

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

**Monday April 14, 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  
Kelly Davis  
Wes Goodner, designee for Honorable  
Charles Robinson  
Peggy Gram, designee for Honorable Charlie  
Daniels  
Danny Knight  
Dr. Tom Kimbrell  
Bobby Lester  
Susannah Marshal, designee for Candace  
Franks  
Robin Nichols  
Deborah Thompson

**Board Members Absent:**

Hazel Coleman  
Janet Watson

**Reporters Present**

Mike Wickline, Arkansas Democrat Gazette

**ATRS Staff Present**

George Hopkins, Executive Director  
Gail Bolden, Deputy Director  
Shane Benbrook, Internal Audit/Risk Mgmt.  
Dena Dixson, Internal Audit/Risk Mgmt.  
Mitzi Ferguson, Chief Financial 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 Porter, Administrative Assistant  
Michael Ray, Dir. Member Services  
Gaye Swaim, Operations Administrator  
Leslie Ward, Manager, Private Equity  
Brenda West, Internal Audit/Risk Mgmt.

**Guest Present**

Donna Morey, ARTA  
Amy Ford, Attorney General's Office  
Katie Rizzo, Hewitt EnnisKnupp  
Chae Hong, Hewitt EnnisKnupp  
Tom Schoenbeck, Hewitt EnnisKnupp  
Jessica Middleton-Kurylu  
Desi Berry, BOSCO, Inc.

- I. **Call to Order/Roll Call.** Dr. Abernathy, Chair, called the Board of Trustees meeting to order at 10:45 a.m. Roll call was taken. Ms. Coleman and Ms. Watson were absent.
  
- II. **Motion to Excuse Absences.**

**Ms. Clayton *moved to excuse Ms. Coleman and Ms. Watson from the April 14, 2014 Board of Trustees meeting. Mr. Stubblefield seconded the motion, and the Board unanimously approved the motion.***

**III. Adoption of Agenda.**

**Mr. Lester *moved for adoption of the Agenda. Mr. Stubblefield 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 February 17, 2014.**

**Ms. Nichols *moved for approval of the Minutes of the Board of Trustees meeting of February 17, 2014. Mr. Stubblefield seconded the motion, and the Board unanimously approved the motion.***

**B. Minutes of March 8, 2014.**

**Mr. Black *moved for approval of the Minutes of the Board of Trustees meeting of March 8, 2014. Ms. Gram seconded the motion, and the Board unanimously approved the motion.***

**VI. Adoption of Interest Rate for T-DROP Accounts for 2014-1015 (June 30, 2015).**

**A. Resolution 2014-24**

**Mr. Knight *moved to adopt Resolution 2014-24, adoption of Interest Rate for T-DROP Accounts for 2014-2015 (June 30, 2015). Ms. Gram seconded the motion, and the Board unanimously adopted the resolution.***

**VII. Adoption of Interest Rate for Post 10 Yr. T-DROP Accounts for 2014-1015 (June 30, 2015).**

**A. Resolution 2014-25**

**Mr. Stubblefield moved to adopt Resolution 2014-25, adoption of Interest Rate for Post 10 Yr. T-DROP Accounts for 2014-2015 (June 30, 2015). Mr. Knight seconded the motion, and the Board unanimously adopted the resolution.**

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

A. Investment Update and Arkansas Related Update.

1. **Woodland Heights Update.** Mr. Hopkins reported that Woodland Heights continued to be the same. Mr. Hopkins told the Board one of the things looked at recently is the fact that most of the independent living centers also have assisted living onsite. Woodland Heights currently does not have assisted living. When that type care is provided, there is a risk of lawsuits and litigations due to medical issues and quality of care. At some point, ATRS may consider leasing or selling the facility to someone who can provide the full activity, which is one of the occupancy issues. People could have a choice of moving into a place then able to move down the hall to assisted living if it becomes necessary versus moving into a place and being told you have to move out to a totally different facility for assisted living.

