MINUTES
ARKANSAS TEACHER RETIREMENT SYSTEM
BOARD OF TRUSTEES

Monday, April 4, 2016
11:30 a.m.
1400 West Third Street
Little Rock, AR 72201

ATTENDEES

Board Members Present
Jeff Stubblefield, Chair
Danny Knight, Vice Chair
Dr. Richard Abernathy
Lloyd Black
Kathy Clayton
Kelly Davis
Bobby Lester
Hon Andrea Lea
Robin Nichols
Deborah Thompson
Janet Watson

Board Members Absent
Candace Franks
Johnny Key
Hon. Dennis Milligan

Guest Present
Donna Morey, ARTA
PJ Kelly, AHIC (Aon Hewitt)
Angela Cantillon, AHIC (Aon Hewitt)
Chae Hong, AHIC (Aon Hewitt)
Neil Mowery, Franklin Park
Sean Barron, Simmons

ATRS Staff Present
George Hopkins, Executive Director
Gail Bolden, Deputy Director
Shane Benbrook, Internal Audit/Risk Mgmt.
Curtis Carter, Chief Fiscal Officer
Laura Gilson, General Counsel
Rod Graves, Assoc. Dir. of Operations
Wayne Greathouse, Assoc. Dir of investments
Jerry Meyer, Manager, Real Assets
Martha Miller, Staff Attorney
Manju, Manager, Data Processing
Linden Maurer, Legal Assistant
Tammy Porter, Administrative Assistant
Michael Ray, Director, Member Services
Clint Rhoden, Director of Operations
Joe Sithong, Software Support Analyst
Leslie Ward, Manager Private Equity
Brenda West, Internal Audit/Risk Mgmt.

Reporters Present
Mike Wickline, Arkansas Democrat Gazette

I. **Call to Order/Roll Call.** Mr. Jeff Stubblefield, Chair, called the Board of Trustee meeting to order at 11:59 a.m. Roll call was taken. Ms. Franks, Mr. Key, and Hon. Dennis Milligan were absent.

II. **Motion to Excuse Absences.**

Mr. Knight *moved* to *excuse* Ms. Franks, Mr. Key, and Mr. Milligan from the April 4, 2016 Board of Trustees meeting. Mr. Lester *seconded* the *motion*, and the Board *unanimously approved the motion.*

III. Adoption of Agenda

Ms. Nichols *moved* for *adoption* of the Agenda. Dr. Abernathy s*econded* 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 Minutes.

A. Approval of February 1, 2016 Minutes.

Ms. Davis *moved* for *approval* of the Minutes of the Board of Trustees meeting of February 1, 2016. Ms. Clayton *seconded* the *motion*, and the Board *unanimously approved the motion.*

VI. 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. No member Interest was waived this reporting period.

VII. 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 One (1) employer penalty with interest for this reporting period in the amount of $178.78.

VIII. Member/Employer Appeal Update

A. **Palestine-Wheatley.** The Court of Appeals affirmed the Circuit Court's decision in favor of ATRS.

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

A. **Investment Update and Arkansas Related Update.**

1. **List of Fund Closings**

   a. **Thoma Bravo Discover,** L.P., a Private Equity Buyout Fund Focused on U.S. Investments with a Specialization in Software Companies, the Board Authorized Commitment of up to $30 Million Dollars on December 7, 2015. $10 Million Dollars of the $30 Million Dollar Recommended Allocation was Obtained on January 29, 2016. Due to high demand for this fund the General Partner would not accept the entire ATRS commitment. ATRS was only able to obtain $10 million dollars of the $30 million dollars authorized. The final agreement for $10 million dollars was negotiated, accepted, and closed on January 29, 2016.

2. **Arkansas Related Update.**

   a. **Report on Farmland Tour and Joint Venture of Halderman Real Assets Management (HRAM) and US Agriculture**. On Friday February 26th ATRS staff George Hopkins, Rod Graves, Jerry Meyer and real assets consultant at Aon Hewitt, Chae Hong, met onsite at US Agricultures headquarters in Indianapolis, Indiana. In attendance for US Agriculture were Steve Hegeman, Anatole Prevnev and Tom Peck. Representing HRAM were David Martin and Adam Gore. The purpose of the meeting was to perform "back-office" due diligence and to determine if ATRS should consent to the two teams working together. ATRS staff and Real Assets Consultant were impressed with the US Agriculture's experience and deal flow opportunity that could benefit ATRS. Chae Hong did additional due diligence work outside the meeting. The ATRS executive director has now consented to the joint venture between US Agriculture and HRAM.

