



ARIZONA STATE RETIREMENT SYSTEM

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Paul Matson
Director

MINUTES PUBLIC MEETING ARIZONA STATE RETIREMENT SYSTEM BOARD

Friday, November 9, 2018
8:30 a.m.

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, 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. Tom Manos, Chair
Mr. Jim Hillyard, Vice-chair
Mr. Rene Guillen
Mr. Michael Lofton
Mr. Michael Miller
Mr. Clark Partridge

Excused: Mr. Kevin McCarthy

Two vacant positions.

A quorum was present for the purpose of conducting business.

2. Approval of the Minutes of the August 31, 2018 Public Meeting and Executive Sessions of the ASRS Board

Motion: Mr. Clark Partridge moved to approve the minutes of the August 31, 2018 Public Meeting and Executive Sessions #1 and #2 of the ASRS Board. 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. The Trustee votes were as follows:

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

3. Presentation, Discussion, and Appropriate Action Regarding the ASRS 2019 Legislative Initiatives

Ms. Jessica Thomas, Government Relations Officer, introduced the topic by reviewing each of the legislative initiatives for the 2019 Legislative Session as follows:

1. **A.R.S. § 38-711:** Amend to indicate what is “compensation” for ASRS purposes for future members. This will:
 - a. Identify what types of payments are considered compensation for ASRS purposes for future members
 - b. Exclude employment benefits from being reported to the ASRS as compensation
 - c. Protect current members by maintaining the current definition and interpretation of “compensation”
2. **A.R.S. §§ 38-719 and 38-797.15:** Add to indicate the ASRS shall not pay interest unless specifically authorized by statute. This will:
 - a. Indicate that the ASRS will only pay interest on monies owed pursuant to the plan and the Long Term Disability (LTD) program if governing statute specifically provides for the ASRS paying interest
 - b. Ensure that the ASRS only pays interest as the legislature intended
 - c. Limit the risk of ASRS paying interest on monies owed for which the ASRS has not accounted actuarially
3. **A.R.S. § 38-726:** Add to indicate that the ASRS does not pay attorney fees unless the opposing party is successful on adjudication of the merits of a contractual argument. This will:
 - a. Indicate that attorney fees can only be awarded based on successful adjudication of the merits
 - b. Limit the risk of the ASRS paying attorney fees on successful cases based on contracts when contractual actions are not at issue
 - c. Protect the fund from paying out additional expenses related to appeals
4. **A.R.S. § 38-738:** Amend to indicate that Employers can pay for a Contributions Not Withheld via a current year adjustment. This will:
 - a. Allow the ASRS to continue accepting current year adjustments without any staffing or programing changes
 - b. Require the employer to obtain written consent from the employee to make a payroll adjustment
5. **A.R.S. § 38-748:** Amend to indicate that the ASRS shall charge the Employer an unfunded liability amount resulting from ineligible contributions. This will:
 - a. Indicate that the ASRS shall charge an unfunded liability amount for benefits paid to a member based on ineligible contributions reported to the ASRS
 - b. Protect the fund from unintended expense of additional benefits paid that should not have been reported to the ASRS
6. **A.R.S. § 38-729:** Amend to indicate that an Employer cannot purchase overlapping prior service credit for a member upon joining the ASRS. This will:
 - a. Ensure that a member cannot obtain overlapping service credit in a fiscal year when the Employer joins the ASRS
 - b. Make prior service purchase consistent with other types of service purchase and earned service

7. **A.R.S. § 38-797.07(11)(a):** Amend to change “position” to “occupation.” This will:
 - a. Indicate that the member cannot perform the duties associated with the member’s occupation vs. the member’s specific position which may include additional duties above and beyond those required for a specific occupation
 - b. Make ASRS LTD program standards more consistent with industry standards
8. **A.R.S. § 38-797.07:** Amend to indicate that the ASRS or the LTD Administrator may conduct active surveillance during an LTD investigation. This will:
 - a. Allow active surveillance of LTD member in order to resolve an LTD claim in dispute
 - b. Make ASRS LTD program more efficient by reducing possibility of LTD fraud
9. **A.R.S. § 38-766.02:** Amend to indicate that an Employer is not required to pay an Alternate Contribution Rate (ACR) if the employer is already paying contributions or an ACR for a member serving in that same position. This will:
 - a. Indicate that an employer does not owe an ACR for a retired member if the retired member is filling in for another employee for which the Employer is currently paying contributions or an ACR
 - b. Require employer to track who is filling-in for someone on a paid leave status for whom the employer is already making contributions

Ms. Thomas and Mr. Paul Matson, Director, answered questions and provided background on this discussion item. Mr. Hillyard shared the OALC opinion that the ASRS should remain neutral.