Mr. Hopkins told the Board there are people who would buy the building and be willing to take on the responsibility of providing more services. Despite mangers best efforts, they add 3 new residents, they lose 2; they add 4 new residents, they lose 3. ATRS have had some casual inquiries asking if it has considered a different approach. ATRS has really looked at the issue of getting increased occupancy. People do not want to leave friends to get extra care, and some people are allowed to come in for some assistance.

From a HEK real asset standpoint, in terms of Woodland Heights, there would be better opportunity to take the money and diversify it into something with a broader, long term opportunity.

The Committee told Mr. Hopkins they would like an exploratory committee formed to look into the options available for selling Woodland Heights and this matter will be revisited at the next Board meeting. Mr. Hopkins told the Board ATRS staff would work with HEK on options regarding this matter.

2. **Victory Building.** Mr. Hopkins reported that occupancy remains steady at 97%. The building remains a popular office building for government agencies and companies with governmental interface.
3. **Property Managers Retained to List Vacant Property.** Mr. Hopkins presented to the Board the recommendation by HEK to explore the potential acquisition of adjoining lots to the current ATRS headquarters. The parking lots are on the market and have been offered to ATRS for \$108,000. The lot would provide ATRS the benefit of maintaining more parking spaces to better serve the members and provide reasonable parking as traffic patterns of active members and retired members who are meeting with ATRS staff increases.

ATRS Staff and HEK recommend to the Board to consider purchase of the lot for the benefit of ATRS and its members.

**a. Resolution 2014-26.**

**Ms. Nichols *moved to adopt* Resolution 2014-26, Approving Staff Authority to Negotiate and Execute the Purchase of Lots 1 & 2, Block 6 Deaf Mute Addition to the City of Little Rock. Mr. Lester *seconded the motion*, and the Board *unanimously approved the motion*.**

**4. List of Recent Closing.**

1. **Castlelake III, LP.** Mr. Hopkins reported that the full commitment of \$25 million dollars was accepted and closed.
2. **Sycamore Partners II, LP.** Mr. Hopkins reported that the full commitment of \$25 million dollars was accepted and closed.

**B. General Investment Consultant Update – Hewitt EnnisKnupp.**

- 1, **Portfolio Performance Update through February 28, 2014, with Preliminary Return Report through March 31, 2014, used by the Board to set T-DROP Interest for June 30, 2015.** Ms. Katie Rizzo of Hewitt EnnisKnupp (HEK) presented the portfolio performance update through February 28, 2014. Ms. Rizzo reported the total market value of ATRS fund was \$14.3 billion dollars. The total fund had a return of 13.5% for the fiscal year-to-date, outperforming its benchmark of 11.9%. ATRS ranked in the 6% percentile of similar sized pension plans across the U.S.

HEK provided the March 2014 Preliminary Return: T-Drop Interest Rate which will be used by the Investment Committee and the Board of Trustees in accordance with ATRS rules as the basis for the interest payable on T-DROP accounts on June 30, 2015. The performance report continues to show strong investment returns of 13.8% through March 31, 2014.

2. **Recommendation to Add Russell Implementation Services, Inc. as an available Third Transition Manager.** Tom Schoenbeck of Hewitt EnnisKnupp presented to the Committee the recommendation to add Russell Implementation Services, Inc. as an additional provider to the ATRS transition manager group. Currently, the ATRS transition manager group consists of BlackRock and State Street Global Markets (SSGM). While BlackRock and SSGM are both best in class providers, HEK recommends that Russell be added as a third transition management provider. The addition of Russell would provide ATRS the ability to work with three of the top transition management firms in the industry and would further diversify the managers going forward.

HEK and staff recommend adding Russell Implementation Services, Inc. as a third transition manager.

- a. **Resolution 2014-27**

**Ms. Nichols *moved to adopt* Resolution 2014-27, To Hire Russell Implementation Services, Inc. for Transition Management. Mr. Knight *seconded the motion*, and the Board *unanimously approved the motion*.**

3. **Update on Arkansas Opportunity Fund.** Ms. Katie Rizzo of Hewitt EnnisKnupp presented the Board with the update on the Fund of Opportunity. ATRS asked HEK to assist in identifying an Arkansas-based investment firm to manage an Opportunity Fund for ATRS. HEK did extensive research and screening of approximately 15 Arkansas based firms to determine each firm's suitability to manager the Opportunity Fund mandate. The screening process yielded a list of three (3) Arkansas-based firms that HEK felt had the potential to manage the Opportunity Fund prudently and successfully. The three semi-finalists are: Stephens, Inc., Circumference Group., and Delta Trust.

