Commonwealth of Massachusetts
Deferred Compensation Committee
Meeting Minutes

March 6, 2018

One Ashburton Place, 12th Floor
Boston, MA 02108

Committee Members Present:

- Robert Sheridan, Committee Chair
- John Curran, Committee Member
- Tom Magno, Committee Member

Also present for all or part of the meeting were: David Lynch, Executive Director, Defined Contribution Plans; Nicola Favorito, Deputy Treasurer / Executive Director, State Retirement Board; Henry Clay, Treasury Director of Investments; Laura Rooney, Director of Operations, Defined Contribution Plans; Giuseppe Caruso, Operations Associate, Defined Contribution Plans; Emily Robbins, Defined Contribution Plans Counsel; Kevin Vandolder, Principal, Aon Hewitt Investment Consulting, Inc.; Beth Halberstadt, Partner, Aon Hewitt Investment Consulting, Inc.; Chris Behrns, Senior Consultant, Aon Hewitt Investment Consulting, Inc.; Phyllis Thomas, Portfolio Manager, NWQ; and Anthony Maramarco, CFA, Managing Director, Portfolio Adviser, NWQ.

I. Opening:

With all Committee Members present, call to order by Committee Chair Mr. Sheridan at 10:00 a.m.

Before beginning with the agenda for the Committee Meeting, Mr. Sheridan wished to comment that it was great to be in the Crane Conference Room, named after former State Treasurer Robert Q. Crane. Mr. Sheridan noted what an outstanding public servant Mr. Crane had been for the Commonwealth.

Mr. Sheridan also congratulated Mr. Curran for his recent reappointment to the Deferred Compensation Committee. Mr. Sheridan noted how invaluable both Mr. Curran and Mr. Magno were to the Committee. Mr. Lynch agreed with Mr. Sheridan and noted that Mr. Curran had been one of the first to suggest expansion of the participant communication materials, which have since become highly successful. Mr. Lynch noted that this also led Plan staff to work with separate account managers to create custom fact sheets. Mr. Sheridan appreciated all the efforts of both Mr. Curran and Plan staff.

II. Approve Minutes:

Mr. Sheridan cited no errors on the minutes but recalled that Mr. Vandolder was promised follow-up from Ms. Shelby Dobson of Empower Retirement regarding the source of various industry benchmarks as pertains to participant communication materials distributed via email. Ms. Rooney responded that the source was in fact provided. Mr. Vandolder confirmed that Ms. Dobson had sent the information a few days following the prior Committee Meeting.

Mr. Sheridan asked for a motion to approve the minutes of the December 7, 2017 meeting. Mr. Curran made the motion to approve the minutes. Mr. Magno seconded the motion and Mr. Sheridan also articulated his approval.

III. Executive Director's Quarterly Update:

- SMART Plan Key Statistical Data: Mr. Lynch directed the Committee's attention to the key points included in the SMART Plan Key Statistical Data Chart that was included in his memorandum. Mr. Lynch noted a rise to over $8.96 billion in Plan assets at the end of the third quarter, up $307 million from the previous quarter. Mr. Lynch then informed the Committee that Plan assets had in fact continued to rise and were $9.1 billion as of March 5, 2018. Mr. Lynch also noted that Mr. Vandolder would speak to the recent market volatility during the Market Review.

    - Mr. Lynch stated that the average full-time participant account balance had risen from just under $76,000 to over $80,000.

    - Mr. Lynch discussed distributions from the Plan, including full withdrawals from the Plan. Per Mr. Lynch, the total full withdrawal figures for 2017 surpassed $65 million, rising over $12 million from the 2016 figure. Mr. Lynch remarked that Plan staff would continue to monitor full withdrawals, particularly large balance accounts. However, Mr. Lynch noted that the larger balance withdrawals, as compared to 2016, were partly a result of strong market performance as well.

    - Mr. Lynch directed the Committee's attention to the Empower Retirement data, as related to participant full withdrawals. Mr. Lynch noted that there were 31,349 termed participants as of the end of 2017, with a total balance of $3.1 billion. Mr. Lynch also cited that 17,318 participants had account balances of over $150,000, which accounted for a total of $5.6 billion in Plan assets. Mr. Lynch reiterated that retention of these high balance accounts remained a priority.

- Mr. Favorito asked Mr. Lynch who is classified as a termed participant. Mr. Lynch responded that a termed participant was a participant with term date on file with the recordkeeper, which could include someone who was retired, about to retire, or whose employment with the employer had ended.

- Mr. Curran asked whether Plan participants could take a withdrawal from their Plan assets prior to retirement. Mr. Lynch responded that, per 457(b) regulations, that participants could access their Plan assets without penalty once they are terminated.

