

**MINUTES  
ARKANSAS TEACHER RETIREMENT SYSTEM  
BOARD OF TRUSTEES**

**Monday, October 5, 2015  
1:00 p.m.  
1400 West Third Street  
Little Rock, AR 72201**

**ATTENDEES**

**Board Members Present**

Jeff Stubblefield, Chair  
Danny Knight, Vice Chair  
Dr. Richard Abernathy  
Anita Bell  
Lloyd Black  
Kathy Clayton  
Kelly Davis  
Robin Nichols  
Deborah Thompson  
Janet Watson  
Susannah Marshall, designee for Candace Franks  
Johnny Key\*  
Wesley Smith, designee for Hon. Andrea Lea  
Jim Harris, designee for Hon. Dennis Milligan

**Board Members Absent**

Bobby Lester

**Reporters Present**

Mike Wickline, Arkansas Democrat Gazette

\* *via teleconference*

**ATRS Staff Present**

George Hopkins, Executive Director  
Gail Bolden, Deputy Director  
Shane Benbrook, Internal Audit/Risk Mgmt.  
Curtis Carter, Chief Fiscal Officer  
Laura Gilson, General Counsel  
Rod Graves, Assoc. Dir. of Operations  
Wayne Greathouse, Assoc. Dir. of Investments  
Manju, Dir. Data Processing  
Jerry Meyer, Manager, Real Assets  
Tammy Porter, Administrative Assistant  
Mike Ray, Dir. Member Services  
Clint Rhoden, Assoc. Director of Operations  
Leslie Ward, Manager, Private Equity  
Brenda West, Internal Audit/Risk Mgmt.

**Guest Present**

Donna Morey, ARTA  
Chris Caldwell, Div. of Legislative Audit  
P.J. Kelly, AHIC  
Katie Comstock, AHIC  
Angela Cantillon, AHIC (Aon Hewitt)  
Chae Hong, AHIC (Aon Hewitt)  
Kirloes Gerges, AHIC (Aon Hewitt)

- I. **Call to Order/Roll Call.** Mr. Jeff Stubblefield, Chair, called the Board of Trustee meeting to order at 1:00 p.m.. Roll call was taken. Mr. Bobby Lester was absent.
  
- II. **Reaffirm and Ratify the Election of Jeff Stubblefield as ATRS Board Chair and Danny Knight as ATRS Vice Chair.**

**Dr. Abernathy moved to Reaffirm and Ratify the Election of Jeff Stubblefield as ATRS Board Chair and Danny Knight as ATRS Board Vice Chair. Mr. Black seconded the motion, and the Board unanimously approved the motion**

**III. Motion to Excuse Absences.**

**Mr. Knight moved to excuse Mr. Lester from the October 5, 2015 Board of Trustees meeting. Ms. Davis seconded the motion, and the Board unanimously approved the motion.**

**IV. Adoption of Agenda**

**Ms. Nichols moved for adoption of the Agenda. Ms. Davis seconded the motion, and the Board unanimously approved the motion.**

**V. Executive Summary.** The Executive Summary was provided for reference with no questions or expansions on the written summary.

**VI. Approval of Minutes.**

**A. Approval of June 1, 2015 Minutes**

**Dr. Abernathy moved for approval of the Minutes of the Board of Trustees meeting of June 1, 2015. Ms. Nichols seconded the motion, and the Board unanimously approved the motion.**

**B. Approval of June 22, 2015 Minutes.**

**Ms. Nichols moved for approval of the Minutes of the Board of Trustees meeting of June 22, 2015. Ms. Clayton seconded the motion, and the Board unanimously approved the motion.**

**C. Approval of September 2, 2015 Minutes.**

**Ms. Marshall moved for approval of the Minutes of the Board of Trustees meeting of June 22, 2015. Ms. Nichols seconded the motion, and the Board unanimously approved the motion.**

**VII. Report of Member Interest Waived Under A. C. A. Section 24-7-205.** Mr. Hopkins presented the member interest amount waived report. ATRS waives interest on members when there is a dispute between ATRS and the member as to whether ATRS made a mistake or otherwise did not do all that was

required on the member's account. ATRS waived six (6) member interest amounts for this reporting period in the amount of \$139.31.

**VI. Report of Employer Interest and Penalties Waived Under A. C. A. Sec. 24-7-411.** Mr. Hopkins presented the employer interest and penalties waived report. ATRS may waive employer interest and penalties when reports/payments are late or have issues due to new bookkeeper, sickness, and other situations that justify a waiver. ATRS waived Nine (9) employer penalty amounts for this reporting period in the amount of \$7,335.02.

**IX. Member Appeals.** An Order to Dismiss the administrative appeal in the Lydia Kearney case was signed by the ATRS Hearing Officer, August 20, 2015. A copy of the Order was presented to the Board.

**X. 2016 Board Election Update.** Mr. Hopkins reported that the terms for member Trustees elected in the 2016 election cycle will begin on July 1, 2016. Two ATRS Board positions are up for election in this fiscal year:

**Position 2:** Member Trustee (Licensed Teacher, 2<sup>nd</sup> Congressional District);

**Position 9:** Retirant Trustee (At Large Position, all Retirees Vote)

An election timeline explaining the election process that was drafted by the ATRS Legal Department was presented to the Board.