   b. **Recommendation to Commit an Estimated $151 Million Dollars for a Revenue Stream of $224 Million Dollars of State of Arkansas Recycling Tax Credits to be paid by the State of Arkansas.** ATRS currently has a policy allocation to place 20% of its assets into fixed income investments. The amount invested is now below 20% due to increases in other areas. ATRS is in a position to address this under allocation. The 10 year outlook for fixed income is an annual return of about **2.5%**. ATRS now has an opportunity for a state of Arkansas recycling tax repurchase agreement that will provide a net annual return of **over 5%** for the next 14 years from the **state of Arkansas**. Other aspects of the total transaction will allow ATRS to lock in the fixed income returns of between **5.3%** and **5.7%** (all the returns on the fixed income investment are a state of **Arkansas** payment risk). In addition, returns of capital from Big River Steel of approximately $31 million through the transaction also benefit ATRS. The raw 5.3% to 5.7% return is over twice the expected return of the ATRS fixed income allocation for the next ten years. The expected return is also enhanced by the state of Arkansas' first payment date being about 6 months after the transaction (June 2017) rather than the modeled 12 month period (December 2017) with all 14 payments being 6 months earlier than modeled (June payments verses December payments). The enhanced transaction is even better when considering the return of capital. The risk in this fixed income proposal is a state of Arkansas payment risk like an Arkansas general obligation (GO) bond. If recommended by the ATRS Board, the expected funding date of the transaction would be near the end of 2016.

As part of the economic incentives provided by the state of Arkansas, Big River Steel is entitled to receive recycling tax credits in the expected amount of $280 million dollars issued by the state of Arkansas. Arkansas law now puts ATRS in possession and control of these tax credits on behalf of Big River Steel. ATRS has obtained and sold state of Arkansas issued tax credits in the past. Here, the state of Arkansas, itself, has committed by law to purchase the tax credits to save the state $4 million dollars a year. The state saves $4 million dollars by paying $16 million dollars for $20 million dollars of tax credits to cancel the tax credits, instead of having $20 million dollars in reduction of state revenue by the tax credits being claimed on tax returns.

The amount of recycling tax credits generated by Big River Steel is expected to be $280 million but could be determined to be between $260 million dollars (very unlikely to be this low) and $320 million dollars (only up to $300 million is involved in the proposal that is presented). The final true up of the recycling tax credits will be certified by the Arkansas Department of Environmental Quality in early 2017. The recycling tax credit is set at 30% of equipment purchases and installation costs at a recycling facility, such as Big River Steel. ATRS and Big River Steel are estimating the total amount of certified tax credits to be issued for Phase 1 of Big River Steel to be at or above $280 million dollars (the state has already given a first estimate of just under $280 million dollars before some additions were made to the equipment ordered and the costs to install the equipment). ATRS staff and Big River Steel limited the proposed transaction to just the first $300 million dollars in recycling tax credits, in any event.

Act 862 of 2015 (Act 862) requires the state of Arkansas to purchase these Big River Steel recycling tax credits for 80% of the face value. The law sets a maximum tax credit submission per year of $20 million dollars. This establishes an annual state of Arkansas payment for the tax credits of $16 million dollars that should last for 14 to 15 years (if the tax credits are over $280 million, the term is 15 years). At 80% of face value, the approximate value of the $280 million dollars of certified recycling tax credits is $224 million dollars, to be paid over exactly 14 years in annual payments. The purchase of $280 million dollars of tax credits by the state through Act 862 will cause the $224 million dollars to be paid at $16 million dollars per year over the 14 years.

