

AGENDA ITEM 2.

APPROVAL OF MINUTES OF THE OCTOBER 16, 2014 MEETING

Submitted for: Action

Summary: This report includes the detailed minutes of the meeting held on October 16, 2014.

Action requested: The Commission approve the minutes of the October 16, 2014 meeting.

MINUTES OF A JOINT MEETING
OF THE
ILLINOIS STUDENT ASSISTANCE COMMISSION
AND THE
INVESTMENT COMMITTEE

DePaul University
DePaul Center – Room 8002
1 E. Jackson Boulevard
Chicago, IL

October 16, 2014

COMMISSIONERS PRESENT: Kym Hubbard, Chair
Miguel del Valle
Mark Donovan, Investment Committee Member
Kendall Griffin, Audit Committee Member
Kevin Huber, Investment Committee Member
Verett Mims, Investment Committee Member
Paul Roberts, Audit Committee Member
Kim Savage, Audit Committee Member

COMMISSIONER ABSENT: Mawi Asgedom

STAFF PRESENT: Eric Zarnikow, Executive Director
Lynne Baker, Managing Director of Communications
Ramnath Cidambi, Managing Director, Information Technology
Carol Cook, Director, Program Services and Compliance
Kent Custer, Chief Investment Officer
Kishor Desai, Director, Internal Audit
Wendy Funk, Director, Accounting
Katharine Gricevich, Director, Government Relations
Sandra Houston, Director, College Illinois![®] Prepaid Tuition Program
Shoba Nandhan, Chief Financial Officer
Roger Rojas, Investment Analyst
Karen Salas, General Counsel
Debora Calcara, Commission Secretary

PUBLIC ATTENDANCE: Ryan Ball, Callan Associates
Eric Hiatt, Illinois Board of Higher Education
Nicole Niwa, Illinois House of Representatives
Brienne Weymouth, Callan Associates

Item 1. Announcements

Chair Hubbard brought the October 16, 2014 joint meeting of the Commission and the Investment Committee to order at 2:00 p.m. and asked that a roll call be taken, which established a quorum was present for the Commission and the Investment Committee.

Chair Hubbard noted the Commissioners have been provided potential meeting dates for 2015 and asked that they contact the Commission Secretary if they had conflicts with the dates. She noted action will be taken to adopt the 2015 meeting dates at the next meeting of the Commission which is scheduled for November 14 at Roosevelt University.

Item 2. Minutes of the July 22, 2014 Meeting

Ms. Savage **MOVED THAT** the Commission approve the minutes of the July 22, 2014 meeting.

Mr. Griffin seconded the motion, which was approved unanimously.

Item 3. Executive Director Report

Mr. Zarnikow briefly reviewed the financial statements provided in the agenda book. In addition, he provided the Commissioners with updates on the “Pay It Forward” study that ISAC is preparing for the General Assembly and activities and priorities related to the FY16 Budget submission that will be shared with the Commissioners at the November meeting as an information item. He also noted that October is College application Month and provided an update on related ISAC activities.

Let the record reflect Mr. del Valle joined the meeting in progress.

Item 4. College Illinois! Prepaid Tuition Program Investments

Item 4A. Approval of Minutes of the August 27, 2014 Meeting of the Investment Committee

Ms. Mims, member of the Investment Committee, **MOVED THAT** the Committee approve the minutes of the August 27, 2014 meeting.

Mr. Donovan, member of the Investment Committee, seconded the motion, which was approved with Mr. Huber abstaining.

Item 4B. Investment Update

Mr. Custer gave a brief overview of the information provided in the agenda book.

Item 4C. Approval of the Absolute Return Asset Class Structure

Mr. Custer reminded the Commission that Balestra Spectrum Partners had been placed on the watch list in May due to organizational changes. He stated that after conversations with the management of Balestra Spectrum Partners he feels the Commission should continue with the termination of Balestra Spectrum Partners following final distribution of redemption proceeds. He then discussed the proposed absolute return asset class structure change.

Mr. Huber asked if the option to not reinvest in the absolute asset class was considered. Mr. Custer responded that this option was considered, but was not deemed the most prudent course of action. He noted

that the role and allocation of each asset class was evaluated in depth as part of the asset allocation and investment policy update approved by the Commission in July. Mr. Custer stated his belief that it was important to adhere to the asset allocation discipline. Ryan Ball of Callan Associated indicated their support for reinvesting in the asset class.

Mr. Donovan **MOVED THAT** the Commission approve the termination of Balestra Spectrum Partners following final distribution of redemption proceeds.

Ms. Mims seconded the motion, which was approved via roll call vote.

Mr. Donovan **MOVED THAT** the Commission approve the proposed absolute return asset class structure with a 60% target weight for the Neuberger Berman Diversified Arbitrage Fund and a 40% target weight for the Pinnacle Natural Resource fund and reevaluate the absolute return allocation as part of next year's asset allocation study.

Mr. Huber seconded the motion, which was approved via roll call vote.

Item 5. College Illinois! Prepaid Tuition Program Contract Prices and Fees for 2014-2015 Enrollment Period

Mr. Zarnikow introduced the agenda item by providing a brief sales history of previous enrollment periods. He stated that the pricing strategy for the recent enrollment periods, after the plan had begun to sell contracts again, had been to minimize price increases to improve the affordability of the plans and reduce the difference between contract prices and current tuition costs. Recently there has been a moderation of tuition and fee growth and that moderation is expected to continue. While this is good news for the plan's funded status, it dramatically slows the narrowing between current tuition and contract pricing. He stated the recent contract sales have not been at a level to sustain the long term future of the plan and that the moderation in tuition and fee increases provides the opportunity to rethink contract prices.