**XI. Audit Committee Report.** Ms. Davis, Chair, gave a report on the Audit Committee meeting.

**A. Vacant At-Large Member Position.**

***Ms Davis recommended Ricky Quattlebaum for the Vacant At-Large Member Position on the Audit Committee. Mr. Knight seconded the nomination, and the Committee unanimously approved the nomination.***

**B. FY 2015 Internal Audit Report – Teacher's Investment Management (TIM) System.** The Arkansas Teacher Retirement System (ATRS) implemented a new investment accounting system, TIM, on July 1, 2014. This new investment accounting system was built in-house by the ATRS IT staff and replaced the Princeton Asset Management (PAM) system that worked in conjunction with State Street, the official custodian of ATRS. Both TIM and PAM were

available concurrently until April 2015. After which, PAM was discontinued, and TIM became the sole investment accounting system.

Information from State Street and various money managers feeds into TIM each month. State Street investment trades are compared to money manager information. Also, TIM performs internal recalculations for income and gain/loss transactions. Finally, foreign currency contracts initiated by State Street are compared to cash transactions for accuracy. Deviations between these comparisons are flagged for research by an investment analyst.

Investment information in the TIM system was tested to ensure the information was accurately recorded and properly documented; however, it should be noted that management requested Internal Audit to review the system before its completion. This was to ensure feedback from Internal Audit while changes could still be easily made to the system.

The objective of the audit is to assess if ATRS investment transactions are accurately recorded and properly documented in TIM. A sample of sixty-four transactions from various money managers was tested. The following procedures were performed:

- Sampled investment data was verified to documents kept by the Investment Department. Types of investments tested included: trades, cash, income, gain/loss, holdings, foreign currency contracts, cost, and manual transactions.
- Discussion with management and the Investment Department regarding processes and calculations.

The objectives of a system of internal controls are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition; that transactions are executed in accordance with policies and guidelines; and are recorded properly.

Audit observations and recommendations were provided to assist management in improving accounting and administrative controls and procedures relating to TIM. Included with the recommendations provided, are departments believed responsible for addressing the

issues noted. It is important to note that the observations and recommendations are directed toward improvement of the system of internal controls and should not be considered a criticism of, or reflection on, any employee of the System.

It should also be noted that the TIM system is still being tweaked, and features are still being added and changed as the project moves forward.

The Findings were:

1. Written procedures are inadequate for the TIM system
2. Visual explanations in the TIM system are lacking for some transactions.
3. Not all types of transactions are recalculated within the TIM system.
4. Currently, there is not 100% recalculation of all income security types by the TIM system, only spot checking by management in some cases.

The Recommendations of the Internal Audit Department were:

1. Written procedures should be fully implemented for TIM once the entire system is completed.
2. We recommend implementing a feature in the TIM system that would visually show calculations as they are performed in the system.
3. Agency management should continue to research and develop the ability to recalculate all types of transactions performed by the custodian.
4. Agency management should incorporate income recalculations on all types of securities within the TIM system to ensure accuracy.

1. **Management's Response to Audit Findings on Teacher's Investment Management (TIM) System.** Mr.

Shane Benbrook presented a copy of the Agency's response to the Committee.

**XII. Investment Committee Report.** Ms. Nichols, Chair, gave a report on the Investment Committee meeting.

A. Investment Update and Arkansas Related Update.

1. List of Recent Fund and Redemptions. Six (6) Fund Closings, One (1) Decision to Not Close Based on Final Due Diligence, and One (1) Redemption

a. Fund Closings

1. **Circumference Group (CG) Core Value Fund, L.P. (Opportunistic/Alternatives Fund Focused on the Fields of Information Technology, Telecommunications, and Business Services, the Board Authorized Commitment of up to \$20 Million Dollars on April 6, 2015, was Accepted and Closed on July 23, 2015).** The ATRS full commitment of \$20 million dollars was accepted and closed on July 23, 2015. As of September 1, 2015, \$9.5 million dollars of the \$10 million dollar commitment has been transferred from the Core Value Fund to the Concentrated Positions Fund.
2. **Circumference Group (CG) Concentrated Positions Fund, LP (Opportunistic/Alternatives Fund Focused on the Fields of Information Technology, Telecommunications, and Business Services, the Board Authorized Commitment of up to \$10 Million Dollars on April 6, 2015, was Accepted and Closed on August 1, 2015).** The ATRS full commitment of \$10 million dollars was accepted and closed on August 1, 2015. As of September 1, 2015, \$9.5 million dollars of the \$10 million dollar commitment has been transferred from the Core Value Fund to the Concentrated Positions Fund.
3. **Franklin Park Co-Investment Fund (Now Known as ATRS/FP Private Equity Fund, L.P.,**

**Expansion of Strategy to Include Select Commitments to Next Generation Manager Funds and an Additional Commitment of up to \$25 Million Dollars, the Board Authorized Expansion of Strategy and Additional Commitment of up to \$25 Million Dollars on April 6, 2015, was Accepted and Closed on May 27, 2015).** The ATRS full commitment of an additional \$25 million dollars was accepted and closed on May 27, 2015.

4. **Long Wharf Real Estate Partners Fund V, L.P. (Value Added Real Estate Fund Focused on Assets at Significant Discounts to Values, the Board Authorized Commitment of up to \$30 Million Dollars on June 1, 2015, was Accepted and Closed on June 30, 2015).** The ATRS full commitment of \$30 million dollars was accepted and closed on June 30, 2015.
  5. **Torchlight Debt Opportunity Fund V, L.P. (Opportunistic Real Estate Fund Focused on High Yield Debt Investments, the Board Authorized Commitment of up to \$25 Million Dollars on June 1, 2015, was Accepted and Closed on June 23, 2015).** The ATRS full commitment of \$25 million dollars was accepted and closed on June 23, 2015.
  6. **Westbrook Real Estate Fund X, L.P. (Value Added Real Estate Fund Focused on Distressed Debt, the Board Authorized Commitment of up to \$25 Million Dollars on June 1, 2015, was Accepted and Closed on June 30, 2015).** The ATRS full commitment of \$25 million dollars was accepted and closed on June 30, 2015.
- b. One (1) Decision to Not Close Based on Final Due Diligence.
1. **As was Expected Based upon Information Provided at the ATRS Board Meeting on June 1, 2015, Castlake IV, L.P. (Private Equity Fund**

