# The Education Trust Board of New Mexico



Approved 10/7/21
Vera Lyons
Board Secretary

**Meeting Minutes of**
**August 5, 2021**
**1516 Paseo de Peralta**
**Santa Fe, New Mexico 87501**

**Board Members (all remote)**
Sandra Liggett, Chair
Robert Desiderio, Vice-Chair
Dr. Jose Garcia, Member
Lawton Davis, Member

**ETB Staff (all remote)**
Carolyn Fittipaldi, Acting Executive Director
Vera Lyons, Board Secretary

**HoganLovells (remote)**
Helen Atkeson, Partner

**SommerUdall (remote)**
Kurt Sommer, Partner

**Ascensus (all remote)**
Tom Hewitt, VP Relationship Management
Tom Lowe, VP Investment Management

**Principal (all remote)**
Paul Schieber, Managing Director, 529 Distribution
Randy Welch, Managing Director, Portfolio Manager
James Fennessey, Portfolio Manager, Director of Research
Tracy Bollin, Managing Director – Fund Operations
Jori Horn, 529 Marketing Director
Tim Hill, Executive Director US Client Group

**Meketa (all remote)**
Kay Ceserani, Managing Director
Eric White, Principal
Nick Buckley, Associate Investment Analyst
Heather Bedont, Senior Performance Analyst

**Morton Accounting Services (remote)**
Janet Pacheco-Morton, Partner

**Sunny 505(remote)**
Jerry Matthews, Senior Account Manager

**1) CALL TO ORDER**

The meeting was called to order at 8:30 AM. There was a quorum and four board members were present.

**2) APPROVAL OF AGENDA**

Chairman Liggett called for a motion to approve the agenda. Dr. Davis so moved. Dr. Garcia seconded the motion. The vote to approve the motion was unanimous.

**3) APPROVAL OF MINUTES**

Chairman Liggett called for a motion to approve four sets of minutes. Chairman Liggett mentioned one revision to make to minutes from 5/27. Chairman Liggett motioned to approve the other three minutes. Mr. Davis so moved. Dr. Garcia seconded the motion. The vote to approve the motion was unanimous. Chairman Liggett pointed out that Dr. Garcia was not in attendance at the 5/27 meeting as noted on the minutes and asked to remove Dr. Garcia as being present at the meeting. Chairman Liggett called for a motion to approve minutes from 5/27 with that change. Mr. Davis so moved. Dr. Garcia seconded the motion. The vote to approve the motion was unanimous.

**4) PUBLIC COMMENT**

Chairman Liggett then called for any public comment. There being none, she moved to the next item.

**5) EXECUTIVE DIRECTOR'S REPORT**

Ms. Fittipaldi announced there are 237 new accounts for TEP for July which is 10 better than last year.

**a) Principal Life Insurance** – Ms. Fittipaldi pointed out that Principal, at ETB's request, has responded to a request for information prepared by Meketa in regards to Principal's announcement that they will discontinue certain life insurance products. She noted a copy of the RFI was sent to the board. She introduced Tim Hill, executive director for US Client Group at Principal to discuss with the board.

Mr. Hill thanked Ascensus and Meketa for the partnership and expressed his enthusiasm and focus on delivering commitments to the board. He noted that Principal did a strategic review of all the business they are involved in to make sure that they are aligned with where the best growth opportunities are. He pointed out the biggest decision was to move away from the retail fixed annuity business and the retail life insurance and focus efforts on asset management and small/medium sized businesses. He noted that Principal continues to achieve some of the highest ratings in the industry with regards to where capital sits. He asked if there were any questions. He asked Paul Schieber to give a quick status.

Mr. Schieber pointed out that from a distribution perspective, none of the strategic announcements change any of the key critical drivers that have been laid out to date for Scholar's Edge. He mentioned that activation of the Principal Financial Network and a focus on pairing 529 payroll with retirement plans is a strategy in the platform where SE can be competitive. Mr. Schieber asked Mr. Hill to elaborate on PFN and capital preservation.

Mr. Hill pointed out that PFN is Principal's own broker/dealer with 1,100 advisors in the network. He noted that moving away from retail life allows the advisors to focus on asset management and talking with clients about 529 plans and the impact of saving for college as well as estate planning opportunities. He mentioned that there have been no departures from PFN as a result of the change and that he felt the change would strengthen the network. He noted that it's business as usual. He pointed out that from a capital preservation perspective, there is no direct impact with regards to the general account. He reiterated the partnership with Ascensus and Meketa is strong. He confirmed that if there are any changes that would impact Scholar's Edge, Principal will provide an update at that point in time. He asked if there were any questions.

