

**MINUTES OF A PUBLIC MEETING OF THE
ARIZONA STATE RETIREMENT SYSTEM
OPERATIONS, AUDIT & LEGISLATIVE COMMITTEE**

**Wednesday, January 13, 2021
2:30 p.m., Arizona Time**

A quorum of the Operations, Audit & Legislative Committee (OALC) of the Arizona State Retirement System (ASRS) met telephonically in public session.

Mr. Clark Partridge, Chair of the OALC, called the meeting to order at 2:33 p.m.

1. Call to Order; Roll Call; Opening Remarks

Present: Mr. Clark Partridge, Chair
Mr. Tom Manos, Vice-chair
Mr. Rene Guillen (joined the meeting at 2:37 p.m.)

A quorum of the Committee was present for the purpose of conducting business.

Mr. Clark Partridge, Chair, welcomed the attendees and thanked the staff for their hard work and preparation for the meeting.

Ms. Gloria Montiel, ASRS Committee Administrator, provided all attendees with telephonic meeting guidelines.

2. Approval of the Minutes of the October 14, 2020, Public Meeting and Executive Sessions of the OALC

Motion: Mr. Tom Manos moved to approve the Minutes of the October 14, 2020, Public Meeting of the OALC. Mr. Rene Guillen seconded the motion.

By a roll call vote of 3 in favor, 0 opposed, 0 abstentions, and 0 excused, the motion was approved. The Trustee votes were as follows:

Mr. Clark Partridge – approved
Mr. Tom Manos – approved
Mr. Rene Guillen – approved

Motion: Mr. Tom Manos moved to approve the Minutes of the October 14, 2020, Executive Sessions of the OALC. Mr. Rene Guillen seconded the motion.

By a roll call vote of 3 in favor, 0 opposed, 0 abstentions, and 0 excused, the motion was approved. The Trustee votes were as follows:

Mr. Clark Partridge – approved
Mr. Tom Manos – approved
Mr. Rene Guillen – approved

3. Presentation, Discussion and Appropriate Action Regarding Legislative Modifications to the Arizona State Governing Committee for Deferred Compensation Plans (Committee) and the ASRS Supplemental Deferred Compensation Plan(s), and Update on Pending non-ASRS Legislative Initiatives

Mr. Paul Matson, ASRS Director, turned the presentation directly over to Ms. Jessica Thomas, Government Relations Officer and Rules Writer.

Ms. Thomas presented to the Committee the proposed legislative recommendation and benefits of consolidating the Arizona (AZ) State Governing Committee for Deferred Compensation (DC) Plans and the ASRS Supplemental DC Plans. A part of the initiative would include automatic enrollment of all ASRS employers in the supplemental deferred compensation plans overseen by the ASRS. Ms. Thomas noted the consolidation would benefit the plans in that it would simplify administration, clarify participant eligibility, reduce duplicative bodies and processes, and ensure low manager and administration costs. She closed her discussion soliciting questions from the Committee and noted the staff's recommendation is to move the proposed legislative initiative to the Board for full approval.

Mr. Matson added additional commentary, explaining there are two key parts of the proposed legislative initiative. The first part is from the Arizona State Governing Committee for Deferred Compensation Plans (the Committee), which is not an ASRS body but is a separate Committee on which the Director is, per statute, a member. As part of the Committee's strategic initiatives in 2020, it was determined that policymakers should consider if it would be beneficial to have a consolidation of their plans with that of the ASRS for the reasons noted by Ms. Thomas. He noted the decision on where the consolidated assets of the plans would be housed would be determined by policymakers; however, there was a general consensus with the bill sponsor, Senator Livingston, and the Arizona Department of Administration that they would likely be housed with the ASRS. He further explained the reason the legislative initiative has come to the ASRS is due to both the Committee's limited resources needed to run legislation and the nature of the bill being retirement-related. The ASRS has previously assisted with managing a Committee bill in the past, primarily because of Mr. Matson's statutory role on the Committee, the retirement nature of the topic area, and the ability of the ASRS to manage a legislative process.

Mr. Matson noted the second part of the bill is the effective auto-enrollment of employers into the ASRS DC plans. Auto-enrolling ASRS employers into the ASRS DC Plans does not mean the employees will be required to participate, but it will give them the option through their employer.

Mr. Partridge inquired how contributions would be made to the ASRS if an employee opted to contribute to one of the plans offered.

