Minutes of the Meeting
of the
College Savings Program Board

Held in the State Treasurer's Conference Room, Fifth Floor
1 South Pinckney Street
Madison, Wisconsin

May 12, 2008
1:00 p.m.

MEMBERS PRESENT: *Darling, Sass, Johnson, Wegenke, Durcan, Oemichen, Adamski, Cook, Sheehy (by phone)*

MEMBERS ABSENT: Plale, Rosen

OTHERS PRESENT: Megan Perkins, EDVEST Program; John Lease, Office of State Treasurer, Michael Wolff, DOA ; Jay Risch, Sen. Darling's office; Andrew Owen, Sarah Henriksen, Shane Martwick, Tom Biwer, Wells Fargo Funds Management; Linda Schlissel, EAI (by phone)

I. Call to Order and Roll Call – The meeting was called to order at approximately 1:05 p.m. by Board Chair *Darling*. (See above for attendance.)

II. Approval of Agenda – *Wegenke* moved, and *Oemichen* seconded a motion to **approve the agenda as distributed.** Motion passed unanimously by voice vote.

III. Public Presentations – None

IV. Approval of Minutes for February 11, 2008 Meeting - *Wegenke* moved, and *Johnson* seconded a motion to **approve the draft minutes from the February 11, 2008 meeting as distributed.** Motion passed unanimously by voice vote.

V. Administrative Reports

A. Board Chair Comments – Senator *Darling* deferred her comments, as the Treasurer had to leave early. She briefly reviewed the main items on the meeting agenda.

B. State Treasurer Comments - Treasurer *Sass* discussed her outreach efforts in ten counties for EdVest, in schools, with parent groups and to the local public media through radio interviews. Statewide the Wisconsin radio network is broadcasting the new EdVest radio ad at least seventeen times over the next week. The program may do another round of the ads in September to coincide with the opening of school.

Sass reiterated her public comments in the press regarding the hiring of the new Program Director. She said that she passed all the OSER requirements to be interviewed for the job, and is fully qualified to fill the position. Other Board members commented that Megan's job is not to make investments for the program, and *Adamski* stated that he had been contacted by the reporter looking for negative comments, and told him he had been very happy with her performance. Cook asked for clarification of the publicity, and other Board members responded with details about the newspaper article and radio talk-show discussions.

C. <u>Program Director Comments</u> - *Perkins* reiterated the comments of Treasurer Sass about the ongoing outreach activities throughout the state, and particularly in the northwest part of the state. A new program mini-web site that Wells Fargo has established will have announcements about locations for upcoming events. Locally WIBA in Madison is running the program advertisement as a generic ad about why families should save for college.

Ratings have recently been released by Hurley's SavingforCollege.com web site. His 2007 performance rankings listed tomorrow's scholar in the top five for one-year performance, not including sales charges. She explained that the ratings construction can affect how our portfolios are ranked against other state 529 offerings. This is especially true for the enrollment-based program portfolios we offer, as the asset allocations of the model that Hurley uses to rank program performance does not always fit well with our selections. We have resisted the urge to refine the structure and asset allocation of EdVest or tomorrow's scholar portfolios to try to increase their rankings by Hurley's methodology. Readers of the rankings do not always understand this. *Darling* stated that since perceptions are such a large part of the investing public's view of 529 plans, the program needs to work with Wells and EAI to make sure we are offering the public the best and most cost-competitive product. *Johnson* suggested an article be placed on the web site to explain the comparison process that appears in these ratings. *Perkins* reported that on the 5-cap ratings on Hurley's site, we have garnered 4 and one-half cap ratings for the programs, which is a very positive result of their review. *Darling* mentioned the possibility of having a marketing committee to consider some of these ranking issues. *Cook* asked about whether a clipping file was kept with ranking comparison articles that appear in various publications, and *Henriksen* stated that these appear in the annual report that was distributed to all the Board members.

