The Arizona State Retirement System (ASRS) Board met in the 10th Floor Board Room of the ASRS Office, 3300 N. Central Avenue, Phoenix, Arizona 85012.

Mr. Tom Manos, Vice-chair of the ASRS Board, called the meeting to order at 8:30 a.m.

The meeting was teleconferenced to the ASRS office at 4400 E. Broadway, Tucson, Arizona 85711.

1. Call to Order; Roll Call; Opening Remarks

Present: Mr. Tom Manos, Vice-chair
         Mr. Clark Partridge (Via teleconference)
         Mr. Jim Hillyard
         Mr. Michael Miller
         Mr. Rene Guillen

Excused: Mr. Kevin McCarthy, Chair
         Mr. Michael Lofton

Two vacant positions.

A quorum was present for the purpose of conducting business.

2. Approval of the Minutes of the February 23, 2018 Public Meeting of the ASRS Board.

Motion: Mr. Michael Miller moved to approve the minutes of the February 23, 2018 Public Meeting of the ASRS Board. Mr. Jim Hillyard seconded the motion.

By a vote of 5 in favor, 0 opposed, 0 abstentions, 2 excused, and 2 vacancies, the motion was approved. The Trustee votes were as follows:

   Mr. Kevin McCarthy – excused
   Mr. Tom Manos – approved
   Mr. Clark Partridge – approved
   Mr. Jim Hillyard – approved
   Mr. Michael Lofton – excused
   Mr. Michael Miller – approved
   Mr. Rene Guillen – approved
3. Presentation, Discussion, and Appropriate Action Regarding the ASRS 2018 Legislative Initiatives and Legislative Update

Ms. Jessica Thomas, Government Relations Officer, introduced the topic by stating that four legislative items were approved for the 2018 Legislative agenda. Ms. Thomas provided an update on the following ASRS legislative initiatives:

HB2080 ASRS Investments Contracts - At the request of the ASRS, this Bill was held in Committee due to concerns regarding recommended amendments made by some of the representatives of the Committee that the ASRS felt needed to be vetted. It will not be moving forward in this legislative session.

HB2034 Social Security State Agency Designation – Regarding the state social security administrator duties, it was not determined which state agency may be assigned. The ASRS will work with stakeholders and other agencies to transfer these duties as necessary. This Bill passed through the House and Senate and was signed by the Governor on March 27, 2018.

HB2035 Deferred Compensation Plans – This Bill regarding the Governing Committee for Deferred Compensation Plans passed through the House and Senate and was signed by the Governor on March 29, 2018.

SB1054 ASRS Nonparticipating Employers - This Bill passed through the House and Senate and was signed by the Governor on April 12, 2018.

4. Presentation, Discussion, and Appropriate Action Regarding the ASRS Investment Program Updates

Mr. Karl Polen, Chief Investment Officer, opened the topic by providing the Board with a market update and reported that the Fund’s current return for the year is approximately 8% with a market value of approximately $39.6 billion.

The stock market continues to be volatile and ASRS maintains a slight underweight in equities. ASRS is also underweight in core bonds in light of rising interest rates. These underweights are balanced by overweights in cash and credit.

Mr. Polen reviewed the ASRS strategic acquisition of Mill Creek Residential Trust, an operator and builder of apartment communities with fourteen offices across the United States. This acquisition will provide expertise in a key sector for investment as well as offers superior access to deal flow. By investing directly, this no-fee no-carry investment enables Mill Creek to be an asset manager in a separate account, with effectively half of any profits coming to the ASRS. Mr. Rene Guillen requested a periodic update of this unique investment.

Mr. Polen reported preliminary results for March 31, 2018, noting that these are estimates based on 95% of data returned. Mr. Polen reported the Total Fund’s performance for the past twelve months was approximately 11.5%, outperforming its benchmark by about 90 basis points (bps). Over the last ten years, that outperformance has resulted in a 7.2% return, and roughly $3 billion has been added to the Fund. Performance outcomes are consistent with the report of last month.

Mr. Polen reviewed the risk report, noting estimated volatility or standard deviation of the portfolio is slightly over 13%, slightly lower than the Strategic Asset Allocation (SAA). Mr. Polen then reviewed
current Investment Management Division (IMD) projects, including the completion of an ongoing review of the SAA. A special Investment Committee meeting will be held on May 21, 2018, and recommendations from that meeting will be presented to the Board in the June 29 Board meeting. Other projects included Staff’s continuing work on improving performance measurement methods and major changes to the custody system, implementing improvements to middle office procedures.

Mr. Tom Manos commended Mr. Polen and the IMD regarding the new reporting format, indicating it is the right balance of performance and activity. Mr. Manos also agreed with Mr. Guillen’s earlier request concerning updates to the Board regarding the relationship with Mill Creek Residential Trust. Mr. Manos left it to Mr. Polen to decide on the appropriate timing of the updates. Mr. Polen agreed.