**that Invests in Debt and Distressed Assets, the Board Authorized Commitment of up to \$25 Million Dollars at the June 1, 2015, ATRS Board Meeting was Not Closed Due to the Size of the Fund Exceeding Franklin Park's Recommended Limit) was Not Closed. An Attempt was Made to Convince Castlelake that the Fund Size Should be Lowered, but that Attempt Failed.** The investment did not pass Franklin Park's final due diligence due to the final size of the fund exceeding Franklin Park's recommended limit and ATRS did not close on the investment. The Franklin Park recommendation presented at the June 1, 2015, Board meeting was based on a target fund size of \$1.5 billion dollars with a potential hard cap of \$1.75 billion dollars, after talks between Franklin Park and Castlelake general partners, the general partners decided on a final closing fund size of \$1.9 billion dollars. Attempts were made to convince Castlelake that the fund size should be lowered, but those attempts failed. The fund size at close exceeded both the preferred and maximum limits that Franklin Park thought were appropriate for this type of fund and based on this final due diligence decided not to continue with their recommendation.

c. Fund Redemptions.

1. **JP Morgan Special Situations Property Fund (Open End Opportunistic Real Estate Fund, the Board Authorized Full Redemption of the ATRS Investment of Approximately \$60 Million Dollars on June 1, 2015, was Processed on September 30, 2015).** The ATRS full redemption request of approximately \$60 million dollars was processed at the first available fund opening on September 30, 2015.

2. Purchase of Farm in Travers City, Michigan.

a. **Addition to the ATRS Halderman Farmland Portfolio of 2,207 Acre Farm in Michigan for Approximately**



**\$11.3 Million Dollars.** The ATRS farm manager, Halderman Real Assets Management (HRAM), made an addition to the farm program purchasing a 2,207 acre farm for approximately \$11.3 million dollars in Wexford and Grand Traverse Counties, Michigan. The farm consists of well drained loam and sandy soils ideal for a variety of crops such as carrots, potatoes, peppers, onions, cucumbers, edible beans in addition to grain crops such as corn and soybeans. This purchase brings the farm program to approximately \$83 million dollars funded out of a \$100 million dollar total commitment. HRAM is currently prequalifying a potential investment pipeline of four farms totaling approximately \$18 million dollars. Based on Halderman's due diligence, the potential investments currently being reviewed could finish the ATRS commitment to the Halderman farmland portfolio. As of June 30, 2015, the Halderman portfolio has generated a net IRR of 8.1%.

3. BTG Pactual Update.
  - a. **Completed Necessary Revisions to the BTG Pactual Investment Management Agreement to Merge Funds and to Clarify the Use of Leverage and Recallable Distributions.** At the June 22, 2015, called meeting the Board approved motions to concur with recommendations from ATRS staff, Aon Hewitt Investment Consulting, and BTG Pactual to add three items in the BTG Pactual Investment Management Agreement. The amended agreement allows the ability to combine the two portfolios, American Timberland LLC and American Timberland II LLC, and should help reduce the expense of maintaining two LLCs by eliminating the need for separate auditing and legal requirements for each LLC. The agreement also clarifies a 20% limit on the use of leverage by BTG Pactual in the portfolio. The use of leverage should benefit ATRS by allowing the freed cash from the loan to be deployed to other areas and could be used to buy diversifying properties and also help bring the timber allocation in line with the target of 2%. Finally the revisions allow the use of recallable distributions for funds managed by BTG Pactual. In other more direct investments by ATRS, ATRS has the ability to reinvest in the projects through returning returned

capital and distributions for reinvestment. The ability to accept distributions and later to redirect the distributions to the projects as needed versus having the currently unneeded capital held by outside management helps enhance ATRS returns by ATRS having immediate use of the distributions for investments and cash flow. The amended agreement was executed on September 14, 2015.

- b. Retirement of Ms. Joyce Niggley, BTG Pactual Portfolio Manager.** ATRS initially hired Wachovia Bank to manage a timberland portfolio in 1997. Various company acquisitions, mergers, and reassignments over the years have evolved the portfolio to its current form managed by BTG Pactual. The Board approved the latest reassignment of the portfolio from Regions Bank to BTG Pactual at the June 3, 2013, meeting. More recently at the June 22, 2015, meeting, the Board approved changes to the Investment Management Agreement including combining American I with American II, clarifying the use of leverage, and allowing recallable distributions. Mrs. Niggley has been involved with the management of this portfolio for a majority of its term and involved with most of the various changes though the years. Joyce announced her plans for retirement in early 2015 and her retirement became effective in August 2015. Joyce was a pioneer for women in timberland portfolio management and will be missed.

Prior to Ms. Niggley's departure ATRS staff toured all the timberland held in the portfolio with Ms. Niggley and her successor, David Cassels. Mr. Cassels has over 17 years of experience in timberland management and has been involved with the ATRS portfolio since 2010. ATRS staff, Aon Hewitt Investment Consulting, and Ms. Niggley have great confidence in Mr. Cassels' experience, knowledge, and abilities in timberland management.

