MINUTES
ARKANSAS TEACHER RETIREMENT SYSTEM
BOARD OF TRUSTEES MEETING

Monday December 2, 2013
1:00 p.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
Susannah Marshal, voting designee for Candace Franks
Wes Goodner, voting designee for Honorable Charles Robinson
Peggy Gram, designee for Honorable Charlie Daniels
Dr. Tom Kimbrell
Danny Knight
Bobby Lester
Robin Nichols
Janet Watson

Board Members Absent
Deborah Thompson

Guest Present
Chris Caldwell, Div. of Legislative Audit
Pat McCollough, CPA,
Ricky Quattlebaum, CPA
Ka Tina Hodge, Attorney General's Office

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 Dixon, Internal Audit/Risk Mgmt.
Mitzi Ferguson, Chief Fiscal Officer
Laura Gilson, General Counsel
Rod Graves, Manager, Investment Dept.
Wayne Greathouse, Assoc. Director
Clementine Infante, Staff Attorney
Manju, Dir. Data Processing
Jerry Meyer, Manager, Real Assets
Linden Maurer, Legal Assistant
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
Judy Kermans, Gabriel, Roeder, Smith & Co.
Brian Murphy, Gabriel, Roeder, Smith & Co.

I. **Call to Order/Roll Call.** Dr. Abernathy, Chair, called the Board of Trustees meeting to order at 1:00 p.m. Deborah Thompson was absent. Dr. Abernathy welcomed Janet Watson to the Board of Trustees.

II. **Motion to Excuse Absences.**

Ms. Nichols *moved* to *excuse* Ms. Thompson from the December 2, 2013, Board of Trustees meetings. Mr. Stubblefield *seconded* the *motion*, and the Board *unanimously approved the motion.*

III. **Adoption of Agenda.**

Mr. Knight *moved* for *adoption* of the Agenda. Ms. Coleman *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. **Scrivener's error November 15, 2012.**

Mr. Stubblefield *moved* for *approval* of the Correction of Scrivener's error to the Board of Trustee Minutes of November 15, 2012. Mr. Black *seconded* the *motion*, and the Board *unanimously approved the motion.*

B. **Minutes of October 7, 2013.**

Ms. Coleman *moved* for *approval* of the Minutes of the Board of Trustees meeting of June 13, 2013. Ms. Nichols *seconded* the *motion*, and the Board *unanimously approved the motion.*

VI. **Preliminary Active Actuarial Valuation.** Judy Kermans and Brian Murphy of Grabiel, Roeder, Smith & Co., gave a presentation of the preliminary active actuarial valuation for the 2012-2013 fiscal year.

ATRS went from 71% funded on June 30, 2012 to 73.25% funded on June 30, 2013. The estimated amortization period that exceeded 100 years on June 30, 2012 was reduced to 69.95 years on June 30, 2013. Those numbers indicated that ATRS is headed in the right direction.

Ms. Kermans reported that the best news was that GRS models project that if ATRS has a 8% return over the next 2 years, ATRS will be close to its desired 30 year amortization period. If ATRS has another good investment year like occurred in the 2012-2013 fiscal year, the 30 year amortization will be achieved faster. ATRS remains strong and the cost-cutting measures that have been nucleus of the last two legislative sessions have restored and will continue to restore the systems' financial position.

VII. **Statement of Financial Interest**. Mr. Hopkins reminded the Board members that their Statement of Financial Interest filings are to be filed with the Secretary of State's office by January 31, 2014, for financial information for calendar year 2013.

VIII. **Proposed 2014 Board of Trustees Schedule.** The Board reviewed the proposed schedule. Mr. Knight asked if meetings could start as soon as the one before it was finished. Mr. Hopkins told the Board he would get with the Attorney General's office and report back to the Board. The Board agreed to bring up any changes to the schedule at the February Board meeting.

Mr. Lester *moved* to *approve* the 2014 Board of Trustee Schedule with any changes to be brought to the February 2014 meeting. Ms. Coleman *seconded* the *motion*, and the Board *unanimously approved the motion.*

IX. **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 was one (1) member who requested interest to be waived. ATRS waived $63.90 in member interest.

X. **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 $4,512.31 in employer interest and penalties.

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

A. **Internal Audit Report: Fixed Assets:** Ms. West reported that the Accounting Department has strong internal controls over fixed assets. No problems were noted during the audit. Internal Audit was very proud of work done by the Department.