Using just above a 5% discount rate (interest rate) the current value of the income stream is approximately $151 million dollars. ATRS would immediately receive **a $1 million** dollar set up fee paid by Big River Steel to make the net cost for the tax credits $150 million dollars. Big River Steel will return at least 50% of the net recycling tax purchase payment back to the equity owners as a return of capital as soon as the transaction is funded in late 2016. This means that contemporaneous with the net payment of $150 million dollars, ATRS would receive **$15 million** dollars back from Big River Steel. The $15 million is reached by ATRS owning 20% of the BRS equity multiplied by $75 million dollars to equal $15 million dollars. Big River Steel plans to hold the additional 50% ($75 million dollars) as reserve and for startup capital, which would also be returned. ATRS would be entitled to 20% of the reserved $75 million dollars or another $15 million dollars. The reserved $75 million dollars is planned to be returned to the equity owners in two tranches, one of $25 million dollars in late 2017 (ATRS gets $5 million dollars) and a second tranche in late 2018 (ATRS gets $10 million dollars). Under this example, ATRS would have a net purchase price of $135 million dollars for the $224 million dollar revenue stream to be paid over 14 years and perhaps as low a net purchase price of $120 million dollars if the reserved $75 million dollars is returned as intended in the two tranches.

ATRS currently has $125 million dollars invested in Big River Steel. If approved by the Board, the purchase price of $151 million dollars for the **$224** million dollar revenue stream, receive back the $1 million dollars (setup fee) and receive back the $30 million dollars in return of capital would produce a net purchase price of **$120** million dollars for ATRS. In this example, the total net dollars would make the ATRS commitment to Big River Steel related opportunities $245 million dollars ($125 million to BRS investments and $120 million dollars to purchase the state of Arkansas tax credits). This converts most of the risk in the project to a state of Arkansas risk, as explained below.

The high probability the state will purchase all the tax credits at a rate of 80% of face value (required by current Arkansas law) will produce an expected revenue stream of $224 million dollars over 14 years. Even if the state did not purchase the tax credits for some unusual reason (not purchasing the credits would cost the state $4 million dollars a year for 14 years), Big River Steel has a duty to make ATRS whole under the proposal that has been negotiated and the tax credits would be sold to others with BRS making up any shortfall from the 80% of value requirement. The net result for ATRS is an investment in Big River Steel opportunities/tax credits for $245 million dollars with $224 million dollars expected to be returned to ATRS **by the state of Arkansas** over 14 years through the state's purchase of the tax credits. The other ATRS equity and debt investments in Big River Steel will remain unchanged and are still expected to produce significant returns for the ATRS portfolio. **This essentially shifts all but $21 million dollars of the ATRS risk in Big River Steel from a Big River Steel risk to a state of Arkansas risk while leaving the quality BRS investments of $125 million dollars intact for quality returns.**

The consultant's report shows that when the projected returns are compared to the expected return of the fixed income portfolio, the result produces**,** on day **one**, a net present value **ABOVE** expected returns of $29 million dollars. That is not a bad day one. When the returns of capital are also considered, it is a very good day one.

The ATRS consultant on this investment, Simmons First National Bank (with leadership from the former Delta Trust team), and ATRS staff recommend ATRS commit to purchase the expected $280 million dollars in recycling tax credits that should generate a revenue stream of $224 million dollars over 14 years for $151 million dollars. In addition, the recommendation is to purchase all the recycling tax credits issued up to **$300** million dollars of tax credits ($20 million dollars of tax credits above the estimate). If the credits are $300 million dollars (an extra $20 million above the expected 280 million dollars), then in March or April 2017, ATRS would pay an additional amount of $10.7 million dollars for the $16 million dollar income stream for year 15. At the time of the secondary purchase by ATRS, ATRS would immediately be given back a return of capital of $2.1 million dollars (20% of the purchase price due to ATRS' 20% equity ownership) for a net cost of the $16 million dollar payment of $8.6 million dollars. This proposal is one that allows ATRS to maintain stronger fixed income returns with a focus on Arkansas investments while reducing nongovernmental risk.

Ms. Nichols *moved* to *adopt* Resolution 2016-11, to Commit an Estimated $151 Million Dollars for a Revenue Stream of $224 Million Dollars of State of Arkansas Recycling Tax

Credits to be paid by the State of Arkansas. The Board *unanimously adopted the Resolution.*

c **Victory Building Update.** Occupancy is currently at 96% which includes the new UAMS clinic space. The UAMS space is nearly complete with move in commencing the first week of April and the clinic opening scheduled for the first week of July.

d. **Remaining Arkansas Related Properties for Sale**. The Board approved Resolution 2014-38 at the June 17, 2014, meeting authorizing the sale of Arkansas real estate assets (except ATRS Headquarters and the Victory Building) for appraised value or higher. Properties sold include Chenal property on 12/10/2014 and John Ashley Drive property on 7/17/2014. The remaining Arkansas properties available for sale are West Memphis DHS, Texarkana DHS, Rahling and Chenal Road commercial land in Little Rock, and John Ashley Drive multifamily land located in North Little Rock.

