City of Mesa
Deferred Compensation Committee
MEETING MINUTES
Monday, May 6, 2013, 11:30am
Mesa City Plaza Room 450 South

Members Present:
Mike Kennington (Co-Chair)
Chuck Odom
Derek Witting
Don Miller
Frank Hoglund
Jayson Vowell
Mary Dellai
Michele Long

Members Absent:
Chuck Odom (Chair)
Michael Claspell
Vicki Eden

Innovest:
Wendy Dominguez

Great West:
Scott Taylor
Lisa Tilley

Other(s):
Alfred Smith
Nikki Rosales

Meeting called to order at 11:30am by Mike Kennington

1. Approval of the following minutes:
    - November 14, 2012
    - November 26, 2012
    - December 17, 2012
    - February 4, 2013
    - April 15, 2013

    Frank motioned to approve the minutes
    Mike seconded the motion
    None opposed

2. Great West Quarterly Update

    Retirement Income Control Panel and Projected Retirement Income
    The retirement income control panel is now on the login page of the website. Scott held a seminar last month about using the website and it was the best turnout he has seen in months. Employees seem interested in utilizing the new tool and it gives them an idea as to whether or not they have enough retirement income. Great West also launched the projected retirement income on the first page of statements, which give participants an estimate based on assumptions. This is not as accurate as the retirement income control panel.

Online Withdrawals

Online withdrawals kicked off in the previous quarter, but GW worked on some items so the process works a little smoother for anyone that chooses to initiate an online withdrawal.

MarCom Award

The GW marketing and communication department and Chris submitted two fliers from last year to MarCom. As a result, the City of Mesa won a Platinum MarCom award, which is the highest level awarded. The recognition indicates that they believe the plan is doing a good job communicating with its participants about the plan.

Beneficiaries

GW was sending out mass mailings, bulk e-mails and putting bulletin notices on the website to reach out to participants that don't have beneficiaries designated. Scott is taking a new approach and is writing personal letters to each of them. He is working on a very small group at a time, starting with oldest to youngest. HR has provided updated addresses for some of the participants. Scott has received a handful of responses to the letters he has mailed out. Beneficiaries also show up on the quarterly statement for participants.

1st Quarter Update for 2013

Plan assets have continued to increase over the last four quarters. Part of it is contributions and part is due to the market. There has been an increase in participant accounts, primarily due to new employees. The net cash flow overall has been positive for the last three years and the first quarter of 2013 appears to be on track, in comparison to last year. Scott indicated that there are more in contributions each year and people are recognizing that they don't have to take out everything, once they retire.

For the 1st quarter, the bulk of the new contributions have been before tax, which means they are payroll contributions. There has been a decrease in rollover amounts, which Scott said they expected. There was a modification to the Public Safety Pension DROP program in 2011, which has made the program less of an incentive. A lot of the rollovers were coming from that program. As for distributions, there were 41 new loans and 1 unforeseeable emergency. There were also 12 outgoing rollovers and 2 qualified domestic relations orders. The majority of distributions were periodic payments or partial lump-sums paid to retirees.

NAGDCA Comparison

The average 457 plan participation rate, among the 84 plans in the 2011 NAGDCA study, was 26%. City of Mesa is at 65.3%, which is increase from last year when it was at 64.7%. These percentages are based on eligible employees that are currently contributing to the plan. The average NAGDCA participant account balance is $42,000 and Mesa's is $49,934. The average participant annual contribution in the NAGDCA study is $4,334, whereas Mesa's is $4,460, which is up from $4,142. Scott will try to have the 2012 NAGDCA study numbers by next quarter.

Department Participation Rate

Department participation for departments with 75 or more employees increased slightly from last year, with the exception of a few departments. Engineering and Transportation Field Operations both dropped by 1%. Gas Utility increased significantly from 61% to 73%. Scott can provide a complete list of departments, if requested.

Investment Advisory Services Usage

This is a new section in the report for employees and retirees that have signed up to have either advice or a fully managed account from the GW registered investment advisor subsidiary. There are 6 people utilizing the advice and 318 participants with managed accounts. Everyone else in the plan is either picking their own investments or using one of the premixed options.

