

STATE EMPLOYEES' RETIREMENT SYSTEM OF ILLINOIS

MINUTES OF THE ANNUAL MEETING
OF THE BOARD OF TRUSTEES

October 30, 2018

A regular meeting of the Board of Trustees of the State Employees' Retirement System of Illinois convened on Tuesday, October 30, 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 Mendoza, Chairperson
David Morris, Vice-Chairperson
Thomas Allison, Appointed Trustee
Yasmin Bates-Brown, Appointed Trustee
Stephen Mittons, Elected Active Trustee
Tad Hawk, Elected Active Trustee
Danny Silverthorn, Appointed Trustee
John Tilden, Elected Retired Trustee
Alan Latoza, Elected Retired Trustee

Absent:

Renee Friedman, Appointed Trustee
Shaun Dawson, Elected Active Trustee
Carl Jenkins, 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, Director, Illinois State Board of Investment
Scott Richards, Senior Investment Officer, Illinois State Board of Investment
Alex Rivera, Consulting Actuary, Gabriel, Roeder, Smith & Co.
Alan Fowler, Manager, Accounting Division
James Knoedler, Acting Manager, IT Division
Casey Evans, Chief Internal Auditor
Jennifer Staley, Recording Secretary
Loren Iglarsh, Chairman, SERS Executive Committee

Chairperson Mendoza called the meeting to order at 10 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.

REVISED MINUTES OF THE APRIL 24, 2018 BOARD MEETING

Revised 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 review. Trustee Hawk moved to approve the minutes as submitted. Trustee Mittons seconded the motion and all were in favor.

MINUTES OF THE JULY 24, 2018 BOARD MEETING

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

REPORT OF THE ILLINOIS STATE BOARD OF INVESTMENT

Johara Farhadieh, ISBI Executive Director, referred the Board to a document detailing changes made by ISBI to simplify the portfolio, reduce fees and increase transparency. Such changes decreased investment fees by approximately \$35 million. Following the review, Director Farhadieh referred the Board to a document detailing the utilization of emerging and minority investment managers as of June 30, 2018. On that date, she reported that 25.6% of assets were managed by emerging and minority managers. The trustees engaged in questions regarding diversity efforts of ISBI and Ms. Farhadieh highlighted specific efforts of the ISBI staff to maximize diversity. Such efforts include forming a staff diversity committee, encourage diversity enhancement strategies among the strategic partners, and increase utilization of diversity among other non-investment related service providers.

Ms. Farhadieh reported that ISBI had recently updated policies, rules, procedures and bylaws to promote Board governance and access to information. Furthermore, the investment policy has been simplified and structured to maximize diversity and inclusion. Ms. Farhadieh remarked that the manager selection process had been altered so that strategic partners would select the investment managers and update the Board on such decisions on a quarterly basis. Ms. Farhadieh added that it was a unanimous decision to adopt the new process of manager selection, so the Board could spend more time on board governance and less time on manager selection.

Scott Richards, Senior Investment Officer of ISBI, continued the ISBI report by distributing copies of the Quarterly Review dated June 30, 2018 and reported that in FY 2018 the total portfolio returned 7.6%, net of fees, slightly outperforming the benchmark return of 7.4%. He added the portfolio totaled more than \$18.3 billion on that date, up by more than a \$1 billion since June 30, 2017.

Mr. Richards continued by reviewing the performance of selected asset classes, first pointing out the Fixed Income portfolio returned 0.9%, net of fees, in FY 2018, outperforming the benchmark return of -0.3%, while the U.S. Equity portfolio re-

turned 14.3% in FY 2018, trailing the benchmark return of 14.8%. The Infrastructure portfolio significantly outperformed its benchmark by returning 13.3% compared to 6.5%. Such return was highlighted by multiple distributions and profitable asset sales, which included the Copenhagen Airport

Mr. Richards continued his report by noting the Private Equity portfolio gained 20.6%, net of fees, in FY 2018, outperforming the benchmark return of 16.4%; the Real Estate Composite portfolio slightly outperformed the benchmark return, 7.3% net of fees, compared to 7.1%. Mr. Richards pointed out that the hedge fund of funds class returned 1.9% compared to the benchmark return of 5.5%. He attributed the underperformance on the ongoing efforts to exit from the asset class.

Chairman Mendoza thanked Director Farhadieh and Mr. Richards for their reports and excused them from the remainder of the meeting. Trustee Allison moved to approve the ISBI report and Trustee Bates-Brown seconded the motion, which passed unanimously. A copy of the June 30, 2018 Quarterly Review is maintained in the ISBI office and made part of these minutes as *Exhibit A*.

REPORT OF CONSULTING ACTUARIES

Alex Rivera, Consulting Actuary from Gabriel, Roeder, Smith & Company, distributed documents to review.

Actuarial Valuation. Mr. Rivera referred the Board to the summary of the draft FY 2018 Actuarial Valuation. He reminded the trustees of the recent Board action to reduce the inflation assumption by 25 basis points, which reduced the June 30, 2017 accrued liability by \$214 million. As of June 30, 2018, total liabilities were approximately \$47.9 billion, up from \$46.7 billion at June 30, 2017. Over the year the funded ratio increased from 35.40% to 36.44%, based on the market value of assets.

