



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

MINUTES OF THE MEETING OF THE BOARD MEMBERS

November 20, 2006

Andrew M. Saul, Chairman of the Federal Retirement Thrift Investment Board, convened a meeting of the Board members on November 20, 2006, at 9:15 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; 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 October 16, 2006 Board member meeting.

Chairman Saul entertained a motion for approval of the minutes of the October 16, 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 September 18, 2006, be approved.

2. Growth of TSP.

Mr. Saul noted that the plan had reached the \$200 billion mark. He remarked that the plan's doubling in less than four years was a testament both to an outstanding organization and to the American economy.

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

a. Monthly Performance Numbers.

Mr. Long reviewed the report on TSP statistics. See "Thrift Savings Fund Statistics" (attached). He noted that

as of the end of October the plan was at \$199 billion (now \$202 billion) and that the number of participants increased by approximately 8,000 in October. The number of outstanding loans was up slightly and the expense ratio continues to decrease. Otherwise, there has been little change. Mr. Amelio noted that the administrative fee for the year may be as little as three basis points. Mr. Saul congratulated the staff for cutting expenses by almost a third while simultaneously doubling assets. This means that the Agency is administering the plan at almost no cost to the participants.

b. Monthly Investment Activity Report.

Ms. Ray reviewed her November 7, 2006 memorandum (attached), on the performance of the G, F, C, S, and I Funds during October 2006.

She reported that, using dollar-weighted returns, the average participant's return would have been 8.5 percent for the 12-month period that ended in September. Mr. Saul remarked how impressive this is considering that approximately 40 percent of TSP assets are invested in the lower yielding G and F Funds.

Ms. Ray noted that the S Fund's tracking error of 25 basis points was caused by it not including all stocks in the index. The I Fund's tracking error of 13 basis points was caused by the tax effect of that Fund. Because we place our I Fund order after the markets are closed, the trading costs for that Fund are higher. She noted that, since inception, all L Funds have outperformed the G Fund and that the 2020, 2030, and 2040 Funds have outperformed the C Fund. Mr. Amelio noted the 11 percent L Fund participation rate is double what the Agency had initially projected, in part, due to exceptional education efforts.

Chairman Saul asked why monthly contributions in 2006 were significantly higher than 2005. He was told this was due to the TSP having more participants and the elimination of the percentage-of-pay contribution limits.

Mr. Amelio then presented the Board with two plaques: the first commemorated the date the Agency introduced Life Cycle funds--August 1, 2005; the second commemorated the date the Agency introduced daily valued accounts--June 16, 2003. The plaques will be hung in the Agency's reception area.

c. Legislative Report.

Mr. Trabucco reported that the Democratic victories in November would lead to a switch in the leadership of the Agency's oversight committees. He anticipated that, for the most part, the current Ranking Member would become Chairman and vice versa. Subcommittee structure may change, but Congress will not make restructuring decisions until the 110th Congress convenes.

c. Participant Survey.

Mr. Long reported that the survey was mailed in late October and early November and that responses were due by Wednesday November 22nd. Chairman Saul asked what response rate we expected and what our timetable is. He was told the Agency would be happy with a 40-50 percent response rate and that we expect to be able to report on the results by the end of the year.

4. New Business.

a. Ennis Knupp Report.

Ennis Knupp reported that it had been asked by the Agency to review the current investment structure of the TSP, i.e., the number and types of investment funds offered to participants, and to evaluate potential investment fund additions.

In response, Ennis Knupp completed a report which: reviewed the current circumstances of the TSP and compared its practices to peer plans; identified key criteria for evaluating investment fund alternatives; applied the key criteria to a broad array of investment fund alternatives to identify investment funds appropriate for consideration; reviewed the appropriateness of adding specific investment fund alternatives; and provided its recommendations to the FRTIB.

Ennis Knupp concluded that the TSP's core investment program is well-structured and found no gaps in the investment line-up. After applying the key criteria, it eliminated the following asset classes/categories from further consideration: non-U.S. small-cap stock; high yield bonds; private market real estate; private equity; hedge funds; and socially responsible/corporate governance funds. It reviewed the merits of offering the following investment fund alternatives in detail:

non-U.S. bonds; U.S. stock funds by value and growth; emerging markets stock; Treasury inflation-protected securities (TIPS); real estate investment trusts (REITs); and commodities. Ennis Knupp found no compelling basis to add any of the six investment fund options as TSP investment funds. It recommended the Agency not add any additional investment funds to its investment program. The Agency serves its participants very well by providing a well-administered, low cost, well-diversified plan, with excellent communication and education materials. Adding any of these funds would only unjustifiably add complexity to the TSP.

In response to questions from Mr. Sanchez, they noted that more and more plans were offering life cycle funds and that only about 8 percent of plans offered a real estate fund. In response to a question from Chairman Saul, they reported that TSP participants were less heavily invested in equity funds (by about three percent) than participants in other plans. This is attributable to inertia. That is, when the plan was set-up, it only offered one equity fund (the C Fund), a money-market like fund (the G Fund) and a bond fund (the F Fund) and many participants have maintained their investments in these funds. Chairman Saul noted that this disproved the assertion that the Government workforce invested more conservatively than other investors.

