Commonwealth of Massachusetts
Deferred Compensation Committee
Meeting Minutes

September 20, 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, Counsel, Defined Contribution Plans; 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.; Steve Mortimer, Portfolio Manager, Wellington Management; Eileen Leary, Investment Director, Wellington Management; Jed Petty, Managing Director, Wellington Management; Jeff Edwards, Senior Relationship Manager, Vanguard Institution Investor Group; and Drew D. Schneider, CFA, Equity Product Manager, Vanguard Institution Investor Group.

I. Opening:

With all committee members present, Committee Chair Mr. Sheridan called the meeting to order at 10:00 a.m.

Before beginning with the agenda for the Committee Meeting, Mr. Sheridan complimented Mr. Lynch and the Plan staff, citing an email circulated by Mr. Lynch in July that announced the Plan as a recipient of the 2018 NAGDCA Leadership Award for the *Stay the Course – Stay SMART* campaign. Mr. Lynch voiced his appreciation for the work of the Treasury's Plan staff on the campaign.

II. Approve Minutes:

Mr. Sheridan cited no errors on the minutes of the June 13, 2018 meeting. Mr. Magno agreed.

Prior to a formal vote to approve the meeting minutes, Mr. Sheridan asked Mr. Lynch about the status of HB29, relative to a SMART Plan auto-enrollment feature. Mr. Sheridan also asked if statistics on other state governmental plans featuring auto-enrollment had been sent as part of a refiling. With respect to legislation for auto-enrollment, Mr. Lynch informed Mr. Sheridan that the bill needs to be refiled and he expected that the Treasury would indeed refile. In response to Mr. Sheridan's inquiry about auto-enrollment statistics in governmental plans, Mr. Lynch and Mr. Vandolder each noted that the best statistics would come directly from NAGDCA. Mr. Vandolder added that he would attend the upcoming NAGDCA Annual Conference, and voiced his intention to speak with NAGDCA President Keith Overly on this matter. Mr. Sheridan thanked Mr. Vandolder and Mr. Lynch, and asked Mr. Lynch to keep the Committee abreast of any legislative updates.

Mr. Sheridan asked for a motion to approve the minutes of the June 13, 2018 meeting. Mr. Magno made a motion to approve the minutes. Mr. Curran seconded the motion. Mr. Sheridan rounded out unanimous approval of the minutes.

III. Executive Director's Quarterly Update:

- SMART Plan Key Statistical Data: Mr. Lynch directed the Committee's attention to the important points included in the SMART Plan Key Statistical Data Chart that was included in his memorandum. Mr. Lynch reported that total Plan assets at the end of the second quarter were up 9.8% as compared to the previous year, totaling just under $9.2 billion, and had continued to rise to over $9.4 billion as of September 12, 2018. Mr. Lynch continued by informing the Committee that second quarter contributions were up over 18% as compared to the same quarter the year prior, with a total figure of over $110 million. Mr. Lynch noted that about $13 million of the contributions were attributed to plan conversions to the SMART Plan from Plymouth County, the Town of Amesbury, and the Town of Bernardston, but that with even with conversions eliminated from statistical consideration, contributions had still risen by over 9%. Mr. Lynch stated that the Plan continued to keep an eye on full-withdrawals but noted that the primary focus was on reduction of accounts taking full-withdrawals, rather than total dollars. Mr. Lynch added that total dollars withdrawn were important but could be inflated due to market performance. Nevertheless, Mr. Lynch cited an 8.8% increase in accounts that have taken full-withdrawals. Mr. Lynch referenced the recent addition of the Retirement Solutions Group (RSG) services through Empower Retirement as a way to address the issue of account retention. Finally, Mr. Lynch noted that the number of total full-time participants were up 3.2% compared to second quarter last year, average full-time participant account balances were up 6.8%, and average full-time participant contributions per quarter were up 14.4%.

- Mr. Magno asked what was causing the rise in participant contributions. Mr. Lynch replied that there were several factors, including improved participant communications and increased use of the auto-escalation feature, amongst others. Mr. Lynch next credited the improved participant communications, including the Restart and STAY Campaigns, as well as the general appetite for investment currently given strong market performance.

- Mr. Magno asked if the figures on increased contributions may be skewed due to increased catch-up contributions, given the older average age of Plan participants. Mr. Lynch responded that this could be a possibility.

- Ms. Robbins asked if more people contribute on a percentage or dollar basis. Ms. Rooney responded that most still do contribute on a dollar basis, but that there has been an increase in those contributing on a percentage basis. Ms. Rooney cited that the local Plan representatives have continued to promote contributions on a percentage basis. Ms. Rooney also noted that the Active Choice Enrollment Form defaults participants to a percentage contribution. Mr. Lynch added that roughly 95% of participants contributed on a dollar basis when he joined the Plan as Executive Director, citing it as the default of prior recordkeepers. Mr. Lynch also noted the comfort level people have with contributing on a dollar basis, knowing an exact dollar figure. Ms. Rooney confirmed and continued, articulating this as a likely cause of participant hesitation to switch to percentage contributions.

