

BOARD OF TRUSTEES
OF THE NORTH CAROLINA SUPPLEMENTAL RETIREMENT PLANS
March 9, 2011, 9:00 am
Dawson Conference Room
Albemarle Building, 325 N. Salisbury Street
Raleigh, NC

The meeting of the Board of Trustees for the Supplemental Retirement Plans was called to order at 9:00 am by the Chair, State Treasurer Janet Cowell.

Members Present

Members present were: Chuck Leedy, Robert Powell, Dexter Perry, Mona Keech, Kel Landis and Janet Pittard.

Members Absent

Libby George was not in attendance.

DST Staff Present

Staff members present were: Rhonda Smith, Arlene Jones-McCalla, Shawn Wischmeier, Timothy Dale, Kitty McCollum, Kara Petteway, Julia Vail, Lisa Page, Jaclyn Goldsmith, and Rita Baker.

Guests Present

Prudential representatives attending were: Bill Walsh, Jessica Quimby, Jennifer Willis, and Tim Bryan. Mercer representative Jay Love and Plan member Bob Slade were in attendance. Attending via phone were Prudential representatives Robb Craddock and Travis Swartwood. Galliard representative Andy Apostol and Segal representative Brian Smith also attended via phone.

Conflicts

The Chair asked the Board members if there were any actual, potential or appearances of a conflict with any item on the meeting agenda. No conflicts were reported.

Resolution of Recognition

The Board moved on a resolution to express deep appreciation and gratitude for the service of Dr. John J. Pringle on the Supplemental Retirement Board of Trustees. Dr. Pringle's dedication to promoting the maximum benefit for plan members, and his service as Chair of the Investment Subcommittee, were recognized by the Board as being instrumental to the Supplemental Plans' success. It was moved by Kel Landis and seconded by Janet

Pittard to pass the resolution acknowledging the appreciation of the Board for Dr. Pringle's service. The motion passed unanimously.

Approval of Minutes

It was moved by Robert Powell and seconded by Dexter Perry to approve the minutes of the NC Supplemental Retirement Board meeting held on December 1, 2010. The motion passed unanimously.

Appointment of Investment Subcommittee Members

It was moved by Janet Pittard and seconded by Mona Keech to appoint Board members Dexter Perry and Chuck Leedy to the Investment Subcommittee, with Dexter Perry serving as the Chair. The motion passed unanimously.

Fiduciary Liability Insurance Report

The Chair recognized Brian Smith from Segal to provide a report on fiduciary liability coverage for the Board. Mr. Smith began by explaining his process for examining and evaluating current protections for the Board under both statutory law and an excess liability policy covering representatives of the State. Mr. Smith stated that from his evaluation of North Carolina General Statutes, particularly those produced by the Defense of State Employees Act, the language seemed permissive regarding whether or not defense would be provided if a lawsuit were brought against the Board. According to Mr. Smith, statutes state that defense may be provided by the State, but the State can choose to not provide protection at their own discretion. However, statutes specifically list instances in which defense will not be provided. Given these findings, Mr. Smith was concerned about the uncertainty of legal defense from the State.

Mr. Smith also talked about the State excess liability policy that provides representatives of the State liability coverage in excess of the statutory protections. The State's excess liability policy would cover additional claims over the initial \$1 million covered by statutes. However, representatives of the State are excluded from coverage in this policy if another current or former State employee is the plaintiff. Mr. Smith stated that since any lawsuit brought against the Board would likely be from a current or former public employee, this policy is not very beneficial to the Board.

Mr. Smith then went on to suggest what types of premiums the Board could expect to see if it pursued fiduciary liability insurance coverage in the market. He stated that the Supplemental Plans would likely need a minimum limit of liability coverage of \$25 million with a preferred range of \$30 to \$50 million. Premiums would likely range between \$200,000 and \$500,000 with a self-insured retention between \$100,000 and \$500,000. However, Mr. Smith stated that since the Board was a public Board and its members were volunteers, the self-insured retention would likely be much lower. Mr. Smith stated that this coverage would guarantee legal defense and provide indemnification coverage should the Board face a lawsuit.

Kel Landis asked what other entities in the State faced the same type of exposure as the Supplemental Board due to the gaps pointed out in the report. Treasurer Cowell responded that many Boards of Trustees providing 403(b) savings plans are exposed,

especially at the University level, along with various other governing Boards across the State. Robert Powell asked where the premium was paid from for the Supplemental Board for the excess policy. Kara Petteway, Assistant General Counsel to the Treasurer, responded that a fraction of the premium was paid from each state agency. Mr. Powell also stated that the Attorney General's office should take charge of this initiative since the gaps in coverage effect governing bodies across the State. Mr. Landis stated that he agreed that this was a much broader issue than for just the Supplemental Board, but that resolving the issue on a State level would take a substantial amount of time. Mr. Landis inquired as to whether or not the Board could continue pursuing fiduciary liability insurance rather than waiting on broader, statewide action. Treasurer Cowell responded that since legislation was required for the Board to purchase insurance, the Board could make a motion to pursue legislation to allow the Board to purchase fiduciary liability insurance. It was moved by Robert Powell and seconded by Dexter Perry to pursue legislation allowing the Supplemental Retirement Board of Trustees to purchase fiduciary liability insurance. The motion passed unanimously.

