

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

**Monday February 17, 2014
11:15 a.m.
1400 West Third Street
Little Rock, AR 72201**

ATTENDEES

Board Members Present

Dr. Richard Abernathy, Chair
Jeff Stubblefield, Vice Chair
Lloyd Black
Kathy Clayton
Hazel Coleman
Kelly Davis
Wes Goodner, voting designee for Honorable
Charles Robinson
Peggy Gram, designee for Honorable Charlie
Daniels*
Dr. Tom Kimbrell*
Danny Knight
Bobby Lester
Robin Nichols
Deborah Thompson
Janet Watson

Board Members Absent:

Candace A. Franks

Reporters Present

Mike Wickline, Arkansas Democrat Gazette

ATRS Staff Present

George Hopkins, Executive Director
Shane Benbrook, Internal Audit/Risk Mgmt.
Dena Dixson, Internal Audit/Risk Mgmt.
Mitzi Ferguson, Chief Fiscal Officer
Laura Gilson, General Counsel
Rod Graves, Manager, Investment Dept.
Wayne Greathouse, Assoc. Director
Manju, Dir. Data Processing
Linden Maurer, Legal Assistant
Jerry Meyer, Manager, Real Assets
Tammy Martin, Retirement Section Manager
Tammy Porter, Administrative Assistant
Michael Ray, Dir. Member Services
Gaye Swaim, Operations Administrator
Leslie Ward, Manager, Private Equity
Brenda West, Internal Audit/Risk Mgmt.

Consultants Present

Michael Bacine, Franklin Park
P.J. Kelly, Hewitt EnnisKnupp
Katie Rizzo, Hewitt EnnisKnupp
Chae Hong, Hewitt EnnisKnupp
Dan Kim, Hewitt EnnisKnupp

* *via teleconference*

- I. **Call to Order/Roll Call.** Dr. Abernathy, Chair, called the Board of Trustees meeting to order at 11:35 a.m. Ms. Franks was absent.
- II. **Motion to Excuse Absences.**

Mr. Stubblefield moved to excuse Ms. Franks from the February 17, 2014 Board of Trustees meeting. Mr. Knight seconded the motion, and the Board unanimously approved the motion.

III. Adoption of Agenda.

Ms. Nichols moved for adoption of the Agenda. Mr. Goodner 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 December 2, 2013.

Mr. Lester moved for approval of the Minutes of the Board of Trustees meeting of December 2, 2013. Ms. Coleman seconded the motion, and the Board unanimously approved the motion.

B. Minutes of January 8, 2014

Ms. Coleman moved for approval of the Minutes of the Board of Trustees meeting of January 8, 2014. Mr. Lester seconded the motion, and the Board unanimously approved the motion

VI. Staff Empowerment. Mr. Hopkins explained the staff empowerment resolutions. Each year the ATRS Board authorizes ATRS staff to transact certain business to set the specific powers of the executive director and to appoint the executive director to manage and delegate operational duties to the limited liability companies that ATRS uses to manage its investments and Arkansas related property.

A. Authority to Transact Business (Resolution 2014-01).

Ms. Nichols moved to adopt Resolution 2014-01, granting authority George Hopkins, Executive Director; Gail Bolden, Deputy Director; and G. Wayne Greathouse, Associate Director of Investments authority to transact investment business on behalf of the ATRS Board of Trustees. Ms. Clayton seconded the motion, and the Board unanimously adopted the resolution.

B. Specific Powers of Executive Director (Resolution 2014-02).

Mr. Lester moved to adopt Resolution 2014-02, authorizing and empowering the Executive Director's actions on behalf of the ATRS Board of Trustees. Mr. Stubblefield seconded the motion, and the Board unanimously adopted the resolution.

C. Appointment of ATRS as Manager of LLC's (Resolution 2014-03).

Mr. Black moved to adopt Resolution 2014-03, authorizing the ATRS Executive Director or his delegates to transact business and perform all duties relating to the management of ATRS LLC's. Mr. Goodner seconded the motion, and the Board unanimously adopted the resolution.

- VII. Authority to Reimburse Trustee Expenses for 2014 (Resolution 2014-04).** Mr. Hopkins explained the trustee reimbursement resolution. Every year, a resolution is adopted by the Board to reimburse Trustees for expenses such as long distance telephone calls, postage, and out of pocket expense associated with employing substitute personnel while performing official Board duties.

Ms. Coleman moved to adopt Resolution 2014-04, authorizing ATRS to reimburse ATRS Trustees for miscellaneous expenses and losses in salary resulting from Board of Trustees meeting attendance or other official Board duties. Mr. Stubblefield seconded the motion, and the Board unanimously adopted the resolution.