- Mr. Sheridan asked Mr. Lynch to confirm whether participants could remain in the Plan, should they leave service for outside employment. Mr. Lynch confirmed that participants can no longer make contributions to the Plan, they are eligible to remain in the Plan.

Mr. Lynch continued on the subject of withdrawals and reiterated that full withdrawals totaled over $65 million for the past year. Mr. Lynch remarked that Plan staff are targeting these accounts and discussing how best to retain these assets. Mr. Lynch cited efforts to educate participants about the ability to remain in the Plan following separation of service, as well as the ability of participants to consolidate their eligible retirement plan assets into the Plan.

- <u>H29 – An Act Relative to the SMART Plan</u>: Mr. Lynch informed the Committee members that House Bill 29 (H29) would create an automatic enrollment feature for the SMART Plan for all future state employees and give an option for the same to participating municipalities. Mr. Lynch noted that the Joint Committee on Public Service has agreed to extend the bill reporting deadline to the end of month to allow for further in-depth discussion. Mr. Lynch stated that to-date the response has been positive and that he would shortly be meeting with the Chair of the Committee on Public Services. Mr. Lynch stated that he then hoped for the Bill to be referred to the Joint Committee on Ways and Means. Mr. Lynch added that 13 states have adopted auto-enrollment for their public employees, with South Dakota further expanding their existing auto-enrollment feature to include any existing state employee not participating in their deferred compensation plan as of June 30, 2019.

  - ❖ Mr. Sheridan asked Mr. Lynch if there had been any opposition to the Bill thus far. Mr. Lynch responded that there was not.

  - ❖ Mr. Magno asked if the municipalities would have the option to join the auto-enrollment program. Mr. Lynch confirmed and noted that this would be available as an optional amendment to the Joinder Agreement.

  - ❖ Mr. Curran thanked Mr. Lynch for his efforts. Mr. Curran then asked Mr. Lynch who else was on the Committee on Public Service. Mr. Lynch stated that he would follow up and provide a link to the legislation that would include the status of the bill as well as the respective committee members assigned.

- Mr. Curran and Mr. Sheridan both asked if there was anything the Committee could do to further support the Bill. Mr. Lynch expressed his thanks and reminded the Committee of their letter of support that had previously been submitted to the Joint Committee on Public Service on July 10, 2017. Mr. Sheridan added that Mr. Lynch should keep the Committee in mind given that the Bill must still be referred to the Joint Committee on Ways & Means.

- Enhanced Glide-Path Services: Mr. Lynch recalled the past Committee Meeting question regarding trigger point rebalancing of the SMARTPath funds. Mr. Lynch stated that Alliance Bernstein (AB) had determined that its solution of "trigger point" rebalancing was more efficient than periodic rebalancing. Mr. Lynch explained that under this new process allocations in the SMARTPath funds are checked versus their strategic target by AB on a monthly basis. Mr. Lynch added that rebalances would be triggered if a single sleeve deviates by +/- 5% absolute or +/- 50% relative to target, as well as a few other potential trigger points based on cost and risks, at which point a rebalance would occur halfway to the strategic target. Mr. Lynch stated that, as part of their Enhanced Glide-Path Services, AB has taken over the rebalancing service from Empower Retirement. Mr. Lynch added that AB had also completed both the SMARTPath microsite and SMARTPath fund fact sheets. Mr. Lynch thanked AB, Ms. Rooney, and Mr. Caruso for their work on these. Mr. Lynch noted the functionality of SMARTPath microsite, which he said allows participants to enter their year of birth to determine which SMARTPath target date fund is most appropriate for them.

    - Mr. Curran stated that he considers both the microsite and fact sheets as valuable pieces of information for participants to have, especially those that are considering moving funds out of the Plan.

- Active Choice Enrollments Summary: Mr. Lynch next directed the Committee to the Active Choice Enrollments Summary chart included in his memorandum. Mr. Lynch commented on the continued success of the program, with nearly 1,200 employees (23%) having enrolled in the Plan in 2017 utilizing the Active Choice Enrollment Form. Again pointing to the data in his memorandum, Mr. Lynch noted that the full-time participant breakdown between state and municipal employees was included in response to a question from Mr. Sheridan posed at the previous Committee Meeting. Mr. Lynch stated that while the full-time participants were split almost evenly between state and municipal employees in 2016, that the figure for state employees had risen to 57% for 2017. Mr. Lynch referred to the Active Choice Enrollment Form as one of the factors explaining this rise, as the Active Choice Enrollment Form is currently unavailable to municipalities.