- Returning to the topic of total contributions, Mr. Lynch identified the new SMART Plan website as a potential source of increased deferrals rates. Specifically, Mr. Lynch stated that the website's new "slider" feature, which allows participants to instantly see what impact an increase in contributions could have on retirement income, and which also allows participants to confirm deferral changes with one click, has made making such changes easy. Mr. Sheridan thanked Mr. Lynch and noted that this was a great feature to have.

- Mr. Vandolder complimented the growth of Roth accounts in the Plan, noting the importance of diversification of income in retirement. Mr. Lynch agreed with Mr. Vandolder and stated that it was very positive to see the increase. Mr. Sheridan asked if the Committee could see an age breakdown of Roth participants at the next meeting. Mr. Lynch confirmed that he would provide this information.

- <u>Executive Order Regarding Retirement Accounts</u>: Mr. Lynch noted that the President signed an executive order on August 31, 2018 that encourages the Department of Labor and the Department of Treasury to push bipartisan changes to how retirement plans operate, changes that include relaxing multiple-employer plan (MEP) requirements, a review of Required Minimum Distribution (RMD) rules, and a review of paperwork and administrative requirements for workplace retirement plans.

  - With respect to the possible changes to the MEP requirements, Mr. Lynch noted that currently MEPs must share a commonality of interests, such as nonprofits or auto dealers. Mr. Lynch then added that a new bill to relax that requirement would increase plan efficiencies and reduce administrative costs.

- ❖ Mr. Sheridan asked if this would affect both public plans as well as private sector retirement plans. Mr. Lynch confirmed that it would. Mr. Magno asked what that would mean for the SMART Plan. Ms. Rooney responded that such a change would primarily affect the private sector, and that currently the Massachusetts Defined Contribution CORE Plan (CORE Plan), also administered by the Treasury staff, was the only governmental MEP. Mr. Behrns explained that the bill would further legitimize the MEP structure. Mr. Vandolder agreed and commented that at least 60 million Americans currently have no access to a workplace retirement plan, primarily in the small business sphere.

- ❖ Mr. Sheridan asked if this would amend ERISA. Mr. Vandolder stated that it would not amend ERISA but would be a change in Treasury regulations. Mr. Vandolder reiterated that this would legitimize the MEP structure, particularly important for the CORE Plan, so not relevant to the Plan overseen by the Committee. Mr. Magno asked if this would encourage expansion of MEPs. Mr. Lynch responded that it would definitely help the expansion in other states, noting that Vermont was currently working on their own government-sponsored MEP. Ms. Halberstadt also noted that a Michigan gubernatorial candidate was campaigning with a promise to create a governmental MEP for small businesses within the state.

- ❖ On the subject of the RMD review, Mr. Lynch noted that this would be done in an effort to delay RMDs beyond the current age of 70½ and/or reduce the minimum amount of the RMDs once they start. Mr. Vandolder stated that this was a Democratic initiative and noted that it was an expensive endeavor for the Department of Treasury to have taxes deferred from distributions.

- ❖ On the item of relaxing distribution standards, Mr. Lynch stated that any changes would likely remove the current requirement for paper document distribution in favor of electronic distribution, a more appropriate method for modern times.

- ▪ <u>Target Date Fund Re-balance</u>: Mr. Lynch informed the Committee that Treasury staff is working with Aon Hewitt and Empower to evaluate a REIT overweight within the target date funds. Mr. Lynch stated that Alliance Bernstein (AB) had identified the overweight when it assumed responsibility for rebalancing the glidepath from Empower Retirement in February 2018. Mr. Lynch stated that more detail would be forthcoming upon receipt of the full analysis from Aon Hewitt.

  - ❖ Mr. Curran asked what the overweight affected within the SMARTPath Funds. Mr. Lynch replied that the overweight affected SMARTPath vintages that had an allocation to JP Morgan Private Real Estate.

- RFR Emerging Markets Debt – TDFs: Mr. Lynch reported that an RFR to procure a blended Emerging Market Debt (EMD) strategy was issued on July 24, 2018, with final bids due by September 11, 2018. Mr. Lynch noted that the EMD allocation within the SMARTPath Funds was currently provided through the PIMCO Emerging Local Currency Fund.

- Statement of Work (SOW) for Audit Services: Mr. Lynch noted that the Treasury posted an SOW to procure audit services for the Plan on September 19, 2018.