Motion: Mr. Jim Hillyard moved to approve the proposed 2019 ASRS Legislative Agenda and that the Agency remains neutral on potential ACR legislation provided the sponsors work with the ASRS to address any concerns. Mr. Michael Lofton seconded the motion.

By a vote of 6 in favor, 0 opposed, 0 abstentions, 1 excused, and 2 vacancies, the motion was approved. The Trustee votes were as follows:

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

4. Presentation, Discussion, and Appropriate Action Regarding the ASRS 2019 Regulatory Agenda and Update on ASRS Rulemaking Initiatives

Ms. Thomas provided the Board with an update on the outstanding rulemaking activities on the 2017 and 2018 Regulatory Agendas as follows:

- 2017 – Two rulemakings have been completed and two have been postponed and placed on the 2018 Regulatory Agenda. One is still in progress – 2 A.A.C. 8, Article 10, Membership Eligibility. The Oral Proceeding was held October 2 for public comment. The Notice of Final Rulemaking was submitted to the Governor’s Regulatory Review Council and is scheduled to be heard in December, 2018.
- 2018 – The 2 A.A.C. 8, Article 5, Service Purchase and 2 A.A.C. 8, Article 7, Contributions Not Withheld have been completed with Oral Proceedings for public input held on October 23. The Notice of Final Rulemaking was submitted to the Governor’s Regulatory Review Council and is scheduled to be heard in January, 2019. The remaining item, 2 A.A.C. 8, Article 1, R2-8-126, is currently being coordinated with staff to develop the rulemaking. Two additional rulemakings that were not on the agenda were worked on this year as well; the

interest rate based on Board action, in addition to an LTD rulemaking to clarify what it means to be under the direct care of a doctor specific to the ailment.

Ms. Thomas presented the 2019 Regulatory Agenda containing three proposed rulemakings to the Board as follows:

- 2 A.A.C. 8, Article 1, R2-8-122: Remittance of Contributions
- 2 A.A.C. 8, Article 1, R2-8-115: Return of Contributions Upon Termination of Membership by Separation from All ASRS Employment by Other Than Retirement or Death; Payment of Survivor Benefits Upon the Death of a Member
- 2 A.A.C. 8, Article 1, R2-8-120: Designating a Beneficiary; Spousal Consent to Designation

Motion: Mr. Clark Partridge moved to approve the proposed 2019 ASRS 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 Trustee votes were as follows:

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

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

Mr. Karl Polen, Chief Investment Officer, reported that the market value of total fund assets was approximately \$38.8 billion and the Fund's current excess performance is approximately 0.5% for the year. Mr. Polen presented a new reporting format to the Board, which illustrates the improvement of the ASRS' excess performance during the most recent difficult market conditions and shows that ASRS' current fund positioning and the performance of our strategies has had a positive impact on the portfolio during current turbulent times.

For periods ending June 30, 2018, the one-year return was 9.4%, outperforming the current actuarial assumption of 7.5% by 1.9% and the Strategic Asset Allocation (SAA) benchmark by 1%. Currently, the primary activity of the division, while continuing the implementation of the new SAA, is working to properly integrate results of the previous and current SAA for the most accurate reporting of performance in one report.

6. Presentation, Discussion, and Appropriate Action Regarding Independent Reporting, Monitoring, and Oversight

Mr. John Krimmel, Partner, NEPC, accompanied telephonically by 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, 2018, the Total Fund returned 9.4% (net of fees), outperforming the Interim Strategic Asset Allocation (SAA) Policy by 1%, placing the ASRS in the top decile of large public pension plans of \$1 billion or greater. For the three-year period, the Total Fund produced a return of 7.8% per annum, outperforming the Interim (SAA) Policy by 0.7%. Further, he noted that over the past ten years, the total Fund has returned 7.4% per annum, and since inception, the portfolio's performance is 9.7%. Mr. Krimmel noted that

these results place the ASRS in the top decile of public fund performance for all of the one, three, five and ten year reporting periods.

Mr. Martin added that the active manager Public Equity program has negatively contributed to performance over the past five years, but replacing the active manager program with factor-based strategies across domestic and international equities is slowly having a positive impact on performance.