    - Mr. Curran voiced appreciation for the information and pointed out the noticeable drop in employees electing to decline participation in the Plan as further proof of the success of the Active Choice Enrollment Form. Mr. Lynch agreed. Mr. Lynch then continued by highlighting for the Committee how most participants had elected to contribute on a percentage basis, which was very favorable. Mr. Curran agreed. Ms. Rooney then added that electing to contribute on a percentage basis instead of a dollar amount would be beneficial to participants who are less engaged in their Plan account, as their contributions would increase automatically whenever there are salary increases.

  - Mr. Magno asked if participants would be auto-enrolled on a percentage basis should House Bill 29 pass. Ms. Rooney responded that they would be.

- <u>NWQ Investment Management – Small Cap Value Strategy Downgrade</u>: Mr. Lynch stated that the NWQ Small Cap Value Strategy, which represents a 20% allocation within the Small Company Stock Fund, had recently been downgraded by Aon Hewitt from "Buy" to "Qualified" following the recent announcement of a new equity buyback transaction. Mr. Lynch noted that in December, NWQ announced that they would be replacing their existing equity program with a long-term incentive program ("LTIP"). Mr. Lynch stated that NWQ partners had sold their equity to parent company Nuveen, and that the LTIP caps additional participation. Mr. Lynch also noted that, per the agreement, Portfolio Manager Phyllis Thomas would be able to receive a full payout of the LTIP before the 5-year vesting period. Per Mr. Vandolder, based on this component of the agreement, there is a question about the succession plan and there is a concern that Ms. Thomas may be likely to retire within the next five years.

  - Mr. Curran asked Mr. Vandolder if these were, in fact, the type of investments that would normally perform well under the new tax reform plan. Mr. Vandolder responded in the affirmative. Mr. Vandolder then added that it was unusual to sell off buybacks and that Aon Hewitt would prefer to see more equity held by NWQ.

  - Mr. Behrns continued and stated that, in Aon Hewitt's discussions with NWQ, it seems that NWQ did not want to go in the direction of selling to Nuveen, but rather that NWQ wanted to purchase more of their own equity from Nuveen. Mr. Behrns stated that Nuveen, meanwhile, wanted to own 100% of NWQ, and that Nuveen has acted similarly with its other boutique managers. Mr. Behrns noted that NWQ was concerned that this would not put them in a favorable situation from a distribution and marketing perspective.

  - Mr. Sheridan asked Mr. Behrns if Nuveen had been acquired by TIAA recently. Mr. Behrns confirmed that the acquisition occurred three years prior.

- <u>Account Retention Initiatives</u>: Mr. Lynch referred to the earlier discussion on account retention and how it remains a priority for the Plan. Mr. Lynch discussed a few initiatives this year which would seek to address this objective.

  - <u>Retiree Readiness Meetings:</u> Mr. Lynch informed the Committee that Retirement Readiness Meetings should help employees understand their options in retirement. He stated that for the coming year, the goal is to have 3,600 Retirement Readiness Meetings, which would be roughly five meetings per week per retirement plan advisor (RPA). In addition, Mr. Lynch noted that a short survey would be distributed to meeting attendees in an effort to identify the primary needs of these participants.

- <u>Retiree Advocate Seminars:</u> Mr. Lynch stated that these seminars would be similar thematically to the Retiree Readiness Meetings, however, these seminars would also promote the unique benefit of access to an RPA, Mr. Sean Brennan. Mr. Lynch noted that these would be promoted at both quarterly payroll user group meetings and in the Massachusetts State Retirement Board quarterly bulletin.

- <u>STAY Campaign:</u> Mr. Lynch noted the success of the STAY Campaign in 2017 and informed the Committee that the STAY Campaign would be implemented in 2018 as well. Mr. Lynch reminded the Committee that the STAY Campaign is a multi-channel approach to informing participants of the benefits of staying in the Plan post-retirement or upon termination from employment, as applicable. Per Mr. Lynch, this multi-channel approach includes a targeted email campaign, website banner, newsletter article, and a flier, all of which highlight the potential benefits of remaining in the Plan.

    - Mr. Curran asked if, for future campaigns, these communications could also be available on the website post-login. Mr. Sheridan also expressed his interest in whether that is a possibility. Ms. Rooney responded that she would refer the question to Empower Retirement to see if there is availability on the new website for all communication pieces. Ms. Rooney cautioned that while the new Plan website offered several advantages over the previous generation in terms of functionality for participants, customization was more limited. Mr. Curran noted that he was unaware of this challenge. Ms. Rooney stated that she would still ask the question.

    - Mr. Curran then commented that it is key is to identify why and where participants are moving their money, as well as what the motivating factors are, so that they can be addressed in future campaigns. Mr. Lynch agreed and reiterated that the surveys following Retiree Readiness Meetings would hopefully garner this feedback. Mr. Curran agreed. Ms. Rooney also agreed and stated that this would be the most appropriate way to identify participant concerns so that they could then be addressed. Ms. Rooney referred to the STAY Campaign email, which referenced the ability to consolidate assets into the SMART Plan. Per Ms. Rooney, this information was added as a direct result of past participant surveys where a desire to consolidate had been cited as a primary motivation to move assets out of the Plan.

