

STATE EMPLOYEES' RETIREMENT SYSTEM OF ILLINOIS

MINUTES OF THE REGULAR MEETING
OF THE BOARD OF TRUSTEES

January 13, 2015

A regular meeting of the Board of Trustees of the State Employees' Retirement System of Illinois convened on Tuesday, January 13, 2015, 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:

Leslie Geissler Munger, Chairperson
David Morris, Trustee
Patricia Ousley, Trustee
Robert Fierstein, Trustee
Thomas Allison, Trustee (by phone)
Renee Friedman, Trustee
Danny Silverthorn, Trustee
Yasmin Bates-Brown, Trustee

Absent:

Lori Laidlaw, Vice-Chairperson
Shirley Byrd, Trustee
Alan Latoza, Trustee
Harold Sullivan, Trustee

Others in attendance were:

Timothy Blair, Executive Secretary
Steve Bochenek, Attorney
William Atwood, Director, Illinois State Board of Investment
Paul Wood, Consulting Actuary, Gabriel, Roeder, Smith & Co.
Alex Rivera, Consulting Actuary, Gabriel, Roeder, Smith & Co.
Alan Fowler, Manager, Accounting Division
Gerry Mitchell, Chief Information System Officer
Jeff Houch, Assistant to Executive Secretary
Casey Evans, Chief Internal Auditor
Alexis Sturm, Office of the Comptroller
Loren Iglarsh, Executive Committee Chairman
Barbara Baird, Manager, SERS Chicago Office
Jennifer Staley, Recording Secretary
Tia Sawhney, SERS member

Chairperson Munger presided and called the meeting to order at 10:10 a.m. with a quorum present. Trustee Allison requested to participate by phone. Trustee Morris moved to allow Trustee Allison to participate by phone. Trustee Silverthorn seconded the motion and all trustees present voted in the affirmative.

PUBLIC COMMENTS

Chairperson Munger asked if there were any members of the public in either the Springfield or Chicago location who wished to address the Board. Dr. Tia Sawhney, actuary and SERS member, introduced herself to Chairperson Munger and the other trustees. She noted the Board had experienced a loss with the recent passing of Comptroller Topinka and offered her condolences. She continued by noting the Comptroller Topinka had agreed with her on the need for transparency regarding SERS and better communicating risk to members.

She then noted that relevant documents need to be posted to the website sooner and that according to the State Actuary's report that limited stress testing had been performed recently. She concluded her brief comments by noting the need for better transparency, better analysis and a better understanding of risk. Chairperson Munger thanked Dr. Sawhney for her comments and asked if there were additional comments from the public. There were none.

MINUTES OF THE OCTOBER 28, 2014 BOARD MEETING

The minutes of the Board meeting held on October 28, 2014 were presented to the members by Chairperson Munger. Copies of these minutes were previously provided to each trustee for preliminary review. Trustee Silverthorn moved to approve the minutes as submitted. Trustee Ousley seconded the motion and all were in favor.

REPORT OF THE ILLINOIS STATE BOARD OF INVESTMENT

William Atwood, Director of the Illinois State Board of Investment (ISBI) distributed copies of the Pension Fund Executive Summary for the period ending November 30, 2014, and introduced himself to Chairperson Munger. He began by reviewing the returns of the various asset classes for the one year period ended November 30, 2014. Director Atwood noted the entire portfolio returned 8.4% (net of fees) over that period, while the benchmark returned 8.1%.

Director Atwood continued by noting that over the year ending November 30, 2014, the Fixed Income portfolio returned 3.0% and the U.S. Equity portfolio returned 11.6%. Both portfolios underperformed their benchmarks, which returned 5.3% and 15.5%, respectively. Mr. Atwood continued by briefly reviewing the returns of several asset classes, noting that several asset classes, and the portfolio as a whole, had outperformed the respective benchmarks.

Director Atwood informed the Board that the strength of the U.S. dollar had affected the returns of non-U.S. based investments and had probably cost investors, including ISBI, 500 basis points, or 5%, in returns over the last year. He then noted that ISBI had made the strategic decision over time to be weighted in small-cap equities. While this tends to be positive over the long term as small cap stocks generally provide higher return, this has not been the case over the last year, when large-cap stocks have outperformed small-cap stocks.

Director Atwood noted this concluded his report. Chairperson Munger asked if there were any questions or comments. There being none, Trustee Silverthorn moved to receive the ISBI Report for the period ending November 30, 2014. Trustee Morris 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 A. Chairperson Munger thanked Director Atwood for his report and excused him from the remainder of the meeting.

REPORT OF THE ACTUARY

Alex Rivera and Paul Wood of Gabriel, Roeder, Smith & Company (GRS), Consulting Actuaries, distributed the final version of the June 30, 2014 actuarial valuation. Mr. Rivera introduced himself to Chairperson Munger and informed the Board there would be three items discussed; the State Actuary's report and the GRS/SERS response, stress testing and potential options for adopting a funding policy for financial reporting purposes.

