instance, presumably Securian could raise the minimum guarantee on the General Account Limited without changing the minimum guarantee on the General Account. After all, benefits from the withdrawal restrictions of the General Account Limited because it is able to invest in longer-term securities. Financial institutions offer different guarantees on different products. Clearly, money that is locked-up benefits Securian because it can invest longer term.

Professor Feeney asked members their preference regarding whether they favored having Securian loosen the General Account Limited restrictions and keeping the minimum rate guarantees the same or whether the University should have Securian explore options for a differential minimum guarantee between the General Account and General Account Limited products. Professor Frank stated that before making this decision he would like the opportunity to discuss with his colleagues their thoughts on this matter. With that said, Professor Feeney asked that this be put on a fall Retirement Subcommittee agenda for further discussion. He then asked Jackie Singer whether there would be a way to randomly survey a subset of General Account and General Account Limited participants to get a sense about which direction to go. Ms. Singer stated that this data would need to be obtained from Securian. Mr. Manke additionally suggested having Securian representatives who take calls from plan participants to solicit their opinions on this matter. Professor Frank stated that he would like a random sampling of both types of account holders to be queried. Mr. Manke proposed that Securian continue this discussion with the State of Minnesota because if the state will not approve the proposed crediting rate changes this would be a moot point. He also stated that he would go back and talk with the Securian actuaries about the possibility of having the minimum guarantee stay at 3% for the General Account and increase the minimum guarantee (nothing specified) for the General Account Limited. Mr. Manke stated that he would report back on this matter to Professor Feeney over the summer.

VI). Professor Feeney then called on Blake Reigert for a demonstration of the Monte Carlo simulation that Securian developed at the committee's request. Mr. Reigert highlighted the enhancements that Securian made since it last demonstrated the simulation in March. He also demonstrated a few different scenarios so members could see how the simulation functioned. Members shared their feedback on the simulation and asked questions. At the conclusion of the discussion, Mr. Reigert stated that because the number of changes that still need to be made are minimal that rather than rolling the simulation out in December as originally planned that it should be able to be rolled out earlier, maybe as early as June sometime.

At the conclusion of the demonstration, Professor Feeney thanked Mr. Manke and Mr. Reigert for their time.

VII). Next, Professor Feeney called on Ms. Singer to provide information on the 2011 retirement plan SOC 1 report summaries. She noted that in previous years she prepared a summary of the results of the Statement of Account Standards (SAS) 70 reports for each of the University's retirement plan vendors. Beginning in 2010, the American Institute of Certified Public

Accountants (AICPA) divided the SAS 70 and replaced it with two new standards, the Statement on Standards for Attestation Engagements (SSAE) No. 16 Reporting on Controls at a Service Organization, and a new SAS Audit Considerations Relating to an Entity Using a Service Organization. Like the old SAS 70, the SSAE 16 applies in situations where an organization outsources a function to a Service Organization and the results from that function are incorporated into the organization's financial statements. SSAE 16 reports are officially titled "Report on Controls at a Service Organization Relevant to User Entities' Internal Control over Financial Reporting," or SOC 1 reports. The new standards were effective June 15, 2011.

Ms. Singer went on to provide members with more information about the two types of SOC 1 reports. She noted that a SOC 1 is not a pass/fail report, as an organization may achieve some control objectives, but not all, and still obtain a "qualified" opinion. A "qualified" opinion means that the auditor found exceptions or control deficiencies, which are detailed in the report. Though it may seem counter-intuitive, an unqualified opinion indicates the highest level of comfort in the recordkeeper's financial system's controls, as no significant deficiencies have been identified.

It should be noted that the University is not subject to ERISA, and thus is not required to obtain a SOC 1 report for Form 5500 filing purposes. Each year, however, Employee Benefits obtains and reviews a copy of its retirement plan vendors' reports as the SOC 1 report provides reasonable assurance that the financial systems' controls in place at the University's vendors are adequate and functioning properly. Ms. Singer then turned members' attention to a chart that summarized the results of this review, and noted that Employee Benefits is pleased to present a full menu of SOC 1 reports with unqualified opinions for 2011. This is the first year for these reports, and the third consecutive year of clean audit reports from all the University's recordkeepers since these formal report summaries began in 2006.

VIII). Moving on, Ms. Singer distributed a fee disclosure analysis for the University's retirement plan assets as of December 31, 2011. She walked members through the analysis and highlighted the following:

- Total annual fees paid to Securian for 2011 were slightly over $7 million. A majority of the $7 million in fees is attributable to the "all in" fees, which includes the fees paid by participants to the various investment managers on those funds for which the individual investment manager provides both recordkeeping and investment management services, e.g., General Account.
- In 2011, Securian charged the University approximately $580,000 for recordkeeping, which is relatively flat from 2010.
- Total 2011 annual fees for all the University's retirement plans was just over $15 million, declining from $16.6 million in 2010.
- If fees had only been incurred on those funds under investment management it would result in an average basis point of 43 for all the University's retirement plans combined, again, down from 47 basis points on average in 2010.
- Total fees paid decreased in 2011 for the first time in the past six years at a rate of 7.1% though overall assets increased at a modest 1.4% for the year. The overall decline in fees may be attributable, at least in part, to the additional review investment providers

have done to their fee structures in preparation for the new fee disclosure regulations, which will take effect in 2012.

Professor Feeney thanked Ms. Singer for her reports.

IX). Prior to adjournment, Professor Hanna thanked Professor Feeney for chairing the committee this past year. Hearing no further business, Professor Feeney adjourned the meeting.

Renee Dempsey
University Senate