

**STATE EMPLOYEES' RETIREMENT SYSTEM OF ILLINOIS**

**MINUTES OF THE REGULAR MEETING  
OF THE BOARD OF TRUSTEES**

**July 19, 2011**

A regular meeting of the Board of Trustees of the State Employees' Retirement System of Illinois convened on Tuesday, July 19, 2011, at 10:00 A.M. in the System's Springfield office located at 2101 South Veterans Parkway with videoconference location at the Bi-landic Building, Room 14-612, 100 West Randolph Street, Chicago, IL.

The following trustees were in attendance:

Judy Baar Topinka, Chairperson  
Lori Laidlaw, Vice Chairperson  
Thomas Allison, Trustee  
Shirley Byrd, Trustee  
David Morris, Trustee  
Michael Noser, Trustee  
Patricia Ousley, Trustee  
Patricia Rensing, Trustee  
Harold Sullivan, Jr., Trustee  
Virginia Yates, Trustee

Absent:

Renee Friedman, Trustee  
Maria Pelaez-Peterson, Trustee  
Danny Silverthorn, Trustee

Others in attendance were:

Timothy Blair, Executive Secretary  
Steve Bochenek, Attorney  
Charles Hagopian, Office of the Comptroller  
William Atwood, Director, Illinois State Board of Investment  
Gerald Mitchell, Chief Information Systems Officer  
Dave O'Brien, Manager, Administrative Services Division  
Nicholas Merrill, Manager, Accounting Division  
Alex Rivera, Gabriel Roeder Smith & Company  
Paul Wood, Gabriel Roeder Smith & Company  
Alexis Sturm, Office of the Comptroller  
Barbara Baird, SERS Chicago Office  
Dawn Blakeman, Recording Secretary

Chairman Topinka presided, and called the meeting to order at 10:00 a.m. with a quorum present.

**CERTIFICATION OF THE 2011 TRUSTEE ELECTION RESULTS**

The SERS Trustee Election held between May 2 and May 31, 2011, was for one (1) Annuitant Trustee and one (1) Contributing Member Trustee. The State Board of Elections (SBE) oversaw the canvassing of results and certified a total of 22,821 ballots were returned to the SBE offices; the number of eligible ballots returned was 22,478. The ballots were counted on June 7, 2011 at the SBE offices in Springfield. Shirley Byrd was elected an Annuitant Trustee, and Lori Laidlaw was re-elected as a Contributing Member Trustee. Both Trustees will serve 5 year terms which began on July 14, 2011, and end on July 14, 2016.

Rupert T. Borgsmiller, Executive Director of the SBE provided a certified copy of the election results, which is made a part of these minutes as Exhibit A. The SBE will destroy the election materials 60 days from the date of election, in accordance with the rules governing the election, and provided no objections are received.

Chairperson Topinka called for a motion to accept the certification of the State Board of Elections for the two elected trustees. Trustee Rensing moved to accept the certification of the State Board of Elections. Trustee Ousley seconded the motion, and the motion passed by the affirmative vote of all trustees present.

## **REPORT OF THE ILLINOIS STATE BOARD OF INVESTMENT**

William Atwood, Director of the Illinois State Board of Investment (ISBI) distributed draft copies of the Flash Report (Executive Summary) for the period ending June 30, 2011, and addressed the Board. He called attention to the portion of the report reflecting a 21.2% return for FY 11 and a 5.1% return for the calendar year to date. The FY 11 benchmark totaled 18.9% while the calendar year to date benchmark was 3.6%. Director Atwood pointed out the portfolio outperformed the benchmark significantly, which it should do in strong markets because of the aggressive nature of the portfolio.

Director Atwood reviewed for the Board various actions taken at the June meeting of the ISBI. Based on an asset allocation study performed by ISBI consultant Marquette and Associates, ISBI has decided to maintain the current target asset allocation levels. Recommendations were made, however, to change investments within the current allocations. Specifically, Marquette suggested making a 5% allocation to the non-U.S. Bond portfolio from the Fixed Income allocation. The current portfolio contains no non-U.S. bonds. The Board will be doing a search over the next 6 months to choose a non-U.S. bond portfolio manager.

Regarding the domestic equity portfolio, the Marquette recommendation was to increase exposure to small-cap and mid-cap equities. In addition, the ISBI accepted the recommendation to shift away from active managers to index managers in the mid-cap and large-cap equity sectors and retain active management in the small-cap sector. ISBI also adopted the recommendation of shifting 3% of the international equity portfolio to index managers.

