FEDERAL RETIREMENT THRIFT INVESTMENT BOARD
77 K Street, NE Washington, DC 20002

MINUTES OF THE MEETING OF THE BOARD MEMBERS

August 27, 2024

Michael F. Gerber, Chair of the Federal Retirement Thrift Investment Board (by telephone), convened a meeting of the Board members on August 27, 2024, at 10:00 a.m., Eastern Daylight Time. The meeting was held at the Board's offices at 77 K Street, NE and was open to the public via teleconference. In attendance were Dana K. Bilyeu of Oregon, member; Leona M. Bridges of California, member; Stacie Olivares of California, member; Ravindra Deo, Executive Director; Dharmesh Vashee, General Counsel and Secretary; Suzanne Tosini, Chief Operating Officer and Deputy Executive Director; Gisile Goethe, Director, Office of Resource Management; James Courtney, Director, Office of Participant Experience; Sean McCaffrey, Chief Investment Officer; Vijay Desai, Chief Information Officer; Thomas Brandt, Chief Risk Officer; and Trevor Williams, Chief Financial Officer.

Welcome and Introductions.

Chair Gerber called to order the monthly meeting of the Federal Retirement Thrift Investment Board (FRTIB or Agency) at 10:00 a.m. and welcomed everyone present to the meeting.

1. Approval of the Minutes of the July 23, 2024, Board Meeting.

Chair Gerber entertained a motion for approval of the minutes of the July 23, 2024 Board meeting. The following motion was made, seconded, and adopted without objection:

> MOTION: That the minutes of the Board meeting held on July 23, 2024 be approved.

Mr. Deo then gave opening remarks and provided a brief summary of the agenda.

2. Monthly Reports.

a. Participant Report

Mr. Courtney reviewed the monthly Participant Activity Report. See "Participant Activity Report August 2024" (attached). He reported that the percentage of Federal Employees' Retirement System (FERS) and Blended Retirement System (BRS) active duty participants contributing enough to receive the full match stood at all-time highs in July, largely due to automatic enrollment. He also reported that in July, the number of new general purpose loans increased 17 percent over the previous July and are up 14 percent for the year. He also noted that private sector plans are seeing increases in 401(k) plan borrowing. Finally, he reported that participant interactions are up across all channels, especially the Thrift Savings Plan (TSP) mobile app, with the number of people accessing My Account through the app more than doubling over the same time last year. He noted that the introduction of biometrics authentication last March is a key reason for the increase.

In response to a question from Chair Gerber, Mr. Courtney explained that the security of biometrics data for the app is equivalent to the security of the biometrics data of the device being used. Mr. Brandt added that the ability to download the app is restricted to Google and Apple's app stores, and that the Agency monitors and takes down any unauthorized sources of the app. Mr. Courtney and Mr. Deo also noted that they have a high degree of confidence in the ability of Accenture Federal Services (AFS) to execute in a high security environment.

In response to a question from Member Olivares, Mr. Courtney reported that about 1.5 million participants have downloaded the TSP app, and logins through the app have risen from accounting for 15 percent of total logins in the previous fall to 21 percent in May and 25 percent now. He further reported that the aggregate number of unique logins to My Account is 3.5 million.

b. Investment Report

Mr. McCaffrey reviewed the monthly investment performance report. See "July 2024 Investment Program Review" (attached). For the month of July, he reported that BlackRock's performance for the F and C Funds was in line with the Funds' respective indices. S Fund performance was ahead of the Small Mid-Cap Index by six basis points, primarily due to securities sampling. I Fund performance exceeded the applicable International Index's return by four basis points, primarily due to fair value pricing.

He further reported that for State Street in July, the F and C Fund performance was in line with the Funds' indices. Performance for the S Fund was ahead of the Small Mid-Cap Index by four basis points, primarily due to securities sampling. I Fund performance fell behind the applicable International Index's return by 20 basis points, primarily due to fair value pricing.

Mr. McCaffrey then commented on the market for July. The Federal Reserve elected not to change its target for short-term interest rates at its July meeting. However, longer-term interest rates trended lower during the month contributing to the F Fund's gain. The C and S Funds rose as a result of the stronger domestic equity markets. The I Fund also rose, boosted in part by a weaker U.S. dollar, and all L Funds finished higher.

