The Education Trust Board of New Mexico

THE HONORABLE SUSANA MARTINEZ
GOVERNOR OF NEW MEXICO

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NEW MEXICO HIGHER EDUCATION DEPARTMENT

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MARK JARMIE

EXECUTIVE DIRECTOR
THEODORE MILLER

APPROVED
Vera Lyons
Board Secretary
5/2/2019

Meeting Minutes of February 7, 2019
1121 4th Street, NW
Albuquerque, NM 87102

Board Members in Attendance
Sandra Liggett – Chair
David Jansen -- Member
Mark Jarmie -- Member

Other Individuals in Attendance
Theodore Miller -- Executive Director ETB
Vera Lyons – Board Secretary ETB
Helen Atkeson -- Hogan Lovells US LLP
Kurt Sommer – Sommer Udall
Raul Anaya – Clifton Larsen Allen, LLP
Janet Pacheco-Morton – Morton Accounting Services
Del Esparza – Esparza Advertising
Eve Wakeland – Esparza Advertising
Kay Ceserani -- Pension Consulting Alliance
Ryan Lobdell – Pension Consulting Alliance
Kathleen Beichert – OppenheimerFunds (by telephone)
Chris Werner – OppenheimerFunds
Keith Hyland – OppenheimerFunds
Heather Holliday -- OppenheimerFunds
Leslie Bednar – OppenheimerFunds
Kendra Sutton -- Court Reporter

1) **CALL TO ORDER**

Ms. Liggett called the meeting to order at 9:08 AM. The roll was called and three board members were present, Ms. Liggett, Mr. Jarmie and Mr. Jansen. A quorum existed.

2) **APPROVAL OF AGENDA**

Ms. Liggett noted the agenda as presented to the Board. She asked if there was a motion to approve the agenda. Mr. Jarmie so moved. Mr. Jansen seconded the motion. The motion was passed unanimously.

3) **APPROVAL OF MINUTES**

Ms. Liggett referenced the minutes of the meetings of the Board for October 25, 2018, November 6, 2018, November 20, 2018, December 11, 2018, December 20, 2018, January 18, 2019 and January 29, 2019. She asked for a motion to approve these minutes. Mr. Jarmie so moved that the minutes be approved. Mr. Jansen seconded the motion. The vote to approve the minutes of the meetings was unanimous.

4) **PUBLIC COMMENT**

Ms. Liggett then asked if there was any public comment. There being none, she moved to the next item on the agenda.

5) **PROGRAM MANAGER'S ACQUISITION REPORT**

Ms. Beichert opened her remarks by noting the fact that OppenheimerFunds and the Board had executed an early termination agreement. In addition OppenheimerFunds, the Board and Invesco are negotiating a post-closing agreement to cover the period after the closing of the acquisition of OppenheimerFunds by Invesco.

She briefly outlined a few of the major points in that agreement including the commitment to market the ScholarsEdge plan to broker dealers until the actual conversion to a new program manager. The agreement would also prohibit marketing of the Rhode Island 529 plan managed by Invesco to the current New Mexico account owners and also prohibit communications to the New Mexico account owners. All New Mexico plan account information would remain confidential. Finally Invesco would agree to not solicit advisors to move New Mexico plan assets to the Rhode Island 529 plan.

She also discussed the existing OppenheimerFunds legal entities that service the New Mexico 529 program. She believes that both OFIPI and OFDI will remain in existence through the closing to facilitate the continued servicing of their clients -- particularly the New Mexico 529 plans.

Ms. Beichert also mentioned the issue of Rights of Accumulation. If a customer invests in mutual funds from a specific company, the commissions on purchase of shares may be reduced based on the overall size of the client's relationship with the fund company. There will be a period of time between the acquisition and the conversion of the 529 plan during which the Rights of Accumulation may or may not be available. To make this available during that period would require sharing of account owner information with Invesco.

Ms. Atkeson noted that this was the first time that the Board had been made aware of this issue, and that it would need to be addressed in the post-closing agreement.

Ms. Beichert brought up the need to review the current selling agreements for

OppenheimerFunds with broker dealers. Some may include the sale of the 529 plans and in other cases there may be a separate 529 selling agreement.