Mr. Davis commented that his experience with insurance companies through his business in the past indicates this is a very positive move for investors in the program and he said he was happy to see this happening.

Mr. Hill agreed that it is a positive step that will give Principal additional opportunities for investment options and he said he believes it will strengthen the Principal distribution team or anyone involved with SE. He pointed out that it's going to put dollars back into the organization.

Chairman Liggett acknowledged that Vice Chair Desiderio joined the meeting. She asked if there were any other questions.

Ms. Fittipaldi introduced Ms. Atkeson and Ms. Ceserani to summarize and address the response to the RFI. Ms. Atkeson stated that Mr. Miller and Ms. Fittipaldi were briefed after the announcement and there was discussion about what issues needed to be considered. She noted that when the new investments in this plan were first set up, the board approved the funding agreement as one of those investments different than all the other mutual funds that make up the different investment option portfolios. The funding agreement, which is with the Principal Insurance Company, is a different type of an investment and for that reason Meketa reports quarterly about the Principal Insurance Company. She pointed out those monies go to that company and are allowed to be used by the company however they want. She noted that when ETB wants the money back or account owners want to withdraw those funds, they are available as long as there is money in the general account of the company. She also noted there is no security or separate account where those funds are held. It's an unsecure investment and different than monies that go into a mutual fund and are invested there and held separately. She pointed out that SE has $318 million invested in this single funding agreement. She added that due diligence and review of the structural changes to that company were necessary as soon as ETB heard of the changes so Meketa sent out the RFI. She pointed out the two general focuses in the RFI, that Mr. Hill and Mr. Schieber gave some responses to, are what's the impact on the funding agreement itself and what's the impact on the insurance company and its general account. She stated ETB needs to feel as though this is still a prudent investment and the distribution efforts are not negatively impacted. She noted that there is still more to learn and ETB staff has made it clear that it wants to be kept in the loop as more information becomes available and will keep the board informed. She asked if there were any questions.

Chairman Liggett asked Ms. Ceserani if she had anything to add. Ms. Ceserani added, we also agree with Mr. Davis that from a business level that would be a smart decision. She also reinforced what Ms. Atkeson said about monitoring the general account if monies leave that portfolio. She confirmed that Meketa will continue to monitor the portfolio as is done on a quarterly basis and will keep the board posted on any potential implications to plan participants and any other updates as they become available.

Ms. Fittipaldi asked Mr. Hill if Principal is committed to providing ETB with additional details as soon as they are available and what the timeline is for additional information. Mr. Hill confirmed that Principal is committed to providing information as soon as it's publicly available while there isn't an exact timeline. Mr. Hill pointed out that on the last Principal quarterly earnings call, Dan Houston, CEO and Deanna Strable, CFO talked about active negotiations with the two business units and they are looking to sell them together versus separate and that would speed up the process.

b) **FY2021 Q4 Financial Report** - Chairman Liggett asked Ms. Pacheco-Morton to give the quarterly financial report. She first reviewed the administrative fund ending June 30, 2021. She pointed out that the operating fund has $11.1 million in total assets offset by $222,000 of total liabilities consisting mostly of accounts payable that are expenses that were incurred through June 30th, but not paid until July. She explained that the accrued expenses and compensated absences for staff leaves ETB with $10.9 million in net position. She noted total program revenue of $1.9 million; marketing grassroots revenue of $927,000 from the contract with Ascensus. Total expenses of $2.7 million at year-end with operating income of $58,000. She pointed out that investment net of associated fees was $17,000 which resulted in an increase in net position of almost $76,000 at year-end and a total of $10.9 million in equity. She noted that all expenses were in line with or under budget. Program fees were slightly better than expected and investment earnings were significantly lower than expected. She reviewed detail by category. All expenses are within budget for contractual services. There was a budget adjustment between marketing assistant and outreach research and PR category of $45,000. Ms. Fittipaldi pointed out that the adjustment was for the edBridge contract which is for the scholarship program being implemented. Ms. Pacheco-Morton noted all other expenses were under budget with one budget adjustment in the travel and miscellaneous category. $4,000 was moved from travel to miscellaneous to cover expenditures consisting of additional printing and postage costs. There was an increase in program fees of $102,000 year over year. Investment earnings were lower than prior year. She pointed out the marketing grassroots in prior year there were two contracts in place with marketing dollars from Ascensus and Invesco. This year only Ascensus contract was in place. She pointed out the prior year had slightly higher expenditures by $71,000. The budget was cut this year due to Covid situation and that's what accounts for the difference. There was an increase in personnel services by $37,000 due to having a full-time marketing director in place for full year compared to shorter period of time in prior year.

