

UNIVERSITY OF MAINE SYSTEM  
Board of Trustees

**Investment Committee**

March 9, 2017

University of Maine System – Executive Offices  
Rudman Conference Room, 253 Etabrooke Hall, Orono

**Present: Committee Members:** Karl Turner, Chair (at USM), Sam Collins (by phone), Gregory Johnson (at USM). **Non-Voting Committee Members:** Robert Blackwood (at USM) and Eric Hayward (at USM). **Staff:** Tracy Bigney, Tracy Elliott (at USM), Ryan Low (at UMA) and Rebecca Wyke (at UMA). **Others:** Jay Roney – NEPC (at USM), and Barry Schmitt – CAPTRUST (at USM).

**Absent: Committee Members:** James Donnelly, Mark Gardner, and Shawn Moody.

Trustee Turner, Chair, called the meeting to order.

**FY2018 Endowment Distribution Rate per Share.** Ms. Tracy Elliott, UMS Controller, provided an overview of the FY2018 endowment distribution rate and estimated spending. Ms. Elliott noted that the campus Chief Business Officers affirmed their support for using a 4.5% spending rate to calculate the FY2018 endowment distribution rate per share. This 4.5% is consistent with prior years and other higher education institutions. Ms. Elliott noted that the recently issued *2016 NACUBO Commonfund Study of Endowments* reported that, for the 805 participating institutions, the FY2016 effective spending rate averaged 4.3%.

A 4.5% endowment spending rate for UMS equates to a rate per share of \$15.13366. Using this rate, an estimated \$5.3 million will be distributed including \$4.2 million for endowed spending and \$1.1 million for management costs in FY2018.

Members discussed whether or not the portfolio can support this level of disbursement in the long run. The investment policy for this portfolio has a minimum long-term return assumption of 7.5% which Mr. Roney noted does not include alpha. As of December 31, 2016, the five year return for the portfolio was 6.7% with the 10 year return at 4.4%. Ms. Elliott will move the annual distribution rate discussion up in the Committee calendar so that we are visiting this topic earlier to more easily accommodate the campus budget building process should any change in rate be recommended in the future.

Lacking a quorum, this and all action items, will go to the Board for approval at its March meeting.

**Action for March Board Meeting:**

That the Board of Trustees approves an endowment distribution rate of \$15.13366 per share for FY2018.

**Investment Committee Duties and Responsibilities Revised.** Since the Committee's last meeting, Trustee Turner worked with staff to review and update the Investment Committee Duties and Responsibilities. Proposed changes include clarifying the Committee's authority to act without referring items to the Board of Trustees. In addition, language was added to allow Committee members to provide direction to staff, with subsequent formal action to be taken by the Committee or the Board, when a quorum of the Committee is not present.

### **Action for March Board Meeting:**

That the Board of Trustees approves the Investment Committee Duties and Responsibilities, as presented.

**Defined Contribution Plan – Quarterly Review.** Mr. Barry Schmitt with CAPTRUST Financial Advisors provided a quarterly review of the Defined Contribution Plan. As of December 31, 2016, there were \$1.4 billion in total plan assets including \$1.4 million in transfers from deselected vendors for the quarter. Mr. Schmitt highlighted the following:

- Morningstar decided to combine its open-end mutual fund universe with its exchange-traded fund (ETF) universe in November 2016. CAPTRUST will evaluate the impact that the addition of ETFs will have on peer groups and how it might affect their approach to monitoring investment policy statements and then decide an appropriate course of action.
- The Labor Department announced that it will delay implementation of the fiduciary rule from April 10<sup>th</sup> to June 9<sup>th</sup> in order to collect another round of comments.
- Tighter labor markets are causing plan sponsors to consider effectiveness of total retirement benefits.
- The potential for tax reform and impacts on retirement plans and deductible contribution limits.
- With litigation on the rise, requests for proposals (RFP's) related to retirement plans and plan benchmarking activities are expected to increase given the focus on allegations related to fees.
- CAPTRUST and the Committee discussed the issue of cyber-attacks. The Committee asked that TIAA's cyber security policy be reviewed by the UMS Chief Information Security Officer.

Mr. Schmitt also provided an update on fund performance. All funds are meeting policy guidelines except one - The Goldman Sachs Growth Opportunities Fund. In November 2016, CAPTRUST performed due diligence procedures including an on-site meeting with the portfolio manager. Following a disappointing performance in 2015, the strategy again lagged its peers and benchmark in 2016. The strategy outperformed in the first half of 2016, but lagged significantly in the second half due to a rally in lower quality stocks. The team also had some missteps in individual positions where their thesis did not work as expected.

CAPTRUST is removing this fund from their recommended list. The strategy has recently faced stylistic headwinds and they do not believe that the team has navigated the challenging backdrop as well as some of its peers. Nonetheless, recent 2017 performance is encouraging. CAPTRUST will report back on this manager at the next Committee meeting.