Ennis Knupp also reported that 33-50 percent of plans were using life cycle funds as the default option. Mr. Whiting asked whether the default funds were targeted at a participant's age and was told that they were. Mr. Amelio remarked that the Agency was analyzing whether it would be appropriate to ask Congress to allow the Agency to set the life cycle funds as the default option and that he planned to report to the Board in 2007. He also stated that the Agency was analyzing asking Congress to add an automatic enrollment feature. Automatic enrollment is also increasing among private sector plans (from 19 to 24 percent). The Agency will also examine adding both an auto-escalation feature that would automatically increase the amount of a participant's contributions and adding a Roth component. Chairman Saul asked that the Agency complete its analysis and make its recommendations during the first half of 2007. Mr. Amelio said that he would and added that we would also look into the merits of providing investment advice to participants.

b. Pension Protection Act.

Mr. Emswiler and Ms. Moran reviewed the Agency's progress toward implementing the provisions of the Pension Pro-

tection Act (PPA) that are applicable to the Agency. The PPA makes the Saver's Credit permanent and indexes it for inflation. The Agency will amend its communication materials and web site to ensure participants are aware of this.

The PPA amends the I.R.C. to allow rollovers of after-tax contributions from a qualified plan (like the TSP) to a section 403(b) plan or a qualified defined benefit plan. We will revise our withdrawal booklet and withdrawal forms to reflect this option. We will also update the website.

Beginning January 1, 2008, the PPA allows direct transfers from tax-qualified retirement plans (like the TSP) to a Roth IRA. This will be a major change. Since the effective date of this provision is 2008, we will wait for IRS guidance next year before we make any changes.

Chairman Saul asked that we notify participants of the changes brought by the PPA as soon as possible and was assured that we would. We will also report on the PPA in the January TSP Highlights. Mr. Whiting noted that the members of the press who were present at the meeting could also inform TSP participants of these pending changes.

The PPA exempts withdrawals of reservists, called to active duty after September 11, 2001 and before December 31, from the 10 percent early withdrawal penalty. The reservist may also, at any time during the two-year period beginning on the day after the end of the active duty period, make one or more contributions to an IRA of such individual in an aggregate amount not to exceed the amount of such distribution. We are changing our tax notice to reflect this and are linking the TSP website to an IRS press release that discusses this. The participant will work directly with the IRS to take advantage of this change. Chairman Saul remarked that we should do all that we can to ensure servicemembers are aware of this change. He was told that in addition to our other efforts, we will post this information in several places on the TSP's website.

Effective January 1, 2007, the PPA will allow a designated non-spouse beneficiary to transfer a death benefit payment directly to an "inherited IRA." We are updating our booklets, website, and forms to implement this change. We have also agreed to defer distribution of several death benefit payments for beneficiaries who want to take advantage of this provision.

The PPA allows tax court judges to participate in the TSP. Mr. Sanchez asked whether any other group of Federal employees have not been authorized to participate in the

TSP. He was told that Congress has not authorized the President or the members of the Federal Reserve Board to participate in the TSP.

The Economic Growth and Tax Relief Reconciliation Act of 2001 contained a number of provisions that were due to sunset on December 31, 2010 (some sooner) that the PPA made permanent. These are the 402(g) elective-deferral limit, the 415(c) limit, and the provision allowing catch-up contributions. The Agency has made all necessary changes to reflect this.

c. 2007 Board Meetings.

Mr. Amelio confirmed that the April 2007 Board member meeting will be a due diligence visit to Barclays. The Board members decided to hold all telephonic meetings at 10:00 a.m. rather than 9:00 a.m. because one of the Board members lives in Alaska, which is four hours earlier than the Eastern Time zone.

d. Audit of Treasury Department Operations.

Mr. Petrick reported that the Department of Labor audit of Treasury Department operations related to the G Fund determined that everything was operated appropriately and that the audit contained no recommendations.

e. GAO Review of the TSP.


Mr. Amelio and Mr. Petrick reported that the Government Accountability Office was conducting a review of TSP operations. The review is looking at a broad range of the TSP operations and also at administrative expenses. We have responded to an extensive list of written questions and have recently received a second set of questions that we are working on. We don't expect the review to wrap up until some time next year.

5. Closed session.

On a vote taken by the Secretary before the meeting, the members closed the meeting for a discussion of procurement and security.

Whereupon, there being no further business, the following motion was made, seconded, and adopted without objection and Chairman Saul adjourned the meeting at 11:50 a.m.

MOTION: That this meeting be adjourned.


Thomas K. Emswiler
Secretary

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

Attachments

1. Thrift Savings Fund Statistics
2. October 2006 Performance Review - G, F, C, S, and I Funds