



ARIZONA STATE RETIREMENT SYSTEM

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*Paul Matson
Director*

MINUTES PUBLIC MEETING ARIZONA STATE RETIREMENT SYSTEM BOARD

Friday, September 25, 2015
8:30 A.M., MST

The Arizona State Retirement System (ASRS) Board met in the 10th Floor Board Room, 3300 N. Central Avenue, Phoenix, Arizona. Mr. Kevin McCarthy, Chair of the ASRS Board, called the meeting to order at 8:30 A.M., Arizona Time.

The meeting was teleconferenced to the ASRS office at 7660 E. Broadway, Tucson, Arizona 85710.

1. Call to Order; Roll Call; Opening Remarks

Present: Mr. Kevin McCarthy, Chair
Mr. Jeff Tyne, Vice Chair
Mr. Tom Connelly
Professor Dennis Hoffman
Mr. Tom Manos
Dr. Richard Jacob
Mr. Robert Wadsworth

Absent: Mr. Clark Partridge

One vacant position.

A quorum was present for the purpose of conducting business.

2. Presentation Regarding PRIDE Award for Improvement

Mr. Anthony Guarino, Deputy Director and Chief Operations Officer, recognized the following nominees for the 2015 PRIDE Improvement award: Marcia Kumamoto and Mark Muraoka; John Doran; Rama Tripuraneni; MAC Action Committee – Judy Simpson, Randy Gray, Marcus Jones, Katie Daigneault, Kathy Palmer, Jan Cameli and Lorra Mizner; and TSD Project Management Team – Teresa Donohue, Brandon Heathcotte, Trent Kendall, Meskel Assefa, Sandy Wang, Megha Choudhari and Bhargavi Ravinuthala.

All were nominated by staff because they exemplify the following PRIDE qualities of improvement:

- Promote new ideas

- Solve problems
- Enhance outcomes or performance
- Improve relationships
- Enhance morale
- Increase efficiency, effectiveness or reduce costs

Mr. Guarino presented the PRIDE Award for Improvement to the award winner, Rama Tripuraneni.

3. Presentation Regarding Government Finance Officers Association (GFOA) Financial Reporting Awards

A. Comprehensive Annual Financial Report (CAFR) for Fiscal Year (FY) 2014

B. Popular Annual Financial Report (PAFR) for FY 2014

Mr. Guarino announced the ASRS has been recognized by GFOA for 26 consecutive years as recipient of the Comprehensive Annual Financial Report (CAFR) award. Mr. Guarino presented the 2014 award to Ms. Liz Rozzell, Controller. Ms. Nancy Bennett, Chief Financial Officer was unable to attend.

A Certificate of Achievement is presented by the GFOA to those government units whose annual financial reports are judged to adhere to program standards and represents the highest award in government financial reporting. The following staff were recognized for having a substantial part in the ASRS receiving the CAFR award: Nancy Bennett, Liz Rozzell, Erin Higbee, John Maczko, Tonia Nemecek, Debbie Motta, Rebecca Fox, Kristin Berry, Lupita Breland, Kerry White and Michael Copeland.

In addition, the ASRS also received the GFOA Award for Outstanding Achievement for the 2014 Popular Annual Financial Report (PAFR). Staff who had a significant part in the ASRS receiving the PAFR award was Nancy Bennett, Liz Rozzell, Erin Higbee, John Maczko and Rebecca Fox.

The GFOA established the PAFR Awards Program in 1991 to encourage and assist state and local governments to extract information from their CAFR to produce high quality PAFRs specifically designed to be readily accessible and easily understandable to the general public and other interested parties without a background in public finance and then to recognize individual governments that are successful in achieving that goal.

4. Approval of the Minutes of the August 28, 2015 Public Meeting and Executive Session of the ASRS Board

Motion: Prof. Dennis Hoffman moved to approve the Minutes of the August 28, 2015 Public Meeting and Executive Session of the ASRS Board. Mr. Tom Connelly seconded the motion.

By a vote of 7 in favor, 0 opposed, 0 abstentions, 1 excused, and 1 vacancy, the motion was approved.