4th Quarter Administrative Report

The Chair recognized Tim Bryan with Prudential to present the 4th Quarter administrative report. Mr. Bryan briefed the Board on the quarterly and annual performance of the Plans. Mr. Bryan noted a strong growth in assets within both plans. Average account balances were up in both plans due to strong market performance. He also noted that while new enrollments in the 401(k) plan are somewhat lower than in 2009, there has been substantial growth in the number of enrollments in the 457 plan. Mr. Bryan continued by identifying the goals set by the Board for 2010 and the Plans' performance in achieving those goals. He noted strong growth in the number of participants electing to use GoalMaker as their asset allocation tool. Dexter Perry asked if the educational sessions were leading such a large number of participants to elect GoalMaker. Mr. Bryan replied that the educational sessions provide clarity and background information on GoalMaker, which is presented as an easy way to diversify your assets if the participant is not investment savvy.

Mr. Bryan went on to mention that total contributions for 2010 were up slightly over 2009, despite many employers reducing their contributions. Janet Pittard asked what types of employers typically offer contributions. Mr. Bryan responded that local municipalities, law enforcement organizations, and some community colleges contributed to participant 401(k)'s. Mr. Bryan continued by mentioning the lower level of loan initiations by participants and an increase in the disbursement amounts from the Plans.

Kel Landis asked if steps were being taken to prepare members who may face layoffs due to budget shortfalls across the State. Ms. Pittard followed up by asking if a handout explaining options could be created for members who may lose their job due to budget woes. Jessica Quimby from Prudential replied that they have a handout similar to the one described by Ms. Pittard available on the website, but they could make it more easily accessible through the employer if necessary. Ms. Quimby also stated that loan information was already being communicated through various channels to participants.

4th Quarter Investment Performance Report

The Chair recognized Jay Love from Mercer to present a report on the investment performance for the 4th Quarter. Mr. Love spoke briefly on the economic environment for the 4th Quarter and the outlook for the upcoming year. He then went on to analyze the performance of each fund currently offered by the Plans. He noted that fixed income and quality equities did not fare as well as growth equities and index funds in the past year. Mr. Love stated that the funds as a whole were doing well, but they would recommend a few changes to some of the investment options. Mr. Love also reviewed fees charged to participants for sponsored investments. In all but one fund, the NC investment options were lower than the median expected fee for the fund.

Mr. Love then yielded to Robb Craddock from Prudential to give a report on the frozen funds performance from the 4th Quarter. Mr. Craddock stated that most of the funds performed well in the 4th Quarter compared to their benchmarks. He did have an issue with the Putnam Multi-Cap Growth Fund as it had merged with another fund and kept the same name. However, Mr. Craddock stated that since the assets within the fund would be mapped to the new separate accounts within the year, he did not think action would be necessary. Mr. Craddock also noted that the number of members within the frozen funds was steadily decreasing and assets in the 401(k) were significantly less than the year before. However, the same reduction in assets was not seen in the 457 plan with total plan assets slightly increasing. With no further action required the Chair thanked both Mr. Love and Mr. Craddock for their presentations.

Report from Investment Subcommittee

The Chair recognized Dexter Perry to report on the recommendations resulting from the February 21, 2011 Investment Subcommittee meeting. Mr. Perry began by giving the Board a summary of reports heard by the Investment Subcommittee and general information relating to the Board. He provided statistics on the number of participants and the remaining assets in the frozen mutual funds. He also informed the Board that RFP responses for the investment consultant relationship could be expected around September of this year.

GoalMaker Allocations

Mr. Perry asked Chuck Leedy to give a general overview of the proposed changes to the GoalMaker allocations. Mr. Leedy informed the Board that the new allocations would shift some allocation from Stable Value to increase allocation for Fixed Income. The new allocations would also shift funds away from domestic equities and toward international equity. Robb Craddock explained that every couple years, Prudential asks Morningstar to look at their GoalMaker lineup and make a recommendation if any changes are needed. The new model represents changes following the recommendation from Morningstar. Kel Landis stated that there must be some type of forward thinking and analysis of future risk and asked if Morningstar considered those factors in their analysis. Mr. Craddock referred the Board to the Morningstar report and stated that some consideration was taken into account when looking toward the future; however, it is difficult to correctly guess the future market environment. Mr. Leedy stated that Morningstar tends to base decisions on history and the report was likely focused more on past trends. Mr. Landis asked Shawn Wischmeier if

Morningstar's analysis is correct and similar to what is being prepared by the Investment Management Division. Mr. Wischmeier responded that he had not looked at the report to verify their analysis, but their recommendations seem to be in line with Investment Management Division planning. It was moved by Kel Landis and seconded by Janet Pittard to approve the new GoalMaker model recommended by the Investment Subcommittee. The motion passed unanimously.

