

**MINUTES
ARKANSAS TEACHER RETIREMENT SYSTEM
BOARD OF TRUSTEES**

**Monday, July 28, 2014
10:45 a.m.
1400 West Third Street
Little Rock, AR 72201**

ATTENDEES

Board Members Present

Dr. Richard Abernathy, Chair
Jeff Stubblefield, Vice Chair
Lloyd Black
Kelly Davis
Candace Franks*
Wes Goodner, designee for Charles Robinson
Peggy Gram, designee for Charlie Daniels*
Danny Knight*
Bobby Lester
Janet Watson
Tony Wood

Members Absent

Kathy Clayton
Hazel Coleman
Robin Nichols
Deborah Thompson

ATRS Staff Present

George Hopkins, Executive Director
Gail Bolden, Deputy Director
Shane Benbrook, Internal Audit/Risk Mgmt.
Cecial Caldwell, Computer Support Analyst
Mitzi Ferguson, Chief Financial Officer
Laura Gilson, General Counsel
Rod Graves, Manager Investment Dept.
Wayne Greathouse, Assoc. Dir. Investments
Manju, Dir. Data Processing
Jerry Meyer, Manager, Real Assets
Tammy Porter, Administrative Assistant
Michael Ray, Dir. Member Services
Clint Rhoden, Operations Manager
Leslie Ward, Manager, Private Equity
Brenda West, Internal Audit/Risk Mgmt.

Guest Present

Donna Morey, ATRA
Chris Caldwell, Legislative Audit
P.J. Kelly, Hewitt EnnisKnupp
Katie Comstock, Hewitt EnnisKnupp
Chae Hong, Hewitt EnnisKnupp
Dan Kim, Hewitt EnnisKnupp

**via teleconference*

- I. **Call to Order/Roll Call.** Dr. Richard Abernathy, Chair, called the Board of Trustee meeting to order at 10:45 a.m. Roll call was taken. Ms. Clayton, Ms. Coleman, Ms. Nichols and Ms. Thompson were absent.
- II. **Welcome New Board Member, Tony Wood, Commissioner of Education.** Dr. Abernathy welcomed and introduced Mr. Tony Wood, Commissioner of Education as the newest member to the Board of Trustees.

III. **Adoption of Agenda.**

Mr. Lester moved for adoption of the Agenda. Mr. Black seconded the motion, and the Board unanimously approved the motion.

IV **Executive Summary.** The Executive Summary was provided for reference with no questions or expansions on the written summary.

V. **Approval of Board Minutes.**

A. **Minutes of June 2, 2014.**

Mr. Knight moved for approval of the Minutes of the Board of Trustees meeting of June 2, 2014. Mr. Goodner seconded the motion, and the Board unanimously approved the motion.

B. **Minutes of June 17, 2014.**

Mr. Black moved for approval of the Minutes of the Board of Trustees meeting of June 17, 2014. Mr. Stubblefield seconded the motion, and the Board unanimously approved the motion.

VI. **Report of Member Interest Waived Under A. C. A. Section 24-7-205.** Mr. Hopkins presented the member interest amount waived report. ATRS waives interest on members when there is a dispute between ATRS and the member as to whether ATRS made a mistake or otherwise did not do all that was required on the member's account. There was one interest amount waived for this reporting period in the amount of \$258.53.

VII. **Report of Employer Interest and Penalties Waived Under A. C. A. Sec. 24-7-411.** Mr. Hopkins presented the employer interest and penalties waived report. ATRS may waive employer interest and penalties when reports/payments are late or have issues due to new bookkeeper, sickness, and other situations that justify a waiver. ATRS waived \$150.00 in employer interest and penalties.

VIII. **Investment Committee Report.** Dr. Abernathy, acting Chair, gave a report on the Investment Committee meeting.

A. **Investment Update and Arkansas Related Update.**

1. **Sale of Property in North Little Rock, AR.** Mr. Hopkins reported that ATRS currently owns approximately three (3)

acres located near the old Memorial Hospital site in North Little Rock. The City of North Little Rock purchased approximately one acre of the three acre tract of land to use as a drive way for the new Veteran's Administration nursing home. The sale was successfully closed on July 17, 2014 for a total of \$35,000 (a price slightly higher than the appraised value of \$33,600).

The remaining two acres will remain for sale with expectations of increased interest in the land as development around the vacant tracts continues to grow.