5. Presentation, Discussion, and Appropriate Action Regarding the ASRS' Performance in the CEM Pension Benefit Administration Benchmarking Survey for the Period Ending June 30, 2014

Ms. Jan Hartford, Director of Pension Benefit Administration Benchmarking, CEM Benchmarking Inc., was present and provided the Fiscal Year (FY) 2014 results for the ASRS. Ms. Hartford explained how the peer comparisons are done, and also discussed how the ASRS ranks among its peers. CEM's analysis also explains how the ASRS can make improvements to its score.

The ASRS has participated in the CEM pension benefit administration benchmarking study since 2001. Each year, the ASRS submits data regarding service features, transaction volume, and costs and staffing, broken down by activity membership, and plan design. CEM compiles the results and provides a report detailing the cost effectiveness of the ASRS. Specifically, the report compares and contrasts:

- Peer Characteristics
- Service Levels
- Total Costs
- Cost by Activity
- Staff Costs and Productivity
- Transaction Volumes
- Complexity
- IT and Major Projects

Currently, the ASRS spends \$83 per member and annuitant which is below the peer average of \$99. Additionally, the ASRS' service score improved from 81 to 87 over the last four years. The outcome demonstrates the ASRS has a productive, low cost, and cost effective operation that provides high levels of service.

6. Presentation, Discussion, and Appropriate Action Regarding the ASRS Real Estate Strategic Plan Revisions

Mr. Gary Dokes, Chief Investment Officer, presented the modifications of the ASRS Real Estate Strategic Plan along with Mr. Karl Polen, Head of Private Markets Investing, and Mr. Allan Martin, Consultant, NEPC, who were present via teleconference to respond to questions from the Board.

The ASRS invests in real estate in accordance with a Real Estate Strategic Plan approved by the Investment Committee and the Board. This Strategic Plan was last updated in October of 2011. At its meeting on July 20, 2015, the Private Markets Committee reviewed and approved proposed changes to the Strategic Plan and recommended them to the Investment Committee (IC) on August 24, 2015. The recommended changes were approved by the IC and are now being recommended to the full Board for approval.

The proposed changes expand the separate account program to encompass a target of 75% of real estate assets. The separate account program is being expanded in order to pursue customized investment strategies, greater alignment of interest and enhanced control through partner of one structures and reduced fees. The proposed changes align the strategic plan with current risk management perspectives by updating the permitted property types and modifying

the risk categories to focus on objective and functional risks of property based on leasing status and life cycle stage. The proposed strategic plan maintains leverage targets in the 50% to 60% range, but measures leverage at the total portfolio level allowing some flexibility at the property level for fixed rate debt while constraining variable rate debt at lower leverage levels.

The ASRS real estate consultant has reviewed the revised plan, and has concluded it is appropriate and concurs in its adoption.

Motion: Mr. Tom Connelly moved to approve the ASRS Real Estate Investment Program Strategic Plan as presented. Dr. Richard Jacob seconded the motion.

By a vote of 7 in favor, 0 opposed, 0 abstentions, 1 excused, and 1 vacancy, the motion was approved.

7. Presentation, Discussion, and Appropriate Action Regarding ASRS Proposed Legislation for the 2016 Legislative Session

Mr. Klein introduced the topic by stating that during the summer of this year the External Affairs Division (EAD) received legislative suggestions from ASRS staff, third party administrators, and Trustees concerning federal statutory requirements; plan inefficiencies, inconsistencies, and inequities; administrative concerns; and others. The EAD researched and discussed each suggestion in conjunction with Trustees, Executive Management, and other internal staff. Staff first presented the legislative package at the September 11, 2015, External Affairs Committee (EAC) meeting. The EAC moved to recommend to the full Board approval of the legislative initiatives at its September 25, 2015 meeting. The EAC also discussed several changes to the member appeal process as a legislative initiative. Mr. Klein turned the discussion over to Mr. Nick Ponder, Government Relations Officer, who reviewed each of the seven ASRS legislative initiatives:

Session Law: Regarding employees who were not covered under the state Social Security Administration Agreement Section 218- The ASRS identified four (4) groups impacted by HB 2050 (2014), but one of the groups needed additional regulatory assistance. As a result, the ASRS submitted a Voluntary Correction Program (VCP) to the Internal Revenue Service (IRS) for those individuals who were, potentially, inappropriately enrolled in the ASRS, and whose accounts remain in the system because the legislature requested a moratorium on removing them. The ASRS received approval from the IRS and must get the approval language in session law to grandfather this group into the ASRS.

