

**MINUTES OF THE REGULAR MEETING OF THE BOARD OF TRUSTEES  
ARKANSAS PUBLIC EMPLOYEES RETIREMENT SYSTEM  
AUGUST 21, 2013**

The regular quarterly meeting of the Board of Trustees of the Arkansas Public Employees Retirement System was held on Wednesday, August 21, 2013 at 9:00 a.m., in the Conference Room, 124 West Capitol, Little Rock, Arkansas. Mr. Artee Williams presided.

**QUORUM PRESENT:**

Mr. Williams recognized the presence of a quorum.

**BOARD MEMBERS PRESENT:**

Mr. Artee Williams (State Employee Member), *Chair*, Director, Dept. of Workforce Services  
Judge Mike Jacobs (County Employee), Clarksville, AR  
Ms. Ouida Wright (State Employee Member), Conway, AR  
Mr. Bill Gaddy (State Employee Member), Little Rock, AR  
Ms. Carol Bevis, (Other, Non-State Employee), Little Rock, AR  
Hon. Charles Robinson, (Ex-Officio Member), State Treasurer  
Hon. Richard Weiss (Ex-Officio Member), Dept. of Finance and Administration  
Ms. Janet Harris, Deputy State Auditor (*proxy*)  
Dr. John Shelnett, Dept. of Finance and Administration (*proxy*)  
Ms. Gail H. Stone (Executive Director), APERS

**BOARD MEMBERS ABSENT:**

Hon. Charlie Daniels (Ex-Officio Member), State Auditor  
Mayor Steve Northcutt (City Employee), Malvern, AR

**VISITORS PRESENT:**

Mr. Ryan Ball, Callan Associates, Inc.  
Mr. Kevin Dolsen, Callan Associates, Inc.  
Mr. Norm Jones, Gabriel Roeder Smith & Company  
Mr. David Hoffman, Gabriel Roeder Smith & Company  
Mr. Wes Goodner, State Treasurer Deputy  
Mr. Mike Knapp, Bureau of Legislative Audit  
Mr. Paul Young, Arkansas Municipal League  
Mr. Danny James, Arkansas State Employee Association  
Mr. Mike Wickline, *Arkansas Democrat-Gazette*

**STAFF PRESENT:**

Ms. Michele Williams, APERS Deputy Director  
Mr. Carlos Borromeo, APERS Chief Investment Officer  
Ms. Susan Bowers, APERS Associate Director of Investments  
Ms. Ashley McAdoo, APERS Chief Fiscal Officer  
Mr. Jay Wills, APERS Attorney Specialist  
Mr. John Treloggen, APERS Internal Auditor  
Ms. Becky Walker, APERS Administrative Service Manager  
Ms. Linda McGrath, APERS Administrative Specialist

**NEWS MEDIA NOTIFIED:**

A letter of notification of the Arkansas Public Employees Retirement System Board meeting was sent to the Arkansas Democrat-Gazette, the Associated Press, Television Station KLRT/FOX16, Radio Station KARN, and Radio Station KAAY. This letter of notification is pursuant to A.C.A. 25-19-101 (Act 93 of 1967) as amended-The Freedom of Information Act.

**ELECTION OF BOARD CHAIR AND VICE CHAIR:**

Mr. Weiss nominated Mr. Artee Williams and Judge Mike Jacobs to continue on as Board Chair and Vice Chair respectively. He was seconded by Mr. Gaddy and the motion carried unanimously.

*(Mr. Weiss asked to be excused from the meeting and Dr. Shelnett took his place at the table.)*

**MINUTES:**

Prior to the Board meeting, a copy of the Minutes from the meeting of May 15, 2013 was mailed to each APERS Board member for review. On a motion made by Judge Jacobs and seconded by Mr. Robinson, the May Minutes were approved as presented.

**RECOGNITION OF NEW BOARD MEMBER:**

Mr. Williams recognized that this was Mr. Charles Robinson's first APERS Board meeting, as he was filling in the remainder of Ms. Shoffner's term as State Treasurer. Mr. Robinson comments that he had a vested interest in APERS, since the Governor had called him out of retirement for the temporary position and he was looking forward to working with the other Trustees.