- B. Private Equity Consultant Report. Franklin Park**
  - 1. Preliminary Private Equity Portfolio Review for the Quarter Ended June 30, 2015.** Michael Bacine of Franklin Park presented the preliminary private equity report for the quarter

ended June 30, 2015. ATRS Legacy Portfolio is in liquidating stage and has a remaining value of 2.5% with a total IRR of 9.2%. CSFB Portfolio is also liquidating and is one-quarter of ATRS portfolio and will continue to see distributions. CSFB has a remaining value of 25.9% with a net IRR of 8.8%. The Post 2006 Portfolio represents 2/3 of ATRS portfolio and will continue to grow as more commitment to capital. The Post 2006 Portfolio has a net IRR of 15.9%. The total fund had a net IRR of 10.0% for the quarter ended June 30, 2015. Big River Steel and Blue Oak Arkansas are both valued at cost. There have been some distributions resulting in an increase in valuation. Both have a net IRR of 2.0%. Mr. Hopkins noted that Blue Oak has four (4) board seats and that all board fees come back to ATRS. Since Blue Oak is not currently in operation, the return of board fees are the result for the 2% IRR for Blue Oak.

2. **Recommendation to Commit up to \$30 Million Dollars in JFL Equity Investors IV, L.P., a Private Equity Buyout Fund that Invests in the Defense, Aerospace and Maritime Industries and Related Businesses.** J.F. Lehman & Company, the general partner of JFL Equity Investors IV, was founded in 1992 to provide financial advisory services to companies in the defense and aerospace sectors. The advisory business ended in 1997 when the firm formed its first institutional private equity partnership. The firm has a history of successful investments in the defense, aerospace and maritime industries primarily in the United States. Based in New York, with satellite offices in Washington, D.C. and London, the firm is led by John Lehman, Louis Mintz, Stephen Brooks and Alexander Harman who average 19 years of experience. ATRS is currently invested in the firm's third fund. Similar to the previous three funds, this fund will make controlled investments in small to lower middle market companies that are either founder-owned or part of a corporate divestiture. The types of companies targeted for acquisition will generally be suppliers to the government or commercial markets and will typically be under-managed, carry excess costs or suffer from insufficient resources. The general partner's experienced and cohesive management team with its specialized knowledge and relationships in the defense, aerospace and maritime industries as well as its overall solid track record make JFL Equity Investors IV an attractive investment. The average performance of the previous three funds is approximately 14% net IRR. There are some risks in the focus sectors of the fund such as

government regulation and dependency on federal and state budgets; however, the team will seek to mitigate those risks by targeting businesses with diverse revenue sources and those in high priority areas of government spending.

**a. Resolution 2015-27**

**Ms. Nichols moved to adopt Resolution 2015-27, to Commit up to \$30 Million Dollars in JFL Equity Investors IV, L.P., a Private Equity Buyout Fund that Invests in the Defense, Aerospace and Maritime Industries and Related Businesses. Dr. Abernathy seconded the motion, and the Board unanimously adopted the resolution.**

- 3. Emerging Managers Report for Fiscal Year Ended June 30, 2015.** The report of Franklin Park's manager research process, including coverage of emerging managers, and provide an update on due diligence activities on emerging managers conducted on behalf of ATRS for the fiscal year ended June 30, 2015 was presented. Eight (8) minority-owned firms were reviewed by Franklin Park during the period of July 1, 2014 through June 30, 2015. Detailed analysis was conducted on two of the eight managers, but ATRS did not make any commitments to these firms.

**C. General Investment Consultant Update.**

- 1. Performance Report for the Quarter Ended June 30, 2015.** P.J. Kelly and Katie Comstock of Aon Hewitt Investment Consulting (AHIC) presented the performance report for the quarter ended June 30, 2015. The total market value of the ATRS fund was approximately \$15.0 billion dollars. The total fund had a return of 8.6% since inception, underperforming its benchmark of 8.7%. The quarter did not have strong return
- 2. Preliminary Performance Report for the Month Ended August 31, 2015.** P.J. Kelly and Katie Comstock of Aon Hewitt Investment Consulting presented the preliminary portfolio update for the month ending April 30, 2015. The total market value of the ATRS fund was \$14.35 billion dollars with return of

8.4% since inception, underperforming its benchmark of 8.5%. Total market value of U.S. equity was \$8.40 billion dollars.

3. **Recommendation to Change the Mandate of the Approximately \$185 Million Dollar Voya Absolute Alpha S&P 500 Trust Fund from U.S. Equity to Global Equity and Change the Strategy Name to the Voya Absolute Alpha Morgan Stanley Capital International (MSCI) All Country World Index (ACWI) Trust Fund to Reflect the Change in the Current Strategy from a U.S. Base to a Global Base.** P.J. Kelly and Angela Cantillon of Aon Hewitt Investment Consulting (AHIC) presented the recommendation to change the mandate of the approximately \$185 million dollars currently invested in the Voya Absolute Alpha S&P 500 Trust Fund to the Voya Absolute Alpha MSCI ACWI Trust Fund.

ATRS has a long relationship with this firm. The Board hired Voya (known as Aeltus at the time, then later as ING, now known as Voya) in 1999 to manage a small cap growth strategy. In 2008 the Board hired Voya to also manage a portable or absolute alpha strategy for ATRS. The absolute alpha strategy seeks to generate alpha or excess return over a benchmark. The fund employs a fund-of-funds approach under which the manager invests primarily in other collective trust funds, pooled vehicles, and various forms of derivatives. Derivatives are used to manage the fund's market exposure, or beta, to closely approximate that of the S&P 500 while also seeking to generate returns over the benchmark, or alpha, by investing in areas that have little or no correlation to the underlying benchmark. Since inception the fund has a net return of 10.4% compared to the S&P 500 Index return of 10.3%.