Perkins related that Morningstar has also just released the top and bottom five state 529 plans, and our programs do not appear in either group. There was a brief discussion of the Morningstar ranking article. The program did not see a pick-up in communications from concerned investors in the first quarter, with the exception of a half-dozen or so calls or e-mails about the Legg Mason portfolio results. *Cook* expressed her concern, and suggested that the Board may need to be more aggressive in its approach to the performance of that portfolio. *Perkins* reported on the first quarter program statistics in terms of total assets which were down largely due to market declines, and new accounts which were up. *Darling* asked to see more on the demographics of where new account activity is coming from at the strategic planning meeting in July. The contingency fund stood at $7.2 million, and expenditures are below projections in the budget. In April, portfolios performed very well, with asset gains in all portfolios from market increases. There is no news about the Strong settlement on the SEC web site. Over 30 states wrote letters, including Wisconsin, on the announcement of proposed permanent federal regulations on 529 operations. There were over 60 letters received by the treasury on the matter.

D. <u>Program Manager [Wells Fargo] Comments</u> - *Henriksen* briefly reviewed the year-end summary which was distributed. The press coverage, which was extensive in 2007 and largely positive, is included in the materials. *Darling* asked to review/discuss the program demographics at the July session, which she said Wells would do. She then did a 1st quarter update on outreach efforts and the marketing campaign that is launched. On client service trends, there was nothing out of the ordinary other than increasing interest in investors from other states. Internet activity has continued to grow versus other sources of investor interest, which may reflect the increased emphasis on internet ads. There have been several upgrades to tomorrow's scholar materials for advisors. The annual program description updates have been completed which is a considerable undertaking. *Oemichen* commented that when he or family members have had reason to call the program the service has been prompt.

VI. Old Business

A. Board Offsite Meeting for July 9, 2008 – *Perkins* commented that in conversations with Andrea Feirstein about the meeting agenda, she would be taking a look at trends in 529 state programs nationally, marketing efforts, trends in program structure and management, and regulatory efforts affecting the programs. We will also be taking a look at the Board, and Board structure and operations. *Darling* mentioned marketing and investment committees, and the potential of having outside members be a part of those committees. *Oemichen* asked about the growth in the non-parent or grandparent ownership of accounts. *Cook* asked for clarification about the date of the meeting, and requested that the budget be kept low for this. She suggested that this spending was perhaps not necessary at this time, given the current state of the economy/investment environment. *Darling* suggested that the site for the conference could be the state capitol, and *Perkins* stated that a location in Madison has not yet been selected. (Treasurer Sass left the meeting at this point.)

