

**MINUTES OF THE REGULAR MEETING OF THE BOARD OF TRUSTEES  
ARKANSAS PUBLIC EMPLOYEES RETIREMENT SYSTEM  
AUGUST 16, 2017**

The regular quarterly meeting of the Board of Trustees of the Arkansas Public Employees Retirement System was held on Wednesday, August 16, 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  
Ms. Carol Bevis, (Other, Non-State Employee), Little Rock, AR  
Mr. David Hudson, (County Employee), Fort Smith, AR  
Mr. Steve Faris (Retired State Employee), Little Rock, AR  
Mr. Daryl Bassett (State Employee Member), Sherwood, AR (*via teleconference*)  
Ms. Candace Franks (State Employee Member), Little Rock, AR  
Hon. Andrea Lea, (Ex-Officio Member), State Auditor  
Mr. Paul Louthian, Department of Finance and Admin. (*proxy*)  
Mr. Jason Brady, State Treasurer's Office (*proxy*)  
Ms. Gail H. Stone (Executive Director), APERS

**BOARD MEMBERS ABSENT:**

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.  
Ms. Brianne Weymouth, Callan Associates, Inc.  
Mr. David Hoffman, Gabriel Roeder Smith and Company  
Rep. Doug House, Co-Chair Joint Retirement Committee  
Ms. Cindy Frizzell, Municipal League  
Mr. Daniel Faulkner, Attorney General's Office  
Mr. Josh Curtis, Association of Arkansas Counties  
Mr. Mike Knapp, Bureau Legislative Audit  
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  
Mr. Jason Willett, APERS Chief Financial Officer  
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

**ELECT BOARD CHAIR AND VICE-CHAIR:**

Mayor Morris asked everyone at the board table to introduce themselves before starting the meeting. Once that was done, Mr. Faris motioned for Mayor Morris to continue on as the Chair of the APERS Board and for Mr. Walther to assume the position of Vice Chair. Ms. Bevis seconded and there was a short discussion, led by Judge Hudson who wanted to clarify if those positions were allowed to vote. Ms. Stone stated that according to Robert's Rules of Order, it was permissible to have either a non-voting Chair (except in case of a tie) or a voting Chair, but it needs to be consistent. Historically, the APERS Chair has been non-voting, however with this new board, new practices could be adopted. Judge Hudson opined that it was important for every board member to vote and express their opinions or they would lose their voice on the issues.

Mr. Faris amended his motion to clarify that the Chair would be free to participate in the meetings the same as any other board member. Ms. Bevis seconded the amended motion. Mayor Morris commented that he had been put on the board to represent roughly 500 cities and town in the State

of Arkansas, while Judge Hudson represented the 75 counties. He expressed his concern that the cities not lose their representation by virtue of him accepting the Chair position on the APERS' Board. Motion passed unanimously.

**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.

**MINUTES:**

Prior to the Board meeting, a copy of the Minutes from the May 17, 2017 meeting was mailed to each APERS Board member for review. Judge Hudson complimented the detail of the Minutes for an especially difficult meeting and motioned the Minutes be approved as presented. He was seconded by Ms. Franks and the motion passed.

**QUARTERLY REPORT FOR THE PERIOD ENDING JUNE 30, 2017 - Presented by Mr. Ryan Ball & Ms. Brianne Weymouth of Callan Associates, Inc.**

The report began with Mr. Ball summarizing the last quarter's investing environment. He noted that the last quarter of Fiscal Year 2017 how the Federal Reserve had raised its rate from 1% to 1.25% and inflation remained stubbornly low as of May. Consumer debt reached an all-time high in June. In the market, equities (both Domestic and International) had impressive returns with Healthcare, Financials and Technology leading the pack. Weakened U.S. Dollar strengthened the International returns. In Fixed Income, falling rates over the quarter helping the broad market.

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 underperformed the policy target earning 12.3% over the trailing 12-months. For the quarter the portfolio earned 3.28%, slightly over its target return. As of June 30, 2017 the fund had a market value of \$8.3 billion.

Ms. Weymouth reviewed how the various asset classes had performed before discussing individual managers. She elaborated how Manning & Napier had been struggling with their performance and also management issues and suggested the board terminate this International Equity portfolio. After a short discussion, Judge Hudson motioned to follow Callan and Staff's recommendation to fire Manning & Napier and place the roughly \$380 million in the MSCI ACWI ex US Index. Ms. Bevis seconded the motion and it carried.

**SMALL CAP VALUE MANAGER INTERVIEWS:**

Mr. Ball gave a short synopsis of what had happened with the Small Cap portfolio in the recent months, beginning with Lombardia's slow collapse and the APERS' monies being moved to the Russell 2000 Index. He explained the selection process Callan used to find the semi-finalists and at the last APERS meeting, the Trustees had chosen to interview two potential managers.

