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

December 19, 2005
1:00 p.m.

MEMBERS PRESENT: *Adamski, Darling (joined at approximately 1:50 p.m.), Johnson, Wegenke, Durcan, Oemichen, Reid, Voight, Cook; By Phone: Sheehy, Plale (joined at approximately 1:17)*

MEMBERS ABSENT: None

OTHERS PRESENT: Marty Olle and Rich Janosik, EDVEST Program; Tom Petri, Sen. Darling's office; Andrew Owen, Nancy Galica, and Sarah Henriksen, Wells Fargo Funds Management; Michael Wolff (joined at approximately 2pm) DOA. By Phone: Jeff Van Orden, Ron Jackson, EAI; Matt Tomasicchio, Susan Lowe, KPMG; Avi Lank, MJS

I. Call to Order – The meeting was called to order at approximately 1:03 p.m. by Board Vice-Chair *Voight.*

II. Roll Call – See above.

III. Approval of Agenda – *Wegenke* moved and *Adamski* seconded approval of the agenda as posted and distributed. Motion passed by voice vote without objection. Olle suggested that the Board allow representatives of KPMG to give their report on the annual program audit at the beginning of the meeting, rather than waiting until later in the agenda under Item A of New Business. Also, he suggested that the Board permit the Program Manager (Wells Fargo) to also give a report under the Administrative Reports section of the agenda and to add this item to future meeting agendas. The revisions to the agenda were accepted by the makers of the motion to approve, and the amended agenda was passed by voice vote without objection.

IV. Public Presentations - None

V. Approval of Minutes – *Reid* moved and *Wegenke* seconded a motion to approve the minutes of the August 17, 2005 meeting of the Board, as distributed. Motion passed on a voice vote without objection.

VI. Administrative Reports

A. Board Chair Comments – Deferred until later in the meeting.

B. State Treasurer Comments – *Voight* reported on a press release that he prepared last week reminding the public to invest before December 31 to receive the state tax deduction for 2005. He also stated that he wants to get back on track to encourage people of middle and lower income to participate in EdVest. *Voight* has suggested to Wells Fargo that they add more detail to the visual presentation of program expenses on the web site, so that the public can easily see the low expenses of the program. *Johnson* asked about uniform disclosure for states operating 529 programs; *Olle* stated that there are standards in place, but they relate to printed materials used as the disclosure documents, not necessarily to program web sites. The EdVest program is committed to following these industry guidelines. *Voight* asked the board to let him know if there were any other improvements members might like to see with the site.

Voight also announced that two weeks ago he had announced his intention to run for re-election.

At this point, two new Board members were introduced. *Mary Cook* and *Pat Sheehy* presented background information and said they were anxious to help the Board with its work. *Voight* recognized two former Board members, *Michael Clumpner* and *Michael Wolff* and thanked them for their work over the past five years in guiding the program to its present size.

Adamski addressed the desirability of having a representative of the Department of Administration participate in Board matters. He mentioned the benefit that *Michael Wolff* had brought to Board activities, and suggested that he be asked to become an advisor to the Board and attend future meetings. *Adamski* moved, and *Wegenke* seconded that the Department of Administration be requested to name an advisory member who is knowledgeable of the program to attend Board meetings in the future. (*Plale* joined the meeting in progress.) Motion passed by voice vote without objection.

Wegenke commented that current actions of Congress would seriously hinder the ability of low and moderate income student to afford a college education. The cost of borrowing for students could go up by as much as 30%, and there will be a decrease in Pell aid. He noted that the Outreach Committee should meet soon, and that it should look at the overall context of paying for college, and not just EdVest. *Voight* responded that he would try to schedule a meeting as soon as possible.

C. Program Director Comments --- (the Board jumped ahead, to allow representatives of KPMG to give their report on the annual audit for the program.)

VIII. New Business

A. Independent Auditor Report -- Financial Audit for Fiscal Year 2004-05 -- Matt Tomasicchio and Susan Lowe from KPMG addressed the Board by conference phone from Philadelphia. They discussed the annual audit results and the report prepared for the meeting. There were no significant revisions to the audit results. Additional "agreed-upon procedures" were completed and used to account for inter-fund transfers between portfolios. KPMG received good cooperation from the participants, the audit was unqualified and the results were very favorable. Tomasicchio mentioned a footnote regarding the stable value portfolio, related to FASB guidance on accounting for stable value funds. The FASB is expected to put out new standards for stable value accounts early in 2006, which may affect accounting for the stable value portfolio. KPMG will keep us and Wells informed about these pronouncements by the FASB.

