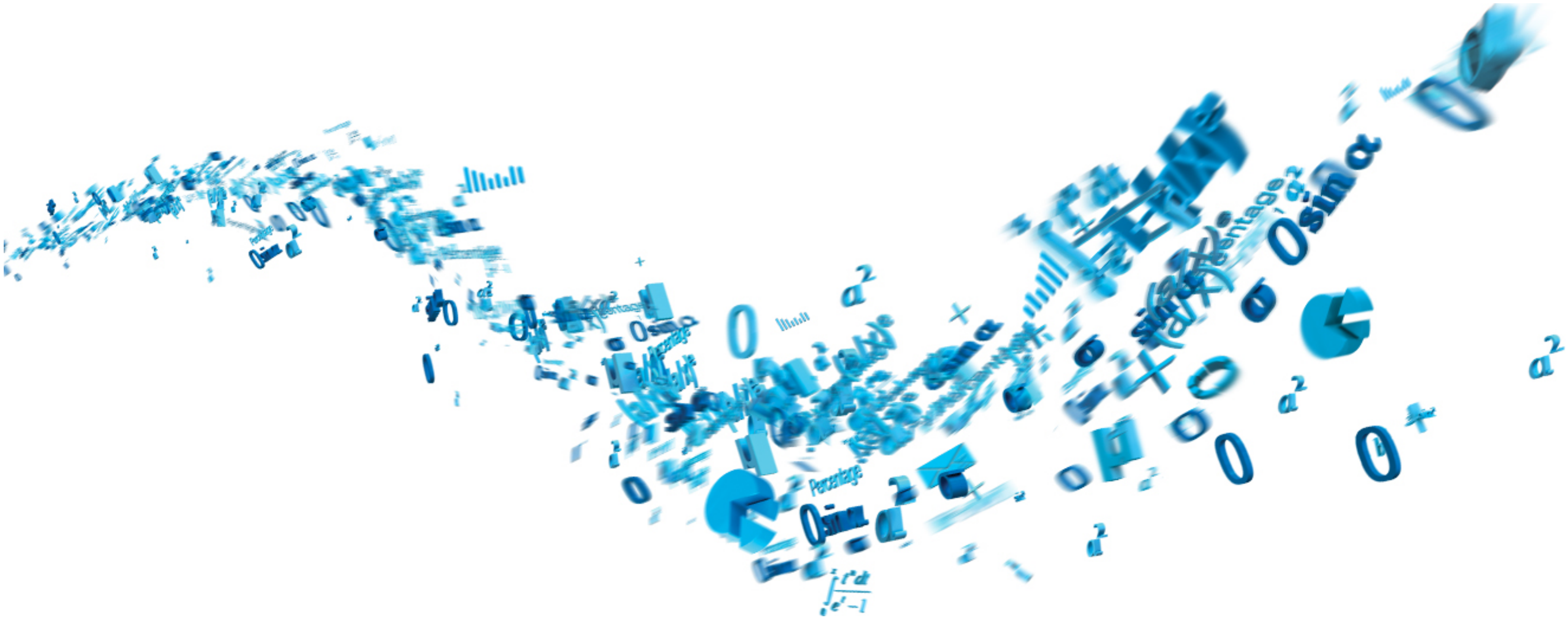

# Nevada System of Higher Education
## First Quarter 2016 Discussion Guide

May 20, 2016

**Aon Hewitt**
Retirement and Investment



Empower Results®

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# Discussion Topics

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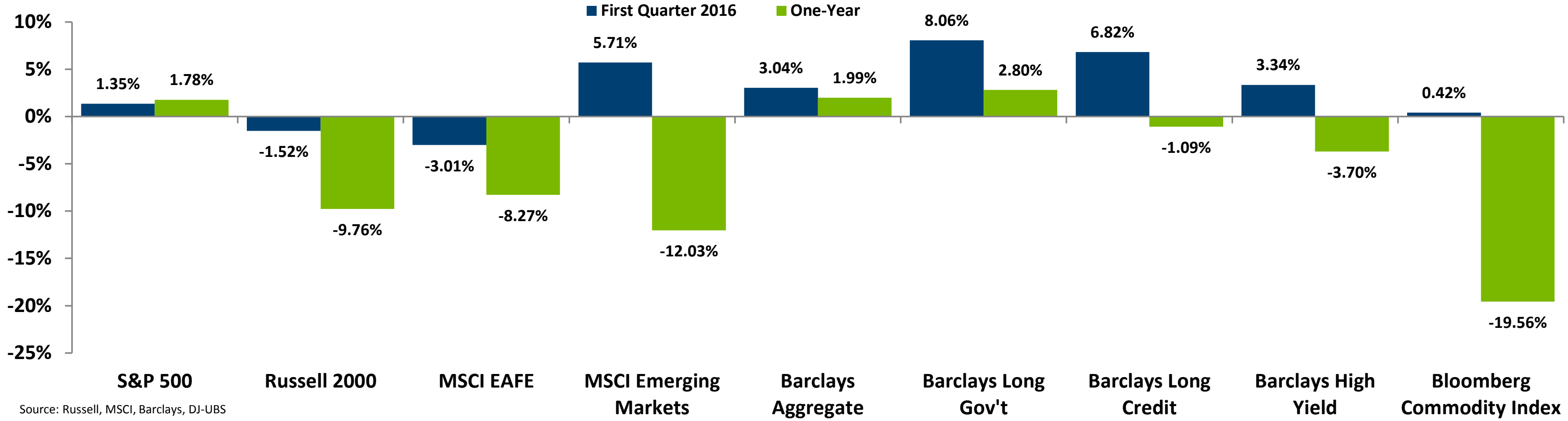
# Agenda Tracker

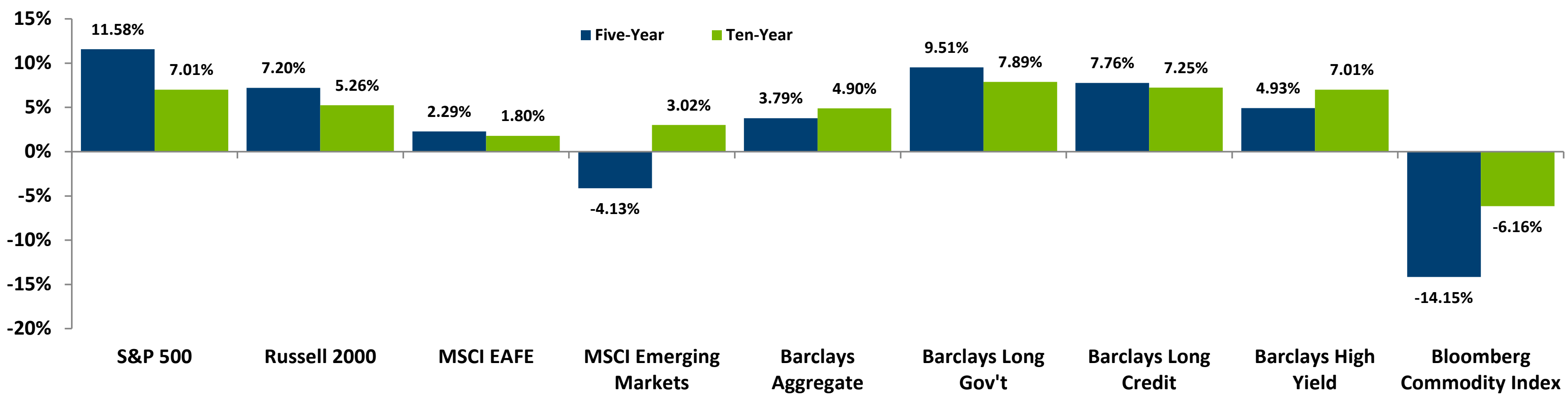
# Market Highlights

SHORT TERM RETURNS
AS OF 03/31/2016




Source: Russell, MSCI, Barclays, DJ-UBS

LONG TERM ANNUALIZED RETURNS
AS OF 03/31/2016



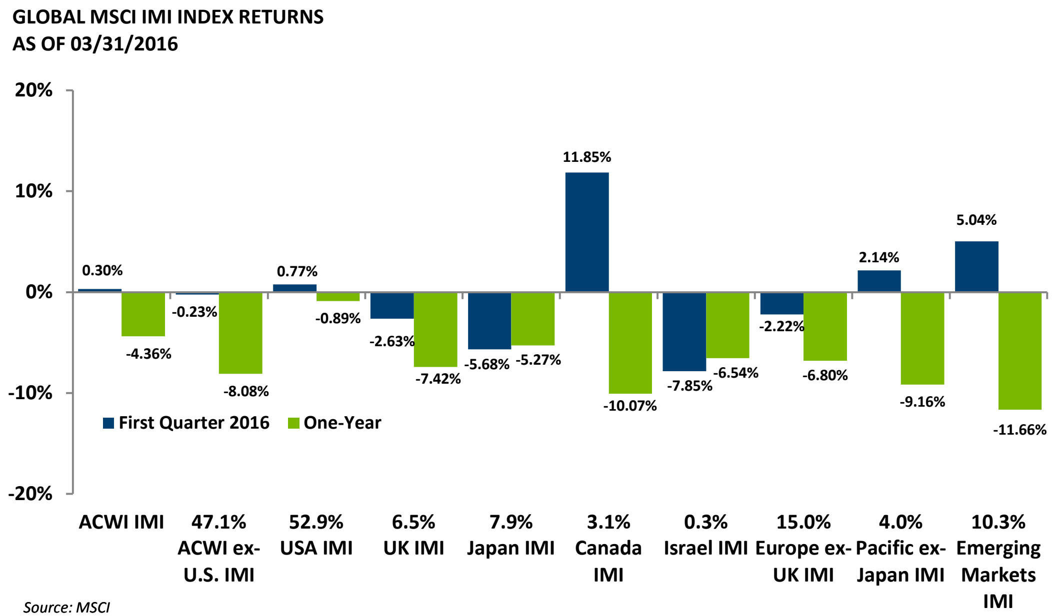

Source: Russell, MSCI, Barclays, DJ-UBS

# Market Highlights

| Returns of the Major Capital Markets | | | | | |
|---|---|---|---|---|---|
| | | | | | Periods Ending 03/31/2016 |
| | First Quarter | 1-Year | 3-Year[1] | 5-Year[1] | 10-Year[1] |
| **Equity** | | | | | |
| MSCI All Country World IMI | 0.30% | -4.36% | 5.59% | 5.24% | 4.26% |
| MSCI All Country World | 0.24% | -4.34% | 5.53% | 5.22% | 4.08% |
| Dow Jones U.S. Total Stock Market | 0.91% | -0.43% | 11.06% | 10.97% | 7.01% |
| Russell 3000 | 0.97% | -0.34% | 11.15% | 11.01% | 6.90% |
| S&P 500 | 1.35% | 1.78% | 11.82% | 11.58% | 7.01% |
| Russell 2000 | -1.52% | -9.76% | 6.84% | 7.20% | 5.26% |
| MSCI All Country World ex-U.S. IMI | -0.23% | -8.08% | 0.76% | 0.58% | 2.19% |
| MSCI All Country World ex-U.S. | -0.38% | -9.19% | 0.32% | 0.31% | 1.94% |
| MSCI EAFE | -3.01% | -8.27% | 2.23% | 2.29% | 1.80% |
| MSCI EAFE (Local Currency) | -6.52% | -11.17% | 6.47% | 6.20% | 1.73% |
| MSCI Emerging Markets | 5.71% | -12.03% | -4.50% | -4.13% | 3.02% |
| **Fixed Income** | | | | | |
| Barclays Global Aggregate | 5.90% | 4.56% | 0.87% | 1.80% | 4.35% |
| Barclays Aggregate | 3.04% | 1.99% | 2.51% | 3.79% | 4.90% |
| Barclays Long Gov't | 8.06% | 2.80% | 6.04% | 9.51% | 7.89% |
| Barclays Long Credit | 6.82% | -1.09% | 4.10% | 7.76% | 7.25% |
| Barclays Long Gov't/Credit | 7.30% | 0.38% | 4.81% | 8.51% | 7.57% |
| Barclays US TIPS | 4.45% | 1.52% | -0.70% | 3.03% | 4.62% |
| Barclays High Yield | 3.34% | -3.70% | 1.85% | 4.93% | 7.01% |
| Citi Group Non-U.S. WGBI | 9.10% | 7.74% | -0.16% | 0.24% | 3.97% |
| JP Morgan EMBI Global (Emerging Markets) | 5.22% | 4.36% | 2.43% | 5.97% | 7.11% |
| **Commodities** | | | | | |
| Bloomberg Commodity Index | 0.42% | -19.56% | -16.87% | -14.15% | -6.16% |
| Goldman Sachs Commodity Index | -2.50% | -28.67% | -24.49% | -17.43% | -10.66% |

MSCI Indices show net returns
All other indices show total returns
[1]Periods are annualized

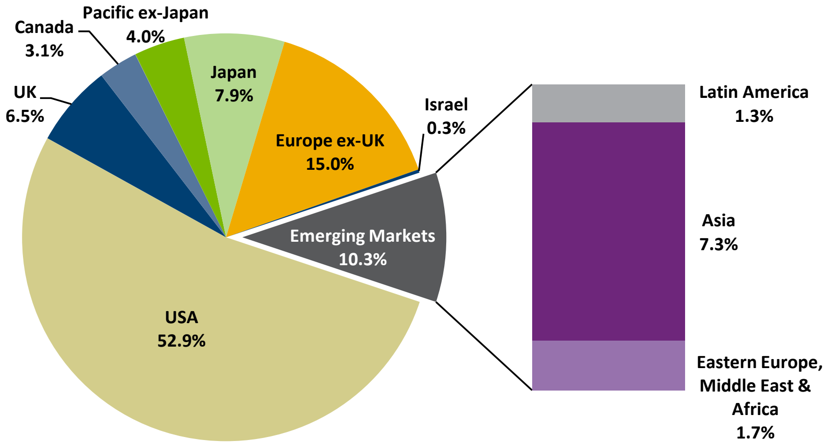
# Global Equity Markets




- Global equities got off to a rocky start in 2016 as renewed concerns over subdued Chinese economic growth, a weaker Chinese yuan, deteriorating economic data globally, and falling commodity prices spooked equity market investors. However, the markets reversed course during the second-half of the quarter following a rebound in energy prices. Further easing moves and dovish statements by the major central banks also fueled the market. Global equity markets returned 0.30% during the first quarter with notable differences in regional returns.
- Canada was the best performer with a return of 11.85% as equities rose on the back of strong Q4 2015 GDP data and rising energy stocks. A strong Canadian dollar pushed up the returns for U.S. based investors.

# Global Equity Markets

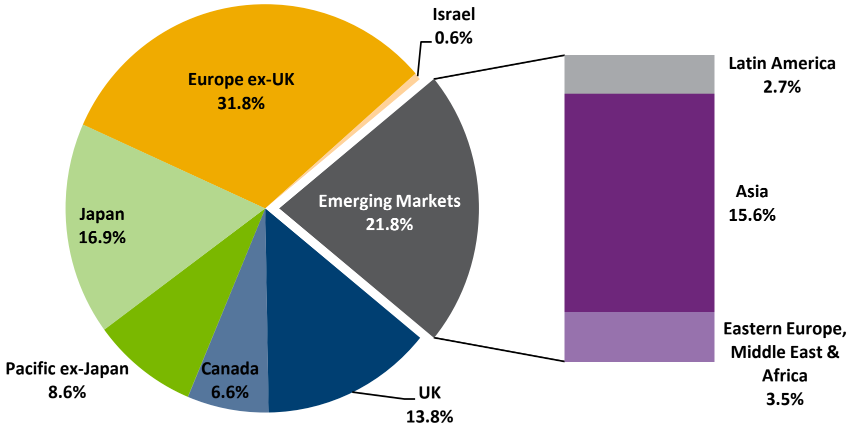
**MSCI ALL COUNTRY WORLD IMI INDEX**
**GEOGRAPHIC ALLOCATION AS OF 03/31/2016**




*Source: MSCI*

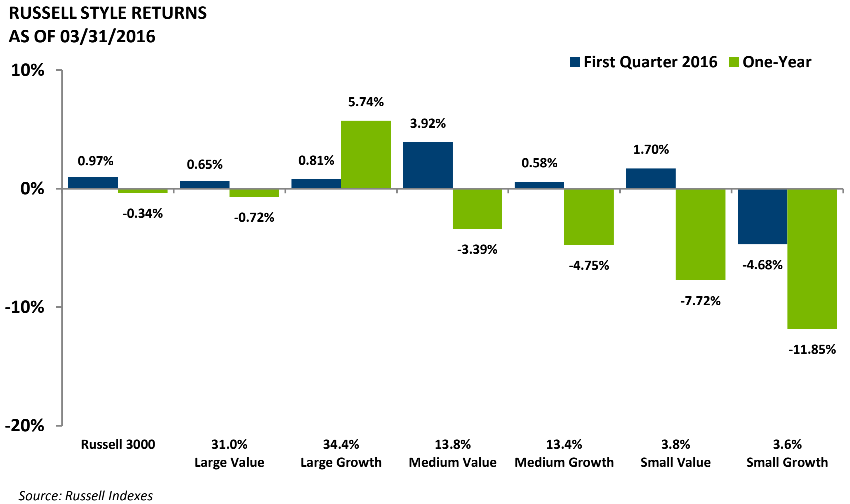
- The two exhibits on this slide illustrate the percentage that each country/region represents of the global equity market as measured by the MSCI All Country World IMI Index and the MSCI All Country World ex-U.S. IMI Index.