Mr. Matson replied, stating the responsibility of remitting contributions to the ASRS on behalf of the employees would be facilitated by the employer.

Mr. Partridge further inquired on the integration process of the plans during the consolidation of the plans.

Mr. Matson noted the vendor would not change upon consolidation, and investment options in terms of asset classes would remain fundamentally the same. The only significant immediate change after a consolidation would be migrating the oversight of a program to a new body. The vendor would not change and would present to one body (likely the ASRS DC Committee) instead of two separate committees.

Mr. Matson further expanded on the potential integration of the investment options for the Committee and the ASRS DC Plans. Although the individual investment offerings are different in some areas, the philosophy is the same, whereby:

- Participants that are very active in managing their accounts can pick from the self-directed brokerage option, or
- Participants that are active in managing their accounts can pick from the available mutual funds in specific asset classes, or
- Participants that are less active can select from target-date funds to fit their expected retirement date, or
- Participants that are less active and want more participant-specific considerations can outsource their portfolios' construction decisions to Nationwide's investment ProAccount process.

Mr. Matson noted the main difference in the investment offerings between the two plans is the specific mutual funds offered. This difference is partly due to history, fund performance on review dates, Committee membership at different points in time, and the disruption that occurs when changes are made. Mr. Matson noted he is not recommending any changes to the investment options for at least approximately six months after a consolidation; however, at that time, the ASRS would likely review, analyze and proceed to either:

- Leave the specific investment options of the two plans unchanged
- Adopt the Committee investment offerings
- Adopt the ASRS's investment offerings
- Choose the best from each plan for a 'best of best' singular investment offering.

Mr. Partridge inquired on how the consolidation of the two contracts with Nationwide works.

Mr. Matson responded that the plans under the two bodies are now under the same contract with the State, except for the trust agreements, which are nonetheless very similar. When the current contract expires, and a new request for proposal process begins, consideration would be given

to the optimal number of separate plans. Fees for plans under both bodies are currently very low at 6 basis points or 0.06% of assets under management.

Mr. Manos inquired if the auto-enrollment applies to subdivisions, cities, and counties and if employers could optout.

Mr. Matson responded that the effective auto-enrollment would apply to all ASRS employers. His interpretation, along with that of Ms. Thomas, is that if an employee who meets the requirements wants to participate, the employer would have to facilitate their participation.

Mr. Manos suggested that Mr. Matson and Ms. Thomas contact the County Supervisors Associated and the League to let them know of the bill that will offer a 457 Plan that may be in competition with what they offer.

Mr. Matson thanked Mr. Manos for the idea and responded that they will certainly be contacted.

Mr. Matson also indicated that a key group that could benefit from this auto-enrollment concept will be certain K-12 employees who currently only have access to plans that have higher fees.

Additional discussions ensued.

Motion: Mr. Tom Manos moved to approve the recommendation of moving the legislative modifications of the AZ State Governing Committee and the ASRS Supplemental Deferred Compensation Committee to the full Board for approval at the next scheduled ASRS Board meeting. Mr. Guillen seconded the motion.

By a roll call vote of 3 in favor, 0 opposed, 0 abstentions, and 0 excused, the motion was approved. The Trustee votes were as follows:

Mr. Clark Partridge – approved
Mr. Tom Manos – approved
Mr. Rene Guillen – approved

Ms. Thomas continued her presentation to the Committee with an update of non-ASRS legislation. She advised the Committee House Bill (HB) 2138, which relates to the Board of Regents and specifically the Arizona State University in that they are requesting a change to Arizona Revised Statute (A.R.S.) § 15-1628 to address whether or not all of their employees, not just administrative staff and faculty, can now have the choice to choose between the ASRS and the Optional Retirement Plan (ORP). The main concern is that such a change would negatively impact the payments towards the ASRS based on those employees who choose to participate in the ORP rather than the ASRS. Based on estimates, the upper threshold of the impact if all current and future employees opted into the ORP would be approximately \$95 million in one year, with a lower threshold of \$14.3 million if all future employees opted into the ORP. Ms. Thomas closed her discussion inquiring if the Committee was interested in taking a position on the legislative initiative and, if so, if they would also like to give staff discretion to adjust the Board's position in the event the legislative language changes.

Mr. Matson provided additional commentary on the effects of such legislative changes. He noted the effects of the payments towards the UAAL would be due to less employee participation from both new and existing University employees who would potentially be given the option of opting out of the ASRS and into the ORP plan due to the change. This change would essentially mean less contributions being paid into the ASRS, which would, in turn, migrate the cost to remaining members of the ASRS due to less members paying down the UAAL. Specifically, the bill does not contain an Alternate Contribution Rate (ACR) for those who would choose to migrate to the ORP.

