

MINUTES
SCHOLARSHARE INVESTMENT BOARD

December 12, 2005, 1:00 p.m.
Teleconference

Chair Ted Eliopoulos called the meeting to order at 1:06 p.m.

Present: Ted Eliopoulos for Phil Angelides, State Treasurer
Tom Dithridge for Michael C. Genest, Department of Finance
Cathleen Cox for Alan Bersin, Office of the Secretary for Education
Allison Jones (departed at 2:28 pm)
Sabrina Kay (via phone)
Allison Levyn (via phone)
Maria Elena Serna

Staff: Carrie Douglas Fong, Executive Director, ScholarShare Investment Board (SIB)
Joanie Jones Kelly, Acting Executive Director, SIB
Don Sherman, Manager, SIB
Stanley Zeto, Analyst, SIB
Julia Bilaver, Staff Counsel, State Treasurer's Office

Consultants: John Charley, Pension Consulting Alliance, Inc.
Andrea Feirstein, AKF Consulting LLC (via phone)

TIAA-CREF: Phillip Rollock, Vice President, TIAA-CREF Tuition Financing, Inc. (TFI)
Doug Chittenden, Vice President, TFI Product Management
Karen Elinski, Senior Counsel, TFI
Chris Lynch, Regional Director, TFI
Kathleen Tunson, Marketing Director, TFI
Andrew Gradus, Business Analysis, TFI
Cindy Wilson, Program Manager, TFI
Christine Doyle, Attorney, TFI (via phone)
Lori Kalahar Johnson, Digitas

The Chair declared a quorum present.

Board Agenda Item Number One
Minutes from July 8, 2005 and August 29, 2005 Meetings

The minutes from the July 8, 2005 and August 29, 2005 ScholarShare Investment Board (SIB) meetings were approved as submitted.

Board Agenda Item Number Two
Staff Report

Ms. Carrie Douglas Fong, SIB, presented the Staff Report to the Board.

Ms. Douglas Fong reported that TIAA-CREF Tuition Financing, Inc. (TFI) and Staff have finalized both an interim and permanent process regarding stale dated checks for ScholarShare and the Governor's Scholarship Programs (GSP) and that these processes meet State regulations. Ms. Douglas Fong stated that there are no new updates regarding legislation or GSP. Ms. Douglas Fong reported that the Request for Proposals (RFP) for Program Manager for California's 529 college savings program was released on Friday, December 9, 2005.

Board Agenda Item Number Three
Appointment of Acting Executive Director for the ScholarShare Investment Board

Ms. Douglas Fong stated that Staff recommends that Ms. Joanie Jones Kelly be appointed as Acting Executive Director of SIB during her leave of absence. Ms. Douglas Fong introduced Ms. Jones Kelly to the Board and provided a brief overview, noting that Ms. Jones Kelly has over thirty years of experience with the State of California, most recently as the Executive Director of the California Industrial Development Financing Advisory Commission (CIDFAC).

Board Action:

Member Levyn moved to approve the appointment of Ms. Jones Kelly as Acting Executive Director of SIB. The motion was seconded by Member Kay and approved by the Board.

Board Agenda Item Number Four
TIAA-CREF Proxy Statement

Ms. Douglas Fong stated in addition to the analysis from Pension Consulting Alliance, Inc. (PCA), Staff has provided the Board with additional materials, including a copy of a letter from Mr. Phillip Rollock at TFI, stating that the apportionment between investments, marketing and administration would not change under the new investment agreement; and a revised Exhibit G from the proxy statement. Ms. Douglas Fong also noted that there is a change on the cover page of Agenda Item 4 (the last sentence in the first paragraph should state that three, not two, actively managed funds had fee increases).

Ms. Douglas Fong asked TFI to explain what would happen if the new agreement does not pass. Mr. Doug Chittenden, TFI, stated that if the new agreement passes, the amount of the underlying mutual fund fees will increase, and if it does not pass, TIAA-CREF will close current funds to new money and have the new money invested in replacement funds and that the fees for the replacement funds will be identical to those in the new agreement.

Chair Eliopoulos stated that in the written analysis provided by PCA and SIB Staff, both PCA and Staff conclude that TIAA-CREF provided sufficient information to support the fee increases, and recommend supporting the new agreement because it is in the best interest of our shareholders.

Board Action:

Member Dithridge moved to approve TIAA-CREF's new management agreement with Teachers Advisors, Inc. for the actively-managed funds in the ScholarShare portfolio. The motion was seconded by Member Serna and approved by the Board.

Board Agenda Item Number Five
Consideration of Changes to the Maximum Account Balance Limit for the Golden State ScholarShare College Savings Trust

Ms. Douglas Fong stated that the maximum account balance limit is set annually by the Board and that Staff recommends increasing this limit from \$285,000 to \$300,000.

Board Action:

Member Cox moved to approve increasing the maximum account balance limit for ScholarShare from \$285,000 to \$300,000. The motion was seconded by Member Kay and approved by the Board.