B. **Internal Audit Report: Investment Accounts Receivable and Payable.** Ms. West informed the Committee the audit is related to investment trades which are usually large amounts. The trades will normally settle in 3-5 days after the trade date of the buys or sales of investments. Income is usually received the next month. Therefore, balances do not remain on the books for very long. No audit findings were identified and no recommendations were made.

C. **Internal Audit Report: Accounts Payable**. Ms. West informed the Committee the audit has to do with purchase accounts and survivor benefits. Members who cancel their purchase accounts are due a refund of their payments. Payments made with employer pick-up contributions cannot be refunded until member terminates employment or retires. As of June 30, 2013, there are 23 who are due refunds.

State law requires a guardian to be appointed before the Agency can issue money to a minor. The Agency requires a copy of a Court Order and Letter of Guardianship for a minor before the Agency will issue benefits. Benefits owed to minors that have not been issued due to a lack of a Court Order and Letter of Guardianship are set up as an accounts payable. The payable to the minors will remain on the books until the required documents are received or the minor reaches age 18. Interest does not accrue on these payables.

Effective August 2013, the restrictions have been eased and more money will be going to the minors sooner. Mr. Hopkins informed the Committee of the process for contacting the guardian for things that have to be done to obtain the benefits before the child reached age 18.

D. **Internal Audit Report: Follow Up on Prior Internal Audits**. Dena Dixson reported that there were 4 previous audits with findings that were reviewed again.

1. Act 793 Annuity Payments: The Manager of the Payroll Department has done a great job of cleaning up and everything is being done timely. Everything is paid immediately and staff is doing a great job. No follow up on this audit will be done.

2. Death Benefit: During the original audit, it was discovered that 1099s were reporting unrecovered cost incorrectly. They have been identified and corrections are being made. Once this is corrected, a follow-up review will be done.

3. Member History Adjustment Process. One of the problems was the policies and procedures not being available. The Accounting Department has employed extra help to write department-wide policies and procedures. Adjustments are being made timely. The queues are being worked until empty. Purchase accounts previously updated incorrectly have been corrected. Procedures are in place and turn around is less than three (3) weeks.

4. Member Information on Member System: No errors were reported and all accounts were being accurately updated.

XII. **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.** Actual occupancy remains at 71% with leases near the 75% level. A new HVAC system was added to the dining area and is powered by the emergency generator. This will give residents a place to congregate during power outages without suffering the effects of extreme heat or cold.

2. **Victory Building**. Occupancy is back up to 97%, and management is working on filling the other 3%. The Victory Building is well positioned and remains a popular office building for government, agencies and companies that have a lot of governmental interface.

3. **Manager Terminations, Investment Maturities, and Changes Update.**

   a. **Payoff of ATRS/Lindsey Partnership Apartment Investment**. The Lindsey partnership apartment investments closed as on October 10th and ATRS received the $46 million due from Lindsey for the purchase of the interest of ATRS by Lindsey. The apartment investment produced a good 1.92x return for ATRS over the life of the investment with an annual return of over 7%.

   b. **Closing Completed on UBS Agrivest Commingled Agriculture Fund.** The Commitment of up to $50 million in the UBS Agrivest Commingled Agriculture Fund has been completed. ATRS is in an investment queue where it is expected to take a year or longer for capital to be fully called.

c. **Closing Completed on Allianz Structured Alpha U. S. Equity 500 L.L.C.** The Board approved reallocating a portion of funds from the current investment in the Allianz Structured Alpha 250 fund to the Allianz Structured Alpha 500 fund. The Structured Alpha 500 fund has a higher return profile and provides for a greater potential to add value. The fund will add to the active risk of the ATRS US equities. The additional active risk was needed due to the level of indexing that ATRS currently uses. The new allocation of $100 million, approximately 20% of the Structured Alpha 250 fund, was successfully redeployed on November 1, 2013, into the Structured Alpha 500 fund. The transaction is now complete.

d. **DLJ Investment Partners II LP**: **Notice in Change of General Partner.** DLJIP II is a mature mezzanine (debt) fund in the ATRS private equity legacy portfolio. ATRS committed $80 million to the fund in 1999 and it has generated returns of 1.5x cost and an annual 10.5% IRR. ATRS' investment in the fund is valued at slightly over $900,000 in three investments. ATRS' interest represents approximately 5% of the fund. There are no management fees being charged at this time.