2. List of Recent Fund Closings.

- a. Harris Associates, L.P. (Global Equity, \$350 million dollar allocation).** Mr. Hopkins reported that due to movement during the transition the Harris account was funded with around \$341 million dollars. The transition is complete and fell within the projected cost range.
- b. GMO Global All Country Equity Allocation (Global Equity, \$350 million dollar allocation).** Mr. Hopkins reported that the full commitment of \$350 million dollars was successfully redeployed from the State Street Global Equity Index Fund.
- c. LaSalle Asia Opportunity Fund IV, L.P. (Real Assets, Real Estate Fund, \$30 million dollar allocation).** Mr. Hopkins reported that a commitment of \$30 million dollars was accepted and closed.
- d. Carlyle Realty Partners VII, L.P. (Real Assets, Real Estate Fund, \$30 million dollars allocation).** Mr. Hopkins reported that the full commitment of \$30 million dollars was accepted and closed

B. General Investment Consultant Update.

- 1. Preliminary Performance Report for Month Ending May 31, 2014.** Mr. P. J. Kelly and Ms. Katie Comstock of Hewitt EnnisKnupp (HEK) presented the preliminary performance report for the month ending May 31, 2014. Ms. Comstock reported the total market value of ATRS fund was \$14.4 billion dollars. The total fund had a return of 8.6% since inception, underperforming its benchmark of 8.7%, and a 16.4% return for

fiscal year-to-date, outperforming its benchmark of 15.8%. ATRS had strong returns in June 2014.

2. **Update on Arkansas Opportunity Fund.** P. J. Kelly of Hewitt EnnisKnupp (HEK) reported on the Opportunity Fund search. HEK has received the last of the requested information from Stephens, Inc. HEK will be meeting with all three candidates, Delta Trust, Circumference Group, and Stephen, Inc., after today's Board meeting to ask questions and obtain additional information on the Request for Information. Mr. Kelly feels like a recommendation will be presented at the next Board meeting. However, there is still some additional work and questions for the candidates. Mr. Hopkins asked the Committee that, if in the next few weeks, or however long it takes the consultant to have a final recommendation, would the Board/Committee rather wait until the October Board meeting to begin activity of reviewing and potentially hiring a this manager, or have a telephonic meeting to start the process earlier. The Committee agreed to move forward once a recommendation is received from the Consultant by having a telephonic Board meeting

C. Real Assets Investment Consultant Report.

1. **Early Preliminary Performance Report for the Quarter Ending March 31, 2014.** Mr. Chae Hong of Hewitt EnnisKnupp (HEK) presented the early preliminary performance report ending March 31, 2014. Through the first quarter, NCREIF's NPI registered at 2.7% and NFI-ODCE (net) returned 2.3%, an increase of 20 bps and decrease of 60 bps respectively over fourth quarter results. Trailing 12-month returns currently remain above the sector's long run average. Timberland Index returned 1.6% for the quarter and is up 9.8% for the trailing one year. Farmland Index gained 2.4% for the first quarter of 2014 and 17.4% for the trailing one year. As of March 31, 2014, the real assets portfolio stands at 11.3% of ATRS' total assets.

ATRS underperformed the real assets benchmark by 130 basis points for the first quarter. ATRS Real Estate portfolio underperformed the quarter by 90 basis points. Agriculture underperformed by 160 basis points, and Timberland underperformed by 270 basis points.

Overall, the portfolio is in compliance with its Statement of Investment Policy with respect to style, leverage, geographic region, and property type diversification.

2. **Recommendation to Commit up to \$50 million dollars in KKR Global Infrastructures Investors II, L.P., Global Infrastructure Focused on Investments in Existing Assets with Core Features such as Links to Inflation and Diversification from Equity Markets.** Mr. Dan Kim, Hewitt EnnisKnupp, presented the recommendation for KKR Global Infrastructures Investors, II, L.P. ("KKR Fund II"). KKR Fund II will seek to make investments in long term (10+ year contracts) infrastructure assets that have low risk profiles and low correlation to the performance of the broader economy. The emphasis will be on investments that offer strong current income generation that still has the potential for long term growth. KRR will be targeting an IRR in the low to mid teens for Fund II. Infrastructure funds tend to be less volatile than the equity markets with returns less dependent on stock prices so infrastructure funds provide greater diversification for the ATRS trust fund.

a. Resolution 2014-40

Dr. Abernathy moved to adopt Resolution 2014-40, to Commit up to \$50 million dollars in KKR Global Infrastructures Investors II, L.L., Global Infrastructure Focused on Investments in Existing Assets with Core Features such as Links to Inflation and Diversification from Equity Markets. Mr. Knight seconded the motion, and the Board unanimously approved the motion.