    - Mr. Curran referred back to the participant full withdrawal data and cited the large number of participants taking full withdrawals from separation of service as opposed to retirement. Mr. Lynch responded that there would be several small balance accounts which would likely be withdrawn following separation of service, but that the goal was to achieve large balance account retention. Mr. Lynch referred to the Retirement Solutions Group (RSG) as a possible new service available through Empower that may be available to the Plan and which would be dedicated to engaging participants about the Plan from enrollment through to retirement. Mr. Lynch stated that he is hopeful that the RSG service can be added, as it will be an additional resource to educate participants throughout their public service and through retirement.

- Mr. Magno stated that, in his experience, local participants cited lack of consolidation and portability as primary concerns, despite the Plan offering consolidation of assets. Mr. Magno asked Mr. Lynch if there was an issue with participants that had multiple IRAs that they wished to consolidate. Mr. Lynch asked Mr. Magno if he was referring to ROTH IRAs. Ms. Rooney noted that Roth IRAs could not be consolidated into the Plan or even into a 401(k), but most other money types could be transferred into the Plan. Ms. Rooney explained that Roth IRAs were the most restrictive in terms of portability, as they can only be transferred into other Roth IRAs. Mr. Curran noted that this was all good information. Mr. Magno then commented that the biggest challenge to retention of Plan participants and their assets were local brokers which advertised the ability to consolidate all retirement accounts, despite potentially higher fees.

- Ms. Rooney, addressing Mr. Curran's previous question about full withdrawals via separation of service, noted that some of those classified as separation of service could in fact also be retirees, as opposed to strictly those separated from service without retiring. Mr. Curran then pointed to the data showing the high number participants taking a full withdrawal in the third quarter of 2017. Ms. Rooney responded that this was a one-off event as a result of the Harding Loevner refund that had occurred, wherein several previously closed accounts were briefly reopened in order to issue a check for the refund amount owed to the participant.

- <u>NAGDCA Benchmarking Report Date Relative to Peers and 2016 Results</u>: Mr. Lynch began by thanking Ms. Rooney and Mr. Caruso for gathering the data necessary to complete the 2016 NAGDCA Benchmarking Report. In the interest of time, Mr. Lynch asked the Committee if they wished to do an in-depth analysis of the data at the following Committee Meeting.

  Mr. Curran made a motion to table the discussion of the NAGDCA Benchmarking Report data for the next Committee Meeting. Mr. Magno seconded the motion.

Mr. Sheridan asked the Committee members for any additional questions on the Executive Summary. With no further questions, Mr. Sheridan suggested moving on to the Market Review.

IV. Market Review, Recommendations, Highlights and Performance Update: Aon Hewitt

- Directing the Committee to Tab 5 of the meeting materials, Mr. Vandolder began speaking on Market Highlights for the Plan. Mr. Vandolder stated that current performance indicated the late stages of a bull market. Mr. Vandolder noted that the S&P 500 finished

2017 up 21.8%, and that as of close of business on March 2, the S&P 500 was up 1% thus far in 2018, despite recent volatility. Mr. Vandolder noted that Russell 2000 Small Cap had 0% growth year to date, but was up 14.6% in 2017. Mr. Vandolder stated that the MSCI EAFE markets were up 25% in 2017, but they had dropped 2% year to date. Mr. Vandolder added that the MSCI Emerging Markets were up over 37% for 2017, and up 2.2% year to date.

Mr. Vandolder continued with a look towards the rising rate market, evidenced in February. Mr. Vandolder called attention to the Barclays Intermediate Bond, which he noted was down 2% year to date. Mr. Vandolder remarked that he found this data interesting, and wondered how participants would react to losing money on bonds. Mr. Vandolder also referenced the Barclays Long Government Bond down 5% year to date, and pondered whether this data was an indication of a potential bond bubble.

- Mr. Vandolder suggested there were three primary indicators watched in monitoring for possible recession conditions. First, per Mr. Vandolder, is housing permits, which he stated did not show expansion like past years. Specifically, Mr. Vandolder noted that to avoid recession, housing permits should be rising at 1.5% for expansion, and were currently just under that rate at 1.4%. Second, Mr. Vandolder opined that an inversion in the yield curve was often an early indicator of recession. According to Mr. Vandolder, to-date the curve had flattened, but not inverted. Third, Mr. Vandolder stated that monitoring the consumer end of the market could illuminate broader strength or weakness in the markets. He added that current market conditions with respect to both consumer jobs and consumer net worth in the U.S. were strong. With these three indicators showing good signs, Mr. Vandolder indicated the overall market condition was still positive.