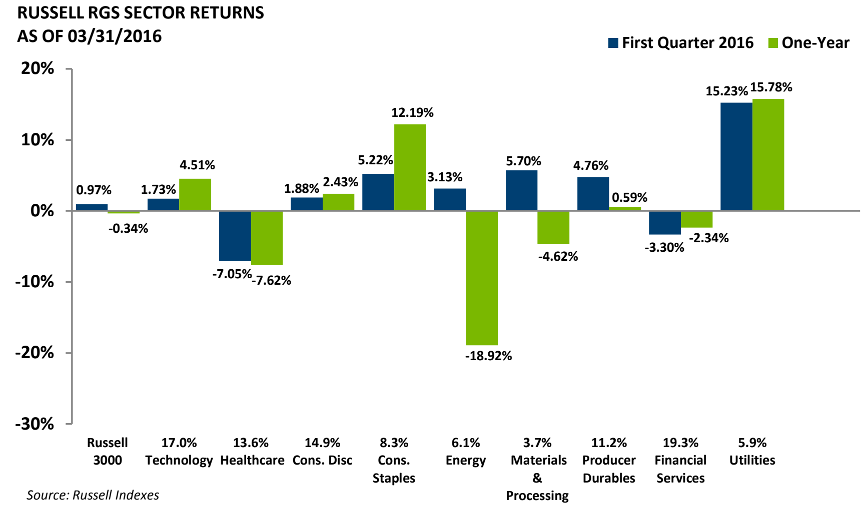
**MSCI ALL COUNTRY WORLD EX-U.S. IMI INDEX**
**GEOGRAPHIC ALLOCATION AS OF 03/31/2016**




*Source: MSCI*

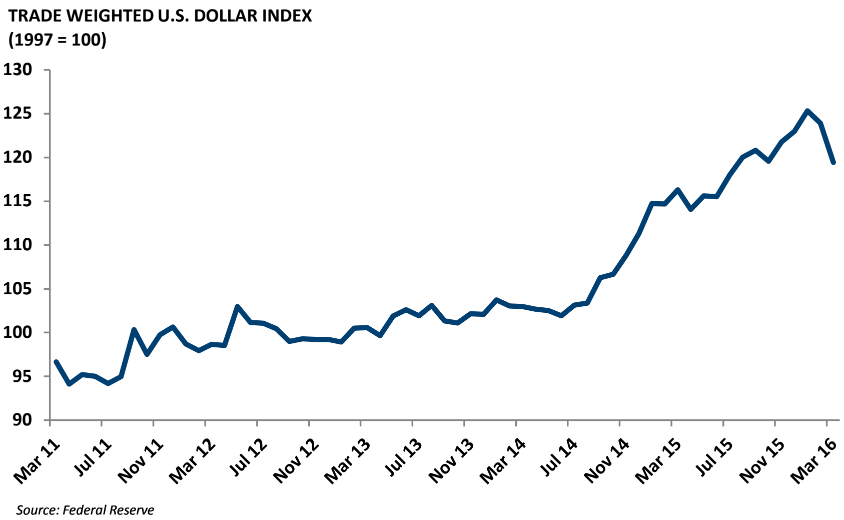
# U.S. Equity Markets

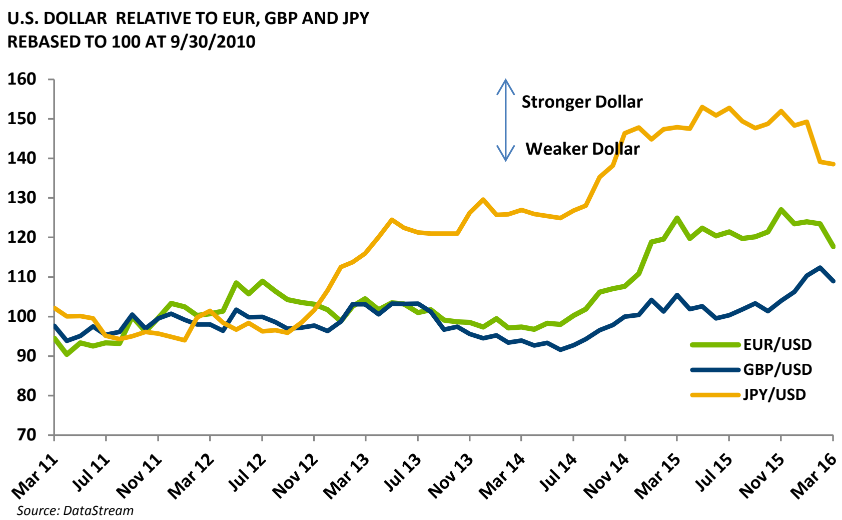



- The Russell 3000 Index returned 0.97% during the first quarter and returned -0.34% over the one-year period.
- During the first quarter, utilities was the strongest performer, posting returns of 15.23%. The health care and financial services sectors were the weakest performers, producing returns of -7.05% and -3.30%, respectively.
- Performance across the market capitalization spectrum was positive over the quarter except for small cap growth stocks. Medium cap stocks outperformed both the larger and smaller segments of the markets. Value stocks outperformed growth stocks across the capitalizations except for the larger segments.

# Currency

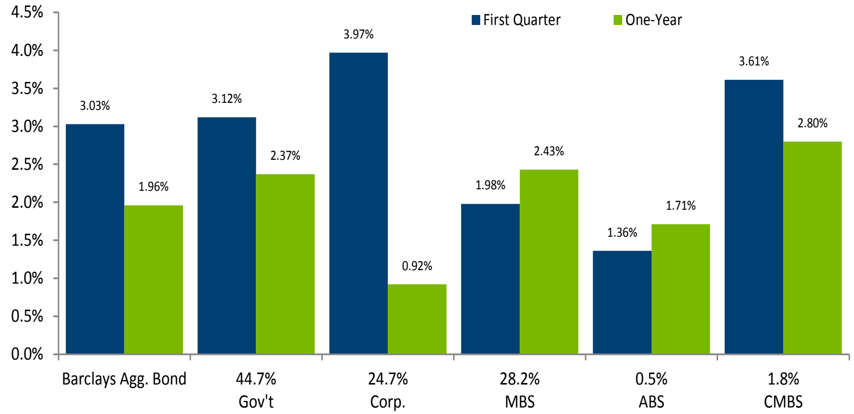



- As measured through the broad trade weighted U.S. dollar index, the U.S. dollar weakened during the quarter.
- The U.S. dollar depreciated sharply against the euro and the yen but appreciated against the pound. The pound weakened due to uncertainty over “Brexit” and downgrade of economic growth forecasts.
- Despite the Bank of Japan’s easing measures, the yen appreciated sharply against the dollar.

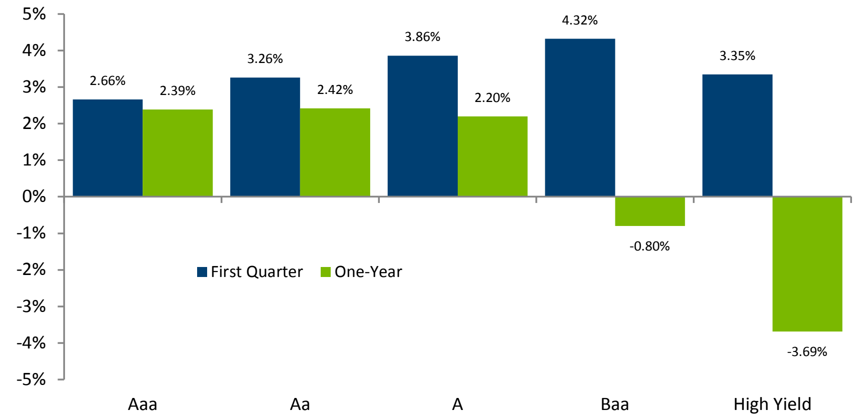
# U.S. Fixed Income Markets

**BARCLAYS AGGREGATE RETURNS BY SECTOR**
**AS OF 3/31/2016**




*Source: Barclays Live*

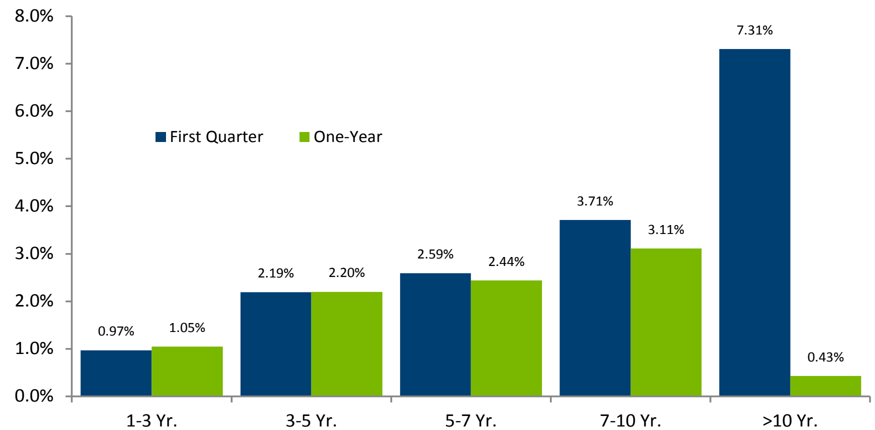
**BARCLAYS AGGREGATE RETURNS BY QUALITY AND HIGH YIELD RETURNS**
**AS OF 3/31/2016**




*Source: Barclays Live*

- The Barclays Aggregate Bond Index returned 3.03% in the first quarter. Corporate bonds were the strongest performing index segment, returning the most at 3.97%.
- Medium credit quality investment grade corporate bonds outperformed high yield bonds.
- Longer duration bonds outperformed shorter duration bonds.

**BARCLAYS AGGREGATE RETURNS BY MATURITY**
**AS OF 3/31/2016**




*Source: Barclays Live*



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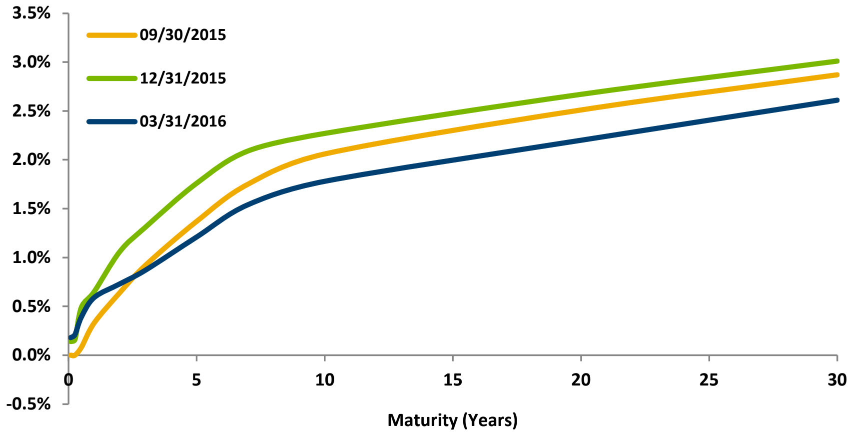
# U.S. Fixed Income Markets

U.S. TREASURY YIELD CURVE




*Source: U.S. Department of Treasury*

U.S. 10-YEAR TREASURY AND TIPS YIELDS


*Source: U.S. Department of Treasury*

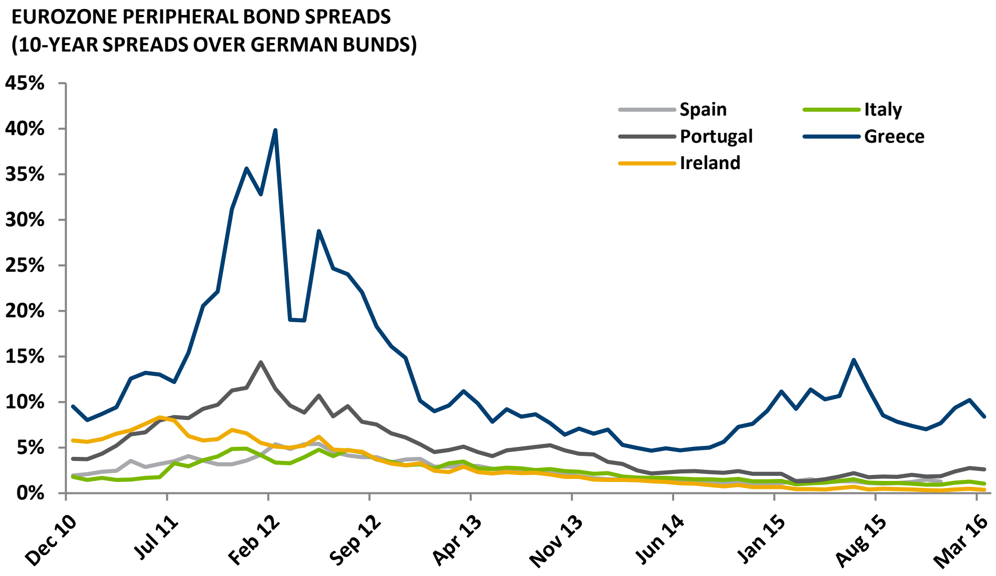
- The Treasury yield curve flattened over the first quarter with yield spreads narrowing between shorter and medium maturities and spreads widening between medium and longer maturities. However, yields rose at the shortest maturities.
- The 10-year U.S. Treasury yield ended the quarter at 1.78%, 49 basis points lower than its level at the beginning of the quarter.
- The 10-year TIPS yield fell by 57 basis points over the quarter and ended the period at 0.16%.

# Credit Spreads

| Spread (bps) | 03/31/2016 | 12/31/2015 | 03/31/2015 | Quarterly Change (bps) | 1-Year Change (bps) |
|---|---|---|---|---|---|
| U.S. Aggregate | 56 | 56 | 46 | 0 | 10 |
| Long Gov't | 4 | 4 | 3 | 0 | 1 |
| Long Credit | 223 | 225 | 187 | -2 | 36 |
| Long Gov't/Credit | 136 | 138 | 118 | -2 | 18 |
| MBS | 22 | 24 | 20 | -2 | 2 |
| CMBS | 109 | 121 | 95 | -12 | 14 |
| ABS | 74 | 72 | 62 | 2 | 12 |
| Corporate | 163 | 165 | 129 | -2 | 34 |
| High Yield | 656 | 660 | 466 | -4 | 190 |
| Global Emerging Markets | 382 | 389 | 354 | -7 | 28 |

- During the first quarter, credit spreads were mixed across all areas of the bond market.
- CMBS spreads (-12 basis points) fell by the most over the quarter, followed by global emerging markets spreads (-7 basis points) and high yield spreads (-4 basis points).
- ABS spreads was the only bond to rise by 2 basis points.

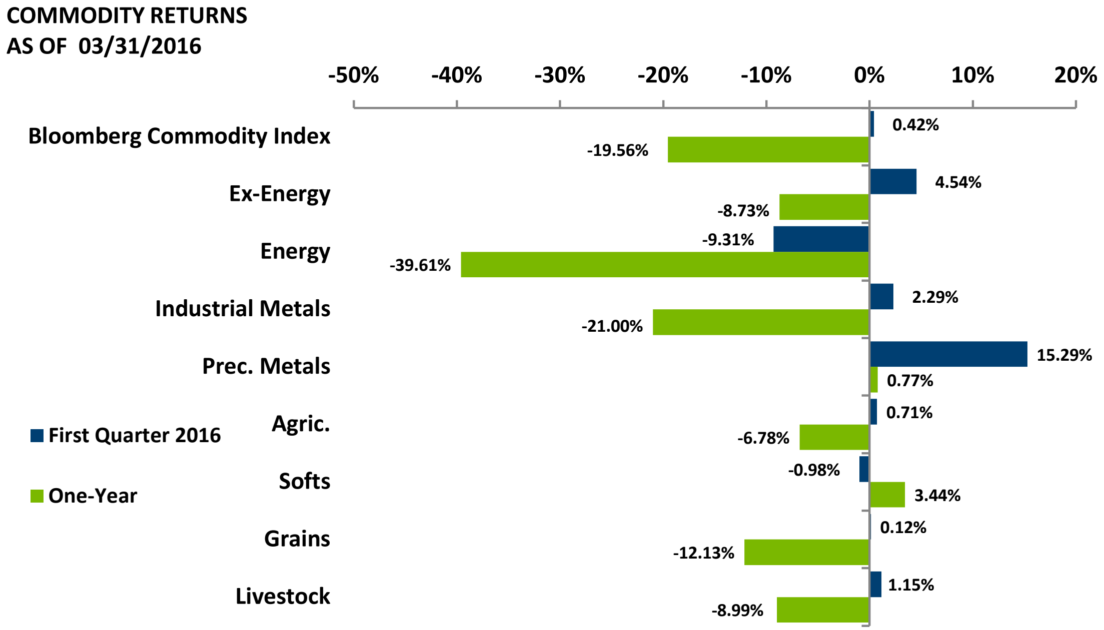
# European Fixed Income Markets




*Source: DataStream*

- In the Eurozone, bond spreads widened during the first quarter of 2016 with the core bond yields falling and the peripheral bond yields being mixed. European government bond yields (except Portugal and Greece) fell over the quarter due to additional monetary stimulus from the European Central Bank (ECB) and dovish statement by the U.S. Federal Reserve (Fed).
- Portuguese government bond yields had a volatile quarter with yields rising sharply in February on the back of concerns of uncertain fiscal outlook, political instability, health of banking system, and chances of the country losing its last investment grade credit rating. Greek bond yields rose over the uncertainty for a third financial bailout.