**PRELIMINARY ACTUARIAL VALUATION FOR FISCAL YEAR 2013 – Presented by Mr. Norm Jones and Mr. David Hoffman of Gabriel, Roeder, Smith and Company**

Mr. Jones began by summarizing the active and retired membership. He noted that it had remained fairly constant for the previous five years; an important factor when trying to keep stable contribution rates. Conversely, the number of retiree has continued to grow and is expected to level off at about 35,000 in just a few years.

He outlined the calculations involved in computing the Employer Contribution Rate and noted the unfunded liabilities were computed over a closed 25-year period (as opposed to a 30-year period last year). Even with this reduction, the Employer Contribution Rate for Fiscal Year 2015 was calculated to be 14.75%; down slightly from the 14.88% currently being paid.

Mr. Jones explained the development of the Funding Value of Assets and how the excess gains and losses are "smoothed" out over a 4 years to provide more stability to the system from year to year. This process has allowed the system to recognize an additional \$191 million in gains for Fiscal Year 2013.

Mr. Hoffman stated that the funded ratio for APERS currently stood at 74%. Previously, on a market value basis, the funded ratio has increased from 70% to 75%, mainly due to the unrecognized gains that Mr. Jones already mentioned. As of June 30, 2013, the market value of assets exceeded the funding value of assets by approximately \$260 million. As this difference is fully realized, and if near term experience matches expectations, the contribution rate will gradually decline over the next three years. He led the Trustees through three possible market return scenarios and noted how the various returns might affect the Funded Ratio and Employer Rate.

Mr. Hoffman pointed out that this year, GRS had shortened the amortization time of the unfunded liabilities by 5 years. This now gave the system some "cushion" going forward to hold the employer rates down.

Ms. Stone asked for provisional approval of the Employer Rate so Staff could notify employers of the new rate. She explained to the new Trustees that the final rate would be set at the November meeting, when the actuaries came back with the completed valuation. Ms. Bevis motioned to accept the provisional Employer Rate of 14.75%, which would become effective on July 1, 2014. She was seconded by Mr. Robinson and the motion passed.

During a short break, while Callan came to the table, Ms. Stone distributed a map of Arkansas that detailed the number of retirees and amount paid out annually (per county) from APERS. She confirmed that the entire state received over \$400 million during the last fiscal year, with 72 of 75 counties each getting well over a million dollars. Calhoun County, with just 86 retirees and beneficiaries, received almost \$605,000. APERS continues to be a powerful economic engine across the state.

**QUARTERLY REPORT FOR THE PERIOD ENDING JUNE 30, 2013 - Presented by Mr. Ryan Ball and Mr. Kevin Dolsen of Callan Associates, Inc.**

Mr. Dolsen reviewed the capital markets, noting that Domestic and International Fixed Income had lost 2.32% and 3.44% respectively. While those numbers were not large by Equity standards, they represented a significant downturn for the Bond market and were a result of the Federal Reserve's talk of "tapering the stimulus". The fact that the APERS Board had chosen to reduce the fund's exposure to that class and increase other areas, was one of the main reasons the

fund was able to generate a 15.58% return during Fiscal Year 2013. This ranked it in the top 5% of all public funds and put APERS at a new high-water mark of just under \$6.7 billion.

The modest (3%) overweight in Domestic Equity was due to market movement, while the 4% underweight in Real Assets was a result of all the funds not yet being called. For the past 12 months, active management added 1.74% to the fund's returns, while asset allocation added an additional 0.26%.

- **Lombardia:** was the best performing domestic equity manager in the portfolio for the quarter, gaining 5.2% for the quarter and 28.04% for the year, landing them in the top decile of their peers.
- **Wellington:** did very well relative to their peers and benchmark, returning 4.61% and 27.75% respectively for the quarter and the trailing 12 months.
- **Westwood:** trailed their benchmark by a significant margin, returning only 0.23% for the quarter, however for the year this manager grew by 26.44% and outperformed its benchmark.
- **AOR:** was the worst performing fund over the past quarter, dropping 11.24%, but Callan noted that it had been the worst possible investing environment for their investing strategy and most diversified strategy portfolios had lost money over the that time period.
- **Blackstone Hedge:** managed to pull 2.25% profits in a very difficult quarter and placed in the top decile of their peers.

