NYS DEFERRED COMPENSATION BOARD
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August 23, 2013

Memorandum To: Files

Minutes of the August 23, 2013
Public Meeting of the
<u>New York State Deferred Compensation Board</u>

A public meeting of the New York State Deferred Compensation Board (the "***Board***") was held on August 23, 2013, in Room 2E of the offices of Shearman & Sterling LLP in New York, New York. The meeting began at approximately 9:00 a.m. and adjourned at approximately 3:10 p.m. A separate memorandum to the files, also dated August 23, 2013, lists the materials prepared for and referred to during the meeting.

Board Members:	Edward M. Cupoli, Robert F. Mujica, Diana Jones Ritter
Staff Members ("***Staff***"):	Edward Lilly, David Fischer, Sharon Lukacs, Peter Drao
Shearman & Sterling LLP ("***S&S***")	Kenneth Laverriere, Jennifer Stadler, Sara Nosaka
The Bank of New York Mellon ("***BNYM***"):	David Blakeley
Dwight Asset Management Company LLC ("***Dwight***"):	David Starr, Marie Mastro
Callan Associates Inc. ("***Callan***"):	Mark Kline, Karen McKechnie, Millie Viqueira
Nationwide Retirement Solutions ("***NRS***"):	Michael Carrel, Keri Metres, Kelly Nguyen, Jill O'Callaghan, Patrick Ray, Ric Whetro
CliftonLarsonAllen LLP ("***CliftonLarsonAllen***"):	Thomas Rey
Wells Fargo Funds Management, LLC ("***Wells Fargo***"):	Charles Rinaldi, Bobby Chen

Diana Jones Ritter acted as Chairperson and Sara Nosaka acted as Secretary of the meeting. Ms. Ritter called the meeting to order at 9:00 a.m.

I. APPROVAL OF MINUTES

The Board reviewed the minutes of the public meeting held on June 26, 2013. Ms. Ritter moved to

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approve the minutes. Edward Cupoli seconded the motion, and the Board unanimously approved the minutes.

II. GENERAL PLAN ISSUES

A. Review of Iran Investment Policy

Edward Lilly explained Staff's recommendation to amend the Board's Iran Investment Policy, initially adopted by the Board in September 2012. Mr. Lilly explained that after reviewing the Iran Investment Policy with the investment managers, Staff was of the view that specific reference to the definition of "person" as defined in the New York State Iran Divestment Act of 2012 and the use of "person" throughout the Iran Investment Policy would further clarify the entities covered by the Iran Investment Policy. Staff then discussed the managers' ongoing efforts to identify such persons covered by the Office of General Services' list of entities engaged in investment activities in Iran. David Fischer discussed with the Board the Staff's review of the level of due diligence exercised by the managers to minimize the violations of the Iran Investment Policy. Karen McKechnie confirmed Callan's belief that the international fund managers understand the requirements of the Iran Investment Policy and have been exercising reasonable diligence to comply with the Iran Investment Policy. In response to Mr. Cupoli's inquiry about similar legislation in other states, Mr. Lilly indicated that he would send to the Board information on the requirements under similar divestment legislation in other states. Mr. Cupoli moved to adopt Staff's recommended amendment to the Iran Investment Policy, Robert Mujica seconded the motion, and it was unanimously approved by the Board.

B. DOMA Decision Issues

Jennifer Stadler gave an overview of the impact of the U.S. Supreme Court's ruling in *United States v. Windsor* ("***Windsor***"), in which the Supreme Court struck down Section 3 of the federal Defense of Marriage Act ("***DOMA***") as unconstitutional, on the New York State Deferred Compensation Plan (the "***Plan***"). Ms. Stadler explained that prior to *Windsor*, "marriage" under federal law was strictly defined as a legal union between one man and one woman. Ms. Stadler explained that as a result of *Windsor*, the Plan is required to extend the same spousal benefits offered to opposite-sex spouses and surviving spouses to legally-married same-sex spouses and surviving spouses. She noted that because the Plan does not reference DOMA, no amendments to the Plan will be required. Ms. Stadler further explained that the Plan is governed by both the Internal Revenue Code and New York law, and until the Internal Revenue Service provides guidance on the application of *Windsor* to plans regulated by the Internal Revenue Code, S&S recommends that the Plan recognize as married any couple that is recognized as married under New York law, regardless of the couple's state of residence.