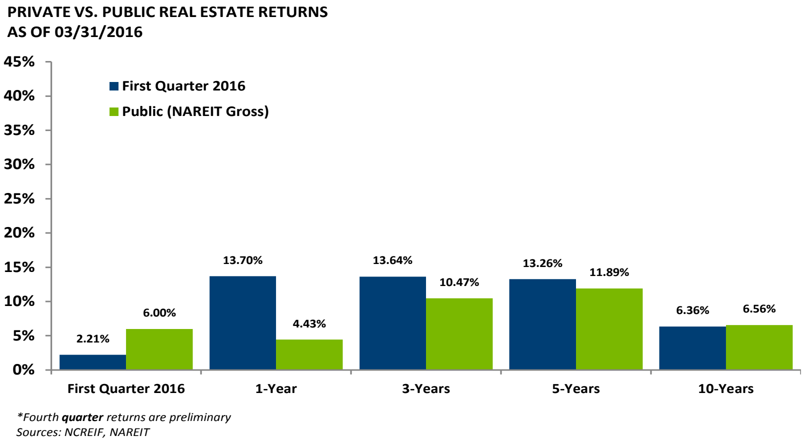
# Commodities

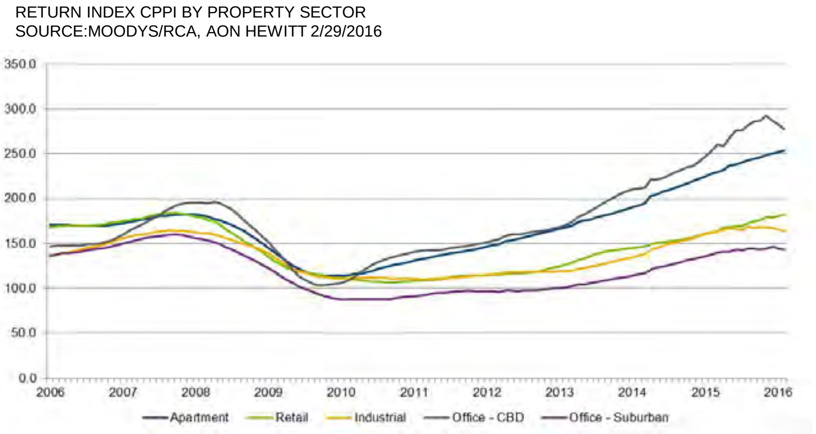



*Source: Dow Jones-UBS*

- The Bloomberg Commodity Index advanced 0.42% during the first quarter.
- During the quarter, the best performing segment was precious metals with a return 15.29%.
- Energy was the worst performing sector of the market with a return of -9.31% during the quarter.

# U.S. Commercial Real Estate Markets




- The U.S. REIT market continued to display volatility during the quarter, rallying in March, after declining more than 10% through mid-February, to end the quarter up 6.0%. Fears of weaker economic growth and credit markets plagued the sector, and broader equities in general, during the first half of the quarter. Additionally, concerns that asset pricing may have peaked or are even poised to decline after significant appreciation also attributed to the sector's volatility. REITs, meanwhile, outperformed the broader equity market during the quarter, which gained 1.4% (S&P 500). Despite all the public market volatility, U.S. REITs ended the quarter trading at approximately 5% premium to private market net asset values. Income from real estate remains attractive, especially versus other asset classes, helping to continue to drive robust capital flows to the sector. REITs' dividends of 3.8% are 203 bps over the 10-Year U.S. Treasury yield.
- Strong underlying sector fundamentals, meanwhile, are expected to support healthy income growth and high occupancies across most property types in 2016. This solid foundation should help real estate offset rising interest rates, though the offset is not expected to be complete. At this point in the cycle, it is important to focus on going forward underwriting assumptions, especially rent growth expectations, new supply impacts, and exit cap rate, as well as monitor use of leverage. Preferred equity and debt structures are also important considerations to help mitigate medium term cyclical risks.

*Indicates preliminary NFI-ODCE data gross of fees

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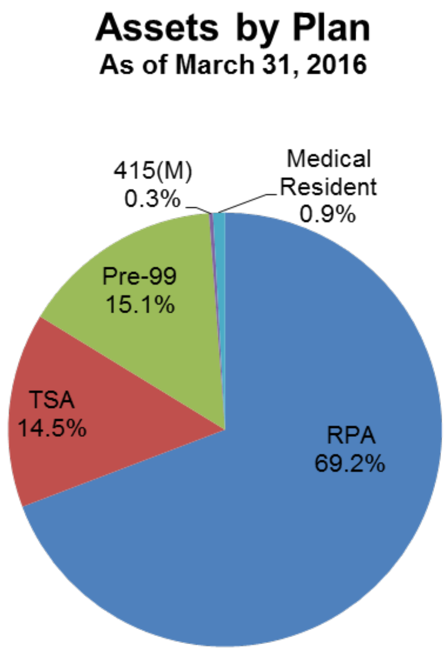
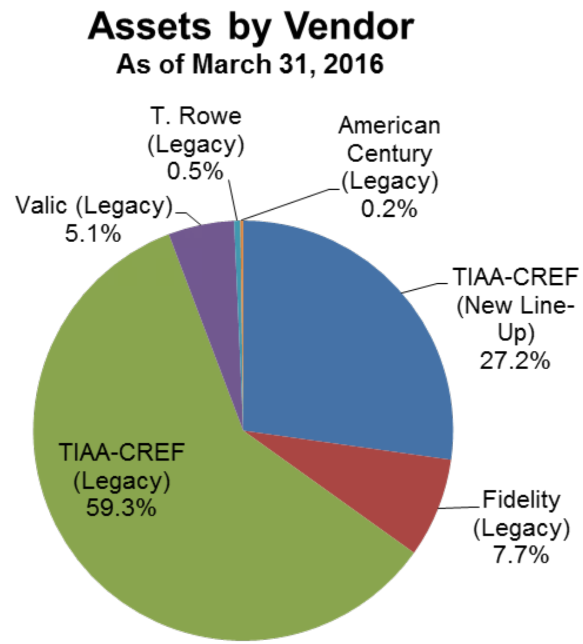
# Agenda Tracker

# Asset Allocation




**As of 3/31/2016**

| Plan | RPA | | TSA | | Pre-99 | | 415(M) | | Medical Resident | | Total | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | $ | % | $ | % | $ | % | $ | % | $ | % | $ | % |
| TIAA-CREF (New Line-Up) | $ 527,135,088 | 30.8% | $ 117,212,923 | 32.6% | $ 11,854,062 | 3.2% | $ 4,488,456 | 61.2% | $ 12,638,840 | 57.7% | $ 673,329,370 | 27.2% |
| Fidelity (Legacy) | $ 146,242,326 | 8.5% | $ 35,408,419 | 9.8% | $ 5,963,996 | 1.6% | $ 1,288,365 | 17.6% | $ 768,963 | 3.5% | $ 189,672,069 | 7.7% |
| TIAA-CREF (Legacy) | $ 940,907,804 | 55.0% | $ 176,667,426 | 49.1% | $ 348,816,053 | 93.5% | $ 1,520,988 | 20.7% | $ 185,627 | 0.8% | $ 1,468,097,897 | 59.3% |
| Valic (Legacy) | $ 86,908,030 | 5.1% | $ 30,535,216 | 8.5% | $ - | 0.0% | $ 38,357 | 0.5% | $ 8,319,891 | 38.0% | $ 125,801,494 | 5.1% |
| T. Rowe (Legacy) | $ 5,909,143 | 0.3% | $ 228,365 | 0.1% | $ 5,693,022 | 1.5% | $ - | 0.0% | $ - | 0.0% | $ 11,830,531 | 0.5% |
| American Century (Legacy) | $ 4,647,495 | 0.3% | $ - | 0.0% | $ 671,076 | 0.2% | $ - | 0.0% | $ - | 0.0% | $ 5,318,571 | 0.2% |
| **Total** | **$ 1,711,749,887** | **100.0%** | **$ 360,052,350** | **100.0%** | **$ 372,998,208** | **100.0%** | **$ 7,336,166** | **100.0%** | **$ 21,913,321** | **100.0%** | **$ 2,474,049,932** | **100.0%** |
| Other Assets* | | | | | | | | | | | $ 1,033,881 | 0.0% |
| **Grand Total** | **$ 1,711,749,887** | **69.2%** | **$ 360,052,350** | **14.5%** | **$ 372,998,208** | **15.1%** | **$ 7,336,166** | **0.3%** | **$ 21,913,321** | **0.9%** | **$ 2,475,083,813** | **100.0%** |

*Other Assets includes Loans and TIAA-CREF Money Market-Instl.

# Tier I(a) Watch List

**Tier I (a)**

| | 1. Underperformed During Trailing 5 Years | 2. Underperformed in 3 of 4 Trailing Calendar Quarters | 3. Diverged from Strategy and/or Portfolio Characteristic | 4. Adverse Change in Portfolio Manager | 5. Weak Manager Research Rating | 6. Significant Organizational Change | Watch List Status | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | | | | | | | 1st Quarter 2016 | 4th Quarter 2015 | 3rd Quarter 2015 | 2nd Quarter 2015 |
| Vanguard Target Retirement Income Trust II | No | No | No | No | No (Buy) | No | | | | |
| Vanguard Target Retirement 2010 Trust II | No | No | No | No | No (Buy) | No | | | | |
| Vanguard Target Retirement 2015 Trust II | No | No | No | No | No (Buy) | No | | | | |
| Vanguard Target Retirement 2020 Trust II | No | No | No | No | No (Buy) | No | | | | |
| Vanguard Target Retirement 2025 Trust II | No | No | No | No | No (Buy) | No | | | | |
| Vanguard Target Retirement 2030 Trust II | No | No | No | No | No (Buy) | No | | | | |
| Vanguard Target Retirement 2035 Trust II | No | No | No | No | No (Buy) | No | | | | |
| Vanguard Target Retirement 2040 Trust II | No | No | No | No | No (Buy) | No | | | | |
| Vanguard Target Retirement 2045 Trust II | No | No | No | No | No (Buy) | No | | | | |
| Vanguard Target Retirement 2050 Trust II | Yes | No | No | No | No (Buy) | No | | | | |
| Vanguard Target Retirement 2055 Trust II | No | No | No | No | No (Buy) | No | | | | |
| Vanguard Traget Retirement 2060 Trust II* | Yes | No | No | No | No (Buy) | No | | | | |

Negative tracking of greater than 0.2% constitutes underperformance for the Plan's target date retirement funds.

- **Notes on Table:** Changes in Watch List designations from the previous quarter are highlighted in red.
- **Yellow-Level Watch List.** An investment fund goes on the Watch List with a yellow designation when two of the above occur, or when item numbers 4, 5, or 6 occur.
- **Orange-Level Watch List**. An investment fund goes on the Watch List with an orange designation when it has been on the yellow watch list for two consecutive quarters or when three of the above occur.
- **Red-Level Watch List.** An investment fund goes on the Watch List with a red designation when it has been on the orange watchlist for two consecutive quarters or when four of the above occur. When an investment fund is placed on the Watch List with a red designation, a formal fund review will be conducted and a recommendation for action will be made.

* Since-inception returns were used since this fund does not have a trailing five-year return.

# Tier I Watch List

**Tier I**

| | 1. Underperformed During Trailing 5 Years | 2. Underperformed in 3 of 4 Trailing Calendar Quarters | 3. Diverged from Strategy and/or Portfolio Characteristic | 4. Adverse Change in Portfolio Manager | 5. Weak Manager Research Rating | 6. Significant Organizational Change | Watch List Status | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | | | | | | | 1st Quarter 2016 | 4th Quarter 2015 | 3rd Quarter 2015 | 2nd Quarter 2015 |
| Vanguard Target Retirement Income | No | No | No | No | No (Buy) | No | | | | |
| Vanguard Target Retirement 2010 | No | No | No | No | No (Buy) | No | | | | |
| Vanguard Target Retirement 2015 | No | No | No | No | No (Buy) | No | | | | |
| Vanguard Target Retirement 2020 | No | No | No | No | No (Buy) | No | | | | |
| Vanguard Target Retirement 2025 | Yes | No | No | No | No (Buy) | No | | | | |
| Vanguard Target Retirement 2030 | Yes | No | No | No | No (Buy) | No | | | | |
| Vanguard Target Retirement 2035 | Yes | No | No | No | No (Buy) | No | | | | |
| Vanguard Target Retirement 2040 | Yes | No | No | No | No (Buy) | No | | | | |
| Vanguard Target Retirement 2045 | Yes | No | No | No | No (Buy) | No | | | | |
| Vanguard Target Retirement 2050 | Yes | No | No | No | No (Buy) | No | | | | |
| Vanguard Target Retirement 2055 | Yes | No | No | No | No (Buy) | No | | | | |
| Vanguard Traget Retirement 2060* | Yes | No | No | No | No (Buy) | No | | | | |

Negative tracking of greater than 0.2% constitutes underperformance for the Plan's target date retirement funds.

- **Notes on Table:** Changes in Watch List designations from the previous quarter are highlighted in red.
- **Yellow-Level Watch List.** An investment fund goes on the Watch List with a yellow designation when two of the above occur, or when item numbers 4, 5, or 6 occur.
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* Since-inception returns were used since this fund does not have a trailing five-year return.

# Tier II and III Watch List

**Tier II & III**

| | 1. Underperformed During Trailing 5 Years | 2. Underperformed in 3 of 4 Trailing Calendar Quarters | 3. Diverged from Strategy and/or Portfolio Characteristic | 4. Adverse Change in Portfolio Manager | 5. Weak Manager Research Rating | 6. Significant Organizational Change | Watch List Status | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | | | | | | | 1st Quarter 2016 | 4th Quarter 2015 | 3rd Quarter 2015 | 2nd Quarter 2015 |
| Vanguard Prime Money Market Fund | No | No | No | No | No (Buy) | No | | | | |
| TIAA Traditional - RC | No | No | No | No | No (Buy) | No | | | | |
| TIAA Traditional - RCP | No | No | No | No | No (Buy) | No | | | | |
| Vanguard Total Bond Market Index Fund | No | No | No | No | No (Buy) | No | | | | |
| PIMCO Total Return Fund | Yes | Yes | No | No | No (Buy) | No | | | | |
| Vanguard Total Stock Market Index Fund | No | No | No | No | No (Buy) | No | | | | |
| Vanguard Total International Stock Index | No | No | No | No | No (Buy) | No | | | | |
| Dodge & Cox Global Stock Fund | No | Yes | No | No | No (Buy) | No | | | | |
| DFA Inflation-Protected Securities | No | No | No | No | No (Buy) | No | | | | |
| Neuberger Berman High Income Bond Fund* | Yes | Yes | No | No | No (Buy) | No | | | | |
| Vanguard Institutional Index Fund | No | No | No | No | No (Buy) | No | | | | |
| T. Rowe Price Instl. Large Cap Growth Fund | Yes | No | No | Yes | In Review | No | | | | |
| Diamond Hill Large Cap* | Yes | No | No | No | No (Buy) | No | | | | |
| Vanguard Extended Market Index Fund | No | No | No | No | No (Buy) | No | | | | |
| William Blair Small/Mid Cap Growth Fund | No | No | No | No | No (Buy) | No | | | | |
| DFA U.S. Targeted Value | Yes | Yes | No | No | No (Buy) | No | | | | |
| Vanguard Developed Market Index Fund | No | No | No | No | No (Buy) | No | | | | |
| Harding Loevner International Equity Instl. | No | No | No | No | No (Buy) | No | | | | |
| MFS International Value Fund | No | No | No | No | No (Buy) | No | | | | |
| Vanguard Emerging Markets Stock Index Fund | No | No | No | No | No (Buy) | No | | | | |
| Laudus Mondrian Emerging Markets Instl. | Yes | No | No | No | No (Buy) | No | | | | |
| Cohen & Steers Instl Realty Shares | Yes | No | No | No | No (Buy) | No | | | | |

Negative tracking of greater than 0.1% for domestic equities and fixed income or 0.3% for non-U.S. equities constitutes underperformance for the Plan's index funds.

- **Notes on Table**: Changes in Watch List designations from the previous quarter are highlighted in red.
- **Yellow-Level Watch List.** An investment fund goes on the Watch List with a yellow designation when two of the above occur, or when item numbers 4, 5, or 6 occur.
- **Orange-Level Watch List.** An investment fund goes on the Watch List with an orange designation when it has been on the yellow watch list for two consecutive quarters or when three of the above occur.
- **Red-Level Watch List.** An investment fund goes on the Watch List with a red designation when it has been on the orange watchlist for two consecutive quarters or when four of the above occur. When an investment fund is placed on the Watch List with a red designation, a formal fund review will be conducted and a recommendation for action will be made.

* Since-inception returns were used since this fund does not have a trailing five-year return.