Mr. Ponder advised the Board that he will be requesting an emergency clause to ensure this is effective by August 31, 2016, in the event the legislative session hasn't closed by May 31, 2016.

A.R.S. § 38-797.10: LTD Disability Program, exempt from "bad faith" claims as it relates to Long Term Disability (LTD)- The ASRS would like similar protection from "bad faith" claims to ERISA plans. The initial language proposed during the 2015 legislative session provided greater protection than protections for private ERISA plans. Because this was not the intent, the ASRS has modified its proposed language. A concern was raised from legislative staff that this modification would violate the anti-abrogation clause in the Arizona Constitution (Article 18, Section 6). In response to that concern the ASRS sought analysis from an outside attorney who concluded it does not violate the anti-abrogation clause in the Arizona Constitution. The analysis was provided to legislative council who concurred with the outside attorney's analysis. Mr.

Ponder confirmed he also inquired with the legislative staff following the attorney and legislative council analysis and staff suggested to proposed the bill for the 2016 session.

A.R.S. § 41-005 Exemptions from Rulemaking- Historically, the ASRS has acted with the understanding that the ASRS has been exempt when acting on certain financial, actuarial or investment decisions which is not properly addressed in the rulemaking process. The ASRS would like to pursue language codified in statute to clarify that.

A.R.S. § 38-738(A): Relating to Employer Credits- The ASRS would like to codify in statute current practice as it relates to employer credits and interest charged on these credits under A.R.S. § 38-738.

A.R.S. § 38-738(B): Clarify the purchase of Contributions Not Withheld (CNW) service by members who are inactive, retired, or on Long Term Disability (LTD)- Currently, the statute refers to “members” as one group and suggests they can purchase service pursuant to A.R.S. § 38-747, which would include rollovers and payroll deduction agreements. The ASRS would like to propose added language to distinguish between those members who are active verses those who are inactive, retired, or on LTD to conform to federal requirements.

A.R.S. § 38-742(B): Purchase of Forfeited Service- Currently, the statute indicates a member must repay what was received in a refund, plus interest, in order to receive service credit for that period. It does not address the situation where, under a Domestic Relations Order (DRO), an ex-spouse may receive a portion of the member’s benefit that was assigned to the ex-spouse. The ASRS would like to propose language to clarify that the member must repay the total amount in order to receive the full amount of service credit, not only the portion received by the member.

A.R.S. § 38-714(E): Modifications to the ASRS Appeals Process- The ASRS would like to propose modifications to the appeal process to enhance the process for the ASRS Board and the Appellant. The following three options were proposed:

- A. Establish an Appeals Board that would hear appeal cases separate from the full Board.
- B. Eliminate the administrative appeal process and Board participation.
- C. Establish a Committee of the board with authority granted in statute to take legal action on appeals.

Mr. Ponder stated the recommendation from staff was Option C above and the Board agreed.

Mr. Ponder briefly apprised the Board of other expected legislative items that will not be initiated by the ASRS but could affect the ASRS.

Motion: Prof. Dennis Hoffman moved to approve the 2016 legislative initiatives as presented by staff, permit staff to make all language changes and negotiate as necessary to obtain the most effective and efficient legislative provision within the construct of today’s discussion. Mr. Jeff Tyne seconded the motion.

By a vote of 7 in favor, 0 opposed, 0 abstentions, 1 excused, and 1 vacancy, the motion was approved.

8. Approval, Modification, or Rejection of the Recommended Administrative Law Judge's Decision Regarding Mr. Robert Merritt's Appeal to Transfer Corrections Officer Retirement Plan Service Credit to the ASRS Based on a May 2008 Cost Calculation

Mr. Chris Munns, Assistant Attorney General, Solicitor General Section, was present via teleconference to provide legal advice to the Board, if requested.

Mr. Robert Merritt was not present.