- VIII. Authorization for 2014 Board Travel and Expense Reimbursement (Resolution 2014-05).** Mr. Hopkins explained the Board travel and expense reimbursement resolution. Every year, a resolution is adopted by the Board to reimburse Trustees for travel expenses incurred for performing official Board duties during the calendar year.

Ms. Coleman moved to adopt Resolution 2014-05, authorizing ATRS to reimburse ATRS Trustees for expenses used in traveling for official Board duties. Mr. Lester seconded the motion. Motion carried.

- IX. 2014-2015 Employer Contribution Rate (Resolution 2014-06).** Mr. Hopkins explained the 2014-2015 employer contribution rate resolution. Every year, a resolution is adopted by the Board to set the employer contribution rate prospectively for each fiscal year. The rate is based upon actuarial valuation and legislative restrictions.

Ms. Nichols moved to adopt Resolution 2014-06, establishing the employer contribution rate at the statutory maximum 14% for the fiscal year starting July 1, 2014. Ms. Davis seconded the motion, and the Board unanimously adopted the resolution.

- X. **Legislative Audit Report, June 30, 2013 – Official Review of Report.** Mr. Hopkins presented the Audit Report from Legislative Audit. For the 5th year in a row, ATRS has received a NO FINDINGS audit report. ATRS Staff works hard every day to address any weaknesses and mistakes to prevent any recurrences in the future.
- XI. **Actuarial Valuations, June 30, 2013.** Mr. Hopkins presented the Annual reports prepared by the Actuaries concerning the valuation of liabilities to "active and Inactive" members long with the valuation of liabilities for annuities being paid to current retirees and current beneficiaries.
- A. **Active & Inactive Members.** This report reflects the liabilities owed by ATRS to active member and inactive members.
- B. **Retirees & Beneficiaries.** This report reflects the liabilities to ATRS retirees, beneficiaries, survivors, and incapacitated children.
- Mr. Stubblefield moved to accept the Actuarial Valuations as of June 30, 2014. Ms. Clayton seconded the motion, and the Board unanimously approved the motion.**
- XII. **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 were no interest waived for this reporting period.
- XIII. **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 \$4,718.64 in employer interest and penalties.
- XIV. **Report on Manifest Injustice Claims.** Mr. Hopkins presented the report from the Manifest Injustice Committee. The Committee held its first meeting on January 27, 2014. The Committee reviewed 40 cases, the majority of which were the lump sum death benefit beneficiaries of the Act 793 and Act 808 members.

- XV. **Member Appeal. Rita Grumbles Administrative Appeal.** Ms. Gilson presented the administrative appeal for member Rita Grumbles to the Board regarding recalculation of his disability benefits. Ms. Grumbles did not appear for the appeal. The Hearing Officer provided a proposed decision for the Board. The Board may affirm the decision of the Hearing Officer, reject the decision of the Hearing Officer and impose its own decision, modify the order, make its own findings, or remand the matter back to the Hearing Officer for additional consideration of matters the Board deems appropriate.

Mr. Lester moved to affirm the Hearing Officer's decision in the matter of Rita Grumbles' administrative appeal. Mr. Knight seconded the motion, and the Board unanimously approved the motion.

- XVI. **Audit Committee Report.** Ms. Nichols, Chair, gave a report on the Audit Committee meeting.

A. **Internal Audit Report: Benefit Calculation and Disbursements:** Ms. Brenda West reported that an Audit on Benefit Calculation and Disbursement was conducted. This Audit was to ensure benefits were accurately calculated and properly disbursed according to written policies, procedures and regulations. Internal Audit tested 134 benefits calculations on members who retired or entered T-Drop during July through September 2013. The test included age and service, disability and survivor benefits, T-Drop deposits for members entering T-Drop, and T-Drop annuities, lump-sums and CBA benefits. Audit objectives were achieved and no audit findings were identified. No recommendations were issued and no action was required of management. Member calculations were accurately calculated and properly disbursed in accordance with written policies, procedures and regulations. Good written policies and procedures are in place and it was a very good audit.

B. **Internal Audit Report: Refunds.** Ms. Brenda West reported that an Audit on Refunds was conducted. This Audit was to ensure refunds were accurately stated and that the System was in compliance with laws, policies, and procedures. Fifty (50) out of 1009 refunds were tested. They were correctly calculated and in compliance. However, a few issues were noted. First, written policies and procedures did not exist. This has been discussed previously with the group. The System has hired an extra help person that is currently working on writing policies and procedures. When he finishes one department, he moves to another department. The other issue was that the Payroll Department is not accruing a liability for state withholding taxes each month on refunds paid; therefore, expenses are understated until taxes are paid. State withholdings on Refunds totally \$35,434 was not accrued as of

June 30, 2013. The Agency also did not accrue the state withholding taxes totally \$1,722,392 on other payments made to members as of June 30, 2013. This has been discussed with staff and they will start accruing state taxes monthly in all required accounts. It is the opinion of the Internal Audit Department that the internal controls over refunds are good and refunds represents an accurate amount of what the System has paid members.