State Actuary's Report. Mr. Rivera began by noting the State Actuary's report concluded that the assumptions and methodology used for the FY 2014 valuation were an improvement over those used in the last two valuations. He then voiced his agreement with the State Actuary that the current statutory funding plan does not comply with Actuarial Standards of Practice. Mr. Rivera continued by noting the State Actuary recommended conservative actuarial assumptions. GRS believes assumptions should be set based on expectations of future experience and that the current SERS assumptions are reasonable.

Mr. Rivera continued by briefly reviewing the remainder of the State Actuary's recommendations. A letter outlining all of State Actuary's recommendations and the GRS/SERS response to these recommendations is attached and made a part of these minutes as Exhibit B.

Stress Testing. Mr. Rivera referred the Board to a handout detailing the result of various stress testing scenarios, as recommended by the State Actuary. Some scenarios used a 4% rate of return (static and variable) to project the future funded ratio of SERS and the resulting effect on State contributions. In addition, the effect of volatility assuming the current long term return of 7.25% annually was provided.

The impact of applying a 4% rate of return, static or variable, significantly reduces the funded ratio of SERS over the remainder of the funding plan, thus greatly increasing the required State contributions to SERS through FY 2045. The stress testing results are made a part of these minutes as Exhibit C.

Funding Policy. Mr. Wood continued the GRS presentation by distributing a handout containing information on possible funding policies for the consideration of the Board. He began by noting the implementation of Governmental Accounting Standards Board (GASB) Statement #67 requires, for financial reporting purposes, an "Actuarially Determined Contribution" or ADC. In order to comply, the Board should consider the adoption of a funding policy.

Mr. Wood provided that a funding policy should include a reasonable cost allocation methodology, adequate actuarial assumptions, an asset smoothing method and a reasonable period and methodology for the amortization of unfunded liabilities. He briefly reviewed several funding policy possibilities and offered to answer any questions of the Board. Trustee Allison asked if an "asset corridor" could be included in a funding policy. Mr. Wood answered in the affirmative and suggested it could be considered.

Trustee Friedman then asked if the adopted funding policy could be used to suggest a change in the statutory funding plan. Mr. Wood explained it was needed for financial report-

ing purposes as provided in GASB Statement 67. The policy could be presented to the General Assembly if the Board so chose as a preferred alternative to the current funding plan. The Board continued to briefly discuss the funding policy and actuarial assumptions and directed GRS to provide a recommended funding policy at the April Board meeting. Chairperson Munger thanked the actuaries for the valuable information and noted her support of transparency and the adequate funding of all of the State-funded retirement systems.

Chairperson Munger asked if there was a motion to approve the FY 2014 actuarial valuation and to certify the required FY 2016 employer contribution of \$2,124,938,000, or 45.598% of projected payroll. The certified contribution includes \$80,061,000, or 1.718% of payroll to be used to pay the debt service on the pension obligation bonds issued in FY 2003. Trustee Friedman moved to approve the FY 2014 actuarial valuation and Trustee Silverthorn seconded the motion. All Trustees present voted in the affirmative.

After a brief discussion on the opportunities for strengthening the statutory funding plan, Trustee Ousley moved to approve the FY 2016 employer contribution rate as required by statute. Trustee Friedman seconded the motion and all were in favor.

REPORT OF CHAIRPERSON MUNGER

Chairperson Munger thanked the Board for their work and expressed her interest in learning all of the business of the Board. She recognized the work of Comptroller Topinka and acknowledged the transition was ongoing. She then notified the Board of her 25 years of service in the private sector, her background in marketing and business administration, and her familiarity with financial reporting.

Chairperson Munger provided that she would be available to discuss the business of the Board with other Trustees and staff and again expressed her appreciation during the time of transition.

REPORT OF ANY TRUSTEE

Chairperson Munger asked if any other trustees would like to offer a report. There were none.

REPORT OF CHIEF INFORMATION SYSTEMS OFFICER (CISO)

Economic Interest Statements. Gerry Mitchell, CISO and Ethics Officer, informed the Board that the Secretary of State (SOS) will be mailing Statements of Economic Interest to all Trustees in mid-March. The statements must be returned to the SOS by May 1st. Mr. Mitchell requested that Trustees return completed statements to the System's Office to be forwarded to the SOS.

Systems Modernization. Mr. Mitchell provided an overview of the modernization project for the new Comptroller. He noted that since the last Board meeting work had begun on re-engineering the pension setup process that will automate many of the current manual processes. This re-engineering will first be implemented with the Judges' Retirement System and General Assembly Retirement System. He continued that analysis is underway to determine the initial services to be provided to active members through the system's website.

Retiree and Survivor statements are being modified to include calendar year earnings information, and this information is also available on the SRS website. He noted for the Board that this information had been provided by the Comptroller's Office in paper form, but a law change eliminated this requirement.

Mr. Mitchell reported that upgrades to hardware and the network have been completed to provide faster and reliable service. Web security systems have also been updated to help protect against internet attacks.

Retiree Health Insurance Premium Refunds. Mr. Mitchell stated that analysis is underway to determine system changes needed to return the increased health insurance premiums collected from retired members. The refund is required due to a recent court decision and the work is being done in conjunction with Department of Central Management Services and the Comptroller's Office.