Ms. Stadler then discussed various issues that could potentially arise from the use of New York law to define "marriage" and "spouse." Ms. Stadler noted that *Windsor* left unresolved the marital status of individuals who are legally married in one state but whose marriage may not be recognized under laws of the state in which they reside. She noted that it is possible that a marriage recognized by the Plan under New York law may not be recognized by the state in which the participant's surviving spouse resides. Ms. Stadler explained that, in rare cases where a participant has not named a beneficiary and the surviving spouse of the participant resides in a state that does not recognize the marriage, other heirs could contest the payment of Plan assets to the surviving spouse. Ms. Stadler stated that this dispute could be avoided by each participant's official designation of his or her spouse as the beneficiary of the participant's Plan assets. She concluded with S&S's recommendation that the Board direct NRS to communicate to participants the importance of keeping beneficiary designations current. The Board then discussed ways to highlight the importance to participants of designating beneficiaries and taking the *Windsor* decision into account for purposes of retirement planning. The Board agreed to include in the participant newsletter a reminder to participants to update their beneficiary information.

C. October Fee Determination

The Board then discussed the amount of the October asset-based fee. Mr. Lilly reported that, if the plan levies an October asset-based fee of 2.25 basis points, total Plan revenues could exceed budget estimates by $187,300 (assuming total assets eligible for the asset-based fee do not decrease prior to the October levy). Mr. Lilly further reported that an asset-based fee of 2.15 basis points would reduce total participant revenue to an amount that may more closely match the Plan's revenue needs (again, assuming the Plan's assets do not decrease). Mr. Lilly explained that the Plan's normal practice has been to levy an asset-based fee to match as closely as possible the revenue needs for each fiscal year and to therefore maintain the current level of reserve for the Plan. Mr. Lilly then asked the Board to authorize him to recommend an asset-based fee in late September, which would give Staff the opportunity to assess the Plan's assets and the market trends at that point in time. The Board discussed the importance of maintaining a reasonable reserve amount in the deferred expense account and a reasonable amount at which to set the reserve. Discussion then ensued regarding a reasonable range for the October asset-based fee. Mr. Cupoli moved to authorize Mr. Lilly to recommend to the Board in late September an asset-based fee between 2.15 to 2.25 basis points, depending on the strength of the market. Mr. Mujica seconded the motion, and the motion carried.

D. Auditor Report

Thomas Rey from CliftonLarsonAllen gave a summary of the three services performed for the Plan by CliftonLarsonAllen. He explained that CliftonLarsonAllen performs a full-scope financial audit of the Plan, conducts a performance criteria review of NRS under its contractual obligations and prepares an "Agreed Upon Procedures" report for the Plan. After reviewing some of the key metrics and facts from the audited financial statements, Mr. Rey stated that the statements reflected a positive year for the Plan in terms of investment returns and participant enrollment and contributions. Mr. Rey then discussed CliftonLarsonAllen's findings from the NRS Performance Criteria Report and the range of potential penalties for non-compliance. Mr. Rey stated that all but one of the performance criteria tests had been completed. Mr. Rey then discussed the process for selection of test samples and confirmed that the selection process conforms to industry standards. Mr. Rey clarified that the sample sizes are determined by the Board and the samples are selected by auditors, but that the auditors do not use statistically random sampling. Mr. Fischer noted that NRS will provide the Board with their responses to CliftonLarsonAllen's Performance Criteria Report, and the Board will have the opportunity to review the responses, together with Staff's recommendations on how to proceed at the next Board meeting.