Oemichen asked about the fee for the stable value portfolio. Tomasicchio stated that the stable value fund required more work, due to the present uncertainties unique to this type of fund. *Voight* asked if audit fees would be lower next year. Tomasicchio stated that it is likely that fees would go down, as this was KPMG's first year with it and it required more effort the first time through. Lowe stated that it would be approximately $15,000 lower, but this could change do to price/wage increases. There should be a net/net decrease for next year, including the agreed-upon procedures that were completed. *Oemichen* asked if there was anything the auditors would like to discuss with the Board in executive session; the response from KPMG was that there was not. KPMG representatives signed off the call at this time.

(Returning to item VI.C)

Olle reported to the Board that American Century Funds had just agreed to acquire Mason Street Funds, one of whose funds is a small part of the new Wisconsin Select Portfolio. It should not create any significant change in that portfolio.

Quarterly tables of activity are not yet available. The activity report shows modest increases to assets and accounts. Assets total approximately $1.5 billion, and total accounts at 200,000. December should be the best month of the year for the program, as the state tax benefit ends at the end of December. The Wisconsin Select Portfolio is growing modestly. *Olle* also reported on program revenue and expenses; revenues reflect the waiver of the EdVest state fee and the decrease in the Tomorrow's Scholar state fee to 10 basis points. The contingency fund balance is $6.1 million. He also reviewed the administrative budget for the program which totals $827,000 for the current fiscal year. He will continue to review the budget with the Board every six months, per comment by *Adamski*. (*Darling* joined the meeting at this point.)

Olle reviewed information presented at the recent College Savings Plan Conference in Boston organized by Joe Hurley, which was also attended by *Sheehy, Cook* and *Plale*. Growth in the 529 industry has slowed, but there remains a lack of public awareness with only about 7% of eligible families participating. Currently 82% of 529 program assets have been generated through financial advisors, with the remainder from individuals directly participating in the programs. The average account size nationally is about $10,000, compared with $6,700 in direct-sold EdVest and $5,500 in EdVest advisor-sold. Hurley thinks one of the big challenges to the industry is the extension of the 2010 sunset provisions of the federal tax benefits. There will be more bank products, more index funds and exchange-traded funds as well. Federal regulators discussed recent settlements in the industry, with the Amerprise action as an example. *Sheehy* reported that other state administrators look to Wisconsin as a success story, given the problems that we have encountered and successfully managed. He also believes that low and moderate-income families need to be targeted to make sure they know the program is available. *Cook* agreed and said she was surprised at how the programs have nationally become a vehicle for high-income families to take advantage of the tax benefits. Also, she appreciates the efforts Ohio has taken to add a bank product to their program for clients who feel more comfortable with that approach to investing. The Board discussed the use of non-traditional methods of reaching potential families. It also invited Michael Wolff to join them at the Board table and discussed the earlier vote to ask a representative of DOA to be sent to future Board meetings.

A. Board Chair Comments -- *Darling* welcomed the two new Board members and thanked the former members for their service.

D. Program Manager Comments – Sarah Henriksen of Wells Fargo gave a summary of the year-end campaign. She reviewed the marketing and promotion plan for the final weeks of the year. They are also doing a direct mailing to take advantage of the Dec. 31 tax deadline. She distributed copies of print ads that are running now. Contributions are running ahead of last year, and phone calls are about double from last year.

VII. <u>Old Business</u>

A. Compendium of Board Decisions and Policies – *Olle* reviewed a list compiled by staff of all decisions made by the Board over the first 30 Board meetings. It is currently organized by date only, but could be sorted in other ways if needed.