Shane Benbrook passed out a response from the System to the findings of the Internal Audit Report. The Handout is attached hereto as "Exhibit No. 1" and made part of the official record.

XVII. **Investment Committee Report.** Ms. Nichols, Chair, gave a report on the Investment Committee meeting.

A. Investment Update and Arkansas Related Update. Mr. Hopkins gave an update on Arkansas real estate and investments.

1. **Woodland Heights Update.** Mr. Hopkins reported that the actual occupancy has increased to 78% pre-leased and 73% occupied. The news on the property is increasingly positive and the initiatives by the management team at RPM are beginning to show good results.
2. **720 W. Third.** Mr. Hopkins reported that on January 27, 2014, ATRS successfully sold and closed on the property located at 720 W. Third. The property sold for \$850,000, which was \$10,000 more than the appraised value. Selling smaller direct investments, like this one, will allow better focus on fund managers.
3. **Property Managers Retained to List Vacant Property.** Mr. Hopkins reported that the Board previously authorized Staff to offer several properties for sale or lease with an option to purchase at the appraised value or higher. He said that the Board also authorized Staff to utilize the existing property managers to represent ATRS for the vacant properties located at 720 West Third and 1512 West Third, and to utilize property brokers to list vacant land located in Chenal Valley and a vacant parcel in North Little Rock at appraised value or higher. As with the improved properties, any sale less than the appraised value will be subject to Board approval. The list of properties and corresponding representatives are below.

Buildings:

720 West Third – Colliers (This property was sold and closed on January 27, 2014.)

1512 West Third – Irwin Saviers Ballard.

Raw Land:

Chenal Valley (52.72 acres) – Irwin Saviers Ballard.

North Little Rock (3 acres near old Memorial Hospital) – Irwin Saviers Ballard

4. **List of Recent Closing/Amendments with Fund Managers.** Mr. Hopkins gave the Board an update for the investments approved at the December 2, 2013 Board meeting.

- a. **Franklin Park.**

1. **International 2014.** Mr. Hopkins reported that the full commitment of \$25 Million Dollars was accepted and closed.
2. **Venture 2014.** Mr. Hopkins reported that the full commitment of \$25 Million Dollars was accepted and closed.
3. **Co-Investment.** Mr. Hopkins reported that the full commitment of \$25 Million Dollars is in process.
4. **Amendment to Franklin Park Venture 2013 to Allow Recallable Distributions.** Mr. Hopkins reported that Franklin Park requested an amended to the Franklin Park Venture 2013 contract to allow for recallable distributions from the fund. Mr. Hopkins informed the Board that this was standard in the industry and needed to ensure the fund manager had enough capital available to meet all fund obligations and investment needs. Mr. Hopkins reported that this was an operational amendment and that Committee or Board action was not necessary.

- b. **Atlas Capital Resources II, L. P.** Mr. Hopkins reported that ATRS made an initial commitment of up to \$25 Million Dollars, but due to the capacity in the fund, it only closed on \$15 Million Dollars.

5. Fund of Opportunities. Mr. Hopkins reported that due to the growth of the ATRS trust fund, the ability of ATRS to take advantage of the often enhanced returns from smaller more specialized opportunities diminish due to the size of the deal in comparison to the size of the ATRS trust fund. He said that opportunities which come from Arkansas based firms due to small size can make it hard for the consultants to recommend. Hewitt EnnisKnupp and ATRS Staff are working on the due diligence process to find a potential manager for this fund of opportunities and establish guidelines for the investment types. The fund is expected to have a targeted return of 8% to 15% and have a mixture of private equity, real estate, loans, equity, and potentially bonds. Mr. Hopkins said that several Arkansas based firms have expressed interest in managing this fund and due diligence is being performed. He said that if an Arkansas manager is located, it should also enhance the availability of deal flow from Arkansas. The due diligence process is still underway and may be ready at the next meeting for Investment Committee and ATRS Board consideration. Mr. Stubblefield said he would like to see this matter expedited.