  - Mr. Magno asked if the contract was for a five-year term. Ms. Robbins responded that it would be for a three-year term, through the audit of Plan Year 2020. Ms. Robbins continued, informing the Committee that the Treasury's Internal Auditor, Karen Guida, had identified seven firms off of the statewide contract list that would be capable of providing the services to a plan of this size, and that the posting was sent to all seven. Mr. Lynch added that there would be a meeting with KPMG the following day, September 21, 2018, to discuss potential dates for the Audit Advisory Board Meeting for Audit Year 2016.

  - Mr. Sheridan asked if the delays were caused by turnover at the firm. Ms. Rooney responded that while the partners have stayed the same, there had been significant turnover amongst the auditors who perform the day-to-day work. Mr. Curran noted that this is not uncommon amongst the Big Four accounting firms, citing difficulty with retention.

  - Mr. Sheridan asked if the Big Four were part of the list of seven firms referred to earlier. Mr. Lynch responded that PricewaterhouseCoopers (PwC) was not, and added that PWC was not on the list of approved statewide contract vendors. Ms. Robbins noted that some firms do not bid on public contracts. Mr. Curran stated he was surprised PwC was not an approved statewide vendor.

- Automatic Enrollment for SMART Plan: Circling back to a subject raised by Mr. Sheridan at the start of the meeting, Mr. Lynch informed the Committee members of the Treasury's intent to again file legislation which would create an automatic enrollment feature for the SMART Plan for all future state employees, with an optional adoption for participating municipalities. Mr. Lynch reminded the Committee that 13 states have already adopted auto-enrollment for their public employees, and the Plan was awaiting statistics and analysis on how different states have rolled-out auto-enrollment.

  - Mr. Curran asked if there had been any changes in the legislature. Mr. Lynch noted the departure of Joint Committee on Public Service Chair Rep. Jennifer Flanagan. Mr. Lynch also noted that there were some additional changes to the Committee but was uncertain if that would impact the legislation. Mr. Sheridan then commented on the upcoming departure of Joint Committee on Ways & Means Chair Jeffrey Sánchez following his re-election loss in the primary.

- ❖ Mr. Lynch complimented the Treasury Legislative staff for their continuous work on the auto-enrollment legislation. Mr. Vandolder asked if the Treasury's Legislative staff were working on gathering data from on other auto-enrollment states. Mr. Lynch confirmed that they were, and that Matt Peterson, NAGDCA Executive Advisor, has also been very helpful.

- <u>Account Retention / Retirement Solutions Group (RSG)</u>: Mr. Lynch stated that the Retirement Solutions Group (RSG) service, offered through Empower Retirement, was designed to engage participants from enrollment through retirement. Mr. Lynch credited Ms. Robbins for expediting negotiations with Empower Retirement to add the RSG service to the Services Agreement. Mr. Lynch stated that RSG has demonstrated results in retention and reduced cash-out rates overall several years with other Empower Retirement plans. Mr. Lynch noted that the program would be rolled out in two phases; Phase One would only engage inbound calls, while Phase Two would involve proactive outbound calls to new participants, participants that have reached certain age milestones, and participants separating from service.

  - ❖ Mr. Sheridan asked if there was an added cost to the service. Mr. Lynch confirmed there was no added cost. Mr. Lynch also noted that outbound calls to participants would engage in conversations about a variety of topics such as contribution rates, auto-escalation, and account consolidation, amongst others. Mr. Sheridan stated that this would be a great feature for participants.

Prior to moving on to the Investment Policy Statement review, Mr. Lynch requested that the team from Aon Hewitt speak on recent litigations against the firm. Ms. Halberstadt stated she could speak regarding these lawsuits.

- Ms. Halberstadt commented on the similarities between the lawsuits brought forward by Lowe's Companies Inc. and FirstGroup America Inc., both alleging that Aon Hewitt, in its capacity as OCIO, had violated its ERISA fiduciary duty with a redesign of each client's respective investment lineups, which recommended proprietary Aon Hewitt investment funds. The lawsuits cited underperformance of these funds as well as a conflict of interest in the recommendation of proprietary funds.

  Ms. Halberstadt continued, noting that the funds in question were not managed directly by Aon Hewitt. Ms. Halberstadt added that the OCIO fee collected by Aon Hewitt was a flat fee and that Aon Hewitt received no advisory fee from these funds. Regarding the underperformance of the funds, Ms. Halberstadt responded that the clients misunderstood the investment vehicles they had selected. Ms. Halberstadt attributed the increase in lawsuits to a concentration of law firms doing this type of litigation, and that Aon Hewitt looked forward to resolution on these matters.

  - ❖ Mr. Sheridan asked the dollar figure of the lawsuits. Ms. Halberstadt could not confirm, noting the amounts varied, but that they were publicly available.