HEK has submitted Request for Information (RFI) and Operational Due Diligence Questionnaires (ODD) specifically for the ATRS Opportunity Fund mandate. The three (3) managers were asked to complete the

RFI and ODD and submit to HEK. HEK is in the process of reviewing the RFI and ODD from each candidate and following a complete review, HEK will hold a telephone conference with each firm asking questions to gain better understanding of each firm's specific area of expertise.

HEK expects to have a recommendation for the Committee at the June 2, 2014, meeting.

### **C. Real Assets Investment Consultant Recommendations.**

- 1. Recommendation to Commit up to \$30 Million Dollars in LaSalle Asia Opportunity Fund IV, L.P., an Opportunistic Real Estate Fund Focused on both Debt and Equity Investments in Asia.** Mr. Chae Hong of HEK presented the recommendation for LaSalle Asia Opportunity Fund IV, L.P. This fund is a closed-end, opportunistic fund focused on taking advantage of attractive real estate fundamentals in the Pan-Asian region. The investment strategy will focus on fulfilling the growing demand for core real estate assets by targeting opportunities resulting from cyclical recoveries, liquidity gaps, and deleveraging. The Fund is targeting an 18% net IRR.

HEK and ATRS staff both recommends an investment of up to \$30 Million Dollars in LaSalle Asia Opportunity Fund IV, L.P., in accordance with the previously approved real estate commitment pacing model for opportunistic strategies in 2014.

#### **a. Resolution 2014-28**

**Ms. Nichols *moved to adopt* Resolution 2012-28, to commit up to \$30 Million Dollars in LaSalle Asia Opportunity Fund IV, L.P., an Opportunistic Real Estate Fund Focused on Distressed U. S. Investments. Ms. Davis *seconded the motion*, and the Board *unanimously approved the motion***

- 2. Recommendation to Commit up to \$30 Million Dollars in Carlyle Realty Partners Fund IV., L.P., an Opportunistic Real Estate Fund focused on Distressed U.S. Investments.** Mr. Chae Hong of HEK presented the recommendation of Carlyle Realty Partners Fund IV., L.P. This fund is also a closed-end opportunistic fund targeting a broad range of U. S. real estate investments. Carlyle will employ a research-driven, value-based investment approach to identify underpriced fundamentals and acquire high quality assets at discounts

to replacement costs. With moderate leverage, the Fund will seek net IRR's of at least 15%.

HEK and ATRS staff both recommends an investment of up to \$30 Million Dollars in LaSalle Asia Opportunity Fund IV, L.P., in accordance with the previously approved real estate commitment pacing model for opportunistic strategies in 2014

**a. Resolution 2014-29**

**Ms. Nichols *moved to adopt* Resolution 2012-29, to Commit up to \$30 Million Dollars in Carlyle Realty Partners Fund IV., L.P., an Opportunistic Real Estate Fund focused on Distressed U.S. Investments. Mr. Knight *seconded the motion*, and the Board *unanimously approved the motion***

**D. Private Equity Investment Consultant Recommendation.**

- 1, Recommendation to Commit up to \$25 Million Dollars in Thoma Bravo XI, L.P., a Buyout Fund Focused on U. S. Investments with a Specialization in Software Companies, using Imminent Need.** Mr. Michael Bacine, of Franklin Park, presented the recommendation of Thoma Bravo XI, L. P. This fund is being formed to acquire software companies in the U. S. The General Partner is targeting capital commitments of \$2.5 billion dollars, up to an expected cap of \$3.5 billion dollars. The GP will primarily seek companies operating in the application, infrastructure, and security software industries, with a secondary focus on business, media, and technology-enabled service industries. The Fund will pursue a compelling strategy and the General Partner has an experienced and cohesive team with an attractive track record.