5. Presentation, Discussion, and Appropriate Action Regarding the Retrospective Rate Agreement (RRA) Distribution Methodology and the Strategic Health Insurance RRA Management and Distribution Policy

Mr. Paul Matson, Director, opened the discussion by expressing his appreciation to the Board for their patience while the ASRS worked through the issues presented as they worked toward implementation of prior Board decisions regarding the RRA distribution. Mr. Matson indicated he feels staff has developed a better product which will allow for a greater distribution to retirees. Mr. Matson provided a brief overview of the RRA to the Board and summarized the prior issues encountered. As the first policy recommendation was beginning implementation, additional research which included an enhanced statutory and tax review revealed several additional considerations concerning a cash distribution of RRA funds. Staff then determined that a partial-year ‘premium reduction’ would be more appropriate, and this amended policy to disburse RRA funds in the form of a six-month ‘premium reduction’ to eligible members with the goal of distributing the RRA corpus over a period of four years was presented to and approved by the Board. As staff began to work toward implementation of the second approved recommendation, several obstacles were uncovered including potential system constraints within our own system as well as third party systems with maintaining two rates in a single plan year and properly processing and accounting for adjustments that cross plan rates within a single year for those eligible members. Staff is now recommending a modification to the policy to reduce premiums throughout the entire plan year for all covered members in eligible plans.

The benefits of such a modification are:

1. Reduction of variability in member’s net benefit caused by different premium levels throughout the year
2. Mitigation of risks associated with maintaining two plan rates within a single plan year
3. Simplification and improved clarity of communications with members
4. Reduction of the substitution effect related to Health Benefit Supplement distributions.

The revised recommendation is designed to:

1. Allocate either 50%, or 33 1/3%, or 25% of the existing corpus of the RRA account, and 100% of future RRA receipts annually such that the RRA account is expected to be exhausted in approximately two, or three, or four years
2. Reduce health insurance premiums each full year beginning in January 2019 and continuing for the full year each subsequent year
3. Benefit all members who are enrolled in an eligible plan in each month premiums are reduced
Mr. Matson reviewed the memo attachments in detail, and indicated that staff’s recommendation is a three year distribution period, which would minimize the substitution effect and allow more immediate benefits to participants. Mr. Matson also recommended that the distribution occur over 12 months rather than less than 12 months in order to avoid significant administrative hurdles, and minimize the possibilities for error. Finally, Mr. Matson recommended that all retirees participate in the same reduced rate. The plan as described would take effect in January 2019.

Mr. Miller asked how this would be communicated to the members, and Mr. Matson said that a draft communication is already being planned. Additionally, it would be posted to the website and included with enrollment information, as well as through a retiree publication. Mr. Miller also asked if there would be two different rates, one for new retirees and another for existing retirees. Mr. Matson answered that the recommendation is to offer the same lower rate to both groups.

Mr. Manos thanked Mr. Matson for the presentation and agrees a better plan has been presented because of the more thorough review. Mr. Manos also agreed the 3-year option made more sense.

Mr. Miller had a final question and asked for a clarification of the reduction difference in member participation in health insurance between the 2-year, 3-year, and 4-year periods documented in the attachments. Mr. Matson explained that the further you go down the page, the smaller the reduction will be to the health insurance premium, and as a result the member would be more able to participate in the health insurance supplement.

Motion: Mr. Jim Hillyard moved to approve the Revised “Retrospective Rate Agreement (RRA) Management and Distribution” Strategic Health Insurance Policy, and the Revised “Retrospective Rate Agreement (RRA) Background, Options and Distribution Methodology” Paper, with a three year distribution of the current RRA account balance, and an annual distribution of future generated RRA funds, in order to reduce future health insurance premiums. Mr. Rene Guillen seconded the motion.

By a vote of 5 in favor, 0 opposed, 0 abstentions, 2 excused, and 2 vacancies, the motion was approved. The Trustee votes were as follows:

- Mr. Kevin McCarthy – excused
- Mr. Tom Manos – approved
- Mr. Clark Partridge – approved
- Mr. Jim Hillyard – approved
- Mr. Michael Lofton – excused
- Mr. Michael Miller – approved
- Mr. Rene Guillen – approved

Mr. Matson took a moment to acknowledge Mr. Brian Crockett, Sr. Strategic Planner, who had a key role in this project.