D. Private Equity Investment Consultant Report.

1. **Portfolio Review for Quarter Ending March 31, 2014.** Mr. Michael Bacine of Franklin Park presented the portfolio review for the quarter ending March 31, 2014. The legacy portfolio represents 5.6% of ATRS' private equity portfolio. Since inception, total fund net IRR is 9.8%. Total commitments for year ended December 31, 2013, were \$185 million dollars. Total approved and pending commitments for 2014 are \$205 million dollars, which is just under the pacing for year 2014 of \$230 million dollars.

- IX. Operations Committee Report.** Mr. Lester, Chair, gave a report on the Operations Committee meeting.

A. Open Forum for Potential Rule or Law Changes by Committee Members and Board Members in Attendance.

1. General Open Forum.

- B. Outsourcing Update.** Mr. Hopkins reported that ATRS staff has continued to look at outsourcing and follow-up with activities from other states. Ohio is a state that has addressed outsourcing in a manner that continues to allow outsourcing in its benefits while at the same time protecting both the Ohio School Employees Retirement System and the individuals in the outsourced positions. The approach in Ohio is compliant with IRS requirements and federal law, and is based upon IRS activity to address attempts in defined contribution plans to eliminate low paid employees to avoid "top heavy" restrictions.

The Ohio approach is for outsourced employees working at a school in a standard type of outsource position like transportation, custodial, classroom assistant, and cafeteria workers to be treated as school employees for the purposes of retirement only and for the school to pay the standard employer contribution rate on the outsourced employees. ATRS currently has one class of member that this employer shift already is in use. ATRS allows schools to pay the contributions on school resource officers even though a law enforcement agency is the actual employer.

If this approach is undertaken, it would probably require a phase in period to allow existing outsourcing contracts to expire prior to implementation. It appears that this achieves the outcome sought by schools such as quicker hiring, better ability to shift responsibilities, uncomplicated termination, and elimination of health insurance responsibilities. Also, it has no impact on the position taken by some schools that outsourced cafeteria operations produce better food results. The hiring, firing and standard employment duties such as payroll tax reporting would remain with the outsourced employer. Apparently there is little complication or red tape by undertaking this approach and also eliminates a separate concern about schools being required to pay contributions on non-salary related payments such as tools, equipment, supplies, and profits.

C. Potential Legislation.

- 1. Technical Corrections.** This is a standard bill that ATRS has every session. Over a two year period, ATRS staff and members find wording in the ATRS law that is unclear or may have a comma in a place that makes it hard to interpret. The technical corrections bill that ATRS has every session is a word and punctuation clean up to ensure the intended meaning of the ATRS law is not lost over time. In other instances, references to laws that were repealed or modified by rules are deleted. The Technical Corrections bill should have no material impact on ATRS process but just clarifies it.

Mr. Lester *moved to approve the development of Technical Correction legislation by ATRS Staff. Mr. Black seconded the motion, and the Committee unanimously approved the motion.*

- 2. Recycling Tax Credit.** In the 2013 session, the ability to reallocate the recycling tax credit by an Arkansas public retirement system was established in the Big River Steel legislative package. It was narrowly tailored to only apply to steel mills. The law change was necessary since ATRS invested in Big River Steel but had no ability to benefit from the tax credits since it is a tax exempt entity. The law change allows ATRS and its equity partners to shift the tax credits within the equity owners of the project so all the tax credits can be realized.

Since that time, ATRS has made an equity investment in the Blue Oak Arkansas e-waste recycling plasma furnace process that will also have recycling tax credits available. Those tax credits should become available in late 2015. This project is much smaller with approximate total project capital of \$35 million dollars with recycling equipment expected to be less than one-half of that amount.

In order to encourage more of these specialized investments, ATRS would like to extend the transferability of the recycling tax credit within the equity owners to additional projects like Blue Oak Arkansas. Extending the tax credit beyond steel would be limited to just Arkansas public retirement systems and to apply only to the recycling tax credit. The tax impact of the Blue Oak project should have very slight nonmaterial impact on the overall state tax collections. Mr. Hopkins will undertake drafting the change for review in the near future.

Mr. Lester moved to approve the development of Recycling Tax Credit legislation by ATRS Staff. Mr. Black seconded the motion, and the Committee unanimously approved the motion.

3. **Concern about growing problem with Pension Advance Companies. (A first cousin to PayDay Lenders).** A growing concern in other states with a large senior citizen population are companies that provide retirees an advance based upon future monthly retirement payments. Often, the interest rate on these "advances" can exceed 100%. Typical interest rates vary from 25% to 90%. Most often targeted groups are elderly and low income retirees. An example would be like this: A retired cafeteria worker with 14 years of service with a \$750.00 per month benefit would be contacted about the availability of an advance. The typical amount of an advance is from \$20,000 to \$50,000. A part of the advance would be used to purchase term life in the amount of the advance for the length of the repayment on the retiree. The rest would be paid to the retiree immediately with all or a material portion of the retirees monthly benefit being used to pay the monthly payment for the advance. (The member would send ATRS a deposit account number that would be controlled by the advance company.)