Mr. Guillen commented on the existing statutes, which allow the ASRS to bill employers who create liabilities by providing employees with retirement incentives to retire early.

Ms. Thomas responded that the statute in place for the provision noted by Mr. Guillen is covered under A.R.S. § 38-749, and the provision which relates to charging an unfunded liability to an employer who is no longer participating is housed under A.R.S. § 38-751.

Additional discussions ensued by the Committee with a general consensus that employers and members should not be given the option to opt-out. Specifically, a system cannot work when members can opt-out when the contribution rates are high and opt-in when contribution rates are low. The Fund must be kept whole from an actuarial perspective with provisions in place to ensure liabilities are not shifted to existing members at the expense of provisional changes such as the ones proposed by HB2138.

The Committee concluded the discussion noting A.R.S. § 38-751 should be evaluated with further legal consultation. The final decisions should then be presented to the full Board for approval on the issues raised and discussed during the agenda item.

4. Presentation, Discussion, and Appropriate Action Regarding the Internal Audit Quarterly Update

Mr. Harold Mackey reviewed the quarterly audit report with the Committee and provided the status of projects the Internal Audit Division (IAD) is currently working on. The Audit Team is currently in the processing of adding an additional staff member to their team. The goal is to attain a new member who has a great amount of institutional knowledge to assist the team with the agency's audit processes. Continuing education among Audit Team members is also ongoing to ensure the team is well rounded in their audit roles. Mr. Mackey also noted the team has been involved in the advisory aspect of their audit roles, as noted in the presentation provided to the OALC. The team has also been actively engaged in Asset Class Committee meetings of the ASRS to ensure their understanding of the ongoing investment strategies of the ASRS.

Mr. Mackey briefly reviewed the "Budget/Hours Allocation" slides.

Additional discussions ensued with Mr. Mackey soliciting questions from the Committee relating to his report.

Mr. Partridge inquired on the Public Safety Retirement System (PSPRS) data inquiry point of discussion and what it entailed.

Mr. Mackey responded, advising the Committee the Audit Team is currently monitoring PSPRS data to ensure ongoing collaboration with the ASRS in terms of their system processes and the transfer of information from one plan to another.

There were no further questions from the Committee.

5. Review of Recently Conducted Internal Audits

Mr. Mackey turned the review of the recently conducted audits over to Mr. Andrew Burch and Ms. Rosie Tomforde, ASRS Internal Auditors.

- Mr. Burch presented the PSPRS Health Insurance Premium Benefit Audit Report. The IAD had three findings. Management agreed with the findings and has either updated processes or is in the process of implementing corrections and updating processes.
- Ms. Tomforde presented the Complaints Handling Internal Audit. The IAD had two findings. Management agreed with the findings and made immediate updates.

6. Call to the Public

No members of the public requested to speak.

7. Presentation, Discussion, and Appropriate Action Regarding the ASRS Information Security Program

Motion: Mr. Tom Manos moved to go into executive session pursuant to A.R.S. § 38-431.03(A)(2) for the purpose of discussion or consideration of records exempt by law from public inspection. Mr. Rene Guillen seconded the motion.

By a roll call vote of 3 in favor, 0 opposed, 0 abstentions, and 0 excused, the motion was approved. The Trustee votes were as follows:

Mr. Clark Partridge – approved
Mr. Tom Manos – approved
Mr. Rene Guillen – approved

The Committee convened to Executive Session at 4:03 p.m.

The Committee reconvened to Public Session at 4:29 p.m.

Prior to moving on to Agenda Item #8, Mr. Partridge reminded all attendees of the executive session that discussions in executive session are required by law to be confidential and shall not be discussed with anyone outside of the executive session.

8. Requests for Future Agenda Items

None were requested.

9. The next regular public OALC meeting is scheduled for Wednesday, April 14, 2021, at 2:30 p.m.

Mr. Clark Partridge noted the next OALC meeting is scheduled for Wednesday, April 14, 2021, at 2:30 p.m.

10. Adjournment of the OALC

Mr. Clark Partridge adjourned the meeting at 4:30 p.m.

Respectfully Submitted,

Gloria Montiel
Committee Administrator
ARIZONA STATE RETIREMENT SYSTEM