Miscellaneous

The new payroll system will go live on May 20th. Jayson worked with GW to test areas that would affect them and everything seems to be fine. Down the road, GW would like to start doing online deferral record keeping where participants could change their contributions on the GW website and the information would feed back to the city. They are going to hold off on this, until after the new payroll system is live. Scott also mentioned that the recovery of the cost for the market value adjustment from a conversion in 2008 where ING and ICMA had their loss charged to the plan is all made up. The adjustment is going away, which will help the crediting rate of the stable value fund.

Strategic Partnership Plan

Lisa explained that the plan is currently a draft and in the future GW will bring it to the committee earlier in the year. The point of the plan is to build strategies, monitor them and measure them. They need to know what our goals and objectives are as a plan sponsor and they will work with us to meet those goals. Compared to our peers, the COM plan is currently doing great.

In the New and Best Practices

Lisa mentioned that there are some good reports available that she will e-mail to Mike. There were two specific reports that focused on 457 plans. One was on revenue sharing and mentioned that it should be evaluated each year. The second was on fee disclosure for government plans. The City of Mesa has been doing this at a plan level, but not at a participant level. Lisa indicated that the DOL and SCC are in disagreement about how the fee disclosure should be displayed, so GW will wait for further clarification.

Industry Best Practices

One practice that our plan doesn't have is various enrollment strategies, such as online, auto or retro enrollment. Those enrollment strategies would require the city to provide information of nonparticipating and new employees, so that plan material could be sent to them. This did not appear to be a legal issue, when reviewed by Jack Schaffer years ago, but is not common practice. Deferral record keeping would allow participants to set up annual increases automatically, with a cap amount. Also, if a participant takes a hardship, GW would set the deferral to zero and wouldn't start again, until the hardship suspension period ended.

Strategic Objectives

There are two types of Roth conversions: 1) Participants eligible for a distribution can take part of their account balance and convert it to Roth, 2) Effective January 1st, participants that are not eligible for a distribution can convert to Roth, but will be taxed. Some plan sponsors believe participants will overlook the tax requirement and will be stuck with a big tax bill the following year, after doing a conversion. GW is still waiting for clarification on certain items, regarding this change. Lisa also mentioned that Ron Nichols, former GW employee, holds retirement readiness seminars & will be in the Mesa area the week of November 18th. His seminars have more of a holistic approach and City of Mesa participants are used to more detailed financial information. Brenda with RECOM will be contacted to see if this seminar would be beneficial and if both can be combined somehow.

Roth 457

GW is looking forward to discussing the Roth 457 option with the committee, since the new system has the capability of supporting it. All employer contributions would go into the traditional 457 plan as pre-taxed. There is still a participant contribution limit, but it can be split between the traditional plan and a Roth 457 option. Participants would need to be educated on the benefits of a Roth account. The plan document would also need to be amended if this option is added.

3. Innovest Quarterly Update

The Markets

The markets were great this quarter and led by small cap stocks, as represented by Russell 2000, which was up 12.4%. Next in line were large cap stocks, with S&P 500 up over 10%. International stocks were up 5.1%. Barclay US Aggregate showed that bonds were slightly down at -.1%.

Quarterly Market Summary

This was the best first quarter for S&P 500 in the last 15 years. The best places to be were healthcare and consumer staples. The worst places to be were technology stocks and materials. Apple was down 16% for the quarter. Gold was also down 8%, which was a big headwind for a lot of the mineral and mining stocks. Bonds were flat to slightly negative. Interest rates crept up. On the international side, Japan had a really nice quarter and was up 11.7%, whereas the worst place to be was the UK, which was only up 2.5%.

Annual Fee Review

This does not reflect the new contract with GW from the RFP process. The new plan with GW is still being negotiated, but the target effective date is September 1, 2013. Currently have a month to month agreement with GW. Right now GW is charging 12 basis points and will charge 9 basis points in the new contract, which equates to a savings of about $40,000 per year. The fee rebate to the plan will most likely increase. Over the next couple of quarters, the committee will need to review options to lower this. The goal is to not create a lot of excess revenue that has to be returned.

