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. Kevin McCarthy, Chair of the ASRS Board, called the meeting to order at 8:31 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. Kevin McCarthy, Chair
Mr. Tom Manos, Vice-chair
Mr. Clark Partridge
Mr. Jim Hillyard (Joined the meeting at 8:34 a.m.)
Mr. Michael Lofton
Mr. Michael Miller

Absent: Mr. Rene Guillen

Two vacant positions.

A quorum was present for the purpose of conducting business.

2. Approval of the Minutes of the August 25, 2017 Public Meeting of the ASRS Board.

Motion: Mr. Michael Miller moved to approve the minutes of the August 25, 2017 Public Meeting of the ASRS Board. Mr. Kevin McCarthy seconded the motion.

By a vote of 6 in favor, 0 opposed, 0 abstentions, 1 excused, and 2 vacancies, the motion was approved.

Mr. Jim Hillyard joined the meeting at 8:34 a.m.

3. Presentation, Discussion, and Appropriate Action Regarding ASRS Legislative Initiatives and Legislative Update
Ms. Jessica Thomas, Government Relations Officer, introduced the topic by stating that during the summer of this year the ASRS received legislative suggestions from ASRS staff, third party administrators, and Trustees concerning federal statutory requirements, plan inefficiencies/inconsistencies/inequities, administrative concerns and others. Staff first presented the legislative package at the October 4, 2017 Operations, Audit, and Legislative Committee (OALC). The OALC moved to recommend to the full Board approval of the legislative initiatives at its October 27, 2017 meeting. Ms. Thomas identified changes made to 38-751. Mr. Matson made a request to Ms. Thomas to provide updated language to the statutes.

Ms. Thomas reviewed each of the legislative initiatives for the 2018 Legislative Session as follows:

1. Amend A.R.S. § 38-718 to exempt all investment related services from the procurement code
   a. Allows the ASRS to contract for investment related services outside of the Procurement Code
   b. Allows the ASRS to contract for investment related services much more simply and quickly which is necessary in a dynamic industry
   c. Allows the ASRS to contract for more expert services such as due diligence on ad hoc investments
   d. Allows the ASRS to contract with necessary companies and individuals such as large investment firms and industry experts that might otherwise be unavailable

2. Amend A.R.S. § 38-701(6) to allow the Governor’s Office to name any state agency as the state social security administration
   a. The ASRS no longer requires 218 agreements
   b. Allows other state agencies who are better suited to carry out these duties
   c. Allow the Governor’s Office more flexibility in assigning the Social Security Administrator duties
   d. Free up more ASRS staff resources for administering the Plan

3. Amend A.R.S. § 38-751 to include information about how the Non-Participating Employer Liability is calculated and charged and to whom it is assessed
   a. Allows the ASRS to determine whether an Employer is no longer participating
   b. Allows the ASRS to calculate an unfunded liability for an Employer
   c. Allows the ASRS to manage asset fund accounts established for the unfunded liability of Employers

Ms. Thomas provided an update on statute 38-751 noting that subsection (D) has been amended to clarify that non-participating employer’s separate account would be adjusted for all other benefits paid out to the employer’s members, beneficiaries, and survivors. Additionally a new subsection (I) has been added to the draft statute to clarify that once an employer was considered no longer participating under the statute, they can no longer begin to participate at a future date.
4. Amend A.R.S. § 38-871 to reorganize Deferred Compensation Committee members and responsibilities
   a. Changes the Board composition to allow for more members with expert experience
   b. Allows the Board more flexibility in administering its duties
   c. Simplifies language

Ms. Thomas answered questions from the Board regarding 38-718 exemptions on 214 and 511 stating she will be meeting with Arizona Department of Administration (ADOA) and the procurement department next week to clarify questions and concerns regarding these exemptions.

Mr. Matson made a request to Ms. Thomas to provide him, the Board Chair, and any other Board member who may request, a final draft of the modified language after she meets with ADOA.

Mr. Matson advised the Board that this is the first time the ASRS moves on any legislation with respect to the Deferred Compensation Board (38-871) within the last 15 years. He also stated that the reason the ASRS is carrying this legislation is the 457 Board doesn’t have direct staff. They currently have a vendor they work with, which is not in position to run legislation.

**Motion:** Mr. Tom Manos moved to approve the proposed 2018 Legislative Agenda. Mr. Jim Hillyard seconded the motion.

By a vote of 6 in favor, 0 opposed, 0 abstentions, 1 excused, and 2 vacancies, the motion was approved.

4. Presentation, Discussion, and Appropriate Action Regarding the ASRS 2018 Regulatory Agenda and Update on ASRS Rulemaking Initiatives

Ms. Jessica Thomas provided an update regarding the outstanding rulemaking activities on the 2016 Regulatory Agenda, which includes the Long Term Disability (LTD) Program and the Overpayments Program. Additionally, Ms. Thomas provided an update on the remaining activities on the 2017 Regulatory Agenda, which include an amendment to the definition of “Board” with regard to hearing appeals, and the Compensation rulemaking.

