Missouri Higher Education Savings Program
Minutes of the MOST Board Meeting

State Capitol Building, Senate Committee Room 2
Jefferson City, MO
March 13, 2008

Item I: Call to Order

Mr. Gaston called the meeting to order at 1:30 p.m. and explained that he was acting as chair with Treasurer Steelman listening in to the call via conference call. Mr. Gaston also acknowledged the passing of Mike Keathley, Commissioner of Administration for the State.

Item II: Roll Call

MOST Board Members present were Dr. Robert Stein, Doug Gaston (proxy for Sarah Steelman), Thomas Baumgardner, John Klebba, Rich Aubuchon (proxy for Larry Schepker) and Rhonda Meyer (proxy for Greg Steinhoff).

State Treasurer's Office (STO) staff present were: Mark Mathers, Jane O'Toole, Denise Chapel and Kelly Gunderson.

Upromise staff present were: Jeff Howkins, Derek Delorenzo, Patricia Brady, Temeka Easter and Janet Kottman.

Vanguard staff present were: Stewart Duffield and Ed Ferko.

Item III: Approval of Minutes

Dr. Stein moved to approve the minutes from the previous Board meeting held on December 11, 2007. Mr. Baumgardner seconded the motion, and the motion passed unanimously.

Item IV: IV. Review of Follow-up Items from Last Meeting

Mr. Howkins discussed recent developments at SLM Corporation and Upromise Investments. Mr. Howkins noted that the consortium of private equity companies and banks that had made an offer for SLM Corporation last year had dropped their offer and that a settlement had recently been reached between the parties. SLM Corporation therefore remains a publicly traded company. Mr. Howkins also noted the recent departure of James Fadule, who formerly headed Upromise Investments, and that Mark Chapleau, current counsel, was appointed CEO. Mr. Howkins explained that this change would not affect the MOST program or servicing of MOST accounts.

Ms. Brady then discussed the two memorandum prepared in response to the Board's questions in December. First, she discussed the treatment of 529 assets for federal financial aid. Mr. Klebba inquired about the situation of grandparents who have an account and whether there were advantages to holding monies until expenses were incurred or making distributions to the child. Dr. Stein also asked for clarification whether grandparents' 529 accounts were treated as income versus assets. Ms. Brady and Mr. Ferko explained that treatments by institutions can vary. Grandparent-owned 529s naming the student as beneficiary are not reportable on the FAFSA. However, the U.S. Department of Education has yet to clarify whether a distribution from a grandparent-owned 529 plan to pay for the student's college expenses is reportable as student income. In other words, if grandparents own the account, none of the value is included, however, gifts received by the student from grandparents or other people may be treated like income for financial aid purposes in the following year.

Ms. Brady and Mr. Howkins then spoke to the question about the ability to market the Upromise rewards program and possibly other programs to MOST account owners. They clarified that an "opt-out" provision was required for e-mails but that this has been implemented by Upromise. They also clarified that the account owner list was the property of MOST but that the State would need to abide by all laws and regulations when using the lists for marketing.

Item V: Legislative Report

Mr. Gaston indicated that the only bill that had been submitted regarding MOST involved a clarification in law of the $16,000 deduction for married couples. Mr. Gaston remarked that it is moving through committee.

Mr. Aubuchon inquired about the status of any bill clarifying or changing the law that imposed a 12-month minimum holding period for MOST contributions. He expressed concern about the current situation in which the Board has not adopted such a period.

Item VI: Annual Investment Review – Direct Plan

Mr. Mathers explained that the MOST Investment Policy requires an annual review of both the Direct Plan's and Advisor Plan's investment options. Additionally, the Investment Policy requires the Director of Investments to comment on any recommendations made by the program manager. Mr. Mathers directed the Board to the packet prepared by Vanguard and his memo to the Board.

Mr. Duffield then began his review of Vanguard's recommendations. The first recommendation was to adjust the allocation among underlying equity funds from the current 85/15 split between domestic and international funds to 80/20. Dr. Stein asked whether Mr. Mathers could give his reasons for his recommendation for a 75/25 split rather than wait for Vanguard to go through their entire report. Mr. Mathers cited his reasons for an increased allocation to international stocks including an increase in the proportionate market cap of international stocks, other agencies' increased international exposure and Vanguard's white paper on this topic. There was a discussion of the impact of the US dollar on global stocks. Mr. Mathers explained that the decision depended on the Board's risk tolerance and comfort level with international stocks. Mr. Baumgardner moved to increase the exposure of international stocks to 25% and Dr. Stein seconded. By roll call, the motion passed unanimously.