Asset Allocation

The plan was at $135 million at the end of March. There's a lot of usage of target date funds and model portfolios.

Table of Returns

For the quarter, 6 out of 17 non-index funds beat their benchmark and 12 of 20 funds were above median. Aston Montag & Caldwell Growth fund is new and performed strongly. It beat the benchmark and was in the top 10% of all large cap growth managers for that time period. Janus Perkins Mid Cap Value continued to underperform. They had a lot of cash in the portfolio and that is a big headwind, with the index up 14%. They're buying more large cap and at the end of March announced that they're adding a new portfolio manager, which happens to be from the large cap value product. Innovest suggests that it is time to look for an alternative fund. Artisan International was slightly below the benchmark, but in the top 6% of all international growth managers. On the fixed income side, PIMCO was up .55% when the index was negative, which placed them in the top 14% of all fixed income managers. Mesa Custom Stable Value fund also did very well and was up .65%, when the index was only up .29%. The duration for the portfolio is about 3.65 years, there are 116 holdings and the current book to market is 102%. Innovest suggest watching that closely to make sure it doesn't drop below 100%, because it is a stable value fund. A lot of the T. Rowe Price target date funds underperformed, but the fund family is still within the top 25%, as it relates to other target date funds. They tend to be more aggressive, so the return is higher when things are going well. The Conservative Model Portfolio beat the benchmark, but the Moderate and Aggressive Portfolios were slightly behind.

Manager Score Card

- Fidelity Contrafund-Style Consistency, Asset Base
- MainStay Large Cap Growth I-People
- Davis NY Venture-Performance*, Overall
- Vanguard Mid Cap Index-Philosophy & Process
- Perkins MC Value-Style Consistency, Asset Base, Performance, Overall
- Vanguard Small Cap Index-Philosophy & Process
- Oppenheimer Global Fund-Organization
- American Funds EuroPacific-Asset Base
- Mesa/Great West Custom Stable Value-Philosophy & Process

**Major Concern*
All others listed as minor concern

Innovest still has concerns about Davis NY Venture. They beat their benchmark for the quarter, but long term performance is still a struggle. Innovest is going to make People a minor concern on the score card for Davis.

Report Card

The committee will take care of Davis NY Venture today and Janus Perkins at the next quarterly meeting.

- Aston/Montag & Caldwell*-Rolling 3 year periods above median
- MainStay Large Cap Growth*-Changes in ownership or key personnel
- Davis NY Venture*-Risk adjusted return above median for 5 years, Trailing 5 years return below median, Rolling 3 year periods above median, Annual periods above median
- Allianz NFJ Dividend Value*- Risk adjusted return above median for 5 years, Trailing 5 years return below median
- Janus Perkins Mid Cap Value*-Manager adherence to style and philosophy, Changes in ownership or key personnel, Trailing 5 years return below median, Rolling 3 year periods above median, Annual periods above median

**On the Watch List*

4. Large Cap Value Search

There were two funds that met the criteria to replace Davis NY Venture, during the screening process, due to teams and managers that Innovest felt would be successful.

Dodge & Cox Stock

- Based in San Francisco, CA and been around since 1930
- $175 billion in strategy assets – Buying large cap stocks and strategy has been in place since 1965
- Expense ratio is inexpensive at .52%, median is 1.25%
- Revenue sharing is 10 basis points
- Looking for well established companies and will hold a security for a very long time, because the team believes in their research. Will hold about 70-100 securities and keep cash under 10%. True team approach. Today they have about 80 securities and are overweight in healthcare and technology.
- Pros: Highly regarded as being one of the best research teams.
- Cons: Has seen significant growth in assets, which could hinder performance in future. High conviction in research drives them to hold stocks and deviate from the benchmark.