The general partner and manager are being assigned to Portfolio Advisors, LLC, a well-established and respected global private equity investor. The present DLJIP II management team will remain intact and there will be no change to fees and carried interest. Both Franklin Park and ATRS staff are comfortable with assignment of the general partner

e. **Notice of Bedlam Withdrawal as Global Equity Manager**. On Tuesday, November 12, 2013, ATRS received both verbal and formal written notice that Bedlam, a global equity manager, would no longer manage the ATRS portfolio. Bedlam had approximately $259 million under management. Prior to their notice, ATRS and HEK recommended termination of Bedlam due largely to loss of critical staff that included the leadership of the investment team. After Bedlam was notified of the pending termination recommendation, Bedlam made a decision to disband as an investment team and terminate its active management of global equity assets, including those of ATRS.

Since Bedlam voluntarily withdrew from management through the terms of the contract, no termination was necessary. All the assets managed by Bedlam are in an account at State Street and all assets are held in the name of ATRS. Bedlam no longer has authority to access the account or to execute any trades. The account is safe and secure at State Street Bank.

After notice and interaction with Dr. Abernathy, one of the two (2) transition managers that the Board has authorized ATRS to use, SSGM, a division of State Street, was chosen as the transition manager that offered the best execution and terms to ATRS for this transition. HEK requested a proposal from the two (2) procured transition managers with SSGM being the one that provided the best results for ATRS.

Both SSGA and BlackRock were contacted to make a transition bid. The mean expected cost estimates from the two transition providers are roughly the same. BlackRock estimated a mean expected cost of 44 bps and SSGM estimated a cost of 42 bps. SSGM has a lower investment management fee and also proposed to waive their investment management fee on the new assets for 3 months. BlackRock has a higher investment management fee and proposed to waive their investment management fee on the new assets for 2 months. Based upon the written recommendation of HEK, the executive director recommended to transition the Bedlam assets to SSGA and hire SSGM. SSGM responded the quickest to the bid proposal, has a lower investment management fee, and will waive the management fee for 3 months.

f. **Recommendation on BTG Pactual: Future Timberland Acquisitions for Diversification.** ATRS Board placed limitations on the remaining commitment to BTG Pactual's timberland fund. The approximate amount of $348 million represents approximately 2.7% of ATRS' total assets and is slightly above the target of the general 2% timber allocation as detailed in the Real Assets Investment Policy. The current Board approved policy requires reauthorization by the ATRS Board to lift the cap or authorization by the ATRS Board to make any purchases. In the current auction environment for timberland, it may be necessary to quicken the process for cap removal or grant purchase approval as BTG Pactual seeks to diversify the ATRS timberland portfolio while only acquiring the highest quality investments. ATRS requests the Board remove the requirement for a Board meeting to lift the cap or authorize purchases and replace it with two alternative means to allow a new purchase.

The first alternative is to allow BTG Pactual to add diversity to the portfolio using existing cash on hand and proceeds from the sale of current timberland investments to purchase other diversifying assets. These types of purchases would require ATRS staff approval after favorable notice to the ATRS Board Chair.

The second alternative would allow BTG Pactual use of the remaining commitment in cases of extraordinary opportunities. These opportunities would have to present the potential for above average returns and would require prior approval by ATRS staff and favorable notice by the ATRS Board Chair. Staff feels these alternatives would allow BTG Pactual the nimbleness needed in the current environment to continue to seek out diversifying properties and to seek enhanced returns for the timberland portfolio. It may also help to strategically move property out of the portfolio that has a lesser return profile in the future and replace it with greater opportunities.

Ms. Nichols *moved* to *approve* removal of requirements of a Board meeting to lift the cap for authorized purchases and allow BTG Pactual use of remaining commitment in case of extraordinary opportunities. Ms. Gram *seconded* the *motion*, and the Committee *unanimously approved the motion.*

g. **Authority to List and Sell Unoccupied Properties and Raw Land**. ATRS own buildings at 720 West Third managed by Colliers and 1512 West Third managed by Irwin Saviers Ballard. Both buildings are currently vacant. ATRS also owns parcels of raw, vacant land located in Chenal Valley (52.72 acres) and near the old Memorial Hospital site in North Little Rock (3 acres). These four properties are either raw land or hard to fill. All require expense to maintain with little upside expected. Disposal of these properties over time would be best. The proceeds of these assets could be redeployed in investments that offer the possibility of greater returns.

As ATRS property managers are attempting to lease the buildings, inquiries have been made as to potential purchase prices. Some interested parties are more interested in a sale or lease with the option to purchase than just a straight lease.

ATRS staff is requesting authority to offer the buildings for sale or in a lease with an option to purchase at appraised value or higher. The respective property managers would represent ATRS. Any sale less than the appraised value would be subject to ATRS Board approval.