Ms. Pacheco-Morton reviewed the fiduciary funds. She noted total assets of $2.7 billion at year-end. Both funds had a positive change in net position mostly due to increase in the fair value of investments due to market conditions offset by the net redemptions for the year. She pointed out that last year there was a net loss of $54.5 million and this year there is a $275 million increase in net position primarily due to increase in fair value of investments. This resulted in an increase of net position from $2.4 million in the prior year to $2.7 billion in the current year. She asked if there were any questions

Chairman Liggett called for a motion to accept the financial report. Mr. Davis so moved. Dr. Garcia seconded the motion. The vote to approve the motion was unanimous.

**6) PROGRAM MANAGER'S QUARTERLY OPERATIONS AND INVESTMENT REPORTS**

Mr. Hewitt reviewed the Program Manager's Quarterly Operations and Investment Reports. He noted that overall, both plans have a positive story relative to Q2 last year.

For SE, the number of total accounts is down quarter to quarter. He pointed out that most are expected withdrawals and account closures due to the aging of the beneficiary base. From an assets point of view, SE is up 9% relative to last year with $54 million in market earnings. He noted that when you look at the overall size of the plan and what's happening with market earnings relative to new cash flow, SE is just over $2 billion. He pointed out the as the beneficiary base is aging over time and accounts are closing, the number of closures will continue to increase until additional new accounts are added at the lower beneficiary age. New accounts are needed to rejuvenate that base. He noted that there is a 30% increase in new accounts year-over-year. He pointed out that a new rollover strategy was implemented in Q4 2020 to increase the amount of assets brought to SE from other plans and there was an immediate spike in assets that continues to trend up. In terms of net cash flow, SE is negative $25 million this year versus $30 million last year. He noted the difference was likely due to a very large spike in rollovers out this time last year that didn't occur this year. He also noted that total contributions are trending up since this time last year. He pointed out that the total lifetime gift contributions from the Ascensus gifting programs is $2 billion and for SE there has been $600,000 in gift contributions YTD. He noted TEP has had $1.5 million in gifting contributions YTD. He asked if there were any questions.

For TEP, accounts are up almost 7% versus this time last year. Assets are up about 18% and market earnings are almost $13 million. He pointed out the beneficiary age for TEP is slightly lower than SE at about 15 and that downward trend could be from the increase in new accounts. The goal for both plans is to see that trend downward. He pointed out new accounts for TEP are up about 25% with about 1,930 new accounts YTD and cash flow is up significantly. This time last year, it was a positive cash flow through the first two quarters at about $1.8 million and this year to date $7.3 million in positive cash flow. He pointed out in Q1 there was a big spike in rollovers in to TEP by one large family bringing over 12 accounts with large rollover amounts. He asked if there were any questions.

Mr. Lowe gave the investment update for TEP. He pointed out the YOY plan growth was about 18% driven by market growth and also cash flow. That same number quarter over quarter is about 5%. As a market overview, Q2 was a strong market in the US with equities up over 8% and close to 6% non-US equities and within the US, growth stocks returned to favor after value stocks dominated during the first quarter. He pointed out that a significant drop in interest rates tends to help growth stocks which are value based and bonds overall returned about 2%. In this declining rate environment, longer bonds outperformed shorter bonds. He pointed that overall, it was a good quarter and the different asset classes acted as expected over a long investment horizon, equities greater than bonds. 60% of TEP assets are in the passive year of enrollment portfolios which are the best low-cost options for direct investors and these portfolios performed in line with their benchmark in a quarter where equities outperformed bonds. The percentiles for these portfolios were 41 percentiles for the one quarter and 40 percent for the year, which is where the passive portfolios should be consistently to do as they are designed. The passive asset allocation portfolios don't change allocation over time and these portfolios performed in line with the indices as designed.

He noted that the active asset allocation portfolios were roughly in line with benchmarks for the quarter but still showing very strong performance over the trailing one-year. Most of these portfolios, net of expenses, around 200 basis points over the benchmark for the one-year period which is quite strong. He noted the DFA international funds were from 400 to 600 basis points over their benchmark for the year. The US equity product for American Funds is showing a little weaker one-year performance but overall, the active portfolios are performing strongly.

He pointed out that two underlying fund products, iShares International Aggregate Bond ETF and the DFA Inflation Protected Fund, were both upgraded by Morningstar. This means all the funds in TEP are now metal rated by Morningstar. He asked if there were any questions.