Mr. Duffield then presented a recommendation to delete the American Century Equity Growth fund from the MOST Aggressive Growth portfolio based on the overlap of large cap stocks with other portfolios in this option. Mr. Mathers concurred with this recommendation. Dr. Stein moved to adopt the recommendation to delete the American Century Equity Growth fund from the MOST Aggressive Growth portfolio, and Mr. Baumgardner seconded. By roll call, the motion passed unanimously.

Mr. Duffield then recommended that the MOST Aggressive Growth portfolio be merged with the Vanguard 100% Stock portfolio. When asked for clarification by Dr. Stein about his comments in his memo, Mr. Mathers indicated that his concurrence was conditional upon Vanguard and Upromise agreeing to keep the expense ratio for this option the same. Mr. Duffield and Mr. Ferko confirmed they had agreed to this. Dr. Stein made a motion to approve the recommendation to merge the MOST Aggressive Growth portfolio with the Vanguard 100% Stock portfolio contingent upon the expense ratio not increasing by virtue of this change, and Ms. Meyer seconded. By roll call, the motion passed unanimously.

Vanguard's fourth recommendation was to delete the American Century Equity Growth fund from the MOST Blended Stock Portfolio, which Mr. Mathers concurred with. Mr. Klebba moved to adopt the recommendation to delete the American Century Equity Growth fund from the MOST Aggressive Growth portfolio, and Dr. Stein seconded. By roll call, the motion passed unanimously.

Mr. Duffield then presented the last recommendation to delete the American Century Equity Growth fund as a static, or stand-alone, investment option in the Direct Plan. Mr. Mathers recommended instead to wait to delete this fund until next year so that Treasurer staff, Vanguard and American Century could spend more time considering possible alternatives. There was discussion by the Board, and the Board agreed not to make a motion to delete the fund but instead to agendize this item for next year.

Item VII: Quarterly Report

Mr. Gaston asked to speak at greater length about the 12-month minimum period for MOST contributions prior to the presentation of the quarterly report. Mr. Gaston noted that the law that was enacted did not provide for an appropriation to cover Upromise's expense of generating additional reports or for the Department of Revenue's additional costs to implement it, and that he believed it was the Board's position that they should not approve a new restriction that cannot yet be implemented. He also noted the Treasurer's philosophical opposition to any minimum contribution period, believing that this law would discourage many more people to contribute to MOST than it stops to prevent abusing the state tax deduction.

Mr. Aubuchon noted that the law requiring a 12-month minimum contribution period was passed in 2006 and that the Board cannot hang in limbo nor disregard the law. He expressed his belief that the Board should follow the law as soon as it has the means to do so. He stated that DOR cannot implement the law without the data and MOST does not have the data.

Mr. Gaston clarified that he was not asking the Board to take any action at this meeting but invited Board members to speak to the author of the previous bill imposing the minimum period or other legislators, if they had contact with those legislators, to discuss the MOST Board's problem.

The quarterly report was presented by Ms. Brady, Mr. Delorenzo, and Mr. Duffield. There was discussion by the Board about the marketing materials and plans.

Item VIII: Fund Performance Monitoring Report

Mr. Mathers explained that this was the first time the Board has seen the new quarterly report reviewing underlying funds' 1- and 3-year returns now required by the MOST Investment Policy. Mr. Mathers reviewed the report, noting short-term underperformance by the Legg Mason Value Fund and Templeton Growth Fund and intermediate term issues with the Van Kampen Comstock fund. All three funds are included in the Advisor Plan; no funds in the Direct Plan showed material underperformance. Mr. Mathers noted that all three funds are managed by high-conviction managers that have good long-term records of performance. Mr. Mathers recommended that all three funds be placed on "WATCH" status, thus requiring increased monitoring by staff. Dr. Stein moved to adopt this recommendation, and Mr. Klebba seconded. Mr. Baumgardner voted "no" to the motion. The motion carried 5-1.

Item IX: Adjournment

Mr. Klebba moved to adjourn, Mr. Baumgardner seconded. Meeting adjourned.