She then turned to staffing matters. She stated that the post-acquisition company would continue to service the New Mexico 529 plans. The service will attempt to be as seamless as possible. All the duties under the contract have been reviewed and written down for marketing, operations and investments in order to inform Invesco what is required. In addition all the required output for these duties have been defined as well. The major hurdle for Invesco is that plan administration for the Rhode Island plan is handled by Ascensus as compared to the in-house administration of the New Mexico plans by OppenheimerFunds. She stated that OppenheimerFunds would seek to retain and incent key personnel to service the plans through the conversion. In the case where Invesco personnel might become involved, they would need to be trained to perform the functions and confidentiality issues would need to be addressed. There could be confidentiality issues associated with utilizing Invesco personnel and these would have to be addressed in the post-closing agreement.

Mr. Jansen asked what the effect would be on the 529 program if the current OppenheimerFunds entities servicing the program were to go out of existence. Ms. Beichert stated that it was highly unlikely that these entities would not continue. Ms. Atkeson asked Ms. Beichert when she would know if the entities would be retained. She said that it was not certain, but that these entities and some other entities would need to remain for the foreseeable future due to certain requirements regarding notice to shareholders. The post-closing agreement would need to incorporate the details with regard to the status of the legal entities.

Mr. Jarmie asked Ms. Beichert the current OFI team would stay in place through the conversion. Ms. Beichert stated that she had received confirmation that the Denver service team would remain in place through the conversion. Mr. Miller asked when the board might receive word on the retention of other positions. She expected to be able to confirm shortly that the marketing team would remain in place.

Mr. Miller then asked Ms. Holliday to update the board on the transition activity related to the current 529 recordkeeping system and the DST transfer agency system.

Ms. Holliday stated that the DST transfer agency project was still going ahead and that the handoff to the new system was expected on May 24. The Envision project was still moving forward with no major issues to date, and three mock conversions were scheduled for testing in the coming months, with the first one scheduled for the end of February.

Mr. Jarmie asked Ms. Holliday what the impact on the current 529 account holders would be. Ms. Holliday responded that they should not notice any difference after the switch to the DST transfer agency system. It should be business as usual for the account owners.

Mr. Miller asked if the conversion would be onto the Invesco version of the DST transfer agency system. Ms. Holliday confirmed that this was the case.

Mr. Jarmie asked how the account owners' information would be kept confidential from Invesco. Ms. Holliday said that the transfer agency system would be used to move money into and out of the underlying funds and for pricing of those funds, but that the account information would remain on the 529 recordkeeping system. Mr.

Jarmie asked if there was any way that the account owner information could be pilfered. Ms. Holliday said there was not.

Mr. Miller noted that there were also contractual commitments regarding confidentiality of information.

Ms. Atkeson asked if there were any implications for the later conversion of the program from the switch to the new transfer agency system. Ms. Holliday stated that she didn't see any issues in that regard. The 529 records were all contained in the current 529 recordkeeping system – not on the transfer agency system.

Mr. Miller asked if the conversion activity was a record keeper to record keeper transfer of plan information. In effect a normal conversion process. Ms. Holliday confirmed that this was the case.

6) INDEPENDENT AUDITOR'S REPORT

The next agenda item was the independent auditor's report for FY 2018. Mr. Raul Anaya, representing CliftonLarsenAllen, introduced himself to the board and noted that he was attending the meeting in the place of the usual audit partner. The usual partner, Mr. Matt Bone, was unable to attending due to travel obligations.

Mr. Anaya noted that an exit meeting had been held on October 31, 2018 with Mr. Miller and the Board Chair. The audit was then submitted to the Office of the State Auditor ahead of the November 1 deadline. The State Auditor released the audit on January 9, 2019.

Mr. Anaya observed that the firm issued an unmodified opinion, which is the highest opinion that an auditor can give. This means that the numbers contained in the financial statements are a fair and accurate representation of what occurred during the year.

He also was happy to report that there were no instances of non-compliance of control matters, and no findings to bring to the board's attention. He noted that a previous year's fin ding had been corrected during the current year.