Franklin Park and ATRS staff both recommends an investment of up to \$25 Million Dollars in Thoma Bravo XI, L.P., a Buyout Fund Focused on U. S. Investments with a Specialization in Software Companies, using Imminent Need.

**a. Resolution 2014-29**

**Ms. Nichols *moved to adopt* Resolution 2012-30, to Commit up to \$25 Million Dollars in Thoma Bravo XI, L. P., a Buyout Fund Focused on U. S. Investments with a Specialization in Software Companies, using Imminent Need. Ms. Davis**

***seconded the motion, and the Board unanimously approved the motion***

XI. **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.** None.

**B. Report on Outsourcing and Discussion of Implications for ATRS.**

Mr. Hopkins reported that Michael Ray and Laura Gilson worked on finding information on outsourcing from other states. More and more ATRS employers (mainly school districts) are outsourcing services such as transportation, custodial, food service, classroom aids/assistants, and substitutes. These positions are being outsourced at an ever increasing rate. For the first time ever, the last ATRS actuarial report had less covered payroll in 2013 than in the previous fiscal year. In the 2012 actuarial valuation, the number of active members dropped for the first time ever. It was not a one-time anomaly since the number of active members dropped again in 2013 for only the second time ever. Both the 2013 drop in covered payroll and the two consecutive losses of active members is unprecedented at ATRS. Cost shifting between employers would occur if ATRS uses the employer contribution payments to maintain sufficient payments on its unfunded liabilities. Under current law, an employer contribution increase is paid by the Department of Education on a line item that would likely otherwise be distributed to all the schools by the funding formula. If this happens, all the schools receive less due to the outsourcing.

A recommendation from ATRS Staff has been that the loss of revenue from outsourcing should be borne by the school districts that are outsourcing. The solution ATRS staff has previously suggested would be to require a surcharge from 7% -10% on all contracts that outsource school functions typically provided by an employee instead of a contractor. The benefit of this approach is that cost shifting to other employers does not occur since the school districts with the outsourced contracts actually pay the amount on the unfunded liabilities of ATRS as if the school district had employees subject to employer contributions. This approach also prevents ATRS from implementing benefit reductions to retirees or reduced benefit accruals to active members to "fund" the cost of outsourcing. At the same time, districts that outsource still have cost

savings, just not as much, since the districts are only paying to ATRS a part of the 14% employer contribution.

Based upon ATRS staff calculations, about one half of the 14% employer contribution is used to offset new liability accruals and one half is used to reduce the unfunded liabilities of ATRS. That percentage can vary somewhat from year to year, so that is why ATRS staff has recommended the Board consider a surcharge of between 7% - 10% on outsourced contracts. That amount essentially holds ATRS, other employers and its members harmless in the outsourcing process generally.

Depending upon how a school district undertakes outsourcing, certain ATRS members may be harmed anyway. ATRS cannot allow private employers to participate in ATRS. The employees who have their positions outsourced face choices between:

- remaining in the outsourced position and never vesting in ATRS;
- remaining in the outsourced position and never qualifying for the health stipend or lump sum death benefit by getting 10 years of service;
- remaining in the outsourced position while having 24 years of service but never reaching 25 years of service to become eligible for early retirement;
- remaining in the outsourced position while having 27 years of service and never entering T-DROP; or
- choosing between staying in the outsourced position or remaining in T-DROP by seeking employment at another school district or just retiring since T-DROP deposits will stop once the member ceases being employed by an ATRS employer.

These members are not helped by a surcharge on the outsourcing.

The Committee agreed that this issue needs to be looked into further and that implementation of a "phase in" for contracts already in existences should be looked into, but not to exclude current contracts from this point forward. In time, all new contracts and current existing contracts should be treated the same. It was the recommendation of the Committee that the Executive Director and Staff put out an Executive Director update with information concerning outsourcing, and to draft possible legislation for the Committee to consider.

