FEDERAL RETIREMENT THRIFT INVESTMENT BOARD
1250 H Street, NW Washington, DC 20005

MINUTES OF THE MEETING OF THE BOARD MEMBERS

January 22, 2008

Andrew M. Saul, Chairman of the Federal Retirement Thrift Investment Board, convened a meeting of the Board members on January 22, 2008, at 9:00 a.m., Eastern Time. The meeting was at the Board's offices at 1250 H Street, N.W., Washington, D.C. Parts of the meeting were open to the public and parts of the meeting were closed to the public. In attendance were Thomas A. Fink of Alaska, member; by telephone, Alejandro M. Sanchez of Florida, member; Gordon J. Whiting of New York, member; Gregory T. Long, Executive Director; Thomas K. Emswiler, Secretary and General Counsel; Mark A. Hagerty, Chief Information Officer; 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 17, 2007 Board member meeting.

Chairman Saul entertained a motion for approval of the minutes of the December 17, 2007 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 17, 2007, be approved.

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

Prior to the formal reports, Chairman Saul asked that the record reflect that no court-reporter was present. The meeting was recorded on a digital recorder and that recording was subsequently transferred to two CDs.

a. Monthly Participant Activity.

Mr. Long reviewed the report on TSP statistics. See "Thrift Savings Fund Statistics" (attached). Ms. Ray stated that the U.S. markets had been uneventful on Friday, January 18th, but the international markets fell by 5 percent over the weekend. As a consequence, the Dow futures were predicting the market would open down 500 points today. When the Federal Reserve cut interest rates .75 percent, the futures rallied but then deteriorated. Mr. Long noted that this volatility will be of concern to the participants and beneficiaries. He added that he hopes most participants invest for the long term, but added, because most transactions are done over the web, even if this market volatility leads to increased interfund transfers, we will be able to handle it.

Chairman Saul said that participants must look to long-term goals; the TSP is meant to be a long-term plan. Nevertheless, each participant must determine what level of market risk is acceptable. The most important thing the Agency can do is ensure that TSP assets are safe and that the system is functioning. He recognizes that there may be some delays at the call centers, but he has complete confidence the staff will handle the influx. He added that he is aware that call center staff has increased recently but that callers may still experience delays.

Mr. Long noted that the $231 billion invested in the TSP is virtually unchanged from last month. The FERS participation rate remains at 85.6 percent and, with rounding, the TSP now has 3.9 million participants. This is a very large plan and it gets bigger every month. The expense ratio for 2007 is one basis point. Chairman Saul noted that the expense ratio will likely increase in 2008 due to the major expenditures the Board approved for the TSP's computer systems.

Mr. Long pointed out that the Active Duty participation rate had increased to 34.8 percent, the Reserve participation rate had increased to 11.9 percent, and the total uniformed service participation rate had increased to 26.2 percent. Mr. Sanchez said that he had spoken with a number of uniformed service members at a dinner he attended in Pensacola. The service members seemed very familiar with the TSP and he was pleased to see that the uniformed participation rate continues to grow.

b. Gross and Net Expenses for 2004-2007.

Mr. Long review two charts showing the TSP's gross and net expenses (attached). One chart shows expenses as basis points and the other shows expenses as dollars. The green areas on the charts show the amounts we charge participants. In 2004, we charged participants 5.8338 basis points (which we rounded to 6 basis points); in 2005, we charged 4.756 basis points (which we rounded to 5 basis points); in 2006, we charged 3.1305 basis points (which we rounded to 3 basis points); and, in 2007, we charged 1.4583 basis points (which we rounded to 1 basis point). Chairman Saul commented that it is important to note that the chart shows basis points, not percentages, because it appears to show percentages. Mr. Petrick agreed and added that in 2004, we charged .058338 percent and in 2007 we charged .014583 percent. Chairman Saul stated that a basis point is 1/100 percent. Mr. Long said that these are very small numbers and added that what we charge participants is much less than is available through any other plan. Chairman Saul asked what does a typical, large, 401(k) plan charge. Mr. Long stated that Ennis-Knupp had determined that a well-run plan typically charged 60-70 basis points. Consequently, the highest amount we charged was still substantially less than what a well-run private sector plan would charge. Chairman Saul stated that this is a very large difference. He stressed that while many in the private sector view the public sector as being inefficient, the TSP was just the opposite. The Agency has cut expenses since the current Board was seated, even though assets under management doubled and the number of participants increased by 800,000. The TSP is running much more efficiently than private sector plans. He is very proud of how well this plan is administered.