Director Atwood then informed the Board the biggest change adopted by ISBI is in the real estate allocation. He pointed out that real estate currently makes up 6.8% of the total invested assets, while the target allocation is 10%. The Board has decided to increase

participation in real estate in order to participate in expected improvement in the sector. Director Atwood pointed out that over the last several years the real estate allocation has lagged its index and hurt the overall performance of the portfolio. ISBI plans to “de-risk” the real estate portfolio by shifting 80% of these assets to “core” or lower leverage real estate.

Comptroller Topinka asked Director Atwood how the current economic and monetary problems in Europe could affect the ISBI portfolio. Director Atwood responded the ISBI portfolio would be affected by any major negative world economic problems as would every other investor. He further explained that the biggest concern at this point is the impact on the portfolio if the current stalemate on increasing the United States’ debt ceiling isn’t resolved. Director Atwood stated the failure to come up with a workable solution would have an “incomprehensible” impact on the portfolio.

Trustee Noser requested updated information on returns net of fees. Director Atwood offered to have that report circulated to the Board electronically but noted it is less timely information when compared to the gross of fees return information. He then told the Trustees that all ISBI minutes, once approved are posted on the ISBI website.

Trustee Noser moved to accept the ISBI Flash Report for the period ending June 30, 2011 and Vice Chairwoman Laidlaw seconded the motion, which passed unanimously. A copy of the report is maintained in the ISBI office and made a part of these minutes as Exhibit B. Chairperson Topinka and the Trustees thanked Director Atwood for his informative report and excused him from the remainder of the meeting.

#### **MINUTES OF APRIL 19, 2011 BOARD MEETING**

The minutes of the meeting of the Board of Trustees held April, 19, 2011 were presented to the members by Chairperson Topinka for approval. Copies of these minutes were previously provided to each trustee for preliminary review. Trustee Allison moved to approve the minutes as submitted. Trustee Rensing seconded the motion, and all were in favor.

#### **REPORT OF THE CHAIRMAN**

Chairperson Topinka indicated she had no formal report, but stated her office was working with ISBI and SERS on several issues including the partial payment of State contributions to all of the State-funded retirement systems. Trustee Allison followed up with a question on the timing of payments to vendors. Comptroller Topinka responded the Comptroller’s Office is attempting to pay down the backlog of 160,000 bills while making the pension payments in a timely manner.

#### **5 YEAR EXPERIENCE REVIEW**

Alex Rivera and Paul Wood of Gabriel, Roeder, Smith & Company, Consulting Actuaries, appeared before the Board to present the results of the June 30, 2010 experience review, which is performed every 5 years to review the appropriateness of all actuarial assumptions. Mr. Rivera explained to the Board the purpose of the review is to ensure all actuarial assumptions reflect economic and demographic trends as closely as possible.

He first reviewed the economic assumptions and said GRS believes a 3% inflation assumption and a 7.75% investment return assumption are reasonable. Mr. Rivera then recommended changing the mortality table to more closely reflect longer life expectancies and retirement rates to reflect earlier retirement ages for most classes of employees.

Mr. Rivera noted the adoption of the recommended assumptions would increase the accrued liability of SERS by approximately \$558 million, resulting in a reduction in the funded ratio of about 0.6%. Consequently, the increase in annual contributions would be approximately 1.4% of payroll, or about \$58 million in FY 13.

Trustee Allison asked Mr. Rivera if the recommended assumptions reflected the possibility of a significant reduction in head count. Mr. Rivera provided the review and recommended assumptions are based on a stable headcount due to the experience of the last 5 years. Comptroller Topinka asked Mr. Rivera about the possibility of providing an alternate valuation based on a reduction of headcount.

Secretary Blair explained that historically the System has assumed a small growth in headcount but that this approach was changed within the last 5 years to assume a static population. He also pointed out that any reduction in membership would be reflected in the data provided to the actuaries when completing the annual valuation. Mr. Rivera agreed that holds true in the short term, but if headcount decreased significantly and remained low, actual state contributions as a dollar amount would be lower during each year of the funding plan, but could well be a larger percentage of payroll.

Comptroller Topinka pointed out that assuming a static headcount may not be realistic going forward due to the financial distress of the State. Trustee Sullivan followed up by pointing out that even if headcount decreases, the Board is responsible for making sure that benefits are paid to the current members. Mr. Rivera agreed and Trustee Noser and Mr. Wood pointed out that assuming fewer members in the future would result in smaller required contributions now due to the statutory funding plan.

