MINUTES OF THE MEETING OF THE BOARD MEMBERS

January 16, 2007

Andrew M. Saul, Chairman of the Federal Retirement Thrift Investment Board, convened a meeting of the Board members on January 16, 2007, at 9:00 a.m., Eastern Standard Time. The meeting was open to the public at the Board's offices at 1250 H Street, N.W., Washington, D.C. In attendance were Thomas A. Fink of Alaska, member; Gordon J. Whiting of New York, member (by telephone); Alejandro M. Sanchez of Florida, member; Gary A. Amelio, Executive Director; Thomas K. Emswiler, Secretary and General Counsel; Mark A. Hagerty, Chief Information Officer; Gregory T. Long, Director of Product Development; Pamela-Jeanne Moran, Director, Participant Services; James B. Petrick, Chief Financial Officer; Tracey A. Ray, Chief Investment Officer; and Thomas J. Trabucco, Director, External Affairs.

1. Approval of the minutes of the December 18, 2006 Board member meeting.

Chairman Saul entertained a motion for approval of the minutes of the December 18, 2006 Board member meeting. The following motion was made, seconded, and adopted without objection:

MOTION: That the minutes of the Board member meeting held on December 18, 2006, be approved.

2. Thrift Savings Plan activity report by the Executive Director.

a. Monthly Participation Activity.

Mr. Long reviewed the report on TSP statistics. See "Thrift Savings Fund Statistics" (attached). He noted that the plan was over the $206 billion mark, that the number of FERS participants decreased slightly, and that participation by CSRS employees continues to decline as members of this group retire. TSP participation by members of the uniformed services declined slightly, most likely due to members switching from the reserve to active components.
Mr. Sanchez remarked that the Navy’s high participation rate demonstrates that it is effectively promoting the TSP. Ms. Moran noted that the Air Force has expressed greater interest in its participation rate. Mr. Trabucco said that the Navy has always been the most interested regarding the TSP.

Mr. Amelio commented that the most important numbers are in the fund balances. The plan has been growing exponentially and investments in the G Fund have decreased a percent a month (from 50 to 35). Most of this money has shifted to the L Funds. The Agency has done an outstanding job in educating participants.


Ms. Ray noted that the fixed income fund had an unusually high tracking error of 5 basis points due to a litigation payment for WorldCom bonds. The S Fund underperformed by 13 basis points, but, for the year, outperformed by one basis point. The I Fund outperformed by 9 basis points, primarily due to taxes. Trading costs for the F, C, S, and I Funds remain relatively low for the year. Trading costs for the I Fund were 19 basis points for the month, eleven for the year, principally because the international markets are not open at the same time as domestic markets.

For the year, the I Fund is up 26 percent, the C Fund is up 15.79 percent, and the S Fund is up 15.3 percent. The G Fund is 48 basis points less than the 3 month T-bill. Chairman Saul remarked that these rates of return are exceptional and that we must advise participants that past performance is no indicator of future performance. This performance is a tribute to the U.S. economy. Mr. Sanchez remarked that the TSP’s size leads even small increases in the market to cause significant growth in the TSP. Chairman Saul noted that the participants owe a lot to the Agency’s senior staff and employees for successfully managing this growth while simultaneously enhancing the TSP. Mr. Sanchez remarked that the Life cycle funds were an especially significant improvement and that everyone he talks to about them likes them.
Ms. Ray noted that the L Funds all showed double digit growth for the year with the exception of the income fund. From inception to date, each L Fund has outperformed the G and F Funds. L Fund balances increased to 9 percent from 8 percent for FERS participants, to 8 percent from 7 percent for CSRS participants, and to 11 percent from 10 percent for uniformed service participants. Nine percent of CSRS participants have amounts in the L Funds, twelve percent of FERS participants have amounts in the L Funds, and fourteen percent of uniformed service participants have amounts in the L Funds.

c. Legislative Report.

Mr. Trabucco reported that Congress has not yet held its organizational meeting. With the Democrats taking the majority, a Democrat will now chair all committees and subcommittees and a Republican will be the ranking member. He expects that the number of House subcommittees on the House Committee on Oversight and Government Reform will be reduced from seven to five. The number of subcommittees on the Senate Homeland Security committee will likely be increased by one.

