

**MINUTES OF THE REGULAR MEETING OF THE BOARD OF TRUSTEES
ARKANSAS PUBLIC EMPLOYEES RETIREMENT SYSTEM
NOVEMBER 19, 2014**

The regular quarterly meeting of the Board of Trustees of the Arkansas Public Employees Retirement System was held on Wednesday, November 19, 2014 at 9:15 a.m., in the Conference Room, 124 West Capitol, Little Rock, Arkansas. Ms. Ouida Wright presided.

QUORUM PRESENT:

Ms. Wright recognized the presence of a quorum.

BOARD MEMBERS PRESENT:

Ms. Ouida Wright (State Employee Member), Conway, AR
Ms. Carol Bevis, (Other, Non-State Employee), Little Rock, AR
Mr. Bill Gaddy (State Employee Member), Little Rock, AR
Dr. John Shelnett, Dept. of Finance and Administration (*proxy*)
Mr. Wes Goodner, State Treasurer Deputy (*proxy*)
Ms. Janet Harris, Deputy State Auditor (*proxy*)
Ms. Gail H. Stone (Executive Director), APERS

BOARD MEMBERS ABSENT:

Mr. Artee Williams (State Employee Member), *Chair*, Director, Dept. of Workforce Services
Judge Mike Jacobs (County Employee), Clarksville, AR
Mayor Steve Northcutt (City Employee), Malvern, AR
Hon. Charles Robinson, (Ex-Officio Member), State Treasurer
Hon. Charlie Daniels (Ex-Officio Member), State Auditor
Hon. Richard Weiss (Ex-Officio Member), Dept. of Finance and Administration

VISITORS PRESENT:

Mr. Ryan Ball, Callan Associates, Inc.
Ms. Brianne Weymouth, Callan Associates, Inc.
Mr. Mita Drazilov, Gabriel Roeder Smith & Company
Mr. David Hoffman, Gabriel Roeder Smith & Company
Mr. Paul Young, Arkansas Municipal League
Mr. Mike Knapp, Bureau of Legislative Audit
Mr. Chris Villines, Association of Arkansas Counties
Mr. Jody Carreiro, Osborne & Carreiro

STAFF PRESENT:

Ms. Michele Williams, APERS Deputy Director
Mr. Carlos Borromeo, APERS Chief Investment Officer
Ms. Susan Bowers, APERS Associate Director of Investments
Ms. Victoria Settles, APERS Internal Auditor
Ms. Sheila Watts, APERS Chief Financial Officer
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 KAAZ. This letter of notification is pursuant to A.C.A. 25-19-101 (Act 93 of 1967) as amended-The Freedom of Information Act.

PRESIDING TRUSTEE FOR THE MEETING:

Due to the absence of both the Chair and Vice Chair, former Chair Ouida Wright was asked to preside.

MINUTES:

Prior to the Board meeting, a copy of the Minutes from the meeting of August 20th was mailed to each APERS Board member for review. On a motion made by Mr. Goodner and seconded by Mr. Gaddy, the August Minutes were approved as presented.

ANNUAL ACTUARIAL VALUATION FOR FISCAL YEAR 2014 – Presented by Mr. Mita Drazilov and Mr. David Hoffman of Gabriel, Roeder, Smith and Company

Mr. Drazilov reminded the Trustees the purpose of the Annual Valuation and stated that there were certain elements that the actuaries needed from APERS to perform the valuation. The first component was the number and status of the members of the retirement system. He showed the breakdown of the 31,914 retirees, beneficiaries, and DROP participants; there were also 13,514 inactive members that needed to be taken into consideration. Mr. Drazilov then compared these figures to the number of active participants (45,837) or about 1.4 active members for every person collecting a benefit.

The second component of the valuation was the derivation of the funding value of assets and Mr. Drazilov stated that 2014 had been a terrific year financially for the system. There was an actuarial gain of over \$351.3 million using the 4 year phased-in recognition of investment gains/losses. APERS' ratio of Funding Value to Market Value now sits at 92% giving the fund a slight cushion against poor investment returns or the ability to lower the Assumed Rate of Return even further. Mr. Drazilov reminded the Board that they had already elected to drop it from 8% to 7.75%.

He noted that not all gains/losses came from investment risks, there were also the non-economic risk areas; these included such areas as disability retirements, death-in-service, and non-vested service withdrawals. These risks accounted for an actuarial gain of \$425.2 million (or about 5% of the accrued liabilities) in Fiscal Year 2014.

