

STATE EMPLOYEES' RETIREMENT SYSTEM OF ILLINOIS

MINUTES OF THE REGULAR MEETING  
OF THE BOARD OF TRUSTEES

July 24, 2018

A regular meeting of the Board of Trustees of the State Employees' Retirement System of Illinois convened on Tuesday, July 24, 2018, at 10:00 a.m. in the System's Springfield office located at 2101 South Veterans Parkway with a videoconference location at the Bilandic Building, Room N-703, 160 North LaSalle Street, Chicago, IL.

The following trustees were in attendance:

Susana A. Mendoza, Chairperson  
David Morris, Vice-Chairperson  
Thomas Allison, Appointed Trustee  
Shaun Dawson, Elected Active Trustee  
Renee Friedman, Appointed Trustee  
Tad Hawk, Elected Active Trustee  
Carl Jenkins, Appointed Trustee  
Alan Latoza, Elected Retired Trustee  
Stephen Mittons, Elected Active Trustee  
Danny Silverthorn, Appointed Trustee  
John Tilden, Elected Retired Trustee

Absent:

Yasmin Bates-Brown, Appointed Trustee

Others in attendance were:

Timothy Blair, Executive Secretary  
Jeff Houch, Assistant to Executive Secretary  
Steve Bochenek, System Attorney  
Chris Maley, Illinois Office of the Comptroller  
Chasse Rehwinkel, Illinois Office of the Comptroller  
Johara Farhadieh, Executive Director, Illinois State Board of Investment  
Alli Wallace, Consultant, Meketa Investment Group  
Alex Rivera, Consulting Actuary, Gabriel, Roeder, Smith & Co.  
Ryan Gunderson, Consulting Actuary, Gabriel, Roeder, Smith & Co  
Alan Fowler, Manager, Accounting Division  
Casey Evans, Chief Internal Auditor  
Staceyann Cabey-Kaufmann, Internal Auditor  
Robert Cooper, Manager, Administrative Services Division  
Jessica Blood, Recording Secretary  
Loren Iglarsh, SERS Retiree

Chairperson Mendoza called the meeting to order at 10:00 a.m. with a quorum present.

PUBLIC COMMENTS

Chairperson Mendoza asked if there were any members of the public in either the Springfield or Chicago location who wished to address the Board. There were none.

## MINUTES OF THE APRIL 24, 2018 BOARD MEETING

The minutes of the Board meeting held on April 24, 2018, were presented to the members by Chairperson Mendoza. Copies of these minutes were previously provided to each trustee for preliminary review. Vice-Chairperson Morris moved to approve the minutes as submitted. Trustee Dawson seconded the motion, and all were in favor.

## REPORT OF THE ILLINOIS STATE BOARD OF INVESTMENT

Johara Farhadieh introduced herself to the Board as the new Executive Director of the Illinois State Board of Investment (ISBI), effective July 1, 2018. She introduced Alli Wallace, a consultant with the Meketa Investment Group, who would assist with the ISBI report. Director Farhadieh distributed copies of the Quarterly Review dated March 31, 2018 and began her report by comparing the actual asset allocation to ISBI's target policy. Ms. Farhadieh pointed out the asset classes that are notably overweight as of March 31, 2018 included U.S. Equities and the Core Fixed Income portfolio. Asset classes that are underweight as of that date included Opportunistic Debt, Private Equity, and Real Estate.

Ms. Farhadieh continued her report by stating that the total portfolio was down 0.2% for the first quarter of the calendar year, but at March 31, 2018, the portfolio had returned 6.5% for the fiscal year, with an anticipated return of 7.1% for the fiscal year ending June 30, 2018. She then began her review of assets class performance, noting that the Fixed Income portfolio returned 0.8% for the first 9 months of the fiscal year, exceeding the benchmark return of 0.0%. The Emerging Market Debt returned 5.9%, slightly ahead of the benchmark return of 5.5%, while the Bank Loan Composite returned 3.6%, lagging the benchmark return of 3.9%.