Mr. Sanchez asked whether Mr. Trabucco had learned anything about legislative priorities. He was told that they hadn't gotten to that level yet as they were focusing on their priorities for the first 100 hours of legislative sessions.

3. Quarterly Reports.

a. Investment Policy.

Ms. Ray reported that Barclays had not changed its proxy voting policy and that its proxy votes were in line with policy. After this discussion, the members made, seconded, and adopted the following resolution by unanimous vote:

RESOLUTION

WHEREAS the Federal Employees' Retirement System Act of 1986, as amended (5 U.S.C. § 8401 et seq.) provides that the Board members shall establish policies for the investment and management of the Thrift Savings Fund (5 U.S.C. § 8472(f)(1) and (2)); and
WHEREAS the Board members at this meeting have reviewed the investment performance and investment policies of the Government Securities Investment Fund, the Fixed Income Index Investment Fund, the Common Stock Index Investment Fund, the Small Capitalization Stock Index Investment Fund, and the International Stock Index Investment Fund; and

WHEREAS the Board members are satisfied with the investment performance and investment policies of these Funds;

NOW THEREFORE BE IT RESOLVED that the current investment policies for the Government Securities Investment Fund, the Fixed Income Index Investment Fund, the Common Stock Index Investment Fund, the Small Capitalization Stock Index Investment Fund, and the International Stock Index Investment Fund are affirmed without change.

b. Quarterly Vendor Review.


SI International continued its strong financial performance and growth through acquisition and new government contracts. We have no concerns regarding SI International.

Spherix International's third quarter numbers are somewhat improved. InfoSpherix remains strong; BioSpherix's expenses are a small drag on its financials. It has significant government contracts. We have no cause for additional concern and will continue to monitor it. Mr. Amelio noted that they had done due diligence visits and that its staff appeared very strong.

Barclays has had no significant new developments. However, they only report twice per year. There have been no further reports that have come to his attention regarding a possible takeover of Barclays. Mr. Amelio noted that a due diligence visit to Barclays is scheduled for April.

Mr. Petrick noted that he had reported on the Agency's due diligence visit to Switch and Data at the November
Board meeting. Since than, officials from SI International have also done a due diligence visit. We agree with their conclusion that Switch and Data is thinly capitalized and that its initial public offering has the potential to significantly improve its financial situation. We have been pleased with their performance and have learned that their leases have been recently renewed.

RR Donnelly has very strong financials and has made aggressive acquisitions. We have no concerns regarding RR Donnelly.

MetLife will be added to the quarterly review of vendors in April.

Mr. Fink noted that service providers like SI, Spherix, and Switch and Data do not have strong financial statements. He asked whether it would make it more difficult to find a responsive bidder if we paid more attention to financial statements when we evaluate proposals. Mr. Petrick disagreed regarding SI's financial statement but noted that the Agency does evaluate and consider financial status when it evaluates proposals. Mr. Hagerty added that the next time we draft a request for proposals we will use an acquisition specialist to ensure that only offerors who are strong financially can make a competitive proposal. Mr. Fink noted that most of SI's capital is represented by goodwill. He added that he preferred to use firms with strong depth of capital such as Barclays and MetLife. Mr. Amelio noted that SI is the fourth largest provider of information services to the Federal government. Mr. Sanchez remarked that the Agency still must monitor these vendors closely because goodwill is a significant part of their total assets.

Mr. Amelio reported that the Agency had significantly strengthened its oversight of its vendors. The Contracting Officer's Technical Representative and Agency staff are in almost daily contact with the vendors. He and other senior managers make due diligence visits to each vendor at least once per year. These visits would allow us to identify any problems, for example, insufficient staff or disorder, but all vendors have maintained meticulous facilities and possess strong staffs. These visits reassure us regarding the status of these vendors.

Mr. Amelio noted that the Agency has also initiated these quarterly vendor reviews and Mr. Petrick and his staff have significantly improved them since becoming responsible for them. Mr. Petrick added that the Board members, Mr.
Fink in particular, each ask probing questions that lead to greater oversight of these vendors.

   a. Participant Survey.

   Mr. Long reported that Watson Wyatt performed as required and that he is pleased with the report. The report shows that the participants are very satisfied with the TSP and that they show an inclination to move toward the L Funds. He highlighted the following areas:

   • The median contribution rate of 10 percent is significantly higher than the private sector rate of 7 percent.