Ms. Thomas noted an update to the 2017 Rulemaking Update provided to the Board, which includes a delayed effective date on the Compensation rulemaking and the Termination Incentive Programs in order to provide employers and members notice that these rules were going to be in effect. Additionally, Ms. Thomas noted that the ASRS has determined to postpone the Lump sum threshold rulemaking and the Definition of “termination of employment” rulemaking until 2018 due to Oracle Modernization of Service Purchase and the anticipated rulemaking regarding R2-1-126: Calculating Optional Forms of Benefits. Further, Ms. Thomas provided an overview of the proposed rulemaking on the 2018 Regulatory Agenda.

**Motion:** Mr. Tom Manos moved to approve the proposed 2018 Regulatory Agenda. Mr. Michael Miller seconded the motion.
By a vote of 6 in favor, 0 opposed, 0 abstentions, 1 excused, and 2 vacancies, the motion was approved.

The record should reflect the response of Mr. Michael Lofton, who was attending via teleconference, was momentarily delayed and he has confirmed that his vote was in favor of the motion and is reflected in the above results.

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

Mr. Karl Polen, Chief Investment Officer provided an update of the ASRS investment Program. He presented the current fund positioning noting the over and under-weights of each asset class. He then provided a review of the IMD Investment House Views. Further, he provided an overview of the IMD projects and Asset Class Committee Activities. Additionally, Mr. Polen provided an update of the MSCI Risk Report. Mr. Polen concluded his report by answering questions from the Board regarding the performance of the Farming portfolio.

6. Presentation, Discussion, and Appropriate Action Regarding Independent Reporting Monitoring, and Oversight of the ASRS Investment Program

Mr. Allan Martin, Partner, NEPC, provided a review of Total Fund performance and an independent assessment of the ASRS investment program. He noted that for the one-year period ending June 30, 2017, the Total Fund returned 13.9% (net of fees), underperforming the Interim Strategic Asset Allocation (SAA) Policy by 0.1%. For the three-year period, the Total Fund produced a return of 5.7% per annum, outperforming the Interim (SAA) Policy by 0.9%. Further, he noted that over the past ten years, the Total Fund has returned 5.6% per annum, and since inception, the portfolio’s performance is 9.7%. Mr. Martin noted that these results place the ASRS in the top quartile of public fund performance for all of the one, three, five and ten year reporting periods.

Mr. Martin also provided a summary of investment performance by asset class. He noted that the outperformance of the total fund was supported by positive results across the asset classes. Notably, the private markets program has materially contributed to both absolute and relative returns, especially from the private debt, opportunistic equity and real estate programs. In public markets, Mr. Martin described the consistent outperformance of the fixed income program, noting however, underperformance in active management in public equities, which is being addressed by changes in that program.

7. Presentation, Discussion, and Appropriate Action Regarding the ASRS Experience Study Presentation

Mr. Ryan Falls, Actuary, Gabriel, Roeder, Smith and Company (GRS) and Mr. Joe Newton, Senior Consultant, GRS, provided a summary of the primary purpose of the annual actuarial valuation and Experience Study. They provided a presentation that includes recommendations to the ASRS for new actuarial assumptions and methods to be effective for the June 30, 2017 actuarial valuation. Mr. Falls described the actuarial impact produced by these recommendations as though they had been effective for the June 30, 2016 actuarial valuation. The recommendations include: Economic Assumptions, Mortality Assumptions, Demographic
Assumptions, Actuarial Methods and Policies, and Assumptions Specific to the Long Term Disability Program.

Mr. Falls and Mr. Newton answered questions from the Board members regarding contribution rate, salary increases, Payroll Growth Assumption (PGA), and the relative impact of PGA. Further, Mr. Newton answered questions with regards to the details of the components of the 2.5% growth assumption in the funding policy.

A discussion took place with regards to the declining population growth and the impact on the rate. Mr. Kevin McCarthy requested data regarding population growth rate within the past five years for Teachers K-12. Mr. Matson will provide the information to Mr. McCarthy when it’s ready.

Motion: Mr. Tom Manos moved to approve adoption of the experience study and recommendations, and the resulting changes in methods and assumptions, as presented by GRS, and to specifically:

- Reduce the investment return assumption from 8% to 7.5%
- Pre-fund possible future Permanent Benefit Increases
- Utilize a generational ASRS specific mortality table with improvement scales
- Move from the Projected Unit Credit method to the Entry Age Normal method
- Utilize level percentage of pay amortization

and to apply these changes with a 5-year phase in to the pension plan, the health insurance premium benefit program, and the long term disability program, and to modify the ASRS Funding Policy to reflect the pre-funding of possible future Permanent Benefit Increases (PBI).

Mr. Jim Hillyard seconded the motion.

By a vote of 6 in favor, 0 opposed, 0 abstentions, 1 excused, and 2 vacancies, the motion was approved.

