



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

MINUTES OF THE MEETING OF THE BOARD MEMBERS

September 15, 2008

Andrew M. Saul, Chairman of the Federal Retirement Thrift Investment Board, convened a meeting of the Board members on September 15, 2008, at 10:20 a.m., Eastern 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, by telephone, Thomas A. Fink of Alaska, member; 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; Thomas J. Trabucco, Director, External Affairs; and Renée Wilder, Director, Research and Strategic Planning.

1. Executive Session.

On a vote taken by the Secretary before the meeting, the members opened an executive session at 9:00 a.m. for a discussion of procurement matters.

At 10:20 a.m., upon completion of the executive session, the members convened the open portion of meeting.

2. Approval of the minutes of the August 18, 2008 Board member meeting.

Chairman Saul entertained a motion for approval of the minutes of the August 18, 2008 Board member meeting. The following motion was made, seconded, and adopted without objection:

MOTION: That the minutes of the Board member meeting held on August 18, 2008, be approved.

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

Mr. Long introduced Michael Auerbach to the Board members. Mr. Auerbach is from the Department of Labor's Employee Benefits Security Administration Office. Mr. Auerbach will likely replace Ian Dingwall as the Department of Labor's representative to the Agency when Mr. Dingwall retires.

a. Monthly Participation Activity.

Ms. Wilder reviewed the report on TSP statistics. See "Thrift Savings Fund Statistics" (attached). She noted that, owing to improved market conditions and a steady inflow of contributions, assets under management increased slightly to \$227.5 billion.

The number of TSP participants increased slightly, but remained under four million. The FERS participation rate fell slightly. The Active Duty participation rate remained the same at 36.1 percent but the Ready Reserve participation increased from 11.7 percent in July to 12.6 percent in August. Mr. Sanchez remarked that this was a big jump and that, with over a quarter of the Active Duty Army participating, over fifty percent of the Active Duty Navy participating, and over a third of the Active Duty Marine Corps and Coast Guard participating, uniformed service participation is heading in the right direction.

Another positive note is that the number of loans and withdrawals declined slightly in August, reversing the increases we had seen in prior months.

b. Monthly Investment Performance Report.

Ms. Ray reviewed the September 5, 2008 memorandum (attached), entitled "August 2008 Performance Review - G, F, C, S, I, and L Funds."

She noted that the S Fund had a tracking error of 22 basis points for the month and 45 basis points for the year due to sampling. The I Fund had a tracking error of 11 basis points for the month and 32 basis points for the year due to a fair value adjustment on August 29th.

Trading volumes are down substantially compared to last year. For example, \$889 billion was traded in the F Fund in August of 2007 compared to only \$271 billion in August 2008. Mr. Sanchez asked whether these decreases were due to the Agency's efforts to educate participants that they should invest

for the long term. Ms. Ray stated that she viewed it as primarily due to the interfund transfer restrictions the Agency implemented this year. Also, many participants have invested in the G Fund and are keeping their investments there. Not much money is currently being transferred into the equity funds. Chairman Saul noted that the markets were down about one percent through September 12th. Ms. Ray stated that the DJIN was down about one percent, the NASDAQ was down 2.3 percent, the S Fund was down 3.4 percent, and the IEAFE Index was down 6.3 percent. Mr. Long noted that these are difficult markets but that we try to educate participants to understand that they must have long-term goals and those goals should include investing in equity.

Ms. Ray stated that all funds had positive returns in August except the I Fund. The I Fund's decline is mainly attributable to the increasing value of the dollar and not due to weaknesses in the foreign equity markets. Tracking error between the TSP Funds and the BGI Funds was zero in August due to the change to four decimal point pricing which eliminated tracking error due to rounding. All the L Funds posted positive returns in August. Only 67,910 interfund transfers were executed in August, the lowest number in years. Despite market volatility, the number of participants invested in the L Funds continues to rise.

c. Legislative Report.

Mr. Trabucco reported that Congress had convened a short session that is expected to run through September 26th. It is unlikely that the TSP legislation that was attached to the tobacco bill will move forward during this session because controversial legislation, like the tobacco bill, is unlikely to move in a short session. Congress is discussing holding a lame duck session and there is a chance the TSP legislation might be enacted then.

Mr. Trabucco then addressed the questions the members had raised at the last meeting regarding the Quadrennial Review of Military Compensation (QRMC) and the pilot program in the Army that provided matching contributions to soldiers in specified categories. The recommendations in the QRMC apply only to enlisted members. As the QRMC is reviewed throughout the Department of Defense, it is likely that many of the recommendations will change and be modified to include officer members. The Rand Corporation has completed a draft report on the effect of the Army's pilot matching program on recruitment and retention. Because the report is still in draft, it has not

been made available outside of the Army. Mr. Trabucco will provide the members with a copy of the report when it is finalized.