Regarding year-to-date performance, Mr. McCaffrey stated that for BlackRock, performance for the F Fund was ahead of the Fixed Income Index's return by ten basis points, primarily due to year-end pricing differences. C Fund performance was in line with the Fund's index; performance for the S Fund was ahead of the Small Mid-Cap Index by seven basis points, primarily due to securities lending; and I Fund performance was ahead of the applicable International Index by 26 basis points, primarily due to tax advantage.

State Street's year-to-date performance for the F Fund was ahead of the Fixed Income Index's return by 11 basis points, primarily due to year-end pricing differences. C Fund returns matched the Large Cap Index; S Fund performance was ahead of the Small Mid-Cap Index by eight basis points, primarily due to securities lending; and the I Fund's performance exceeded the applicable International Index by five basis points, primarily due to tax advantage.

Mr. McCaffrey next reported that TSP Fund performance is mostly ahead so far in August. As of market close on August 26, for month-to-date, the C Fund is ahead 1.82 percent, the S Fund held steady, the I Fund is up 2.48 percent, the F Fund has a gain of 1.89 percent, the G Fund is ahead by 0.30 percent, and all of the L Funds are showing gains so far.

He then shared that the L 2070 Fund was successfully introduced into the L Funds lineup on July 26. It was a joint effort by the Offices of the Chief Financial Officer, Investments, and Participant Experience, working with AFS to finish on schedule. He noted that, beginning with this month's report, the Office of Investments' monthly reports will include the L 2070 Fund with the other L Fund reporting.

Mr. McCaffrey reported that, despite launching only a few days before the end of the month, the L 2070 Fund finished July with almost 300 million dollars in assets and approximately 4,000 investors, making the L 2070 Fund larger than over 90 percent of defined contribution plans in the United States. The L 2070 Fund is designed for participants born in 2005 and later, so it will be the default investment for many of the newest members of the Uniformed Services. Therefore, the Agency expects that growth in headcount will accelerate for L 2070.

He concluded by noting that, for the month, participation in the L Funds grew by over 11,000 accounts. Growth in participation is in large part due to the automatic enrollment of new participants and the L Funds' status as the default investment.

In response to a question from Member Olivares, Mr. McCaffrey clarified that the L Funds are trending up in allocation, and that this is the first time the L Funds' allocation has been higher than that of the G Fund.

c. Legislative Report

Mr. Deo provided the legislative update. He began by reporting that Congress is out for the remainder of the month and they did not come to an agreement on any appropriation bills before their departure. Both the House of Representatives and the Senate are set to reconvene on September 9, and they will have approximately three weeks to reach a funding agreement or continuing resolution before the end of the fiscal year. Congress is then expected to leave for state and district work on September 30 before returning around November 12.

In response to a question from Member Olivares, Mr. Deo acknowledged a recent Government Accountability Office report about the FRTIB. Mr. Deo stated that the FRTIB has addressed many findings from the report and is committed to working with AFS to resolve the rest.

3. <u>Quarterly Metrics Report</u>.

Mr. Brandt reviewed the Quarterly Metrics Report. See "FY24 Q3 Metrics Report" (attached). He reported that, as of the end of the third quarter of fiscal year (FY) 2024, FRTIB is at or above the target for all metrics. He further reported that the Agency is working on metrics and targets for FY 2025.

In response to a question from Member Bilyeu, Mr. Brandt noted that metrics and targets are based on past performance, industry benchmarks, and opportunities for improvement, but noted that possible gains could be subject to diminishing returns. He further noted that future targets may be adjusted to match current performance. Mr. Deo added that in many areas, the TSP sets its standards far above those of the industry. In response to a question from Member Bilyeu, Mr. Deo noted that the majority of participants that take out their money within the first year of separation are rolling it into other plans. Mr. Brandt added that the Agency is conducting a survey to better understand why participants are withdrawing their funds.