Ms. Wallace continued the performance review by noting the Non-U.S. Equity portfolio returned 12.3%, well ahead of the benchmark return of 10.6%, while the Infrastructure portfolio returned 11.1%, compared to the benchmark return of 4.5%. Ms. Wallace directed the Board's attention to the Hedge Fund of Funds Legacy Portfolio noting the portfolio is in the process of liquidation, which is why it has returned -0.7% through the fiscal year, significantly lagging the benchmark return of 5.1%.

Ms. Wallace added the Private Equity portfolio returned 5.6%, significantly lagging the benchmark return of 13.0%. She reminded the Board that the underperformance as compared to the benchmark is a byproduct of increasing capital into this asset class. As committed capital increases, initial drawdowns have occurred impacting the return of the asset class as the portfolio is experiencing the same level of fees as when the capital committed to the asset class is fully deployed. This experience is hindering performance and was anticipated by staff and consultants at ISBI.

Following the summary of the portfolio performance, Director Farhadieh reported on the usage of minority, women, disabled, and emerging (MWDE) owned firms for the nine months ended March 31, 2018. She stated that 25.7% of the portfolio is invested with MWDE owned firms. This represents an increase from the prior year's utilization, which totaled 24.5% of the portfolio. Ms. Farhadieh stated that this rate is notable given the recent transition within the portfolio and concluded this portion of her report by noting that 7.7% of all bills paid to non-investment related vendors involved MWDE owned entities.

After some discussion related to the report, Chairperson Mendoza asked if there were any further questions regarding the report. There being none, she asked if there was a motion to adopt the ISBI report ending March 31, 2018. Trustee Hawk moved to adopt the ISBI Quarterly Review for the period ending March 31, 2018. Trustee Silverthorn seconded the motion, which passed unanimously. A copy of the report is maintained in the ISBI office and made part of these minutes as *Exhibit A*.

## REPORT OF CONSULTING ACTUARIES

Alex Rivera, Consulting Actuary, Gabriel, Roeder, Smith & Co., distributed the economic assumption update review for the June 30, 2018 actuarial valuation.

Actuarial Assumptions. Mr. Rivera began his report by referring the Trustees to the Economic Assumption Update Review for the June 30, 2018 Actuarial Valuation, which concluded with the recommendation of maintaining the annual investment return assumption of 7% while reducing annual price inflation assumption from 2.75% to 2.5% and reducing annual wage inflation assumption from 3.25% to 3.00%.

Mr. Rivera noted that the change in the total price and wage inflation assumptions would have a slight impact on the statutory contribution, causing an increase of \$5 million in the first year. He added that the actuarially determined contribution would also be impacted, with an increase to \$17.7 million. Mr. Rivera cited the statutory funding policy which spreads the unfunded actuarial liability relative to projected payroll and the reduction of payroll as the reasons for the slight increase in contribution rate.

Mr. Rivera referred the Board to the data gathered that was used to provide the recommendation. He pointed to the downward trend in the forward-looking annual inflation forecasts of the Federal Reserve Bank of Cleveland and noted this as the reason for their recommendation to lower the inflation assumption for the actuarial valuation. Mr. Rivera noted the recommendation to reduce the total wage inflation assumption from 3.25% to 3.00% and stated this was due to the reduction of general inflation.

Mr. Rivera noted the investment return assumption review was based on asset allocation and capital market assumptions that were developed by Meketa Investment Group, ISBI's investment consultant, as well as samples from seven other investment consultant firms. Mr. Rivera stated that the probability of achieving the 7% investment return using the Meketa capital market assumptions and current target asset allocation over a 20-year period was roughly 55%. He added that the same likelihood is closer to 47% using the capital market assumptions of the seven independent consulting firms over a 10-year period. Mr. Rivera then pointed to the capital market assumption data of three investment consulting firms with a long-term investment horizon. He noted the probability of achieving a 7% investment return is closer to 54%, lining up more with the data from Meketa.