4. Acquisition of SI International by Serco, Inc.

Mr. Petrick reported that Serco, Inc. and SI International had reached an agreement whereby Serco, Inc. would acquire SI International for \$423 million. He did not expect that this acquisition would adversely affect TSP operations.

Serco, Inc., is a U.S. Corporation headquartered in Reston, Virginia. It is a subsidiary of the United Kingdom company, Serco. Serco, Inc. already has significant contracts with other Federal agencies including the Departments of Defense and Homeland Security. As a consequence, he anticipates this acquisition will not create security concerns such as typically arise when a foreign company purchases a U.S. Corporation that deals with U.S. agencies. Mr. Sanchez asked, when Mr. Petrick referred to security, he was referring to the Department of Commerce's authority to decide whether a foreign company may purchase a U.S. Corporation. Mr. Petrick replied that he was as well as the issues related safeguarding sensitive information. Mr. Sanchez asked whether Serco is privately held in the United Kingdom and was told it was a public company. This will allow us to report on its financials at the next Board member meeting. Mr. Petrick's initial review determined that it has strong financials.

Mr. Long noted that, after the acquisition, the same people who are currently working for the Agency will continue to work for the Agency at the same locations. The acquisition will not affect the TSP's day-to-day operations.

5. Preparing for an Emergency Transfer of TSP Assets.

Mr. Long reviewed the memorandum entitled "Preparing for an Emergency Transfer of TSP Assets" (attached). The Board had asked the Agency to conduct a "fire-drill" in the unlikely event that some circumstance arises that would require the Agency to move its funds to a different investment manager. He stated that we could transfer all assets that are not under the securities lending pool in three days. Transferring assets under the securities lending pool would take a little longer because we would need to determine the most efficient way to transfer those assets. Such a transfer would require some changes to the TSP's computer system. However, we could manually input all required data until we implemented the necessary

changes. Mr. Sanchez stated that it seems the Agency could make such a transfer with minimal interruption and was told that that is what we had concluded.

6. Annual Budget Report.

Mr. Long reviewed the memorandum entitled "Fiscal Year 2008 Projected Expenditures, Fiscal Year 2009 Budget, and Fiscal Year 2010 Budget Estimate" (attached).

He reported that the Agency projects that it will expend \$97.8 million in fiscal year (FY) 2008 which is \$10.6 million under the amount budgeted for FY 2008. Chairman Saul asked what the Agency had expended in FY 2007 and what it had expended on system modernization in FY 2008. He was told \$84 million and \$13.4 million respectively. He pointed out that the increase in 2008 was attributable to system modernization rather than other budgetary increases. Absent this, the Agency's budget was flat as compared to FY 2007.

Mr. Long stated that the Agency had expended less in FY 2008 than it had projected because its implementation of account numbers, annual statements, and interfund transfer restrictions among other things left insufficient time to implement all planned budget items. Chairman Saul asked how much of the planned system modernization was deferred until FY 2009 and was told approximately \$3.4 million. Mr. Long explained that much of the delay in system modernization was due to the unplanned move of the data center. Since this move will likely not be completed for six months, it makes sense to defer purchase rather than purchase now but not be able to install. He summarized FY 2008 by stating that several events came up which we were required to focus on. Nevertheless, we completed all essential business and improved the TSP dramatically. Mr. Sanchez added that we did so while at the same time keeping the operating environment secure. Chairman Saul said that it is important for the participants to understand that, if you deduct the costs attributable for system modernization, operating expenses for the TSP were unchanged from FY 2007.

Mr. Long reported that the Agency is proposing a budget of \$114.5 million in FY 2009. This represents an increase of \$6.1 million over the amount budgeted in FY 2008. This increase is due to deferred projects, projects to enhance security, and a general increase in prices. Chairman Saul asked how much of the FY 2009 budget would be attributable to system modernization and was told approximately \$6 million (\$3.4 mil-

lion in deferred projects as well as \$2.4 million for security initiatives). Chairman Saul noted that, if you subtract these one-time costs from the projected budget, the budget would be the same as last year's budget. Mr. Long agreed and added that he and the Agency's senior staff were very aware of their mandate to spend money solely in the interest of the participants and beneficiaries. These projected in expenditures are prudent.

Mr. Long then added that, if the pending TSP legislation is enacted, the Agency would incur some additional expenses. Proposed record keeping expenditures are \$4.1 million above the amount budgeted for FY 2008. Much of this is attributable to increased personnel support in the core activities of system engineering, quality assurance, and system security. Additionally, we are experiencing greater transaction costs as more and more Federal employees are retiring and withdrawing their funds from the TSP. We also have experienced an increase in death claims and in court order processing. Even though interfund transfers have decreased this year, the decrease has not led to a significant savings in processing costs because most interfund transfers are implemented via the web and do not require manual intervention.