Mr. Zarnikow stated that after a lot of work and consideration by the team, they are proposing to substantially reduce contract prices for the upcoming enrollment period to make the contracts more affordable for the people of Illinois, while also being appropriate for the long term financial soundness of the plan. He indicated the proposed pricing will offer different contract pricing at each age up to ninth grade and above ninth grade all the prices will be the same. The prices better reflect the economics of the contract at each age category and because the prices are lower for younger children they could encourage parents to buy contracts earlier. He also noted the installment payment options have changed to be more flexible, but the down payment options continue the same as previous enrollment periods.

In addition, Mr. Zarnikow indicated that the team felt it was appropriate to adjust the contract price for contract holders who purchased in recent years at a higher price. He stated based on current estimates that the impact of the price adjustment for current contract holders would be less than a 1% reduction in the funded status of the plan.

Mr. Zarnikow stated that in working with the plan's actuaries, they have estimated that approximately 25 percent more contracts will need to be sold overtime to offset the cash flow impact on the plan of the reduced contract prices. He stated that the key business judgment to be made is do we feel the lower pricing will help drive at least 25% more contract sales compared to the current contract pricing.

Chair Hubbard applauded staff on their work and the difficult issues they have been charged with. She feels the Commissioners have been successful in the mission they were charged with when appointed to the Commission which included; providing greater transparency, establishing a glide path for a more

appropriate asset allocation, increasing the funded status of the portfolio, and hiring more competent management and investment professionals to run the agency. Chair Hubbard feels everything is moving in the right direction. She stated that the fact that staff is willing to try to adjust pricing is significant and the right thing to do.

Chair Hubbard requested that the Commission seriously consider all the options and potential unintended consequences of approving the new pricing structure as it required “giving back” a small portion of the increased funded status. She noted that if the price reduction is successful in increasing the number of contract sales, as price has frequently been mentioned as an obstacle by contract holders, Commissioners and the Legislature, then a small step back is worth it to move the Plan forward. Although as an investment professional any decrease in the funded status is always a little uncomfortable.

Responding to Chair Hubbard, Mr. Zarnikow stated that based on the actuarial report as of June 30, 2013, it was estimated that the plan needs to sell approximately 1,500 per year to maintain the cash flow of the plan. He stated that the plan will need to sell approximately 25% more contracts, or 1,900-2,000, per year with the new reduced pricing. While there will be a strong marketing plan for the upcoming enrollment period, he did indicate there are obstacles that may impact the success of the plan, including the plan’s previous reputation, the overall fiscal condition of the state, and the rate of the tuition and fee growth, may make people unable or unwilling to purchase a contract. He feels the reduced prices and the flexibility in payment options should help drive contract sales.

Referring to the price adjustments being given to current contract holders, Chair Hubbard inquired how many price adjustments will be made. Mr. Zarnikow confirmed an estimated 1,500 contracts may be affected by the pricing adjustment, noting that the bulk of those were purchased over the last three enrollment periods. Chair Hubbard recommended to staff that they confirm there would be no negative tax consequences to contract holder that may receive a refund. She directed staff to secure a legal opinion, preferably in writing, on the tax implication, prior to issuing refunds. Mr. Zarnikow responded, based on ISAC’s initial conversations with legal counsel, no tax consequences are anticipated.

Ms. Salas indicated they have received legal counsel and will be getting a tax opinion and that we believe there are no tax implications at the federal level. However, the price adjustment will generally be taxable at the state level to the extent the contract holder took a state tax deduction. Chair Hubbard asked that the contract holder receiving a refund be notified of the State tax issue in advance.

Commissioner del Valle commended staff on the work done on the pricing proposal and feels the marketing effort of the past enrollment period should continue. He stated the message should be to position their children to compete in tomorrow’s job market either through a community college or a four year institution. He feels the message should be positive showing that this is in their best interest as this is a way you can save for college. Commissioner del Valle offered to personally assist in the marketing effort.

After further discussion, Mr. Zarnikow stated that we will have the marketing firm provide a presentation on the new enrollment effort at the November Commission meeting.

Chair Hubbard asked for a motion to approve the contract pricing, fees and adjustments as set forth in the agenda item for the College Illinois! Prepaid Tuition Program enrollment period beginning on November 18, 2014 and ending on April 30, 2015.

Mr. Donovan **SO MOVED**, Ms. Savage seconded the motion, which was unanimously approved via roll call vote.

Item 6. Audit Committee Update

Ms. Savage, Chair of the Audit Committee, provided a brief update on the Audit Committee meeting held prior to the Commission meeting.

Item 7. Public Comment

Chair Hubbard asked if anyone from the public wished to address the Commission. There were no comments from the public.

Ms. Savage **MOVED THAT** that the October 16, 2014 meeting be adjourn, Mr. Griffin seconded the motion, which was approved unanimously. The meeting adjourned at 3:11 p.m.

Respectfully submitted,

A handwritten signature in cursive script that reads "Debora A. Calcara". The signature is written in black ink on a light-colored background.

Debora A. Calcara
Secretary to the Commission