Chairperson Mendoza asked if there were any questions regarding the review of economic assumptions. Hearing none, she requested a motion to adopt the actuaries' recommendations regarding economic assumptions. Trustee Hawk moved to approve the recommendations as presented, seconded by Trustee Latoza and the motion passed unanimously. A copy of this review is made part of these minutes as *Exhibit B*.

## EXECUTIVE SESSION

Comptroller Mendoza made a motion to go into executive session to discuss personnel matters per 5 ILCS 120/2. Vice-Chairperson Morris seconded the motion and the motion carried in a roll call vote:

Trustee Allison	Aye
Trustee Dawson	Aye
Trustee Friedman	Aye
Trustee Hawk	Aye
Trustee Jenkins	Aye
Trustee Latoza	Aye
Trustee Mittons	Aye
Trustee Silverthorn	Aye
Trustee Tilden	Aye
Vice-Chairperson Morris	Aye
Chairperson Mendoza	Aye

The Rules and Personnel Committee reported to the Board regarding those items referred to the Committee in connection with the OEIG Referral. The Committee reported that it found no substance to the allegations made and recommended that no action be taken on the Referral.

Regarding the handling of referrals from the OEIG the Committee recommended a policy to the Board for adoption. The policy will be considered and acted on by the Board in open session immediately following this Executive Session. The proposed policy includes a provision for any referrals regarding the System's Executive Secretary or Ethics Officer to be directed to the attention of the Comptroller at the Comptroller's office in Chicago and not to the System's address. Upon conclusion of the presentation of this proposed policy the Board voted to return to the open meeting.

Chairperson Mendoza then requested a motion regarding the Rules and Personnel Committee's recommended policy discussed during executive session. A motion was made by Trustee Hawk to accept the recommendation of the Rules and Personnel Committee. The motion was seconded by Trustee Silverthorn and carried with an affirmative vote from all present.

## REPORT OF CHAIRPERSON MENDOZA

Chairperson Mendoza began her report by stating that the bill backlog was currently at \$7.859 billion. She noted that in contrast the July 2017 backlog stood at \$14.5 billion and was growing monthly. Chairperson Mendoza added that her office made enough payments to drop the backlog by nearly \$1 billion as of June 30, 2018 but added the bill backlog is expected to rise due to an increase in general state aid payments to schools under the new education funding formula and the approval of over \$1 billion in supplemental FY 2018 appropriations for several state agencies. She told the Board that the FY 2019 budget does not specifically address the bill backlog and that her office would continue to prioritize payments to education, human services, debt service and pension payments with limited resources.

Chairperson Mendoza then provided an update on HB 5121, the Truth in Hiring legislation. She reminded the Board that the bill would prohibit the practice of using appropriations from various state agencies to pay personnel costs for individuals working directly for the Governor's office, thereby ensuring the funds are used for services appropriate to their respective agencies. She noted that the bill passed the House unanimously and the Senate nearly unanimously. She added that the bill is now awaiting signature by the Governor and if approved, it would take effect with the FY 2020 budget.

Chairperson Mendoza then provided an update on HB 5814, which would require late payment interest penalties to be accounted for in gubernatorial budgets as liabilities and include a way to pay for those costs. She added that the bill was sponsored by Republican Representative McSweeney and has passed both the House and Senate.

Chairperson Mendoza then mentioned that in May 2018, her office unveiled a newly designed and more user-friendly website to better serve state agencies, the public and other users. She noted that some of the changes on the new website include a cleaner look, keyword search capability, organization by service rather than internal departments, drop down menus and concise reports. She added that agencies can now submit all reports from one standard page. Chairperson Mendoza noted that much of the redesign was done by her staff to minimize the use of taxpayer dollars.