Trustee Sullivan stated that the Judges Retirement System (JRS) and the General Assembly Retirement System (GARS) have adopted an investment return assumption of 7% annually. Secretary Blair pointed out that even though SERS assets are commingled with those of JRS and GARS, those smaller funds have more significant liquidity issues than SERS does currently, due primarily to being more poorly funded than SERS. For this reason it may be fiduciarily more appropriate for SERS to maintain a higher investment return assumption than JRS or GARS, even though the assets of all 3 systems are commingled for investment purposes. Trustee Sullivan further pointed out that assumptions should reflect the Board's best estimates for the future, and should not be used to "fix" a back-loaded funding plan.

Following further discussion on the investment rate assumption, Secretary Blair asked Mr. Rivera if GRS found a 7.75% assumption within the range of reasonableness. Mr. Rivera responded that GRS found the assumption within the range of reasonableness.

Trustee Allison moved to accept the changes in assumptions as recommended by GRS. Vice-Chairperson Laidlaw seconded the motion and a roll call vote was taken.

Allison	Yes	Rensing	Yes
Byrd	Yes	Yates	Yes
Morris	Yes	Laidlaw	Yes
Noser	No	Topinka	Yes
Ousley	Yes	Sullivan	No

The motion carried with eight affirmative votes and two no votes.

**REPORT OF EXTERNAL AUDITOR**

Larry Stone, Chief Internal Auditor, was not at the Board meeting. Executive Secretary Blair provided a brief overview of Mr. Stone’s report by pointing out the death match has been completed and reduced overpayments for the quarter by an estimated \$75,000. In addition, the Board was informed that Mr. Stone had completed an audit of the 2011 Trustee election and found no audit issues. All planned FY 11 audits had been completed.

Trustee Sullivan moved acceptance of the Internal Auditor's report for this period. Trustee Noser seconded the motion, all were in favor.

**REPORT OF CHIEF INFORMATION SYSTEMS OFFICER**

Gerry Mitchell, CISO of SRS, provided an update on the System’s modernization efforts. Tier 2 system changes were reported as being completed.

Mr. Mitchell provided an update on the imaging project. Since the last board meeting, CMS established a master contract for the Docuware imaging software. This software fits SRS’ needs and budget and Mr. Mitchell reported they are proceeding with its procurement rather than issuing the IFB recommended in the previous meeting.

Building changes are in process to accommodate the imaging system. Mr. Mitchell is estimating imaging will begin for Judges/GA in September. In addition, meetings have been held with the Secretary of State’s (SOS) Office concerning the record retention requirements of member files. Current Joint Committee on Administrative Rules (JCAR) retention rules dictate that any files saved over ten years must be microfilmed and kept permanently. SERS feels these files are not needed seven years after the death of the member or beneficiary. SOS, SERS and the Attorney General’s Office agree on this point. An application has been submitted to JCAR requesting approval of the seven year retention. Regarding the backfile conversion, Mr. Mitchell reported he is researching examples of RFPs to aid in the development of the backfile RFP. The meeting with the Union to discuss the outsourcing approach has not yet been scheduled.

Mr. Mitchell reported the re-engineering of the Active Member systems continues with the recent implementation of automated payroll file balancing, standardization of processing with the Judges/GA Divisions and on-line payroll queries. He estimates implementation is saving approximately three hours of staff time weekly. The process for system-generated letters has also been modernized, as the prior system was obsolete and failing. Member statements will be re-designed and produced in a PDF format to allow for

emailing. A high speed color printer is being pursued to print the statements in lieu of outsourcing this printing which was determined by staff to be to expensive.

### **THIRD QUARTER FINANCIAL REPORT**

Nicholas Merrill, Manager of the Accounting Division, presented the financial reports for the 3<sup>rd</sup> quarter of FY 11. Mr. Merrill noted that in March 2011, proceeds from the State sale of General Obligation Bonds, in the amount of approximately \$689,100,000, were forwarded to ISBI. These proceeds represented the General Revenue Fund (GRF) portion of the FY 2011 employer contribution to SERS.

Mr. Merrill indicated employee and employer contributions have increased when compared to the 3<sup>rd</sup> quarter of FY 11. The increase in employee contributions is due to an increase in covered payroll and the increase in employer contributions was the result of the employer contribution rate increasing from 28.377% in FY 10 to 30.253% in FY 11. For the 3<sup>rd</sup> quarter, Mr. Merrill pointed out that benefit payments had increase by \$26.6 million when compared to the 3<sup>rd</sup> quarter of FY 10.