- **Boston Partners** – Ms. Kerry James, CFA & Mr. George Gumpert, CFA
- **LSV Asset Management** – Mr. Scott S. Kemper, Director & Mr. Josef Lakonishok, Ph.D

Each manager gave a twenty minute presentation that detailed the firm's history, personnel, investment philosophy, succession plans, past performance, and fees. After an intense discussion, Mr. Faris motioned to hire LSV and give them an initial \$200 million. He was seconded by Mr. Brady and the motion carried unanimously.

Ms. Stone pointed out that if the board affirmatively approved, Staff could begin immediate implementation of the contract, hire and begin funding LSV without waiting for the formal approval of the Review Committee. She explained that the Review Committee was meeting that day, so it would be next month before she could present the contract to them. Mr. Faris cautioned about sending the wrong signals to the General Assembly and advised Staff to wait until the contract had been approved and that a month was not too long to wait.

Ms. Lea asked if Ms. Stone would be attending the Review Committee meeting this afternoon and she acknowledged that she would be. Ms. Lea stated that she felt it would be proper if Ms. Stone explained to the committee that she had an add-on item from a decision that had been made

earlier that day and wished to include it in the discussion. Ms. Stone agreed that if she could get the contract before them later today, she would do so and if not, she would hold it until the meeting next month.

**BREAK**

*(Mr. Bassett left the meeting at this time)*

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

Mr. Hoffman explained to the new Board members that for years GRS has presented the APERS' Trustees with a preliminary Valuation at the August meeting in an effort to assist the Board in setting the next fiscal year's employer rate. Setting the projected rate at that time allows the employers plenty of time to adjust their budgets before next July 1, when the new rate would go into effect. He noted that this valuation was a considered to be tentative since GRS had very little time to work the numbers between the fiscal year-end (June 30<sup>th</sup>) and the APERS' August meeting. This was also the first year the membership data was provided by the new computerized pension administration system.

Based upon the submitted financial information, the computed funding value rate of return for the year ending June 30, 2017 was 7.8%. Given the assumed rate of investment return over that period was 7.5%, a small investment gain of \$19.6 million was realized. The biggest effect on the valuation this year was the new assumptions adopted at the May meeting. Those included lowering the investment return assumption from 7.5% to 7.15%, adopting a wage inflation assumption of 3.25% and a 30-year amortization for the Unfunded Actuarial Accrued Liabilities (UAAL). Using those assumptions, Mr. Hoffman told the Trustees that the tentative Employer Rate for Fiscal Year 2019 (beginning on July 1, 2018) would be 15.32% (up from 14.75%)

Mr. Hoffman also reminded the Board members that every five years, the actuaries did an experience study on the system and the next one was due in the spring of calendar year 2018. All the actuarial assumptions used in the valuation would be reviewed at that time. He also cautioned that the system still had almost \$158 million in unrecognized losses that would need to be factored in against next year's investment gains.

Judge Hudson clarified that cities and counties planned their budgets based on a calendar year while the state agencies and offices worked off a fiscal year. After a short discussion on that topic, Judge Hudson motioned to establish an expected 15.32% employer rate, beginning July 1, 2018. He was seconded by Mr. Faris and the motion carried.

**2017 AUDIT RESULTS AND 2018 PROPOSED AUDIT PLAN – Presented by Mr. Johnny Owens, APERS Internal Auditor**

Mr. Owens explained that the eight audits he performed were all in the Investments section of the agency. It was really just two audits, but conducted over four different asset classes. This was intentional, due to COMPASS still being in the design phase. There was also a special project reviewing the data integration.

List of 2017 Audits Performed:

1. Review of investment calculations (Domestic Equities)
2. Review of investment calculations (Domestic Fixed Income)
3. Review of investment calculations (International Equities)
4. Review of investment calculations (International Fixed Income)
5. Review accounting of year-end accruals (Domestic Equities)
6. Review accounting of year-end accruals (International Equities)
7. Review accounting of year-end accruals (Domestic Fixed Income)
8. Review accounting of year-end accruals (International Fixed Income)

2017 Special Project Audit:

COMPASS – APERS New Pension Administration System - SFY 2015-SFY 2017  
Tested derived data to be integrated into the newly designed pension administration system COMPASS from the old system MARSS.

All eight (8) of the audits conducted resulted in the achievement of audit objectives and no audit findings were identified. The special project conducted was determined that no errors existed in the integration of data from the old to new computer software.

Mr. Owens noted that the following areas were selected to be audited in the upcoming year.