B. Watchlist Update [Evaluation Associates, Inc. and Wells Fargo] – *Schlissel* apologized for airline problems which prohibited her colleague from attending the meeting in person. (She explained that a family graduation commitment precluded her in-person attendance.) She reported on a telephone conference call with Legg Mason concerning the manager's market philosophy, and EAI didn't find any qualitative reasons to make a stronger recommendation for removal at this time. Their performance has continued to be very disappointing through the first quarter. All the manager's processes were discussed at length with them. Sector weightings have really hurt the fund. *Biwer* commented regarding the manager's assessment of the contributing factors to the underperformance of the Legg Mason portfolio over the past six months. *Johnson* asked about the process for any automatic action or notification informing potential investors about watch list action from last meeting. *Schlissel* replied that there was not any resolution of the question at the last meeting in her recollection, and *Perkins* stated that she had checked with other states and an attorney regarding what was required to be done. The watch policy is posted on the program web site and investors are told of the watch status of the funds if they inquired about it, but the funds on watch are not listed on the site. *Cook* suggested that waiting to take action until year end is a long time, and that given the six months of performance data she questioned whether EAI would feel that there should be a need to remove the fund immediately. She felt that given the investor inquiries about Legg Mason, it is a big issue and felt that the Board may want to move more quickly to remove it, or possibly at the next Board meeting. *Darling* concurred that it was a big issue and the Board could act at any time. *Schlissel* felt that year-end would be a worst case scenario and that the portfolio should be given a little time. The managers feel that the portfolio is strongly under valued and that daily market performance would indicate that time should be given to see if the manager's efforts to improve the results would succeed. *Cook* said she would like to hear from Wells Fargo and EAI when the period of waiting for improved performance was over. *Adamski* asked about how and when the watch policy kicked in to force the Board to act. *Schlissel* read from the policy regarding the steps to be followed by the independent investment advisor and the Board, under the circumstances that benchmarks are not met. The policy is broad and leaves much to the Board's discretion. *Johnson* reiterated that the policy would have the Board take action to follow up on watch list placement by next February in this case. *Adamski* recommended that a copy of the watch list policy be attached to the agenda whenever a discussion of funds on watch is on the Board agenda. *Owen* stated that Wells would, in cooperation with EAI, make a recommendation at the appropriate time as called for in the watch policy regarding the funds currently on the watch list. *Schlissel* advised the Board that EAI has seen other investment managers struggle in the current market environment, and that for the Board to take any more severe action with Legg Mason at this time would not be appropriate. She would prefer to see the performance rebound a bit. *Oemichen* noted that a number of other funds have underperformed their benchmarks in the first quarter of 2008, and he agreed that it was an unusual quarter for investment performance. *Darling* stated that if EAI thought quicker action was required, they would recommend it. *Wolff* suggested that the mechanics ending an investment option could be controversial, and the Board needs to be deliberate in this process. *Adamski* asked that Wells Fargo's recommendations in regards to the watch list policy should also be taken into consideration, even if the policy does not explicitly state that. *Schlissel* suggested that the policy was drawn in such a way as to not bias the evaluation of all funds used in the program, including Wells Fargo funds. *Johnson* asked about the other funds that were placed on watch at the February meeting. *Biwer* responded that the WF Opportunity Fund and the WF US Value Fund which are on watch have shown marked improvement. The Opportunity Fund is 227 basis points ahead of its benchmark for year to date through April and rank in the 13th percentile in their category, and the US Value Fund has also picked up. *Schlissel* concurred with this assessment of the Opportunity Fund's improvement. The US Value Fund is now right around the middle of the pack in its category, trailed its benchmark by 50 basis points through April, but rank in the 43rd percentile in their peer group universe. *Schlissel* commented that US Value had outperformed its benchmark in the first quarter, but fell behind in April.

Johnson asked about the performance of the Baird Bond funds which are not on the watch list currently. He felt that there was fairly significant underperformance there. *Schlissel* responded that its underperformance shows up for one and now three year periods, but the Baird Aggregate Bond Fund has done fairly well, at the 52nd percentile just below its group median. She explained that the comparisons for the static portfolio peers and their benchmarks. The watch list looks at both. She wanted to check as to why they were not recommended for watch at the last meeting. *Darling* asked if decisions could be made between meetings by conference call, if deemed necessary and urgent. It was affirmed that the Board could do so. *Owen* commented about active management of the Baird and Legg Mason funds in periods prior to the recent market turmoil, and noted how this previous good performance can be cyclical of this type of strategy. He suggested that is a reason not to react too quickly and be cautious in either up or down periods for any of the funds in the program.

VII. New Business

A. First Quarter 2008 Investment Performance Report - *Schlissel* highlighted the report of the quarterly performance data. She pointed out the good performance of the Vanguard Balanced fund, the Wells Fargo Bond fund, and the Ultra-Conservative portfolio versus their benchmarks in a very difficult environment. The US Value, Opportunity, and Mid-Cap Disciplined funds all beat their benchmarks in the quarter. She reviewed the number of funds that out-performed versus benchmarks for EdVest and tomorrow's scholar, and highlighted the Harbor International fund as an outperformer for tomorrow's scholar, besides the others mentioned earlier. *Adamski* commented that he looked forward to 5 and 10 year comparisons at some point, and *Schlissel* concurred that we are moving in that direction with the funds in the program.