As part of the newly adopted funding policy, Gabriel, Roeder Smith had promised to provide risk metrics that would illustrate the riskiness of either asset allocation or liabilities within the system. Mr. Drazilov pointed out how in 2007 valuation, the Market Value of Assets (MVA) had APERS at 97% funded, while the Actuarial Value of Assets (AVA) showed the system 89% funded. Just two years later in 2009, the MVA was down to 62% (a change of 38%) while the AVA had slipped to 78% (a change of only 11%). He noted that one of the reasons for using the AVA was to smooth out the fluctuations of the plan to allow for more informed financial decisions.

Mr. Hoffman revisited the historical numbers comparing the system now to how it looked in the early 1980's. He emphasized that, now that the plan was fully mature, it would tend to be much more volatile than it had been in the past. Actions the Board had taken with the investment policy would be useful in dampening some of the volatility. While employer/employee contributions are currently running just less than 18% of pay, the benefits being paid out is around 30% with the difference (~\$100 million annually) being made up from investment income. Mr. Hoffman reassured the Trustees that this was normal, things were going as planned and the system was doing well.

Mr. Drazilov noted the final component of the valuation was to set the employer contribution rate for the upcoming fiscal year (beginning on July 1, 2015). Amortizing the unfunded liabilities over a 23-year period (down from a 25-year period used last year), the total employer contribution was calculated to be 14.50%. This is down from 14.76% currently being collected.

Approval of Year-End Transfers

At each November meeting, the Board is also asked to approve the year-end transfers, as directed by statute §24-4-201. The actuaries briefly described the transfers that were displayed on page A-6 of their report. Ms. Harris motioned to approve the requested transfers and was seconded by Mr. Goodner. Motion passed. Mr. Drazilov then requested the Board adopt the Employer Contribution Rate of 14.50% beginning July 1, 2015. Mr. Gaddy motioned to accept the rate and he was seconded by Ms. Harris. Motion passed.

Draft Amendment to Reg. 408 Reflecting Change of Interest on Purchase of Service Effective January 1, 2015

Ms. Stone drew the Trustee's attention to a draft amendment concerning Regulation 408 which read:

REGULATION 408 – 1997 – REGULAR INTEREST (as amended May 2001)

In accordance with A.C.A. 24-4-101 (38), the rate of interest to be charged for all provisions of Chapter 4 of Title 24 where reference is made to "regular interest", ~~for payments received on or before December 31, 1999, shall be 7.75% per annum, compounded annually. Effective January 1, 2000, regular interest shall be 8% per annum,~~

compounded annually. shall be the actuarially assumed rate of return as adopted by the board of trustees from time to time. Unless otherwise directed by the board of trustees, the change in the level of "regular interest" shall become effective on the first day of the calendar year. Any commitment already in active payment status at that time, wherein APERS has received at least one installment payment, shall remain at the rate previously established by the board.

She reminded the Board that if they approved the amendment, it would still need to go through the A.P.A. process of being advertised, having a public hearing and then be approved by the legislature. Mr. Gaddy moved to approve the new wording. Ms. Bevis seconded the motion and it passed unanimously.

Request from Member

Mr. Gaddy displayed a letter from an APERS member, Capt. Gary Mullins, asking the Board to revisit, and hopefully increase, the interest paid on the DROP accounts. Capt. Mullins had sent a copy of his letter to each APERS Board member. Mr. Gaddy stated that he felt the Trustees should get input from the actuaries before making any decisions at the next meeting. Ms. Wright asked if he would make a motion along those lines and Mr. Gaddy motioned to request GRS do a study on the effects of raising the DROP interest from 2.5% to 3%, 3.5% and 4%. After a short discussion, Dr. Shelnett seconded. Ms. Stone pointed out that the current interest rate on a 10-year Treasury Bill (the closest comparable investment) was holding at 2.35%.

Board Transitions

In honor of the Trustees for whom this would be their last meeting, Ms. Stone passed out a platter of pumpkin-spiced cupcakes and thanked those Board members for their dedicated service to APERS.

QUARTERLY REPORT FOR THE PERIOD ENDING SEPTEMBER 30, 2014 - Presented by Mr. Ryan Ball and Ms. Brianne Weymouth of Callan Associates, Inc.

Mr. Ball gave a brief backdrop of the investing environment during the recent quarter noting it was an especially bad quarter for energy stocks. While Europe and Japan struggled, it was a moderately positive quarter for the U.S. as the dollar strengthened.

The fund's asset allocation maintained its 4% overweight in Domestic Equities due to market returns and did help the fund's return for the quarter.

For the quarter, the portfolio returned (2.26%), but still maintained a 9.61% return for the trailing 12 months and was ahead of its benchmark by 0.15%. This ranked APERS at the 50th percentile against its peers over the last year, but in the top 8% over the past three years.

- **INVESCO Core** - had a very strong quarter adding almost 3.5%.
- **TA Realty** - was recently sold to the Rockefeller Group; Callan is watching closely.
- **Baillie Gifford** - had some organizational changes, but the investment team was quite large and this one individual shouldn't have an effect.