# Tier I(a) Performance Summary

## As of 3/31/2016

| | Allocation | | Performance(%) | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | Market Value ($) | % | 1 Quarter | 1 Year | 3 Years | 5 Years | 10 Years | Since Inception | Inception Date |
| **Total Plan** | **2,475,083,813** | **100.0** | | | | | | | **03/01/2014** |
| **Tier I (a)** | **311,869,850** | **12.6** | | | | | | | **03/01/2014** |
| Vanguard Target Retirement Income Trust II | 3,004,403 | 0.1 | 2.3 (1) | 0.4 (2) | 3.7 (66) | 5.0 (57) | | 4.8 (56) | 03/01/2008 |
| *Vanguard Target Income Composite Index* | | | *2.3 (1)* | *0.6 (1)* | *3.9 (65)* | *5.1 (50)* | | *4.8 (55)* | |
| Vanguard Target Retirement 2010 Trust II | 7,356,404 | 0.3 | 2.2 (21) | 0.1 (15) | 4.5 (14) | 5.5 (16) | | 5.0 (6) | 03/01/2008 |
| *Vanguard Target 2010 Composite Index* | | | *2.2 (25)* | *0.3 (10)* | *4.6 (10)* | *5.6 (14)* | | *4.9 (8)* | |
| Vanguard Target Retirement 2015 Trust II | 24,855,907 | 1.0 | 2.0 (22) | -0.5 (21) | 5.4 (4) | 6.1 (8) | | 5.3 (1) | 03/01/2008 |
| *Vanguard Target 2015 Composite Index* | | | *1.9 (25)* | *-0.4 (16)* | *5.5 (3)* | *6.1 (5)* | | *5.2 (1)* | |
| Vanguard Target Retirement 2020 Trust II | 37,907,825 | 1.5 | 1.8 (32) | -1.0 (27) | 6.1 (3) | 6.5 (4) | | 5.4 (1) | 03/01/2008 |
| *Vanguard Target 2020 Composite Index* | | | *1.7 (35)* | *-0.9 (24)* | *6.2 (3)* | *6.7 (3)* | | *5.5 (1)* | |
| Vanguard Target Retirement 2025 Trust II | 37,971,032 | 1.5 | 1.6 (41) | -1.4 (27) | 6.4 (3) | 6.8 (9) | | 5.5 (1) | 03/01/2008 |
| *Vanguard Target 2025 Composite Index* | | | *1.5 (43)* | *-1.3 (23)* | *6.6 (3)* | *7.0 (5)* | | *5.5 (1)* | |
| Vanguard Target Retirement 2030 Trust II | 41,760,392 | 1.7 | 1.3 (37) | -1.9 (24) | 6.8 (11) | 7.0 (10) | | 5.5 (12) | 03/01/2008 |
| *Vanguard Target 2030 Composite Index* | | | *1.3 (38)* | *-1.7 (20)* | *6.9 (6)* | *7.2 (4)* | | *5.6 (9)* | |
| Vanguard Target Retirement 2035 Trust II | 51,891,253 | 2.1 | 1.1 (36) | -2.3 (19) | 7.1 (6) | 7.2 (13) | | 5.6 (7) | 03/01/2008 |
| *Vanguard Target 2035 Composite Index* | | | *1.1 (37)* | *-2.2 (17)* | *7.3 (3)* | *7.4 (8)* | | *5.7 (3)* | |
| Vanguard Target Retirement 2040 Trust II | 50,692,904 | 2.0 | 0.9 (31) | -3.0 (28) | 7.2 (11) | 7.4 (11) | | 5.7 (11) | 03/01/2008 |
| *Vanguard Target 2040 Composite Index* | | | *0.9 (31)* | *-2.7 (21)* | *7.4 (4)* | *7.6 (9)* | | *5.8 (8)* | |
| Vanguard Target Retirement 2045 Trust II | 35,716,559 | 1.4 | 0.8 (36) | -3.0 (26) | 7.2 (14) | 7.4 (13) | | 5.7 (8) | 03/01/2008 |
| *Vanguard Target 2045 Composite Index* | | | *0.8 (36)* | *-2.7 (15)* | *7.4 (7)* | *7.6 (8)* | | *5.8 (2)* | |
| Vanguard Target Retirement 2050 Trust II | 15,526,159 | 0.6 | 0.8 (34) | -3.0 (27) | 7.2 (14) | 7.3 (12) | | 5.7 (6) | 03/01/2008 |
| *Vanguard Target 2050 Composite Index* | | | *0.8 (34)* | *-2.7 (17)* | *7.4 (10)* | *7.6 (9)* | | *5.8 (1)* | |
| Vanguard Target Retirement 2055 Trust II | 3,760,629 | 0.2 | 0.9 (30) | -3.1 (24) | 7.1 (19) | 7.4 (15) | | 10.9 | 09/01/2010 |
| *Vanguard Target 2055 Composite Index* | | | *0.8 (31)* | *-2.7 (14)* | *7.4 (11)* | *7.6 (9)* | | *11.1* | |
| Vanguard Target Retirement 2060 Trust II | 1,426,385 | 0.1 | 0.8 (31) | -3.1 (24) | 7.1 (19) | | | 8.3 (17) | 04/01/2012 |
| *Vanguard Target 2060 Composite Index* | | | *0.8 (31)* | *-2.7 (14)* | *7.4 (11)* | | | *8.6 (11)* | |

# Tier I Performance Summary

**As of 3/31/2016**

| | Allocation | | Performance(%) | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | Market Value ($) | % | 1 Quarter | 1 Year | 3 Years | 5 Years | 10 Years | Since Inception | Inception Date |
| **Tier I** | **55,616,568** | **2.2** | | | | | | | **03/01/2014** |
| Vanguard Target Retirement Income | 942,761 | 0.0 | 2.3 (1) | 0.4 (2) | 3.6 (67) | 5.0 (58) | 5.2 | 5.2 | 11/01/2003 |
| *Vanguard Target Income Composite Index* | | | *2.3 (1)* | *0.6 (1)* | *3.9 (65)* | *5.1 (50)* | *5.3* | *5.2* | |
| Vanguard Target Retirement 2010 | 2,665,180 | 0.1 | 2.2 (25) | 0.1 (14) | 4.4 (17) | 5.5 (22) | | 5.4 | 07/01/2006 |
| *Vanguard Target 2010 Composite Index* | | | *2.2 (25)* | *0.3 (10)* | *4.6 (10)* | *5.6 (14)* | | *5.4* | |
| Vanguard Target Retirement 2015 | 10,149,587 | 0.4 | 1.9 (26) | -0.6 (23) | 5.3 (8) | 6.0 (11) | 5.3 | 5.9 | 11/01/2003 |
| *Vanguard Target 2015 Composite Index* | | | *1.9 (25)* | *-0.4 (16)* | *5.5 (3)* | *6.1 (5)* | *5.3* | *6.0* | |
| Vanguard Target Retirement 2020 | 7,757,554 | 0.3 | 1.7 (35) | -1.1 (32) | 6.0 (3) | 6.5 (8) | | 5.7 (1) | 07/01/2006 |
| *Vanguard Target 2020 Composite Index* | | | *1.7 (35)* | *-0.9 (24)* | *6.2 (3)* | *6.7 (3)* | | *5.8 (1)* | |
| Vanguard Target Retirement 2025 | 7,422,742 | 0.3 | 1.5 (43) | -1.5 (32) | 6.3 (6) | 6.7 (14) | 5.4 | 6.2 | 11/01/2003 |
| *Vanguard Target 2025 Composite Index* | | | *1.5 (43)* | *-1.3 (23)* | *6.6 (3)* | *7.0 (5)* | *5.5* | *6.3* | |
| Vanguard Target Retirement 2030 | 5,855,739 | 0.2 | 1.3 (39) | -2.0 (30) | 6.7 (14) | 6.9 (12) | | 5.6 (11) | 07/01/2006 |
| *Vanguard Target 2030 Composite Index* | | | *1.3 (38)* | *-1.7 (20)* | *6.9 (6)* | *7.2 (4)* | | *5.8 (1)* | |
| Vanguard Target Retirement 2035 | 5,420,092 | 0.2 | 1.1 (40) | -2.5 (24) | 7.0 (10) | 7.1 (14) | 5.4 | 6.6 | 11/01/2003 |
| *Vanguard Target 2035 Composite Index* | | | *1.1 (37)* | *-2.2 (17)* | *7.3 (3)* | *7.4 (8)* | *5.5* | *6.8* | |
| Vanguard Target Retirement 2040 | 4,833,210 | 0.2 | 0.8 (35) | -3.1 (30) | 7.1 (16) | 7.3 (13) | | 5.8 (12) | 07/01/2006 |
| *Vanguard Target 2040 Composite Index* | | | *0.9 (31)* | *-2.7 (21)* | *7.4 (4)* | *7.6 (9)* | | *5.9 (5)* | |
| Vanguard Target Retirement 2045 | 5,149,608 | 0.2 | 0.8 (38) | -3.1 (28) | 7.1 (16) | 7.3 (15) | 5.5 | 6.9 | 11/01/2003 |
| *Vanguard Target 2045 Composite Index* | | | *0.8 (36)* | *-2.7 (15)* | *7.4 (7)* | *7.6 (8)* | *5.6* | *7.1* | |
| Vanguard Target Retirement 2050 | 4,702,743 | 0.2 | 0.8 (38) | -3.1 (27) | 7.1 (15) | 7.3 (12) | | 5.8 | 07/01/2006 |
| *Vanguard Target 2050 Composite Index* | | | *0.8 (34)* | *-2.7 (17)* | *7.4 (10)* | *7.6 (9)* | | *5.9* | |
| Vanguard Target Retirement 2055 | 459,034 | 0.0 | 0.8 (36) | -3.3 (27) | 7.0 (24) | 7.3 (19) | | 10.8 | 09/01/2010 |
| *Vanguard Target 2055 Composite Index* | | | *0.8 (31)* | *-2.7 (14)* | *7.4 (11)* | *7.6 (9)* | | *11.1* | |
| Vanguard Target Retirement 2060 | 258,319 | 0.0 | 0.8 (38) | -3.2 (26) | 7.1 (21) | | | 9.4 (28) | 02/01/2012 |
| *Vanguard Target 2060 Composite Index* | | | *0.8 (31)* | *-2.7 (14)* | *7.4 (11)* | | | *9.7 (14)* | |

# Tier II and III Performance Summary

## As of 3/31/2016

| | Allocation | | Performance(%) | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | Market Value ($) | % | 1 Quarter | 1 Year | 3 Years | 5 Years | 10 Years | Since Inception | Inception Date |
| **Tier II** | **135,661,597** | **5.5** | | | | | | | **03/01/2014** |
| Vanguard Prime Money Market Fund | 11,019,000 | 0.4 | 0.1 (2) | 0.2 (11) | 0.1 (10) | 0.1 (12) | 1.3 (4) | 3.3 (1) | 11/01/1989 |
| *Citigroup 3 Month T-Bill* | | | *0.1 (31)* | *0.1 (32)* | *0.0 (26)* | *0.1 (22)* | *1.1 (62)* | *3.0 (46)* | |
| TIAA Traditional - RC | 35,868,832 | 1.4 | 1.1 (3) | 4.2 (1) | 4.4 (1) | 4.4 (1) | 4.5 (1) | 4.5 (1) | 08/01/2005 |
| *Hueler Stable Value Index* | | | *0.4 (20)* | *1.8 (16)* | *1.7 (20)* | *2.0 (32)* | *3.0 (38)* | *3.1 (33)* | |
| TIAA Traditional - RCP | 22,778,499 | 0.9 | 0.9 (3) | 3.5 (1) | 3.6 (1) | 3.5 (1) | | 3.8 (2) | 06/01/2006 |
| *Hueler Stable Value Index* | | | *0.4 (20)* | *1.8 (16)* | *1.7 (20)* | *2.0 (32)* | | *3.0 (33)* | |
| Vanguard Total Bond Market Index Fund | 16,522,880 | 0.7 | 3.1 (20) | 1.8 (27) | 2.4 (35) | 3.7 (53) | 4.9 (44) | 5.5 (21) | 10/01/1995 |
| *Performance Benchmark* | | | *3.1 (20)* | *1.9 (21)* | *2.5 (24)* | *3.8 (46)* | *4.9 (43)* | *5.6 (18)* | |
| PIMCO Total Return Fund | 8,664,015 | 0.4 | 1.8 (97) | 0.3 (90) | 1.5 (88) | 3.7 (61) | 6.0 (1) | 7.6 | 06/01/1987 |
| *Barclays Aggregate Index* | | | *3.0 (28)* | *2.0 (15)* | *2.5 (21)* | *3.8 (47)* | *4.9 (44)* | *6.7* | |
| Vanguard Total Stock Market Index Fund | 20,279,167 | 0.8 | 0.9 (32) | -0.4 (41) | 11.1 (39) | 11.0 (34) | 7.1 (28) | 6.6 (25) | 08/01/1997 |
| *Performance Benchmark* | | | *0.9 (32)* | *-0.4 (41)* | *11.1 (39)* | *11.0 (34)* | *7.0 (29)* | *6.5 (26)* | |
| Vanguard Total International Stock Index | 3,475,994 | 0.1 | -0.1 (28) | -8.1 (57) | 0.8 (78) | 0.7 (82) | | 2.8 (83) | 12/01/2010 |
| *Performance Benchmark* | | | *-0.3 (32)* | *-8.0 (53)* | *1.0 (74)* | *0.8 (81)* | | *2.8 (78)* | |
| Dodge & Cox Global Stock Fund | 17,053,210 | 0.7 | -1.3 (67) | -10.6 (81) | 6.3 (45) | 5.9 (42) | | 3.0 (50) | 05/01/2008 |
| *MSCI AC World Index (Net)* | | | *0.2 (50)* | *-4.3 (44)* | *5.5 (58)* | *5.2 (54)* | | *2.7 (56)* | |
| **Tier III** | **167,359,629** | **6.8** | | | | | | | **03/01/2014** |
| DFA Inflation-Protected Securities Portfolio | 4,833,697 | 0.2 | 5.0 (12) | 1.9 (5) | -0.8 (36) | 3.2 (8) | | 4.7 (10) | 10/01/2006 |
| *Barclays U.S. TIPS Index* | | | *4.5 (25)* | *1.5 (12)* | *-0.7 (22)* | *3.0 (15)* | | *4.4 (24)* | |
| Neuberger Berman High Income Bond Fund | 7,212,539 | 0.3 | 2.9 (27) | -4.1 (59) | 1.5 (52) | | | 1.5 (52) | 04/01/2013 |
| *Barclays Corporate High Yield Index* | | | *3.4 (14)* | *-3.7 (55)* | *1.8 (38)* | | | *1.8 (38)* | |
| Vanguard Institutional Index Fund | 47,158,484 | 1.9 | 1.3 (18) | 1.8 (11) | 11.8 (5) | 11.6 (5) | 7.0 (4) | 9.4 | 08/01/1990 |
| *S&P 500 Index* | | | *1.3 (12)* | *1.8 (5)* | *11.8 (1)* | *11.6 (3)* | *7.0 (4)* | *9.4* | |
| T. Rowe Price Instl. Large Cap Growth Fund | 11,962,545 | 0.5 | -6.4 (93) | -2.4 (71) | 14.3 (15) | 12.0 (30) | 8.4 (15) | 8.5 (7) | 11/01/2001 |
| *Russell 1000 Growth Index* | | | *0.7 (10)* | *2.5 (14)* | *13.6 (27)* | *12.4 (21)* | *8.3 (22)* | *6.9 (36)* | |

# Tier III Performance Summary (cont'd)

**As of 3/31/2016**

| | Allocation | | Performance(%) | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | Market Value ($) | % | 1 Quarter | 1 Year | 3 Years | 5 Years | 10 Years | Since Inception | Inception Date |
| Diamond Hill Large Cap | 9,831,708 | 0.4 | 1.2 (37) | 0.3 (16) | 10.9 (9) | | | 13.6 (25) | 01/01/2012 |
| *Russell 1000 Value Index* | | | *1.6 (30)* | *-1.5 (32)* | *9.4 (31)* | | | *13.7 (20)* | |
| Vanguard Extended Market Index Fund - Instl. | 17,616,451 | 0.7 | -0.9 (90) | -8.9 (79) | 8.1 (36) | 8.5 (39) | 6.7 (37) | 7.6 (80) | 08/01/1997 |
| *Performance Benchmark* | | | *-0.9 (90)* | *-9.0 (82)* | *8.0 (40)* | *8.4 (40)* | *6.6 (42)* | | |
| William Blair Small/Mid Cap Growth Fund | 6,446,558 | 0.3 | -2.9 (35) | -5.4 (14) | 11.2 (5) | 9.8 (11) | 8.0 (12) | 9.5 (8) | 01/01/2004 |
| *Russell 2500 Growth Index* | | | *-2.7 (31)* | *-9.6 (38)* | *9.2 (19)* | *8.8 (22)* | *7.0 (23)* | *8.5 (22)* | |
| DFA U.S. Targeted Value | 15,442,152 | 0.6 | 2.6 (74) | -7.0 (77) | 7.7 (44) | 8.0 (45) | 5.9 (72) | 11.1 | 03/01/2000 |
| *Russell 2500 Value Index* | | | *3.3 (65)* | *-5.2 (50)* | *7.2 (58)* | *8.3 (43)* | *5.8 (72)* | *9.8* | |
| Vanguard Developed Market Index Fund | 12,778,670 | 0.5 | -2.0 (41) | -7.3 (28) | 2.6 (25) | 2.5 (32) | 2.1 (43) | 3.5 (54) | 02/01/2001 |
| *Performance Benchmark* | | | *-2.7 (57)* | *-7.8 (37)* | *2.3 (32)* | *2.4 (35)* | *1.8 (49)* | *3.3 (62)* | |
| Harding Loevner International Equity Instl. | 3,407,786 | 0.1 | 0.7 (19) | -5.8 (33) | 2.9 (40) | 3.1 (40) | 4.4 (1) | 5.7 | 06/01/1994 |
| *MSCI AC World ex USA Growth (Net)* | | | *-0.3 (30)* | *-6.1 (34)* | *1.9 (61)* | *1.6 (61)* | *2.7 (49)* | | |
| MFS International Value Fund | 9,241,257 | 0.4 | 2.7 (7) | 2.8 (1) | 9.6 (1) | 9.7 (1) | | 6.4 (1) | 06/01/2006 |
| *MSCI AC World ex USA Value (Net)* | | | *-0.4 (26)* | *-12.3 (85)* | *-1.3 (96)* | *-1.0 (85)* | | *1.0 (61)* | |
| Vanguard Emerging Markets Stock Index Fund - Instl. | 8,461,803 | 0.3 | 5.4 (41) | -12.6 (67) | -4.3 (46) | -4.1 (52) | 2.9 (37) | 6.8 (58) | 07/01/2000 |
| *Performance Benchmark* | | | *6.1 (34)* | *-12.0 (60)* | *-4.0 (42)* | *-3.9 (47)* | *3.2 (33)* | *6.6 (60)* | |
| Laudus Mondrian Emerging Markets Instl. | 1,159,379 | 0.0 | 7.0 (26) | -12.9 (72) | -8.9 (89) | -4.3 (55) | | -2.5 (51) | 05/01/2008 |
| *MSCI Emerging Markets Index (Net)* | | | *5.7 (38)* | *-12.0 (60)* | *-4.5 (47)* | *-4.1 (52)* | | *-2.0 (45)* | |
| Cohen and Steers Instl. Realty Shares | 11,806,598 | 0.5 | 3.9 (78) | 3.9 (44) | 11.0 (22) | 11.1 (57) | 6.9 (18) | 12.9 (7) | 03/01/2000 |
| *FTSE NAREIT Equity REIT Index* | | | *6.0 (15)* | *4.4 (32)* | *10.5 (42)* | *11.9 (18)* | *6.6 (41)* | *12.5 (39)* | |