In response to questions from Member Olivares, Mr. Courtney clarified that FRTIB maintains information on its website, YouTube channel, and other sources for retirees, but that it is largely incumbent upon retirees to keep themselves educated. Further, FRTIB provides a scorecard rather than a calculator for comparing costs of the TSP to outside providers. Since cost is generally always lower with the TSP, the scorecard allows for a more interactive experience. He further noted that cost is not the driver for most people rolling funds out of the TSP – often it is convenience. Mr. Deo added as an example that an individual who maintains a joint account with their spouse cannot move that account into the TSP, so they may prefer to move their assets out of the TSP to maintain everything in one place. In response to a question from Member Bridges, Mr. Courtney confirmed that lack of withdrawal flexibility is no longer a driver.

4. <u>Enterprise Risk Management Report</u>.

Mr. Brandt reviewed the Enterprise Risk Management (ERM) Update. See "Enterprise Risk Management Update" (attached). He began by explaining that FRTIB has a continuous five-phase cycle each year for identifying, assessing, treating, monitoring, and reporting on enterprise risks. At this point in the fiscal year, they are in the monitoring and reporting stages.

Two new enterprise risks were introduced this year. The first, Artificial Intelligence (AI), was introduced not only because of how quickly technology is evolving but also because Executive Orders and the Office of Management and Budget (OMB) guidance are creating specific expectations of Federal agencies in this area. FRTIB has developed a project plan to ensure that proper guidance, policies, and strategies are in place. The second new risk, fiduciary risk, was added due to the current operating environment. This risk relates to potential challenges to whether the Agency's oversight of its vendors meets the legal standard required of fiduciaries.

Mr. Brandt further reported that the Agency's level of risk exposure has gradually decreased over time. In 2020, there were 17 enterprise risks, three of which were rated high, three at medium-high, and 11 at medium-low. There are no longer any risks rated high.

In response to a comment from Member Bilyeu, Mr. Brandt agreed that one of the three high risks from 2020 was likely cybersecurity. He also noted that risks can be removed as enterprise risks. As an example, insider threat was removed as an enterprise-wide threat based on an assessment that the risk had been mitigated to a level where the residual risk could be managed at the office level instead. Mr. Deo added that cybersecurity is likely an example of a risk that will never be removed as an enterprise risk due to its ever-evolving nature.

Ms. Goethe confirmed that the three high risks from 2020 were insider threat, information security, and disaster recovery/business continuity. Mr. Brandt noted that in 2020, cybersecurity and information technology (IT) were one risk, but they were later separated because they each require their own treatment plan. Mr. Deo added that IT generally refers to issues such as whether things like printers, applications, and microphones work, whereas cybersecurity refers to whether the IT operates in a secure environment. As previously mentioned, while the IT risk may eventually be removed, cybersecurity almost certainly will not.

Mr. Brandt continued by explaining that any enterprise risk rated medium-high or higher requires a risk treatment plan. The Agency rated two risks as medium-high: AI and cybersecurity. He reported that if all actions planned for the year are accomplished with AI, he expects the risk level will be reduced to medium. He also reiterated that even with taking all actions planned to mitigate cybersecurity risk, the risk level will likely remain medium-high.

He then reported that the Agency's overall risk appetite is low, which means the Agency tries not to undertake activities that would create a level of risk that would impair the Agency's ability to achieve its mission, goals, or objectives. However, there are some individual risk categories where the Agency has a more moderate appetite for risk.

In response to a question from Member Olivares, Mr. Brandt explained that the different categories of risk themselves may have sub-categories that inform the overall level of risk for that category. As an example, not only does the Agency monitor vendor performance as part of managing vendor risk, it also monitors the vendor's cyber posture.

Mr. Brandt then reported that his office is continuing to do additional work to identify emerging risks, as the office identified AI as an emerging risk in the previous year. He also reported that his office continues to host risk case studies to increase Agency communication and awareness.

5. Internal Audit Update.

Ms. Barbara Holmes, Chief Audit Executive, reviewed the Internal Audit Update. See "Internal Audit Update" (attached). She began by reporting her team has completed audits regarding Audit Now/Service Now implementation and Executive Order 14035 compliance. The court ordered payment and contracting audits are underway, and the government purchase card audit is nearly complete. Two IT-related audits have been added to the 2024 internal audit plan that will likely span into early 2025. One will cover contractor onboarding and vetting, and the other will cover zero trust architecture for both FRTIB and Converge. This contractor vetting audit has begun, and the Federal Information Security Modernization Act (FISMA) audit has concluded.