- Mr. Sheridan asked where the lawsuits were filed. Ms. Halberstadt responded that FirstGroup filed in a U.S. District Court in Ohio, while Lowe's filed in a U.S. District Court in North Carolina. Mr. Sheridan then inquired as to whether Aon Hewitt had issued a public statement regarding this litigation. Ms. Halberstadt replied that as with any litigation that arises, Aon Hewitt does not issue public statements.

- Mr. Magno asked if it was common that there would be more than one lawsuit. Mr. Vandolder responded that it was fairly common, particularly as certain law firms such as Schlichter, Bogard & Denton, identified these as potential litigation targets. Mr. Vandolder stated that he often speaks directly with the Aon Hewitt consultant overseeing the plans cited for potential litigation for further explanation as well. Mr. Sheridan asked that the Committee be kept informed of any new developments on relevant lawsuits.

- Ms. Robbins noted that the SMART Plan does not contract with Aon Hewitt as an OCIO, but Aon Hewitt does provide this service on the CORE Plan. Ms. Robbins added, however, that the Plan continues to monitor developments and speak with Aon Hewitt on these issues regularly. Ms. Halberstadt confirmed that Aon Hewitt does not provide OCIO services to this Plan, but to the CORE Plan, and further, as a point of clarification, the CORE Plan is not invested in the same funds as those of the aforementioned litigants. Per Ms. Halberstadt, the CORE Plan has custom funds. Mr. Magno reiterated that the Committee wished to be kept abreast of any new developments.

- Mr. Clay stated that the allegations in these lawsuits were very concerning. Mr. Vandolder responded that he understood the concerns but noted that the current legal climate meant the potential for litigation was high. Mr. Vandolder also stated that threat of legal action can lead to a "race to the bottom" regarding investment management fees, which could result in an all passive investment lineup.

In the interests of time, Mr. Sheridan asked the Committee for any additional questions on the Aon Hewitt matter or the Executive Summary. With no further questions, Mr. Sheridan suggested moving on to the Investment Policy Statement review.

IV. Investment Policy Statement Review

- Directing the Committee to the Investment Policy Statement (IPS) drafts provided with their materials, Mr. Behrns noted the importance of an annual review of the IPS for potential updates and edits. Mr. Behrns pointed out an edit on page 6 of the IPS made to provide clarification that the Plan does not oversee participant investments made within the Self-Directed Brokerage Mutual Fund Window, and that this was further mentioned in Appendix B: Description of Tier Structure. Mr. Behrns also noted the addition of clarifying language regarding the responsibility of participants to monitor their contribution rate and investment allocations within the SMART Plan. Mr. Behrns concluded his summary of the proposed edits with the updates to Appendix C: Description of Investment Options, noting an update to a SMARTPath Fund language and the new allocation on the Real Estate "REIT" Fund, as well as minor grammatical edits elsewhere in the IPS.

- ❖ Mr. Sheridan asked if the Committee members were considered fiduciaries to the Plan. Mr. Vandolder responded that the Committee was not considered a fiduciary, but the Treasury would be.

- ❖ Mr. Curran asked if Appendix C would need to be updated each time a change in managers occurred. Ms. Rooney pointed to the footnote on page 23 of the IPS, which reads that investment options, managers, and allocations may be subject to change. Mr. Vandolder stated that the annual review process was an opportunity to update any changes that occur.

Mr. Curran asked for a motion to approve the changes to the Investment Policy Statement. Mr. Magno made a motion to approve the amended IPS. Mr. Sheridan seconded the motion. Mr. Curran rounded out a unanimous vote in support of the IPS changes.

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

In the interest of time, Mr. Vandolder began with a quick recap of the Market Review.

- Directing the Committee to Tab 6, page 60, Mr. Vandolder referenced the positive short-term and long-term returns as indicative of a consumer-led recovery, noting that tax reform provided additional cash for both people and corporations. Mr. Vandolder next commented that small cap markets were up 12% over five years, while emerging markets were down 8% over the same timeframe, indicative of the strength of the U.S. dollar.

- Mr. Vandolder continued on page 64 and noted the lag of value stocks over the past 12 months compared to their growth equivalents. Mr. Vandolder stated that this has had an impact on the Vanguard Dividend Growth Strategy, which has a significant value discipline within the Large Company Blend Stock Fund. Mr. Vandolder noted the difficultly of investing in value markets during what was currently a growth-led economy. Mr. Vandolder cited growth-oriented stocks such as Facebook and Alphabet.

  - ❖ In reference to the annual review of fund allocations to be held at the Third Quarter Committee Meeting, Ms. Robbins asked if it was still too early to give a recommendation on the Vanguard Dividend Growth Strategy. Mr. Vandolder responded that there is currently no recommendation by Aon Hewitt to shift away from the Vanguard Dividend Growth Strategy, though that stance remains tentative until the Third Quarter Committee Meeting. Mr. Vandolder added that if market were to shift, the Plan will be happy to have retained the strategy.

