

**MINUTES OF THE REGULAR MEETING OF THE BOARD OF TRUSTEES  
ARKANSAS PUBLIC EMPLOYEES RETIREMENT SYSTEM  
NOVEMBER 15, 2017**

The regular quarterly meeting of the Board of Trustees of the Arkansas Public Employees Retirement System was held on Wednesday, November 15, 2017 at 9:00 a.m., in the Conference Room, 124 West Capitol, Little Rock, Arkansas. Mayor Morris presided.

**QUORUM PRESENT:**

Mayor Morris recognized the presence of a quorum.

**BOARD MEMBERS PRESENT:**

Mayor David Morris, (City Employee), *Chair*, Searcy, AR  
Mr. David Hudson, (County Employee), Fort Smith, AR  
Ms. Candace Franks (State Employee Member), Little Rock, AR  
Mr. Steve Faris (Retired State Employee), Little Rock, AR  
Hon. Andrea Lea, (Ex-Officio Member), State Auditor  
Mr. Larry Walther, (Ex-Officio Member), Department of Finance and Admin.  
Mr. Jason Brady, State Treasurer's Office (*proxy*)  
Ms. Gail H. Stone (Executive Director), APERS

**BOARD MEMBERS ABSENT:**

Ms. Carol Bevis, (Other, Non-State Employee), Little Rock, AR  
Mr. Daryl Bassett (State Employee Member), Sherwood, AR  
Mr. Dennis Milligan, (Ex-Officio Member), State Treasurer  
Mr. Larry Walther, (Ex-Officio Member), Department of Finance and Admin.

**VISITORS PRESENT:**

Mr. Ryan Ball, Callan Associates, Inc.  
Mr. David Hoffman, Gabriel Roeder Smith and Company  
Mr. Mita Drazilov, Gabriel Roeder Smith and Company  
Mr. Paul Louthian, Department of Finance and Admin.  
Dr. John Shelnett, Department of Finance and Admin.  
Mr. Kevin Liang, General Counsel for the Auditor  
Rep. Doug House, Co-Chair Joint Retirement Committee  
Rep. Bruce Coleman  
Rep. Johnny Rye  
Rep. Les Warren (*arrived late*)  
Ms. Cindy Frizzell, Municipal League  
Mr. Chris Villines, Association of Arkansas Counties  
Mr. Marc Watts, AR State Employees Association  
Mr. Mike Knapp, Bureau Legislative Audit  
Mr. Hank Klein  
Mr. Mike Wickline, *Arkansas Democrat-Gazette*

**STAFF PRESENT:**

Mr. Jay Wills, APERS Deputy Director  
Mr. Carlos Borromeo, APERS Chief Investment Officer  
Ms. Usha Doolabh, APERS Investments Manager  
Ms. Jessica Middleton, APERS General Counsel  
Mr. John Owens, APERS Internal Auditor  
Ms. Becky Walker, APERS Director of Operations  
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.

**QUARTERLY REPORT FOR THE PERIOD ENDING SEPTEMBER 30, 2017 - Presented by Mr. Ryan Ball of Callan Associates, Inc.**

Mr. Ball began the presentation by noting the new format of the Callan quarterly report and then moved into a market perspective of the recent quarter. Riskier assets did well, and Equities had a strong quarter across the board. The S&P experienced 13 all-time highs during this quarter. Emerging Markets did particularly well driven by a strong performance out of China (over 14.5%). Fixed Income was steady and finished the quarter up slightly. While the Fed took no action this quarter, it is predicted they will raise the rate by 25 basis points before the next quarter is over.

Mr. Ball discussed the current stock market rally and other post-recession recoveries. He examined inverted yield curves and current debt levels in an attempt to predict when the present rally might end.

The Fund's Asset Allocation is close to the target, with the small overweight in Equities coming from market movement at the expense of Fixed Income. The fund slightly outperformed the policy target by 23 basis points over the last quarter; the portfolio earned \$313.7 million or 3.81% over that same time. For the trailing 12-month period, the fund grew by 12.15%. As of September 30, 2017 APERS' portfolio had a market value of almost \$8.56 billion.