7. Presentation, Discussion, and Appropriate Action Regarding the ASRS' Comprehensive Annual Financial Report (CAFR) for Fiscal Year 2018

Mr. Jason Ostroski, CPA, CliftonLarsonAllen Principal, introduced himself to the Board and spoke on behalf of CliftonLarsonAllen, LLP, the ASRS' external auditor. Mr. Ostroski presented an unmodified Independent Auditor's Opinion for the fiscal year ending June 30, 2018, on the ASRS financial statements that collectively comprise the ASRS' financial statements in the CAFR. Regarding the Independent Auditors' Report on Internal Controls, Mr. Ostroski reported there were no material weaknesses or significant deficiencies identified during the audit. Mr. Ostroski further noted that there were no additions to the requirements and standards of GASB 74. Additionally, Mr. Ostroski noted that the accounting estimates which are focused on alternative investments and actuarial information including the pension and the health plans were determined to be reasonable in relation to the financial statements as a whole.

Mr. Ostroski reported, as in the past audits, it was a pleasure to work with Staff.

Further Mr. Ostroski reported no uncorrected misstatements or corrected misstatements, therefore no adjusted journal entries were reported during the audit.

On behalf of the Board, Mr. Manos acknowledged the tremendous amount of work involved and congratulated Ms. Erin Higbee, CFO, Assistant Director, Financial Services Division, and her staff.

8. Presentation, Discussion, and Appropriate Action Regarding a Correction of the Minutes of the October 27, 2017 Public Meeting of the ASRS Board

Mr. Matson explained that during implementation of Board acceptance of the actuarial valuation and the experience study, an error was found in the minutes from that Board meeting, held October 27, 2017. The effective date of the new actuarial assumptions and methods was incorrectly recorded in the minutes as June 30, 2019 and the actual effective date was June 30, 2017.

Motion: Mr. Jim Hillyard moved to correct the effective date of the second sentence of the first paragraph of Agenda Item #7 of the minutes of the October 27, 2017 public meeting of the ASRS Board to be June 30, 2017 rather than June 30, 2019. Mr. Michael Lofton seconded the motion.

By a vote of 6 in favor, 0 opposed, 0 abstentions, 1 excused, and 2 vacancies, the motion was approved. The Trustee votes were as follows:

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

9. Presentation, Discussion, and Appropriate Action Regarding the application dates of the 2017 ASRS Experience Study

Mr. Matson explained that this agenda item seeks to clarify the application dates of the 2017 ASRS experience study. The implementation is completed in two phases. The first phase is the approval of the actuarial valuation beginning on June 30, 2017. The second phase takes into account the time required to complete all the software and factor table modifications. The date for the second phase of these changes to be completed and applied was set for July 1, 2018.

Motion: Mr. Michael Miller moved to clarify the motion of Agenda Item #7 of the October 27, 2017 public meeting of the ASRS Board that the adopted recommendations of the experience study be applied to the Pension Plan, Health Benefits Supplement Plan, and LTD plan actuarial valuations beginning with the June 30, 2017 valuations and applied benefit-related calculations beginning July 1, 2018. 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. The Trustee votes were as follows:

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

10. Presentation, Discussion, and Appropriate Action Regarding the ASRS Actuarial Valuations

a. The Pension Plan and Health Benefit Supplement Valuation

Mr. Ryan Falls and Mr. Paul Wood of Gabriel, Roeder, Smith and Company addressed the Board and summarized the results of the 2018 ASRS valuations. They presented charts summarizing the contribution rates and the funded status. The resulting Plan contribution rate is 11.94% for both the employee and employer, which includes both pension as well as health benefit supplement rates. This represents an increase from the fiscal year 2019 contribution rate of 11.64%. The actuarial value of assets funded status of the Plan as of June 30, 2018 is 71.2%. The market value of assets funded status of the Plan as of June 30, 2018 is 74.1%.

b. The System Valuation

GRS provided information regarding accrued liabilities, market value of assets and funded status for the System. The resulting funded status of the System as of June 30, 2018 is 78.9%.

c. The Long Term Disability (LTD) Valuation

GRS addressed the Board regarding the ASRS LTD Valuation. The resulting contribution rate is 0.17% with the experience study changes phased in, which results in a 0.01% increase from the fiscal year 2019 rate. The actuarial value of assets funded status of the LTD Plan as of June 30, 2018 is 75.8%. The market value of assets funded status of the LTD Plan as of June 30, 2018 is 75.4%.

d. Actuary's Recommendation Regarding 13th Checks for Retired System Members

Based on the results, GRS recommended there will be no addition to the 13th check or supplemental credit balances.