- Turning the Committee's attention to the Fund Monitoring Summary, Mr. Behrns noted that a couple of funds are on watch due to underperformance. Referencing Tab 2, page 12 of the materials Mr. Behrns highlighted the underperformance of the SMARTPath Target

Date Funds over a 12-month period, and underperformance over a five-year span compared to the custom benchmark. However, Mr. Behrns noted that the SMARTPath Funds still performed well compared to equivalent products offered by other firms, such as Fidelity, Vanguard, and Blackrock, with strong returns over a five and ten-year period in particular. Per Mr. Behrns, while the funds have underperformed slightly due to fees or active management, on the whole it looks good. Mr. Vandolder noted that Mr. Behrns and he would work with Mr. Lynch, Ms. Rooney, and Mr. Caruso to bring AB in to discuss the SMARTPath Funds.

- Still on the subject of the Fund Monitoring Summary, Mr. Behrns noted that the Large Company Blend Stock Fund is on watch, largely due to the Vanguard Dividend Growth Strategy's underperformance. Also on watch per Mr. Behrns is the REIT Fund, primarily attributed to the Brookfield US Real Estate Securities Value Income Strategy and its underperformance over the past one to three years. Mr. Behrns noted that analysists from Aon Hewitt would be meeting with Brookfield the following week to discuss the performance and future strategy.

    - Mr. Lynch asked when the Plan should expect a report on Brookfield. Mr. Behrns replied that he would refer that question back to the researchers. Mr. Sheridan asked what caused the underperformance. Mr. Vandolder responded that Brookfield had missed the opportunity to invest in self-storage facilities. Mr. Curran stated that this missed investment has affected the strategy for some time. Mr. Vandolder concurred, but pointed out that the strategy has overperformed this past quarter. Mr. Vandolder noted that the mixed performance of the strategy led to the decision to allot a 20% asset allocation to a passive State Street REIT strategy within the REIT Fund. Mr. Vandolder reiterated that Aon Hewitt still felt positive about the Plan retaining Brookfield.

    - Mr. Clay asked if there had been any changes in portfolio managers at Brookfield. Mr. Vandolder responded that the firm has been relatively stable, but he would review and respond back.

- Mr. Behrns continued on with other updates, next regarding Manager Research Items. Per Mr. Behrns, Alec Walsh, co-lead Portfolio Manager on the Harding Loevner International Equity strategy, would be retiring effective January 2, 2019, but would remain with the firm as a paper Portfolio Manager. Mr. Behrns also noted that Mr. Walsh's co-lead, Ferrill Roll, would remain as co-lead, and that Mr. Walsh would be replaced by Andrew West, a paper Portfolio Manager on the International Equity strategy since 2011. Mr. Behrns commented that Harding Loevner would work to onboard Mr. West to the co-lead Portfolio Manager role over the next six months to ensure a smooth transition.

    - Mr. Clay asked if Aon Hewitt was familiar with Mr. West and his experience. Mr. Vandolder confirmed they were. Mr. Behrns responded that they are confident in Mr. West as a co-lead Portfolio Manager and noted that paper Portfolio Managers such as Mr. West are fairly involved in the day-to-day strategy operations. Mr.

Behrns then added that Aon Hewitt has not changed the buy rating it has for this strategy based on the aforementioned changes.

- Mr. Behrns next stated that Peter Simons, Portfolio Manager on the JP Morgan Asset Management Core Bond Fund, would resign effective June 2019. Mr. Vandolder continued on the subject, informing the Committee that while Mr. Simons was not a direct portfolio manager, his departure gave Aon Hewitt pause regarding the longevity of the Columbus, Ohio based platform for JP Morgan. However, Mr. Vandolder stated that performance has otherwise been positive. Mr. Vandolder added that Aon Hewitt continued to encourage its clients to retain this strategy.

- Mr. Vandolder next began to discuss the structural changes to come for the JP Morgan Strategic Property Fund, which would now allow non-US and non-ERISA investors into the fund. Mr. Vandolder remarked that this would likely result in additional assets coming into the fund. Mr. Behrns added that at this time Aon Hewitt does not recommend any changes to the Plan's investment in this fund, but noted that Aon Hewitt was going to obtain the underlying documents to review the structural changes so as to determine how, if at all, such changes would affect those Aon Hewitt clients already invested in the fund.

    - ❖ Mr. Clay asked if it takes time for invested funds to become active. Mr. Vandolder replied in the affirmative, noting that it normally takes 9 to 12 months for the money to be utilized. Mr. Behrns then voiced his curiosity as to why the fund would open to further investment, noting it as one of the largest currently available in its markets. Mr. Clay responded that he had wondered the same, and hoped this would not indicate a lowering of standards. Mr. Vandolder, aware of the concerns, stated that Aon Hewitt would do their due diligence on the investment given the large Plan exposure to it.