In addition he was happy to note that the financial statements were prepared by the board staff as opposed to the audit firm. They just had to be checked for accuracy.

He also noted that the management of the board and OppenheimerFunds were very easy to work with, and this aided the completion of the audit.

Mr. Anaya then noted the conversion of the program administration fund from a general fund to an enterprise fund. This is a change is classification that better represents the nature of the fund. Mr. Sommer asked if the State Auditor had any issue with the reclassification. Mr. Anaya said that he did not.

Ms. Leggett called for a motion to accept the independent auditor's report for FY 2018. Mr. Jansen so moved. Mr. Jarmie seconded the motion. The motion passed by unanimous vote.

Mr. Jarmie then moved to commend Mr. Miller for the exceptional audit. Mr. Jansen seconded the motion. The vote to approve the motion was unanimous. Mr. Miller thanked the board both for himself and for the team that assisted him.

7) EXECUTIVE DIRECTOR'S REPORT

Ms. Liggett then asked Mr. Miller to give the Executive Director's report. Mr. Miller asked Ms. Pacheco-Morton financial report for both the trust funds and the administrative fund for the second quarter of fiscal 2019. She began with the report on the fiduciary fund.

The net position of the two funds at quarter- end was $2.25 billion. The net fair value of investments declined by $220 million. The poor stock market during the quarter was the principal reason for the decline.

She also observed that redemptions exceeded subscriptions by $81 million for the quarter. Mr. Miller observed that the program, particularly Scholar'sEdge, has been in net distribution for several years.

Mr. Jarmie observed that the fiduciary fund had declined by $216 million year over year. He asked Ms. Pacheco-Morton if that was primarily from the decline in the markets. She agreed that it was.
Ms. Pacheco-Morton then reviewed the Statement of Net Position, the Statement of Activities and the review of the Budget to Actual Report. Revenue and spending in all major budget categories were within budget for the quarter. She also reviewed revenue and spending year over year for the quarter.

Mr. Miller noted that the proposed acquisition of OppenheimerFunds by Invesco would mean that the budget as originally planned and approved was adjusted at the last board meeting by $150,000 to anticipate increased expenses associated with the RFP, contract negotiations and the conversion process to a new program manager. He told the board to expect to see an increase in expenses in the next quarter as a result of this activity.

Mr. Jarmie expressed his concern that amounts budgeted for marketing be fully and properly spent in light of the pending acquisition of OppenheimerFunds and the early termination of the program manager agreement. Mr. Miller concurred. He noted that the marketing spend tended to be somewhat lumpy as campaigns were put on and taken off. Ms. Bednar observed that the remaining spend for the year would be accounted for as part of the marketing presentation at the meeting.

Ms. Pacheco-Morton then noted that the budget to actual figures were good. Variances were generally positive with less spending than anticipated. She also observed that a budget adjustment was made to move money for temporary contract help into the outreach section of the budget. She confirmed that this type of adjustment within a single budget category is within state budget rules.

In the year over year comparison she noted that the amount expended for fee rebates in the prior year was no longer present. The board had authorized fee reductions in the program that allowed the elimination of fee rebates. The fee reductions far exceeded the value of the rebates. With that Ms. Pacheco - Morton concluded her remarks.

Mr. Miller noted how the downturn in the value of investments has a direct impact on fee revenue. Fortunately the downturn in fee revenue was mostly made up by the increase in interest income from cash in the board's administrative fund.

Mr. Miller then advised the board that the RFP for program manager services was 95% complete. He noted that the RFP would be for services for both plans. The desire is to keep the costs of the direct-sold plan low. To bid the plans separately would not have been in the best interests of the program.

He also noted that a five to seven year time frame for the contract was being considered – both as an incentive to the provider to offer better terms as well as the desire to contract for a significant period of time with a strong provider. Mr. Jarmie asked if it would be possible to ask for pricing based on a variety of time frames from five to ten years. Mr. Miller noted that he was uncomfortable with a ten year term. He thought that five years to seven years was preferable.