We have budgeted \$6.3 million for participant communications in FY 2009, approximately \$700,000 less than in FY 2008. Chairman Saul asked about the status of the project to enhance the TSP website. Ms. Moran reported that a contractor had produced a plan and that Agency staff were deciding the implementation schedule for the planned upgrades. Once the schedule is set, we will begin implementing the enhancements. Mr. Long said that the bulk of the work on what the website should look like and should be capable of performing had been completed. Mr. Whiting asked whether the Agency would continue to maintain the www.tsp.gov website (the TSP's participant website) and www.frtib.gov website (the TSP's business website) separately or combine them. Ms. Moran explained that, because each website serves a different audience, we will keep them separate. Mr. Long stated that a significant portion of the budget for participant communications was for web redesign and that the project would be implemented in FY 2009. This budget item also includes \$2.6 million for postage. Mr. Sanchez asked whether we receive a discount for bulk mailing. Ms. Moran stated that we do but that the requirements for obtaining the discount are very stringent. She is working with Mr. Hagerty to ensure we have the necessary software to comply with these requirements.

Mr. Long reported that he was requesting an additional \$2.2 million for personnel in FY 2009. Chairman Saul how many staff members the Agency would need to hire to reach the number authorized. He was told thirteen (89 positions authorized, 76 positions filled). Mr. Whiting asked what these thirteen positions were for. They are for web design, content management, applications support, quality assurance, and security. Current staff is sufficient for critical work but not for all planned enhancements.

Mr. Long reported that we have tentatively budgeted \$118 million for FY 2010. This number will likely change, but, we are required by law, to submit a tentative FY 2010 budget to the Office of Management and Budget. Mr. Sanchez stated that the 2010 budget represents a real increase that is not due to one-time costs. He was told that this does reflect an increase in other costs. Chairman Saul asked what the Agency's budget was in Fiscal Years 2002/2003 and was told around \$100 or \$101 million. Chairman Saul pointed out that since then the amount of money under management has increased 2 ½ fold, we have added a million participants, we now have two call centers, a real-time back-up data center, and have added the L Funds. In essence, despite all these additions/improvements, if you subtract system upgrades, we are operating with the same budget as in 2002. Mr. Sanchez added that the Agency now has a deeper management bench. Chairman Saul agreed and stated that this Agency demonstrates that the government can run efficiently. This Agency is providing a better and safer service at a budget virtually the same as six years ago. Mr. Long added that, when compared to private-sector 401(k) plans, it is incredible how little the TSP charges its participants for administrative expenses. Chairman Saul stated that this is quite a record and the Executive Director and senior staff deserve the credit. What other Federal Agency could double its responsibility at the same budget it had six years ago? He noted that this is a very favorable budget and added that, he knows if Mr. Long can find ways to reduce it, he will do so.

Mr. Whiting asked what the FY 2009 budget would work out to in basis points. He was told it was 2.7 basis points gross, net of forfeitures, 1.4 basis points. Mr. Long pointed out that while we cannot control forfeitures, gross expenses have trended down while assets under management have increased. Combined, this allows the Agency to charge very little for administrative expenses. Chairman Saul and Mr. Sanchez remarked that the Agency should publish this news in the quarterly bulletins Ms. Moran's office sends out. Mr. Long replied that Ms.

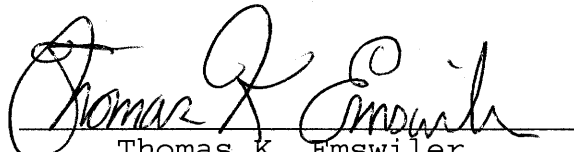
Moran has produced a slide that shows how the basis points the Agency charges to participants have reduced from 26-28 basis points at the TSP's inception to 1.4 basis points currently. Ms. Moran noted that this news will be transmitted to the participants in the annual letter Mr. Long sends to all participants in February. Mr. Long noted that the monthly participant activity report (attached) also shows gross and net administrative expenses going back to 2004. Here too, gross expenses have trended down from approximately 7 basis points to 3 basis points in 2008. Chairman Saul stated that while everyone seems to say the government cannot be run efficiently, this Agency proves that it can be.

Chairman Saul entertained a motion for approval of the fiscal year 2009 budget. The following motion was made, seconded, and adopted without objection:

MOTION: That the Agency's proposed fiscal year 2009 budget, as set out in the September 5, 2008 memorandum, be approved.

Whereupon, there being no further business, the following motion was made, seconded, and adopted without objection and Chairman Saul adjourned the meeting at 11:25 a.m.

MOTION: That this meeting be adjourned.


Thomas K. Emswiler
Secretary

Attachments

1. Thrift Savings Fund Statistics
2. August 2008 Performance Review - G, F, C, S, I, and L Funds
3. Preparing for an Emergency Transfer of TSP Assets
4. Fiscal Year 2008 Projected Expenditures, Fiscal Year 2009 Budget, and Fiscal Year 2010 Budget Estimate