Mr. Welch reviewed the performance of the SE portfolios. He noted that most assets were in a positive territory and the riskier the assets, the more prevalent they were in fixed income, as high yield did well. TIPS did well and overall, the markets were quite positive across just about any asset class. All 11 vintages outperformed their benchmarks for the quarter and the one-year numbers all positive for all vintages as well. He noted that returns are mostly positive since inception with 7 of 13 outperforming their indexes.

Mr. Welch noted that the static portfolios also had a good quarter. All four outperformed their benchmarks on a quarter basis as well as on a one-year basis.

He pointed out peer rankings for the quarter with SE at an overall rank of 37th. He noted that the way SE has sloped the glide path in relationship to the investor's time line going to college means that the investments are much more conservative than the peers by design. He pointed out that the capital preservation and minimizing volatility is more important as these investors are looking to tap into their savings. He pointed out that in the middle of the curve SE is more aggressive, taking greater capital market risk which was rewarded in the quarter.

He reviewed the underlying funds and noted there was a nice bounce-back in active management. Core Fixed Income strategy by Principal outperformed its benchmark ranking in the 37th percentile. US Equity had a strong quarter and outperformed the benchmark by 400 basis points, ranking in the second percentile. Equity Income Strategy bounced back versus the benchmark and peers after a struggle in first quarter.

He noted the Vanguard Index performed well versus the S&P 400. He also noted a bounce-back from JP Morgan in the emerging markets in the second quarter and it outperformed. He pointed out that Diversified International was the only disappointment as they lagged the benchmark and ranked in the fourth quartile. He noted that July was a very strong month for Diversified, they outperformed the benchmark by 100 basis points. The July number moved them YTD positive against the benchmark.

Mr. Fennessey reviewed the qualitative and quantitative assessments of the SE funds prepared by the Principal manager research team. He noted that all funds are looking good and in favorable status with the exception of International Small Cap. It was placed on Principal's quantitative watch list effective March 31st because of underperformance over the last 18 months. This portfolio helps stocks that were hurt by the pandemic and they have lagged a bit in the upturn. This investment option has improved in 3rd quarter relative to peers and index. The lead portfolio manager has been managing this portfolio for over 20 years. Principal manager research team is closely monitoring this portfolio. He reiterated that it is not used in the year of enrollment or the static allocation portfolios. It is only used as a stand-alone option to advisors or investors who want exposure to the small cap market overseas. He asked if there were any questions.

7) **INVESTMENT CONSULTANT'S QUARTERLY REPORT AND WATCH LIST RECOMMENDATIONS**

Ms. Ceserani gave the investment consultant's report and watch list recommendation. She highlighted the index return and noted that the one-year numbers are amazing with US equities ranging from 40 to 73% and that trickles down into the non-us as well. She pointed out a great quarter and one-year. She went over the equity allocations in the two glide paths for each age band and how the portfolios did on a risk-adjusted basis versus their benchmarks. She discussed the passive versus active funds for TEP and SE. She noted for TEP that all of them had positive returns and only one underperformed by more than 1% (American Fund). She noted for SE all of them were positive and only one fund returned 1% below the benchmark (Principal Diversified Fund). She pointed out the detail on each of the funds that are outside the window plus or minus 1%. She noted that Meketa reviews each of the funds using the criteria outlined in the monitoring procedures for the program and highlighted the summary of their review. Most of the funds are either in the positive or acceptable for both programs. Only one fund for each program continues to qualify for watch. American Fund Fundamental Investors in the TEP portfolio has $58 million and the Principal International Small Cap in SE has $5.2 million. Neither of the funds are used in the overall portfolios which is where most of the assets are. She pointed out that American Funds has been on the list for 9 months and the Principal International for 6 months. She noted there is no change to the watch list for this quarter so no recommendation for any funds to come on or off. She said they will continue to monitor these as time goes on. She pointed out there were no portfolio manager changes for any of the funds in the program. She concluded the review and stated there is no change to the watch list.
Ms. Fittipaldi pointed out that a vote to accept the watch list recommendation was needed.

Chairman Liggett asked why a fund remains on the watch list for 12- 18 months before it is moved off the watch list. Ms. Ceserani explained that it is expensive to make changes and that when a fund is on watch, it's really due to some biases that are in the fund itself by the way it's constructed. No fund is going to always outperform and they go through cycles. The time period is built in to allow for that. She pointed out that it isn't uncommon for a fund to stay on the watch list for longer so it can continue to be monitored. The funds need room to correct themselves and roll through an investment cycle.