Manning & Napier was terminated and APERS' new Small Cap manager, LSV, was funded (\$200 million) during this quarter

Mr. Ball quickly reviewed some of the better and worst individual manager performances over the past quarter and compared them to their indexes. He discussed the strong returns from the Value-added Real Estate funds, namely Lasalle-6 and TA-10. LaSalle-7 and TA-11 are already returning cash and Mr. Ball noted that at the next meeting, he'd like to discuss reinvesting those funds to keep the allocation of the portfolio stable.

Mr. Walther asked if there were any areas of the portfolio that needed the Trustees' attention and Mr. Ball stated that anything that would lower the portfolio's equity exposure should be considered; he specifically discussed reducing REITs and Energy exposure. Callan is actively looking for investments to suggest as replacements. Currently, APERS has about 70% of the portfolio in a wide variety of Equities.

Mr. Hudson asked for clarification on quarterly/annual returns versus benchmarks/targeted returns. Ms. Stone explained that over the last year, the fund returned 12.15%, however the benchmark returned 12.89%, while other similarly-sized funds averaged 12.33% during that one year. Mr. Hudson asked how that figured against the 7.15% Assumed Rate of Return the board had adopted several meetings earlier and Ms. Stone detailed the process.

Mr. Hudson also requested that Callan create a "Summary Letter" condensing what the Board would need to focus on into 2-3 bullet points, so the Trustees knew in advance what they would be asked to make decisions upon. Mr. Ball and Ms. Stone reviewed several of the various pages in the Callan Report in an attempt to decide how best to present the information in a form that the Board desired.

Ms. Stone commented that she had been planning on reinstating her "Monthly Review" to the Trustees. She explained that previously she sent out a 1-2 page monthly review to the Trustees highlighting a snapshot of the current market, APERS' returns, and any legal, actuarial or investment issues needing the Trustee's attention. All agreed that this sounded very helpful.

Mr. Hudson added that he would like to see "action items" noted on the agenda.

**ANNUAL VALUATION RESULTS – Presented by Mr. David Hoffman and Mr. Mita Drazilov of Gabriel Roeder Smith and Company**

Mr. Drazilov detailed the results of the June 30, 2017 APERS Actuarial Valuation, by first explaining the two reasons for the annual valuation: to measure the financial progress (funded position) and to establish the Employer Contribution Rate for Fiscal Year 2019 (beginning July 1, 2018). The Board would also need to establish a separate rate for the District Judges portion of the retirement plan based upon the actuaries' findings. Mr. Drazilov reminded the Trustees that they had adopted a tentative APERS' Employer Rate of 15.32% of payroll back in August and now that the Valuation was complete, there was nothing suggesting it needed to be changed.

Since this would be the first APERS Valuation for most of the Board members, Mr. Drazilov took great pains to break down each step the Actuaries took and explained how to interpret the results. He reviewed the process, and the demographic and economic assumptions used to arrive at their conclusions. Mr. Drazilov explained that these assumptions were reviewed and updated (if necessary) every 5-years. The results of the latest Experience Study would be presented to the Board at the May meeting for their adoption.

Mr. Drazilov then discussed how they had calculated the Employer Contribution for the small, closed-plan segment of APERS referred to as the District Judges. This division of APERS was incorporated in 2007 and consists of several 3 parts: New Plan, Old Plan and Still-Paying Old Plan. Unlike APERS "cost sharing" where the 15.32% employer rate is paid by all APERS Employers, the Still-Paying Old Plan calculates each political subdivision's rate separately, based upon the amount they owe and number of members. This will continue until they pay off their balance to APERS. At that point, the entity will be moved into the New Plan and begin Cost Sharing with the other APERS employers. Currently, there are 46 political subdivisions in the Still-Paying Old Plan that are making annual payments against their Unfunded Accrued Liability from prior to 2007.

He explained how the Employer Normal Cost for these District Judges was developed and then added to their Unfunded Accrued Liability to calculate the Employer Contribution for Fiscal Year 2019. Beginning July 1, 2018, their Employer Contribution will be 38.99%, while the Employees continue to pay 5%. Mr. Drazilov told that Trustees that later in the meeting, they would be asked to approve this rate, and ratify the APERS rate of 15.32%.

Mr. Hoffman took over at this point to discuss the APERS Valuation. He noted that he'd been listening to the Board's request of Callan for an Executive Summary and promised to provide one at future meetings, meanwhile, at this meeting he would try to stick to the high points. He noted that as of June 30, 2017, APERS had about 46,000 Active Members, 36,000 people receiving benefits and another 15,000 people who had left employment but were still vested with the System, or almost 100,000 people who were counting on APERS. The June 30<sup>th</sup> benefit payout was close to \$540 million, while the payroll on that same date was only \$1.7 million. Mr. Hoffman noted that this was possible because of the investment earnings and the solid health of the plan.