Ms. Holmes shared that the Audit Now/Service Now implementation review was to validate that all previous audit findings were transferred to the new system. While all audit findings were successfully transferred, there were some missing data pieces related to closed audit findings. She also reported that the objective of reviewing for compliance with Executive Order 14035 was to verify alignment, and further reported that substantial progress has been made on this initiative. The Office of Personnel Management has established a related maturity model, and FRTIB was rated at level two on a three-point scale for all but four actions, which were rated at level one.

Ms. Holmes concluded by stating that her office is working with other offices to close older audit findings, starting to plan for the 2025 internal audit plan, and developing a project plan for the fraud, waste, and abuse hotline.

6. FY 2024 FISMA Report.

Ms. Holmes introduced Edwen Delcid, Senior Manager, and Tony Wang, Partner, of Williams Adley to present the results of the FY 2024 FISMA audit. See "FY24 FISMA Audit Report" (attached). Mr. Delcid explained that the objective for the FY 2024 audit was to determine the effectiveness of FRTIB's information security program for the reporting period of October 1, 2023, to June 30, 2024. Williams Adley evaluated the design, implementation, and operating effectiveness of entity-wide and system-specific controls, with a particular focus on Converge. They also reviewed corrective actions taken by FRTIB to address previously issued recommendations that remained open at the end of FY 2023.

Mr. Delcid also explained that independent assessors are given reporting metric questions which focus on evaluating the effectiveness and maturity of Federal agencies' information security controls, compliance with security requirements, and risk management practices across nine domains. Maturity is determined by utilizing a five-level maturity model, where level four is considered to be effective.

Mr. Delcid reported that the FRTIB has an effective information security program and achieved a level five rating across all nine FISMA domains. This determination was based on evaluating 37 metric questions where no issues or conditions were found, and Williams Adley also identified improvements in six of the nine domains. Finally, no recommendations remained open at the end of the fiscal year.

Mr. Delcid further explained that of the 20 core metrics evaluated, 13 increased in maturity from the previous year, and of the 17 supplemental metrics last evaluated in 2021, all increased. Mr. Delcid concluded by acknowledging the hard work of FRTIB leadership and employees, and emphasized that continued strategic leadership and forward thinking will be required as FISMA metrics will be refreshed.

Mr. Wang began his remarks by commending FRTIB's proactive approach to cybersecurity. In response to a question from Chair Gerber, Mr. Wang explained that FRTIB is ahead of many agencies in its information security maturity, and that in order to succeed, agencies need the right people, the discipline to set up processes, and money. Mr. Wang also noted that he has audited FRTIB since 2017 and has personally witnessed the Agency grow from using an ad hoc approach to problem-solving to a much more mature flow. In response to comments from Member Bilyeu, Mr. Wang noted that the work is not done, as cyber risks are constantly evolving. In response to a question from Member Olivares, Mr. Wang explained that zero trust represents a paradigm shift compared to traditional cybersecurity measures in that it emphasizes verification over trust. Both the National Institute of Standards and Technology (NIST) and Department of Homeland Security (DHS) have developed initial assessment models to use as a framework. He also explained that with generative AI, there is opportunity as well as risk. Among the risks relevant to FRTIB could be more advanced phishing and social engineering schemes utilizing deepfake audio and video.

Mr. Patrick Bevill, Chief Information Security Officer, provided FRTIB's response. See "FRTIB FISMA Audit Management Response" (attached). He began by thanking Williams Adley for their work and highlighted that FRTIB's cybersecurity efforts over the years have brought about the closure of all open FISMA audit recommendations. He noted that cybersecurity will continue to be a top priority for senior management.

