



ARIZONA STATE RETIREMENT SYSTEM

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Paul Matson
Director

MINUTES PUBLIC MEETING ARIZONA STATE RETIREMENT SYSTEM BOARD

Friday, August 31, 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 8:30 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, Chair
Mr. Jim Hillyard, Vice-chair
Mr. Rene Guillen (joined the meeting at 8:35 a.m.)
Mr. Michael Lofton (via teleconference)
Mr. Kevin McCarthy
Mr. Michael Miller
Mr. Clark Partridge (joined the meeting at 8:47 a.m.)

Two vacant positions.

A quorum was present for the purpose of conducting business.

2. Approval of the Minutes of the June 29, 2018 Public Meeting and Executive Session of the ASRS Board

Motion: Mr. Jim Hillyard moved to approve the minutes of the June 29, 2018 Public Meeting and Executive Session of the ASRS Board. Mr. Kevin McCarthy 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. Tom Manos – approved
Mr. Jim Hillyard – approved
Mr. Rene Guillen – excused
Mr. Michael Lofton – approved
Mr. Kevin McCarthy – approved
Mr. Michael Miller – approved
Mr. Clark Partridge – excused

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

Mr. Paul Matson, Director, on behalf of Mr. Anthony Guarino, Deputy Director and Chief Operations Officer, announced the ASRS has been recognized by the GFOA as the recipient of the

Comprehensive Annual Financial Report (CAFR) award. 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.

In addition, the ASRS received the GFOA Award for Outstanding Achievement for the 2017 Popular Annual Financial Report (PAFR).

Mr. Matson detailed the complex nature of financial reporting required by the ASRS, which includes tracking, following, and understanding approximately \$38 billion in global assets, including often complex and sophisticated investments in areas such as securities lending, private equities, private real estate, and other investment strategies. In addition, approximately \$2 billion in cash flow comes in to the system annually and approximately \$3 billion in cash flow is paid out of the system annually in various forms including retiree benefits, service purchase, forfeitures, and incoming and outgoing transfers from other pension systems.

Mr. Matson presented the two awards and recognized the members of the reporting team: Erin Higbee, Chief Financial Officer, Jeremy Pond, Hong Mayhew, Rebecca Fox, John Maczko, Karl Polen, Lupita Breland, Kerry White, and Nate Brengle. Ms. Higbee described some additional legislation that her team is tasked with to help employers do their financial reporting under GASBs 68 and 75. Ms. Higbee then recognized the reporting team individually and detailed the nature of their contributions.

On behalf of the ASRS Board, Mr. Manos thanked Ms. Higbee and her team for their continued excellent work in financial reporting for the ASRS.

Mr. Rene Guillen joined the meeting at 8:35 a.m.

4. 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 \$41 billion and the Fund's current fiscal year to date return since June 30, 2018 is approximately 3%. Tactical investment positioning has remained consistent, continuing the slight underweight in equities as well as an underweight in interest rate-sensitive securities.

For periods ending June 30, 2018, return calculations are not finalized but the preliminary one-year return was 9.5%, outperforming the current actuarial assumption of 7.5% by 2% and the Strategic Asset Allocation (SAA) benchmark by 1.1%.

Mr. Polen noted that performance of domestic equities fiscal year-to-date is very strong providing the strongest contributor to returns in that period. He also noted that market volatility has declined to near historic lows, which is welcome, but may be the calm before the storm with markets at record highs and valuation metrics above historic norms.

Currently, the primary activity of the division is implementing the new SAA.

Mr. Polen concluded with a report of NEPC's analysis of the ASRS' ranking among similarly sized public pension funds. The NEPC analysis concluded that ASRS total fund performance placed it in the top decile among public pensions for each the 1, 3, 5 and 10-year periods.

Mr. Polen responded to questions from the Board.

Mr. Clark Partridge joined the meeting at 8:47 a.m.

5. Presentation, Discussion, and Appropriate Action Regarding the ASRS Retiree Health Insurance Program Contract Renewal

Mr. Dave King, Assistant Director, Member Services Division, oversees retiree health insurance programs and gave highlights of the Contract to the Board. Mr. King also acknowledged the contributions of Ms. Julie Lockwood, Program Manager; Mr. Frank Perri, Benefits Administrator; Segal Consulting, and Mr. Dan Cadriel, UnitedHealthCare (UHC). Mr. King's summary of the information distributed in the Board materials included replacement of the Senior Supplement plan with the Group Medicare Advantage Prescription Drug (MAPD) PPO; feedback from the Health Insurance Advisory Group, which unanimously advised the adoption of this proposed plan; and a significant reduction in Medicare eligible plan premiums for calendar 2019.