Regarding other funds in the plan, Jack Moore asked if an analysis could be done on CREF Stock relative to other funds that have similar objectives. There are \$217 million (15.7%) of total plan assets invested in this fund. CAPTRUST and the Committee discussed the current structure of CREF Stock - 70% U.S. equity (Russell 3000), 23% international developed, and 7% emerging markets. In addition to performance, CAPTRUST and the Committee discussed the current revenue sharing of this fund and the impact it could have on plan expenses if CREF Stock, over time, was eliminated. In addition, because this fund is in individual contracts, unless the System made the decision to migrate over to group contracts (as opposed to individual contracts today), CREF Stock must remain open to new investments and cannot be eliminated. While future contributions can be

re-directed, participants can re-defer back into this fund. CAPTRUST will evaluate further and provide the Committee with an analysis at the next Committee meeting.

**Defined Contribution Plan Share Class Change.** Ms. Elliott and Mr. Schmitt provided an overview of recent share class changes and the sequence of events and TIAA's missteps related to these changes. For five funds, the Plan has moved to a lower fee share class and CAPTRUST is working with TIAA to evaluate the related impact on plan economics. As part of this process, TIAA is also reassessing their record keeping fee which CAPTRUST will bring to a future Committee meeting. CAPTRUST recently discovered that there was a period, between November 2016 and February 2017, where both share classes were mistakenly offered in the plan. TIAA is evaluating the data and will retroactively apply earnings, as applicable, to participants whose assets should have been mapped to the lower share class. In addition, Ms. Elliott will be working with CAPTRUST and TIAA on a memorandum of understanding related to signature authorities and protocols regarding the Plan.

**Action for March Board Meeting:**

That the Board of Trustees approves:

<b>Replacing Old Share Class</b>	<b>Adding New Share Class</b>
Oppenheimer Intl Growth Y	Oppenheimer Intl Growth I
Goldman Sachs Growth Opp I	Goldman Sachs Growth Opportunities R6
RidgeWorth Ceredex Mid-Cap Value Eq I	RidgeWorth Ceredex Mid-Cap Value Eq IS
Harbor Capital App Institutional	Harbor Capital Appreciation Retirement
JHancock Disciplined Value R5	JHancock Disciplined Value R6

**NEPC Performance Reviews.** Jay Roney, with NEPC, reviewed performance for all 3 UMS portfolios with the following highlights.

**Managed Investment Pool (MIP).** The Managed Investment Pool (MIP) returned 3.1% fiscal year-to-date as of December 31<sup>st</sup>. This return ranked in the 92<sup>nd</sup> percentile in the InvestorForce Endowments and Foundation \$100-500 million universe. Managers detracted 30 basis points of value during this time period with an international equity manager and emerging market equity managers detracting the most value relative to benchmarks. On a trailing one year ending December 31<sup>st</sup>, the MIP returned 5.2% ranking in the 77<sup>th</sup> percentile.

**Defined Benefit Pension Fund Performance Review.** The Pension returned 1.5% fiscal year-to-date as of December 31<sup>st</sup>. This return ranked in the 80<sup>th</sup> percentile in the InvestorForce Total Fund Universe due to the conservative asset allocation. Managers detracted 20 basis points of value during this time period with international equity and emerging market equity managers detracting the most value relative to benchmarks. On a trailing one year ending December 31<sup>st</sup>, the Pension returned 5.0% ranking in the 79<sup>th</sup> percentile.

**Operating Fund.** The Operating Fund returned 1.2% fiscal year-to-date as of December 31<sup>st</sup>. This portfolio had a lower return compared to the other 2 portfolios given the very conservative risk profile of the Fund. Managers added 20 basis points of value during this time period as most managers were ahead or in-line with stated benchmarks. On a trailing one year ending December 31<sup>st</sup>, the Operating Fund returned 3.6%.

**Asset Allocation Study and Recommendations.** Mr. Roney provided an overview of NEPC's 2017 capital market observations, including investment opportunities. NEPC discussed asset allocation and their recommendations as outlined below:

**Managed Investment Pool (MIP):**

- Allocate 5% to International Equity Small Cap (new mandate) from International Equity
- Reduce core bonds from 10% to 5% and allocate 5% to TIPS
- Allocate 5% to Bank Loans (new mandate) from Global Multi-Sector Fixed Income

**Pension Fund**

- Reduce core bonds from 27% to 20% and allocate 7% to TIPS (new mandate)
- Allocate 5% to Bank Loans (new mandate) from Global Multi-Sector Fixed Income

**Operating Cash Fund**

- Reduce core bonds from 10% to 5% and allocate 5% to TIPS (new mandate)

Committee members supported the recommended portfolio allocations with a modification that the portfolio holdings of EntrustPermal (credit hedge fund) be eliminated in the Operating Fund and reduced in the MIP and Pension Fund. NEPC will modify their recommendation for action at the March Board meeting.

**MSCI Environmental Social and Governance (ESG) Report.**

Subsequent to the Board's approval of an ESP policy for the MIP in September 2016, the UMS engaged MSCI to provide annual reporting that will measure the MIP's equity and fixed income holdings with regards to ESG factors. Mr. Roney reviewed MSCI's recently completed baseline report, which will allow the Committee to monitor progress toward improving ESG factors.

Adjournment

Submitted by  
Tracy Elliott for  
Tracy B. Bigney, Clerk