B. General Investment Consultant Update – Hewitt EnnisKnupp.

- 1. Portfolio Performance Update for the Quarter Ended December 31, 2013.** Mr. P. J. Kelly and Ms. Katie Rizzo both of Hewitt EnnisKnupp (HEK) presented the portfolio performance update for the fourth quarter ending December 31, 2013. Ms. Rizzo reported that the quarter ended with \$14.1Billion Dollars total market value. The total fund had a return of 6.0% for the quarter ending December 31, 2013, outperforming its benchmark of 5.9%. ATRS ranked in the 6% percentile of similar sized pension plans across the U. S.
- 2. Update to Investment Policy Statement.** Ms. Katie Rizzo of Hewitt EnnisKnupp (HEK) presented a recommendation for an update to the current Investment Policy Statement. Ms. Rizzo reported that a review of the Investment Policy Statement showed the need to clarify/align a few items they wanted to tweak and accurately define comments on the table such as the name or type of existing benchmarks for certain asset classes, as well as a few other minor edits. The proposed changes will help to align the Investment Policy Statement's reporting benchmark names with those utilized on the monthly and quarterly reports.

Ms. Nichols moved to approve changes and updates to the Investment Policy Statement. Mr. Black seconded the motion, and the Board unanimously approved the motion.

3. **BlackRock Core Plus Separate Account Change in Structure.** Mr. P.J. Kelly reported that as of December 31, 2013, ATRS had approximately \$330 Million Dollars invested in an actively managed BlackRock Fixed Income Core Plus Account. ATRS asked HEK to inquire about alternative vehicle options with BlackRock. HEK and BlackRock had discussions about creating a collective trust fund that would meet ATRS needs, taking both strategy and cost into consideration. HEK concluded that moving to a collective trust vehicle is the most appropriate solution for ATRS portfolio and ATRS Staff. Currently BlackRock does not offer a fund with an investment mandate equivalent to the separate account strategy ATRS currently holds. However, Mr. Kelly reported that BlackRock offered to create a collective trust fund with the same investment strategy at effectively the same cost.

Mr. Kelly reported that the new trust fund would be managed by the same portfolio manager with the same investment process. Additionally, BlackRock is offering ATRS a very attractive fee structure for the new fund, making the switch economically neutral for ATRS and potentially economically favorable. BlackRock has offered ATRS a lower investment management fee to offset the additional operational costs.

HEK recommends ATRS work with BlackRock to transfer their assets from the current core plus separate account to the newly created core plus collective trust fund. Provided the fund will need to be created, which can take up to six (6) weeks, HEK recommend ATRS initiate the transfer as soon as it is feasible.

a. Resolution 2014-07

Ms. Nichols moved to adopt Resolution 2014-07, Staff work with the Board to transfer assets from the current core plus separate account to the newly created core plus collective trust fund. Mr. Black seconded the motion, and the Board unanimously approved the motion.

4. **Recommendation for Redeployment of Assets from Two (2) Terminated Western Accounts.** On December 2, 2013, the ATRS Board approved termination of two (2) fixed income funds. As of

December 31, 2013, ATRS had a total of approximately \$748 Million Dollars invested with the two (2) terminated Western Accounts which represented a significant portion of the ATRS trust fund's fixed income portfolio. HEK recommends allocation of the assets to \$300 Million Dollars each to Reams Core Plus Bond Fund and Wellington Global Total Return II Fund, \$100 Million Dollars to existing SSgA Aggregate Bond Index Fund, and remainder of the assets to the BlackRock Core Plus Fund.

- a. **Recommendation to Initially Fund up to \$300 Million Dollars in Wellington Management Company, L. P., Global Total Return II Fund.** Mr. P. J. Kelly of HEK gave the background history on Wellington. ATRS is familiar with Wellington Management Company from its global equity management for the System. Wellington has managed a global equity strategy for ATRS since 2009, and as of September 30, 2013, has a strong annual return of 21.3% since inception. Wellington Management Company, L. P., Global Total Return II Fund has an absolute return strategy that strives to provide consistent, positive returns through diversified alpha sources. Wellington's team is comprised of a group of senior investment professionals whom HEK finds talented and stable. Wellington's Global Total Return I Fund has a very favorable track record and HEK expects similar long-term success from Global Total Return II Fund.

HEK recommends allocation of \$300 Million Dollars of the Western Assets to Wellington Global Total Return II Fund.

1. Resolution 2014-08

Ms. Nichols *moved to adopt* Resolution 2014-08, Allocation of \$300 Million Dollars of the Western Assets to Wellington Management Company, L. P., Global Total Return II Fund. Mr. Black *seconded the motion*, and the Board *unanimously approved the motion*.

- b. **Recommendation to initially Fund up to \$300 Million Dollars in Reams Core Plus Bond Fund LLC.** Mr. P. J. Kelly of HEK gave the background history on Reams. Reams is a specialty firm based in Indiana that is focused exclusively on fixed income. Reams has an experienced, stable and talented management team that expects to thrive during periods of

elevated marked volatility. The opportunity set for investments by this fund includes municipal bonds, high yield bonds, and securitized assets. The strategy has strong performance over both short and long term periods and has produced a return of 7.2% since inception compared to its benchmark of 5.9%.