At the June 1, 2015, Board meeting, the Board approved changes to the ATRS Investment Policy Statement (IPS) that combined the previous allocation of 20% for domestic equity and 30% for global equity into one allocation of 50% for total equity. The update was recommended by AHIC and ATRS staff to help reduce the overlap in global and domestic equities since global equities can also contain domestic equities. If approved, the Voya Absolute Alpha mandate change from a domestic based benchmark to a global based benchmark will help further diversify the ATRS portfolio by increasing the strategy's global opportunities while maintaining some U.S. exposure. Given the cost effectiveness of only having to change the underlying

benchmark without disrupting the fund or having to transition assets, AHIC and ATRS staff recommended this change as part of the ATRS revised IPS target of a 50% allocation to total equity.

The change will require an amendment to the existing Voya Investment Management Agreement that details the change of the benchmark from the domestic S&P 500 benchmark to the global ACWI benchmark. The tiered management fee structure of 0.6 basis point for asset values under \$250 million dollars and 0.4 basis points for asset values greater than \$250 million dollars will remain the same. The performance fee currently calculated by taking 20% of the difference of the annual return of the fund compared to the annual return of the S&P 500 plus 1.25% will be modified to reflect the new benchmark of the MSCI ACWI.

AHIC research has shown the most efficient way to access public equities is through a global mandate that will offer a wider opportunity set and greater flexibility for skilled managers. The combination of equity asset classes into one global allocation will provide more consistency with the IPS view of public equities as one asset class. The move from separate classes will also help to reduce certain portfolio biases or benchmark misspecifications, such as domestic small-cap, by aligning the overall global equity portfolio with a blended benchmark weighted to accommodate the underlying fund manager's strategies. Mr. Hopkins confirmed that staff concurs with the recommendation.

**a. Resolution 2015-28**

**Ms. Nichols *moved to adopt* Resolution 2015-28, To Change the Mandate of the Approximately \$185 Million Dollar Voya Absolute Alpha S&P 500 Trust Fund from U.S. Equity to Global Equity and Change the Strategy Name to the Voya Absolute Alpha Morgan Stanley Capital International (MSCI) All Country World Index (ACWI) Trust Fund to Reflect the Change in the Current Strategy from a U.S. Base to a Global Base. Ms. Davis *seconded the motion*, and the Board *unanimously adopted the resolution***

- 4 **Recommendation to Commit up to \$50 Million Dollars in the Five Year Commitment Option of Trian Partners L.P., managed by Trian Fund Management, L.P., an Equity Activist Manager Focused on High Quality Mid to Large Cap Companies with Sustainable Business Models and Strong Cash Flows.** Trian Fund Management, L.P., headquartered in New York, was founded by Nelson Peltz, Peter May, and Edward Garden in 2005. The founders have over 100 years of combined business and investing experience including direct operating and corporate turnaround involvement. The firm seeks to identify undervalued investments in high quality mid to large cap companies that are leaders in their industries with strong cash flows and balance sheets. Once a potential investment is identified, the firm seeks to implement operational or financial changes to the company as large shareholders or board members of these companies with direct input to the company's existing management teams. The firm has a history of successful investments across several sectors including consumer staples, financial services, industrial, and material. Since inception the Trian Partners, L.P. five year commitment fund has an annualized net return of 9.7% compared to the benchmark of 7.4%.

Terms for this fund vary based on the amount of time the investor is willing to commit to the fund. Options for commitment times range from a minimum of quarterly to a maximum of five years. The fee structure is more advantageous for the longer periods with the five year commitment having the best fee structure. For the five year commitment the management fee is reduced to 1.5% from the 2% charged for a quarterly commitment. For the five year period the incentive fee is 15% of profits above an 8% preferred return. The 8% preferred return means the fund manager is only entitled to 15% of the profits after the investor has earned 8% on the investment. Aon Hewitt Investment Consulting recommends that ATRS invest \$50 million dollars in the 5 year share class of the Trian Partners, L.P. Mr. Hopkins confirmed that staff concurs with the recommendation.

a. **Resolution 2015-29**

**Ms. Nichols *moved to adopt* Resolution 2015-29, To Commit up to \$50 Million Dollars in the Five Year Commitment Option of Trian Partners L.P., managed**

**by Trian Fund Management, L.P., an Equity Activist Manager Focused on High Quality Mid to Large Cap Companies with Sustainable Business Models and Strong Cash Flows. Mr. Knight *seconded the motion*, and the Board *unanimously adopted the resolution*.**

5. **Recommendation to Commit up to \$100 Million Dollars in Trian Co-Investment Opportunities Fund, L.P., also managed by Trian Fund Management, L.P., an Equity Activist Manager Focused on High Quality Mid to Large Cap Companies with Sustainable Business Models and Strong Cash Flows.** A co-investment occurs when ATRS invests directly in a company alongside a fund manager. The recommendation, if approved, would broaden ATRS co-investment opportunities to include public companies in addition to the existing private company access offered through the ATRS investment in the ATRS/FP Private Equity Fund, L.P.

The Trian Co-Investment Opportunities Fund is also managed by Trian Fund Management, the same successful team detailed in the summary for the Trian Partners, L.P. recommendation. Investors in the co-investment fund are limited to a maximum of four times their commitment to other Trian Fund Management funds, so entry into this investment is contingent on the Board approving the recommendation for Trian Partners, L.P.