B. Board Meeting Dates for 2006 – *Olle* suggested months that would work for meetings during the next year. In late March, the Board could have an annual review of portfolio performance with consultants Evaluation Associates, Inc. A second meeting in May, a third in September or October, and a fourth meeting in either December or January might work. *Voight* suggested that the next meeting be in January 2006 to discuss the selection of a new vendor under the RFP. *Darling* agreed. *Johnson* thought that a meeting dedicated to long-range strategic planning would also be useful. Members were requested to give dates that work for them; Monday afternoons seems to be the preferable times to meet, either at noon or 1pm. *Voight* also added that a meeting inviting investors might be a good idea, and it might also include a speaker.

VIII. New Business

C. Procedure for Removing Underperforming Investment Portfolios – Jackson and VanOrden of EAI presented an overview of a draft policy. *Sheehy* asked if the board has an investment committee. He thought it might be appropriate to have such a committee, to more efficiently deal with these issues. *Johnson* asked what authority the board has under the present contracts to remove an investment option. *Olle* suggested that since the Board has the authority to approve investment options, by inference, it also has the authority to remove an option. Wolff suggested that if it is not possible under the current contract, it will be after May when it is redrafted. Jackson of EAI suggested that some 529's do use a subcommittee, but it is entirely up to the Board as to how the policy should work.

Janosik discussed the origin of the language used as a basis of the draft policy. The state's deferred compensation program uses such a policy. EAI added several items to the original performance criteria that had been included in an earlier draft. Jackson said that these are guidelines that can be used to monitor more closely funds that might be in trouble, and these criteria would "raise red flags" when appropriate. He discussed examples of how the criteria would come into play.

The plan is to vote on the policy at the next Board meeting. *Adamski* asked about using the word guidelines instead of criterion in the last sentence of the first paragraph of the policy. Jackson responded that he thought the word "criterion" is more appropriate here; a decision about wording would be carried over to the discussion at the next meeting. *Voight* asked about disclosing the performance evaluation to the public, and whether it should be on the web-site. *Johnson* stated that there is a fine line between monitoring performance and disclosing information that might cause undue consternation with investors. He thought that the shortterm evaluation of the performance, or putting portfolios on the watch list, should be carefully considered and put in context when making it public.

B. Investment Performance Review, Third Quarter 2005 – Jackson reviewed investment results for the period ending September 30, 2005. He stated that the age-based EdVest portfolios performed very strongly relative to their benchmarks in the quarter. All performed above their benchmarks, with the exception of the moderate portfolio, which met its benchmark. For the static EdVest portfolios, the Vanguard index met its benchmark, the Vanguard balanced portfolio exceeded its benchmark, the Legg Mason aggressive portfolio outperformed it benchmark and the Baird bond portfolio met its benchmark. The third quarter was a very strong quarter for stocks, while bonds were off during the quarter.

Year-to-date, nearly all the funds are in the top half or top quartile of their fund peers. The enhancements made to the fixed income portfolio in September have improved performance. The age-based portfolios were below their benchmarks, although the gap is narrowing. Jackson mentioned several underlying funds in the portfolios whose performance or leadership merit scrutiny; the Wells Fargo Advantage US Value Fund, WF Opportunity Fund and the Riversource New Dimensions Fund. *Olle* suggested that the discussion continue at the next meeting, and agreed that written information will be distributed to the Board prior to the meeting.

Darling asked about comparisons with other 529 program performance. Jackson stated that they are not yet ready to comment on this, but would be ready to speak about 529 performance comparisons with the year-end report in March. *Adamski* suggested that the verbal report was good, but that he would like to see the written comparisons and data from which EAI was drawing its recommendations and conclusions. Jackson and VanOrden stated in response to Board questions that the relative performance of the funds in the program is improving when compared to overall market performance over the past quarter and past year. *Johnson* cautioned against putting too much stock in one quarter performance numbers, and suggested they always be accompanied by 12 month results as well. EAI confirmed that they will continue reporting on a quarterly and annual basis, and if situations of concern arise, they will be in touch with program staff.

Johnson suggested that the Board might want to consider having representatives of each fund family come in each year to make a presentation to the Board and meet the managers. VanOrden mentioned that another 529 client schedules an annual all-day meeting and invites in all of their fund managers on that day to hear from them. This might be an alternative for the Board. Jackson also reported that another 529 client that he works with has just the fund managers that are on the watch list come in to talk with the client. Both these approaches are possibilities and might be considered going forward.