B. General Investment Consultant Update

1. **Preliminary Performance Report for the Month Ended March 31, 2016. P.J. Kelly and Angelia Cantillon o**f Aon Hewitt Investment Consulting presented the performance report for the month ended March 31, 2016. A handout of the report was passed out to the Committee. As of March 31, 2016, the ATRS fund had a market value of approximately $14.3 billion dollars. The total fund had a return of 8.2% since inception, underperforming its benchmark of 8.4%. Fixed income had a market value of $2.4 billion dollars, with a return of 5.5% since inception, underperforming its benchmark of 5.9%.

2. **Recommendation to Commit up to $50 Million Dollars in Nephila Capital Rubik Holdings, Ltd., an Opportunistic/Alternative Reinsurance Fund Specializing in Property Catastrophe Insurance Coverage.** ATRS already has an investment in a reinsurance fund, Aeolus, discussed in the next item. Reinsurance returns are generated by charging an insurance premium to an insurance company for taking a specific type and level of risk for specified natural disasters (e.g. Hurricane Katrina, Japanese Earthquake). The risk is specific

and not general. The risk may only apply to certain areas or states, certain types of damage and are also limited to windows of risk, such as only to damages over $150 billion dollars. The great benefit of this type of fund in the ATRS portfolio is that these funds are great diversifiers and have almost no correlation to the equity or bond markets. This means that the returns of these funds may be strong when equity markets are down. This type of investment helps maintain returns when markets are under pressure.

Nephila is the oldest and largest dedicated manager in the insurance linked securities (ILS) sector, with over 100 employees across 4 global offices and assets under management (AUM) of approximately $9.3 billion. The company's investment staff is primarily based in Hamilton, Bermuda; the Portfolio Management and Analytics Team contain 31 investment professionals. Nephila launched its first fund in April 1998 and has the longest track record in the industry.

Since inception, Nephila has introduced to market six different ILS offerings that differ by return, risk and underlying portfolio composition. The product offerings are balanced between long/short and long-only and have generally been capacity constrained for a number of years. This means that the fund has had limited room for new investors. It is a great time to enter the market to ensure ATRS has the ability to maintain this type of investment as it becomes a more common and understood investment vehicle.

The Nephila Capital Rubik Holdings, Ltd, launched in January 2014, has a return objective of 3 month T-bills plus 6%-12% on an annualized basis net of fees and losses and has modeled losses of approximately 4% to 6% per year. While the Rubik Fund has a limited performance, it has delivered a return ahead of its 3 month T-bills + 6% minimum objective: The Fund has returned 6.1% in calendar year 2014 and in calendar year 2015. Nephila has successfully run funds with similar return/risk profiles over much longer periods. Across the platform, annualized returns since inception across product offerings range from 4.5% (lower risk) to 10.5% (higher risk).

Frank Majors is a co-founder of Nephila Capital Ltd. and is a Managing Principal at its affiliate, Nephila Advisors LLC. Since

1997, Mr. Majors has been involved in most aspects of the business but is currently focused on risk management and firm strategy. Greg Hagood is the other co-founder of Nephila Capital Ltd. and is a Managing Principal at its affiliate, Nephila Advisors LLC. Mr. Hagood has been involved in all aspects of the business but is currently focused on risk management, firm strategy and investor relations. Mr. Hagood is also a Director of Nephila Capital Ltd. and Nephila Holdings Ltd.

Mr. Hopkins reported that both Aon Hewitt Investment Consulting and Staff concur with the recommendation.

> **Ms. Nichols *moved* to *adopt* Resolution 2016-12, to Commit up to $50 Million Dollars in Nephila Capital Rubik Holdings, Ltd., an Opportunistic/Alternative Reinsurance Fund Specializing in Property Catastrophe Insurance Coverage. The Board *unanimously adopted the Resolution.***

3. **Recommendation to Commit up to an Additional $37 Million Dollars in Aeolus Catastrophe Keystone PF Fund, LP, an Opportunistic/Alternative Reinsurance Fund Specializing in Property Catastrophe Insurance Coverage.** Aeolus Reinsurance, based in Bermuda, was founded in 2006 by Peter Appel and David Eklund. This firm was seeded by large investors, such as Bank of America and Merrill Lynch, and successfully provided global catastrophic protection to the reinsurance market for several years. In 2011 the founders transformed the firm into Aeolus Capital Management in order to raise capital from other third party investors to provide additional flexibility in deploying capital. The fund, Aeolus Property Catastrophe Keystone PF Fund, LP, seeks to use highly customized portfolios based on actuarial projections concerning catastrophic events, such as hurricanes, to provide returns that are not usually correlated to other asset classes.