III. STABLE INCOME FUND

A. Updates to Cash Portfolio Investment Guidelines

Marie Mastro from Dwight provided a summary of the proposed changes to the cash portfolio investment guidelines. She highlighted clarity, investment flexibility and diversification as key reasons for the updates to the investment guidelines. David Starr noted that Dwight worked closely with BlackRock and Staff in identifying the need for changes to the investment guidelines for the cash portfolio. Mr. Starr explained that the proposed changes seek to expand the universe of securities in which managers may invest in order to reduce risk and increase yield. Ms. Mastro discussed the various proposed updates to the investment guidelines for the cash portfolio and summarized the proposed changes to approved investments, diversification limits, credit quality, and duration of holdings. With respect to diversification limits, Ms. Mastro further explained that expanding maturity limits would allow for the inclusion of more securities to allow for further diversification of the cash portfolio. She also noted that the proposed changes to credit quality guidelines include expanding eligible investments to allow up to 10% of assets invested in securities rated A-2/P-2. Following Dwight's presentation, the Board discussed the proposed changes. The Board agreed that a combined recommendation from Callan, Dwight, and Staff would be helpful at the next Board meeting. Mr. Cupoli noted his expectation that the presentation include an analysis of any potential adverse effects of the changes.

B. Overview of Stable Income Fund

Mr. Starr gave a brief overview of the performance of the Plan's Stable Income Fund. Mr. Starr confirmed that there had not been any material changes to the portfolio's structure. Ms. Mastro summarized the factors contributing to the portfolio's favorable performance in both the short- and long-term. She concluded by noting that despite a negative quarter in fixed income, the portfolio was performing well overall.

IV. ADMINISTRATIVE SERVICE AGENCY PRESENTATION

Patrick Ray began the presentation by explaining recent changes to the NRS team. Ric Whetro announced that he will no longer be working on Plan matters at NRS and that Jill O'Callaghan had returned to the team as his replacement. Mr. Ray introduced Michael Carrel to the Board, and he described his responsibilities as a member of the senior advisory board of technology at NRS. Mr. Carrel noted the high satisfaction rates with the NRS website and described some of NRS' goals for their website. He explained his current role in facilitating the processes for upgrading the website so that participants could have better access on their mobile devices. He also explained the efforts to upgrade the security protections on the website and the efforts to streamline the process of accessing information on the website. Finally, Mr. Carrel explained NRS's "green" security campaign to migrate data held by NRS to a new LEED-certified center in a Columbus suburb, which would provide an additional level of protection for Plan and participant information that is compiled and stored by NRS. Mr. Cupoli requested that NRS provide a written summary that specifically addresses these internet technology advancements.

Mr. Ray then gave a brief overview of the improvements to account statements. He stated that most changes have been implemented and the remaining changes will be implemented in the third quarter. He noted the need to further improve the presentation of data on the website.

Mr. Ray next provided a summary of administrative highlights. He noted that the number of participants enrolled in the Plan is currently at an all-time high, with the number of new enrollments having increased by 23% from 2012. He noted that NRS is optimistic that it will reach its enrollment goal of 200,000 participants by the end of the year. Mr. Ray expressed his gratitude toward Staff for their efforts in assisting with the adoptions of the Plan by a number of public jurisdictions in New York and further noted that the Plan is continuing to receive requests for additional adoptions and conversions. Mr. Ray then provided an update on the performance of the Helpline, explaining that, due to improvements to the service center for the Helpline, NRS has met its service level for the Helpline for the past six months.

Kelly Nguyen then discussed various marketing initiatives that NRS has taken in the recent quarter to increase enrollment. She described the idea behind the Third Trimester Campaign to align the marketing practices of account executives. Ms. Nguyen explained the timeline for the launch of this campaign, noting that the flyers and marketing materials will be sent first to Account Executives, then employers and finally participants.