Mr. Petrick returned to the discussion of the charts. The yellow and blue areas represent credits against gross expenses for loan fees and plan forfeitures. Gross expenses (3.5 basis points in 2007) are higher than the net expenses we charge to participants. Gross expenses, have, however, also fallen. The second chart shows real dollars (gross and net); the gross amount has declined. There was a slight increase in 2005 due to some charges attributable to the new record-keeping system (to include associated communication materials).

The $31.5 million forfeited to the plan in 2007 was a significant offset to gross expenses. This may be a short-term phenomenon caused by the correction of retirement system coverage of employees who had been misclassified when the Federal government adopted the FERS retirement system but retained the CSRS retirement system for employees hired before the new system was implemented. Mr. Long added that the Board members might recall Ms. Moran speaking about FERCCA (Federal Erroneous Retirement Coverage Corrections Act). We are not sure when most corrections will be completed, but, this year, the plan's net expense ratio would have been 2-3 basis points but for the forfeitures attributable to FERCCA corrections. As a consequence, while Agency staff is doing its best to reduce expenses, factors external to the Agency, like FERCCA, have helped. Chairman Saul noted that, even so, gross expenses have fallen from $89.9 million in 2005 to $75.7 million in 2007 despite the significant growth in assets under management and in TSP participants. Mr. Long stated that he wanted to ensure that the Board understood that this year's charge of 1 basis point will not last forever.

Mr. Fink commented that the forfeitures and loan fees offset more than 50 percent of gross expenses this year; while forfeitures constituted the largest portion of this offset, loan fees have increased also. Mr. Petrick said that we expect the amount attributable to loan fees will be stable (it was much lower in 2004 only because that was the first year we charged loan fees and we only charged fees for part of 2004). Mr. Long added that loan fees will likely increase as the plan increases and plan loans increase commensurately. Mr. Fink and Chairman Saul stated that this had been an excellent presentation. Chairman Saul asked that, next time, the charts more clearly show that we charge basis points, not percentages.

Mr. Sanchez stated that, at 9:40 a.m., he must leave the meeting and expressed his apologies.

c. Legislative Report.

Mr. Trabucco reported that, during Congress' recess, he, Ms. Moran, and Mr. Emswiler had worked with Congressional staff on the language of the automatic enrollment/L Fund default bills. He expects the bills will be introduced in the near future.

3. Quarterly Reports.

a. Quarterly Investment Policy Review.

Ms. Ray reviewed the January 9, 2008 memorandum (attached), on the performance of the G, F, C, S, I, and L Funds during December 2007.

She noted that, in December, all funds tracked the indexes perfectly with the exception of the small-mid cap fund. It outperformed its index by 7 basis points due to the sampling technique used by the fund. The fixed income fund has outperformed its index by 10 basis points for the year, primarily due to a class action settlement. The I Fund outperformed its index by 28 basis points for the year, primarily because the index is net of taxes whereas the I Fund is tax-exempt.

The 2007 trading costs for the I Fund are 6.2 basis points or $16.5 million. In 2007, $26.7 billion was traded in the I Fund--which represents approximately 100 percent of its market value. During December, $1.3 billion was traded in the I Fund--incurring trading costs of $759,987.

Mr. Fink asked whether interfund transfer activity had decreased since the Executive Director was given authority to ask abusive traders to reduce their activity. Mr. Long explained that the interim regulation allows him to send letters to the abusive traders and that he expects to send those letters next week. We anticipate sending the draft final regulation to the Employee Thrift Advisory Counsel next week for its comments and to then publish the proposed regulation in the Federal Register with a 30-day comment period. If someone suggests a better way to address the problem, we will adopt it. Mr. Fink asked when we anticipated the policy to be mandatory and was told late-March or early-April. Mr. Fink then asked whether interfund transfers have decreased. Mr. Long replied that they have; this decrease may be due to press coverage of the issue. Mr. Trabucco stated that we will fully consider all comments because we are a good ideas place; that is why we surveyed industry practice before developing a proposal. Mr. Long said that we can't have 100 percent turnover of a fund during a year.