   The fund is expected to yield a gross return of the Treasury bill rate plus 15% and a net return of 10-11%. Prior funds managed by this team have a net average return of 18% for three years and 16.9% for four years. Reinsurance and retrocession markets underwrite in two seasons, January 1st and June 1st.

   The Board authorized commitment of up to $110 million dollars in the fund at the October 5, 2015, meeting was for the January underwriting season. Both Aon Hewitt Investment Consulting and staff recommend an additional allocation of up to $37 million dollars to Aeolus Property Catastrophe Keystone PF Fund, LP, for the June underwriting season.

ATRS will be entering the June renewal term that runs for a 1 year period. Investment in reinsurance funds will help ATRS to continue to add diversification to the ATRS portfolio and help reduce the reliance on the traditional stock and bond markets.

Mr. Hopkins reported that both Aon Hewitt Investment Consulting and Staff concur with the recommendation.

Ms. Nichols *moved* to *adopt* Resolution 2016-13, to Commit up to an Additional $37 Million Dollars in Aeolus Catastrophe Keystone PF Fund, LP, an Opportunistic/Alternative Reinsurance Fund Specializing in Property Catastrophe Insurance Coverage. The Board *unanimously adopted the Resolution.*

4. **Recommendation to Transition out of the BlackRock U.S. Equity Market Fund A, a Passive U.S. Equity Index Fund.** At the June 6, 2011, meeting, the Board approved investment in the BlackRock U.S. Equity Market Fund and the BlackRock MSCI ACWI IMI Index Fund. Both are passive index funds with the BlackRock U.S. Equity Market Fund designed to track the Dow Jones U.S. Total Stock Market Index and the BlackRock ACWI IMI Fund designed to track global markets including the U.S. The funds were initially approved by the Board to provide ATRS with low cost, liquid investment opportunities for the domestic and global portfolio allocations.

The Board approved the amendment of the ATRS Investment Policies and Procedures at the June 1, 2015 meeting to combine the domestic and global equity asset allocations into one total equity allocation. The combining of asset allocations has eliminated the need for a separate passive index tracking only the U.S. market. In addition, transitioning out of this fund is in line with the long term goal of continuing to globally position the total equity portfolio. The remaining BlackRock global index fund will provide the ATRS total equity asset class with similar low cost, liquid investment opportunities including the U.S. Both ATRS staff and Aon Hewitt Investment Consulting recommend transition out of the BlackRock U.S. Equity Market Fund A. The recommendation to transition out of the U.S. index should not be considered a negative view of BlackRock, but rather a change in investment direction to global equities. BlackRock has performed well.

Mr. Hopkins reported that both Aon Hewitt Investment Consulting and Staff concur with the recommendation.

> **Ms. Nichols *moved* to *adopt* Resolution 2016-14, to Transition out of the BlackRock U.S. Equity Market Fund A, a Passive U.S. Equity Index Fund. The Board *unanimously adopted the Resolution.***

5. **Investment Opportunities Update**. AHIC was prepared to discuss Small Cap Securities' Passive Management style within U. S. Equities as an educational item. The Committee tabled this item until a later meeting.

C. Real Assets Investment Consultant Report – AON Hewitt Investment Consulting.

1. **Recommendation to Commit up to $25 Million Dollars in Harbert European Real Estate Fund IV, L.P., a Value Added Real Estate Fund Focused on Office, Industrial, Retail, and Residential Investments in Major European Markets.** Established in 1993, Harbert Management Corporation (Harbert) is headquartered in Alabama with other offices in London, Paris, and Madrid. Harbert European Real Estate Fund IV, L.P., is a closed-end, value add fund targeting institutional quality office, industrial, retail and select residential investments located in the major markets in Western Europe particularly the UK, France and Spain. Fund IV will focus on making equity investments in assets that can be repositioned to institutional quality through active asset management and physical enhancement.