The co-investment fund will utilize the same proven activist approach taken by Trian in the other funds managed by the firm. The co-investment fund will offer increased opportunity for investment return by allowing ATRS additional investments in those companies in which Trian believe hold the most upside potential or offer the best value. Unlike the other Trian fund with optional commitment periods recommended above, this fund has a commitment period of two years with an optional one year extension. The management fee is a tiered structure based on the amount of commitment.

Aon Hewitt Investment Consulting recommends a commitment amount of up to \$100 million dollars. If approved, the investment is intended to give ATRS an investment in a fund that is within the fund guidelines for allowed commitments based on investments in other Trian funds. This would place ATRS at the tiered fee structure breakpoint of 0.5% for commitments of \$100 to \$299.9 million dollars. All management fee tier levels also contain a 10%



incentive fee. Mr. Hopkins confirmed that staff concurs with the recommendation.

**a. Resolution 2015-30**

**Ms. Nichols moved to adopt Resolution 2015-30, To \$100 Million Dollars in Trian Co-Investment Opportunities Fund, L.P., also managed by Trian Fund Management, L.P., an Equity Activist Manager Focused on High Quality Mid to Large Cap Companies with Sustainable Business Models and Strong Cash Flows. Ms. Davis seconded the motion, and the Board unanimously adopted the resolution**

6. **Reinsurance Investment Review and Recommendation to Commit up to \$110 Million Dollars in Aeolus Property Catastrophe Keystone PF Fund, LP, an Alternative/Opportunistic Reinsurance Fund Specializing in Property Catastrophe Insurance Coverage.** Aon Hewitt Investment Consulting (AHIC) provided the Board with an educational presentation on reinsurance investments and make a recommendation to commit up to \$110 million dollars in the Aeolus Property Catastrophe Keystone PF Fund, LP. An updated report was presented to the board during the meeting.

Aeolus Reinsurance, based in Bermuda, was founded in 2006 by Peter Appel and David Eklund. This firm was seeded by large investors, such as Bank of America and Merrill Lynch, and successfully provided global catastrophic protection to the reinsurance market for several years. In 2011 the founders transformed the firm into Aeolus Capital Management in order to raise capital from other third party investors to provide additional flexibility in deploying capital. The fund, Aeolus Property Catastrophe Keystone PF Fund, LP, seeks to use highly customized portfolios based on actuarial projections concerning catastrophic events, such as hurricanes, to provide returns that are not usually correlated to other asset classes.

The fund is expected to yield a gross return of the Treasury bill rate plus 15% and a net return of 10-11%. Prior funds managed by this team have a net average return of 18% for three years and 16.9% for four years. Reinsurance and retrocession markets underwrite two seasons, January 1<sup>st</sup> through May 31<sup>st</sup>, and June 1<sup>st</sup> through December 31<sup>st</sup>. If approved, ATRS will be

entering the January renewal term that runs for a 1 year period. Investment in reinsurance funds will help ATRS to continue to add diversification to the ATRS portfolio and help reduce the reliance on the traditional stock and bond markets. Mr. Hopkins confirmed that staff concurs with the recommendation.

**a. Resolution 2015-31**

**Ms. Nichols *moved to adopt Resolution 2015-30, To Commit up to \$110 Million Dollars in Aeolus Property Catastrophe Keystone PF Fund, LP, an Alternative/Oppportunistic Reinsurance Fund Specializing in Property Catastrophe Insurance Coverage. Ms. Clayton *seconded the motion, and the Board *unanimously adopted the resolution*****

7. **Emerging Manager Report for Fiscal Year Ended June 30, 2015.** The report of AHIC's manager research process, including coverage of emerging managers, and provided an update on due diligence activities on emerging managers conducted on behalf of ATRS for the fiscal year ended June 30, 2015 was presented.

**D. Real Assets Investment Consultant Report.**

1. **Performance Report for the Quarter Ended June 30, 2015.** Kirloes Gerges of Aon Hewitt Investment Consulting presented the performance report for the quarter ended June 30, 2015. Through the second quarter, NCREIF's NPI returned at 3.1% and NFI-ODCE returned at 3.6%, a decrease of 50 bps and an increase of 40 bps respectively. The trailing 12-month returns currently remain above the sector's long run average. The NCREIF Timberland Index returned 0.5% for the quarter and 10.0% for the trailing one year, a decrease of 130 bps over the quarter and a decrease of 60 bps over the trailing one year. The NCREIF Farmland Index gained 1.2% for the second quarter of 2015 with a 11.6% return for the trailing one year, a decrease of 90 bps and 70 bps respectively over the first quarter results. The Real Assets portfolio stands at 12.1% of ATRS' total assets, a decrease of 30 bps from the first quarter of 2015.

The portfolio is in compliance with its Statement of Investment Policy with respect to style, leverage, geographic region, and

property type diversification. The total returns of ATRS' Total Real Assets Portfolio and the Real Assets Benchmark both underperformed the real assets benchmark by 30 basis points for the first quarter. The underperformance can be attributed to underperformance in the underlying timber and real estate portfolios as well as new commitments to infrastructure. Real Estate has been a positive contributor to the overall portfolio over the long term.

2. **Recommendation to Revise the Real Assets Investment Policy and Procedures to Include as an Additional Benchmark for Agriculture and Timber in the Real Assets Portfolio a Comparison to the Consumer Price Index (CPI) Plus 500 Basis Points.** In 2013, the Board approved the Real Assets Investment Policy and Procedures. The purpose of this policy is to formalize the ATRS investment objectives and procedures for real asset investments including timber and agriculture. Aon Hewitt Investment Consulting and ATRS staff recommend revising the ATRS Real Assets Investment Policy and Procedures to include a benchmark of Consumer Price Index (CPI) plus 500 basis points (5%) as an additional measurement of performance for timber and agricultural investments. This benchmark will be in addition to the NCREIF Timberland Property Index (“NTPI”) for timber and NCREIF Farmland Index (“NFI”) for agriculture. The additional benchmark is intended to help gauge the correlation of the timber and agricultural investments effectiveness in providing a hedge against inflation. The recommendation will be a complimentary benchmark to help measure the timber and agricultural investments relative to the opportunity cost of investing in those asset classes compared to other more traditional asset classes such as stocks and bonds. Mr. Hopkins confirmed that staff concurs with the recommendation.