He reviewed how the Employer Contribution Rate was calculated and explained that if all the assumptions were met, it would allow the plan to continue to pay out benefits in excess of 30% of pay. Mr. Hoffman concluded by showing the Summary of the System Resources and Obligations and pointing out how those numbers figured into calculating the Employer Contribution Rate.

*(Chair Morris left at this time and Vice-Chair Walther took over.)*

Ms. Stone asked if there were any further questions before ratifying the Employer Rate of 15.32% the board had tentatively adopted in August, as well as the new District Judges rate for Fiscal Year 2019, beginning on July 1, 2018.

Mr. Walther questioned the components that the actuaries used to calculate the "Normal Cost" and how the assumed rate of return impacted the cost; Mr. Drazilov broke down the calculations and how they were intertwined. Discussion continued regarding investment gains and losses, and how the actuaries used a "4-year smoothing" formula to limit the volatility of the returns.

Mr. Hudson put forth a request for a special meeting with the Trustees, the Actuaries and Financial Consultants so all the board members could have a better understanding of how Callan and GRS functioned with the retirement system. Ms. Stone agreed to set up a private, one-day Callan College, with both teams, in Little Rock so all the Trustees could attend

Ms. Lea reminded the Board that Staff was waiting for a motion to adopt the Employer Contribution Rates for APERS and District Judges. Mr. Faris motioned to ratify the proposed rate of 15.32% for APERS employers beginning July 1, 2018. Ms. Lea seconded and the motion passed.

Mr. Hudson motioned to accept the Actuarial recommended Employer Contribution rate for District Judges of 38.99% and the other recommended political sub-division rates. He was seconded by Ms. Franks and the motion passed.

### **SUMMARY OF RETIREES FOR SEPTEMBER , OCTOBER & NOVEMBER 2017:**

Ms. Stone commented that this was simply for the Trustees' review. She noted that if the Trustees reviewed these over each quarter, they would get a feel for the ebb and flow of retirements as Baby Boomers continued to retire. Ms. Stone pointed out that APERS had been Contributory for 12 years and currently enjoyed almost 70% participation. She estimated that within the next 7-10 years, the plan would be close to 100% Contributory.

### **FINANCIAL STATEMENTS FOR THE QUARTER ENDING SEPTEMBER 30, 2017:**

Ms. Stone stated that at the end of the quarter, APERS had a market value of almost \$8.3 Billion. She noted that this number differed slightly from Callan's because theirs included the ASPRS (State Police) assets. For the first quarter of the fiscal year, APERS has paid out close to \$133 million in benefits.

*(Mayor Morris came back and Vice-Chair Walther returned control of the meeting to him.)*

Mr. Faris requested that Ms. Stone compile a short history of how State Police Retirement System ended up being combined with APERS. She commented that was an excellent idea and she would work on it.

### **OTHER BUSINESS**

#### **Litigation Update – Presented by Mr. Jay Wills, APERS Deputy Director**

Mr. Wills reminded the Board that Ellis Sloan's Claims Commission case against APERS and Ms. Stone had recently been thrown out. They still have seven days in which to appeal directly to the Legislature. Mr. Wills reminded the Board that this case involved an individual who worked for one of APERS' Money Managers, who moved to a new investment firm and mistakenly thought he could take the APERS portfolio with him. When the Board declined to allow him, he sued Ms. Stone for \$1.5 million stating that she had promised him he could do it. The Claims Commission agreed with APERS Staff and threw the case out since cases arising out of APERS legislation are explicitly excluded from the Claims Commission's jurisdiction. Mr. Wills opined he didn't see this case going any further.

In February, the Board will be hearing in regards to a Survivor's Benefit question. In summary, a gentleman filed for retirement in 1997 and listed his fiancée as the beneficiary of his B50 option. The man recently passed away, but unfortunately, never got around to marrying the woman. APERS has a regulation that requires any dependent to be shown as such on the last filed tax-return. She has never shown up as a dependent on any of the deceased member's returns. Both of their tax forms had been submitted to Staff and he had been providing about 80% of their income. Given that APERS has a regulation requiring Staff to use the IRS test, they did not feel comfortable ignoring the regulation, so the woman is appealing the Executive Director's decision in order to get the survivor benefits. Under the Administrative Procedures Act, this is the proper path for them to take before appealing to Circuit Court.