# Tier IV and Other Assets

**As of 3/31/2016**

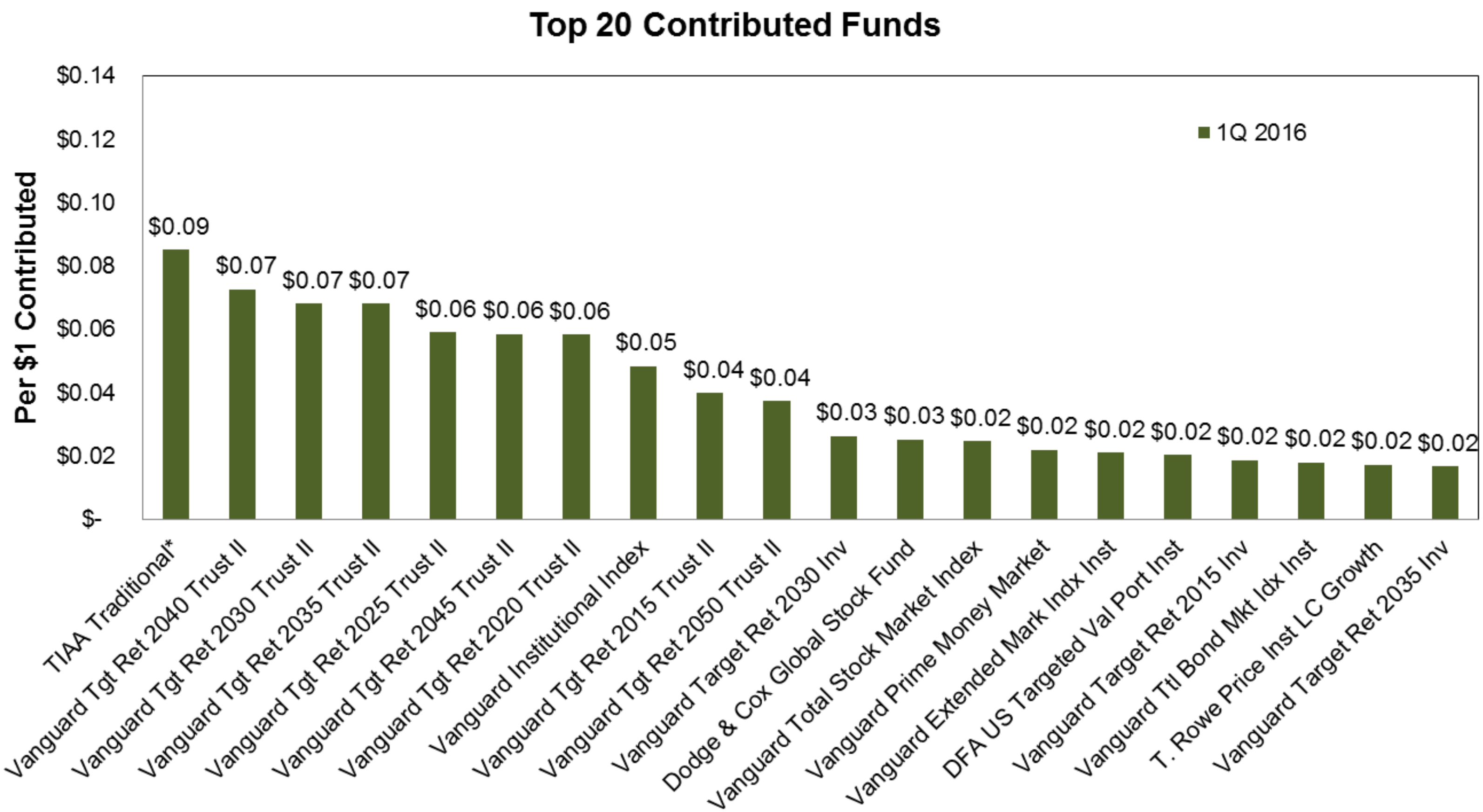
| | Allocation | | Performance(%) | | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Market Value ($) | % | 1 Quarter | | 1 Year | | 3 Years | | 5 Years | | 10 Years | | Since Inception | | Inception Date |
| **Tier IV** | **2,821,726** | **0.1** | | | | | | | | | | | | | |
| Mutual Fund Window | 2,821,726 | 0.1 | | | | | | | | | | | | | |
| **Orphan Accounts** | **1,800,720,562** | **72.8** | | | | | | | | | | | | | |
| Fidelity Orphan Accounts | 189,672,069 | 7.7 | | | | | | | | | | | | | |
| TIAA-CREF Orphan Accounts | 1,468,097,897 | 59.3 | | | | | | | | | | | | | |
| VALIC Orphan Accounts | 125,801,494 | 5.1 | | | | | | | | | | | | | |
| T. Rowe Price Orphan Accounts | 11,830,531 | 0.5 | | | | | | | | | | | | | |
| American Century Orphan Accounts | 5,318,571 | 0.2 | | | | | | | | | | | | | |
| **Other Assets** | **1,033,881** | **0.0** | | | | | | | | | | | | | |
| Loans | 476,291 | 0.0 | | | | | | | | | | | | | |
| Loans Deemed Distributed | 314,960 | 0.0 | | | | | | | | | | | | | |
| Plan Loan Default Fund | 48,154 | 0.0 | | | | | | | | | | | | | |
| TIAA-CREF Money Market-Instl. | 194,476 | 0.0 | 0.1 | (25) | 0.1 | (29) | 0.0 | (33) | 0.0 | (30) | 1.3 | (17) | 2.0 | (13) | 08/01/1999 |
| *iMoneyNet Prime Institutional Average* | | | *0.1* | *(30)* | *0.1* | *(27)* | *0.1* | *(24)* | *0.1* | *(23)* | *1.2* | *(27)* | *1.9* | *(33)* | |



Empower Results®

# Top Contributed Funds

**As of 3/31/2016**




Source: As reported by TIAA-CREF

* TIAA Traditional Contribution Split: RC = 62% / RCP = 38%

# Annual Fee Transparency

| Investment Option | Market Value | Mgmt. Fee (%) | Mgmt. Fee ($) | Revenue Sharing (%)* | Revenue Sharing ($) | Total Expense (%)** | Total Expense ($) |
|---|---|---|---|---|---|---|---|
| Vanguard Target Retirement Income Trust II | $3,004,403 | 0.08% | $2,404 | 0.00% | $0 | 0.08% | $2,404 |
| Vanguard Target Retirement 2010 Trust II | $7,356,404 | 0.08% | $5,885 | 0.00% | $0 | 0.08% | $5,885 |
| Vanguard Target Retirement 2015 Trust II | $24,855,907 | 0.08% | $19,885 | 0.00% | $0 | 0.08% | $19,885 |
| Vanguard Target Retirement 2020 Trust II | $37,907,825 | 0.08% | $30,326 | 0.00% | $0 | 0.08% | $30,326 |
| Vanguard Target Retirement 2025 Trust II | $37,971,032 | 0.08% | $30,377 | 0.00% | $0 | 0.08% | $30,377 |
| Vanguard Target Retirement 2030 Trust II | $41,760,392 | 0.08% | $33,408 | 0.00% | $0 | 0.08% | $33,408 |
| Vanguard Target Retirement 2035 Trust II | $51,891,253 | 0.08% | $41,513 | 0.00% | $0 | 0.08% | $41,513 |
| Vanguard Target Retirement 2040 Trust II | $50,692,904 | 0.08% | $40,554 | 0.00% | $0 | 0.08% | $40,554 |
| Vanguard Target Retirement 2045 Trust II | $35,716,559 | 0.08% | $28,573 | 0.00% | $0 | 0.08% | $28,573 |
| Vanguard Target Retirement 2050 Trust II | $15,526,159 | 0.08% | $12,421 | 0.00% | $0 | 0.08% | $12,421 |
| Vanguard Target Retirement 2055 Trust II | $3,760,629 | 0.08% | $3,009 | 0.00% | $0 | 0.08% | $3,009 |
| Vanguard Target Retirement 2060 Trust II | $1,426,385 | 0.08% | $1,141 | 0.00% | $0 | 0.08% | $1,141 |
| Vanguard Target Retirement Income | $942,761 | 0.14% | $1,320 | 0.00% | $0 | 0.14% | $1,320 |
| Vanguard Target Retirement 2010 | $2,665,180 | 0.14% | $3,731 | 0.00% | $0 | 0.14% | $3,731 |
| Vanguard Target Retirement 2015 | $10,149,587 | 0.14% | $14,209 | 0.00% | $0 | 0.14% | $14,209 |
| Vanguard Target Retirement 2020 | $7,757,554 | 0.14% | $10,861 | 0.00% | $0 | 0.14% | $10,861 |
| Vanguard Target Retirement 2025 | $7,422,742 | 0.15% | $11,134 | 0.00% | $0 | 0.15% | $11,134 |
| Vanguard Target Retirement 2030 | $5,855,739 | 0.15% | $8,784 | 0.00% | $0 | 0.15% | $8,784 |
| Vanguard Target Retirement 2035 | $5,420,092 | 0.15% | $8,130 | 0.00% | $0 | 0.15% | $8,130 |
| Vanguard Target Retirement 2040 | $4,833,210 | 0.16% | $7,733 | 0.00% | $0 | 0.16% | $7,733 |
| Vanguard Target Retirement 2045 | $5,149,608 | 0.16% | $8,239 | 0.00% | $0 | 0.16% | $8,239 |
| Vanguard Target Retirement 2050 | $4,702,743 | 0.16% | $7,524 | 0.00% | $0 | 0.16% | $7,524 |
| Vanguard Target Retirement 2055 | $459,034 | 0.16% | $734 | 0.00% | $0 | 0.16% | $734 |
| Vanguard Target Retirement 2060 | $258,319 | 0.16% | $413 | 0.00% | $0 | 0.16% | $413 |
| Vanguard Prime Money Market Fund | $11,019,000 | 0.10% | $11,019 | 0.00% | $0 | 0.10% | $11,019 |
| TIAA Traditional - RC & RCP | $58,647,331 | 0.40% | $234,589 | 0.15% | $87,971 | 0.55% | $322,560 |
| Vanguard Total Bond Market Index Fund | $16,522,880 | 0.06% | $9,914 | 0.00% | $0 | 0.06% | $9,914 |
| PIMCO Total Return Fund | $8,664,015 | 0.46% | $39,854 | 0.00% | $0 | 0.46% | $39,854 |
| Vanguard Total Stock Market Index Fund | $20,279,167 | 0.04% | $8,112 | 0.00% | $0 | 0.04% | $8,112 |
| Vanguard Total International Stock Index | $3,475,994 | 0.10% | $3,476 | 0.00% | $0 | 0.10% | $3,476 |
| Dodge & Cox Global Stock Fund | $17,053,210 | 0.55% | $93,793 | 0.10% | $17,053 | 0.65% | $110,846 |
| DFA Inflation-Protected Securities Portfolio | $4,833,697 | 0.12% | $5,800 | 0.00% | $0 | 0.12% | $5,800 |
| Neuberger Berman High Income Bond Fund | $7,212,539 | 0.62% | $44,718 | 0.00% | $0 | 0.62% | $44,718 |
| Vanguard Institutional Index Fund | $47,158,484 | 0.04% | $18,863 | 0.00% | $0 | 0.04% | $18,863 |
| T. Row e Price Instl. Large Cap Grow th Fund | $11,962,545 | 0.56% | $66,990 | 0.00% | $0 | 0.56% | $66,990 |
| Diamond Hill Large Cap | $9,831,708 | 0.60% | $58,990 | 0.00% | $0 | 0.60% | $58,990 |
| Vanguard Extended Market Index Fund - Instl. | $17,616,451 | 0.08% | $14,093 | 0.00% | $0 | 0.08% | $14,093 |
| William Blair Small/Mid Cap Grow th Fund | $6,446,558 | 0.95% | $61,242 | 0.15% | $9,670 | 1.10% | $70,912 |
| DFA U.S. Targeted Value | $15,442,152 | 0.37% | $57,136 | 0.00% | $0 | 0.37% | $57,136 |
| Vanguard Developed Market Index Fund | $12,778,670 | 0.07% | $8,945 | 0.00% | $0 | 0.07% | $8,945 |
| Harding Loevner International Equity Instl. | $3,407,786 | 0.71% | $24,195 | 0.15% | $5,112 | 0.86% | $29,307 |
| MFS International Value Fund | $9,241,257 | 0.69% | $63,765 | 0.00% | $0 | 0.69% | $63,765 |
| Vanguard Emerging Markets Stock Index Fund - Instl. | $8,461,803 | 0.12% | $10,154 | 0.00% | $0 | 0.12% | $10,154 |
| Laudus Mondrian Emerging Markets Instl. | $1,159,379 | 1.20% | $13,913 | 0.00% | $0 | 1.20% | $13,913 |
| Cohen and Steers Instl. Realty Shares | $11,806,598 | 0.75% | $88,549 | 0.00% | $0 | 0.75% | $88,549 |
| Mutual Fund Window | $2,821,726 | 0.00% | $0 | 0.00% | $0 | 0.00% | $0 |
| **Total** | $673,329,370 | 0.19% | $1,270,421 | 0.02% | $119,806 | 0.21% | $1,390,227 |
| **Without Brokerage** | $670,507,643 | 0.19% | $1,270,421 | 0.02% | $119,806 | 0.21% | $1,390,227 |

# Ibbotson Model Portfolios – Performance

**As of 3/31/2016**

| | Performance(%) | | | |
|---|---|---|---|---|
| | 1 Quarter | 1 Year | Since Inception | Inception Date |
| **RC** | | | | |
| Very Conservative | 1.7 | 1.6 | 3.4 | 01/01/2014 |
| *Very Conservative Benchmark* | *1.6* | *0.3* | *2.0* | |
| Conservative | 1.6 | 0.6 | 3.3 | 01/01/2014 |
| *Conservative Benchmark* | *1.8* | *-0.6* | *2.2* | |
| Moderately Conservative | 1.4 | -0.3 | 3.8 | 01/01/2014 |
| *Moderately Conservative Benchmark* | *1.9* | *-1.1* | *2.8* | |
| Moderate | 1.4 | -1.3 | 3.7 | 01/01/2014 |
| *Moderate Benchmark* | *1.7* | *-2.2* | *2.6* | |
| Moderately Aggressive | 1.0 | -2.3 | 3.5 | 01/01/2014 |
| *Moderately Aggressive Benchmark* | *1.7* | *-2.9* | *2.6* | |
| Aggressive | 0.3 | -3.5 | 3.3 | 01/01/2014 |
| *Aggressive Benchmark* | *1.6* | *-3.9* | *2.4* | |
| Very Aggressive | 0.2 | -5.4 | 2.2 | 01/01/2014 |
| *Very Aggressive Benchmark* | *1.5* | *-4.8* | *2.2* | |
| **RCP** | | | | |
| Very Conservative | 1.6 | 1.3 | 3.1 | 01/01/2014 |
| *Very Conservative Benchmark* | *1.6* | *0.3* | *2.0* | |
| Conservative | 1.6 | 0.2 | 3.1 | 01/01/2014 |
| *Conservative Benchmark* | *1.9* | *-0.6* | *2.3* | |
| Moderately Conservative | 1.5 | -0.6 | 3.6 | 01/01/2014 |
| *Moderately Conservative Benchmark* | *2.0* | *-1.1* | *2.9* | |
| Moderate | 1.5 | -1.6 | 3.5 | 01/01/2014 |
| *Moderate Benchmark* | *1.9* | *-2.3* | *2.7* | |
| Moderately Aggressive | 1.1 | -2.5 | 3.5 | 01/01/2014 |
| *Moderately Aggressive Benchmark* | *1.8* | *-3.0* | *2.7* | |
| Aggressive | 0.3 | -3.5 | 3.3 | 01/01/2014 |
| *Aggressive Benchmark* | *1.6* | *-3.9* | *2.4* | |
| Very Aggressive | 0.2 | -5.4 | 2.2 | 01/01/2014 |
| *Very Aggressive Benchmark* | *1.5* | *-4.8* | *2.2* | |