Dr. Garcia asked how the overall performance of SE and TEP compared to other 529 plans. Ms. Ceserani pointed out that for other states there might be a third of the funds in the positive, a third in the acceptable and a third on caution or watch. From that standpoint the New Mexico plan looks very good. There are only a couple funds that are in caution or watch. She pointed out that portfolios are evaluated versus Morningstar medians and shown on a risk-adjusted basis. TEP has been doing really well over this last one-year period from a risk-adjusted basis versus peers. SE has been doing really well from and underlying fund perspective as well as a peer comparison versus the median.

Dr. Garcia asked what the level of concern about New Mexico products is and Ms. Ceserani said the level of concern is very low. She pointed out that the results were very good during the annual review process. The asset allocation structure for the glide paths was reviewed for both plans and future expectations based on market expectations were looked at. She pointed out that expected returns in the future are strong and they should beat the tuition inflation.

Chairman Liggett called for a motion to accept the investment report and recommendations of Meketa. Mr. Davis so moved. Dr. Garcia seconded the motion. Ms. Fittipaldi pointed out the watch list needs to be accepted. Chairman Liggett amended the motion to accept the watch list recommendations. The vote to approve the motion was unanimous.

Chairman Liggett moved to the next agenda item - the investment policy. Ms. Fittipaldi pointed out that this is something that was discussed during the RFP process for the investment consultant. ETB wants the investment consultant to take a more active role in reviewing and making investment recommendations. She pointed out language was added on page 6 to enhance the role of the investment consultant, as outlined in the new contract. Ms. Ceserani noted that the investment policy and the monitoring procedures get updated formally on an annual basis and then ad hoc as things change. Ms. Ceserani went over the investment policy and pointed out that a lot of thought was put into the way it was structured. The monitoring procedures document outlines how the investment consultant reviews and monitors the program and goes through the steps and all the criteria. It's important to make sure the investment consultant is doing what they are supposed to be doing. She pointed out that the policy is reviewed annually to see what's changed and the monitoring procedures are updated more frequently given the structure of the portfolio. Ms. Atkeson added that everyone worked together on the policy and that it is integral to the relationships with the program manager and plan managers and central to their contracts and is a baseline that is referenced numerous times for them to carry out their responsibilities. It is a key document that the board is responsible for presenting and they are responsible for complying and following it in their services. Chairman Liggett agreed that this is a very important part of how this board meets its fiduciary obligations to oversee and manage the investments as well as the consultants to hold them accountable for the performance. Chairman Liggett asked if anybody had any concerns with the document. Not hearing any, she called for a motion to approve the New Mexico Education Trust Board Monitoring Procedures and Criteria for The Education Plan Trust New Mexico. Mr. Davis so moved. Dr. Garcia seconded the motion. The vote to approve the motion was unanimously approved.

**8) Hiring Committee Report**

Chairman Liggett moved to the next agenda item – the hiring committee report. Vice Chair Desiderio gave an update on the hiring of the executive director. He pointed out that EFL is the search firm and the contact is Dan Cummings. Dan has sent two requests to the board. One is to have telephone interviews with each board member. The other is to review the draft position specification document and provide input. He pointed out that Dan Cummings is waiting for responses from each board member to proceed and that until this document is sent out, there isn't any movement in the process. There are no applicants yet because there has not been any solicitation of applicants. He asked each board member to contact Dan Cummings and provide input to move the process forward. Chairman Liggett asked if the comments on the job description should be sent to everyone including Dan Cummings and Vice Chair Desiderio replied yes. Vice Chair Desiderio stated that he told Dan Cummings that he wanted to have the largest pool that meets minimum qualifications. He said that Dan will keep him updated on the process.

Chairman Liggett asked if there were any other questions. Mr. Davis had a comment. Mr. Davis pointed out a concern he had when he made a withdrawal from his account to pay his granddaughter's tuition. He said he tried to deposit the money into an account and the bank held the money for 14 days. He said he thought he should bring the matter to the board to consider adding language to plan documents that says " National banks may hold funds for 14 days upon withdrawal". Chairman Liggett suggested to ask Ms. Fittipaldi to look at the issue. Ms. Fittipaldi said she would talk with Ascensus and get some answers and get back to Mr. Davis. Chairman Liggett asked Ms. Fittipaldi to communicate with the whole board with any information about this.

Ms. Fittipaldi announced the next board meeting is Thursday, October 7th at 8:30 and the marketing reports will be at that meeting.

Mr. Davis thanked the consultants and everyone at the meeting for doing their part to get the information to the board and respecting the requests for brevity. Chairman Liggett agreed and pointed out it was a good meeting and the information was excellent.

**9) ADJOURNMENT**

Ms. Liggett called for a motion to adjourn. Mr. Davis so moved. Dr. Garcia seconded the motion. The vote to approve the motion was unanimous. The meeting adjourned at 10:11 AM.