- Mr. Vandolder stated that while some are concerned regarding a potential student loan crisis, he pointed out that 92 cents of every dollar in student loans is government-backed. Mr. Vandolder continued and noted that the issue of student loans was not similar to the subprime mortgage crisis because this would directly impact government finances.

- Mr. Vandolder concluded his comments on the Market Highlights by noting that there are currently 415 million millennials in China, or roughly 115 million more than the United States, Canada, and West European combined. Mr. Vandolder cited this as a positive sign for emerging markets. Mr. Vandolder noted the sizeable equity exposure in target date funds and that the long-term horizon remained positive overall.

    - ❖ Mr. Sheridan asked Mr. Vandolder for his thoughts on recent or potential government changes as it relates to the economic environment. Mr. Vandolder responded that, from an economic perspective, the Trump administration has been fairly similar to the previous administration in terms of stable interest rate rises and quantitative easing. Mr. Vandolder also noted that up until recently, European junk bond yields were actually lower than US 10-Year Treasury Bond yields, at 2.1% and 2.7%, respectively. Mr. Vandolder further added that subsequently, the European junk bond yields had quickly risen to their current rates at just under 3%.

In addition, Mr. Vandolder noted that the substantial quantitative easing that has flooded money supply needs to unwind.

❖ Mr. Magno asked if these should be viewed as signs of a bullish market. Mr. Vandolder responded in the affirmative and stated that these conditions should continue. Mr. Vandolder cited the example of Amazon, which had a PE ratio of 240. Mr. Vandolder stated that the market valuations currently were very high and that these were frightening number to most investors.

❖ Mr. Magno asked Mr. Vandolder if he knew the savings rate for 2017. Mr. Vandolder responded that the answer on this would depend on Mr. Magno's definition of "savings." Mr. Magno remarked that some economists were concerned that people are saving too much as opposed to investing and he clarified that he was referring to a bank savings account. Mr. Vandolder answered that did not have that information but he could follow-up on it.

❖ Mr. Sheridan asked if there were concerns of a "day of reckoning" on the horizon financially. Mr. Vandolder stated that there was the potential of a bubble, but that those were obviously difficult to identify in advance of the occurrence.

❖ Mr. Sheridan then referenced the previous Committee Meeting where Mr. Lynch had discussed the potential for investment in infrastructure. Mr. Vandolder responded and pointed to the Australia deferred compensation plan as having instituted infrastructure investment in participant directed plans. Mr. Vandolder reiterated that these investments were not available in the United States yet, and that the Commonwealth of Massachusetts would be a trailblazer should it elect to invest in infrastructure. Mr. Vandolder warned that given the investment, fees would likely rise. However, Mr. Vandolder also stated that as the investments would primarily be in highways, buildings, and other infrastructure, asset changes would be smooth. Mr. Vandolder noted the challenges of this type of investment, namely daily valuation and daily liquidity, which lead to higher fees.

Mr. Sheridan asked whether Aon Hewitt would advise for infrastructure investment. Mr. Vandolder responded that Aon Hewitt could prepare an educational session for the Committee regarding the investment.

Mr. Magno asked Mr. Lynch if there would be difficulty in pursuing this type of investment from a legislative perspective. Mr. Lynch responded there could be, but he would need more information on it. Mr. Magno asked if any other states or countries currently had infrastructure investments. Mr. Vandolder responded that Australia does currently, with about $2 billion in assets invested.

Mr. Lynch asked Mr. Vandolder where an infrastructure investment option would fall in the Glide-Path. Mr. Vandolder responded that as it would be a mixture between stocks and bonds, and it would depend on the type of infrastructure. Mr. Vandolder stated that these types of investments would typically be labelled as an alternative fund. Mr. Behrns then added that these investments were slightly similar to real estate, however, infrastructure investments work solely with the funds available to them.

- ❖ Mr. Sheridan asked how valuation of infrastructure investment would work. Mr. Vandolder responded that full insight would likely involve another meeting, but that Aon Hewitt could show what other countries were currently doing. Mr. Sheridan voiced his appreciation.

- Mr. Behrns directed the Committee to slide 48 on U.S. Equity Markets, framing the discussion around NWQ's performance in 2017. Mr. Behrns called attention to the large differential between Russell Style Returns for Small Value and Small Growth, which grew 7.8% and 22.2%, respectively, in 2017. Mr. Vandolder added that while NWQ, which had a 13.1% return for 2017, was below Russell Style Return for Small Growth, it outperformed Small Value, which was more aligned with the NWQ Small Cap Value Strategy.