Mr. Rivera then discussed the “buyout program” feature added by Public Act 100-0587, which created a COLA buyout option and a total buyout option. Mr. Rivera noted that such programs will have a positive impact on SERS, as the programs will reduce accrued liabilities without impacting fund assets, as the buyouts will be funded by a bond issuance. Mr. Rivera added that buyout assumptions will be developed when there is utilization data to analyze.

Mr. Rivera then discussed the actuarially determined contribution (ADC) which is used for financial reporting purposes and provides a better measurement of true cost. He reminded the Board that the SERS ADC method is normal cost plus a 22-year amortization of the unfunded liabilities, and added that for FY 2020, such amount totals 64.512% of payroll. Mr. Rivera stated the main reason unfunded liabilities increased from the prior year is attributable to the inadequacy of the statutory funding formula. Mr. Rivera then directed the Board to charts in the valuation that illustrate the back-loaded nature of the statutory funding plan and that a large portion of investment earnings in the short term will be used for benefit payments.

After some discussion on the details of the valuation and financial condition of the fund, Trustee Allison made a motion to approve the draft FY 2018 actuarial valuation. Trustee Bates-Brown seconded the motion and the Board approved the motion unanimously. A copy of the valuation is made a part of these minutes as *Exhibit B*.

FY 2020 Preliminary Certification. Mr. Rivera directed attention to the preliminary FY 2020 State contribution rate of 51.152% of payroll, or \$2,385,359,000. Trustee Latoza motioned to approve the preliminary FY 2020 State contribution, and Trustee Mittons seconded the motion. The Board approved the motion unanimously. A copy of the preliminary certification is made a part of these minutes as *Exhibit C*.

REPORT OF AUDIT & COMPLIANCE COMMITTEE

Chief Internal Auditor Casey Evans began the Audit and Compliance Committee report by stating the committee met before the Board meeting. He reminded the Board that each trustee must complete the annual ethics training and sexual harassment training by the end of the calendar year.

Mr. Evans provided a summary of recent audits relating to retirement eligibility testing and tier status testing. Those audits resulted in no material findings. He then briefly reviewed ongoing disability fraud issues, which are mainly attributed to false information provided by members on certification forms. Discussion then focused on the procedures associated with the verification of disability claims. Mr. Evans summarized that members complete certification forms on a semi-annual basis in order to substantiate continued eligibility for SERS disability benefits. In addition, quarterly data matches are performed with Illinois Department of Employment Security to ensure disability recipients are not exceeding gainful employment limitations.

REPORT OF RULES AND PERSONNEL COMMITTEE

Trustee Latoza, Chairman of the Rules and Personnel Committee, noted the committee met on Monday afternoon and turned the presentation over to Jeff Houch. Mr. Houch summarized the committee's recent action authorizing staff to pursue rule-making associated with the buyout programs that were created by Public Act 100-587. He noted that staff would file emergency rules that would take effect before the December 1, 2018 COLA buyout program implementation date. He explained that emergency rules remain valid for 150 days, so staff would file identical permanent rules to replace the emergency rules when they expire.

Mr. Houch provided a brief summary of the rules, which clarify the administrative details of the program and allow implementation in an efficient manner. Additionally, the rules were structured to allow the buyout programs to be administered in compliance with other applicable State and Federal laws. Following Mr. Houch's review of the rules, he offered to answer questions. None were offered.

REPORT OF CHAIRPERSON MENDOZA

Chairperson Mendoza began her report by stating that as of that morning, the State's bill backlog totaled \$6.99 billion, down from \$16.4 billion from the preceding year. She noted the bond issuance was instrumental in such reduction and allowed her office to secure an additional \$2.2 billion in federal reimbursement money. Chairperson Mendoza added that managing the cashflow for FY 2019 will be challenging due to changes to the education funding formula, and the need to pay down previously underreported, unpaid bills at several agencies. She added that no additional tools were provided in the FY 2019 budget to help her office attack the bill backlog.

Chairperson Mendoza then outlined successful efforts to pass several laws associated with government transparency, noting overwhelming support in the legislature. The legislation included the Debt Transparency Act, which requires agencies to include late payment interest penalties in the budget proposal, and an act that will allow the Treasurer to use state assets to pay down portions of the bill backlog at an interest rate that is lower than the late payment penalty interest rate.

Chairperson Mendoza concluded her report by stating that her office will continue to work with the retirement systems to ensure the buyout programs work as intended and stated her office is committed to ensuring that contributions to the retirement systems continue to be made in a timely manner.

Election of 2019 Vice-Chairperson and Committees. Chairperson Mendoza announced that elections for Vice-Chairperson and committee membership were in order. Trustee Allison motioned to re-elect Trustee Morris as Vice-Chairperson and to retain the current committee membership structure for 2019. Trustee Bates-Brown seconded the motion, which passed unanimously.