HEK recommends allocation of \$300 Million Dollars of the Western Assets to Reams Core Plus Bond Fund, LLC.

1. Resolution 2014-09

Ms. Nichols *moved to adopt Resolution 2014-09, Allocation of \$300 Million Dollars of the Western Assets to Reams Core Plus Bond Fund, LLC. Black seconded the motion, and the Board unanimously approved the motion.*

- c. Notice of Planned Addition of approximately \$50 Million Dollars to the Existing BlackRock Core Plus Strategy Fund or, if approved, the new BlackRock Structure in Item "C" above. Mr. P. J. Kelly of HEK reported that this is part of the reallocation strategy and not a new manager recommendation and is being provided as notice only. No board action is required.
 - d. Notice of Planned Addition of approximately \$100 Million Dollars to existing SSgA U.S. Aggregate Bond Index Fund. Mr. P. J. Kelly of HEK reported that this is part of the reallocation strategy and not a new manager recommendation and is being provided as notice only.
5. **New Global Equity Manager Recommendations.** Mr. P.J. Kelly of HEK reported that recent reductions in the number of active managers employed by ATRS in the global equity asset class, due to the Board approved termination of the Wellington Opportunistic fund and the withdrawal of Bedlam, have created a need to add more active management in the global equity asset allocation. The goal of active management is to beat, net of fees, passive index strategies through superior investment strategies to help ATRS better meet its overall investment assumptions. An adequate level of active risk is a required component of the prudent investor rule.

HEK is prepared to make recommendations to hire open end fund managers in the public markets asset class, and to initially fund each investment with up to \$350 Million Dollars. Many private equity or real

asset investments are of the closed end fund variety and require specific amounts that will be locked up for a period of time making them illiquid investments. The distinction is that open end funds, particularly those in the public markets asset class, are more fluid by design and can be used by ATRS for liquidity and rebalancing needs. The initial funding amount of up to \$350 Million Dollars each represents the amount to be funded at this time based on current asset allocation percentages. If approved, the actual fund amounts will vary over time with funds in excess of the initial allocation added at times and at other times funds would be withdrawn taking the funding level lower than \$350 Million Dollars based on market returns, liquidity needs, and HEK recommended rebalancing from time to time.

- a. **Recommendation to Initially Fund up to \$350 Million Dollars in Grantham, Mayo, Van Otterloo & Co., LLC. (GMO), Global All Country Equity Allocation.** The GMO Global All Country Equity Allocation is based in Boston and solely focused on institutional asset management. The strategy relies primarily on the team's seven-year asset class return forecasts to determine a target asset allocation. The target allocation is implemented using quantitative or computer driven stock selection. The opportunity set for investments by this fund include various GMO funds or products.

HEK and ATRS Staff both recommend an initial investment of up to \$350 Million Dollars in the GMO Global All Country Equity Allocation.

1. Resolution 2014-10

Ms. Nichols *moved to adopt* Resolution 2014-10, to fund up to \$350 Million Dollars in Grantham, Mayo, Van Otterloo & Co., LLC. (GMO), Global All Country Equity Allocation. Mr. Black *seconded the motion*, and the Board *unanimously approved the motion*

- b. **Recommendation to Initially Fund up to \$350 Million Dollars in Harris Associates L.P., Global Equity.** Mr. P. J. Kelly of HEK reported that Harris Associates is a Chicago based firm and this strategy uses a value based approach that results in a concentrated portfolio of 30 to 60 stocks. The strategy is disciplined with a focus on companies that

have a strong franchise value and company management that exhibits good capital allocation.

HEK and ATRS Staff both recommend an initial investment of up to \$350 Million Dollars in Harris Associates L.P., Global Equity.

1. Resolution 2014-11

Ms. Nichols *moved to adopt* Resolution 2014-11, to fund up to \$350 Million Dollars in Harris Associates L.P., Global Equity. Ms. Davis *seconded the motion*, and the Board *unanimously approved the motion*.