### **C. Potential Legislation.**

1. **Potential Change in Disability Benefits Law.** ATRS staff looked at a way to balance the need for an efficient and effective ATRS disability process that supports the smooth operation of the public school system by allowing employees with significant disabilities to retire quickly while at the same time ensuring that the process continues to have integrity after a disability retirement is approved by the ATRS Medical Committee. With new medical treatments and time, some disability retirees may improve and no longer have a disability that prevents the retiree from working gainfully in the work force. ATRS currently prohibits a disability retiree from returning to work at an ATRS employer to maintain integrity in the System. That rule is easily monitored by ATRS staff. ATRS staff has no method or legal authority to monitor if the disability retiree works elsewhere. Occasionally a disability retiree may work full time at a factory or other location. Many people in the school community may know about the work and the disability status. This undermines the integrity and credibility of the disability process at ATRS.

Staff presented the Committee with three (3) proposals for the Committee to consider if the Operations Committee wants to recommend action to the ATRS Board.

- a. **Eliminate current monitoring and provide Board Authority to set rules in future (OPTION 1).** The first option is for legislation that eliminates the current post- disability review and replaces it with ATRS rule making authority. This approach eliminates any review process post retirement unless and until the Board promulgates rules.
- b. **Continue current monitoring and provide Board Authority to set additional rules in the future (OPTION 2).** Option 2 maintains the current review process, even though it has not effectively worked, while the Board considers any additional rules that it determines should be implemented. Unlike Option 1, the review authority would be just modified instead of starting from scratch.
- c. **Continue Existing with 3-4 year Social Security Disability Trigger (OPTION 3).** Option 3 is a hybrid of what most retirement systems do and what ATRS has traditionally done. Most retirement systems require a member to be approved for Social Security disability in order to first qualify for disability retirement at the pension system. Since it is important to provide a quicker path for educators who are ill to exit the classroom and the education setting, the ATRS disability process provides a much swifter

decision. The ATRS process uses a Medical Committee of 3 doctors to decide if a member is disabled using medical reports. Option 3 maintains that quick initial process, but also blends in a future use of Social Security disability for continued eligibility after an appropriate 3- 5 years to be approved for Social Security disability retirement. Under Option 3, the member still submits a disability application that has the lightning fast review by the ATRS Medical Committee. If approved for disability, once the ATRS disability payments begin, the member would have a duty to also apply for Social Security disability and ultimately be approved for Social Security disability. If the member is not approved for Social Security disability after 3 – 5 years, then the member would keep all previous disability payments but the benefit payments would end until the member is eligible for retirement by reaching age 60.

**Mr. Lester moved to approve Option No. 3, Continue Existing 3-4 Years Social Security Disability Trigger. Mr. Knight seconded the motion, and the Board unanimously approved the motion.**

- 2. Private School Certification by ATRS Staff Instead of Department of Education.** Staff advised the Operations Committee on February 17, 2014, that the Department of Education no longer tracks private schools, and therefore no longer has a reasonable basis to certify private school positions to ATRS as eligible for licensure as teachers whether in or out of Arkansas. ATRS staff advised the Committee that that ATRS staff regularly makes determinations about related items and that the staff could make an evaluation for private school certification in full compliance with federal law standards. The Committee and Board asked the staff to draft potential legislation that would allow this process to change from the Department of Education Certification to the ATRS staff.

The ATRS Legal Department drafted a very simple change that illustrates this change. After review, the Committee approved the draft, and recommends the change to the Board, along with ATRS staff recommendation. .

**Mr. Lester moved to approve the draft legislation for Private School Certification by ATRS Staff instead of Department of Education. 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 February 2014 and March 2014. In February 2014, there were 13 applicants and 13 were approved. In March 2014, there were 8 applicants, 6 were approved, and 2 needed more information.

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

XX. **Other Business.** None

XXI. **Adjourn.**

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

**Meeting adjourned at 11:10 a.m.**

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George Hopkins,  
Executive Director

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Dr. Richard Abernathy, Chair  
Board of Trustees

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Tammy Porter,  
Recorder

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Date Approved