

DRAFT

MINUTES OF MEETING
STATE OF WISCONSIN
DEFERRED COMPENSATION BOARD

May 11, 2004
1:00 p.m.

801 West Badger Road
Conference Room GB
Madison, Wisconsin

BOARD PRESENT: Edward Main, Chair
John Nelson, Vice-Chair
Michael Drury
Jon Traver

BOARD NOT PRESENT: Martin Beil, Secretary

PARTICIPATING STAFF: Eric Stanchfield, Secretary
Dave Stella, Deputy Secretary
Pam Henning, Director, Office of Strategic Services
Shelly Schueller, Director, Wisconsin Deferred
Compensation Program
Sharon Walk, Board Liaison

OTHERS PRESENT: John Brandt, Janus
Mike Cullen, Federated Investments
Christina Licari, Department of Employee Trust Funds
Tony Mason, Legislative Fiscal Bureau
Curt Morrow, Nationwide Retirement Solutions
Sue Oelke, Nationwide Retirement Solutions
Vicki Poole, Department of Employee Trust Funds
Mike Studebaker, Nationwide Retirement Solutions
Ryan Wager, T. Rowe Price
Mary Willett, Willett Consulting
Kurt Umbarger, T. Rowe Price
Art Zimmerman, Legislative Fiscal Bureau

Edward Main, Chair, called the meeting to order at 1:06 p.m.

Consideration of Minutes of November 11, 2003, Meeting

Motion: Michael Drury moved acceptance of the minutes of the November 11, 2003, meeting as submitted by the Board Liaison. Jon Traver seconded the motion, which passed without objection on a voice vote.

Election of Officers

Motion: Mr. Drury moved to cast a unanimous ballot for Edward Main as Chair, John Nelson as Vice-Chair and Martin Beil as Secretary. Mr. Traver seconded the motion, which passed without objection on a voice vote.

Annual Investment Performance Review and Recommendations

Shelly Schueller presented the 2003 Annual Investment Performance Report to the members of the Deferred Compensation Board (Board).

She noted that since the 2002 Wisconsin Deferred Compensation (WDC) investment performance review, the following changes have been made to the WDC Program investment spectrum:

- The Dreyfus Premier Third Century Fund (Class R) was closed to new participant elections effective February 20, 2003, and will be phased out of the WDC investment spectrum entirely during 2004.
- The Calvert Social Investment Fund: Equity Portfolio (Class I) was added to the WDC investment spectrum on April 21, 2003.
- The Small Cap Equity Index Fund (Barclays Global Investors) was approved for addition to the investment spectrum. This fund opened to participants on March 1, 2004.

Curt Morrow, Investment Services Manager, Nationwide Retirement Solutions (NRS), discussed his observations regarding the 2003 investment performance review with the Board. He reminded the Board that the report is based upon investment policy criteria set by the Board. The data in the report is as of December 31, 2003. Morningstar is changing some benchmarks to be more reflective of the funds within a given benchmark. For example, foreign large cap funds will be compared only with other foreign large cap funds. This change is expected to provide more accurate indicators of a fund's ability to meet or exceed the benchmark.

Motion: Mr. Traver moved to accept the benchmark changes as recommended on pages 17-18 of the report. Mr. Nelson seconded the motion, which passed without objection on a voice vote.

Kurt Umbarger, Portfolio Specialist, and Ryan Wagner, T. Rowe Price Relationship Manager, were given an opportunity to present information to the Board regarding the investment performance of the T. Rowe Price International Stock Fund. The firm's goal is for the fund to be in the thirty to forty percentile for performance and recently it has been in the fifty-five percentile. They noted that the growth style favored by the T. Rowe Price International Fund has been out of favor in the marketplace recently and anticipate better investment performance by the fund when or if growth comes back in favor.

Blaine Rollins, Janus Portfolio Manager, also spoke to the Board about the investment performance of the Janus Fund. Mr. Rollins discussed the growth orientation of the fund and the team approach used by Janus to help manage and navigate the fund. His goal is to generate alpha by capturing any market or consumer spending increases. Mr. Rollins noted that he is very committed to Janus: three-quarters of his personal assets are in the Janus Fund with the other one-quarter being in Janus Capital Group stock.

The Deferred Compensation Investment Committee (DCIC) met in March 2004. Upon review of the recent investment performance of the Janus Fund and the T. Rowe Price International Fund, the DCIC concluded that: 1) staff should complete a comparison of other international stock funds as well as look into possible alternatives to the T. Rowe Price International Stock Fund; 2) it would be appropriate to begin the search for a replacement for Janus; and 3) Janus will be walled off to new deferrals.

Motion: Mr. Drury moved to adopt the DCIC recommendation to begin looking for alternatives to the T. Rowe Price International Stock Fund. Mr. Nelson seconded the recommendation, which passed without objection on a voice vote.

Motion: Mr. Nelson moved to accept the DCIC recommendation to look at alternatives to the Janus Fund and to wall off the Janus Fund to new deferrals effective June 1, 2004. Mr. Traver seconded the motion, which passed without objection on a voice vote.

The Board discussed the most effective method to notify participants of the Board's decision regarding the Janus Fund. The Board asked staff to send an informational letter to all WDC participants and to place similar information in the next issue of the WDC Newsletter *Money Talks* and on the WDC Web site.