Mr. King responded to questions from the Board. Mr. Manos asked about the reasons for the cost reduction. Mr. King responded by describing strong negotiations, the end of the current contract term, migration to the PPO plan, and distributions from the Retrospective Rate Agreement (RRA) fund as among the main contributing factors to our ability to achieve lower premiums. Mr. Matson added that enhanced data analytics and elimination of a federal reinsurance fee as additional factors.

Mr. Matson also stated that significant strategic goals in the area of health insurance have been significantly accomplished, but at least two additional items need to be focused on at this time.

- 1) Reducing Pre-Medicare premium levels, and determining whether self-insurance makes sense for the ASRS, and
- 2) Sustaining the 2019 low Medicare premium levels

Mr. Matson added that step one would be the issuance of a preliminary Request for Proposal (RFP) document referred to as a Request for Information in order to gather additional information prior to issuing a formal RFP. Responses to the formal RFP will likely require or allow both a fully insured option for the Medicare plans, and self-insured option for the pre-Medicare plans, with the successful bidder in the latter case to provide the administrative apparatus for the plans.

Motion: Mr. Clark Partridge moved to accept the Operations, Audit and Legislative Committee (OALC) and staff recommendation for UHC renewal for the 2019 plan year for Medicare and non-Medicare eligible ASRS, Public Safety Personnel Retirement System, Corrections Officer Retirement Plan, Elected Officials Retirement Plan and University Optional Retirement Plan retirees, eligible disabled members, and eligible dependents. Mr. Michael Miller seconded the motion.

By a vote of 7 in favor, 0 opposed, 0 abstentions, 0 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 – approved
Mr. Michael Miller – approved
Mr. Clark Partridge – approved

6. Presentation, Discussion, and Appropriate Action Regarding a Draft Five-Year Strategic Plan for the ASRS

Mr. Matson introduced this agenda item as well as the three presenters. He then stated that Ms. Sara Orozco will be the substitute presenter, filling in for Mr. Guarino, and that this will serve as a

good opportunity for the Board to become acquainted with the three key staff members: Ms. Orozco, Mr. Brian Crockett, and Mr. Jeremiah Scott.

Ms. Orozco recognized Ms. Lisa King, the absent member of the Strategic Planning Team, before presenting the Strategic Plan. Ms. Orozco identified the six priorities identified by Executive Management, which fall into two categories.

- 1) Priorities that aim to maintain our current state/level of achievement
 - a) Maintain Sustainable Benefit Plans
 - b) Achieve Investment Goals
 - c) Provide Outstanding Customer Service
- 2) Priorities that aim to improve upon our current state/level of achievement
 - a) Enhance Risk Management Capabilities
 - b) Optimize Operational Effectiveness
 - c) Ensure Operational Continuity

Several Trustees of the ASRS Board commended Ms. Orozco and her team on all their hard work with this comprehensive report. Ms. Orozco, Mr. Crockett, and Mr. Scott responded to questions from the Board.

Motion: Mr. Jim Hillyard moved to approve the Five-Year Strategic Plan with No Modifications. Mr. Michael Miller seconded the motion.

By a vote of 7 in favor, 0 opposed, 0 abstentions, 0 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 – approved
Mr. Michael Miller – approved
Mr. Clark Partridge – approved

7. Presentation, Discussion, and Appropriate Action Regarding ASRS Budget-Related Topics

Ms. Martha Rozen, Chief of Administrative Services, introduced Mr. Russ Levine, Procurement and Budget Manager, and Ms. Kerry White, Assistant Chief Investment Officer. Mr. Levine reviewed the administrative spending plan and budget request for FY 2020, and Ms. White did the same with regard to the investment spending plan for FY 2020.

Mr. Matson mentioned that in addition to their work on budget preparation, he relies on Ms. Rozen, Mr. Levine, and Ms. White for other analytical information which they also use to ensure that the agency is reaching its budgetary targets.

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

- 1) An appropriated budget request for FY 2020 in the amount of \$24,130,300, with an understanding there may ultimately be changes to the total appropriated budget amount due to legislative and executive recommendations.
- 2) The proposed administrative spending plan of \$30,799,700, and continuously appropriated investment spending plan of \$157,631,100 for FY 2020, subject to revised

management projections, and to include private markets performance incentives and other fees when identified and paid.

Mr. McCarthy seconded the motion.