Voight mentioned that EAI is involved in the review of the investment options proposed in the responses to the RFP. Wolff stated that DOA had received a very comprehensive analysis of the proposals that are under review by the RFP evaluation team. He stated that it has been very helpful to the process.

D. New Expectations for Advisor Disclosure to Clients – *Olle* reported on the 529 Technical Conference at which he heard a presentation from an NASD representative on disclosure for financial advisors. In particular, each financial advisor who recommends an out-of-state program to a client needs to review four items. Sales suitability specific to 529's, a process and procedure for supervisory review of out-of-state recommendations, review of the impact of the loss of a tax deduction and fee/performance comparisons, and finally documentation of why the out-of-state 529 plan is better for a particular investor. He feels that it is a good time to work with Wells Fargo to communicate with all financial advisors who are selling the program, to be sure they are covering these considerations. *Cook* stated that she was not clear how far they wanted the advisor to take the suitability determination with an investor. The presentation seemed to take the suitability determination much further for a 529 investment than an advisor would have to do for other investments. *Olle* felt that we would have to work with CSPN and other state 529 programs to see how much the message needs to say, relative to what others are doing. He would like to discuss this further with Wells as a next step. *Wegenke* suggested that staff proceed to investigate what message needs to be sent. *Adamski* felt that we need to do this, but we should first talk with Wells and to the CSPN. The Ameriprise settlement on this issue was one of the triggers for this action on NASD's part. Wolff felt that broker/dealers are already quite aware of their responsibilities in this area. For direct-sold accounts, this is not really a consideration. An update of progress on this issue will be given at the next meeting.

E. New Benchmark for the Vanguard Balanced Fund Portfolio – Janosik reported that during a review of the benchmarks for the various funds for the program, it was noted that the Vanguard Balanced fund (Wellington) may not be paired with a benchmark that fits the fund as well as might be expected. Henriksen reported that when the fund was added to the program, the Russell 3000 was used, whereas there should be recognition of the fixed income part of the fund which the benchmark does not currently address. *Johnson* asked if EAI has opined on this change. Janosik reported that they agreed that this change is needed. *Johnson* felt that something in writing should be sought from EAI regarding their recommendation regarding this portfolio benchmark change. *Adamski* moved, and *Reid* seconded a motion to change the Vanguard Balanced portfolio benchmark as recommended. *Oemichen* asked if there is a conflict for him voting on the motion since he has money invested in the portfolio. It was clarified that he would not be considered to have a conflict on this matter.

Johnson asked if the action would be retroactive. *Olle* stated that it would only affect the 4th quarter of 2005. *Adamski* reminded the Board that this is the first time that EAI has had an opportunity to comment on fund benchmarks. Sheehy suggested that the motion be delayed until the next meeting. Motion and second were withdrawn.

F. Clarification of Policy on Advisor-Sold B-Shares – Henriksen reviewed an issue affecting a number of current B-share investors who want to make an investment change to another B-share portfolio. Wells does not feel that earlier action of the Board restricting B-share sales made it clear that this was an option, and asked for clarification. *Voight* moved, and *Wegenke* seconded a motion to allow B share investors to make a once-per-year investment change within the B-share class if desired. [*Note: Investors are also allowed to convert to another share class.]* Motion passed on a voice vote without objection.

G. Intent to Contract for Program Manager Services – Wolff reviewed for the Board the RFP process that has been underway since October. Proposals submitted have been evaluated and the process is coming closer to the end. The process will end when the DOA Bureau of Procurement issues a notice of intent to contract with the selected vendor. Then contract negotiations will begin. It would be a week to three weeks before this is completed. *Darling* thought that this could be discussed further at the next Board meeting. Closed session was not necessary at this time. The Board will be notified of the decision when it becomes public.

IX. Announcements

There were no other announcements. Board discussed holding the last Monday in January, the 30th, for the next meeting date possibly beginning at noon. *Darling* recognized Wolff and Clumpner for their service to the Board.

X. Adjournment

Cook moved, and *Reid* seconded a motion to adjourn. The motion carried by voice vote and the Board adjourned at approximately 3:35 p.m.