The Board reviewed Mr. Traver's May 3, 2004, memo. In his memo, Mr. Traver raised some discussion points regarding the performance of actively managed mutual funds and active versus index fund policy questions. Mr. Traver suggested that the Board may want to examine whether or not the WDC should have anything beyond passive index funds in the core investment spectrum, with active funds being available to participants through the Schwab Personal Choice Retirement Account. Mr. Main recommended that Mr. Traver's memo and suggestions be discussed at the August DCIC meeting, and the Board agreed to do this and bring the topic back to the full Board for discussion at the November 2004 meeting.

WDC Program Annual Statistics Update

This presentation was deferred to the November 2004 meeting.

**Recommendation for Amendments to the Plan and Trust Document and
Administrative Services Contract Amendment**

Uniform Prudent Investor Act

Ms. Schueller discussed the Uniform Prudent Investor Act which was signed by Governor Doyle as 2003 Wisconsin Act 264. This Act regulates investments of personal representatives, trustees, conservators and guardians of the estate. Ms. Schueller explained that in order to be in compliance with the Act, the Board must amend the State of Wisconsin Public Employees Deferred Compensation Plan and Trust to substitute the prudent investor standard for the prudent person standard currently found in Section 9.04(b) of the Plan and Trust document.

Motion: Mr. Drury moved to accept the recommended change from the word "person" to "investor" in the Plan and Trust document in order to be in compliance with the Uniform Prudent Investor Act. Mr. Traver seconded the motion, which passed without objection on a voice vote.

Domestic Relations Orders

Ms. Schueller presented information on Domestic Relations Orders, a law that was signed by Governor Doyle as 2003 Wisconsin Act 160. This law authorizes the WDC Program to divide participant accounts per a Domestic Relations Order (DRO). Before the WDC may begin processing DRO requests, the Board must:

- 1) Approve revisions to the State of Wisconsin Public Employees Deferred Compensation Plan and Trust as outlined in Ms. Schueller's memo of April 21, 2004. If approved, implementation would begin on or before August 1, 2004; and
- 2) Amend the administrative services contract with NRS to include:
 - Article 5.19, which states that NRS will develop and implement procedures for reviewing, processing and administering DROs in accordance with the terms of the WDC Plan and Trust, Wisconsin Statutes Section 40.80(2r), the Internal Revenue Code and as approved by the WDC Board; and
 - Article 4.3B, which outlines the compensation NRS will receive for administration of DROs. The fee NRS is proposing for this service is \$20,100 per year, or \$1,675¹ per month, added to the base fee for the contract year and subject to the fee increase formula in the contract. NRS will deduct compensation for the administration of DROs from the WDC's bank account.

¹ \$1,675 per month based on an estimate of 5 DRO requests per month, each taking 5 hours/month of legal staff review at \$67/hour in the NRS home office in Ohio.

Motion: Mr. Traver moved to accept the revisions to the Plan and Trust document as recommended by staff. Mr. Drury seconded the motion, which passed without objection on a voice vote.

Motion: Mr. Traver moved to amend the administrative services contract with NRS to include the cost of administering Domestic Relations Orders. Mr. Drury seconded the motion, which passed without objection on a voice vote.

Recommendation to Amend Excessive Trading Procedures

As a means of enhancing the current excessive trading policy, NRS proposed a new excessive trading procedure to the Board. In this new procedure, NRS will use a computer program to identify participants who exceed four exchanges per month. These participants will receive a warning letter that explains the risks of excessive trading to the WDC and the consequences if the activity continues. If the excessive trading activity continues, the participant will receive a second letter notifying them that they are restricted to exchanges through the U.S. mail in the funds where excessive trading has been identified through the NRS process.

Motion: Mr. Traver moved to approve the excessive trading procedures as recommended by NRS. Mr. Drury seconded the motion, which passed without objection on a voice vote.

Mutual Fund Industry Investigation Update

Ms. Schueller presented an update on the mutual fund industry investigation and regulatory proposals to curb perceived abuses. Overall, the firms in the WDC core spectrum responding to the letter indicated they have or are in the process of conducting internal reviews. They are supportive of fair treatment for investors and regulators' efforts to eliminate any improper trading that harms other investors. Since the delivery of their responses, two mutual fund firms in the WDC core spectrum (Federated and Janus) have announced results from their investigations.

Steve Scheid was present via conference call to discuss his role as the new CEO for Janus. Mr. Scheid discussed the settlement that Janus has reached with the New York and Colorado Attorneys General, the Colorado Division of Securities and the U.S. Securities and Exchange Commission (SEC). As part of the settlement, Janus has agreed to establish a pool of \$100 million that will be available to compensate investors for the adverse effects of frequent trading activities. This amount includes \$50 million in civil penalties. Janus will make \$1.2 million in other settlement-related payments required by the State of Colorado. Finally, Janus has agreed to reduce management fees by \$25 million per year for the next five years. Mr. Scheid noted that the settlement, while large and painful, was now behind them. He said that Janus as a firm was disappointed in aspects of the settlement but needed to move forward. The balance sheet of the firm can handle the settlement, and they intend to work on the basics of investing for the next year.

John Nelson requested that Janus provide the Board with a copy of the Independent Trustee's audit done by Ernst and Young. Mr. Scheid said he would check into the release of that report.

Miscellaneous

Numerous miscellaneous items were presented to the Board including standard reports and participant correspondence. The Board was advised that the administrative services contract with NRS expires in December 2005. A UW La Follette School of Public Affairs summer intern will assist staff in evaluating recordkeeping services available from other providers and costs paid by other similar-sized s. 457 plans.

Adjournment

Motion: Mr. Drury moved to adjourn. Mr. Traver seconded the motion, which passed without objection on a voice vote.

The meeting was adjourned at 3:48 p.m.

Date Approved: _____

Signed: _____

Martin Beil
Secretary