C. Real Assets Investment Consultant Update.

1. Portfolio Performance Update for Quarter Ended September 30, 2013.

Mr. Chae Hong of HEK presented the Real Assets Portfolio Performance Update. NCREIF's NPI registered at 2.6% and NFI-ODCE (net) returned 3.4%, a decrease of 30 bps and 20 bps from second quarter results. The NCREIF Timberland Index returned 1.0% for the quarter and is up 9.7% for the trailing one year as of September 30, 2013, an increase of 10 bps and 30 bps over second quarter results. This is the highest one year return since Q3-2008. The NCREIF Farmland Index gained 2.9% for the third quarter of 2013 and 21.2% for the trailing one year, an increase of 90 bps and 120 bps over second quarter results. ATRS real assets portfolio is at 12.9% and progressing towards its target allocation. Overall, the portfolio is in compliance with its Statement of Investment Policy. ATRS underperformed its real assets benchmark by 30 basis points for the third quarter. ATRS Real Estate portfolio underperformed the quarter by 50 bps, Agriculture underperformed by 350 bps, and Timberland outperformed by 60 bps. The net return for ATRS' real estate investments is expected to meet or exceed the net NCREIF Fund Index Open-end Diversified Core Equity Index ("NFI-ODCE") over a five (5) year rolling period. ATRS' core portfolio has been a significant driver of performance. Non-core performance is expected to have a more meaningful impact as new funds move out of the J-Curve and the non-core market segment's recovery accelerates.

- 2. Recommendation to Commit up to \$50 Million Dollars in First Reserve Energy Infrastructure II, L.P.** Mr. Dan Kim of HEK presented the recommendation for First Reserve Energy Infrastructure Fund II, L.P. This fund will invest in an energy focused core plus strategy. These

infrastructure asset investments are located in North America and Europe. Potential investments include power plants, pipelines, storage, electrical transmission and production equipment/services as well as renewable power such as wind and solar. Throughout its 30-year history, First Reserve has developed a track record of investing exclusively in the energy industry, utilizing its specialized industry knowledge as a competitive advantage.

HEK and ATRS Staff both recommend an investment of up to \$50 Million Dollars in First Reserve Energy Infrastructure Fund II L.P.

a. Resolution 2014-12

Ms. Nichols *moved to adopt* Resolution 2012-12, to commit up to \$50 Million Dollars in First Reserve Energy Infrastructure II, L.P. Ms. Clayton *seconded the motion*, and the Board *unanimously approved the motion*

- 3. Recommendation to Commit up to \$50 Million Dollars in Antin Infrastructure Partners II, L.P.** Mr. Dan Kim of HEK presented that Antin Infrastructure Partners II recommendation. This is a diversified core infrastructure fund investing in Western Europe. The fund is aiming for a 5% annual cash return and 15% total annual IRR from infrastructure assets. The diversification is among communications, energy, environment and transportation sectors. No more than 50% will be invested in any single sector.

HEK and ATRS Staff both recommend an investment of up to \$50 Million Dollars in Antin Infrastructure Partners II L.P.

a. Resolution 2014-13

Ms. Nichols *moved to adopt* Resolution 2014-13, to commit up to \$50 Million Dollars in Antin Infrastructure Partners II, L. P. Ms. Clayton *seconded the motion*, and the Board *unanimously approved the motion*.

D. Private Equity Investment Consultant Update – Franklin Park.

1. Portfolio Review for the Quarter ended September 30, 2013.

Michael Bacine of Franklin Park presented the Portfolio Review for the Quarter ended September 30, 2013. Net IRR for the aggregate portfolio since inception was 9.4%. ATRS has committed approximately \$3.0 Billion Dollars to 41 primary funds, 11 fund-of-

funds, and 1 co-investment fund through September 30, 2013. ATRS' portfolio has outperformed the Dow Jones U. S. Total Stock Market Index equivalent ("PME") by 390 basis points since inception.

2. **Recommendation to Commit up to \$25 Million Dollars in Castlelake III, L.P. with Imminent Need.** Castlelake was formerly known as TPG Capital, and in 2012 ATRS invested in the General Partner's fund known as TPG Credit Strategies II (TCS II). TCS II is performing very well with an IRR of 24.1% as of September 30, 2013. Based in Minneapolis, this fund was founded as an affiliate of TPG Capital by Rory O'Neill who previously led Cargill's global credit and special situations business. The fund is targeting commitments of \$1 Billion Dollars and will pursue an opportunistic distressed investment strategy primarily in the U.S. and Europe. Over long periods of time, distressed strategies are expected to generate slightly lower returns than equity oriented corporate finance strategies such as "buyout" or "turnaround" types. At the same time though, distressed strategies are relatively less risky than other types and often perform well when equity strategies are weak. This also helps keep ATRS better diversified across all asset classes.

Although some of the fund may be invested in secured corporate debt, the majority of the fund will be focused on acquiring distressed assets primarily in the aviation space, mortgage and consumer loan portfolios and various financial assets. When distressed corporate debt prices are stable with low default rates, the fund will target distressed asset investments. If default rates climb rapidly and corporate debt prices are volatile, the fund will shift towards corporate debt investments. Due to the fact that this investment will need to close by the end of this month and the next scheduled ALC meeting is March 21, 2014, Imminent Need is requested.