Mr. Miller asked Ms. Atkeson if she had any comments on the tri-party agreement under negotiation with the board, OppenheimerFunds and Invesco. She observed that the clash of exclusivity provisions between the OppenheimerFunds contract with New Mexico and the Invesco contract with Rhode Island was an important issue. The early termination agreement and the consent to assign the OppenheimerFunds advisory contract were conditioned on the execution of the tri-party agreement

Mr. Miller then went on to advise the board of the filing of legislation by Senator Romero of Bernalillo regarding the establishment of children's savings accounts in New Mexico. He noted that he attended a Senate Education Committee hearing on the bill, and that the bill was amended at the last moment to involve the state's 529 program as the investment option for the moneys. Since this bill contemplated $500 accounts for every child born in the state each year, the administrative costs would be large. He advised the Education Committee that other states with similar programs purchased special software and allocated administrative staff to run the program. The state's 529 program simply created a single omnibus account to hold all the money for each year's cohort of recipients. All the underlying account detail would be maintained by administrative staff. Under the New Mexico legislation, the state treasurer's office would administer the program. Mr. Miller noted that he assisted the sponsors of the bill in a redraft designed to accommodate these concerns.

Mr. Jarmie observed that the legislation could still run afoul of the anti-donation clause in the state constitution. Mr. Miller agreed that this was a concern that needed to be addressed.

Mr. Miller then turned the board's attention to the merger of Pension Consulting Alliance with the Meketa Investment Group. Since PCA was a registered investment advisor, the board must give consent to the assignment of the current PCA contract to Meketa. Ms. Ceserani outlined the advantages to PCA and its clients of joining a much larger consulting firm. She observed that there were no plans to have PCA personnel leave the combined firm, and support of 529 clients would continue as before.

Mr. Jansen made a motion to consent to the contract assignment. Mr. Jarmie seconded the motion, but asked Ms. Ceserani if she would remain on the New Mexico account and that the level of service would remain the same. She assured him that she would. The motion was approved by unanimous vote of the board.

8) PROGRAM MANAGER'S QUARTERLY INVESTMENT REPORT

Mr. Werner then gave the quarterly investment report. He began with the Supplemental Investment Summary. He noted continuing volatility in the markets. He noted that markets in the U.S. were down as were international equities - particularly emerging markets. Small cap indices were down over 20%. The S&P was down over 13%. International Developed markets were down more than 11% and Emerging markets over 8%. Value performed better than Growth during the quarter. Only bonds showed small gains for the quarter.

He turned to the list of largest funds in the program. He noted that the list is usually pretty static, but T. Rowe Price Blue Chip Growth Fund and the Money Market Fund moved up on the list as did some bond funds. International funds global funds moved down.

He then turned to fund performance. In TEP the index age based portfolios in line with their benchmarks net of fees.

With regard to the TEP blended portfolios, the actively managed portfolios held back performance. The Portfolios generally underperformed net of fees.

Ms. Ceserani noted that with regard to the peer groups for the underlying funds 90% of peer group funds underperformed their benchmarks. She thought this would give some perspective on the underperformance.

He then turned to Scholar'sEdge. He noted Portfolios 100 through 60 underperformed their benchmarks net of fees. Below that the Portfolios somewhat underperformed by about the amount of the fees.

The Oppenheimer International Growth Fund underperformed by almost 3.16% for the quarter. The Main Street Mid Cap Fund underperformed the benchmark by 1.6%. The Oppenheimer Developing Markets Fund underperformed by .31% The International Fund underperformed as previously noted, and the Global Focus Fund (formerly the Global Value Fund) underperformed by 3.5%. He noted that the T. Rowe Price Blue Chip Fund underperformed by .67% in Q4.

Mr. Miller referred to the full quarterly report. He noted the year over year decline in assets for both plans. This was caused by poor market performance as well as continued net distribution of assets. TEP accounts were up 4% while SE accounts were down 4.6% year over year. Mr. Miller noted the large number of older, higher value accounts in each plan, and the effect of those assets and accounts leaving both plans. He noted the need to drive account growth to compensate for this fact.