   Mr. Saul asked if that meant that if someone was earning $100,000 they would be contributing $10,000 and was told that was correct. When he considered matching, he noted that this was a significant contribution. He then asked whether the survey sample was large enough to rely on these responses. He was told that we have a 95 percent confidence that these answers are correct with a margin of error of two percent.

   • Eleven percent of uniformed service participants contribute 20 percent of pay or higher.

   Mr. Sanchez asked whether members of the uniformed services also had a pension and was told that they have a pension that vests after twenty years service. He was also told that FERS and CSRS participants have pensions, but that the TSP is a larger piece of the retirement package for FERS participants. New Federal employees are not eligible to participate in the CSRS retirement system. There are, however, still approximately 400,000 CSRS participants.

   • Eighty-five percent of participants report being satisfied with the TSP and only three percent report not being satisfied with the TSP.

   • Most participants obtain information about the TSP via the Web. Fewer than five percent obtain information via the ThriftLine, with CSRS participants being the group most likely to use the ThriftLine.

   Mr. Sanchez asked how this compared to a few years ago and was told that we don't have that data. Ms. Moran
noted that approximately two million participants used the ThriftLine last year and spoke with a participant service representative. The numbers are similar this year.

- Sixty percent viewed favorably auto-enrollment for new employees whereas twenty percent did not.

- Fifty percent of respondents preferred to have the L Funds as the default option; twenty-six percent preferred the G Fund.

Mr. Amelio remarked that these facts are supportive of the Agency's plan to recommend to the Board to seek legislation for auto-enrollment and making the L Funds the default option.

Mr. Fink asked whether all respondents had a TSP account and was told that they did. He then asked whether the majority of respondents were making contributions to the TSP and responding that they believed all other Federal employees should be doing so also. He was told that this was correct. The Agency plans to survey those participants with accounts that receive only Agency Automatic (1%) Contributions and will report on their responses at a future Board meeting. Future surveys will also focus on particular groups of TSP participants by age, sex, and retirement system.

Mr. Sanchez asked whether this was the first time the Agency had conducted a survey. He was told that the Agency had previously conducted a survey in 1991. We had hoped to survey before now, but adding the S and I funds and implementing the new recordkeeping system became higher priorities. Mr. Sanchez stated that it is important that we continue to survey in order to ensure that we are providing the highest quality service.

Mr. Fink noted that one response showed that 21.3 percent of respondents felt they did not have enough money to participate yet 86 percent actually contribute and remarked that this is very good. He then asked whether it makes sense to propose automatic enrollment since we already have such a high participation rate. Mr. Long responded that participation rates are much lower than 86 percent among members of the uniformed services. Therefore, it is this group that would be most affected by automatic enrollment. The Board will have to decide whether it makes sense to extend automatic enrollment to members of this group.
Mr. Saul asked whether the provision in the Pension Protection Act would lead to automatic enrollment in all private sector plans. He was told that this provision was not mandatory; each plan's administrator must decide whether to implement automatic enrollment. The Agency would need separate legislation in order to make automatic enrollment applicable to the TSP.

Mr. Sanchez asked why 5.3 percent of FERS participants as compared to only .7 percent of CSRS participants and 1.8 percent of uniformed service participants reported that they do not participate in the TSP because it was too complex. He was told that this was likely because the latter groups must affirmatively elect to participate (and therefore have done some research), whereas FERS participants automatically receive contributions from their employing agency. Mr. Sanchez then asked what might be responsible for approximately 25 percent of uniformed service and CSRS participants indicating that they save for retirement using vehicles other than the TSP whereas only 8.9 percent of FERS participants report saving in other ways? He was told that it was likely because the TSP was a significant part of their retirement plan and they are likely saving at higher rates than these other participants.

- Sixty percent of respondents indicated that they would like to add a ROTH/401(k) feature to the TSP but only 32.2 percent have a ROTH IRA—so this may be a feature they would not use.

- Forty-six percent of respondents indicated that more investment options would be a good idea. No one fund was favored by a majority of participants. None of the options were favored if it would cost more than existing funds.