2018 Internal Audit Risk Assessment:

Custodian Bank	Review of daily transactions.
Service Purchases	Review retroactive service calculations
Social Security	Review of process for handling Section 218 Agreements
Retirement Contributions	Review employee contributions
Computer Systems/Applications	Review COLA calculations in COMPASS
Age and Service Benefits	Review allocation of work (calculating retiree benefits)
Age and Service Benefits	Review processing of PAW participants
Benefit Accounting	Review distributions of member contributions for compliance to IRS guidelines
Special Projects	COMPASS – APERS New Pension Administration System -Review of internal controls and segregations of duties for system controls -Other testing and reviewing as requested during software design -Projects concerns identified prior to and after the “GO LIVE” date in March 2017 -Occasional meeting on design detail specific for APERS operations

Judge Hudson motioned to accept the 2017 Audit Report and Proposed 2018 Audits as presented. He was seconded by Mr. Louthian and the motion passed.

**SUMMARY OF RETIREES FOR JUNE , JULY & AUGUST 2017:**

Ms. Stone remarked that there were an average number of retirees in July and Staff had worked diligently to integrate their old processes with the new system and get everyone retired on time.

**MEDICAL REVIEW BOARD RECOMMENDATIONS:**

The Medical Review Board met at 10:00 a.m. on Tuesday, August 8, 2017 in the APERS Library to discuss two (2) cases: Ms. Tammy K. Rochelle and Ms. Regina Saffell.

- After review and discussion, the Medical Review Board found that Ms. Rochelle was suffering from an illness or injury at the time of her termination in March 2011, which subsequently led to the disability determination.
- After review and discussion, the Medical Review Board found that Ms. Saffell was suffering from an illness or injury at the time of her termination in November 2015, 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, 2017. Ms. Franks motioned to accept the recommendations of the Medical Review. She was seconded by Ms. Bevis. Motion passed.

**FINANCIAL STATEMENTS FOR THE QUARTER ENDING JUNE 30, 2017:**

At the end of Fiscal Year 2017, APERS had a market value of just over \$8 billion, an all-time high. Over the last twelve months, APERS has paid out over \$508 million in benefits to retirees and beneficiaries.

Most of this money stays in Arkansas and is immediately directed back into the local economy.

**OTHER BUSINESS**

**Regulation Update**

Ms. Stone reminded the Trustees that they had approved a number of regulation changes at the May meeting largely to conform to the new computer system. All of these updates had been approved by the Governor and have been properly advertised. There is a Public Hearing on these new regulations scheduled for September 8<sup>th</sup> and then they will be heard by the Retirement Committee on October 12<sup>th</sup>. Lastly, there will be a final review of them by the ALC on October 17<sup>th</sup>.

### COMPASS Update

APERS' new computer system went live on March 20<sup>th</sup> and currently 100% of the Employers are online and using it. There was some initial resistance, but Staff was instrumental in getting the employers trained and up to speed with the new reporting and remitting process.

There has been a soft roll-out of the member portal and participation has been much greater than expected. There will be a more formal roll-out later this fall. Ms. Stone noted that COMPASS was not "bug free" but the developers were identifying and correcting these problems as fast as possible.

### Security Litigators – Personnel Moves

Ms. Stone informed the Board that two of the former employees of Spector, Roseman, Kodroff & Willis, Mr. Mark Willis and Mr. James McGovern, had recently left that securities litigating firm to go work for another: Labaton Sucharow. APERS has initially selected SRKW specifically for these individual's expertise in international litigation and with their departure, SRKW will no longer be pursuing those cases. Ms. Stone recommended that APERS terminate their contract with SRKW and replace them with Labaton Sucharow. There were no fees involved since the only money the security litigators receive is part of the settlement granted by the Court.

Ms. Lea motioned to terminate APERS' contract with SRKW and hire Labaton Sucharow in their place. She was seconded by Mr. Brady and the motion carried.

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

Mr. Wills began by reminding the Board that at the last meeting, he had opined that the Woodruff County Nursing Home appeal would be dismissed by Supreme Court. It has been dismissed, however, recently the lawyer for the Woodruff County employees had filed a new application on behalf of some of the same people, based on the decision of the Pulaski County Judge in the Pulaski County cases. Mr. Wills stated he had responded to his overture by asking him to address two issues: *res judicata* and *collateral estoppel*. He explained what each meant and how they applied to the case. Once he received a response, he would invite a response from Woodruff County before he and Ms. Stone made a Director's Determination. The only material change is the Pulaski County decision where the Judge ruled the words "or" and "and" meant the same when reading for APERS membership status.

As far as that Pulaski County decision, Mr. Wills noted that timely notices of appeal had been filed by all parties, including the nursing homes and the record had already been ordered. APERS will file the record on or before October 24<sup>th</sup> and then start the briefing process for the appeal to the Supreme Court. He remained cautiously optimistic about a favorable ruling.

Mr. Wills also reminded the Trustees that there had been discussion at previous Board Meetings regarding an 8<sup>th</sup> Circuit case that involved two of APERS' securities litigators accused of putting their fee interests ahead of the class member interests. The 8<sup>th</sup> Circuit Court has resolved that and reversed the decision of the original Judge on all findings. No one had appealed, so that is a final decision.