Ms. Jothi Beljan, Assistant Attorney General, advised the Board that the ASRS did not receive notification from the appellant that he would be present. Ms. Beljan provided a brief summary of her position regarding Mr. Merritt's appeal to the Board. Ms. Beljan requested that the Board modify the Recommended Administrative Law Judge's Decision as follows:

1. Replace the phrase "Corrections Officers' Retirement Program" with the phrase "Corrections Officer Retirement Plan" in Finding of Fact No. 1 because A.R.S. § 38-882 establishes the Corrections *Officer Retirement Plan*.
2. Replace the date "January 14, 2015" with the date "August 8, 2014" in Finding of Fact No. 6 based on ASRS Exhibit G referenced in the Recommended Decision, footnote 5.
3. Correct the typographical errors in Conclusion of Law No. 3 mislabeling A.R.S. § 38-922 paragraph A as C and mislabeling paragraph B as D with the correct statutory paragraphs in A.R.S. § 38-922.

Motion: Dr. Richard Jacob moved to modify the Administrative Law Judge's Decision as requested by the ASRS to include amendments #1-3 as stated above. Mr. Tom Manos seconded the motion.

By a vote of 7 in favor, 0 opposed, 0 abstentions, 1 excused, and 1 vacancy, the motion was approved.

9. Presentation, Discussion, and Appropriate Action Regarding the 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.

Mr. Guarino requested to make a correction to an earlier statement he made regarding staff turnover. Mr. Guarino's earlier statement of staff turnover being under ten percent was as of July 15, 2015; however, as of August 31, 2015, the current rate is eleven percent.

10. Presentation and Discussion with Respect to Informational Updates from Prior and Upcoming Committee Meetings

a. Operations and Audit Committee (OAC)

Mr. Jeff Tyne announced the next OAC meeting will be held on November 10, 2015 at 10:30 a.m. in the 14th floor conference room to further discuss health care, external and internal audits and other developments and accomplishments.

b. External Affairs Committee (EAC)

Dr. Richard Jacob announced the October 9, 2015 EAC meeting will be cancelled. The next meeting will be held on November 13, 2015 at 10:30 a.m. in the 14th floor conference room and will provide an update on the legislative efforts to secure bill sponsorships and additional legislative issues that may arise, along with possible discussion of the ASRS' 2016 regulatory agenda as it pertains to administrative rule changes and additions the ASRS will request from the Governors Regulatory Review Council.

c. Investment Committee (IC)

Mr. Tom Connelly announced the next IC meeting will be held on October 26, 2015 at 2:30 p.m. in the 14th floor conference room. In addition a special Round Table event will be scheduled for this fall to discuss the impact of the end of Federal Reserve easing.

d. Ad Hoc Compensation Committee

Mr. Tom Manos announced all outstanding tasks have been completed; therefore, a future meeting of the Ad Hoc Compensation Committee has not been scheduled.

11. Board Requests for Agenda Items

No requests were made.

12. Call to the Public

No one from the public requested to speak.

13. The next regular ASRS Board meeting is scheduled for Friday, October 30, 2015, at 8:30 A.M., at 3300 N. Central Avenue, 10th Floor Board room, Phoenix, Arizona.

The public meeting was adjourned from the 10th floor Board Room at 10:23 a.m. and moved to the 14th floor conference room.

14. Presentation, Discussion, and Appropriate Action Regarding ASRS Actuarial Services

Motion: Dr. Richard Jacob moved to go into executive session to seek legal advice. Prof. Dennis Hoffman seconded the motion.

By a vote of 7 in favor, 0 opposed, 0 abstentions, 1 excused, and 1 vacancy, the motion was approved.

The Board convened to executive session at 10:35 a.m.

15. Presentation, Discussion, and Appropriate Action Regarding the Review of the Director and Employment Contract for the Director

The Review of the Director and Employment Contract was not heard and will be presented at the October 30, 2015 Board meeting.

16. Adjournment of the ASRS Board

Mr. McCarthy adjourned the public meeting and executive session at 11:10 a.m.

ARIZONA STATE RETIREMENT SYSTEM

Melanie A. Alexander
Board Administrator

Paul Matson
Director