Ms. Ray noted that the I Fund fell 2.25 percent in December but was up 11.17 percent for the year. The F Fund was the next best performer, returning 7.09 percent for the year and continuing to perform well in January. The G Fund returned 4 percent in December. For the year, all L Funds outperformed the G, C, and S Funds. The 2030 and 2040 Funds outperformed all Funds except the I Fund. Since inception, the 2020, 2030, and 2040 Funds outperformed all underlying Funds except the I Fund.

Mr. Long stated that page 8 shows interfund transfer activity. Mr. Long added that the 133,550 interfund transfers in December was the lowest monthly total for the year; press coverage of this issue must have had some affect.

Ms. Ray referred to page nine and pointed out that the amount invested in the L Funds had grown from $16.8 billion at the end of 2006 to $23.8 billion at the end of 2007.

The number of participants with L Fund balances had increased from 433,025 to 566,232.

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

Ms. Ray said that an audit of Barclays' proxy votes showed no exceptions.

Mr. Fink said that he was aware that Barclays lent securities. He had heard that, due to turmoil in the markets, some larger firms had been unable to return the securities they borrowed. He then asked whether we have asked Barclays to verify that it only makes solid loans. Ms. Ray stated that we receive collateral equal to 105 percent of all loans, and Mr. Long stated that we have been in touch with Barclays about this and are closely monitoring it, but have not seen any problems.

b. Quarterly Vendor Financial Report.

Mr. Petrick reviewed the January 4, 2008 memorandum entitled "Quarterly Financial Assessment of TSP's Primary Vendors—January 2008" (attached). He stated that there have been no significant changes since the last report. Chairman Saul asked Mr. Petrick to review by exception—except for the call center which had recently been acquired by The Active Network. Mr. Petrick reported that The Active Network continues with its strategy of aggressive growth through acquisition. The transition from Spherix to The Active Network was seamless. The scheduled move of the Cumberland call center to Frostburg is on-track. Chairman Saul asked how far it was from Cumberland to Frostburg and whether the call center would keep the same employees. He was told it was approximately 10 miles, that it would keep the same employees, and that it would have access to college students as potential employees. Chairman Saul asked whether the expense of this move would be borne by the TSP and was told that it would not. Ms. Moran stated that the move is scheduled for President's Day weekend and will have no affect on service to participants (the TSP is not open for business on weekends and holidays and the Clintwood call center will have additional staff as a back-up).

We have no real concerns about the financial status of The Active Network. Mr. Long said that because it is a private company, it provides its financials under a confidentiality agreement, and we must review it in private session. Since this was not on the Agenda for this month, the Board voted to discuss it at the next Board member meeting and also adopted the following policy by unanimous vote:

RESOLUTION

> Anytime the Agency receives vendor financial data pursuant to a confidentiality agreement, the Board will review that data in closed session during the next meeting that includes the quarterly financial assessment of the TSP's primary vendors.

Chairman Saul asked when the contract with The Active Network expires. Mr. Petrick stated that it expires in March of 2009 and added that Ms. Moran is well into the transition planning process. Chairman Saul then asked when the contract with the Clintwood call center expires and was told 2010.

Mr. Fink asked when the contract with Switch and Data expires. He was told that we are considering requesting proposals for that contract at the same time we request proposals for the general record-keeping contract. Mr. Long added that the Board will be given an opportunity to review the selection criteria. Chairman Saul inquired about the Agency's financial assessment of Switch and Data. Mr. Petrick reported that it was performing much better. While it had yet to earn a profit, its losses were much smaller. Financial status will be a criterion in the record-keeping solicitation. But, generally, the IPO gave Switch and Data the results it wanted.

4. Audit Status Report.

Mr. Petrick reviewed the January 11, 2008 memorandum entitled "Report on audit recommendations 2003-2007" (attached). The report shows the number of audit recommendations the Agency has reviewed since it implemented the new record-keeping system. No recommendations from before this time are still open. Of the 42 recommendations received from the Department of Labor, 20 are closed. Of the 21 from Deloitte and Touche, 17 are closed. Of the 26 from Office of Personnel Management (OPM), none are closed. Of the 5 from the Government Accountability Office (GAO), 1 is closed. The Agency has, however, complied with most of the audit recommendations. The Agency cannot close an audit recommendation until the auditor returns to complete a new review. The Agency rarely non-concurs with an audit recommendation and any non-concur decision is discussed with the Board. The recommendations shown as "open per Agency" are those recommendations we have yet to implement. The senior staff reports on the status of such recommendations each month.