Chairperson Mendoza concluded her report by offering to answer any questions from the Board. Vice-Chairperson Morris inquired about vouchers for back pay. Chairperson Mendoza stated that her office had not yet received any but would prioritize those payments along with step increase payments as soon as they are received. No further questions were offered by the Board.

#### REPORT OF ANY TRUSTEE

Chairperson Mendoza asked if any trustee would like to offer a report. None did.

#### REPORT OF AUDIT AND COMPLIANCE COMMITTEE

Vice-Chairperson Morris referred the Board to Chief Internal Auditor Casey Evans to provide the report of the Audit and Compliance Committee. Mr. Evans began his report by stating that the committee met at 9:00 am to discuss regular business.

Mr. Evans stated that the committee approved the internal audit charter which provides the authority, purpose, scope and responsibilities of the internal auditors, management and the Audit and Compliance Committee. Mr. Evans noted that the Committee approved a 2-year audit plan that would review accounts receivable, payable death benefits and back wage claims.

Mr. Evans then reported on the recently completed administrative expenditures audit. He noted that the audit had two minor findings which could be attributed to recent reorganization of the agency and stated that fixes are already being put into place to correct the findings.

Mr. Evans then mentioned upcoming audits. He noted that the internal audit division would perform a retirement eligibility audit by pulling data from the system and looking for

individuals who may not have been eligible. He added that they would also be performing a tier determination audit to ensure that members are categorized under the correct tier.

Chairperson Mendoza asked if there were any questions regarding the Audit and Compliance Committee's report. None were offered.

#### REPORT OF RULES AND PERSONNEL COMMITTEE

Trustee Latoza referred the Board to Jeff Houch, Assistant to Executive Secretary Blair, to make the report of the Rules and Personnel Committee.

Mr. Houch noted that SERS staff had been authorized to pursue rulemaking with JCAR and reported on three rule provisions that would be pursued. Mr. Houch stated the first rule being pursued is to codify that for purposes of calculating final average salary, compensation received for unused compensatory time shall be assigned to the month it was accrued. He added that staff would also pursue rulemaking regarding the accelerated benefit payment program, first to clarify that a member eligible for the automatic annual increase buyout can elect to either take the buyout payment option or the level income option, but not both and also to clarify the legislative intent that only SERS covered service may be used for purposes of determining eligibility under the vested inactive buyout program.

Mr. Houch concluded his report by offering to answer any questions from the Board. Vice-Chairperson Morris requested clarification for overtime worked the prior calendar year and being paid in the subsequent calendar year. Mr. Houch clarified that any overtime would be attributed to the month the member performed those hours. Chairperson Mendoza asked if there were any other questions regarding the report of the Rules and Personnel Committee. No further questions were offered.

#### REPORT OF ACCOUNTING DIVISION MANAGER

Second and Third Quarter Financial Statements. Alan Fowler, Accounting Division Manager, presented the financial statements for the second and third quarters of FY 2018. Mr. Fowler noted that in comparison to the second quarter, there was an increase of \$208.3 million in employer contributions primarily due to the timing of the release of General Revenue funds. When compared to the second quarter of FY 2018, Mr. Fowler noted that there was an increase of retirement annuities of \$31.8 million primarily due to the annual 3% COLA increase and the net increase in the number of retirees from the previous year. In addition, Mr. Fowler pointed to the reduction of \$30 million in sale of investments.

FY 2017 Comprehensive Annual Financial Report. Mr. Fowler then noted the Comprehensive Annual Financial Report that had been distributed to the Board at the April 2018 meeting. Mr. Fowler provided a brief overview of the various sections of the report and the information contained in them.

Mr. Fowler thanked the Comptroller and her staff for the ease of use of their new website as well as being up to date on employer contributions. He concluded his report by offering to answer any questions from the Board. None were offered. Chairperson Mendoza requested a motion to adopt the report. Trustee Latoza moved to adopt the FY 2018 second and third quarter financial statements. The motion was seconded by Trustee Jenkins and passed unanimously. Copies of these financial reports are made part of these minutes as *Exhibit C*.