GRS addressed two additional topics, public plan mortality tables and proposed revisions to Actuarial Standards of Practice, and responded to questions from the Board.

Motion: Agenda Item No. 10a Mr. Jim Hillyard moved to accept the actuarial valuation of the Plan and Health Benefit Supplement Program as presented with the resulting contribution rates of 11.94% for each employee and employer. Mr. Clark Partridge seconded the motion.

By a vote of 6 in favor, 0 opposed, 0 abstentions, 1 excused, and 2 vacancies, the motion was approved. The Trustee votes were as follows:

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

Motion: Agenda Item No. 10b Mr. Clark Partridge moved to accept the Actuarial Valuation of the System as presented. 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 Trustee votes were as follows:

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

Motion: Agenda Item No. 10c Mr. Michael Miller moved to accept the Actuarial Valuation of the LTD Program as presented with the resulting contribution rate of 0.17% for each employee and employer. Mr. Michael Lofton seconded the motion.

By a vote of 6 in favor, 0 opposed, 0 abstentions, 1 excused, and 2 vacancies, the motion was approved. The Trustee votes were as follows:

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

Motion: Agenda Item No. 10d Mr. Michael Lofton moved to accept the Actuary's recommendation to not provide an increase to the 13th check for retired System members and no additions to the supplemental credit balances of non-retired System members. Mr. Rene Guillen seconded the motion.

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

approved. The Trustee votes were as follows:

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

Motion: Agenda Item No. 10e Mr. Rene Guillen moved to accept the alternate contribution rate of 10.41% consisting of 10.29% for the Plan and 0.05% for the Health Benefit Supplement Program and 0.07% for the LTD Program as presented. Mr. Michael Lofton seconded the motion.

By a vote of 6 in favor, 0 opposed, 0 abstentions, 1 excused, and 2 vacancies, the motion was approved. The Trustee votes were as follows:

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

11. Presentation, Discussion and Appropriate Action Regarding the 2019 Board Meeting Calendar

Mr. Matson presented the proposed 2019 Board meeting calendar options A (Staff-recommended) and B. Mr. Partridge noted that although he does have a conflict in July, he preferred option A.

Motion: Mr. Clark Partridge moved that the Board adopts option A for the Board meeting schedule for 2019 calendar year. 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. The Trustee votes were as follows:

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

12. Presentation, Discussion, and Appropriate Action Regarding the ASRS Internal Board Per Diem Compensation and Reimbursement Policy

Mr. Matson reviewed the proposed internal policy for the Board, specifying that this policy would apply to the Board of Trustees. This policy establishes agency policy for per diem compensation and for payment and/or reimbursement of eligible travel-related expenses.

Motion: Mr. Clark Partridge moved that the Board approve the ASRS Internal Policy for Board member per diem, compensation, and expense reimbursements as presented with the inclusion of

additional language that it be consistent and in accordance with the State accounting 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. The Trustee votes were as follows:

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

13. 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.

14. Presentation and Discussion Regarding Informational Updates from Prior and Upcoming Committee Meetings

a. Operations, Audit and Legislative Committee (OALC)

Mr. Jim Hillyard announced the next OALC meeting will be held on January 9, 2019.

b. Investment Committee (IC)

Mr. Clark Partridge announced the next regularly scheduled IC meeting is to be held on December 14, 2018.

c. Appeals Committee (AC)

Mr. Tom Manos announced the next AC meeting is scheduled to be held on December 11, 2018.

15. Board Requests for Future Agenda Items

No requests were made.

16. Call to the Public

Mr. Joe Geusic requested to address the Board.

Mr. Geusic made general comments, including his admiration of the Wisconsin retirement plan, the lean budgets of the State of Arizona, and his expectations of excellence and 100% funded status.

17. The next regular ASRS Board meeting is scheduled for Friday, December 7 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, December 7, 2018 at 8:30 a.m.

18. Adjournment of the ASRS Board

Mr. Manos adjourned the ASRS Board meeting at 10:42 am.

Respectfully Submitted by:

Joyce Williams
Board Administrator
ARIZONA STATE RETIREMENT SYSTEM