Mr. Saul remarked that he was surprised that this high a percentage of respondents wanted new features because it adds complexity. Mr. Long agreed, noting that adding more funds tends to hurt participation rates. Mr. Saul then remarked that it was interesting that the respondents favored debt options to equity options, with Treasury Inflation Protected Securities being the most preferred option.

Mr. Fink noted that the survey showed we did not have current addresses for nine percent of the individuals surveyed and asked whether this was representative of the TSP as a whole? He was told that it is. Mr. Fink then noted that the
lowest percentage of responses came from FERS participants. He was told that future surveys will focus to a greater extent on FERS participants. He then asked about the response indicating that thirty-two percent of respondents receive paper quarterly statements when the Agency only mails ten percent of its statements. Mr. Long replied that this likely means they view their statements on-line and then print a copy. Mr. Fink then noted the response showing that sixteen percent of respondents never review their account and seventeen percent review it only semi-annually or annually and remarked that these participants are vulnerable to fraud. Mr. Long noted that this will be subject to further study and that we will share the results with the Board. Mr. Sanchez asked how this compares to the private sector. Mr. Amelio replied that some studies have shown that eighty to ninety percent of participants either never review their account or do so less frequently than once a year. Mr. Sanchez pointed out that he was pleased that eighty percent of respondents indicated that they check it at least annually. This is a retirement savings plan and it is not necessary that those who invest for the long term check their accounts frequently. He added that we do need to work to reduce the sixteen percent who never review their account. Mr. Amelio added that many of the new investment options may sound good to the participants, but he questioned how well many of them could define them. He added that, as fiduciaries who must act solely in the interest of the participants and beneficiaries, there is only so much they can do. Some participants will simply never review their statements. He concluded, however, by remarking that Mr. Fink's priorities were very good. Mr. Long stated that the survey was valuable because, among other things, it made us aware of potential problem areas and that we can now build an action plan to address them.

Chairman Saul noted that the survey is a good start and remarked that the real question is what will the Agency do with the data? He noted that this should be a topic of constant update and that the staff should use it to formulate policy recommendations. He was assured that the staff will do so. He then remarked that this was a good use of the participants' money and that it was something that we needed to do. Mr. Fink and Sanchez concurred. Chairman Saul cautioned them not act solely on the findings, but to consider other factors such as complexity and added expense. Mr. Amelio replied that we did try to address these factors when we framed the questions. He added that adding a ROTH feature may be popular with participants simply because most participants have heard of ROTH IRAs. This does not mean, however, that all participants under-
stand the plusses and minuses of using a ROTH 401(k). Mr. Saul compared adding features to buying a new car: there are many great options, but they all come with costs, and, when you’ve added them, they really don’t make it a better car.

Mr. Fink asked Mr. Long when he would report on what other plans do with dormant accounts and was told he expected to report in February or March.

b. Fraud.

Approximately two dozen participants had money fraudulently removed from their TSP accounts. It appears that each participant’s home or work computer was infected with key logger software which allowed others to monitor their keystrokes and thereby obtain PINs and other account identifiers. The Agency’s system was not breached.

The Agency posted notices on its website that caution participants about the need to protect their computers from such intrusive software. The Agency is working with the Secret Service and financial institutions in an effort to recover this money and has, in fact, recovered approximately two-thirds of this money. Mr. Sanchez expressed his hope that the publicity surrounding these thefts would cause those TSP participants who do not monitor their accounts regularly to do so now.

c. Awards to Board Members.

Mr. Amelio presented each Board member with a plaque bearing the Agency seal that read: “In recognition of fiduciary service to the Thrift Savings Plan, the participants and beneficiaries extend their appreciation for unwavering loyalty and protection in their sole interest.”

Mr. Saul thanked Mr. Amelio and stated that it was the Executive Director and Agency staff who deserve the credit.

5. Closed session.

On a vote taken by the Secretary before the meeting, the members closed the meeting for a discussion of security and internal personnel matters.
Whereupon, there being no further business, the following motion was made, seconded, and adopted without objection and Chairman Saul adjourned the meeting at 12:11 p.m.

MOTION: That this meeting be adjourned.

Thomas K. Emmswiler
Secretary

NOTE: Ace-Federal Reporters, Inc. made a verbatim transcript of this meeting.

Attachments

1. Thrift Savings Fund Statistics