6. Presentation, Discussion, and Appropriate Action Regarding the Operational and Fiscal Status of the ASRS and its Programs

Mr. Manos noted that the Board has the option of entering into executive session during this presentation as deemed appropriate. Mr. Matson advised that he didn’t feel it would be necessary to discuss this topic in executive session. The primary concern was regarding confidential security documents included in the materials. If the Trustees wanted to discuss those documents in more
detail the decision could be made at that time to move into executive session. Mr. Matson presented his objectives:

1. For the Trustees to have a sense of the Director's overall opinion on how the Fund is doing;
2. To create a dialogue so he has a better sense of the priorities of Board members by the questions asked; and
3. To preface all (Trustees, senior management team, the Director himself) for upcoming strategic planning.

Mr. Matson reviewed the scorecard and provided an overview of the Director's perspective on the current organizational and financial status of the ASRS and its programs using the following categories:

1. Governance
2. Operational Risk Management
3. Financial
4. Investment Management
5. Actuarial
6. Information Security
7. Operational Cost Effectiveness
8. Customer Service
9. Operational Sustainability

Mr. Miller noted that this was the best information he has received about the functions and details of the ASRS operations. Mr. Miller then expressed his appreciation. Mr. Guillen added his appreciation and expressed his desire to increase his knowledge of investments. Mr. Guillen commended Mr. Matson and his leadership team regarding employee engagement results. Mr. Hillyard concurred, and added that he would like to know more about the operational stability category, most notably succession planning, and the customer service domain, particularly the employer engagement survey. Additionally, how the ASRS is marketing itself to new state employees to ensure that they understand the importance of their contributions to the ASRS and benefits of the Defined Benefit Plan. Mr. Manos also concurred and expressed an interest in knowing more about succession planning. He further indicated he would like to know more about the senior staff and hopes they will have more involvement in future presentations. Mr. Guillen added he would be interested in the ASRS marketing plan and expressed his concerns about the changing workforce in public service.

7. Notification of Upcoming Board Elections to Occur at the June 29, 2028 Board Meeting

Mr. Tom Manos announced the upcoming Board elections to occur at the June 29, 2018, Board Meeting.

8. Presentation, Discussion, and Appropriate Action Regarding Director's Report as well as Current Events

Mr. Paul Matson stated he had nothing further to add regarding the Director's Report, but would answer any questions the Board may have regarding the report; there were none.
9. Presentation and Discussion Regarding Informational Updates from Prior and Upcoming Committee Meetings

a. Operations, Audit and Legislative Committee (OALC)

Mr. Clark Partridge announced the next OALC meeting will be held on July 11, 2018.

b. Investment Committee (IC)

Mr. Clark Partridge announced the next regularly scheduled IC meeting is to be held on June 22, 2018. There is also a special meeting to be held in the third week of May.

c. Appeals Committee (AC)

Mr. Tom Manos announced the next AC meeting is scheduled to be held on June 12, 2018.

10. Board Requests for Future Agenda Items

Ms. Jothi Beljan asked for suggestions from the Board of topics they would like covered in an upcoming Fiduciary Training session, suggesting fiduciary law or a review of selected Arizona pension cases.

11. Call to the Public

A member of the public, Mr. Joe Geusic, requested to address the Board.

Mr. Geusic introduced himself stating he’s an advocate of the entire K-12 education system. Mr. Geusic made general comments with regard to his appreciation for Director Matson’s recent presentations at the Capital, especially the Director’s address to the House of Representatives. He also expressed concerns regarding the rising contribution rates and provided an example of the financial impact for one school district.

12. The next regular ASRS Board meeting is scheduled for Friday, June 29, 2018 at 8:30 a.m., at 3300 N. Central Avenue, 10th Floor Board Room, Phoenix, Arizona.

Mr. Manos noted the next Board meeting is scheduled for Friday, June 29, 2018 at 8:30 a.m.

The Board took a recess from 9:53 a.m. to 10:05 a.m. to transition to the 14th floor conference room for the final agenda topic and executive session.

13. Presentation, Discussion, and Appropriate Action Regarding the 2017 Review of the Director of the ASRS

Motion: Mr. Tom Manos moved to go into Executive Session for the purpose of the Director’s review. Mr. Guillen seconded the motion.

By a vote of 5 in favor, 0 opposed, 0 abstentions, 2 excused, and 2 vacancies, the motion was
approved. The Trustee votes were as follows:

- Mr. Kevin McCarthy – excused
- Mr. Tom Manos – approved
- Mr. Clark Partridge – approved
- Mr. Jim Hillyard – approved
- Mr. Michael Lofton – excused
- Mr. Michael Miller – approved
- Mr. Rene Guillen – approved

The Board convened to Executive Session at 9:53 a.m.

14. Adjournment of the ASRS Board

Mr. Manos adjourned the April 27, 2018, public meeting and executive session of the Board at 10:39 a.m.

Respectfully Submitted by:

Joyce Williams
Board Administrator
ARIZONA STATE RETIREMENT SYSTEM