Board Agenda Item Number Six
Consideration of Changes to the Asset Allocation and Age Bands for the Age-Based Options for the Golden State ScholarShare College Savings Trust

Ms. Douglas Fong stated that the age bands and asset allocation of the investment options for ScholarShare are reviewed annually. Ms. Douglas Fong reported that TFI completed an analysis of the current asset allocation, but does not recommend any changes. The age bands for the Age-Based and Aggressive Age-Based Asset Allocation Options do need to be updated annually, and this item would add a new band for beneficiaries born in 2006 and 2007 and consolidate the two oldest age bands.

Board Action

Member Dithridge moved to approve the changes to the age bands used for the Age-Based and Aggressive Age-Based Asset Allocation Options. The motion was seconded by Member Jones and approved by the Board.

Board Agenda Item Number Seven
Consideration of Changes to the Statement of Investment Policy for the Golden State ScholarShare College Savings Trust

Ms. Douglas Fong stated that as part of writing the RFP for a college savings program manager, PCA, AKF Consulting LLC (AKF), and Staff reviewed both the Investment Policy and the Fund Monitoring Procedures and Criteria. Ms. Douglas Fong reported that in developing the proposed changes to the Investment Policy, PCA, AKF and Staff reviewed investment policies for other state 529 programs and revised the Investment Policy to more clearly define ScholarShare's investment objectives and establishes policies and procedures. Ms. Douglas Fong stated that a draft of this revised Investment Policy has been included in the RFP for a college savings program manager and that, if approved, this revised Investment Policy would go into effect upon passage.

Member Serna inquired whether this is the first time the Investment Policy has been reviewed. Ms. Douglas Fong responded that, although the Investment Policy is reviewed annually, this is the first substantial review. Mr. John Charley, PCA, stated that annual changes, such as changes to asset allocation or age bands, can be made to the addendum to the Investment Policy and that the Investment Policy content would remain intact, but would be reviewed as needed.

Member Cox recommended making "Investment Consultant", on page 3, reflect that it may be plural, and Member Dithridge recommended changing the word "submit", in the second bullet under "Asset Allocation" on page 4, to "submitting." The Board agreed with these proposed changes.

Board Action:

Member Serna moved to adopt the revised Investment Policy for ScholarShare with the recommended minor changes proposed by Members Cox and Dithridge. The motion was seconded by Member Levyn and approved by the Board.

Board Agenda Item Number Eight
Consideration of Changes to the Fund Monitoring Procedures and Criteria for the Golden State ScholarShare College Savings Trust

Ms. Douglas Fong reported that the recommended changes to the Fund Monitoring Procedures and Criteria (Procedures) for ScholarShare have the same goals as the current Procedures. The revisions make the Procedures less vendor specific and provide additional clarification. Ms. Douglas Fong stated that these changes, if approved by the Board, would go into effect upon passage.

Board Action:

Member Dithridge moved to approve the recommended changes to the Fund Monitoring Procedures and Criteria for ScholarShare. The motion was seconded by Member Cox and approved by the Board.

Board Agenda Item Number Nine
Review of TIAA-CREF's Second Quarter and Third Quarter 2005 Investment Performance

Ms. Douglas Fong stated that the International Equity Fund has moved from caution to positive as of the third quarter and that the Large Cap Value Fund and Small Cap Equity Fund are currently on caution status.

Mr. Charley stated that though these funds have underperformed during the last two quarters, the time period is relatively short at this point since they have only been funded since March. Mr. Andrew Gradus, TFI, stated that the basis points for the Large Cap Value Fund have improved during the month of November and that it is a five star rated fund. Member Cox inquired about other reasons for underperformance besides timing. Mr. Gradus responded that this fund is actively-managed and noted some environmental factors, such as gas prices, hurricanes and energy problems, and consumer factors. Member Cox inquired as to how long this team has been in place. Mr. Gradus stated that this information was not available, but that he would follow up.

Member Kay inquired about the International Equity Fund's allocation within the ScholarShare portfolio and Mr. Gradus stated that it ranges from about 20% to 5%. Additionally, Ms. Douglas Fong stated that the allocation for the Age-Based Asset Allocation Option, the Aggressive Age-Based Asset Allocation Option and the 100% Equity Option are about 4% - 16%, 6% - 20%, and 20%, respectively. Member Kay inquired about whether the allocations would change. Mr. Gradus stated that the allocation would not change and that analysis has been done to determine the appropriate amounts. Member Cox inquired if additional resources from the fee increases would be applied to these funds. Mr. Phillip Rollock, TFI, added that part of the mutual fund increase will go to enhancing TFI's resources and attracting the best talent.

Board Agenda Item Number Ten
Review of TIAA-CREF Tuition Financing, Inc.'s 2005 Administrative Performance

Mr. Don Sherman, SIB, provided an update of TFI's 2005 administrative performance and stated that there has been some improvement in performance. Mr. Sherman stated that ideally it would be

beneficial to wait to review performance through the end of the year prior to doing additional analysis. Chair Eliopoulos stated that the Board has worked hard to gather this information and appreciates the continued improvement in performance, and will continue to observe the six criteria that are significantly underperforming the benchmark.