- Mr. Behrns shifted the discussion to U.S. Fixed Income Markets. Mr. Behrns stated that one of the Plan's detractors was the unconstrained mandate managed by Reams Asset Management. Mr. Behrns stated that longer termed bonds had done well in 2017, with 10.5% returns for 10-Year Bonds. Mr. Behrns noted that this would be reversed for 2018 following higher interest rates, resulting in reduced yields.

- Moving on to Manager Research Items, Mr. Behrns continued the discussion on Aon Hewitt's recent downgrade of NWQ from "Buy" and "Qualified". Mr. Behrns explained that the Nuveen buyback of NWQ shares and NWQ discontinuing its equity program in favor of a long-term incentive program (LTIP) was a factor which led to this downgrade by Aon Hewitt's analysts. Mr. Behrns stated that as a result of the Nuveen buyback NWQ employees would no longer be able to acquire equity in the firm, which was viewed as a more compelling incentive than a standard performance bonus. Mr. Behrns stated the Aon Hewitt viewed this as a step in the wrong direction.

  Mr. Behrns continued speaking on the subject of NWQ noting that Ms. Phyllis Thomas would be presenting today on behalf of NWQ, and that Aon Hewitt puts a high degree of confidence in her as a lead portfolio manager. Mr. Behrns again mentioned concerns about the LTIP program and noted that Ms. Thomas would not need the full five-year vesting period normally required for the LTIP benefits in order to receive her full allocation.

  - ❖ Mr. Sheridan asked Mr. Behrns if he thought it may be an appropriate time to consider a new investment manager search to replace NWQ. Mr. Behrns responded that he did not believe that to be appropriate now. Mr. Behrns expressed the high degree of confidence Aon Hewitt has in Ms. Thomas and articulated that the possibility of Ms. Thomas leaving NWQ is why Aon Hewitt has qualified NWQ as "qualified" and not "buy" rated. Mr. Behrns then stated that, given the multi-manager structure of the Small Company Stock Fund, of which NWQ has 20%, there are other two managers holding assets in this portfolio, each of which would be available to accept NWQ's share of assets should there be any future concerns.

- Continuing the discussion, Mr. Vandolder noted that the Small Company Stock Fund accounted for roughly 7% of all Plan assets. Mr. Vandolder also stated that Plan assets with NWQ totaled roughly $120 million which, though not insignificant, could still be transferred amongst the other Small Company Stock Fund managers should the Plan cease its investment in NWQ. Mr. Vandolder stated that NWQ assets could be split evenly between the DFA Small Cap Portfolio and the PENN Small Cap Equity, or it could even be transferred to Northern Trust Russell 2000 liquidity pool.

- Mr. Behrns reiterated to the Committee that he did not want Aon Hewitt's "Qualified" rating to be considered a negative. Mr. Behrns noted that these ratings are based on long-term investment views.

    - Mr. Sheridan asked if the positive investment outlook relied on Ms. Thomas remaining with NWQ. Mr. Behrns confirmed that it did. While not currently applicable to the Small Company Stock Fund mandate, Mr. Lynch noted that through its procurement process for the Plan, the Treasury has recently and will continue to add a bench of pre-qualified investment managers, which should help if the Plan elects to divest from a given manager over time. Mr. Sheridan asked how long the RFR process would take. Mr. Lynch responded that it could take roughly twelve to eighteen months.

    - Mr. Magno asked if Ms. Thomas was currently in the five-year vesting timeframe required for the LTIP. Mr. Vandolder noted that, per her negotiations, Ms. Thomas was already vested.

- Finally, turning attention to the Diversified Bond Fund, Mr. Vandolder noted that despite Reams Unconstrained Bond performing 2% lower than benchmark for 2017, the Diversified Bond Fund had a 5% return for 2017. Mr. Vandolder cited the Loomis Sayles Core Plus Fixed Income investment as a key driver of this return, noting that Loomis Sayles had positioned itself well in regard to long interest rates, given the economic environment.

    - Mr. Sheridan asked if there was anything to be concerned about going forward. Mr. Behrns responded that Aon Hewitt had no additional items at the moment.

Mr. Sheridan asked the Committee members if there were any further questions. Mr. Curran and Mr. Magno responded in the negative. With no further questions, Mr. Sheridan suggested moving on to the NWQ Small Cap Value Strategy Review.

V. NWQ Small Cap Value Strategy Review

At the invitation of the Plan, representatives from NWQ, who oversee the NWQ Small Cap Value separate account strategy for the Plan, were invited to present before the Committee.

Present on behalf of NWQ was: Phyllis Thomas, Portfolio Manager, NWQ; and Anthony Maramarco, CFA, Managing Director, Portfolio Adviser, NWQ.

Mr. Sheridan welcomed the representatives from NWQ.

- Mr. Maramarco thanked the Committee for inviting NWQ in to present and introduced Ms. Thomas and himself.