By a vote of 7 in favor, 0 opposed, 0 abstentions, 0 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 – approved
Mr. Michael Miller – approved
Mr. Clark Partridge – approved

8. Presentation, Discussion, and Appropriate Action Regarding the ASRS Audit Plan for Fiscal Year (FY) 2019

Mr. Harold Mackey, Chief Internal Auditor, presented the proposed ASRS Audit Plan for FY 2019, starting with an Internal Audit Work Plan Overview which proposes auditable activities for the Fiscal Year (FY) beginning July 1, 2018 through June 30, 2019. Ongoing risk assessments conducted by the ASRS executive and senior managers are the basis for the plan, and will be performed in addition to the following other audit activities.

- 1) The Internal Audit Division (IAD) will audit areas of the agency that are not included in the current ASRS Risk Assessment.
- 2) Consultative and advisory services, as well as analysis of new agency processes and functions, will also be provided by IAD.
- 3) The support services of IAD will be enhanced with external auditors and assessors.

Mr. Mackey then reviewed the Risk Assessment and Resource Allocation, the budget/hours allocation, and descriptions of auditable areas. Mr. Mackey indicated the OALC will provide oversight and will collaborate with the IAD.

Mr. Mackey and Mr. Matson responded to questions from the Board.

Motion: Mr. Clark Partridge moved to approve the ASRS Audit Plan for FY 2019 as presented. Mr. Jim Hillyard seconded the motion.

By a vote of 7 in favor, 0 opposed, 0 abstentions, 0 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 – approved
Mr. Michael Miller – approved
Mr. Clark Partridge – approved

9. Presentation, Discussion, and Appropriate Action Regarding Appointment of Board Committee Officers and Membership

Mr. Tom Manos noted, for the record, appointment to the ASRS Board Committees as follows:

Investment Committee (IC)

Chair: Clark Partridge
Vice-chair: Jim Hillyard
Member: Michael Lofton

Operations, Audit, and Legislative Committee (OALC)

Chair: Jim Hillyard
Vice-chair: Clark Partridge
Member: Michael Miller

Appeals Committee (AC)

Chair: Kevin McCarthy
Vice-chair: Michael Miller
Member: Rene Guillen

10. 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.

11. 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 October 3, 2018.

b. Investment Committee (IC)

Mr. Clark Partridge announced the next regularly scheduled IC meeting is to be held on September 28, 2018.

c. Appeals Committee (AC)

Mr. Tom Manos announced the next AC meeting is scheduled to be held on October 9, 2018.

12. Board Requests for Future Agenda Items

No requests were made.

13. Call to the Public

No one from the public requested to speak.

14. The next regular ASRS Board meeting is scheduled for Friday, November 9 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, November 9, 2018 at 8:30 a.m.

Mr. Manos announced there would be a 10 minute recess while the meeting moved to the 14th floor conference room for the final agenda items. Prior to moving the meeting to the 14th floor conference room, the following motions were made to move the final agenda items to executive session.

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

Motion: Mr. Clark Partridge moved to go into Executive Session #1 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. Michael Miller seconded the motion.

By a vote of 7 in favor, 0 opposed, 0 abstentions, 0 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 – approved
Mr. Michael Miller – approved
Mr. Clark Partridge – approved

16. Presentation, Discussion, and Appropriate Action Regarding the Employment Agreement for the ASRS Director

Motion: Mr. Clark Partridge moved to go into Executive Session #2 pursuant to A.R.S. § 38-431.03(A)(1) for the purpose of reviewing the employment agreement for the Director of the ASRS. Mr. Jim Hillyard seconded the motion.

By a vote of 7 in favor, 0 opposed, 0 abstentions, 0 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 – approved
Mr. Michael Miller – approved
Mr. Clark Partridge – approved

The Board took a recess from 10:20 a.m. to 10:30 a.m. to transition to the 14th floor conference room for the final agenda items and executive sessions.

The Board convened to Executive Session.

The Board reconvened to Public Session at 11:32 a.m.

Motion: Mr. Clark Partridge moved to accept the amendments to Director Matson's employment agreement as presented. Mr. Kevin McCarthy seconded the motion.

By a vote of 7 in favor, 0 opposed, 0 abstentions, 0 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 – approved
Mr. Michael Miller – approved
Mr. Clark Partridge – approved

17. Adjournment of the ASRS Board

Motion: Mr. Kevin McCarthy moved to adjourn the August 31, 2018 public meeting of the Board at 11:34 a.m. Mr. Jim Hillyard seconded the motion.

By a vote of 7 in favor, 0 opposed, 0 abstentions, 0 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 – approved
Mr. Michael Miller – approved
Mr. Clark Partridge – approved

Respectfully Submitted by:

Joyce Williams
Board Administrator
ARIZONA STATE RETIREMENT SYSTEM