Franklin Park and ATRS Staff both recommend an investment of up to \$25 Million Dollars in Castlelake III, L.P. using Imminent Need.

a. Resolution 2014-14

Ms. Nichols moved to adopt Resolution 2014-14, to commit up to \$25 Million Dollars in Castlelake III, L.P. with imminent need. Ms. Davis seconded the motion, and the Board unanimously approved the motion.

3. **Recommendation to Commit up to \$25 Million Dollars in Sycamore Partners II, L.P. with Imminent Need, subject to Due**

Diligence. The ATRS Board authorized an investment in the first Sycamore fund back in 2012. However, due to legal issues regarding Sycamore's information disclosure policies at that time, the deal was not closed. ATRS believes Sycamore is now committed to disclosure policies that are acceptable to ATRS and other public pension plan investors. The heart of Sycamore's investment team has been together for a number of years, first at Golden Gate Capital and then with the first Sycamore fund. The insight and deep understanding of retail makes the team cutting edge and exceptional in name brand/store retail. They have a stellar track record for the investments that they have directly managed to date.

The fund was created to acquire underperforming U.S. companies primarily in the retail and restaurant sectors. Companies such as Express, Apogee, J. Jill, Macaroni Grill, On the Border, Zales, Eddie Bauer and Talbot's are among the companies that have been turned around by the principals of Sycamore. Franklin Park and ATRS Staff agree that this firm has the ability to source great deals and has excellent contacts in the industries which it targets in order to acquire companies at attractive prices. This investment will close before the next scheduled ALC meeting on March 21, 2014, therefore Imminent Need is requested.

Franklin Park and ATRS Staff both recommend an investment of up to \$25 Million Dollars in Sycamore Partners II, L.P. with Imminent Need. Virtually all due diligence has been completed and is expected to be completed with a "green light"; however, a few items need to be checked and double checked prior to all due diligence being complete. Therefore this recommendation is made subject to final due diligence, if completed with a positive recommendation from Franklin Park. If approved by the Investment Committee and ATRS Board, no further action will be necessary at the ATRS Board level.

a. Resolution 2014-15

Ms. Nichols moved to adopt Resolution 2014-15 to commit up to \$25 Million Dollars in Sycamore Partners II, L.P. with imminent need, subject to due diligence. Mr. Black seconded the motion, and the Committee unanimously approved the motion.

- 4. Recommendation for True-Up Commitment of an Additional \$5 Million Dollars to Court Square Partners III, L.P. with Imminent Need.** In April 2012, the ATRS Board authorized a commitment of \$35

Million Dollars to Court Square III, L.P., a \$3.25 Billion Dollar buyout fund focused on mature middle market companies in the U.S. In July of that year, ATRS actually closed on a \$40 million dollar commitment to the fund. At this time, the fund is performing on plan with some expected write-ups of investments during the first half of this year.

Both Franklin Park and ATRS Staff recommend an authorization of an additional \$5 Million Dollars to the fund to true-up the amount authorized to the amount committed based on the fund's performance, the interest from secondary buyers who think the position is worth more than current value, and the belief that the General Partner is positioned to produce solid returns as the remaining capital is drawn. Since closing on this investment has taken place, Imminent Need for ALC review of the additional authorization is requested.

a. Resolution 2014-16

Ms. Nichols *moved to adopt* Resolution 2014-16 a true-up commitment of an additional \$5 Million Dollars to Court Square Partners III., L.P. with imminent need. Ms. Davis *seconded the motion*, and the Committee *unanimously approved the motion*.

XVIII. 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. The Committee discussed the issue of "outsourcing". The Committee asked that Staff contact other school systems and see what they are currently outsourcing. Mr. Hopkins told the Committee Staff would have something presented at the next Board meeting.

2. General Discussion of Definition of "Salary" at Request of Trustee. Prior to the 2013 Legislative Session, the definition of salary was "the remuneration paid to a member employed in a position covered by the Arkansas Teacher Retirement System on which the employer withholds federal income tax." Mr. Hopkins explained that Act 521 of 2013 gave the Board broad latitude to consider future changes needed for the definition of salary by developing rules. One

example is Rule 7-1 which will be considered for recommendation to the Board later on this agenda on early retirement incentive plans.

Mr. Hopkins explained to the Committee that Act 521 was designed to allow the ATRS Board flexibility to adjust the definition of salary over time to better reflect the reasonable salary of members to ensure fairness and completeness. No action was taken by the Committee at this time.

B. Potential Legislation.

- 1. Potential Disability Benefits Law.** Mr. Hopkins explained that at the request of the Operations Committee and ATRS Board, Staff evaluated the law and the current rule on disability retirement and determined that a law change would be necessary to implement any change.