In addition, ATRS staff is requesting authority to utilize property brokers to list and potentially sell the vacant land located in Chenal Valley and a vacant parcel in North Little Rock at appraised value or higher. ATRS staff requested authority to hire one of the existing three realty firms based on commission amount and experience. The selected firm would list the raw land properties and represent ATRS in marketing these parcels that currently have no property manager. Any sale for less than the appraised value would be subject to ATRS Board approval.

1. **Resolution 2013-38**

   Ms. Nichols *moved* to *adopt* Resolution 2013-38, Approving Authority to List and Sell Unoccupied Arkansas Properties and Raw Land. Dr. Kimbrell *seconded* the *motion*, and the Committee *unanimously approved the motion.*

h. **Fund of Opportunities Manager Search**. As the size of the ATRS trust fund has grown, the ability of ATRS to take advantage of the often enhanced returns from smaller more specialized opportunities can be diminished due to the size of the deal in comparison to the size of the ATRS trust fund. Often opportunities come from Arkansas firms that due to small size make it hard for the consultants to recommend. Recently, an Arkansas based private equity manager was seeking ATRS participation in Fund III since ATRS had been in Fund I and Fund II. ATRS staff has high regard for the team but the size of the $2.5 million commitment that was sought was among the factors that Franklin Park considered in not recommending this fund. Similar, smaller transactions are often brought to ATRS staff from all over the country that seem to have compelling results but often do not receive consultant recommendations due to the commitment size.

ATRS staff has been in discussions with Arkansas firms about becoming the fund of opportunities manager. It appears to be a strong likelihood that an Arkansas firm would be the best fit for a fund of opportunity manager. HEK and ATRS staff will begin the due diligence process on finding a new manager for this fund of opportunities and work on guidelines that would be set for the investment types. The ultimate target return for the fund of opportunities would be in the 8% to 15% range, depending upon the ultimate allocation of assets within the fund. It is expected the fund would have a mixture of private equity, real estate, loans, equity, and potentially bonds. If an Arkansas manager is located, it should also enhance the availability of deal flow from Arkansas.

B. General Investment Consultant Update – Hewitt EnnisKnupp.

1. **Portfolio Performance Update for the Quarter Ended September 30, 2013.** Mr. P. J. Kelly of Hewitt EnnisKnupp (HEK) presented the portfolio performance update for the third quarter ending September 30, 2013. The third quarter ended with $13.2 billion total market value, a $500 million increase from last quarter. The total fund had a return of 5.5% for the quarter ending September 30, 2013, outperforming its benchmark of 4.8%. ATRS ranked in the 15% percentile of similar sized pension plans across the U. S. US Global equity and fixed income outperformed the benchmarks for their asset classes.

2. **Portfolio Performance Update for the Month Ended October 31, 2013, Preliminary.** Mr. P.J. Kelly of Hewitt EnnisKnupp (HEK) presented the preliminary portfolio performance update for the Month ended October 31, 2013. The total fund had a return of 2.4% for month ending October 31, 2013, underperforming its benchmark of 2.6%.

3. **Recommendation to Terminate Western Asset Management Company, Arkansas Teacher Retirement System Core Full Discretion.** The recommendation of Hewitt EnnisKnupp and ATRS staff is for ATRS to terminate Western Asset Management Company, Arkansas Teacher Retirement System Core Full Discretion Account. Western Asset Management Company, Arkansas Teacher Retirement System Core Full Discretion Account is a fixed income manager that currently has approximately $422 million in ATRS assets under management for this account. The essential reason justifying the termination of Western Asset Management Company, Arkansas Teacher Retirement System Core Full Discretion Account is concerns regarding change in leadership and significant turnover within the

mortgage backed securities team at Western Asset. Hewitt EnnisKnupp and ATRS staff have followed the issue closely.

Several changes in upper management at Western Asset including the retirement of Steve Fulton, head of the agency mortgage-backed securities sector team, prompted the Fixed Income Manager Team at Hewitt EnnisKnupp to conduct several onsite visits over several months to assess the changes. During this process certain Western Asset Management product ratings were changed from hold or buy to review.