Dr. Shelnutt questioned the recent losses in this asset class, saying it was his understanding that the Diversified Strategies was supposed to provide a less volatile investment risk. Mr. Dolsen reminded him that much of the initial funds had come from equities and assured him that this had been an extremely, non-typical quarter. Research has shown that there is normally a drawdown in approximately 1 out of 10 quarters, but not usually to this magnitude, but Callan saw no reason for alarm.

#### **Global Equity Manager Replacement:**

Mr. Ball reminded the Trustees that they had terminated UBS at the May meeting and instructed Callan to search for possible replacements. In order to best complement the existing managers, Callan looked for "growth at a reasonable price" and expected an initial funding of approximately \$300 million. From the initial list of 70-100 possible managers, Callan narrowed down the list to the following six semi-finalists:

- Baillie Gifford International LLC
- EARNEST Partners, LLC
- Harding Loevner LP
- MFS Investment Management
- Schroder Investment Management North America Inc.
- T. Rowe Price Associates, Inc.

After reviewing the six firms' significant history, past performance, quoted fees and other noteworthy factors, the Board asked Mr. Ball and Mr. Dolsen which managers they thought would be the best fit with APERS' existing managers, The Callan team chose Baillie Gifford, EARNEST, and Harding and explained their reasons for each.

Mr. Gaddy motioned to follow the consultants' recommendations and invite Baillie Gifford, EARNEST, and Harding to give presentations. Ms. Wright seconded and the motion passed.

#### **Investment Policy Amendment:**

Ms. Stone explained that last year the Board had adopted and ratified a new asset allocation, and at the November meeting, at the actuaries' suggestion, they had changed their assumptions on real rate of return and inflation rate. In order not to run afoul of APA rules, she asked the Trustees to approve these same items in the Investment Policy Statement so they could be promulgated through the regular process.

Judge Jacobs motioned to reapprove the designated changes to the ISP and was seconded by Ms. Bevis. Motion passed unanimously.

**Investment Guidelines Amendment:**

Mr. Ball explained that one of APERS' Fixed Income managers had requested a change in their guideline regarding the duration of how long a bond can be held. Previously, the average effective duration was allowed to vary from the benchmark by no more than +/- 10%. After discussing it with that manager, Staff felt that all Fixed Income managers' guidelines should be amended to allow them the same variance of -30% to +15%. After a short discussion on how this allowed the manager to act more defensively Judge Jacobs motioned to adopt this guideline amendment for all APERS' Fixed Income managers. He was seconded by Ms. Bevis and the motion passed.

The second request for guideline amendments was from Artisan, one of APERS International Equity managers. Mr. Dolsen explained that Artisan wanted to raise their limit on Emerging Market from the current maximum of 20% to 30%, as well as increase the limit on a single security from 5% to 10%. Finally, they were requesting to add the ability to invest up to 10% of the market value of the portfolio in debt/convertible securities. Callan and Staff had no problems with any of these changes, but would request that Artisan notify them whenever they exceeded the old guidelines and ventured into the range of these new ones. Ms. Wright motioned to accept the new guidelines for Artisan, with the reporting of exceptions. Ms. Harris seconded and the motion carried.

**SUMMARY OF RETIREES FOR JUNE, JULY & AUGUST 2013 :**

Ms. Stone stated there was nothing unusual during the quarter. Currently, APERS is retiring a steady stream of 135-140 people a month. During December and June, this number can swell to over 400.

**MEDICAL REVIEW BOARD RECOMMENDATIONS:**

The Medical Review Board met at 10:00 a.m. on Tuesday, August 13, 2013 in the APERS Library to discuss two (2) cases: Ms. Evelyn M. Paulie and Ms. Beverly K. Harris.