# Ibbotson Model Portfolios – Allocations

**RC**

| Fund Name | Very Conservative | Conservative | Moderately Conservative | Moderate | Moderately Aggressive | Aggressive | Very Aggressive |
|---|---|---|---|---|---|---|---|
| TIAA Traditional | 40% | 34% | 30% | 22% | 15% | 7% | - |
| Cohen & Steers Instl Realty Shares | - | - | 3% | 3% | 3% | 3% | 3% |
| DFA Inflation-Protected Securities I | 7% | 7% | 6% | 4% | 3% | - | - |
| DFA US Targeted Value I | - | 3% | - | - | - | - | - |
| Diamond Hill Large Cap Y | - | - | 3% | 5% | 6% | 8% | 4% |
| Dodge & Cox Global Stock | - | 3% | 14% | 15% | 22% | 27% | 27% |
| Harding Loevner International Eq Instl | - | 7% | 4% | - | - | - | - |
| MFS International Value R5 | 3% | - | - | 5% | 5% | 7% | - |
| Neuberger Berman High Income Bond R6 | 7% | 8% | 6% | 6% | 3% | - | - |
| PIMCO Total Return Instl | 28% | 14% | 5% | - | - | - | - |
| T. Rowe Price Instl Large Cap Growth | - | - | - | - | - | 6% | - |
| Vanguard Developed Markets Idx Instl | - | - | - | - | - | - | 11% |
| Vanguard Emerging Mkts Stock Idx I | - | - | - | 3% | 3% | 4% | 6% |
| Vanguard Extended Market Idx I | 3% | 3% | 5% | 11% | 12% | 13% | 18% |
| Vanguard Institutional Index I | 3% | 13% | 16% | 18% | 23% | 20% | 31% |
| Vanguard Prime Money Market Instl | 6% | 4% | - | - | - | - | - |
| Vanguard Total Bond Market Index I | 3% | 4% | 8% | 8% | 5% | 5% | - |

**RCP**

| Fund Name | Very Conservative | Conservative | Moderately Conservative | Moderate | Moderately Aggressive | Aggressive | Very Aggressive |
|---|---|---|---|---|---|---|---|
| TIAA Traditional | 40% | 32% | 25% | 16% | 10% | 5% | - |
| Cohen & Steers Instl Realty Shares | - | - | 3% | 3% | 3% | 3% | 3% |
| DFA Inflation-Protected Securities I | 7% | 7% | 6% | 4% | 3% | - | - |
| DFA US Targeted Value I | - | 3% | - | - | - | - | - |
| Diamond Hill Large Cap Y | - | - | 3% | 5% | 6% | 8% | 4% |
| Dodge & Cox Global Stock | - | 4% | 14% | 15% | 22% | 27% | 27% |
| Harding Loevner International Eq Instl | - | 6% | 4% | - | - | - | - |
| MFS International Value R5 | 3% | - | - | 5% | 5% | 7% | - |
| Neuberger Berman High Income Bond R6 | 7% | 8% | 6% | 6% | 3% | - | - |
| PIMCO Total Return Instl | 28% | 14% | 6% | 3% | - | - | - |
| T. Rowe Price Instl Large Cap Growth | - | - | - | - | - | 6% | - |
| Vanguard Developed Markets Idx Instl | - | - | - | - | - | - | 11% |
| Vanguard Emerging Mkts Stock Idx I | - | - | - | 3% | 3% | 4% | 6% |
| Vanguard Extended Market Idx I | 3% | 3% | 5% | 11% | 12% | 13% | 18% |
| Vanguard Institutional Index I | 3% | 13% | 16% | 18% | 23% | 20% | 31% |
| Vanguard Prime Money Market Instl | 6% | 4% | - | - | - | - | - |
| Vanguard Total Bond Market Index I | 3% | 6% | 12% | 11% | 10% | 7% | - |

# Ibbotson Model Portfolios – Benchmarks

**RC Contract Portfolio Benchmarks**

| Index | Very Conservative | Conservative | Moderately Conservative | Moderate | Moderately Aggressive | Aggressive | Very Aggressive |
|---|---|---|---|---|---|---|---|
| Russell 1000 Growth Index | - | 5% | 7% | 9% | 11% | 13% | 15% |
| Russell 1000 Value Index | 4% | 8% | 9% | 12% | 15% | 16% | 18% |
| Russell Mid Cap Growth Index | 3% | 3% | 4% | 4% | 5% | 7% | 7% |
| Russell Mid Cap Value Index | - | 3% | 6% | 7% | 9% | 10% | 11% |
| Russell 2000 Growth Index | - | - | - | 3% | 3% | 4% | 4% |
| Russell 2000 Value Index | - | 3% | 3% | 4% | 5% | 6% | 7% |
| MSCI All Country World ex-U.S. Index | 3% | 5% | 10% | 13% | 16% | 20% | 24% |
| MSCI Emerging Markets Index | - | 3% | 3% | 5% | 6% | 8% | 10% |
| FTSE NAREIT Equity REIT Index | - | - | 3% | 3% | 3% | 3% | 4% |
| Barclays Corporate High Yield Index | 9% | 8% | 6% | 5% | 3% | - | - |
| Barclays U.S. TIPS Index | 9% | 7% | 6% | 4% | 3% | - | - |
| Barclays Long-Term Bond Index | 6% | 5% | 4% | 3% | 3% | 3% | - |
| Barclays Capital US 1-3 Year Government/Credit Bond Index | 22% | 13% | 9% | 6% | 3% | 3% | - |
| BofA Merrill Lynch US 3-Month Treasury Bill | 4% | 3% | - | - | - | - | - |
| Hueler Stable Value Index | 40% | 34% | 30% | 22% | 15% | 7% | - |

**RCP Contract Portfolio Benchmarks**

| Index | Very Conservative | Conservative | Moderately Conservative | Moderate | Moderately Aggressive | Aggressive | Very Aggressive |
|---|---|---|---|---|---|---|---|
| Russell 1000 Growth Index | - | 5% | 7% | 9% | 11% | 13% | 15% |
| Russell 1000 Value Index | 4% | 8% | 9% | 12% | 15% | 16% | 18% |
| Russell Mid Cap Growth Index | 3% | 3% | 4% | 4% | 5% | 7% | 7% |
| Russell Mid Cap Value Index | - | 3% | 6% | 7% | 9% | 10% | 11% |
| Russell 2000 Growth Index | - | - | - | 3% | 3% | 4% | 4% |
| Russell 2000 Value Index | - | 3% | 3% | 4% | 5% | 6% | 7% |
| MSCI All Country World ex-U.S. Index | 3% | 5% | 10% | 13% | 16% | 20% | 24% |
| MSCI Emerging Markets Index | - | 3% | 3% | 5% | 6% | 8% | 10% |
| FTSE NAREIT Equity REIT Index | - | - | 3% | 3% | 3% | 3% | 4% |
| Barclays Corporate High Yield Index | 9% | 8% | 6% | 5% | 3% | - | - |
| Barclays U.S. TIPS Index | 9% | 7% | 6% | 4% | 3% | - | - |
| Barclays Long-Term Bond Index | 6% | 6% | 6% | 5% | 4% | 5% | - |
| Barclays Capital US 1-3 Year Government/Credit Bond Index | 22% | 14% | 12% | 10% | 7% | 3% | - |
| BofA Merrill Lynch US 3-Month Treasury Bill | 4% | 3% | - | - | - | - | - |
| Hueler Stable Value Index | 40% | 32% | 25% | 16% | 10% | 5% | - |

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# Agenda Tracker

# Vanguard Target Retirement Funds

- All of the Vanguard Target Retirement Funds posted positive returns which approximated their respective performance benchmarks and exceeded the average return of their respective peer groups during the first quarter
  - In  a reversal from the fourth quarter, the shorter-dated Funds, with their greater exposure to fixed income, posted the strongest absolute returns
    - The 10-year U.S. Treasury yield fell to historic lows not seen since 2012, the Barclays Aggregate Bond Index returned 3.0% during the period
    - Treasury Inflation-Protected Securities generated a 4.5% return during the quarter
  - The longer-dated funds, with their greater international equity exposure, posted lower absolute returns
    - The FTSE Global All Cap ex US Index declined 8.0% during the quarter
- For the trailing one-year period, the returns for the Target Retirement Funds varied depending on their maturity
  - The shorter-dated funds, with their greater fixed income exposure, posted modestly positive returns
  - The longer-dated funds, with their greater exposure to equities, posted negative absolute returns
- Longer-term results continued to closely track their respective performance benchmarks and rank favorably among their respective peer-groups

***The 403(b) Plans will transition to the lower cost "Institutional" class shares  of the Target Retirement Funds on July 29, 2016***

# Vanguard Passive Equity Team Changes

- Vanguard recently announced a number of portfolio manager changes that involve the Vanguard Equity Index Group effective April 27, 2016
  - Vanguard Institutional Index Fund
    - Continuing manager: Donald M. Butler, CFA
    - New manager: Scott E. Geiger
  - Vanguard Extended Market Index Fund
    - Continuing manager: Donald M. Butler, CFA
    - New manager: Scott E. Geiger
- The funds' investment philosophies, objectives, strategies, and overall portfolio management processes will remain the same
- These changes reflect the firm's long-standing practice of periodically rotating members of its day-to-day portfolio management teams to broaden their experience and provide them with new responsibilities
  - There were no departures from the firm
- After review, our Global Investment Management research team believes that the team changes will have no impact on the passive equity strategies at Vanguard
- Our rating for the Vanguard Passive Equity Platform remains "Buy" rated and we recommend that the Committee take no action
- A memorandum detailing our observations is included in Section 4 of this presentation

# PIMCO Total Return Fund

- The Fund registered “Yellow” on the Watch List during the first quarter
  – Due to the manager’s historical underperformance relative to its benchmark over the trailing five-year period and in three of the four most recent trailing calendar quarters
- The Fund underperformed its benchmark, the Barclays U.S. Aggregate Index, by 1.2 percentage points during the first quarter
- The Fund’s underperformance was primarily attributable to:
  – Shorter-than-benchmark duration positioning within the U.S. as interest rates fell
  – An underweight allocation to investment grade corporate credits
  – Negative security selection within non-agency mortgage-backed securities (MBS)
- Partially offsetting the period's negative results was sector and security selection within dollar-denominated emerging market (EM) debt which rallied during the period
- For the trailing one-year period, the Fund generated a return of 0.3% versus the benchmark’s return of 2.0%
- Longer-term results remain mixed relative to the Barclays U.S. Aggregate Index and peers
- We continue to closely monitor the Fund’s positioning and performance but recommend the Committee take no action as the investment team remains consistent and continues to execute on its historic philosophy and process
- The strategy remains “Buy” rated by our Global Investment Management research team

# Dodge & Cox Global Stock Fund

- The Fund underperformed its benchmark, MSCI All Country World Index, by 1.5 percentage points during the first quarter
- The Fund's underperformance was primarily attributable to:
  - Negative stock selection within the energy sector along with an underweight positioning within the utilities sector
  - Holdings within the financials sector combined with an overweight allocation
    - Detractors included Credit Suisse (-34%), Barclays (-32%), Standard Chartered (-18%), Bank of America (-19%), and Charles Schwab (-15%).
- Partially offsetting negative results was the Fund's overweight positioning in emerging markets and positive stock selection within the information technology and materials sectors
- For the 12 months ending March 31, 2016, the Fund underperformed its benchmark by 6.3 percentage points
  - An overweight positioning within emerging markets, a particularly weak region of the portfolio, significantly detracted from results
- Longer-term results continued to remain favorable
- The strategy remains "Buy" rated by our Global Investment Management Research Team

# Neuberger Berman High Income Bond Fund

- The Fund continued to register "Red" on the Watch List during the quarter
  - Due to the manager's historical underperformance relative to its benchmark over the trailing five-year period and in three of the four most recent trailing calendar quarters
- While positive in absolute terms, the Fund's performance lagged its benchmark, the Barclays Corporate High Yield Index, by 0.5 percentage points during the first quarter
- The Fund's underperformance was primarily attributable to:
  - Negative security selection within the health care sector (Valeant Pharmaceuticals)
  - An underweight allocation to the energy and metals/mining sectors
- For the trailing one-year period, the Fund generated a return of -4.1% versus the benchmark's return of -3.7%
- Longer-term results continued to underperform the Barclays Corporate High Yield Index
- We continue to closely monitor the Fund's positioning and performance but recommend the Committee take no action as the investment team remains consistent and continues to execute on its historic philosophy and process
- The strategy remains "Buy" rated by our Global Investment Management research team

# T. Rowe Price Instl. Large Cap Growth Fund

- The Fund continued to register “Yellow” on the Watch List during the first quarter due to:
  - The Fund’s historical underperformance relative to its benchmark over the trailing five-year period
  - An adverse change in portfolio manager talent
- The Fund underperformed its benchmark, the Russell 1000 Growth Index, by 7.1 percentage points during the first quarter
- The Fund’s underperformance was primarily attributable to:
  - An overweight allocation and negative stock selection within the health care sector
    - Notable detractors include: Valeant Pharmaceuticals and Alexion Pharmaceuticals
  - Negative security selection within consumer discretionary and information technology sectors
- Partially offsetting the period's negative relative results was an underweight to the energy sector and positive stock selection within the materials sector
- For the trailing one-year period, the Fund generated a return of -2.4% versus the benchmark’s return of 2.5%
- Our Global Investment Management research team has maintained its “In Review” rating pending an upcoming meeting with Mr. Rob Sharps to gain additional insight into the transition as well as with Mr. Taymour Tamaddon to discuss his approach to managing a broader market portfolio
- We are continuing to monitor the situation closely and will keep the Committee informed of any change in our views
- We recommend the Committee take no action at this time

# DFA U.S. Targeted Value Fund

- The Fund registered "Yellow" on the Watch List during the first quarter due to:
  - Due to the manager's historical underperformance relative to its benchmark over the trailing five-year period and in three of the four most recent trailing calendar quarters
- The Fund underperformed its benchmark, the Russell 2500 Value Index, by 0.7 percentage points during the first quarter
- The Fund's underperformance was primarily attributable to:
  - The portfolio's higher allocation to deep value stocks
  - An underweight allocation to the REITs sector
- Partially offsetting negative results was favorable stock selection within the telecommunications services and utilities sectors
- For the trailing one-year period, the Fund generated a return of -7.0% versus the benchmark's return of -5.2%
- Longer-term results continued to remain favorable
- We continue to closely monitor the Fund's positioning and performance but recommend the Committee take no action as the investment team remains consistent and continues to execute on its historic philosophy and process
- The strategy remains "Buy" rated by our Global Investment Management Research Team

# Laudus Mondrian Emerging Markets Fund

- The Fund outperformed its benchmark, the MSCI Emerging Markets Index, by 1.3 percentage points during the first quarter
- The Fund's outperformance was primarily attributable to:
  - Positive stock selection and an underweight allocation to China
  - Overweight allocations to the outperforming Indonesian and Taiwanese markets
  - Positive stock selection within the health care sector
- Partially offsetting the period's positive results was underweight positions to the outperforming, commodity influenced, South African and Russian markets along with underweight exposure to the energy and materials sector
- For the trailing one-year period, the Fund generated a return of -12.9% versus the benchmark's return of -12.0%
- Longer-term results remained unfavorable relative to the benchmark
- As an important part of the ongoing due diligence process, the Committee asked AHIC to identify emerging market equity manager candidates that could serve as a potential replacement to the Laudus Mondrian Emerging Markets Fund
- A "Competitive Review" profiling alternative manager candidates has been included with this presentation

# Cohen and Steers Instl. Realty Shares

- The Fund had a positive return for the quarter, although it underperformed its benchmark, the FTSE NAREIT Equity REIT Index, by 2.1 percentage points
- The Fund's underperformance was primarily attributable to:
  - An overweight allocations and negative stock selection within the office sector
  - Negative security selection within the health care property, apartment, and data center sectors
- Partially offsetting negative results was favorable stock selection within the regional mall sector and an overweight allocation to self storage REITs
- For the trailing one-year period, the Fund generated a return of 3.9% versus the benchmark's return of 4.4%
- Longer-term results remained mixed relative to the benchmark
- The strategy remains "Buy" rated by our Global Investment Management Research Team

# Agenda Tracker

# Flash Report

## Vanguard Group Inc. – Passive Equity Team Announcements

### Recommendation

Vanguard recently announced several portfolio manager changes that involve the Vanguard Equity Index Group effective April 27, 2016. There were no departures from the firm and the portfolio manager changes made were simply a rotation of internal staff. Some of the individuals who were previously named portfolio managers on the firm's index funds have now taken on broader leadership positions within the firm and gave up their day-to-day portfolio management responsibilities for the funds. In addition, some of the changes were promotions of existing staff to portfolio manager positions.

After further review, we believe that the team changes will have no impact on the passive equity strategies at Vanguard, including the investment objectives, strategies, and overall portfolio management processes. As a result, our rating for the Vanguard Passive Equity Platform remains "Buy" rated and we recommend that clients take no action at this time.

### Background

We conducted a conference call with representatives from Vanguard to discuss the portfolio manager changes in more detail. We learned that no one is leaving the firm as a result of this news. Rather, these changes reflect the firm's long-standing practice of periodically rotating members of its day-to-day portfolio management teams to broaden their experience and provide them with new responsibilities. There will be no impact to the investment process or trading of the funds listed below as a result of the team changes.

The portfolio management duties for an equity index portfolio manager include monitoring cash flows, submitting trades when needed, and implementing trading around index holding changes when they occur. These duties contrast greatly with that of active equity portfolio managers who are actively making stock purchase and sell decisions by conducting qualitative and/or quantitative research on companies.