ATRS Staff presented the Committee with a list of "talking points" to give the Board a view of potential legislation that would give the Board the ability to set thresholds and potential reviews to determine if a member remains disabled. The law change would require the disability retiree to submit a copy of his or her federal tax returns, including W2s and 1099s to ATRS to show that the member has no or limited earned income. If the ATRS Board is interested in moving forward on this issue, then ATRS staff proposes a law be drafted to authorize a certification form that must be completed and returned with the required documents if disability benefits are to continue to be paid by ATRS.

The Committee concurred with the direction of the legislation, and if the Board agrees, ATRS Staff will draft law for consideration by the Committee for the 2015 legislative package. Mr. Hopkins informed the Committee a draft of the proposed legislation would be presented at the next Board meeting.

- 2. Private School Certification.** Mr. Hopkins told the Committee that the ATRS law concerning the purchase of private school service credit requires that the private school or agency *"Has positions recognized by the Department of Education for the issuance of teaching licenses; or Is recognized as a private educationally related entity by resolution adopted by the Board of Trustees of the Arkansas Teacher Retirement System."*

The Department of Education no longer tracks private schools and has no position on the issuance of teaching licenses for private schools, especially out of state private schools. Under federal law, a person

with certified teaching service is eligible to purchase up to 15 years of private school service. All other service is limited to only 5 years. Over the years, the Department of Education has certified private school service, both in and out of state.

The Department has determined that it no longer has a reasonable basis to certify private schools, both in and out of state, and the work performed by a person at that school as certified teaching service.

ATRS Staff proposes to the Committee to remove the language in the law concerning the Department of Education, and to replace it with language requiring the ATRS staff to make the determination. ATRS Staff regularly makes determinations about related items and can do so without burdening the Department of Education and can do so in full compliance with federal law standards. Mr. Hopkins explained that if authorized, ATRS would develop a questionnaire for the member and private school employer to use in the determination.

The Committee concurred with the direction of the legislation and if the Board agrees, ATRS Staff will begin drafting draft changes to the private school service law for consideration by the Committee for the 2015 legislative package. Mr. Hopkins informed the Committee that proposed legislation would be presented at the next board meeting.

C. Final Approval of Policy Change to Rule 7-1 Calculation of Final Average Salary. Rule 7-1 was presented for the 3rd approval by the Committee and ATRS Board. This will be the final approval if accepted by the Committee and ATRS Board. Mr. Hopkins stated that as a reminder that this rule is narrowly tailored to only remove payments made as early retirement incentives in a group offering in return for separation of employment/retirement from calculation in a member's final average salary for benefits, or in the highest salary for survivor benefits. The rule continues to expressly allow general bonuses, payment of sick leave, and other regular payments to members usually given at the end of their careers. This rule also does not affect settlements, buyout agreements, or other payments won through litigation. Often these agreements are reached to resolve a claim of wrongful termination or similar resolution to a contract dispute.

The rule was adopted by the Board on December 2, 2013, under emergency rule making authority. The emergency rule expires April 7, 2014. The rule was immediately started through the regular adoption

process in order to have the rule adopted before the emergency rule expired.

The Joint Committee on Public Retirement met on January 22, 2014, and reviewed Rule 7-1. The rule was also reviewed by the Arkansas Legislative Council Administrative Rules and Regulations Committee on February 5, 2014. There were no public comments made on the rule. If the Committee recommends and the Board moves to adopt the rule in the February 17, 2014, meetings, then the rule will become effective on March 18, 2014, before the expiration of the emergency rule.

ATRS Staff recommends that the Committee recommend adoption of the Resolution to the Board for final approval of Rule 7-1.

1. Resolution 2014-17

Mr. Lester *moved to adopt* Resolution 2014-17, Final approval of Rule 7-1. Mr. Black *seconded the motion*, and the Board *unanimously approved the motion*.

XIX. Staff Reports.

A. Medical Committee Reports. Michael Ray presented the Medical Committee reports for December 2013 and January 2014. In December 2013, there were 11 applicants and 9 were approved, 1 was denied and one needed more information. In January 2014, there were 10 applicants, 9 were approved, and one needed more information.

Ms. Nichols *moved to approve* the December 2013 and January 2014 Medical Committee reports. Mr. Knigh *seconded the motion*, and the Board *unanimously approved the motion*.

XX. Other Business. None

XXI. Adjourn.

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

Meeting adjourned at 12:10 p.m.

George Hopkins,
Executive Director

Dr. Richard Abernathy, Chair
Board of Trustees

Tammy Porter,
Recorder

Date Approved