- After review and discussion, the Medical Review Board found that Ms. Evelyn M. Paulie was suffering from an illness or injury at the time of the member's termination in February 2010, which subsequently led to the disability determination.
  
- After review and discussion, the Medical Review Board found that Ms. Beverly K. Harris was suffering from an illness or injury at the time of the member's termination in May 2004, which subsequently led to the disability determination.

With APERS Board approval, in accordance with ACA 24-4-511(e)(3) benefits for both members will be effective September 1, 2013. On a motion made by Ms. Harris and seconded by Ms. Wright, the Trustees approved the Medical Board Reviews' recommendations.

**2013 INTERNAL AUDIT RESULTS AND PROPOSED 2014 AUDIT SCHEDULE – Presented by Mr. John Treloggen, APERS Internal Auditor**

Mr. Treloggen reminded the Trustees that at the May meeting they had approved a revised the original list of eight planned audits down to four audits due to the Internal Audit position being vacant from October, 2012 until April, 2013. Those audits included:

- Disability Benefits
- Refunds of Contributions (employee)
- Benefit Accounting
- Refunds of Contributions (employer)

There were no Special Projects planned or conducted in Fiscal Year 2013. Each of the four audits conducted resulted in achievement of audit objectives and no audit findings were identified.

Mr. Treloggen listed the eight planned audits and their objectives scheduled for Fiscal Year 2014; they included:

<u>Audit Area</u>	<u>Audit Objective</u>
General	Review written procedures of agency position.
Equities, Fixed Income	Review process for handling investment transactions.
Age and Service Benefits	Review process for verifying benefit calculations.
Age and Service Benefits	Review of agency practices regarding collection of required documents.
Age and Service Benefits	Review of Final Average Salary (FAS) in benefit calculations: to evaluate months used for FAS.
Age and Service Benefits	Review of Age 62 Temporary Annuity.
Age and Service Benefits	Review of Tax Withholding for Monthly Annuities.
General	Review agency workflow for identification of work duplication.

Ms. Wright wondered if there was a planned audit for “customer satisfaction” from the members that had visited APERS. Ms. Stone responded that currently APERS regularly sends out random surveys to people who have come in for pre-retirement information. Overall, the responses are generally very favorable, but when a complaint or problem is reported, it is immediately addressed. She admitted that a more comprehensive questionnaire could be introduced once the new Pension Administration System comes online.

Judge Jacobs motioned to accept the FY2013 Audit Report and the FY2014 Planned Audit. He was seconded by Ms. Wright and the motion carried.

#### **FINANCIAL STATEMENTS FOR THE QUARTER ENDING JUNE 30, 2013:**

Ms. Stone stated that for Fiscal Year 2013, APERS has paid out just under \$397 million in benefits and had still grown the assets quite nicely.

#### **OTHER BUSINESS:**

##### **Legal Update – Presented by Mr. Jay Wills, APERS Attorney Specialist**

Mr. Wills introduced himself to the new Trustee and said he had three items to bring to the Board’s attention. The first issue concerned a long-time employee of Jefferson County, J. Y. Williams, who discovered he was missing five years of service when he filed for his retirement from APERS. Currently, Mr. Williams is being represented by Judge Marion Humphrey (ret.). Together, they checked with the Social Security office and discovered that during those missing five years, Jefferson County had filed W-2s, withheld taxes, paid FICA, etc. on his wages. County officials were of the opinion that during those five years, Mr. Williams had not been a “county employee” as he was being paid through a federal grant.

Staff had calculated the past due contributions for those for those five years, excluding late fees and interest, were around \$87,000. APERS has tried to work with the county officials, showing them the documentation from Social Security and attempting to work out a comfortable payment plan for the past due monies, but all Staff’s efforts have been ignored. In mid June, APERS attempted to collect the past due amount via interception of Jefferson County’s “turn-back” funds, as permitted by statutory authority. However, on July 25, APERS was served with an ex parte temporary restraining order from an attorney from Hot Springs, Mr. Burt Newell, along with a handful of FOIA requests.