OPM audited the Agency in 2004. OPM had many human resource (HR) related recommendations. Because OPM has not been back, all are shown as open. Nevertheless, the Agency has made good progress toward implementing these recommendations. We've hired the Department of Interior to process personnel actions and have hired an outside consultant to help with writing position descriptions and with hiring actions. We are still working on about 10 of the recommendations. We are developing an overall HR plan, HR manuals, and a Human Capital Plan. We anticipate having these in place by the end of 2008. Barbara Torres, the Agency's new administrative officer, will be responsible for overseeing this effort.

Mr. Long proposed making this report a regular Board meeting agenda item. He assured the Board that Agency staff is well aware of open audit recommendations and is constantly working to implement them. Mr. Fink asked when OPM would be back and was told this summer.

5. Board Calendar.

Mr. Long noted that "procurement evaluation criteria" had been added to the March meeting agenda. Mr. Sanchez had asked the Board to reschedule the June meeting to June 23rd. This meeting had been tentatively scheduled as a due diligence visit to Barclays. The Board agreed to move the meeting to June 23rd. However, since Mr. Sanchez had had to leave today's meeting early, the Board deferred discussion of the meeting's location until February.

Chairman Saul then stated that it was important the Board members know what they could do to help see the Agency's legislative proposals through to enactment. Mr. Long promised that Mr. Trabucco would give a full report in February.

Chairman Saul requested an update on the implementation of the TSP computer modernization plan at the next Board member meeting. He then noted that the switch to account numbers had put a stress on the call centers, but stated that he knew Agency staff was working on a fix. Mr. Hagerty stated that they were working on fielding a customizable user ID and that he hoped to have this feature available in 60 to 90 days. Chairman Saul asked when the Agency switched from using Social Security numbers to account numbers and was told October 8th. Mr. Hagerty stated that a 13-digit account number was hard to remember and that he and Ms. Moran were working on a customizable user ID. He added that this would require a lot of programming, but a customizable user ID, coupled with the TSP web redesign project that Ms. Moran is working on, would make the entire system more user friendly. He stated that we will also introduce challenge questions on the web site. Chairman Saul asked whether Mr. Hagerty still believed the switch to account numbers was a good idea. Mr. Hagerty replied that it was absolutely essential for security. Mr. Long added that we always balance being user friendly with security, but security must always be the top priority. Chairman Saul reiterated he wanted a complete review of the computer modernization plan at the next Board member meeting.

Mr. Trabucco commented on the Agency's legislative initiatives. He noted that Agency staff had remained fully engaged with Congressional staff during Congress' recess. The big obstacle remains cost. Informal estimates show that automatic-enrollment would reduce tax revenue by hundreds of millions of dollars. The Congressional Budget Office will give a formal estimate once the legislation is introduced. We will have to see whether the House will hold to the pay-as-you-go rules. If it does, adding a Roth feature to the TSP could provide an offset. However, because the private sector has been slow to adopt a Roth feature, the Agency has not been able to determine whether it would be in the interest of the participants and beneficiaries to incur the expense of adding a Roth feature when it might ultimately prove unpopular.

6. Closed session.

On a vote taken by the Secretary before the meeting, the members closed the meeting for a discussion of personnel matters.

At 11:34, upon completion of the closed session, the members reconvened the open portion of meeting.

Whereupon, there being no further business, the following motion was made, seconded, and adopted without objection and Chairman Saul adjourned the meeting at 11:35 a.m.

MOTION: That this meeting be adjourned.

Thomas K. Emswiler
Secretary

Attachments

1. Thrift Savings Fund Statistics
2. Gross and Net Expense 2004 - 2007
3. December 2007 Performance Review - G, F, C, S, I, and L Funds
4. Quarterly Financial Assessment of TSP's Primary Vendors—January 2008
5. Report on Audit Recommendations 2003-2007