**Ms. Nichols *moved to approve* the Recommendation to Revise the Real Assets Investment Policy and Procedures to Include as an Additional Benchmark for Agriculture and Timber in the Real Assets Portfolio a Comparison to the Consumer Price Index (CPI) Plus 500 Basis Points. Ms. Davis *seconded the motion*, and the Board *unanimously approved the motion*.**

**XIII. Operations Committee Report.** Dr. Abernathy, Vice Chair, gave a report on the Operations Committee meeting.

**A. Trends Report.** ATRS Trends report was presented to Committee.

**B. Open Forum for Potential Rule or Law Changes by Committee Members and Board Members in Attendance.**

1. General Open Forum. None.

**C. Change in Method of Valuation for ATRS Private Equity and Real Assets.** Mr. Hopkins reported that the statewide Comprehensive Annual Financial Report (CAFR) encompasses the financial statements of all state agencies and institutions. ATRS has placed stress on the recommended deadlines for submission of required data due to the delayed availability of market values for our private equity and real asset investments (the closed end and illiquid components of the ATRS trust fund). In order to speed up the process and help eliminate some stress on the timeliness of the statewide CAFR, the previous ATRS Chief Fiscal Officer, Mitzi Ferguson, researched alternative methods of valuing these assets that would allow ATRS to close the ATRS books earlier.

Currently, the Government Accounting Standards allow for the estimation of values under these circumstances, if properly tied back to confirmed values. The Investment Department developed a method of estimation using March 31 confirmed values adjusted by cash flows for the last quarter of the State fiscal year. This method was demonstrated to show a difference from actual values of less than 1% over the past 4 years. Both the Division of Legislative Audit and the Department of Finance and Administration have favorably reviewed the alternative valuation process. Based upon the favorable notice by the Board Chair and the favorable review by state government, ATRS has moved to this valuation process.

**D. Potential 2017 Legislation.**

1. **Disability Retirement Requirements.** A proposed legislative draft was presented to the Committee. The proposed legislation would allow a disability retiree to appeal the termination of disability status to the ATRS Medical Committee beginning six months before and up to six months after termination of ATRS disability due to not receiving a Social Security disability

determination letter. The draft of the legislation is intended to generate additional discussion on the topic.

**Dr. Abernathy moved to approve Drafting of Legislation on Disability Retirement Requirements. Mr. Black seconded the motion, and the Board unanimously approved the motion.**

2. **Sick Leave – Allow Unused Sick Leave to be Credited as Service for Members Who Die in Active Service.** A draft of the proposed legislation was presented to the Committee. The change would allow active members, including those active members who are accruing deposits in T-DROP, to count unused sick leave as service credit if death occurs while in active service or T-DROP. The days counted as service might help the deceased member's family to qualify for a lump sum death benefit or survivor benefits. This proposed law would not be used in very many instances, because of the small addition by using sick days and the small number of deaths of active members. On a member basis, it could be important and also provides an incentive for ATRS members to sparingly use sick leave.

**Dr. Abernathy moved to approve Drafting of Legislation on Sick Leave – Allow Unused Sick Leave to be Credited as Service for Members Who Die in Active Service. Mr. Black seconded the motion, and the Board unanimously approved the motion.**

C. **Potential Rule Change.**

1. **Rule 4-1: Board of Trustees Composition and Elections.** This rule change became necessary upon the passage of Act 301 of 2015. Act 301 was a technical corrections bill that addressed many things that ATRS has regularly done in practice and was allowed under previous law, but may not have been codified specifically in the law. For this rule change, in order to avoid a conflict of interest on the Board, Act 301 of 2015 does not allow an employee of ATRS to be eligible to run or serve on the ATRS Board in any capacity. The rule change adds a new paragraph "H" under section "I" that includes the language of the new law. Additionally, a clarification change in the rule under 4-1-1(C) adds the word "educational" in front of

the word cooperative to prevent confusion in the election eligibility rules.

**Dr. Abernathy *moved to approve* Rule Change to Rule 4-1: Board of Trustees Composition and Elections. Mr. Knight *seconded the motion*, and the Board *unanimously* approved the *motion*.**

- 2 **Rule 5-4: Investment Goals.** This rule change became necessary upon the passage of Act 301 of 2015, a technical corrections bill, to remove obsolete language and provide that the Board has authority to act at any Board meeting to adjust investment policies, procedures, and asset allocations so that the Board can react swiftly to changing international or national markets by adjusting investments to maximize profits and avoid market downturns. The remainder of the language of Rule 5-4 was deleted as outmoded, obsolete, and inconsistent with Board best practices and the law.

**Dr. Abernathy *moved to approve* Rule Change to Rule 5-4: Investment Goals. Ms. Davis *seconded the motion*, and the Board *unanimously* approved the *motion*.**

3. **Rule 5-5: Investment Strategy.** Similarly with the changes necessary in Rule 5-4 above regarding nimbleness in investment decisions in order to meet fiduciary duties to members, all of the language in Rule 5-5 became obsolete upon the passage of Act 301 of 2015, which authorized the Board to adjust investment policies, procedures, and asset allocations at any meeting by Board motion or resolution, so that the Board can react swiftly to changing international or national markets by adjusting investments to maximize profits and avoid market downturns. Thus, all language in Rule 5-5 was deleted as outmoded, obsolete, and inconsistent with Board best practices and the law.