V. INVESTMENT CONSULTANT PRESENTATION

Ms. McKechnie provided an overview of the Plan's investment performance over the last quarter. She explained that the performance of U.S. securities remained strong but that of international and emerging market securities had been weaker. She pointed out that the performance of the Target Date Funds of T. Rowe Price was above the median and the Pax World Balanced fund was below the median. She highlighted the Davis New York Venture Fund's recent improved performance, noting that it outperformed its index in the last quarter. Ms. McKechnie next highlighted Eaton Vance Large Cap Value's stronger performance in the last quarter, also outperforming the benchmark, despite its recent underperformance. Ms. McKechnie identified Janus Perkins Mid Cap Value as a fund that has struggled against its benchmark over the last quarter, year and 3-year periods. Ms. McKechnie attributed the underperformance to the managers' focus on downside protection, which limits the fund's returns in strong markets, but further noted Callan's intent to meet with the fund's managers in the near future to discuss performance. Ms. McKechnie then gave a brief overview of the Active International Equity fund's performance and noted that the active portfolio had outperformed its benchmark. She noted that the positive returns of the Active International Equity fund were mostly carried by MFS International Advisors, with whom Callan and Board Staff met at the end of July. Ms. McKechnie expressed Callan's satisfaction with the strategies and results of MFS International Advisors. She then noted some recent management changes within the funds.

In advance of the Wells Fargo presentation, Ms. McKechnie provided a summary of Wells Fargo Small Cap Value Fund's performance, noting that recent performance had not been strong. She cited the manager's strong reliance on investments in the precious metals sector (particularly gold) as a key factor of the fund's underperformance. Ms. McKechnie also noted that the fund has significant holdings in its top two investments, which comprise 15% of the fund's total assets. Ms. McKechnie stated that Wells Fargo has experienced volatile performance on a year-to-year basis, significantly outperforming its index in 2005, 2007, and 2009 and underperforming in 2006 and 2008. She added that Wells Fargo underperformed the Russell 2000 in the last quarter, year, 3-year, 5-year, 7-year, 10-year periods.

VI. PORTFOLIO REVIEW

Charles Rinaldi and Bobby Chen from Wells Fargo then joined the meeting. Mr. Chen presented an overview of the firm's investment strategies and the recent performance of the Wells Fargo Small Cap Value Fund. Mr. Chen described the fund's investment philosophy, noting that the fund identifies small cap value funds under $2 billion in market capitalization for investment. Mr. Chen summarized the different methods of valuation used to value their targets. Mr. Rinaldi further discussed the fund's investment strategy, emphasizing that their trend analysis allows the investment team to identify stocks with positive dynamic change.

Mr. Rinaldi and Mr. Chen answered several questions from the Board and Callan regarding the fund's allocation to gold mining companies, increased concentration in the energy sector and overall performance. Mr. Rinaldi explained that he believes in the growth potential of Interoil Corporation, its most significant holding, and the energy sector. Mr. Rinaldi stated that he is comfortable with the fund's gold mining holdings, discussing the future upsides of the currently weak investment and noting that gold mining holdings add to the portfolio's diversification. Mr. Rinaldi also stated that despite gold's recent poor performance, returns in the fund's energy holdings have doubled and returns in financials, industrials, and technology are all positive. Mr. Rinaldi then provided a brief history of the fund's performance. He stated that the fund has outperformed its benchmark 83% of the time since inception, noting that the underperformance of the fund in the past few years is not the norm. Mr. Rinaldi then discussed with the Board his strategy to improve performance over time. A general discussion then followed regarding Mr. Rinaldi's presentation. Following the discussion, Messrs. Rinaldi and Chen left the meeting.

After the presentation from Wells Fargo, Mr. Kline further discussed their presentation. Mr. Kline stated that despite Wells Fargo's recent underperformance, management for the fund has been stable and Callan does not believe that any action with respect to the fund is currently necessary.

There being no further issues to discuss, the meeting was adjourned at approximately 3:10 p.m.

Sara Nosaka
Secretary of the Meeting