After several months of review, Hewitt EnnisKnupp and ATRS staff have been unable to achieve a comfort level with senior management of Western Asset and are concerned with the lack of stability of the mortgage backed securities platform. The result is a sell rating for Western Asset Management Company strategies that have historically held a meaningful allocation to mortgage backed securities. Proper experience in the area of mortgage backed securities is extremely crucial. In addition, Hewitt EnnisKnupp and ATRS staff recommended the assets in this Western Asset account be transitioned in a methodical manner at a point in the future using timing established by Hewitt EnnisKnupp, ATRS staff, and Western Asset Management Company to minimize transaction costs. P. J. Kelly will also address issues of timing on the termination and the latest Hewitt EnnisKnupp view of the risk in the fixed income portfolio due to the interest rate pressures. Additionally, P. J. Kelly will address the need to use the proceeds from both Western terminations in the future to readjust the fixed income allocations to be better positioned for the interest rate and inflation rate expectations over the next several years.

a. **Resolution 2013-39.**

   Ms. Nichols *moved* to *adopt* Resolution 2013-39 to Terminate Western Asset Management Company, Arkansas Teacher Retirement System Core Full Discretion Account. Mr. Stubblefield *seconded* the *motion*, and the Committee *unanimously approved the motion.*

4. **Recommendation to Terminate Western Asset Total Return Unconstrained Bond, LLC.** The recommendation of Hewitt EnnisKnupp and ATRS staff is to terminate the Western Asset Total Return Unconstrained Bond, LLC fund. Western Asset Total Return Unconstrained Bond, LLC is a fixed income fund managed by Western

Asset that currently has approximately $325 million of ATRS assets in the account.

This fund has also historically held a meaningful allocation to mortgage backed securities and is also recommended for termination by Hewitt EnnisKnupp and ATRS staff for reasons outlined above in item C. Additionally, Hewitt EnnisKnupp is recommending the assets in this Western Asset account be transitioned in a methodical manner at a point in the future using timing established by Hewitt EnnisKnupp, ATRS staff, and Western Asset Management to minimize transaction costs. P. J. Kelly will also address issues of timing on the termination and the latest Hewitt EnnisKnupp view of the risk in the fixed income portfolio due to the interest rate pressures. Additionally, P. J. Kelly will address the need to use the proceeds from both Western terminations in the future to readjust the fixed income allocations to be better positioned for the interest rate and inflation rate expectations over the next several years.

a. Resolution 2013-40.

Ms. Nichols *moved* to *adopt* Resolution 2013-40 to Terminate Western Asset Total Return Unconstrained Bond LLC. Mr. Black *seconded* the *motion*, and the Committee *unanimously approved the motion*

C. **Real Assets Investment Consultant Update – Hewitt EnnisKnupp.**

1. **2014 Pacing Schedule of $200 Million in Real Assets.** Chae Hong of Hewitt EnnisKnupp (HEK) presented the 2014 pacing schedule for real assets. For calendar year 2014. Hewitt EnnisKnupp is advocating approximately $200 million divided among value-added, opportunistic, and infrastructure real asset investments. These targets are subject to availability of quality investments and prevailing market conditions. Actual amounts may vary as pacing is subject to change over the year according to funding opportunities.

    a. **Value Added $30 Million.** These are funds that invest in properties and make improvements to fairly stable properties but are one step below the core funds in quality. These have slightly more risk but have a better return opportunity.

b. **Opportunistic $60 Million.** These are funds that seek to take advantage of distressed opportunities and are higher in the risk profile.

c. **Infrastructure $110 Million.** These are funds that invest in physical, operational systems and in monopolistic opportunities such as governmental functions (transmission line and toll roads).

Ms. Nichols *moved* to *approve* the 2014 Pacing Schedule of $200 Million in Real Assets. Mr. Stubblefield *seconded* the *motion*, and the Committee *unanimously approved the motion.*

D. **Private Equity Investment Consultant Update – Franklin Park**.

1. **2014 Private Equity Pacing Schedule.** Michael Bacine of Franklin Park presented the 2014 pacing schedule for private equity. Typically, ATRS has been pacing up to 2% of its underlying value for private equity for the next calendar year. Based upon assumptions of the projected market value of total assets for the next ten years, Franklin Park and ATRS staff recommend private equity pacing of $230 million dollars for 2014 in order to maintain a 10% allocation to private equity. The total pacing amount includes a $25 million allocation to the Franklin Park Venture Fund 2014, $25 million to the Franklin Park International Fund 2014, and $25 million to the Franklin Park Co-Investment Fund. Franklin Park also expects to commit approximately $25 million to a debt/distressed asset fund as well as a total of $130 million in four to six funds with buyout, growth equity or turnaround strategies. These targets are subject to availability of quality investments and prevailing market conditions. Actual amounts may vary as pacing is subject to change over the year according to funding opportunities.

a. Small/Mid Buyout/Growth/Turnaround $30 Million.