Details of the portfolio manager changes are below:

Vanguard 500 Index Fund
Former manager: Michael H. Buek, CFA
New managers: Donald M. Butler, CFA and Scott E. Geiger

Vanguard Extended Market Index Fund
Continuing manager: Donald M. Butler, CFA
New manager: Scott E. Geiger

Vanguard Growth Index Fund
Continuing manager: Gerard C. O'Reilly
New manager: Walter Nejman

Vanguard Institutional Index Fund
Continuing manager: Donald M. Butler, CFA
New manager: Scott E. Geiger

Vanguard Institutional Total Stock Market Index Fund
Former manager: Michael Perre
New managers: Gerard C. O'Reilly and Walter Nejman

Vanguard Large-Cap Index Fund
Former manager: Ryan E. Ludt
New managers: Michael A. Johnson and Walter Nejman

Vanguard Mid-Cap Growth Index Fund
Continuing manager: Donald M. Butler, CFA
New manager: Michael A. Johnson

Vanguard Mid-Cap Index Fund
Continuing manager: Donald M. Butler, CFA
New manager: Michael A. Johnson

Vanguard Mid-Cap Value Index Fund
Continuing manager: Donald M. Butler, CFA
New manager: Michael A. Johnson

Vanguard Small-Cap Growth Index Fund
Continuing manager: Gerard C. O'Reilly
New manager: William Coleman

Vanguard Small-Cap Index Fund
Former manager: Michael H. Buek, CFA
New managers: Gerard C. O'Reilly and William Coleman

Vanguard Small-Cap Value Index Fund
Former manager: Michael H. Buek, CFA
New managers: Gerard C. O'Reillyand William Coleman

Vanguard Total Stock Market Index Fund
Continuing manager: Gerard C. O'Reilly
New manager: Walter Nejman

Vanguard Value Index Fund
Continuing manager: Gerard C. O'Reilly
New manager: Walter Nejman

## Disclaimer

This document has been produced by the Global Investment Management Team of Aon plc. Nothing in this document should be treated as an authoritative statement of the law on any particular aspect or in any specific case. It should not be taken as financial advice and action should not be taken as a result of this document alone. Consultants will be pleased to answer questions on its contents but cannot give individual financial advice. Individuals are recommended to seek independent financial advice in respect of their own personal circumstances.

The Aon Centre
The Leadenhall Building
122 Leadenhall Street
London
EC3V 4AN

# Agenda Tracker

# Responsibilities in Relation to Service Providers

- Hiring a service provider is a fiduciary function
  - Service providers must indicate the services they will provide to the plan and the compensation they will receive
- Once hired, a service provider must be monitored
  - A formal review process should be established and followed regularly
  - Process will decide whether to continue using current service provider or to find a replacement
  - An employer must ensure they are performing the services they agreed to when hired
  - The Department of Labor (DOL) suggests the following:
    - ➢ Evaluating any notices received from the service provider about possible changes to their compensation;
    - ➢ Reviewing the service providers' performance;
    - ➢ Reading any reports they provide;
    - ➢ Checking actual fees charged;
    - ➢ Asking about policies and practices (such as trading, investment turnover, and proxy voting); and
    - ➢ Following up on participant complaints.

Source: Meeting Your Fiduciary Responsibilities, United States Department of Labor, February 2012
https://www.dol.gov/ebsa/publications/fiduciaryresponsibility.html

# Challenge of Committee Confidentiality and Communications

- As NSHE is a public entity, the confidentiality of items discussed in the meeting can be challenging as the meeting minutes and other information are posted publicly
- RPAC members should be aware of the importance of the method and timing of communications to service providers or other third parties
  - The impact of these actions can reduce NSHE's ability to negotiate the most favorable terms on products and/or services
- Although there is not a specific confidentiality or communication policy in place at this time, communications with all service providers should be done as agreed upon
  - This includes communicating decided-upon actions or exploring (when warranted) ideas that have not yet been fully vetted
- AHIC recommends that all communications with service providers are directed by the Executive Officer
- Other alternatives that AHIC has observed with public entity clients include:
  - Developing a formal communication policy that addresses what information not contained within the minutes can be conveyed to the public and by whom
  - Adding a section in the Charge to the Committee that addresses any post-meeting communications

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# Agenda Tracker


Second Quarter 2016

# Quarterly Update

*Aon Hewitt Retirement Legal Consulting & Compliance*

## In this Issue



## Prior Issues


Prior issues can be found on aon.com.

**Four most recent issues** - Click here Select “Newsletters”

**Older editions** - Click here
Select “Retirement Practice Legal Consulting & Compliance Quarterly Update” in the Newsletters section.


## Notes From Your Editor

Hello and welcome to the second quarter 2016 edition of the *Retirement Legal Consulting & Compliance Quarterly Update*. We start this issue with an overview of long-promised final regulations on fiduciary requirements related to employee benefit plans and IRAs. This initial article gives an overview of the regulations and some guidance to plan sponsors on where to begin assessing the applicability of these rules.

Next we provide a detailed update of the status of fiduciary litigation involving employer stock investments in qualified plans. We have been following several of the leading cases in this area, and the holdings can be quite instructive for plan sponsors.

The Internal Revenue Service (IRS) has issued welcome nondiscrimination testing relief for closed defined benefit plans. Included is an extensive article on the proposal and what this means for plan sponsors. As part of the same regulations, there was an effort to curtail the practice of shifting nonqualified plan benefits to qualified plans. The IRS withdrew that portion of the regulations for now but we can anticipate that the IRS will continue to scrutinize this area and may provide further guidance in the future. The IRS has also loosened up its rules about the changes that can be made mid-year to safe harbor plan formulas, changes that should provide more flexibility for plan sponsors.

The Department of Labor (DOL) has also raised some concerns about missing participants in large pension plans. An article outlining details of this initiative is included and describes some actions that plan sponsors can take now to mitigate the risk of a plan audit.

We also discuss new case law related to a plan sponsor’s successful attempt to limit litigation by imposing a plan-based limitation period on filing a Federal lawsuit as part of the plan’s claim procedures. Finally, as plan sponsors continue to evaluate their pension funding obligations, we have provided an excerpt of a longer report detailing items to consider when pre-funding pension plans.

If you have any questions or need any assistance with the topics covered, please contact the author of the article or Tom Meagher, our practice leader.

Regards,

Jennifer R Berrian


**Jennifer Ross Berrian**
Partner
Aon Hewitt
Jennifer.Ross.Berrian@aonhewitt.com

# New Fiduciary Rules—Initial Steps for Plan Sponsors

by Tom Meagher and Elizabeth Groenewegen

The U.S. Department of Labor (DOL) has now issued the final fiduciary regulations under the Employee Retirement Income Security Act of 1974 (ERISA), but the path to issuance was not without its challenges. As part of the regulatory process, the DOL heard from more than 75 speakers and received more than 3,000 comment letters from consumer groups, plan sponsors, trade and industry associations, and financial services companies. This initial article on the new regulations focuses on some of the more significant highlights of the final rules. The new rules are intended to protect employee benefit plans, plan fiduciaries, plan participants and beneficiaries, IRAs, and IRA owners. In reviewing the final regulations from the standpoint of plan sponsors, there are a number of areas that should be examined and evaluated as plan sponsors confirm the fiduciary status of those individuals and organizations providing support to the plans and their participants.

As a starting point, it is important to note that the final fiduciary rules will cover employee benefit plans as well as certain individual savings arrangements (including individual retirement accounts or annuities, health savings accounts, Archer Medical Savings Accounts, and Coverdell Education Savings Accounts) that are tax-favored under the Internal Revenue Code (Code). A 403(b) plan will be covered by the fiduciary rules if the plan is subject to ERISA. Programs that are either a "governmental plan" or a nonelecting "church plan" are not subject to ERISA, and thus, not subject to the new fiduciary regulations, but other Code and state law provisions will continue to apply.

At the outset, the DOL issued the final regulations in an effort to identify who may be treated as a fiduciary under ERISA and the Code as a result of receiving a fee or other compensation for providing investment advice to a plan or IRA, or to their participants, beneficiaries, or owners. The fiduciary rules are intended to expand the group of persons who may be viewed as fiduciaries and require that they act in the best interest of their clients.

From a plan sponsor perspective, there are a number of situations and relationships that may require closer scrutiny in an effort to determine if they may involve the provision of investment advice for a fee or other form of compensation. One area expected to receive significant attention from plan sponsors is the provision of investment education designed to advise plan participants as to how best to save and invest for retirement. There has long been a concern that such education may rise to the level of providing investment advice and may cause the plan sponsor to become an ERISA fiduciary with respect to such underlying investment decisions by participants. Under the final rules, there are four broad categories of investment education that will not subject the plan sponsor (or educator) to the fiduciary rules, provided the necessary criteria are satisfied:

- Providing information about the plan (Plan Information)
- Providing general financial, retirement, and investment information
- Providing asset allocation models
- Providing interactive investment materials

In addition, an area that has been of some concern to plan sponsors (and the DOL) relates to communications or information provided to participants regarding rollovers. Recommendations with respect to rollovers or other forms of distribution may be treated as fiduciary investment advice under the final regulations. However, plan sponsors will not be considered to be providing investment advice to the extent that they provide information and materials under the Plan Information exception noted above that describes, for instance, the terms or operation of the plan and the forms of distribution available (including rollovers, annuitization, and other forms of lifetime income payment options). This exception does not apply to the extent that the information references the appropriateness of any individual investment alternative or individual benefit distribution option, or its applicability for a particular plan participant.

"The fiduciary rules are intended to expand the group of persons who may be viewed as fiduciaries and require that they act in the best interest of their clients."

As a practical matter, plan sponsors should begin to evaluate the roles of any financial advisors with whom the plan fiduciaries work to confirm if such advisors are acting as fiduciaries to the plan, and will want to confirm the roles of in-house employees who may provide investment recommendations to a plan or fiduciary committee. Depending on what roles are in-sourced or outsourced, plan sponsors also may want to confirm the roles that call center and human resources employees may play with respect to communicating with plan participants regarding plan investments and rollover alternatives.

The above summary is only the very beginning of what will likely involve a careful analysis by plan sponsors as to who provides services to the plan and its participants, what activities rise to the level of being fiduciary investment advice, and how third parties and other service providers may be positioned in terms of having fiduciary obligations to act in the best interest of the plan participants. We will be providing much more detail on how these rules will apply to plan sponsors in these and other areas in the coming weeks. While the new regulations are effective on June 7, 2016, the rules will not become applicable until April 10, 2017, and some provisions may have later phased-in effective dates. This delay will allow plan sponsors to carefully evaluate how the new rules apply to their plans and to take any necessary actions.

# Federal Courts Raise Bar for Employer Stock Claims

by Hitz Burton

As various fiduciary breach class action claims involving qualified retirement plan investments in employer stock continue to be litigated, four recent decisions and one settlement agreement highlight difficulties faced by plaintiffs in articulating plausible claims. As you will recall, the U.S. Supreme Court's 2014 decision in *Fifth Third Bank v. Dudenhoeffer* rejected the employer-friendly presumption that qualified plan investments in employer stock were generally prudent. While the U.S. Supreme Court decision decided against a presumption of prudence, it replaced the presumption with new, more rigorous pleading standards for lawsuits challenging qualified plan investments in employer stock. Additionally, and as a benefit to public company sponsors with employer stock investments in their 401(k) or other qualified plans, *Dudenhoeffer* emphasized that the market for publicly traded securities is generally efficient and the best estimate of market value absent "special circumstances."

Mindful of the new pleading standards, plaintiffs in various recent class-based employer stock claims have argued that fiduciaries breached their duties under the Employee Retirement Income Security Act of 1974 (ERISA) because they:

- Knew or should have known, based on publicly available information, that the employer stock at issue was mispriced; or
- Imprudently permitted ongoing investments in "artificially inflated" employer stock (or held stock they previously bought but should have sold at a higher price) based on "inside information" allegedly known to the plan fiduciaries.

**Update on *Amgen, Inc. v. Harris***

In *Amgen, Inc. v. Harris*, the U.S. Supreme Court issued a pointed rebuke to the Ninth Circuit Court of Appeals which, in the view of the Supreme Court, failed to properly apply the post-*Dudenhoeffer* pleading standards in evaluating whether a complaint alleged sufficient facts in an employer stock-drop case to support a fiduciary breach claim under ERISA.

The Ninth Circuit had previously held, shortly before the U.S. Supreme Court announced its decision in *Dudenhoeffer*, that the Amgen plaintiffs had plausibly alleged that removing the employer stock fund from the Amgen 401(k) plan would not have resulted in "undue harm" to the plan. Surprisingly, and contrary to custom in the federal courts, the Ninth Circuit declined to reevaluate this finding in light of the result reached by the U.S. Supreme Court shortly thereafter in *Dudenhoeffer*; and even after the U.S. Supreme Court, in its instructions on remand in an earlier appeal in *Amgen*, indicated that the lower court would likely need to reconsider its determination in light of *Dudenhoeffer*.

Going forward, plan sponsors should understand that litigants who wish to bring similar breach of fiduciary duty of prudence claims will likely need to allege with specific detail that fiduciaries should have directed that the plan either stop additional purchases of employer stock (which investors may view as a negative sign) or disclose the relevant nonpublic information to the public. Additionally, plaintiffs also will likely have to articulate how such decisions would not cause more harm than good to plan participants and, further, how they could make these disclosures without violating federal securities law.

***Rinehart v. Lehman Brothers Holdings, Inc.***

In an action involving an employee stock ownership plan (ESOP) covering employees of Lehman Brothers, the Second Circuit Court of Appeals affirmed the determination made by the district court that the class participants failed to allege, with sufficient specificity, that the Lehman ESOP fiduciaries breached their ERISA duty of prudence.

The primary allegation put forward by the Lehman participants in *Rinehart* was that the ESOP fiduciaries knew or should have known, based on publicly available information, that continued investment by the ESOP in Lehman Brothers stock was "too risky" and, therefore, imprudent.

> "While the U.S. Supreme Court decision decided against a presumption of prudence, it replaced the presumption with new, more rigorous pleading standards for lawsuits challenging qualified plan investments in employer stock."

The Second Circuit saw little to no distinction between the participant claims that Lehman stock was "too risky" and previous, typically unsuccessful, post-*Dudenhoeffer* claims made by unrelated plaintiffs since 2014 that certain employer securities were "overvalued." Putting forward allegations of imprudence based on information that was available to the investing public, regardless of whether these allegations are framed in terms of market value (i.e., fiduciaries allowed the plan to imprudently purchase shares at too high a price) or excessive risk must still overcome the efficient market hypothesis that the perceived risk (or perceived value) associated with a particular stock is already accounted for in the then-current market price of the security.

**Update on *Tatum v. R.J. Reynolds Tobacco Co.***

In perhaps the most surprising recent development in this area, the district court in *Tatum* held that, despite the fact that the fiduciaries were previously found by the Fourth Circuit Court of Appeals to have failed to follow a prudent process in deciding to eliminate two stock funds from the RJR 401(k) plan, their decisions, were, nonetheless, prudent. "It is more likely than not," the district court noted, "that had a prudent fiduciary reviewed the information available at the time, including plan documents, public disclosures, analysts reports and associated research . . . it *would have* decided to divest the Nabisco Funds at the time and in the manner as did RJR." (Emphasis added). Among other considerations, the outcome in this district court decision may reflect that the potential problems associated with the Fourth Circuit's controversial "would have" standard (i.e., fiduciaries defending themselves from a breach of fiduciary prudence claim need to demonstrate not simply that a reasonable fiduciary <u>could have</u> decided to pursue the same course of action they pursued but that a reasonable fiduciary <u>would have</u> decided on the same or similar course of action).

**Update on *Tibble v. Edison International***

An approximately 10-year battle between class litigants and Edison International that previously resulted in the U.S. Supreme Court holding that ERISA fiduciaries have an ongoing duty to monitor the prudence of a plan's designated investment options, including any applicable employer stock fund, ended on procedural grounds when a three-judge panel of the Ninth Circuit Court of Appeals determined, not surprisingly, that the Edison plaintiffs had waived their ability to make this particular breach of fiduciary prudence claim when the same plaintiffs had previously failed to raise this specific claim in their initial complaint before the district court or in their brief on appeal to the Ninth Circuit.

**Update on *Fifth Third Bank v. Dudenhoeffer***

Finally, a settlement agreement was recently announced between the *Fifth Third Bank* defendants and the *Dudenhoeffer* plaintiffs intended to end the case that reignited so much activity in this type of ERISA litigation. While it is not unusual for ERISA stock-drop claims to end with settlement agreements between the parties, certain terms of the settlement with the *Dudenhoeffer* plaintiffs were noteworthy, including Fifth Third Bank's agreement to (1) close the employer stock fund to new investments; (2) bar new participants from making investments in the employer stock fund and to fund employer matching contributions in cash for the next eight years; (3) provide annual notification to employees with 20% or more of their account balance invested in the employer stock fund and remind them of the importance of a diversified investment portfolio for retirement; (4) provide twice annual training to plan fiduciaries; and (5) pay a comparatively small $6 million dollar settlement amount to be split between the attorneys and the eligible class participants.

**Other Information**

Prior articles on these cases are available by clicking on the following links:

**"Evaluation of Employer Stock Fund Investments"**

**"Fiduciaries Have Ongoing Duty to Monitor Investments"**

**"Post-Dudenhoeffer Court of Appeals Decision Provides Surprises"**

**"Employer Stock: Renewed Focus Required of Plan Fiduciaries"**

**"Recent Case Law Developments"**

# More Mid-year Changes to Safe Harbor Plans Permitted

by Dan Schwallie

The Internal Revenue Service (IRS) recently issued Notice 2016-16, providing safe harbor 401(k) plan sponsors with welcome flexibility to make additional mid-year plan changes. Previously, once a sponsor provided the plan's safe harbor notice, the safe harbor formula generally could not be amended mid-year unless the employer was operating at an economic loss or a prior notice of intent to reduce or suspend safe harbor employer contributions had been provided. Although certain mid-year changes are still prohibited (or covered by other guidance), the new rules permit many mid-year changes that previously were thought impermissible.