B. Wells Fargo Corporate Bond Fund Merger and Fund Reallocation - *Biwer* stated that the WF Corporate Bond Fund is merging into the WF Income Plus Fund which necessitates reallocations of the fixed-income funds in the EdVest/tomorrow's scholar program portfolios. The major factor is that the RiverSource Mortgage fund, which is virtually all mortgage-backed securities, does not allow tracking of the Lehman Bond Aggregate. The sector allocations are too heavily weighted in the mortgage area, and must be adjusted as shown in the proposal handout presented to the Board. He mentioned that with three different manager teams in fixed income between the funds being used, the diversification of management was being preserved. A brief discussion of the slight changes in fees followed. *Wolff* questioned WF as to whether the changes in fees could be waived, and WF responded that it would be difficult at the level being discussed operationally to adjust for 1 or 2 basis points. He asked *Henriksen* to quantify the amount she was talking about in dollars. *Wolff* felt that while these were possibly insignificant changes, they do affect what the investor had been told that they would be paying when buying into the portfolios and expressed concern. He was still not comfortable with the changes and asked for quantification of the dollar amount of the fee adjustments. *Owen* mentioned that another 2 basis point fee reduction was going to be reported on later for a different fund that would impact the same shareholders, but will essentially be an offset to what is being done here with the allocations (WF Diversified Small-Cap fee reduction). *Wolff* stated that this made him more comfortable about the fee changes being proposed in the fund merger process. *Oemichen* moved and *Wegenke* seconded a motion that " **as recommended by Wells Fargo, approve the merger of the WF Corporate Bond Fund into WF Income Plus Fund, and accept the fund reallocations in the program portfolios as shown in the presentation."** *Johnson* asked for clarification as to how this flowed through to the participants in the portfolio, how they would be made aware of these changed. *Henriksen* stated that investors would be provided a program description supplement detailing all the changes that impact shares of the portfolios involved, as this represents a material change in their investment. Typically sixty days advance notice is provided to investors in a situation such as this. As it subject to shareholder approval, it will not happen until summer. Motion passed unanimously by voice vote.

C. EdVest 30% Equity Portfolio Proposal – *Henriksen* reviewed the rationale for adding a 30% equity portfolio to the program, between the WF Balanced portfolio, and the more conservative Bond and Ultra-Conservative (money market) portfolios in the enrollment-based investment tracks. The idea is to avoid an abrupt shift in the investment mix between fixed income and equity percentages in these popular investor options and make the transitions smoother. This is something that Morningstar had commented on and that WF had been discussing internally. *Henriksen* discussed the fund allocations for the Board as shown in a brief presentation from WF about the proposed new portfolio. *Schlissel* commented that she had consulted with Wells regarding the allocation of growth verses value amounts in the proposal, and Wells adjusted the weightings to give more weight to value rather than growth as this is supposed to be moving towards a more conservative asset allocation. WF agreed with EAI's comments and recommendations in this regard to the new portfolio and make tweaks from their original presentation, and they are now comfortable with the proposal. *Henriksen* walked through the placement of the new 30% equity (Conservative) portfolio in each of the three enrollment-based EdVest tracks. *Wegenke* moved, and *Adamski* **seconded a motion "to create a 30% Equity Portfolio to be used in the Enrollment-Based investment tracks in EdVest, as shown in the presentation to the Board with the fund allocations as presented by Wells Fargo. This "Conservative Portfolio" would also be available as a stand alone fixed-allocation option within EdVest**." There was not other discussion. Motion passed unanimously by voice vote.