Ms. Stone commented that over the last 7 days of October the fund turned the corner and the portfolio was just down 1.1% from its June 30th closing. Those losses had been pared even further during November and unofficially the portfolio's current value was around \$7.68 million.

SUMMARY OF RETIREES FOR SEPTEMBER, OCTOBER & NOVEMBER 2014 :

The high number of retirees continued to pass through the APERS offices. Ms. Stone pointed out that she was expecting a surge in December as incumbents who had lost their positions in local elections and various high-level agency personnel opted for retirement. These names would show up in the February meeting summary.

MEDICAL REVIEW BOARD RECOMMENDATIONS:

The Medical Review Board met at 10:00 a.m. on Wednesday, November 5, 2014 in the APERS Library to discuss 2 (two) cases: Ms. Quonya L. Brazil and Ms. Karen Cobb.

- After review and discussion, the Medical Review Board found that Ms. Brazil was suffering from an illness or injury at the time of her termination in October 2009, which subsequently led to the disability determination.

- After review and discussion, the Medical Review Board found that Ms. Cobb was suffering from an illness or injury at the time of her termination in December 2012, 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 December 1, 2014. Ms. Harris motioned to accept the recommendation of the Medical Review Board. He was seconded by Mr. Goodner. Motion passed.

2014 INTERNAL AUDIT RESULTS – Presented by Ms. Victoria Settles, APERS Internal Auditor

Ms. Settles explained how between March 1st and June 30th she had performed the five audits listed below:

- A. Review of agency workflow for identification of work duplication
- B. Review the process for handling investment transactions
- C. Review the process of benefit reconciliations
- D. Review of agency practices regarding collection of required documents
- E. Review of tax withholdings for monthly annuities

Four of the above five audits conducted resulted in achievement of audit objectives and no audit findings were identified. The audit related to the review of tax withholdings for monthly annuities resulted in the following finding and recommendation:

The audit of tax withholdings resulted in a finding for the Retiree Services Section and the Administrative Services Section. Both sections failed to ensure the correct equation or formula was being used by the system for the state calculation and failed to update the state and federal tax tables in a timely manner. The audit of tax withholdings also resulted in a recommendation to improve and update procedures in the Benefit Accounting Unit.

Director’s Response to Audit Findings – Presented by Ms. Gail Stone

Ms. Stone’s explanation for this finding was the change-over in management in two sections during the past year and this institutional knowledge failed to get passed along. Each of the new section managers thought it was the other’s responsibility. She noted that once it was brought to APERS’ attention, the managers began scrambling to notify the approximately 17,000 affected retirees. They will be getting a letter in January 2015 explaining what is happening with their checks regarding withholding of State and Federal taxes. In most cases, more money will need to be withheld from the retirement checks to avoid owing money on April 15th.

Ms. Stone distributed a handout detailing the written procedure that was now incorporated into each manager’s procedure manual. She apologized for the oversight and promised there would be no repeats. Originally, the problem had been masked by tax-cuts at the federal level so it went largely unnoticed. Dr. Shelnett added that newer tax-tables would be implemented soon and Ms. Stone acknowledged that this would probably be an annual mail-out for the retirement system.

FINANCIAL STATEMENTS FOR THE QUARTER ENDING SEPTEMBER 30, 2014:

For the first quarter of the fiscal year, Ms. Stone stated that APERS had paid out \$117.5 million in benefits, but the fund is sustaining strong asset levels at \$7.3 billion

OTHER BUSINESS:

Consideration of a Special Meeting Regarding Woodruff County Nursing Home – Presented by Mr. Jay Wills, APERS Attorney Specialist

Ms. Stone explained that Mr. Wills had planned to be at this meeting, but he was still recovering from surgery. The plaintiffs’ attorney Randy Hall was insisting on a hearing to receive testimony from the Woodruff County judge and was refusing to accept it as an affidavit. This would require a special hearing before the APERS Board. Due to the upcoming holidays and people’s schedules, the meeting probably will not be scheduled until after the first of January.

Travel Report

The Board members noted the two trips made by Mr. Borromeo, APERS CIO.

Tentative Schedule for 2015 Meetings

- February 18, 2015
- May 20, 2015
- August 19, 2015
- October 20, 2015 – Educational Investment Seminar
- November 18, 2015

The Trustees expressed no problems with the standard dates scheduled for 2015.

NEXT QUARTERLY BOARD MEETING:

The next quarterly meeting of the APERS Board of Trustees is scheduled for Wednesday, February 18, 2015 at 9:00 a.m.

ADJOURNMENT:

There being no further business, the meeting was adjourned.


MR. ARTEE WILLIAMS, CHAIR


MS. GAIL STONE, EXECUTIVE DIRECTOR