   The experienced management team consists of fourteen investment professionals with the senior staff averaging nineteen years of real estate experience. The most recent fund, Harbert European Real Estate Fund III, is projected to outperform the target rate and deliver a 22.5% net IRR. Fund IV is targeting a 12% to15% net IRR. Both Aon Hewitt Investment Consulting and ATRS staff recommend an investment in

Harbert European Real Estate Fund IV, L.P., with a commitment of up to $25 million dollars. If approved by the Board the commitment will be made in Euros and the subscription amount may be less than $25 million dollars to account for the fluctuation of currency rates at time of closing.

Mr. Hopkins reported that both Aon Hewitt Investment Consulting and Staff concur with the recommendation.

Ms. Nichols *moved* to *adopt* Resolution 2016-15, to Commit up to $25 Million Dollars in Harbert European Real Estate Fund IV, L.P., a Value Added Real Estate Fund Focused on Office, Industrial, Retail, and Residential Investments in Major European Markets. The Board *unanimously adopted the Resolution.*

D. Private Equity Consultant Report – Franklin Park

1. Recommendation to Commit up to $30 Million Dollars in Thoma Bravo XII, L.P., a Private Equity Buyout Fund that Invests in Middle to Large Market Software Companies with Imminent Need. Based in both Chicago and San Francisco, Thoma Bravo is a very experienced manager that acquires software companies in the U.S. ATRS invested in Thoma Bravo XI in 2014 and the fund is currently on track to perform very well. The general partner's three funds prior to Fund XI have generated net returns greater than 23% IRR. The manager typically pursues a buy and build strategy seeking middle market and large companies where profitability can be significantly increased. Once operating improvements have been completed, Thoma Bravo seeks to make add-on acquisitions to rapidly grow portfolio companies to increase scale and attractiveness to strategic buyers. The general partner will primarily seek opportunities in the application, infrastructure and security software industries. ATRS also recently invested in Thoma Bravo Discover that employs a similar strategy in lower middle market businesses.

The senior team managing the fund is experienced and cohesive with principals that average fourteen years tenure with Thoma Bravo and over twenty years of experience in private equity. This fund will provide additional exposure to the software industry for ATRS. Both Franklin Park and ATRS staff recommend an investment in Thoma Bravo XII, L.P. with a commitment of up to $30 million dollars. Due to the fact that ATRS will need to close on this highly sought-after investment within a week of the board meeting, Imminent Need is requested.

Mr. Hopkins reported that both Aon Hewitt Investment Consulting and Staff concur with the recommendation.

Ms. Nichols *moved* to *adopt* Resolution 2016-16, to Commit up to $30 Million Dollars in Thoma Bravo XII, L.P., a Private Equity Buyout Fund that Invests in Middle to Large Market Software Companies with Imminent Need. The Board *unanimously adopted the Resolution.*

X. Operations Committee Report. Bobby 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. Open Forum. None

B. Potential 2017 Legislation

1. **Disability Retirement to Return to Work Options.**

a. **Return to Active Covered Employment.** This option would allow an ATRS disability retiree to return to work for an ATRS employer in the same type of position held prior to disability retirement (parallel position) in an attempt to cancel disability status and return to work as an active member. This activity would cancel ATRS disability retirement benefits for any month in which the member is paid by an ATRS employer, and allow the member to earn additional service credit for an enhanced retirement benefit. A two-year period was suggested before the member must surrender all past and future disability benefit rights. This would include being considered disabled by the ATRS Medical Committee without reapplication for disability benefits, and returning to disability status with the greater of the member's last disability benefit payment amount or a recalculated benefit using enhanced service credit for a higher benefit. Service credit would be reported to ATRS with all other active employees. Employee contributions (if contributory) would be withheld, and employer contributions would be paid on the member's covered salary. Days of service would accumulate for service credit.

The Committee discussed changing the two-year period to three years and asked staff to draft potential legislation with the change.

b. **Return to Limited Covered Employment.** This legislation would allow an ATRS disability retiree to return to limited covered employment, less than 40 days of service credit per fiscal year, using a Disability Special Needs Waiver form that would be developed by ATRS staff. The Waiver form would be initiated by the employer and submitted to the ATRS executive director contemporaneously with the employment engagement. The Disability Special Needs Waiver form would include the expected duration and type of employment, such as testing, bus driving, or substitute services, and would be effective for only one fiscal year. The retiree would continue to receive monthly disability retirement benefits during the time the retiree works under the Special Needs Waiver. Salary would be reported to ATRS as a working retiree, and employer contributions would be paid on the reported salary.