D. Proposal for a Temporary Moratorium on tomorrow's scholar Administrative Fees – *Perkins* reviewed for the Board the accumulation of fee income that is now well over $7 million, and which continues to grow from monthly fees from tomorrow's scholar. The benefits to this step would include being able to report that the state would no longer be collecting any fees for operating its 529 college savings program, and the public relations impact of this statement could be substantial. She stated that the program could easily operate for a considerable period of time from the surplus funds, given the current and projected future budgets for the program. *Johnson* asked about any other thoughts about how to put the contingency to use in the future. *Perkins* responded that there have been some discussions on this point, but that any use would require a statutory 13.10 request to the Joint Finance committee of the legislature. Possible uses of some portion of the funds might include targeted marketing, scholarships, matching grants, etc. *Wolff* stated that he thought for a program with over $2 billion in assets under management, the size of the contingency was quite small and possibly too small rather than the opposite. For litigation alone, the amount available would not cover attorney expenses in the unforeseen event of having to deal with an investor lawsuit or some other type of issue. He gave some examples of some other state operations and their contingency provisions. *Wegenke* stated that his concern is that the operational costs of the program are being borne principally by out-of-state investors, as state fees have been cut to zero on EdVest accounts already. He restated the potential uses of the funds, and felt that once a moratorium on the fee was put in place on tomorrow's scholar it would be very difficult to reinstate it without substantial negative public impact. He felt uncomfortable with cutting the fee now, given the state of the market at this time. *Durcan* agreed, and felt that using the funds for Wisconsin scholarships would be a better approach, as an example of what to do with any operational surplus. *Cook* stated that she felt that the program should not incur the loss of this income source at this time. *Oemichen* asked the Board what level of balance in this fund they would like to see, but that would not incur an unfavorable response from the legislature. *Wolff* responded that he thought it would be very politically difficult for these funds to be used for anything other than somehow providing a direct benefit to the present investors. Second, his feeling was that it would be easy to remove the fee and of small consequence, but very difficult if it had to be re-established. *Henriksen* said that Wells was comfortable with whatever the Board decides, and that a temporary fee waiver still has to be disclosed and the fee included in calculations about the investment returns, since it is a voluntary waiver. She felt however that anything that could show a positive impact on the tomorrow's scholar actual investor returns would certainly be of benefit, even if relatively small.

Board consensus was to defer any action on the state administrative fee moratorium at this time, as opinion was divided. *Adamski* stated that the Outreach (low to moderate income) Committee of the Board has yet to make any firm recommendations, so that this move to cut the tomorrow's scholar fee might be premature. He was comfortable with putting this on hold for a year.

E. <u>Proposal to Raise the Plan Maximum for the State of Wisconsin</u> – *Perkins* distributed a presentation that Wells Fargo assembled on the maximum investment limits for other state 529 college savings plans. Wisconsin is now pretty low, and the average is close to $290,000. Five years at the current highest cost university nationally, George Washington University, would put the program maximum at $330,000 which is the level the Utah program currently uses. *Wegenke* thought it was in Board policy or state statute to peg this maximum program investment to the highest cost school in the country. The Board discussed whether this was in policy already, and if the maximum was indexed. *Johnson* asked if EdVest was limited to undergraduate expenses or if graduate expenses could be included. EdVest can be used to pay for graduate expenses. *Wolff* asked if there was some federal rule about this in regulations governing 529 programs, and *Henriksen* stated that it was five years of undergrad expenses and two of graduate school in the current regulations we operate underr. *Adamski* suggested looking at the early Board minutes to see if the Board had set the number to be automatically indexed. *Cook* suggested that if the level is going to be changed now, it should be set high enough so the issue would not have to be revisited again soon. *Sheehy* suggested tabling action on the proposal until it could be investigated further. Wells was asked for their recommendation on the matter, and *Henriksen* responded that anywhere between $300,000 and $330,000 was comfortable for them, but that going beyond what the rest of the industry is using as a maximum was not something they would feel comfortable with. She stated that a few investors had reached the current maximum and had to be told they could not invest additional funds. She felt that rolling as many of these program changes together so that they can be disclosed to investors and potential investors at the same time, works best from an operational standpoint of the program manager. *Darling* suggested that the current policies of the Board be available and up to date when agenda action items of this type are being debated. *Wegneke* **moved "that the Board increase the value of the maximum investment in the EdVest and tomorrow's scholar programs from the current level of $246,000 for a single beneficiary, to ~~$300,000 or whatever maximum level current Board policy permits, whichever is higher~~."** Motion was seconded by *Oemichen.*