Crediting Rate Change on NC Stable Value Fund

Mr. Perry then proposed the recommendation from the Investment Subcommittee that the Stable Value Fund crediting rate be changed from a declared rate that is given at the beginning of the quarter, to a floating rate calculated on a daily basis. Mr. Perry stated that this would help the crediting rate better reflect fund and market activity for the quarter. Andy Apostol stated that with using a declared rate, there is more variation from quarter to quarter. However, if you calculate the crediting rate on a daily basis, it eliminates the larger variations seen when calculating the rate on a quarterly basis. Mr. Apostol said that they would like to have this crediting rate structure in place on April 1st. Tim Bryan asked that the crediting rate change be moved to July 1st to allow time to communicate the change to participants. It was moved by Mona Keech and seconded by Janet Pittard to change the crediting rate from a quarterly declared rate to a daily floating rate. The motion passed unanimously.

Manager Searches and Benchmark Changes

Mr. Perry then brought to the Board's attention the list of recommendations presented by Mercer and approved by the Investment Subcommittee at the meeting on February 21, 2011. Following the recommendations made by Mercer, Mr. Perry recommended that the Board: reduce the allocation to investment manager Hotchkis and Wiley within the Large Cap Value fund to 40%, change manager benchmarks within the SMid Cap Value fund to match the Russell 2500 Value benchmark of the fund, and change manager benchmarks within the SMid Cap Growth fund to match the Russell 2500 Growth benchmark of the fund. The Investment Subcommittee also recommended manager searches be conducted for the Large Cap Growth fund, the Large Cap Value fund, the Global fund, and the SMid Cap Value fund.

Janet Pittard remarked that since the Board is about to embark on the manager searches, the Board should show leadership and give stronger consideration to women- and minority-owned businesses. Ms. Pittard stated that it had been an objective of the Board before to incorporate more women- and minority-owned businesses into Plans and asked that Mercer give preference to those organizations. Jay Love stated that they have been able to provide a list of recommended minority and women-owned investment managers in the past and two of the current investment managers are women or minority owned. Mr. Love continued on to say that Mercer would be able to provide a list of qualified women and minority-owned investment managers to choose from. It was moved by Dexter Perry and seconded by Robert Powell to approve the recommendations from the Investment Subcommittee. The motion passed unanimously.

Administrative Updates

The Chair recognized Timothy Dale to provide a list of administrative updates. Mr. Dale brought to the Board's attention recommended Plan Document amendments to the Supplemental Retirement Income Plan (401(k)). The first three amendments listed were modifications recommended by the Internal Revenue Service agent in charge of reviewing the Plan's application for a favorable determination letter. The last amendment was modifying the Plan Document to state that the Plan was administered by the Supplemental Retirement Board of Trustees rather than the Board governing the Teachers' and State Employees' Retirement System and the Local Governmental Employees' Retirement System that had previously administered the Plan. Seeing no issues with the changes, it was moved by Robert Powell and seconded by Chuck Leedy to approve the Plan Document amendments. The motion passed unanimously.

Mr. Dale informed the Board that there were currently 20 individuals approved to rollover their 401(k) or 457 into the Retirement Systems with 12 more pending. He informed the Board that the rate of participants opting to use the Transfer Benefit was increasing. He then recognized Julia Vail to give the Board a Communications update.

Ms. Vail presented a communication calendar for the Board to review with preparation and release timelines for all communication pieces that are expected for the year. She also stated that the Annual Benefit Statement expected completion date was May 17th.

Mr. Dale then informed the Board that the proxy voting policy for the Plans' was currently being modified by legal counsel for the Defined Benefit plan. Since the Supplemental Plans use the same proxy voting guidelines as the DB plan, the Board would have a chance to review and alter the new guidelines at a future meeting.

Mr. Dale then presented the administrative budget updates for the Board's review. Due to the additional equity oversight assumed by Mercer while the Investment Management Division completed an RFP for a longer-term investment consultant relationship, the budget would need to be expanded \$55,000 to compensate Mercer for the additional services. Mr. Dale also asked for authority for staff to use funds from the plan expense accounts to conduct the manager searches approved earlier in the meeting. It was moved by Kel Landis and seconded by Dexter Perry to approve the budget expansion request and to authorize staff to conduct the manager searches.

Adjournment

There being no further business, the meeting was adjourned at 11:25 a.m.


CHAIR