Mr. Jarmie noted that the program manager was coming to the end of a long road, but that every account that could be gained in the remainder of the term is important to the education of the citizens of New Mexico. He hoped that Oppenheimer funds would finish strong. Mr. Werner stated that he had conveyed that same message to the 529 sales team at the recent national sales meeting of the firm. **PAGE 73**

9) INVESTMENT CONSULTANT'S QUARTERLY REPORT AND WATCH LIST RECOMMENDATIONS

Ms. Liggett then asked Ms. Ceserani to give the quarterly consultant's report. She then

turned to the PCA economic and market overview report for 4Q 2018. She noted that GDP was not yet out due to the government shutdown. Inflation was slightly lower at 1.2%. Unemployment was up slightly at 3.9%, but job growth was still strong. She noted the near inversion of the yield curve as short term rates were raised and long term rates declined.

The equity markets sold off due to fears of further rate rises in 2019, but bonds rallied except for high yield.

Equity markets experienced a significant correction during the fourth quarter, both domestically and internationally. The sell-off drove many indices into the red for the year.

Ms. Ceserani then gave a brief overview of the Morningstar ratings for the various underlying funds in the 529 program. She explained the star rating and its difference from the medal rating the former being backward looking and the latter being forward looking. She noted that of the 35 funds in the program 43% are medal rated and 89% have a 3 star or better rating.

She then referenced the relative performance of the actively managed funds in the 529 program. With regard to TEP and Scholar'sEdge only 6 funds outperformed their benchmarks for the quarter. 13 funds underperformed by more than 1% under their benchmarks. In particular she noted the 12.3% underperformance of the Global Opportunities Fund. This was in comparison to the 29.2% outperformance of the fund in 2017. She noted the relatively small exposure of the program to the fund at $10 million. It is a standalone fund in SE. Mr. Werner noted that some advisors and their clients like this type of highly volatile fund. Ms. Ceserani observed that indeed the fund was up 14% in early 2019.

She then turned to the status of the funds versus the watch criteria for the program. In TEP, out of nineteen funds, eight funds were positive and seven acceptable relative to the watch criteria. In SE, out of 27 funds, nine were positive and 12 acceptable. She noted that these statistics were better than most state funds that her firm follows.

She then turned to the Watch List Memo. She noted that four funds that were on the Watch List last quarter still qualify for watch. These are the Oppenheimer Total Return Bond Fund, the Oppenheimer International Small-Mid Cap Fund. The Small-Mid Cap Fund and the Oppenheimer Capital Income Fund. She explained the reasons why each fund was on watch status and recommended that they remain on watch status. She did not recommend any other funds for watch status.

Mr. Jarmie moved that all four funds remain on the Watch List. Mr. Jansen seconded the motion. The vote to keep these funds on the Watch List was unanimous.

10) QUARTERLY MARKETING REPORT

Ms. Liggett then asked Esparza and OppenheimerFunds marketing to present the quarterly marketing report. Mr. Hylind discussed the relationship with Strategic Insight and the webinar sponsored with that firm for financial advisors. Ms. Bednar noted that there were 127 attendees. She thought this was a good number of advisors to get on line to attend a 529 webinar. The focus was on 529 education and not pushing a product.

She also mentioned the revised LinkedIn campaign. There was about a 2.7% engagement rate. The benchmark is about 1%. She noted the increase in registration for the webinar after it was promoted on LinkedIn.

Ms. Liggett asked if activity on the plan website could be matched to the LinkedIn activity. Ms. Bednar said that it could through technique known as "heartbeat ID'.

Mr. Esparza then gave an overview of telephone research in New Mexico done by Research & Polling on behalf of The Education Plan. The survey was directed at respondents 25 or older with at least one child or grandchild that they anticipated would go to college. It was a statistically significant survey or 500 respondents. $0% indicated that they were saving in some way for college. He then went on to discuss the various categories of data discovered from the survey. He noted that while Native American savings rates were low, in New Mexico the greatest savings rate was in the Hispanic population. Also it was clear that the age at which savings began was younger than had been expected.

He also noted that most savings was deposited in banks. Mr. Jarmie asked if this was because the savings were also an emergency fund for other needs. Mr. Esparza agreed. He noted that many save with CDs, which are not as liquid for emergencies. These people might be a target for 529 advertising.