- Mr. Behrns stated that Empower Retirement remained on watch due to personnel changes.

- Turning to Research Items on page 45 of Tab 5, Mr. Behrns referred to an article on environmental, social and governance (ESG) investing included in the materials. Mr. Behrns informed the Committee that the Department of Labor has stated that while plans can elect for an ESG investment option, they cannot sacrifice fiduciary duties in terms of performance, fees, and risk/return. Mr. Lynch noted that socially responsible fund options are available through the Plan's mutual fund window. In response to an inquiry from Mr. Sheridan, Mr. Lynch stated that unlike PRIM, there are not any legislative investment restrictions on the Plan with respect to guns.

Mr. Behrns asked if the Committee had any additional questions.

- Mr. Sheridan asked what the Plan's exposure to Wells Fargo was. Mr. Lynch responded that Wells Fargo is the directed trustee and pass-through account for money but were not involved in investments. Mr. Sheridan cited his concerns regarding the reputation damage to Wells Fargo following that retail bank account scandal in 2017. Mr. Sheridan then asked Mr. Lynch if he was satisfied with what Wells Fargo is doing for the Plan. Mr. Lynch responded in the affirmative, stating that for the services Wells Fargo is providing, he was satisfied with job Wells Fargo is doing. Ms. Rooney then reiterated the limited scope of the services Wells Fargo provides to the Plan.

Mr. Sheridan asked Mr. Magno if he had any additional questions on the Market Review. Mr. Magno responded in the negative. With no further questions, Mr. Sheridan suggested moving on to the Wellington Management Dynamic Growth Strategy review.

VI. Wellington Management – Dynamic Growth Strategy

At the invitation of the Plan, representatives from Wellington Management, who oversee the Wellington Dynamic Growth Fund separate account strategy for the Plan, were invited to present before the Committee. Present on behalf of Wellington Management were Steve Mortimer, Portfolio Manager, Wellington Management; Eileen Leary, Investment Director, Wellington Management; and Jed Petty, Managing Director, Wellington Management.

Representatives from Vanguard, who oversee the Vanguard Dividend Growth separate account strategy for the Plan, were also invited before the Committee at this time. Present on behalf of Vanguard were Jeff Edwards, Senior Relationship Manager, Vanguard Institution Investor Group; and Drew D. Schneider, CFA, Equity Product Manager, Vanguard Institution Investor Group.

Prior to the presentations, Mr. Vandolder reminded the Committee that the Vanguard Dividend Growth strategy was sub-advised by Wellington Management.

Mr. Sheridan welcomed the representatives from Wellington Management and Vanguard. Mr. Sheridan voiced his appreciation for the Wellington Management Morning Meeting broadcasts online. Mr. Petty thanked Mr. Sheridan and noted the broad range of discussions in these meetings.

- Mr. Petty introduced himself, Ms. Leary and Mr. Mortimer and stated that Wellington Management directed the Dynamic Growth Fund, which has a 45% asset allocation within the Large Company Growth Stock Fund.

- Directing the Committee to page 5 of the Wellington handout, Mr. Mortimer stated that the Investment Objective of the fund is to outperform the Russell 3000 Growth Index, and he then identified the key tenets of the fund investment philosophy. Mr. Mortimer stated that the strategy sought to take advantage of these opposing market environments by moving in the opposite direction of the rest of the market. He stated that where they can they look to find differentiation from consensus.

    - Mr. Vandolder noted that Amazon remained the top holding within the strategy and asked which side of the pendulum Amazon was currently on, in Wellington's view. Mr. Mortimer responded that they were content to have held the investment and regretted not having held enough, noting that he had believed it to be overvalued briefly. Mr. Mortimer attributed the continued strong performance to domestic and international retail growth, as well as the expansion of web services and Amazon's advertising platform. Mr. Mortimer noted that the strategy has reengaged Amazon since January, and that it remains its biggest position. Mr. Mortimer also cited exiting the position in Facebook prior to the stock downturn.

- ❖ Mr. Sheridan asked if and when Amazon would purchase Wayfair. Mr. Mortimer responded that while the strategy also has a position in Wayfair, and that Amazon had previously shown interest in a takeover, the time may have passed for both parties. Mr. Mortimer stated that Wayfair also demonstrated strong performance.

- Mr. Mortimer next addressed team updates. Specifically, Mr. Mortimer noted the addition of Frank D. Catrickes, Equity Portfolio Manager, to the fund's team. Mr. Mortimer stated that Mr. Catrickes is a longtime Wellington employee whose previous team at Wellington had been dissolved, but that Mr. Catrickes brought a wealth of experience regarding domestic corporate investments, particularly technology and software companies, and would be an excellent resource.