The Board inquired about underperformance in specific areas including Reporting and New Account Set-Up Accuracy. Member Dithridge inquired about what typographical errors were made during account set-up. Ms. Cindy Wilson, TFI, stated that TFI has increased its performance in this area from 74% to 94%, but that it still remains difficult to reach the 97% benchmark. In regards to the type of typographical errors, Ms. Wilson stated that the information was not available, but that she would follow up and report back to the Board at the next meeting.

Board Agenda Item Number Eleven

Review of TIAA-CREF Tuition Financing, Inc.'s 2005 Marketing Performance

Ms. Douglas Fong stated that there was an error on page 3 of Attachment 2 and that an errata sheet has been provided by TFI for the Board's information. Ms. Douglas Fong requested that TFI include both an errata sheet and a replacement page for future items that require correction. Ms. Douglas Fong stated that Staff has provided TFI with comments on its marketing reports and marketing plan and requested that they be more concise. Mr. Sherman stated that TFI has provided a number of items, including many marketing pieces, that contain extensive grammatical errors and require additional proofreading.

Ms. Andrea Feirstein, AKF, commented on TFI's marketing performance and stated that account generation continues to lag and that the annual total of unique accounts opened is just under 35% of where account generation should reside. Ms. Feirstein stated that TFI has met the annual benchmark in terms of total assets collected and anticipated that this number will reach about \$360 million by the end of the year. With regards to the satisfaction rate, Ms. Feirstein stated that although it does meet the benchmark of less than 2% accounts closed due to rollovers, it has increased from last year, which indicates greater dissatisfaction.

Ms. Feirstein commented that we should question whether the marketing dollars should be re-directed to the marketing efforts that have performed more successfully. Ms. Feirstein stated that the web seminar was a great idea, but that the technical problems appeared to have made it much less effective and that it needs to be reviewed before future use. Ms. Feirstein stated that after reviewing the 3rd Quarter Marketing Initiatives Report, it remains difficult to draw conclusions about the web seminar in terms of participation, costs, and the number of accounts opened.

Ms. Kathleen Tunson, TFI, stated that TFI is working aggressively to improve its proofreading process and that it has hired and has in place a new service company, Digitas. Ms. Lori Kalahar Johnson, Digitas, stated that it will be taking over reporting for the 529 program and that it has a very robust strategy, which includes more frequent year-to-year comparisons and formal analysis results by campaign.

Board Agenda Item Number Twelve

TIAA-CREF Tuition Financing, Inc.'s 2006 Marketing Plan

Ms. Feirstein provided comments on TFI's 2006 Marketing Plan and stated that the plan should be tailored specifically to California, given the size and significance of the state. Ms. Feirstein stated that in the past, TFI has committed to a marketing budget above the contracted amount, and that for the 2006 marketing budget, it has committed to the contracted amount. Ms. Feirstein inquired about what results can be expected with a budget decrease of about 40%. Mr. Lynch responded that the

marketing budget for 2006 is about \$3 million, but that this amount is for 2006 through the month of October.

Ms. Kalahar Johnson provided the Board with additional details about the marketing plan and stated that Digitas is performing new tests, promotions and campaigns to gather names and to educate the public about the 529 plan. Ms. Tunson stated that they are shifting their target audience to the parents with children 0-6 years of age in their marketing efforts. Ms. Kalahar Johnson stated that there are many of the same marketing strategies as the current year, but that it recommends an emphasis on where parents are in their life stage.

Member Kay commented on the 2006 strategy to allocate a portion of the marketing budget from acquisition to account owners to increase the average account size. Member Kay stated that it would make sense to have more Californians benefiting from ScholarShare. Mr. Sherman agreed that the number of total accounts needs to be increased, with a strategy to simultaneously increase the assets held with current account owners.

Member Cox commented that the information provided is not as detailed as anticipated and inquired about what changes are in place to make up the account generation this past year. Mr. Rollock stated that Digitas has strong marketing capability and changes will be made quickly. Member Serna inquired about when TFI would be able to get the Board information about what works, and what needs to be done to make it work. Ms. Kalahar Johnson stated that the data will be provided as soon as possible.

Chair Eliopoulos stated that the Board really needs a tracking device, or some way to measure the changes and whether they are working or not. Chair Eliopoulos stated that in the end, we fall back to annual benchmarks, and that it would be helpful to propose something new and point us somewhere. Ms. Douglas Fong stated that annual marketing information for 2005 should be available at the next meeting.

Board Agenda Item Number Thirteen
ScholarShare Investment Board 2006 Meeting Calendar

Ms. Douglas Fong stated that because the RFP went out on December 9, the March 2006 meeting is likely to be re-scheduled. Member Dithridge recommended having a separate SIB meeting to address the RFP.

Public Comment

Chair Eliopoulos called for public comment. There was none.

There being no further business before the Board, the Chair adjourned the meeting at 2:45 p.m.

Respectfully submitted by,

Carrie Douglas Fong, Executive Director
SCHOLARSHARE INVESTMENT BOARD