Darling asked *Sheehy* if he was comfortable with the motion, given his earlier request to delay action on the issue to a future meeting. He asked why the Board wouldn't tie the maximum program investment to the highest level permitted by federal regulations. *Henriksen* replied that from an operational standpoint, this would require the program manager to monitor constantly tuition costs for every institution of higher education in the country. This would be a substantial administrative burden, and would require frequent updating and reprinting of the program's disclosure documents. *Cook* stated that the Board possibly has an indexing policy for this limit, but both *Perkins* and *Henriksen* replied that this is not the case to their best recollection. *Cook* then suggested that $330,000 should be a good number based on the data presented about George Washington University, and *Darling* concurred. *Henriksen* mentioned the criticism that 529 programs have incurred as being a tax shelter for the rich, which is why she felt that other states have avoid going higher. Wegenke suggested using $330,000 for now, and revisiting the possibility of indexing the maximum at the Board retreat in July. He moved to withdraw his earlier motion and "**amend the language to set the program maximum investment to $330,000"** instead of the draft language proposed earlier. *Oemichen* and the Board accepted this amended language. *Darling* asked for a vote on the amended motion, hearing no further discussion from Board members. Motion passed unanimously by voice vote.

Adamski reiterated his position that the maximum investment should be indexed. *Wolff* felt that is should not be constantly dynamic, as this becomes unmanageable. (*Schlissel* signed off from the meeting at this point.)

VIII. Status of Proposed CD Option – Vote on Recommended Structure – *Adamski* reported on the CD Working Group meeting of the past week, and said that he is more comfortable with the recommendation for the proposed structure than he previously had been. *Henriksen* made the powerpoint presentation that was distributed to the Board that recapped the structure options and what had occurred since the February Board meeting.

Structure A is the preferred approach for both the credit union and bank option at this point in the development of the product. The Working Group has recommended that the program manager, Wells, proceed with this approach, both because of cost considerations and operational issues that arose during the investigation of Structure B for banks including the potential impact on breaking a CD by an investor. Members United CU was fully supportive of Structure A, and Banker's Bank, although preferring Structure B could use the Structure A approach. *Adamski* said that it became a practical consideration of including both banks and credit unions go ahead with the Structure A recommendation of the group, although he still did not understand point four on the presentation and questioned why it was so stated. He has been assured by the participants in the discussions of the investment structure that Structure B would continue to be pursued for the bank part of the CD option at some point in the future. Adamski volunteered to continue work on Structure B through the low-moderate income committee (Outreach) in the future because he felt that depending on the demand for the product, we could run out of banks that were interested in participating and this would be a serious impediment to the product's success. He felt that some banks might just think, "Why bother" with such a small investment size limitation. The final consideration from his point of view is that

Structure B would be a better inducement for more banks to promote the product that Structure A would. *Cook* asked *Adamski* why he would want to go forward now, rather than tabling it and studying it further given the caveats he just described. *Adamski's* response was that there is not a workable system to get the program up and running. The credit union broker has said they could not use Structure B, and consistency was important in addition to the costs involved to build out the other approach at this time. He thought that low and moderate income persons would be better served with Structure B and eventually would like to see that happen as interest in the CD option grows. *Adamski* **moved "that the staff and Wells Fargo proceed to develop the CD investment option using "Structure A", which presumes that a maximum CD of $100,000 per financial institution will be offered through the CD brokers. The CDs will be titled in the name of the program to satisfy the FDIC qualifications for the CDs obtaining FDIC insurance."** *Oemichen* seconded the motion. *Henricksen* gave a brief review of the CD option survey results that were received from current and potential program investors. The results were distributed to the Board. *Wolff* asked about the earlier discussions on the spread to the deposit brokers, given the reduced level of work they seemingly will be required to do under Structure A. *Henricksen* responded that final discussions on this point have not be held yet and this was all still negotiable. Motion passed unanimously by voice vote. (*Wengeke* left the meeting at this point.)

XI. Announcements

A. Upcoming Conferences for Board Members – *Perkins* reported that the upcoming boot camp for Board members being offered in Las Vegas by Joe Hurley's organization would be on September 24-26, 2008. If interested, early registration is until the end of June. There are no future CSPN conferences planned at this time, but it is expected ther will be one late in the year, possibly in December as there was in 2007. Board policy permits and encourages each Board member to attend a conference at least once during their tenure, and this travel should be approved in advance at the prior meeting. The program will pay travel and registration expenses.

X. Adjournment— The Chair adjourned the meeting at approximately 3:10 p.m. on a motion by *Oemichen*, seconded by Adamski, which passed by a voice vote.