b. Small/Mid Buyout/Growth/Turnaround $25 Million.

c. Small/Mid Buyout/Growth Turnaround $25 Million.

d. Small/Mid Buyout/Growth/Turnaround $25 Million.

e. Debt/Distressed Assets $25 Million.

f. Debt $25 Million.

g. **ATRS Franklin Park Co-Investment Fund $25 Million.**

h. **Franklin Park International Fund 2014 $25 Million.**

i. **Franklin Park Venture Capital Fund 2014 $25 Million.**

Ms. Nichols *moved* to *approve* to 2014 Pacing Schedule of $230 Million in Private Equity Investments. Ms. Gram *seconded* the *motion*, and the Committee *unanimously approved the motion.*

2. **Recommendation to Commit up to $25 million in Franklin Park Venture Fund 2014.** This is the traditional annual Franklin Park Venture Fund. Franklin Park acts as the manager of a fund of funds in the venture space, since venture is a very volatile segment of private equity. In order to offset some of that risk, Franklin Park acquires an interest in several venture funds and spreads those through its investors to create greater diversity of managers and styles. Franklin Park does not charge a fee on the investment and only recovers its legal costs and accounting costs for ensuring the fund is set up properly and has appropriate accounting and auditing performed. This is a big win for Franklin Park's clients due to the availability of a fund of funds without the fee on fee cost that a fund of funds typically requires. Franklin Park recommends ATRS commit approximately ten percent of the pacing amount or up to $25 million dollars to the 2014 Franklin Park Venture Fund.

   a. **Resolution No. 2013-41**

   Ms. Nichols *moved to adopt* Resolution 2013-41, Approving Franklin Park Venture Fund 2014, L.P. Ms. Gram *seconded* the *motion*, and the Committee *unanimously approved the motion.*

3. **Recommendation to Commit up to $25 million in Franklin Park International Fund 2014.** The International Fund has essentially the same model as the venture fund, except it is a vehicle for ATRS to get exposure to international private equity. Franklin Park created a fund of funds vehicle to invest in several private equity funds that invest internationally. The fund of funds is used to diversify and reduce risk

for ATRS and the other clients of Franklin Park. Franklin Park charges no fee and only recovers the cost for legal and accounting required to properly operate the fund. This provides ATRS with diverse international private equity opportunities that otherwise would be difficult to obtain. Franklin Park recommends an ATRS commitment to the Franklin Park International Fund of up to $25 million dollars for 2014.

a. **Resolution 2013-42**

Ms. Nichols *moved to adopt* Resolution 2013-42, Approving Franklin Park International Fund 2014. Mr. Knight *seconded* the *motion*, and the Committee *unanimously approved the motion.*

4. **Recommendation for an Additional Commitment up to $25 million in Franklin Park Co-Investment Fund.** ATRS began investing in private equity co-investments during 2012. As of this time, the ATRS Board has authorized total commitments of $45 million to the Franklin Park Co-Investment Fund and $29.2 million of that amount has been invested in six co-investments. Presently, three additional co-investment opportunities are under review by Franklin Park.

A co-investment occurs when ATRS invests directly in a private company alongside a private equity manager. Co-investments usually are fairly limited to just private equity. Co-investments are typically not available in a public equity setting since ATRS has managers to directly purchase stocks and other securities in a liquid market. The benefit of private equity co-investment for ATRS is that Franklin Park as the fund manager does not charge management fees or any incentive fees that are also called "carried interest" or "carry". Therefore, the potential for return on co-investments is much greater since no fees are netted from the investment. As with the venture and international funds, Franklin Park does not charge a fee on the co-investment fund and only recovers its legal costs and accounting costs for ensuring the fund is set up properly and has appropriate accounting and auditing performed.

The Franklin Park Co-Investment Fund in which ATRS is currently invested is exclusive to ATRS and Franklin Park. ATRS is the sole limited partner and Franklin Park is the general partner with a 1% ownership interest in the fund. Due to the new appetite of its other clients for co-investments, the firm is instituting a second co-investment fund and will make a small investment in this fund as well. ATRS will not participate in the new co-investment fund but rather use the existing ATRS co-investment fund. The new fund is expected to invest approximately $20 million per year, similar to the ATRS co-investment fund. In the new fund, Franklin Park will be entitled to management fees as well as carried interest and clients will not have the advantage of the more favorable terms that ATRS has in our separate account type of co-investment fund. Staff is comfortable that this new fund will not materially compete with our existing fund due to the fact that Franklin Park will be making investments in both funds on a pro-rata basis.