Based upon the length of the payments, an assumed interest rate can be determined. As stated above, the interest rates range from 25% to 100%. The State of Missouri is the first state to outlaw pension advances and the federal government through the Government Accountability Office (GAO) has written reports on the predatory aspects of these companies. ATRS staff presents this to the Operations committee for its consideration as to what, if anything, ATRS should do to address this situation.

Mr. Lester moved to approve the development of Pension Advance Companies legislation. Mr. Black seconded the motion, and the Committee unanimously approved the motion.

D. Legislation Approved by Committee and Board.

1. **Disability.** The Arkansas Teacher Retirement System (ATRS) Board of Trustees directed staff to seek a way to balance the need for a fast, efficient, and effective ATRS disability process that supports the

smooth operation of the public school system by allowing employees with significant disabilities to retire quickly while at the same time ensuring that the process continues to have integrity after a disability retirement is approved by the ATRS Medical Committee.

ATRS staff currently lacks the resources and legal authority to appropriately monitor ATRS disability retirees after a disability retirement is approved. With new medical treatments and time, some disability retirees may improve and no longer have a disability that prevents the retiree from working gainfully in the work force.

ATRS prohibits a disability retiree from returning to work at an ATRS employer to maintain integrity in the disability process. That rule is easily monitored by ATRS staff. ATRS staff has no method or legal authority to monitor if the disability retiree works elsewhere in the community, state, or otherwise. Occasionally a disability retiree may work full time at a factory or other community establishment. Many people in the school district area may know about the work and the disability status. This undermines the integrity and credibility of the disability process at ATRS.

The request was for ATRS staff to find a method to better monitor disability retirees after retirement. The solution should be one that would not unduly disrupt or penalize disability retirees who are often genuinely and critically ill, while at the same time providing a reasonable method to maintain the creditability and integrity of the program.

Most retirement systems require a member to be approved for Social Security disability in order to first qualify for disability retirement at the pension system. Since it is important to provide a quicker path for educators who are ill to exit the classroom and the education setting, the ATRS disability process provides a much swifter decision. The ATRS process uses a Medical Committee of 3 doctors to decide if a member is disabled using medical reports.

The proposed law change maintains a quick initial process, but also blends in a future use of Social Security disability for continued eligibility after an appropriate 3- 5 years to be approved for Social Security disability retirement. Under the proposed change, the member still submits a disability application that has the lightning fast review by the ATRS Medical Committee. If approved for disability, once the ATRS disability payments begin, the member would have a duty to also apply for Social Security disability and ultimately be

approved for Social Security disability. If the member is not approved for Social Security disability after 3 – 5 years, then the member would keep all previous disability payments but the benefit payments would end until the member is eligible for retirement by reaching age 60.

2. **Private School Certification by ATRS Staff Instead of Department of Education.** ATRS staff is aware that the Department of Education no longer tracks private schools, and therefore no longer has a reasonable basis to certify private school positions to ATRS as eligible for licensure as teachers whether in or out of Arkansas. ATRS staff regularly makes determinations about related items and that the staff could make an evaluation for private school certification in full compliance with federal law standards.

- E. **Update on Member's Internet Access scheduled for August 1, 2014.** Mr. Clint Rhoden gave a brief update on the member's internet access to ATRS accounts from the ATRS website. The scheduled date to go live with the access is August 1, 2014.

X. **Staff Reports.**

- A. **Medical Committee Reports.** Michael Ray presented the Medical Committee reports for June 2014 and July 2014. In June 2014, there were 20 applicants, 16 were approved, and 4 needed more information. In July 2014, there were 15 applicants, and all 15 cases were approved.

Mr. Lester *moved to approve* the June 2014 and July 2014 Medical Committee reports. Mr. Knight *seconded the motion*, and the Board *unanimously approved the motion*.

XI. **Other Business.** None

XII. **Adjourn.**

Mr. Lester *moved to adjourn* the Board Meeting. Mr. Stubblefield *seconded the motion*, and the Board *unanimously approved the motion*.

Meeting adjourned at 10:55 a.m.

George Hopkins,
Executive Director

Dr. Richard Abernathy, Chair
Board of Trustees

Tammy Porter,
Recorder

Date Approved