He noted that 4 out of 10 respondents were aware of TEP as a 529 college savings plan. This is a high percentage compared to the national averages. He also noted that the burden of student debt was a big concern for the respondents. This is in line with many of our current advertising initiatives. Mr. Jarmie remarked on the value of this type of consumer research.

Ms. Liggett asked if any research was done on the employer channel. Mr. Esparza said that this research did not include that. But future research would. Mr. Miller noted that nationally employer deduction has been difficult to implement. It is perceived by HR departments as conflicting with the importance of core company benefits such as retirement. Also the accounting arms of the firms don't want the perceived extra work. Finally, some firms are under the misimpression that the 529 plan would carry fiduciary liability for the company and require some form of government reporting.

Mr. Hylind mentioned that the plan does offer an AIP or auto investment plan. This allows the employee to save regularly through her or her own bank account. If many people are saving at banks for college, then perhaps some of them could be convinced to send some of that money the 529 plan.

Ms. Wakeland then reviewed the new TEP marketing front end website. Since the launch there has been a 26% increase in consumer traffic to the site. Site traffic is aligned with the top 10 states that are targeted by TEP. She then overviewed further enhancements to the site that were designed to simply the investment decision making process.

Mr. Sommer asked if the new design would expose the board to any increased liability regarding investment. Mr. Hylind noted that Oppenheimer would review the site for compliance to regulatory guidelines. Mr. Miller noted that all site materials are subject to FINRA review and approval.

Mr. Miller noted that the marketing front end website is responsive for mobile devices and tablets, but the transactional site is not. One aspect of the new program manager's service would be to provide a responsive transactional site.

Ms. Bednar then reviewed the marketing budget. She noted the spending so far in the year as well as the remaining budget available. She noted that rollover dollars from previous years have increased the available amount. She noted that expense will be associated with the revisions necessary to address the acquisition of Oppenheimer by Invesco.

11) STRATEGIC ASSET ALLOCATION PROJECT

After a break, the meeting resumed with an update on the Strategic Asset Allocation project. Mr. Miller reminded the board that it has adopted a Statement of Investment Beliefs that will be used to inform the content of the Investment Policy Statement and ultimately the design of the portfolio options for the plans. He reviewed the concept of strategic asset allocation and the concept of economic risk that is at its core. He noted that the project had stalled because of the acquisition of Oppenheimer. However, one aspect of the project still under review is the creation of Enrollment Date Portfolios as opposed to the current Age Based Portfolios.

Ms. Ceserani and Mr. Lobdell then went into more detail on the creation of the glidepaths for such portfolios and why the enrollment date model provided for smoother glidepaths versus age based models.

Ms. Ceserani noted that the traditional age based design still dominates among state plans. Fourteen states have adopted enrollment date designs. Mr. Miller noted that there operational and cost advantages associated with enrollment date portfolios. Fewer CUSIPS need to be registered and maintained. The portfolios are less expensive to implement on omnibus platforms with brokers.

Ms. Ceserani noted that while enrollment date funds have benefits, there are also a couple of negatives. Investors are accustomed to age based portfolios, so some education will be needed. Also performance history will be lost when the new portfolios are introduced. Mr. Jarmie asked what Morningstar thinks of enrollment date models. Ms. Ceserani noted that Morningstar likes them quite a bit. He also asked if medal ratings were assigned to these models. She said that they were.

Mr. Lobdell then reviewed some risk mitigation strategies that are used for investment portfolios including the trend following strategies and the used of long dated treasuries. Mr. Jansen asked if these strategies would be an overly on the existing portfolios or separate investments. Mr. Lobdell considered them as separated investments to be added to or reduced within the enrollment date portfolios as the need arose.

He then went into the reasoning behind why such strategies work to reduce risk, as well as the pros and cons of such strategies. They don't always work for all market conditions. He then showed what the benefit could be to the performance of the glidepath models.

12) ADJOURNMENT

At this point Mr. Jansen made a motion to adjourn. Mr. Jansen seconded the motion. The motion to adjourn was unanimously approved. The meeting adjourned at 1:13 PM.