The Committee discussed the potential violation of working more than 40 days. Staff was instructed to draft potential legislation with a provision stating violation of the term of employment would prevent participation in the return to limited covered employment the following fiscal year.

c. **Return to Covered Employment Using a Disability Exemption.** This legislation would allow an ATRS disability retiree to return to work for an ATRS employer in a non-parallel position on a part-time or full-time basis, using a Disability Retirement Exemption form. For example, a certified teacher may become disabled to perform teaching duties, but may be able to return in a teacher's aide position. The Exemption form would be initiated by the employer and submitted to the ATRS executive director contemporaneously with the employment engagement. The Disability Exemption form would include the expected duration, job duties, and rate of pay for the employment, and would be effective for only one fiscal year. If the waiver were approved, the retiree would continue to receive monthly disability retirement benefits during the time the retiree works under the Disability Retirement Exemption. Salary would be reported to ATRS as a working retiree, and employer contributions would be paid on the reported salary.

The Committee asked staff to draft potential legislation for review.

2. **Marriage Eligibility for Survivor Benefits.** Current ATRS survivor benefits law providing lifetime benefits to a surviving spouse of a deceased active or T-DROP member contains a two-year marriage requirement. If married for two years preceding the member's death, the surviving spouse is **automatically** entitled to a lifetime benefit, even if the member has chosen a different person as the member's residual beneficiary (for instance a child or parent). Current law supersedes the member's designation and the spouse receives the lifetime benefit. ATRS staff has expressed concern that the survivor benefit marriage requirements and rights are different than the marriage requirements for option beneficiaries of retirees.

Since all other option-beneficiary selections have a one (1) year marriage requirement, the staff felt the survivor benefit marriage requirement should also reflect one (1) year for equality and consistency of the application of law and rules. The issue of the difference between the automatic qualification of the surviving spouse verses a member-requested residual beneficiary should also be examined. A possible solution could leave the member in control without an automatic override of the member's residual beneficiary designation.

Mr. Michael Ray, Director of Member Service and Ms. Deborah Kelly, Retirement Counselor spoke to the Committee regarding the problems incurred related to this matter. After discussion, the Committee decided to table this issue until the next scheduled meeting.

3. **Concurrent Service Credit with APERS.** Some members of ATRS have worked for an ATRS covered employer in a position that would normally be covered by ATRS, and at the same covered employer concurrently work in a position that would normally be covered by another state reciprocal retirement system. One example is a teacher who may work at the Arkansas Correctional School, which is normally a position that is covered by ATRS, and at the same employer, work as a guard, which is normally a position that is covered by APERS. When the concurrent service is found, either by ATRS or by the reciprocal system, a long standing procedure has been for the two retirement systems to determine which position is the primary position (usually the position yielding the highest pay), then the retirement system with the non-primary positon would cancel the concurrent service and refund employee/employer contributions.

   In 2013, legislation was passed allowing members of ATRS to receive full service credit in ATRS without reduction of service credit due to concurrent service with another state reciprocal retirement system. The concurrent service that credits the member with more than one (1) year of credited service for a fiscal year is not used for the purpose of vesting, retirement eligibility, or calculating final average salary. For example, if an ATRS member had concurrent service for 3 fiscal years with LOPFI, and each reciprocal system credited the member with 3 years of service credit, ATRS would not count 6 years of service credit for the 2 systems to determine the member was vested with a minimum of 5 years of service credit.

   One exception to this law states that APERS will allow a concurrent employee to remain with APERS only if the reciprocal system allows the member to forfeit the concurrent service by refunding all employee/employer contributions. Otherwise, APERS will not allow the member to retain service credit and will cancel the member's service and refund the employee/employer contributions.

This exception to the law has been problematic for a few ATRS members who have concurrent service credit with APERS. If the APERS position has service that yields a higher pay and thus a higher final average salary than the concurrent service with ATRS, and ATRS' law does not currently have a provision to waive concurrent service with a reciprocal system, then APERS cancels the concurrent service in their system and the member is not allowed to use the higher salaries from APERS for retirement in ATRS. This has caused great financial harm for a few members in this situation. ATRS staff is recommending that this slight adjustment be made to the ATRS law in order to allow members to waive the ATRS service credit that is concurrent with APERS. Since this law would remove service credit from the books at ATRS, there should be little or no costs to ATRS associated with this change.