- Mr. Mortimer moved on to describe the Investment Process and stated that Wellington models were built in-house. Mr. Mortimer also cited the use of 49 global research analysts as key to the decision-making process on whether to take on a new investment position. Mr. Mortimer reflected on the highly collaborative Wellington environment, with many questions and ideas shared across a variety of investment teams.

11: 30 a.m. **Mr. Favorito joined the meeting.**

- Mr. Mortimer stated that the investment analysis process was both qualitative and quantitative, and that Wellington tries to have all relevant data to create appropriate models. Mr. Mortimer noted that this included purchasing data, such as sell-through rate data and credit card data. Mr. Mortimer cited investment in NVIDIA as a result of purchased sell-through data. Mr. Mortimer explained that the data demonstrated how NVIDIA graphics board sales compared to competitors such as AMD. Mr. Mortimer stated that while AMD had higher sales, demand overall for graphics boards have grown due to rise in cryptocurrency mining. Mr. Mortimer next cited investment in Wayfair as a result of purchased credit card data, as all purchases from Wayfair must be made via credit card and using this data, Wellington can see how much people are spending.

- Mr. Mortimer next discussed the strategy's quantitative process, noting that models are created to demonstrate an upside and downside estimation to judge risk/reward before buying into a new position. Mr. Mortimer cited Facebook and IPG Industrial Lasers, which faced disruption due to ongoing trade issues between the U.S. and China, as examples of downside scenarios playing out. Mr. Mortimer noted that despite that strong performance of Facebook the year prior, he decided to sell the position in the company even before the earnings came out in July due to poor performance and public profile following several scandals involving Facebook. Mr. Mortimer said that their upside/downside philosophy helped the team determine to sell Facebook at an attractive number and the fund did not lose alpha.

- Continuing on to portfolio construction and risk monitoring, Mr. Mortimer stated that the portfolio was not benchmark-focused, but rather benchmark-aware, regarding sector allocations. Mr. Mortimer noted the market cap as generally over $2 billion as well. Mr. Mortimer cited the recent sale of Facebook stock as giving the portfolio significant liquidity, which in turn provided the portfolio with the ability to look at other potential investment opportunities.

- Directing the Committee to the Dynamic Growth one-year performance review, Ms. Leary reported a strong performance year for both the portfolio and the Russell 3000 Growth benchmark. Ms. Leary also reported positive year-to-date performance as of August 31, 2018, with the portfolio up 21.5%, attributed primarily to stock selection and strong performance in the consumer, healthcare and technology sectors.

In the interest of time, Mr. Mortimer asked if there were any additional questions for the review.

- Mr. Vandolder asked Mr. Mortimer if he could answer a question on the short-term investment future. Specifically, Mr. Vandolder asked what could potentially turn in the market or stay the same after the upcoming midterm elections in November. Mr. Mortimer noted the current economic tailwind, primarily attributed to tax reform and deregulation. However, Mr. Mortimer noted his hesitation to look too far ahead, and cited potential trade issues and tariffs, particularly with China, and subsequent economic consequences that could arise from them.

- Mr. Sheridan asked what the portfolio's exposure to cloud providers was. Mr. Mortimer responded that it was a big position within the portfolio, particularly with Amazon. Mr. Mortimer also stated that cloud providers were relatively insulated from recessions compared to other sectors. On that topic, Mr. Mortimer cited Polaris Industries, makers of off-road vehicles, as an example of this, considering potential tariffs on steel and manufacturing could increase production costs. Mr. Sheridan asked about Google Cloud Platform compared to Amazon. Mr. Mortimer responded that Amazon still leads in the cloud services market.

Mr. Sheridan asked the Committee members if there were any further questions for Mr. Mortimer and his team. Mr. Curran and Mr. Magno responded in the negative. With no further questions, Mr. Sheridan thanked the representatives from Wellington Management for their presentation.

VII. Vanguard – Dividend Growth Strategy

Mr. Edwards introduced himself and Mr. Schneider and thanked the Committee for the invitation to review the Dividend Growth fund, and then turned the review over to Mr. Schneider. Mr. Schneider explained that the Vanguard Portfolio Review Department provided oversight over all sub-advised funds, including the Vanguard Dividend Growth Strategy, which is sub-advised by Wellington. Mr. Schneider added that Wellington represents Vanguard's largest sub-advisor.

- Moving on to the Fund Review, Mr. Schneider noted the lower beta approach of the portfolio, citing its higher liquidity and its dividend-focused approach. Mr. Schneider stated that the portfolio was more defensive compared to its peers to protect against downside. However, Mr. Schneider also noted that current markets favored growth-oriented funds as opposed to value investments, such as this portfolio. Mr. Vandolder commented that the performance of the portfolio has consequently led to poor performance overall in the Large Company Blend Stock Fund compared to benchmark. Mr. Schneider confirmed.