APERS is being defended by Ms. Mindy Pipkin from the Attorney General’s Office and she has already filed a motion to dismiss. Staff has advised Jefferson County that they will not try to intercept any funds until the APERS’ Board has a chance to adjudicate whether or not Mr. Williams was indeed a county employee. Mr. Wills stated that he did not feel comfortable with the Board being asked to adjudicate unless Mr. Williams could be present to argue for his retirement. Mr. Wills said he was trying to coordinate a day in September or October that would be convenient for all parties. At this time, Mr. Williams has decided to postpone his retirement, so no one is pressing for an immediate decision and Mr. Wills wanted to wait until the Attorney General’s Office got the Jefferson County lawsuit dismissed, before scheduling the hearing.

The second issue was regarding the dissolution of the National Timber Partner’s association. Attorney General has prepared a complaint to file that they hoped to have filed by today. Ms. Regina Harrelson is the A.G. lawyer handling the case, which is basically a simple breach of contract. NTP owes APERS \$15 million (of an outstanding \$25 million) that is due this year to

buy out APERS interest in the Limited Partnership. To date, they have paid only \$8 million while their financial sheets show assets with an amount sufficient to pay off their debt. Their response to the question of when might they pay off the balance was "perhaps November 2014." Mr. Wills stated the retirement system would be entitled to pre-judgment interest as soon as the lawsuit was filed. He speculated that once the interest clock starts running on the approximately \$14 million currently due to APERS, it might sharpen their focus on getting APERS paid off. This case would fall under the jurisdiction of the Arkansas Courts and subject NTP to both pre- and post-judgment interest.

Mr. Wills stated that the final issue has arisen in response to the Montgomery County Nursing Home decision. He noted that the same lawyer who handled the case for Montgomery County has discovered three other nursing homes (Eldorado, Jonesboro and Lawrence County) and 5 plaintiffs that he felt were really run by the county, so the employees should be entitled to APERS membership. Mr. Wills felt that the plan was to use the APERS Board's determination as leverage to get the counties to pay off and noted that none of the three nursing homes in question have ever appeared in APERS' data-bass. In his opinion, all the outfits had been set-up correctly as a stand-alone, but he wanted to make sure he had every bit of information available before making a recommendation to Staff. Mr. Wills opined that this would probably not become an issue before sometime next year, if at all.

**Technology Update – Presented by Ms. Gail Stone, APERS Executive Director**

Ms. Stone started by polling the Board and Callan as to availability dates in September and October for the Global Equity Manager interviews; early October seemed to be the most convenient for most.

Ms. Stone announced that "Intention to Award" has been posted for APERS to retain the services of Vitech Corporation to develop a new Pension Administration (computer) System. Staff anticipates that this will take 3 to 3½ years, at a cost of \$12.5 million. This new system will replace MARSS, the currently used main frame system that was created in 1994 and is now obsolete. The advent of this new system will represent a huge upgrade in APERS' ability to service its members and employers through interactive features and will be server based.

**Staff Travel Report**

Ms. Stone commented that the report contained the reviews from Staff Attorney Jay Wills regarding the annual NAPPA convention, as well as Madison Davis' account of the recent NCSSSA convention. She reminded the Board that APERS is charged with the duty of keeping the state employers compliant with Social Security's 218 Agreement.

**2013 Annual Educational Seminar**


Ms. Stone reminded the Trustees that the APERS Annual Educational Seminar would be held on Tuesday, October 22<sup>nd</sup> at the Capital Hotel in Little Rock. This year's topic will be: Interest Rates and how they affect all the Investments.

**NEXT QUARTERLY BOARD MEETING:**

The next quarterly meeting of the APERS Board of Trustees is scheduled for Wednesday, November 20, 2013 at 9:00 a.m.

**ADJOURNMENT:**

There being no further business, the meeting was adjourned.

  
MR. ARTEE WILLIAMS, CHAIR

  
MS. GAIL STONE, EXECUTIVE DIRECTOR