- Mr. Maramarco began by providing an overview of organizational changes since November 2017, most noteworthy that at the end of the year, Nuveen once again became a 100% owner of NWQ. Mr. Maramarco explained there was a five-year period where NWQ partners were on track to acquire 40% of NWQ from Nuveen, however, that decision was overturned or reversed. Providing additional background, Mr. Maramarco explained that since 2002, Nuveen has performed certain functions (legal and technical) for NWQ and will now expand their role to include trading desk support and some marketing and sales; and according to Mr. Maramarco, all of which would be a benefit to NWQ.

- Mr. Maramarco recalled regular interactions and meetings with Mr. Clay, wherein Mr. Clay has asked if Nuveen's ownership would affect NWQ's investment philosophy or process. Mr. Maramarco explained that neither the philosophy nor process has changed or will change. Mr. Clay voiced his appreciation of Mr. Maramarco.

    - Mr. Sheridan asked about recent staff turnover at NWQ. Ms. Thomas, noting that Mr. Sheridan was likely referring the departure of executives including Head of Institutional Sales Mr. George Webb and Co-President Mr. John Conlin, understood the concern. Ms. Thomas noted that Mr. Conlin's role was primarily in institutional administration and that the role would be going away as a result of the consolidation. Ms. Thomas stated that Mr. Webb had moved to another firm, and also that another senior analyst, Mr. Gregg Tenser, had decided to leave NWQ as well. According to Ms. Thomas, Mr. Tenser's decision to depart NWQ was the result of Nuveen deciding not to seed a new product. Mr. Sheridan asked if there were any additional departures anticipated. Ms. Thomas replied that there had been some support people who have left the firm, but the people she named were the senior-level folks who had departed. Mr. Maramarco then added that, at the senior staff level, there were no imminent departures expected.

At the juncture, Ms. Thomas asked the Committee whether they would prefer a discussion on the process or performance of the portfolio. Mr. Sheridan deferred to Mr. Lynch. Mr. Lynch suggested a review of the portfolio performance.

- Prior to the performance analysis, Ms. Thomas began with a brief view into the portfolio process, which she said is based on risk-reward. Ms. Thomas stated that a majority of the time NWQ attempts to find and analyze what they view as mispriced stocks and consider what the problems are and how to resolve them. In particular, Ms. Thomas explained that NWQ does not rely on historical PE ratios, stating that "PE ratios are moving parts you must seek to understand." Ms. Thomas noted common catalysts regarding investment decisions, such as potential management "epiphanies" or new management coming into a company. Ms. Thomas cited other key indicators, such as new revenue and cost controlling, as other potential factors to determine investments.

- Ms. Thomas transitioned to the discussion on performance. Ms. Thomas noted the current year to date underperformance but referred back to the strong performance overall in 2017 with a 13.9% return, compared to the 7.8% benchmark return.

  - Mr. Vandolder asked Ms. Thomas whether NWQ carries cash as a defensive. Mr. Thomas responded that NWQ does not do defensive. Ms. Thomas stated NWQ is pretty liquid compared to historically and further that it is rare for NWQ to be with no cash, particularly with the run up in the markets. Mr. Vandolder asked Ms. Thomas if she was talking about tax reform. Ms. Thomas replied in the affirmative. Rising interest rates, deregulation, have been very powerful for smaller companies.

  - Mr. Magno asked Ms. Thomas whether NWQ placed more importance on the mechanical process or personnel's ability to identify the right investments. Ms. Thomas responded that while the process remains important, ultimately judgement was required. Ms. Thomas noted that NWQ does not utilize screeners, instead preferring to visit the companies identified as potential investments. Ms. Thomas again stressed the importance of identifying companies they viewed as mispriced, in an effort to buy in at a lower price level. Ms. Thomas stated that this often involves waiting for market corrections.

  - Referring back to the initial question, Mr. Maramarco asked what Mr. Magno meant by mechanical process. To clarify his initial question, Mr. Magno asked if the NWQ investment formula had reached a point where employees could be plugged into a role and execute the NWQ investment strategy. Ms. Thomas responded that this was not the case. Ms. Thomas reiterated that NWQ did not use historical PE ratios, but instead, they develop analysis on best case and worse case scenarios in order to determine potential risk/reward for a given investment. Ms. Thomas stated that NWQ analysts were tasked with understanding their industry of expertise, the supply and demand in the industry, and management teams for the investments. Ms. Thomas again acknowledged the importance of judgement in determining investments. Mr. Maramarco continued and spoke on the experience of the NWQ Global Investment Team, noting that all current analysts have over a decade of experience. Mr. Maramarco stated that in the investment business, experience matters, as there is a lot to absorb about the industry over time, some of which may assist in a decision to be made years down the road.