**Dr. Abernathy *moved to approve* Rule Change to Rule 5-5: Investment Strategy. Ms. Nichols *seconded the motion*, and the Board *unanimously* approved the *motion*.**

4. **Rule 5-6: Investment Consultants.** This rule change is not predicated upon legislation; however the change from the word "system" to the word "ATRS" is useful for consistency throughout the Rules.

**Dr. Abernathy moved to approve Rule Change to Rule 5-6: Investment Consultants. Ms. Marshall seconded the motion, and the Board unanimously approved the motion.**

5. **Rule 8-1: Purchase of Service Credit/Repayment of Refunds.** Act 90 of 2015 changed the certification of private school service to allow ATRS to determine whether the service can be recorded for retirement purposes, consistent with Arkansas Department of Education teaching licensure practices. The addition of the clause "as determined by ATRS staff" in paragraph "2" of 8-1-1 Definitions, was the only change to this rule.

**Dr. Abernathy moved to approve Rule Change to Rule 8-1: Purchase of Service Credit/Repayment of Refunds. Ms. Nichols seconded the motion, and the Board unanimously approved the motion.**

6. **Rule 8-7: Free Military Service.** After the passage of Act 558 of 2015, which addressed how military service was credited, this rule was changed to remove obsolete language and to restate the act language to allow active duty service "during a period that a federal military draft is in effect". Other non-substantive changes remove the word "system" and replace with the word "ATRS" is for consistency throughout the rules.

**Dr. Abernathy moved to approve Rule Change to Rule 8-7: Free Military Service. Ms. Clayton seconded the motion, and the Board unanimously approved the motion.**

7. **Rule 9-2: Age and Service (Voluntary) Retirement.** This rule change is consistent with Act 301 of 2015, which defines "de minimus amount" and gives the Board the authority to set by motion or resolution a de minimus amount for collecting or distributing payments, penalties, interest, funds, or other moneys. This change was necessary because ATRS calculates retirement benefits on salary amounts reported to ATRS by the

employer. Occasionally there are small adjustments to the amount that the employer had previously reported, and these small amounts are referred to as "de minimus". Rule 9-2 was amended to strike obsolete language dealing with "de minimus" amounts in the rule, since the Board now sets those amounts by resolution or motion at any Board meeting.

**Dr. Abernathy moved to approve Rule Change to Rule 9-2: Age and Service (Voluntary) Retirement. Ms. Bell seconded the motion, and the Board unanimously approved the motion.**

8. **Rule 9-4: Disability Retirement.** Act 219 of 2015 significantly amended the disability retirement laws to require proof of a disability determination by the Social Security Administration (SSA) for disability retirement. The law allowed disability benefits to begin for the member, but not to continue indefinitely, until the member submits the SSA determination letter. Such an important change in the law that requires a process, criteria, deadlines, and extension of deadlines necessitated this rule change. The process in Act 219 of 2015 is now new language inserted under 9-4-1(C).

**Dr. Abernathy moved to approve Rule Change to Rule 9-4: Disability Retirement. Ms. Watson seconded the motion, and the Board unanimously approved the motion.**

9. **Rule 10-3: Teacher Deferred Retirement Option Plan (T-DROP).** This rule change was necessary to clarify that although a member may not have accrued a full year in T-DROP, plan interest in the T-DROP account will accrue at the end of each fiscal year. (10-3-1(F)) Another rule change allows a T-DROP participant to withdraw funds from their T-DROP Cash Balance account (or "CBA") two (2) times per quarter, when the current rule only allows one (1) withdrawal per quarter.

Not only does this additional withdrawal ability allow greater flexibility of the CBA and use by the member, it also makes leaving T-DROP accumulations within ATRS more financially attractive. CBA accounts leave funds with ATRS that could otherwise be withdrawn by the member and placed with another retirement administrator. (10-3-7 (VIII)(B)). All other changes are non-substantive, and are made for clarity within the rule.



**Dr. Abernathy moved to approve Rule Change to Rule 10-3: Teacher Deferred Retirement Option Plan (T-DROP). Ms. Davis seconded the motion, and the Board unanimously approved the motion.**

**XIV. Staff Reports.**

- A. Medical Committee Reports.** Michael Ray presented the Medical Committee reports. A total of eighty-five (85) disability applications were received, seventy-three (73) were approved for disability benefits, and twelve (12) needed more information.

**Ms. Nichols moved to approve the Medical Committee Reports. Dr. Abernathy seconded the motion, and the Board unanimously approved the motion.**

- XV. Other Business.** Mr. Hopkins reported that Mitzi Ferguson retired as Chief Financial Officer, but would be working as extra help with the Internal Audit Department. Mr. Hopkins introduced Mr. Curtis Carter as ATRS New Chief Financial Officer. Mr. Hopkins gave a brief update on Big River Steel and Blue Oak Arkansas. Mr. Michael Ray reported that disability letters were sent out and have received approximately 200 replies.

**XVII. Adjourn.**

**Dr. Abernathy moved to adjourn the Board Meeting. Ms. Nichols seconded the motion, and the board unanimously approved the motion.**

**Meeting adjourned at 2:04 p.m.**

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George Hopkins,  
Executive Director

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Mr. Jeff Stubblefield, Chair  
Board of Trustees

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Tammy Porter,  
Recorder

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Date Approved