The new rules do not modify the information required to be included in the safe harbor notice. They make clear that no additional notice or election opportunity is needed for changes to information that was included in the safe harbor notice but not required. However, if a permitted mid-year plan change would change required content in the safe harbor notice, the plan sponsor must:

- Provide an updated safe harbor notice 30–90 days before the effective date of the change that describes the midyear change and its effective date; and
- Give each participant a reasonable period of time to change the participant's elections after receipt of the notice and before the effective date of the change.

"...the new rules permit many mid-year changes that previously were thought impermissible."

Assuming the sponsor satisfies the updated notice and election opportunity rules described above, a few examples of midyear amendments permitted by the new rules that plan sponsors may have occasion to consider include:

- Increasing future safe harbor nonelective (nonmatching) contributions for all eligible employees
- Changing the plan's default investment
- Adding an age 59½ in-service withdrawal feature
- Increasing the plan's safe harbor matching contribution or adding discretionary matching contributions, provided that the change is retroactive for the entire plan year and the amendment is adopted, and an updated notice and election opportunity are provided, at least three months prior to the end of the plan year

Aon Hewitt's Retirement Legal Consulting & Compliance consultants can assist plan sponsors in understanding these new rules, planning for a mid-year safe harbor plan change, and amending the plan.

# Strategy for Prefunding Pension Plans

by Vlad Sachelarie

Seven years after the U.S. stock market hit bottom in the global financial crisis, defined benefit (DB) pension plans continue to run significant deficits. At year-end 2015, Aon Hewitt estimates the aggregate pension deficit for S&P 500 companies to be $445 billion. One might expect that the prolonged underfunded position would result in significant required contributions on the horizon. However, two key themes have emerged from regulatory activity over this period:

- Required contributions have been deferred by Congress; and
- The annual penalty for maintaining an underfunded plan has increased significantly. The Pension Benefit Guaranty Corporation (PBGC) premium assessed on pension deficits will rise five-fold, from 0.90% in 2013 to 4.50% by 2020.

This mixed bag of regulatory changes has given plan sponsors the flexibility to reduce contributions to DB pension plans, while at the same time increasing the financial penalties for doing so. These conflicting factors have prompted many plan sponsors to review their approach to pension plan funding. In an effort to assist plan sponsors with such a review, Aon Hewitt has recently published a report laying out the considerations for prefunding an underfunded pension plan. Some of the key highlights of the report include:

- The decision to make discretionary pension contributions (i.e., prefund) should be considered as part of an organization's overall capital budgeting strategy. Like other capital budgeting decisions, pension funding should be evaluated both relative to the organization's cost of capital and other uses of capital.
- Many plan sponsors will find significant advantages to prefunding to avoid PBGC premiums. Organizations without sufficient cash reserves may find it attractive to borrow to fund the plan.
- Borrowing to fund effectively exchanges soft debt for hard debt. While most rating agencies and lenders consider pension deficits to represent long-term liabilities similar to long-term debt, there are differences in the impact on other financial risk measures such as interest coverage ratios that should be considered.
- The attractiveness of such a strategy depends on the pension discount rate (typically, investment grade corporates), the tax status, and borrowing costs and capacity of the sponsor.
- If the after-tax borrowing cost is less than the sum of the pension discount rate and PBGC variable premium rate, the math is likely favorable to borrow to fund the plan.

**Please click here** to obtain a copy of the complete report. Contact your Aon Hewitt consultant for more information.

# Plan Document Deadline Bars Civil Suits

by Susan Motter

Every employee benefit plan covered by the Employee Retirement Income Security Act of 1974 (ERISA) must maintain claims procedures that outline the plan's procedural requirements for processing benefit claims. These claims procedures govern initial and appeal-level decisions, time frames for decision making, and disclosure requirements. If a plan fails to establish or follow claim procedures, a claimant will automatically be deemed to have exhausted all administrative remedies available under the plan, thus entitling the claimant to pursue any available remedy, including a federal lawsuit under ERISA.

As part of its claims procedures, a plan also may impose upon a claimant a deadline for bringing a civil suit. A recent case—*Smith v. The Boeing Company*—illustrates how a robust claims procedures process, including a plan requirement to bring suit within a stated deadline, may bar a claimant from suing if the claimant files suit after the plan's stated deadline.

The pension plan in the *Boeing* case maintained claims procedures for the processing of claims and appeals, as well as provided for a 180-day deadline for the filing of any civil suit following a decision on appeal. Smith, the widow-claimant, sought spousal death benefits, and was denied on appeal. She sued the plan five months after the plan's 180-day deadline. She did not claim that she was unaware of the deadline. Instead she contended in her suit that the 180-day deadline was unreasonable under Texas contract law, which requires a two-year limitations period.

The federal court in *Boeing* ruled in favor of the plan, holding the 180-day deadline as being reasonable, and therefore dismissed the widow's suit for being time-barred. The court cited a number of circuit court cases that upheld shorter limitations periods than those provided under state contract statutes based on the rationale that the application of borrowed state statutes runs the risk of creating a "national crazy quilt" of limitation periods enforceable in some states, but not in others.

In finding the 180-day deadline to be reasonable, the court applied a three-factor test. Specifically, the court found that the 180-day deadline was reasonable since (i) the Boeing plan gave the widow-claimant notice regarding the 180-day deadline, (ii) the Boeing plan promptly notified the widow-claimant of the decision on appeal, and (iii) the deadline to file a civil suit did not begin until the end of the appeals process.

The *Boeing* case provides the opportunity for some strategic planning on the part of plan sponsors. Plan sponsors, in an effort to mitigate the risk of plan litigation, may want to consider amending their employee benefit plans (and including such information in an updated summary plan description or summary of material modifications) to provide for a specified deadline for the filing of civil suits by a claimant after notice of a decision on appeal. A plan provision that limits the time for the bringing a civil suit by a claimant may be enforceable if the plan follows its claims procedures and satisfies the *Boeing* three-factor test.

Aon Hewitt's Retirement Legal Consulting & Compliance consultants have worked with a number of clients on these matters and are available to assist plan sponsors in evaluating their plans' claims procedures in light of the *Boeing* case.

# DOL Investigating Large Plan "Missing" Participant Procedures

by Elizabeth Groenewegen

Ongoing investigations of large defined benefit plans have revealed hundreds of millions of dollars of unpaid pension benefits, according to comments recently made by a Department of Labor (DOL) official. Elizabeth Hopkins, Counsel for Appellate and Special Litigation for the Plan Benefits Security Division of the DOL, spoke at a benefits conference in Los Angeles earlier this year. The DOL's investigation initiative may be a wake-up call to plan sponsors regarding locating terminated vested plan participants once those participants reach the date on which plan payments must commence.

According to Ms. Hopkins, the DOL focused its investigations on a handful of pension plans (reportedly, five or six) that have large numbers of participants. DOL requests were made for plan records of the ages and the payment status of those entitled to benefits under the plan. The DOL investigators reportedly found numerous instances of terminated participants past their required beginning dates for whom the payment of benefits had not yet commenced. Based on comments from the DOL, it appears that some of these individuals could have been located if reasonable steps had been taken to find them. Specific details about the results of these investigations, including any corrective actions, will not be forthcoming while the investigations remain ongoing. However, Ms. Hopkins noted that a plan's failure to locate individuals when benefits are due to be paid could be a breach of fiduciary duty under the Employee Retirement Income Security Act of 1974 (ERISA).

For background, a vested pension benefit becomes payable once the participant reaches normal retirement age (commonly, age 65). Payment can be delayed if the individual either remains in the employ of the plan sponsor or the plan permits deferral of the commencement of the pension benefit. If the individual is no longer employed by the plan sponsor, payment of the benefit must begin upon the individual's attainment of his or her required beginning date (April 1 of the calendar year after the calendar year in which the participant attains age 70½). No further delay is permissible beyond that age (unless the individual remains in the employ of the plan sponsor and the plan permits such delay).

From a plan sponsor perspective, challenges emerge if individuals have not remained in contact with the plan and cannot be located when benefit payments are due to commence. The DOL's enforcement effort is a reminder for plan sponsors of the importance of having procedures designed to ensure that vested benefits are paid in a timely fashion. While it is not entirely clear which particular steps may be required for a search to meet the applicable fiduciary standard, at a minimum a plan should have appropriate procedures to search for missing individuals and should ensure that those procedures are followed and participant situations addressed in advance of any required beginning date.

"The DOL investigators reportedly found numerous instances of terminated participants past their required beginning dates for whom the payment of benefits had not yet commenced. Based on comments from the DOL, it appears that some of these individuals could have been located if reasonable steps had been taken to find them."

In light of the DOL's initiative, it is a good time for plan sponsors to review their current plan practices. Are there comprehensive procedures for locating plan participants and beneficiaries? Are those procedures being consistently followed and coordinated with other organizations within the plan sponsor? Are the actions taken being adequately documented? Aon Hewitt is available to help. If Aon Hewitt provides recordkeeping services for the plan, the client team will be your primary resource for current plan practices. If Aon Hewitt is not the record keeper, please reach out to your Aon Hewitt retirement consultant or any member of the legal compliance and consulting group for assistance with reviewing and evaluating your plan's compliance.

# IRS Considering Rules to Eliminate Shifting of Executive Benefits to Qualified Plan

by Dan Schwallie

As part of the proposed regulations on closed defined benefit plans published January 29, 2016, the Internal Revenue Service (IRS) included rules that would have made it difficult for employers to take advantage of a nondiscrimination testing technique to shift nonqualified executive benefits to their qualified plans. This testing technique also has been relied upon by some employers to provide executives with enhanced qualified plan benefits. The proposed regulations would have made it quite difficult for plans identifying individual employees as eligible for an enhanced formula or nonqualified benefit shift by name or another identifier that does not satisfy IRS criteria as being based on a "reasonable business purpose."

However, IRS Announcement 2016-16, issued April 14, 2016, states that this aspect of the proposed regulations will be withdrawn, indicating that further consideration is needed. Plan sponsors should watch for future IRS guidance targeting plan designs that shift nonqualified benefits or otherwise enhance benefits to a select group. Employers who want to apply this nondiscrimination testing technique may wish to act quickly before the opportunity is gone. After revised guidance is finalized, plans may need to be amended to cease utilizing this technique, although it is not likely that past actions will need to be unwound. Please contact any member of the Retirement Legal Consulting & Compliance group for more information.

# IRS Proposes Permanent Testing Relief for Closed Plans

by Ron Gerard

The Internal Revenue Service (IRS) has delivered on its commitment to propose permanent relief from certain nondiscrimination testing requirements for defined benefit plans that provide ongoing accruals but are closed to new participants. These types of plans, known as "closed plans," present unique compliance challenges and have been the subject of limited, temporary relief that was scheduled to expire at the end of 2016. The IRS has now proposed to broaden that relief so that certain testing restrictions will no longer apply.

> "The primary purpose of the proposed regulations is "to help . . . preserve the retirement expectations of certain grandfathered groups of employees" in "situations in which the proportion of the grandfathered group of employees who are [HCEs] compared to the employer's total workforce has increased due to ordinary demographic changes.""

For closed plans, ongoing coverage testing requirements often become more difficult to satisfy over time, as nonhighly compensated employees (NHCEs) experience higher turnover rates than highly compensated employees (HCEs), pay increases push some of the participating NHCEs into the HCE category, and new employees (who are generally NHCEs) are not covered by the closed plan. Often the only way for the closed defined benefit (DB) plan to satisfy coverage requirements is for it to be aggregated with the defined contribution (DC) plan that covers the employer's new hires. In that case, the closed DB plan also is required to be aggregated with the DC plan to satisfy the other nondiscrimination rules of the Code, which can prove difficult to do unless the aggregated plans can meet the current regulatory requirements that allow them to be tested on the basis of equivalent benefits (a technique referred to as "cross-testing"). In Notices 2014-5 and 2015-28, the IRS provided temporary additional eligibility criteria that permit DB and DC plans to be cross-tested even if the plans do not meet any of the existing eligibility conditions for testing on that basis.

On January 29, 2016, the IRS issued proposed permanent changes to the regulations that would make it easier for closed plans to continue to satisfy nondiscrimination requirements. The primary purpose of the proposed regulations is "to help . . . preserve the retirement expectations of certain grandfathered groups of employees" in "situations in which the proportion of the grandfathered group of employees who are [HCEs] compared to the employer's total workforce has increased due to ordinary demographic changes." As a result, the IRS added a closed plan exception to the DB/DC plan rules in order to allow the aggregated plans to be cross-tested that would otherwise generally require that the DC plan provide a minimum allocation (gateway) for each NHCE in order to allow the aggregated plans to be cross-tested. The following conditions must be satisfied to qualify for the exemption:

- The DC plan must provide for nonelective employer contributions (fixed or discretionary profit-sharing contributions), not just matching contributions to 401(k) deferrals or employee stock ownership plan (ESOP) allocations.
- The closed DB plan must have been in effect for at least five years prior to the closure date and no significant change made to the closed plan during or since that time (except for certain permitted amendments).
- During the five-year period beginning on the closure date, either the closed plan must meet the nondiscrimination requirements without aggregation with any DC plan or the DB/DC plan must meet those requirements without resort to the gateway allocation.

The proposed regulations also establish a special nondiscrimination testing rule for a benefit, right, or feature (BRF) that is restricted to either a grandfathered group of employees who benefit under a closed formula or a nongrandfathered group that no longer benefits under a closed formula.

Greater flexibility is proposed for cross-testing defined benefit replacement allocations in DC-only plans, those that are reasonably designed to replace some or all of the benefits that would have been provided under the closed plan subject to a requirement that the allocations be provided in a consistent manner to all similarly situated employees. They also provide additional testing relief for DB/DC plans, including those that do not include a closed plan. These provisions are highly technical but may prove to be quite helpful under appropriate circumstances.

These regulations are in proposed form and will not take effect until the plan year beginning on or after the date they are issued as final regulations. Plan sponsors are permitted to apply the provisions of the proposed regulations related to closed DB plans to plan years beginning on or after January 1, 2014.

There is a lot that's included in these regulations and a lot that is not. Certain plans would be helped by the proposed relief and certain plans would receive no help (for example, closed plans that fail testing within five years of the closure date). Plan sponsors who have closed plans, have or are considering 401(k) plan designs that require aggregated testing or cross-testing under the nondiscrimination requirements for their profit-sharing contributions, or have converted their DB plan to a cash balance formula will want to contact any member of the Aon Hewitt Retirement Legal Consulting & Compliance practice for assistance in evaluating the applicability of these proposed regulations.

## Recent Publications

### ADP/ACP Safe Harbor Compensation Compliance Confusion

Dan Schwallie

*Journal of Deferred Compensation* 42 (Spring 2016)

ADP and ACP safe harbor plans require that a nondiscriminatory definition of compensation be used to determine safe harbor matching contributions. However, the plethora of permitted compensation definitions, and the rules surrounding them, can create compliance issues, particularly if the plan document, payroll, and record keeping are not properly coordinated.
**Click here to read the article.**

### Nonqualified Deferred Compensation and Domestic Relations Orders

Hitz Burton, Elizabeth Groenewegen, and Lee Nunn

*Journal of Deferred Compensation* 42 (Spring 2016)

Retirement plan assets are often a significant part of marital assets in a divorce. For executives, the most substantial retirement asset is often benefits due under one or more nonqualified plans (rather than under their employer's broad-based qualified pension and 401(k) and retirement saving plans). Unlike qualified pensions and retirement savings benefits, however, nonqualified benefits may be so difficult to divide that transferring other nonretirement assets to the nonemployee spouse is ordinarily more practical.
**Click here to read the article.**

### A Choice for Tax-Exempt Employers: 403(b) or 401(k) Plan?

Dan Schwallie

*Benefits Quarterly* (Second Quarter 2016)

Tax-exempt organizations can have either a 403(b) or 401(k) plan, or both, which leads some to consider whether they should have one over the other. Key differences between 403(b) and 401(k) plans are summarized in a convenient table of contrasts.
**Click here to read the article.**

# Key Contacts


**Tom Meagher**
Practice Leader
Somerset, NJ
732.302.2188
thomas.meagher@aonhewitt.com

**David Alpert**
Somerset, NJ
732.302.2502
david.alpert@aonhewitt.com

**Hitz Burton**
Newport Beach, CA
949.823.7417
hitz.burton@aonhewitt.com

**Ron Gerard**
Norwalk, CT
203.523.8266
ron.gerard@aonhewitt.com

**Elizabeth Groenewegen**
San Francisco, CA
415.486.6934
elizabeth.groenewegen@aonhewitt.com

**Dick Hinman**
San Francisco, CA
415.486.6935
dick.hinman@aonhewitt.com

**Clara Kim**
Somerset, NJ
732.537.4068
clara.kim@aonhewitt.com

**Meghan Lynch**
Lincolnshire, IL
847.442.3311
meghan.lynch@aonhewitt.com

**Susan Motter**
Atlanta, GA
770.690.7443
susan.motter@aonhewitt.com

**Beverly Rose**
Austin, TX
512.241.2115
beverly.rose@aonhewitt.com

**Jennifer Ross Berrian**
San Francisco, CA
415.486.6959
jennifer.ross.berrian@aonhewitt.com

**Dan Schwallie**
Hudson, OH
330.221.4155
dan.schwallie@aonhewitt.com

**John Van Duzer**
Lincolnshire, IL
847.442.3155
john.van.duzer@aonhewitt.com


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