  - Mr. Behrns asked Ms. Thomas about her collaboration with Mr. Andy Hwang, Portfolio Manager, and whether they regularly involved interactions on the topic of the addition or removal of an investment. Ms. Thomas responded that the collaboration was constant, and that generally NWQ analysts collaborate regularly. Ms. Thomas described that every week she and Mr. Hwang do calls with company management teams. Ms. Thomas stated that she and Mr. Hwang have worked together for 17 years and she has full confidence in his ability and decision making, should she ever be unavailable for a particular investment decision.

- ❖ Mr. Vandolder asked Ms. Thomas how NWQ felt in regard to rising interest rates in recent months. Ms. Thomas responded that NWQ saw this as an opportunity, suggesting a clear return of value strategy compared to growth, favoring NWQ. Ms. Thomas stated that growth strategies and investments had become much more expensive recently. Ms. Thomas said that she believes spreads would continue to widen and that the small cap sector would benefit greatly from the current tax reform.

- Turning to the performance overview by sector, Ms. Thomas began by citing NWQ's strong performance in technology, noting that several companies were purchased as turnarounds. Ms. Thomas stated that despite the underweight in financial services investment compared to the Russell 2000 Value Index – 27.8% to 42.5% – NWQ had better returns as a result of stock selection. Ms. Thomas noted that REIT investments had struggled. Despite the struggles, Ms. Thomas cited potential positives for the future. Ms. Thomas also pointed to investment in Ramco-Gershenson Properties Trust, a Michigan-based REIT with investment in strip malls. Ms. Thomas commented that despite recent underperformance, NWQ viewed this investment as reasonably undervalued with opportunity to grow.

12:00 pm At this time, Mr. Lynch and Mr. Favorito exited the Meeting.

- Ms. Thomas concluded with consumer stables. Ms. Thomas cited Treehouse Food Inc as a problem in 2017, and that NWQ ultimately sold their position. Ms. Thomas noted that performance continued to decline following the divestment. Ms. Thomas stated that mismanagement and a difficult food environment were contributing factors to the decline. Ms. Thomas noted that Treehouse Food Inc did have the potential to rebound, as the former CEO of Smucker's would be coming into the management team. Ms. Thomas stated that they would continue to monitor Treehouse Foods Inc for future investment.

- To conclude, Ms. Thomas stated that she believed NWQ had performed well in 2017, but that they would continue to improve.

- ❖ Ms. Rooney asked Mr. Maramarco if his departure from NWQ was imminent, in regard to recent news of his retirement. Mr. Maramarco confirmed he would be retiring effective May 4th, 2018.

- ❖ Mr. Sheridan asked Ms. Thomas if she intended to remain with NWQ. Ms. Thomas responded that it was her intention to remain as long as she was healthy, and that she continued to enjoy her work. She said she has no plans to retire and really loves her work.

12:05 pm Mr. Sheridan thanked Mr. Maramarco and Ms. Thomas for their presentation and insight. Mr. Maramarco and Ms. Thomas both thanked the Committee once again for having them.

VI. Miscellaneous

- Mr. Curran wanted to note, once again, that the Committee would be revisiting the 2016 NAGDCA Benchmarking Report at the next Meeting.
- Mr. Magno asked that it be relayed to Mr. Lynch his interest on whether there was any research data in regard to how the Plan's investments have performed relative to investments of other government deferred compensation plans. Mr. Vandolder responded that this would be difficult to research or analyze due to the participant-directed nature of the Plan. For example, Mr. Vandolder cited that Plan participants have roughly 60% of their investments in equity, which was a larger percentage share than many other plans. Mr. Vandolder stated that the most appropriate comparisons for investment performance would be relative to established benchmarks.

VII. Future Meeting Dates

Mr. Sheridan asked for future meeting dates to be determined based on what would be most convenient for attendees. Mr. Sheridan noted that Mr. Lynch mentioned early June for potential availability. Ms. Rooney responded that she would gather all available dates and forward them to the Committee members to establish what would be most convenient. Mr. Sheridan thanked Ms. Rooney.

VIII. Close of Meeting

12:18 p.m. Close of Meeting.

- Motion to adjourn by Mr. Curran and seconded by Mr. Sheridan.

Documents Used at the Deferred Compensation Committee Meeting of March 6, 2018

- Agenda for the March 6, 2018 Deferred Compensation Committee Meeting;
- Executive Director's Quarterly Update dated March 6, 2018;
- Minutes of the December 7, 2017 Deferred Compensation Committee Meeting;
- Plan Quarterly Highlights Report, Fourth Quarter 2017;
- Quarterly Investment Report, Fourth Quarter 2017;
- SMART-to-Stay Campaign Flier;
- NAGDCA Plan Performance Report; and
- NWQ Handout, March 6, 2018.