After discussion, the Committee asked staff to draft potential legislation for review.

C. **Outsourcing.** Clint Rhoden, Director of Operations presented the Committee with a PowerPoint presentation concerning Outsourcing. In the 2015 actuarial report, a concern was raised that employee salaries have been essentially flat since 2011. The assumption of 3.25% annual growth in employee payroll is not being met. One of the reasons given was the drop in the number of covered employees. An in depth ATRS in-house study was performed to determine how much of the drop was due to the recent practice of outsourcing substitute teachers and other support staff. The study involved taking the total decline in member numbers and salary over the past five years and drilling down to find the suspected impact of outsourcing. The group of members with biggest drop in number was the group that consisted of noncontributory support staff that had an annual salary of $10,000 or less**.** The Committee discussed looking into this matter further.

D. **Reduction in Paper Checks produced by State Auditor's Office.** In the February 1, 2016, Board meeting, Auditor Lea asked ATRS to evaluate the possibility of reducing the number of paper checks printed for the System by the Auditor's Office. ATRS had just over 16,000 paper checks printed by the Auditor's Office during calendar year 2015. The majority of the paper checks was issued to retirees who have not signed up with ATRS to have monthly benefit checks deposited directly into bank accounts using electronic fund transfer (EFT). There we approximately 11,700 paper checks issued for retirees during 2015, or approximately 975 checks per month. There were over 3,700 paper checks issued during 2015 for various types of refund disbursements: employer 14% refunds, lump sum death payments, CBA withdrawals, T-DROP lump sum and survivor payments, member termination refunds, residue death refunds, and CASH program refunds. There were over 500 miscellaneous manual checks issued directly through the statewide accounting system, AASIS.

Auditor Lea suggested that ATRS contact our retirees to request that they use EFT, listing the benefits of EFT such as no lost checks, reliable deposit dates, and convenience. ATRS would include the forms and instructions for signing up for EFT in the mailing, as well as instructions for signing up for direct access to their personal retirement account information through the ATRS website member portal. ATRS currently has retiree pay information on its member portal, as well as the retiree benefit payroll schedule of direct deposit dates. This is a very effective first step to the process.

Because there is currently no law or rule that requires retirees to use EFT, ATRS has strongly recommended that retirees use EFT, but hesitated to enforce it as a requirement. At the time of retirement, ATRS provides the EFT form as part of the standard retirement packet of forms. Many ATRS' retirees have asked for and been granted hardship waivers for not using EFT. This is a policy question ATRS felt should be discussed with the Operations Committee and Board prior to any changes in the benefit delivery process to our retirees.

Changes to the delivery of refund type disbursements should not be problematic, since these are mostly one-time payments and often involve large sums of money. ATRS would have to modify its software to allow for the entry of EFT information, test the prenote and payment activities, and change applicable forms. No action was taken on this matter. After discussion, the Committee decided to table this issue until the next scheduled meeting.

XI. Legislative Audit Report, June 30, 2015. The Division of Legislative Audit has provided ATRS staff with the 2015 fiscal year audit report for the fiscal year that ended on June 30, 2015. The audit report has been shared with the

Board via email and also in the Board documents for this meeting. The law requires that the ATRS Board have the Legislative Audit report on the ATRS Board agenda and that the ATRS Board pass a motion reflecting that the audit report was reviewed by the Board in the event issues arise in the future related to the audit.

Mr. Lester *moved* to *approve* the Legislative Audit Report of June 30, 2015, as presented. Ms. Nichols *seconded* the *motion* and the Board *unanimously approved the motion.*

XVII. Staff Reports.

A. Medical Committee Reports. Michael Ray presented the Medical Committee reports. A total of twenty three (23) disability applications were received, twenty one (21) were approved for disability benefits, and two (2) were denied disability benefits.

Ms. Nichols *moved* to *approve* the Medical Committee Reports. Mr. Lester *seconded* the *motion*, and the Board *unanimously approved the motion.*

XV. Other Business: None

XVII. Adjourn.

Ms. Nichols *moved* to *adjourn* the Board Meeting. Mr. Lester *seconded* the *motion*, and the board *unanimously approved the motion.*

Meeting adjourned at 12:13 p.m.

George Hopkins, Executive Director	Mr. Jeff Stubblefield, Chair Board of Trustees
Tammy Porter, Recorder	Date Approved