MainStay ICAP Equity

- Based in Chicago, IL and been around since 1970
- $6 billion in strategy assets – strategy has been in place since 1994
- ICAP has 3 share classes, but Innovest would recommend the lowest share class at 0.90%, which offers 20 basis points in revenue sharing
- Strategy is team based, but Jerry Senser has the final say. Look to identify stocks that are trading at a discount that have a catalyst. Portfolio usually holds 40-50 securities, so it is

more consolidated than Dodge & Cox. Today they have about 45 securities and 4% cash. They are under allocated in financials right now.

- Pros: Process unchanged since inception in 1994. Very experienced team with an average of 20 years of experience. Have a lot of their own money invested in the strategy.
- Cons: Concentrated portfolio. Allow a very short time for ideas to work out, which is usually about 18 months.

Looking at the cumulative performance over several years, Dodge & Cox and MainStay ICAP have both outperformed Davis NY Venture. ICAP is more conservative and when the market is up they capture about 96%, as when it's down they capture about 92%. Dodge & Cox captures about 111% when the market is up and 108% when it's down.

Derek questioned whether the values presented are truly large cap values. Wendy did say that they are more true to their style than Davis. She also mentioned that both funds would equally fit and complement growth managers that we currently have. It was mentioned that Dodge & Cox have a lower fee. Chuck added to Derek's point that Dodge & Cox are more true to the type of fund we're trying to buy in to. There wasn't anything presented that made either fund a clear cut winner.

Don motioned to replace Davis NY Venture with Dodge & Cox Stock
Derek seconded the motion
None opposed

Innovest will work with GW to make the change in funds. Next quarter they will bring choices to replace Janus Perkins.

5. Innovest's Long-Term Outlook for the Economy and Capital Markets

Innovest does this exercise annually. They have 15 people on their capital market team. Their capital market process covers four categories, which are Global Economics, Asset Class Fundamentals, Asset Class Projections & Asset Allocation Studies.

Global Economics
The growth and balance sheets don't show any real velocity from the stimulus yet. Employment and wages have been pretty sluggish, but could improve with housing improvements. Debt levels are still a huge drag on the economy. Inflation is currently subdued, but could be a wildcard going forward. The gap between spending and revenue from the government is huge. Political polarization is at levels we haven't seen since the early 1900's. There is no grand solution to the problem in the near future. Economic growth will likely remain sluggish.

Equities
2012 was a good year for the markets and 2013 is off to a good start, yet expectations are slightly below what they were last year. Valuations are higher than they were a year ago. Expect large caps stocks to outperform.

Fixed Income
Fixed income returns are going to be anchored by really low nominal yields. High yield is one of the areas with the biggest change and people are putting a lot of money into that field. Innovest would like to discuss cutting our exposure in that area.

6. Asset Allocation Study 2013

High yield bonds are trading above par. On the stable value side, low current yields are pushing stable value returns lower. Wendy went over the asset allocation study for all three models (Conservative, Moderate & Aggressive). In the conservative model the mix didn't change much, but the expected return is lower this year. Making a moderate change and going to Mix 2 would make sense, because of high yield.

Model Type	2012 Expectation per year over the next 5 years	2013 Expectation Mix 1	2013 Expectation Mix 2
Conservative	3.91%	3.50%	3.75%
Moderate	5.68%	5.26%	5.50%
Aggressive	8.32%	7.90%	8.10%

There was question and minor discussion by the committee about moving high percentages out of stable value. Scott indicated that the rate on stable value is 2.15 right now and is trending lower. Wendy said Innovest's expectation for stable value is 1.5% going forward. Fixed income isn't much higher, but it's a little better. Innovest recommends moving to Mix 2 for all models.

Derek motioned to change all three models to Mix 2
Michelle seconded the motion
None opposed

7. Next Quarterly Meeting will be held on Monday, August 5th
   Will discuss Roth 457 option
   Chuck and Mike will continue to work with GW on the contract
   - Mike will post an article on InsideMesa, confirming the award to GW, once all documents have been finalized

8. Meeting Adjourned at 1:20pm