Mr. Merrill informed the board that SERS had received a check in the amount of almost \$2.4 million, representing the FY 10 shortfall in employer contributions from GRF. In addition, the System has refunded about \$19 million to non-GRF employer contributions due to a mid-year statutory reduction in the employer contribution rate. In January 2011, the FY 11 employer contribution rate was statutorily decreased from 28.377% to 27.988%.

On motion by Trustee Ousley, seconded by Vice Chairwoman Laidlaw, and by unanimous vote, the Board approved the financial reports as presented for the period January 1, 2011 through March 31, 2010. Copies of the financial reports are attached as Exhibit C.

### **REPORT OF EXECUTIVE SECRETARY**

#### **Final Review of FY 12 Budget**

The final proposed budget for the fiscal year July 1, 2011 through June 30, 2012 was presented for the Board's consideration. Copies of the executive summary, as well as a detailed budget, were previously provided to the trustees for review prior to the meeting. The proposed operating budget for FY 12 includes the imaging project as approved at the April 19, 2011 Board meeting. The budget represents an increase of \$1,474,200 from the preliminary budget approved in April. The proposed FY 12 budget totals \$18,755,300, or 20.3% more than the FY 11 budget amount of \$15,588,400.

The Personal Services proposed budget provides for the addition of 2 position in the Claims Division and 2 positions in Administrative Services to provide imaging support. The total Personal Services line will increase by \$334,500 from FY 11 budget amounts, a 6.45% increase. The budget includes no annual increases for merit compensation employees, per the CMS pay plan. It does include cost of living adjustments pursuant to the AFSCME collective bargaining agreement for employees covered by the agreement. Termination pay for 9 employees and 2 temporary (75 day) employees are also included.

The Board certified employer contribution rate of 34.19% (from 30.253% in FY 11) will result in an increase of \$318,500 in the retirement line when compared to the FY 11

budgeted amount, a 20.3% increase. The FY 12 contractual line increased by \$589,300, or 23.31% from the FY 11 budget, primarily due to the inclusion of the backfile conversion cost of the imaging project and the increase in the fiduciary insurance premium.

The IT department budget increased \$1,767,400, or 41.28%, from the FY 11 budget amount. This increase is the result of the purchase of imaging hardware, software and an imaging consultant. In addition, a new production printer and a new computer room air conditioner is included in the FY 12 IT budget.

Trustee Noser asked about the fiduciary insurance premium amount. Secretary Blair pointed out the Board had approved a higher premium amount (up to \$17,000 higher) in order to receive an additional \$100,000 in coverage for attorney's fees. In addition, Secretary Blair said the \$500,000 in FY 12 assumes the premium for the next coverage period would not increase much from the current levels. Trustee Allison commented that the annual premium may even decline due to the improved financial condition of the State and the increased ability of the State to make the employer contributions to SERS in a more consistent manner. Secretary Blair promised to inform the Trustees of any developments pertaining to any changes in premiums so the Board can make timely decisions regarding the insurance coverage and premiums.

Trustee Ousley presented a motion to approve the preliminary FY 12 budget request. Trustee Rensing seconded the motion and all were in favor.

### **EXECUTIVE COMMITTEE MEETING MINUTES**

The trustees had previously been furnished with copies of the April, May and June, 2011, Executive Committee minutes for review.

Following a brief discussion of the policy changes contained in the minutes, Trustee Rensing moved for their adoption. Vice-Chairwoman Laidlaw seconded the motion, which prevailed by the affirmative vote of all trustees.

### **OLD BUSINESS**

There was no old business brought before the Board.

### **NEW BUSINESS**

Secretary Blair reviewed a new Identity Protection Policy and explained to Trustees that the State Employees' Retirement System must be in compliance with the recently effective Identity Protection Act (5 ILCS 179/1). Following questions and discussion, Trustee Rensing presented a motion to approve the procedures for identity protection. Trustee Yates seconded the motion and all were in favor.

### **ADJOURNMENT**

There being no further business to be brought before the Board, Trustee Silverthorn moved for adjournment at 11:43 A.M. The adjournment motion was seconded by Trustee Rensing and all were in favor.

\_\_\_\_\_  
Judy Baar Topinka, Chairperson

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

ATTEST:

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

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