Franklin Park recommends that ATRS commit up to an additional $25 million to the Franklin Park Co-Investment Fund in order to allocate ten percent of the annual pacing amount to co-investment opportunities.

a. **Resolution 2013-43**

Ms. Nichols *moved to adopt* Resolution 2013-43, Approving Additional Allocation to Franklin Park Co-Investment Fund 2014, L.P. Ms. Coleman *seconded* the *motion*, and the Committee *unanimously approved the motion.*

5. **Recommendation to Commit up to $25 million in Altas Capital Resources II, LP (a Turnaround Fund) Using Imminent Need.** Atlas is a Greenwich, Connecticut based firm that makes turnaround investments in small and middle market companies undergoing financial or operational distress. The fund will primarily make acquisitions through pre-bankruptcy restructurings, bankruptcy purchases and corporate carve outs of U.S. based companies. The general partner was founded in 2002 and had made eight investments in individual deals before forming its first fund in 2010. The aggregate performance of both the individual deals and the first fund is exceptional generating a 76.3% IRR.

   A turnaround strategy is difficult and time intensive, and there are few high quality competitors in this type of private equity. Because of its expectation to make a profit, Atlas will be entitled to increase its carried interest from 20% to 25% if cumulative distributions to partners represent 2.5 times or more of aggregate capital contributions. This is a trend that we are seeing more often among very high quality private equity managers that implement labor intensive strategies   Because of its proven ability to execute turnaround deals, Atlas is expected to yield excellent net returns despite the high carried interest rate.

Franklin Park recommends an investment of up to $25 million in Atlas Capital Resources II, LP. Due to the fact that the only closing for this fund is expected before the next scheduled meeting of the Arkansas Legislative Council on December 20, 2013, Imminent Need is requested.

a. Resolution 2013-44.

Ms. Nichols *moved to adopt* Resolution 2013-44, Approving Atlas Capital Resources, II, LP Using Imminent Need. Ms. Coleman *seconded* the *motion*, and the Committee *unanimously approved the motion*

XIII. **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. The Operations Committee had the opportunity to discuss potential rule or law changes. No additional discussion was made.

B. Potential Legislation.

1. Addressing Multiple Employer Voluntary Retirement Incentive Plans. Mr. Hopkins explained ATRS has seen an escalation in the number of school districts that are offering voluntary multiple employee incentive packages to encourage experienced teachers to retire. He explained a typical program is for the school district to agree to pay an extra $5,000 to a participant in return for the teacher agreeing to retire from the school district. If a teacher begins receiving these payments in the 29th and 30th year of service, and the teacher is totally contributory, then if the teacher retires with 30 years of service, the teacher's final average salary is increased $3,333. That additional final average salary provides an extra $2,150 annually ($180 per month) to the retirement benefit of the teacher. ATRS would have received $2,000 in total contributions which means ATRS received less than 1 year of the enhanced benefit in contributions. Mr. Hopkins told the Board he felt this was something that was worth discussing.

The Board also discussed the issue regarding disability retirees providing information on returning to work for non ATRS employers. ATRS currently has no way of knowing if a member receiving disability retirement benefits from ATRS goes to work for a non ATRS employer. It was recommended to draft a law or rule that would require disability retirees to provide necessary information on outside income other than disability benefits. The Board asked Mr. Hopkins to begin work on such law or rule.

C. **Update on Cash and Savings Help (CASH) Program.** Mr. Hopkins updated the Board on the Cash and Savings Help (CASH) program. Act 606 of 2013, also known as the discount buyout plan, allows the ATRS Board to establish a voluntary buyout plan for inactive vested members of ATRS. If a member elects to receive a one-time lump sum payment under the CASH plan, all service credit and benefit rights in ATRS are forfeited.

Any buyout plan is developed by Board rules and regulations. The first buyout plan applies only to inactive noncontributory vested members. Rule 16 was first approved by the Board July 26, 2013, and became effective November 12, 2013. The calculation for the buyout was developed in conjunction with the ATRS actuaries as follows:

$monthly benefit payable x actuarial factor for age x 30%

The CASH program will end June 30, 2014, unless extended by Board resolution. Letters were mailed to approximately 5,600 eligible members as soon as the rules became effective in November. To date, ATRS has received approximately 800 applications and the first set of payments will be going out on December 6, 2013.