Since the last meeting, APERS has received from the Claims Commission, a claim against the Board of Trustees by Ellis Sloan for \$1.55 million claiming that Gail Stone had misled him into leaving his previous employer with the promise that he would be allowed to take this Board's business onto his new employer. The Trustees are aware, through two presentations from Mr. Sloan and his lawyers, that the Board declined to take action. It also appears that Mr. Sloan has since left his new employer, Katon & Kernodle, for other employment.

Mr. Wills expressed great concern over this matter, because by statute, any claims or issues arising from APERS' retirement code are removed from Claims Commission jurisdiction. He had filed a motion-to-dismiss earlier, pointing out the pertinent statute but was rebuked with the statement that these were "common law" claims against the Board both on *promissory estoppel* and *constructive fraud*. Mr. Wills stated that on September 15<sup>th</sup>, there was a hearing scheduled on his motion to dismiss and if anything other than a complete dismissal from the Claims Commission, he was confident that the Arkansas Attorney General's office would step in on APERS' behalf.

**Regulation 222 – Presented by Ms. Jessica Middleton, APERS General Counsel**

Ms. Middleton directed the Board’s attention to a copy of a new regulation for the Board’s approval. She explained that Ms. Stone, as the Executive Director of APERS, is called to issue a Director’s Determination, usually in conjunction with a benefit determination. Currently, APERS uses an informal process, however the General Assembly has stated that they would prefer a more formal process be followed. In response to A.C.A. §25-15-208 and §25-15-213, Staff has drafted Regulation 222. Ms. Middleton asked for the Board’s approval and permission to promulgate the new rule through the Governor’s office and General Assembly.

Mr. Faris stated that it looked like fairly standard language and motioned for Staff to move forward on it. He was seconded by Ms. Lea and the motion passed.

**Schedule Special Board Meeting**

Under Regulation 105, the Board needs to set a meeting time/date for the Hudlow Administrative Appeal. Mr. Wills commented that this was a straight-forward legal question; there are no facts an issue. Mr. Hudlow was an appointed City Treasurer for City of Russellville and the City of Rogers, however Mr. Hudlow claims that his time in those positions entitles him to enhanced service credit as an elected-official. APERS has never awarded elected-official enhanced credit to appointed position in the past. Mr. Wills cautioned the Board that in his letter, Mr. Hudlow will claim that APERS initially granted him enhanced service credit, but that was based solely on an affidavit which Mr. Hudlow submitted, which turned out to be false.

This has been an on-going case and Mr. Wills hoped that the Board could find a sometime in late September to hear this case. After some discussion, Friday, September 29<sup>th</sup> at 9:00 a.m. was selected for the Hudlow hearing. Mr. Faris commented that if other issues came up and needed to be included on the agenda for that meeting, he was open to additional topics and other Trustees concurred.

Ms. Lea motions for the Board to convene again on Friday, September 29, 2017 for a special hearing. She was seconded by Mr. Faris and the motion carried. Ms. Stone explained that anyone who could not be physically present was welcome to teleconference into the meeting.

There was a discussion by several members regarding the feeling of “rushing” through the meetings to get everything accomplished. Mr. Faris made a case for breaking off into committees to be able to delve deeper into some of the issues, while others wanted to full board to be in attendance for all decisions. Judge Hudson requested that all information that would be voted upon be sent to all Trustees several days in advance, so they had an opportunity to study them prior to the meeting. Ms. Lea commented that it sounded like Judge Hudson had something in mind and suggested he write a draft of his recommendations and let the entire Board vote on it.

Judge Hudson also gave high praise to his recent attending of “Callan College” and said that he was told Callan would come to Little Rock and hold a special, all-day educational event just for the APERS Board members, if requested. He encouraged Staff to coordinate such an event and strongly urged other Trustees to attend and elevate their skill sets.

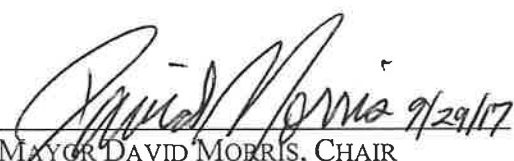
**NEXT QUARTERLY BOARD MEETING:**

The next quarterly meeting of the APERS Board of Trustees is scheduled for Wednesday, November 15, 2017 at 9:00 a.m.

Annual Trustee Educational Seminar is scheduled for Tuesday, October 24, 2017 (all day) at the Capital Hotel, Little Rock.

**ADJOURNMENT:**

There being no further business, the meeting was adjourned.

  
MAYOR DAVID MORRIS, CHAIR

  
MS. GAIL STONE, EXECUTIVE DIRECTOR