2019 Executive Committee. Trustee Morris will continue to serve as the elected member and Vice-Chairperson of the committee and Trustee Hawk will continue to serve as the alternate elected member. Loren Iglarsh will continue to serve as Chairperson Mendoza's designee.

2019 Audit and Compliance Committee. Trustees Morris and Dawson will continue to serve as elected members of the committee and Loren Iglarsh will continue to serve as Chairperson Mendoza's designee.

2019 Rules and Personnel Committee. Trustees Latoza, Hawk, and Silverthorn will continue to serve as elected members of the committee, with Trustee Latoza continuing as Chairperson.

REPORT OF ANY TRUSTEE

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

REPORT OF THE EXECUTIVE SECRETARY

Calendar Year 2019 Meeting Dates. In order to comply with the Open Meetings Act, it is necessary to post a schedule of meetings for the upcoming calendar year in the System's offices in Springfield and Chicago and on the SERS website. Trustee Alison moved to adopt the 2019 schedule, including the standing committees, as presented. The motion was seconded by Trustee Latoza and all voted in the affirmative for the 2019 meeting dates:

Tuesday, January 15, 2019

Tuesday, April 30, 2019

Tuesday, June 25, 2019

Tuesday, October 29, 2019

All 2019 meetings will begin at 10 a.m. The System's Springfield office is located at 2101 South Veteran's Parkway. The Chicago meeting location is Room N-703 of the Bilandic Building, 160 N. LaSalle St. All meetings will be available via videoconference at both locations.

Inclusion Policy. Secretary Blair presented the Board with an amended inclusion policy as it relates to the SERS procurement procedures for the inclusion of increased diversity of SERS employees and service providers, consistent with 40 ILCS 5/1-109 and 40 ILSC 5/1-109.1. Secretary Blair informed the Board that employment diversity associations will be notified of any job postings and MWDBE firms will be notified of upcoming Requests for Proposal (RFP) or Invitations for Bid (IFB). Trustee Bates-Brown moved to adopt the Inclusion Policy amendment. The motion was seconded by Trustee Tilden and it passed unanimously.

FY 2019 Funding Update. Executive Secretary Blair informed the Trustees that SERS had received the November contribution and that FY 2019 funding is current.

Back Wage Claims Update. Executive Secretary Blair provided an update relating to the payment of frozen wages from 2011 and 2012 for certain State employees. Approximately 35,000 State employees had received frozen wages and SERS staff was working to adjust earnings records and recalculate retirement benefits for employees that had retired.

He added that approximately 20% of the members receiving frozen wages were retired, creating a significant increase in workload for the staff. Secretary Blair said the System's efforts to address the increased workload include bringing back recently retired SERS employees authorizing overtime. He emphasized the magnitude of the project and that it will require significant time and resources to complete.

Buyout Program Update. Secretary Blair echoed the statements of the actuaries by stating the buyout programs will have a positive impact on the fund given that the

liabilities will decrease but the System's assets will not be impacted. He mentioned that the COLA buyout program will be available on December 1, 2018 and that some COLA buyout election forms have already been returned. Secretary Blair indicated that there has been substantial interest from the membership in the program. He stated that an online buyout estimator tool is available on the member services website and added that it was recently promoted by an email blast to all active members.

REPORT OF ACCOUNTING DIVISION MANAGER

Alan Fowler, Accounting Division Manager, began by reporting on the financial statements for the fourth quarter of FY 2018, ending June 30, 2018. Mr. Fowler noted that the report contains the normal variances, caused by the timing of the receipt of the GRF portion of employer contributions, the sale of some invested assets to cover disbursements, and the increase in benefit payments primarily attributed to automatic annual increases.

Mr. Fowler thanked the Comptroller's Office staff and mentioned that payments were up to date through November, which means the System will be able to pay benefits for the month without having to draw down any invested assets.

Mr. Fowler concluded his report by offering to answer any questions. None were offered. Chairperson Mendoza asked for a motion to adopt the report. Trustee Hawk moved to adopt the FY 2018 fourth quarter financial statements. The motion was seconded by Trustee Allison and it passed unanimously.

APPROVAL OF EXECUTIVE COMMITTEE MINUTES

The trustees had previously been furnished with copies of the July, August, and September 2018 Executive Committee minutes for review. There being no changes to the minutes, Trustee Tilden 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 consider. Executive Secretary Blair introduced Jim Knoedler as acting IT Division Manager, noting the unexpected retirement of former IT Division Manager Kevin Rademacher in May 2018.

ADJOURNMENT

There being no further business, Chairperson Mendoza called for a motion to adjourn. Trustee Allison moved to adjourn and Trustee Bates-Brown seconded the motion. All members voted in the affirmative and the meeting adjourned at 12:00 p.m.

Chairperson Mendoza reminded the Trustees that the next meeting is scheduled for January 15, 2019, at 10 a.m. in the Springfield Office with the usual videoconference location in the Bilandic Building.

Susana Mendoza, Chairperson

Date: _____

ATTEST:

Timothy Blair, Executive Secretary

Date: _____