8. Presentation, Discussion, and Appropriate Action Regarding ASRS Retiree Health Insurance Including:
   a. Goals
   b. Health Insurance, Cost Allocation and Pricing Options; and
   c. Retrospective Rate Agreement and Distribution (RRA) Methodology Options

Mr. Paul Matson, Director, presented the ASRS Health Insurance Program including the following:
   a) Goals
   b) Health Insurance Cost Allocation and Pricing Options
   c) Retrospective Rate Agreement and Distribution Methodology Options
   d) Strategic Health Insurance Policies

Mr. Matson reviewed the Health Insurance Premium Setting Policy and recommended two changes as follows:
1. A minor mechanical change regarding the parameters that will apply in order to utilize the Integrated Case Underwriting (ICU). The two limits that are listed under Roman numeral I and II will become a continuation (condition 3 and condition 4) of the list of conditions that will apply in order to utilize the ICU.

2. Insert “including the maximum ASRS Health Insurance premium benefit” to condition 1 and condition 2 after ‘premium level’.

The updated list of conditions that must exist in order to utilize the ICU approach after Mr. Matson’s recommended changes is as follows:

1. The monthly single rate premium level including the max of one or more in-state plans is equal to or greater than 20% of the Mean Average Annuity (MAA).

2. The monthly single rate premium including the maximum ASRS Health Insurance premium benefit differences between in-state plans is equal to or greater than 10% of the MAA.

3. The expected increase in the premiums for any Plan will not exceed 15% compared to the premiums with no ICU for the same respective Plan.

4. The expected decrease in the premiums of any Plan will not exceed 20% compared to the premiums with no ICU for the same respective Plan.

Further, Mr. Matson reviewed the Strategic RRA Management and Distribution Policy to which he made a recommendation; to change “U.S. Gov’t/Credit Float Adjusted: 1-5 Year” on the second page under Investment Benchmark to be referenced as “Intermediate Government Credit One Index”

**Motion:** Mr. Jim Hillyard moved to approve the:

1. Health Insurance Goals
2. Strategic Health Insurance Premium Setting Policy; and the amendments Mr. Matson suggested.
3. Strategic Health Insurance RRA Management and Distribution Policy

Mr. Michael Miller seconded the motion.

By a vote of 6 in favor, 0 opposed, 0 abstentions, 1 excused, and 2 vacancies, the motion was approved.

**9. Presentation, Discussion, and Appropriate Action Regarding the FY2019 Budget**

Mr. Paul Matson reviewed the background of the August 25, 2017 Board motion regarding the ASRS appropriated budget, continuously appropriated budget and administrative and investment spending plans for fiscal year (FY) 2019. He explained this motion is being recommended to clarify the understanding and the intent of the appropriated and continuously appropriated spending plans.
**Motion:** Mr. Jim Hillyard moved to replace the August 25th Board motion pertaining to the ASRS budget, by approving an appropriated budget request for FY 2019 in the amount of $24,642,700 with an understanding there may ultimately be changes to the total appropriated budget amount due to legislative and executive recommendations, and to also accept the proposed continuously appropriated administrative and investment spending plans for FY 2019 subject to revised management projections, and to include private markets performance incentives and other fees when identified and paid. Mr. Tom Manos seconded the motion.

By a vote of 6 in favor, 0 opposed, 0 abstentions, 1 excused, and 2 vacancies, the motion was approved.

The record should reflect the response of Mr. Michael Lofton, who was attending via teleconference, was momentarily delayed and he has confirmed that his vote was in favor of the motion and is reflected in the above results.

10. Presentation and Discussion, Regarding a Change in the Operations, Audit, and Legislative Committee (OALC) Membership Make-up

Mr. McCarthy announced that due to the departure of one Board member who also served on the (OALC), he reduced the OALC from four to three members, with the current three members; chairmanship and vice-chairmanship remaining the same.

11. 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; there were none.

12. 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 January 4, 2017.

   b. Investment Committee (IC)

      Mr. Clark Partridge announced the next IC meeting is scheduled to be held on December 15, 2017.

   c. Appeals Committee (AC)

      Mr. Tom Manos announced the next AC meeting is scheduled to be held on November 14, 2017

13. Board Requests for Future Agenda Items

Amended 11/09/2018
No requests were made.

14. 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 thanked Mr. Matson for the time to meet with him to share some thoughts and knowledge regarding where we are and where we’re going. Mr. Geusic made general comments with regard to contribution rates that have risen over the years and the impact on members of the K-12 system. Mr. Geusic referenced a consolidated report from Joint Legislative Board Commission (JLBC) and provided copies for the Board Chair and the ASRS Director, and asked that they review it to ensure it is accurate.

15. The next regular ASRS Board meeting is scheduled for Friday, December 1, 2017 at 8:30 a.m., at 3300 N. Central Avenue, 10th Floor Board Room, Phoenix, Arizona.

Mr. McCarthy noted the next Board meeting is scheduled for Friday, December 1, 2017 at 8:30 a.m.

16. Adjournment of the ASRS Board

Motion: Mr. Tom Manos moved to adjourn the October 27, 2017, Board Meeting at 10:20 a.m. Mr. Jim Hillyard seconded the motion.

By a vote of 6 in favor, 0 opposed, 0 abstentions, 1 excused, and 2 vacancies, the motion was approved.

Respectfully Submitted by:

Alicia Guzman
Board Administrator
ARIZONA STATE RETIREMENT SYSTEM