- On sector allocation and diversification, Mr. Schneider noted that while there was a healthy weight to information technology, at just over 10% of the portfolio, this sector allocation remained slightly below the Russell 1000 benchmark allocation. Mr. Schneider cited Microsoft and Accenture the largest holdings in this sector. Staying within the sector, Mr. Schneider noted that omission of Amazon and Facebook from the portfolio, which were more growth-oriented investments. Mr. Schneider then focused on the bottom-up analysis.

- Mr. Vandolder pointed to page 21 of the Vanguard materials and noted that in 2008 and 2015, the markets were not great, but the strategy saw production. Mr. Vandolder then asked where Vanguard sees things now. Mr. Schneider responded that the fund's Portfolio Manager, Donald Kilbride, is cautious in his outlook. Mr. Schneider then explained that the recent underperformance could be attributed to an underweight in industrials and an overweight in energy relative to the benchmark.

- Mr. Schneider continued by describing the cash flow trends and balance sheet strength as determinants in stock selection, noting the low 15% turnover in stocks by fiscal year end.

    - Mr. Sheridan asked what Mr. Schneider thought of Nike, considering the new advertising campaign. Mr. Schneider responded that Mr. Kilbride viewed Nike favorably and that similar campaigns have generated opportunities in the past, despite potential public backlash.

- Mr. Schneider noted the data-oriented approach that Vanguard utilized, similar to Wellington. However, Mr. Schneider stated that this data has demonstrated the past three years to be growth-oriented markets, with technology a driving force behind growth. Mr. Schneider noted that Mr. Kilbride focused primarily on investment quality and protecting downside, stating that this would benefit investors over a longer term. Mr. Schneider attributed more recent underperformance of the portfolio to the higher healthcare sector allocation weight, relative to stronger performers such as technology and energy. Mr. Schneider cited Exxon and Schlumberger as the only energy firms within the portfolio.

    - Mr. Petty interjected, and noted that while Wellington serves as advisor on both the Vanguard Dividend Growth Strategy and the Wellington Dynamic Growth Strategy, the two teams maintain a very different investment philosophy and process. Mr. Petty also stated that both utilize Wellington data for their analysis. Mr. Petty stressed the significance of the two different investment philosophies and noted that it was important both remained true to their respective objectives.

The question, he said, was whether the strategies were performing the way they should be given the market environment, and are they staying true to the philosophy.

- Mr. Schneider continued and reiterated the focus on quality investments. Mr. Schneider also stated that Mr. Kilbride would stay true to the investment strategy and not chase the current growth market.

  - Mr. Lynch asked if there was a stated policy regarding the subadvisory relationship between Wellington and Vanguard. Mr. Schneider did not confirm a policy but noted that Vanguard works to secure top-tier talent at a reasonable cost. Mr. Schneider stated that the fund expense ratio of 26 bps was far below its peers. Mr. Schneider also referenced the performance incentives for portfolio managers such as Mr. Kilbride. However, Mr. Schneider noted that while strong portfolio performance can result in bonuses, long term underperformance could lead to a reduction in base pay. Per Mr. Schneider, this is unique within the mutual fund space.

  - Mr. Curran asked if the strategy currently uses the S&P 500 Index as its benchmark. Mr. Vandolder responded that the current benchmark was the Russell 1000, and cited stylistic differences as a potential challenge if the S&P 500 were to be used. Mr. Vandolder noted that current underperformance by the strategy relative to benchmark was primarily due to sector allocation. Mr. Curran thanked Mr. Vandolder and stated he simply wanted to confirm the correct benchmarks were utilized.

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 thanked the representatives from Vanguard for their presentation.

12:00 p.m. Wellington Management and Vanguard depart.

VIII. Future Meeting Dates

Mr. Sheridan asked for future meeting dates to be determined based on what would be most convenient for attendees, and suggested December 3 or 4, 2018. Mr. Vandolder responded that he would be available for December 4, 2018. Mr. Curran and Mr. Magno also confirmed their likely availability on that date and Ms. Rooney agreed to confirm availability via email.

IX. Close of Meeting

12:12 p.m. Close of Meeting.

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

Documents Used at the Deferred Compensation Committee Meeting of September 20, 2018

- Agenda for the September 20, 2018 Deferred Compensation Committee Meeting;
- Executive Director's Quarterly Update dated September 20, 2018;
- Minutes of the June 13, 2018 Deferred Compensation Committee Meeting;
- Draft Investment Policy Statement, Revised as of September 20, 2018 (clean and red-lined version);
- Plan Quarterly Highlights Report, Second Quarter 2018;
- Quarterly Investment Report, Second Quarter 2018;
- Wellington Management Handout, September 20, 2018; and
- Vanguard Handout, September 20, 2018.