The APERS Board still needed to hear Mr. Jerry Hudlow's appeal. He was seeking to get enhanced service credit as an elected public official, although he had never been elected to any position. The Board had previously heard Staff's arguments, but had lost the quorum when it was Mr. Hudlow's time to present. Mr. Hudlow's lawyer indicated that Mr. Hudlow was requesting about 4 hours to present his side of the case. Mr. Wills said that if the board approved, he would organize a special meeting after the holidays for the Trustees to hear Mr. Hudlow's side of the case and make a final decision. Trustees asked if it might be possible to teleconference in for this hearing and Mr. Wills stated that would not be possible since Trustees really needed to be present to witness the demeanor and non-verbal characteristics that could not be seen over the telephone and gather more information using all their senses.

Finally, Mr. Wills gave an update on the status of the Nursing Home litigation. APERS' brief is due at the Court of Appeals on December 27, 2017. He said Staff was well into writing the brief and foresaw no difficulties in getting it submitted in a timely fashion. He was optimistic that the Court of Appeals would know the difference between "and" and "or". He noted that if Judge Gray's decision stood, then APERS would be forced to recognize the nursing home employees as APERS members and sue the counties for payments on them going back as far as the 1960s. This would most likely bankrupt all the counties involved.

**Manifest Injustice – Presented by Mr. Jay Wills, APERS Deputy Director**

Mr. Faris stated that the discussion regarding Manifest Injustice had been added to the agenda at his request and he felt that it might be better to postpone the discussion until the next meeting. In answer to several members’ queries, Mr. Wills explained that the Manifest Injustice Rule had been instituted at Teacher Retirement (ATRS) which allows them to alter the terms of their plan if a manifest injustice arose as a result of the strict application of the 5-year “look back” to correct their records. APERS does not have that issue. The Manifest Injustice rule was designed to cure a problem that APERS does not have.

**Regulations Updated**

Staff had recently performed a comprehensive review of the APERS Regulations and found that many needed to be tweaked to conform to the new electronic Pension Administration System. They had been reviewed by the Governor and the Legislature and had been approved by all. Ms. Stone handed out the updated regulations and instructed the Board members to replace the outdate copies in their Trustee Handbook.

**Private Label Callan College for Trustees**

Since this new board has been seated, there has been talk of holding a special Trustee training session on how to evaluate a pension investment system. Ms. Stone had checked with Callan about their availability and cost. Callan had waived their cost to APERS. She proposed that Staff coordinate with both Callan and GRS to host a customized, all-day training session to go over Investments 101 and Actuary 101 for all the Trustees. January seemed to be the best bet and Ms. Stone asked everyone to check their schedules. Mr. Hudson described his experience attending Callan College in San Francisco and felt that a custom session held locally with Staff in attendance would be invaluable.

Everyone seemed to think this was an excellent idea and Mr. Faris wanted to extend an invitation to the entire Joint Retirement Committee so that they might have a better understanding of how the APERS Board functioned.

**Approval of 2018 Board Meeting Dates**

- February 14, 2018
- May 14, 2018
- August 14, 2018
- October 23, 2018 – Trustee Educational Seminar
- November 14, 2018

**Annual Payout Graphic**

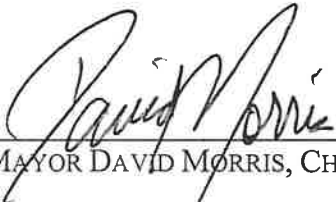
Ms. Stone handed out a Map of Arkansas Counties that showed graphically how much APERS paid out in benefits annually. In Calhoun County alone, the least populated county with just 85 retirees, the retirement system paid out \$833,000 last year. For the entire state, APERS pumps over \$500 million directly into the economy annually, with that number growing every year.

**NEXT QUARTERLY BOARD MEETING:**

The next quarterly meeting of the APERS Board of Trustees is scheduled for Wednesday, February 14, 2017 at 9:00 a.m.

**ADJOURNMENT:**

There being no further business, the meeting was adjourned.

  
MAYOR DAVID MORRIS, CHAIR

  
MS. GAIL STONE, EXECUTIVE DIRECTOR