## REPORT OF THE EXECUTIVE SECRETARY

Final Review of FY 2019 Operations Budget Request. Executive Secretary Blair began his report by stating that the final budget request had been reduced by \$455,855 from the FY 2018 budget, noting the reduction was due to consolidation of staff positions and sections within the agency. Secretary Blair stated that the proposed budget fully funds the call center staff, an attorney for the second half of the year and the SERS Board election. Secretary Blair also noted that the proposed budget covers the employer contribution for a significantly higher employer contribution rate.

Secretary Blair continued his report by stating that SERS is currently looking at options at becoming more energy efficient, noting the possibility of solar powering the Springfield office building as well as current improvements in lighting efficiency.

Trustee Allison inquired what job duties would be assigned to the new attorney. Secretary Blair replied the new attorney would handle routine rulemaking, reviews of legislation and contracts and validation of QILDROs.

Hearing no further questions, Chairperson Mendoza requested a motion to approve the FY 2019 budget request. Trustee Silverthorn made a motion to approve the FY 2019 Final Operations Budget Request. The motion was seconded by Trustee Hawk and passed unanimously. A copy of this request is made part of these minutes as *Exhibit D*.

Legislative Report. Jeff Houch, Assistant to the Executive Secretary, began his report by directing the Board's attention to Public Act 100-587, the Voluntary Accelerated Benefit Payment Programs legislation available to those eligible to retire before June 30, 2021.

Mr. Houch stated that the first option allows Tier 1 members to voluntarily elect to diminish their automatic annual increase (AAI) to a non-compounding 1.5% of the originally granted annuity in exchange for a lump sum payment. Mr. Houch added that the diminished annual increases shall begin on January 1 following the later of the member's retirement anniversary or his or her 67<sup>th</sup> birthdate. The lump sum payment awarded to these members shall total 70% of the present value of the difference in the Tier 1 AAI and the diminished AAI and must be rolled over into a qualified retirement plan.

Mr. Houch then covered the second option under PA 100-587, the vested inactive accelerated benefit program. Members choosing this option may forfeit service credit accrued in the System in exchange for a lump sum payment equal to 60% of the present value of the retirement benefits the member is entitled to at the date of the election, including AAIs and survivor benefits. He added that members who choose this option would remain eligible for health insurance under the State group plan.

Mr. Houch noted that the payouts of these voluntary accelerated benefit programs will be funded by bond proceeds, so the System's assets will not be impacted. He added that the law requires the System to recertify the FY 2019 contribution prior to the end of FY 2019 that factors in the utilization and financial impact of the programs.

Mr. Houch concluded his report by offering to answer any questions from the Board. Following some discussion amongst the Board, Comptroller Mendoza asked if there were any further questions regarding the legislative report. No further questions were offered.

FY 2018 Funding Update. Executive Secretary Blair stated that the System is current in the receipt of State contributions, with FY 2018 funding complete.

APPROVAL OF EXECUTIVE COMMITTEE MINUTES

The trustees had previously been furnished with copies of the April, May and June 2018 Executive Committee minutes for review. There being no changes to the minutes, Trustee Hawk moved to approve the minutes as presented. Trustee Latoza seconded the motion, which prevailed by the affirmative vote of all present.

OLD BUSINESS

Chairperson Mendoza asked if there was any old business to consider. There was no old business.

NEW BUSINESS

Chairperson Mendoza asked if there was any new business to be brought before the Board. There was no new business.

ADJOURNMENT

There being no further business to be brought before the Board, Chairperson Mendoza called for a motion to adjourn. Trustee Hawk made the motion to adjourn, seconded by Trustee Silverthorn and the meeting adjourned at 12:00 p.m.

\_\_\_\_\_  
Susana A. Mendoza, Chairperson

Date: \_\_\_\_\_

ATTEST:

\_\_\_\_\_  
Timothy Blair, Executive Secretary

Date: \_\_\_\_\_