7. FY 2025 Budget Proposal and Approval.

Mr. Williams and Mr. Deo reviewed the FY 2025 Budget Proposal. See "FY 2025 Budget Proposal" (attached). Mr. Williams began by reviewing the FY 2024 budget, noting that FRTIB primarily used it to accomplish the Agency's FY 2024 priorities: emphasize new TSP tools and enhancements, understand and respond to participant needs and expectations, determine workspace for the next decade, and focus on quality and continuous improvement in FRTIB. He further stated that the Board-approved budget for FY 2024 was 476.1 million dollars, with recordkeeping accounting for 65 percent of the total, Agency operations for 20 percent, payroll for 12 percent, and communications for three percent. He also noted that FRTIB handled over five million participant- and beneficiary-initiated transactions, answered over nine million inquiries, mailed over 27 million pieces of communications and materials to participants, processed over 91 million participant contributions totaling 33 billion dollars, and managed a projected 862 billion dollars in average assets for more than seven million active and separated participants in FY 2024.

Mr. Deo then presented the FY 2025 proposed budget request. He explained that the Agency's FY 2025 priorities are to make greater use of data and analytics to improve the participant experience; leverage compliance, oversight, and assurance processes to optimize vendor performance; embrace a culture of collaboration and trust; and continue to focus on quality and continuous improvement. He stated that the Agency's proposed budget for FY 2025 is 500.9 million dollars, or a five percent increase over FY 2024's budget. He explained that the increase is driven primarily by activities designed to improve the participant experience as well as the implementation of cybersecurity Executive Orders to continue keeping the TSP safe for participants.

Mr. Deo explained that the proposed budget for FY 2026 is projected to decrease under the assumption that the cybersecurity Executive Orders will be fully implemented. He also explained that assets are projected to continue to grow at a conservative rate of return, the budget is expected to remain stable, and the number of participants is expected to grow primarily driven by automatic enrollment of new participants. He noted that the projection for FY 2024 gross basis points is 5.5, which is then expected to decrease steadily through FY 2029 to around 4.4 gross basis points. He also explained that due to forfeitures and offsets, the Agency charges a slightly lower net basis points figure to participants.

Mr. Deo reported that the bulk of the proposed FY 2025 budget is for recordkeeping and communications, and much smaller portions for personnel and Agency operations. He then emphasized that FRTIB spends only what it needs to, and that in prior years, the Agency has spent somewhere between 80 and 95 percent of its budget. Reviewing the administrative expense ratios, he noted that in 2022, there was a temporary jump both because assets decreased when the market fell, and because the conversion took place in 2022, resulting in decommissioned legacy systems continuing for a time.

In response to a question from Member Olivares, Mr. Deo explained that the TSP's 4.8 basis points is very low compared to other 401(k) plans, which tend to fall between 20 and 45 basis points, but warned that the comparison is difficult because 401(k) plans tend to have expenses on investments much higher than the TSP's. In response to questions from Member Bilyeu and Member Olivares, Mr. Deo and Mr. Brandt noted that the Agency could look into benchmarking its expenses against other plans.

Mr. Deo then reported that for FY 2025, the Agency is seeking a slight increase in authorized staffing. In response to a question from Member Bilyeu, Ms. Goethe stated that the Agency's turnover rate has tapered off from what was reported the previous year, which was approximately 13 or 14 percent, but that she would need to conduct research to determine a current Federal turnover projection rate.

Chair Gerber entertained a motion for approval of the proposed FY 2025 budget of 500.9 million dollars. The following motion was made, seconded, and adopted without objection:

MOTION: That the proposed FY 2025 budget be approved.

8. Adjourn.

On a vote taken by the Chair, the members closed the meeting at 11:17 a.m. to enter into executive session.

At 1:29 p.m., upon completion of the executive session, the members reconvened the open portion of the meeting.

Whereupon, there being no further business, the following motion was made, seconded, and adopted without objection and Chair Gerber adjourned the meeting at 1:29 p.m.

MOTION: That this meeting be adjourned.

Dharmesh Vashee
General Counsel and Secretary

Attachments

1. Participant Activity Report August 2024
2. July 2024 Investment Program Review
3. FY24 Q3 Metrics Report
4. Enterprise Risk Management Update

5. Internal Audit Update
6. FY24 FISMA Audit Report
7. FRTIB FISMA Audit Management Response
8. FY 2025 Budget Proposal