D. **Possible Solution for Disability Retirees Who Return to Work for Non ATRS Employers.** Mr. Hopkins stated that ATRS staff was asked to provide possible solutions to the issue of ATRS disability retirees working for non ATRS employers, and the bad perception of this practice. ATRS staff researched the number of disability retirees as of October 2013 that would have less than 28 years of service credit or be less than age 60. The number was just over 700 disability retirees that would have disability cancelled if they returned to work for an ATRS employer. Mr. Hopkins stated that currently the staff has no way to monitor if the disability retirees return to work for a non ATRS covered employer. Mr. Hopkins discussed a possible "random sample" to be done for members to provide additional documents regarding employment. The Board asked that staff draft legislation or draft a rule authorizing ATRS to request various proofs of income such as income tax returns, or medical reports on disability retirees. Staff will present appropriate drafts at the next Board meeting.

E. Proposed Board Policy Change

1. **Rule 7-1 Calculation of Final Average Salary**. Mr. Hopkins presented a draft of the proposed change to Rule 7-1. The proposed rule is tailored to only reach payments made as early retirement incentives in return for separation of employment/retirement by the member, and expressly allows general bonuses, payment of sick leave, and other regular payments to members to be counted as salary. The Board obtained authority in the last session to address these kinds of salary issues by defining "salary" as needed. The proposed rule shows how it would look in the official rules of ATRS.

Mr. Lester *moved* to *approve* rule change to Rule 7-1, both emergency rule making process and official rulemaking process. Mr. Black s*econded* the *motion*, and the Committee *unanimously approved the motion*

XIV. **Staff Reports.**

A. **Medical Committee Reports.** Michael Ray presented the Medical Committee reports for October 2013 and November 2013. In October 2013, there were 20 applicants and 20 were approved. In November 2013, there were 5 applicants, 4 were approved, and one needed more information.

Ms. Nichols *moved* to *approve* the October 2013 and November 2013 Medical Committee reports. Ms. Clayton *seconded* the *motion*, and the Board *unanimously approved the motion.*

B. **Financial Reports.**

1. **Financial Statement Report.** Mitzi Ferguson gave the Board a summary for the financial reports for the year ending June 30, 2013. Plan net assets increased 11.72% or 1.345 billion for fiscal year 2013. This is a result from returns on ATRS investments which improved by $1.8 billion.

2. **Travel Report**. Ms. Ferguson presented the travel report showing the expenses for staff and Trustees for fiscal year ending June 30, 2013. Both Board and Senior Staff travel expenses decreased in 2013 as compared to fiscal year 2012. Other staff travel increased during 2013 due to Counselors being able to visit more schools than in 2012.

C. **Contract Review.** Rod Graves presented the Board with a list of contracts which is reviewed by ATRS Board annually.

Mr. Knight *moved* to *approve* all current Contacts and authorize Staff to prepare the annual contracts and send to vendors for completion. Ms. Nichols *seconded* the *motion*, and the Board *unanimously approved the motion.*

D. **Personnel Report**. Vicky Fowler presented the Board with the annual personnel report. For the first year of the current biennium (July 1, 2013 through June 30, 2015), ATRS will have 101 positions to be filled. Currently, 81 of the positions are filled, and 21 are vacant. Of the vacant positions, 4 are advertised at this time. For the fiscal year that ended June 30, 2013, ATRS spent $503.34 in overtime salary. This compares to $2,700.84 for the fiscal year ended June 30, 2012. From July 1, 2013 through November 2013 there were 938 Applications received, 38 Interviews, 5 new hires, 3 promotions, 1 transfer, 5 terminations and 21 Vacancies (4 posted, 3 pending interviews and 1 offered).

XV. **Executive Session to Discuss Executive Director's Performance Evaluation.** Chair, Dr. Abernathy, called the Executive Session of the Board of Trustees to order at 2:14 p.m.

Dr. Abernathy, Chair, reconvened the Board of Trustees meeting at 2:20 p.m.

The Board expressed their satisfaction with Mr. Hopkins and praised him for his hard work and dedication to ATRS and its members.

Mr. Lester *moved* to *approve* Mr. Hopkins' current employment contact and provide the maximum salary as allowed by law. Mr. Knight *seconded* the *motion*, and the Board *unanimously approved the motion.*

XVI. **Other Business.**

XIX. **Adjourn.**

Ms. Nichols *moved to adjourn* the Board of Trustees Meeting. Ms. Clayton *seconded* the *motion*, and the Board *unanimously approved the motion.*

Meeting adjourned at 2:22 p.m.

George Hopkins,
Executive Director

Dr. Richard Abernathy, Chair
Board of Trustees

Tammy Porter,
Recorder

Date Approved