Risk Assessment. Mr. Mitchell reported that activities related to the risk assessment are ongoing, including the addition of locks to all interior doors in the lobby and adding walls to restrict access to the second floor.

REPORT OF AUDIT AND COMPLIANCE COMMITTEE AND INTERNAL AUDITOR

Trustee Morris reported the Audit and Compliance Committee had met prior to the Board meeting as scheduled at 9 a.m. He then referred the Board to Chief Internal Auditor Casey Evans to provide a report to the Board.

Mr. Evans began by introducing himself to Comptroller Munger and continued by briefly reviewing the internal audit plan, which includes statutorily required audits and audits based on internal risk assessment. One audit required by an Executive Order required all agencies to review all Rutan-exempt positions and report to the Governor and General Assembly by December 31, 2014. Mr. Evans completed the audit and noted one finding and one recommendation. The minor finding was the inclusion of certain forms in employee personnel files rather than the Rutan files that are used for audit purposes. He also noted the recommendation to implement a checklist and quality review process to ensure accuracy had been adopted by the Human Resources Division.

Mr. Evans continued by noting a risk at SERS is created due to retirement eligibility of a large portion of SERS employees, including management. He informed the Board that he is going to look into the adequacy of succession planning at SERS and the effect a large number of retirements may have on the operations of SERS. Mr. Evans completed his report by noting an upcoming audit of the Claims Division and offered to answer questions from the Board. There were none.

REPORT OF THE EXECUTIVE SECRETARY

Appointed Trustee Status. Secretary Blair referred the Board to a memo prepared by Steve Bochenek, attorney for SERS, detailing the status of appointed trustees who have not been confirmed by the Senate. The main concern regarding trustee status is the ability of the Board to continue operations during the period of transition.

Mr. Bochenek began by noting that 6 trustees are appointed by the Governor with the advice and consent of the Senate, 6 trustees are elected by the membership of SERS, and the

Comptroller of the State of Illinois serves as the ex-officio Chairperson. Statute requires a majority of Trustees must concur in any action taken; meaning 7 votes are required for any Board action to be effective.

He continued by noting that one appointed trustee position is vacant, four appointed trustees have been reappointed but not confirmed, and one appointed trustee position has not been reappointed. He continued by noting the Senate Rules regarding confirmation and unknown status of those potential appointments. He offered to answer any questions regarding appointments. Trustee Silverthorn asked about the status of his appointment and Secretary Blair noted the reappointment message of Trustee Silverthorn and the 3 other unconfirmed appointees were in the Senate Executive Appointments Committee.

Executive Committee Election. Secretary Blair informed the Board that Vice-Chairperson Laidlaw was going to retire on April 1st. Vice-Chairperson Laidlaw began serving on the Executive Committee in 2006 and a replacement would have to be elected to serve out the remainder of her calendar year 2015 term. He offered that Trustee Morris had expressed a willingness to serve on the Committee. Trustee Silverthorn moved to nominate Trustee Morris as a member of the Executive Committee for the remainder of calendar year 2015. Trustee Ousley seconded the motion and all voted in the affirmative.

FY 15 Funding Update. Executive Secretary Blair reported that SERS has received 5.5 months of employer contributions, or slightly more than \$500 million from the General Revenue Fund (GRF). The system also receives approximately 1/3 of the employer contributions from Non-GRF payrolls, and those are made as non-GRF payrolls are processed. The Comptroller's Office's efforts to provide a more stable employer contribution to all of the retirement systems has made a big difference in the financial condition of SERS, as the system has not withdrawn assets from the ISBI investment portfolio in order to pay benefits.

FIRST QUARTER FINANCIAL STATEMENTS

Alan Fowler, Accounting Division Manager, presented the financial statements for the first quarter of FY 15. Mr. Fowler noted that in comparison to the last quarter of FY 14, there was a slight increase in employer contributions of approximately \$5.1 million. He also noted a \$1.5 million decrease in resignation refunds due to fewer members terminating State employment, when compared to the previous quarter.

Mr. Fowler continued by noting that in comparing the first quarter of FY 15 to the first quarter of FY 14, retirement annuities increased by \$28.7 million. The increase is the result of the statutory 3% COLAs provided to retirees in January and an increase in the number of retirees from the previous year. He concluded by noting the quarter was uneventful from a financial statement perspective.

Chairperson Munger asked if there were any questions. There being none, Trustee Ousley moved to accept the first quarter financial statements and Trustee Silverthorn seconded the motion, which passed unanimously. Copies of these financial statements are attached to these minutes as Exhibit D.

APPROVAL OF EXECUTIVE COMMITTEE MINUTES

The trustees had previously been furnished with copies of the October, November, and December 2014 Executive Committee minutes for review. There being no changes to these

minutes, Trustee Morris moved to approve. Trustee Silverthorn seconded the motion, which prevailed by the affirmative vote of all trustees.

OLD BUSINESS

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

NEW BUSINESS

Chairperson Munger asked if there was any new business to be brought before the Board. No new business was offered.

ADJOURNMENT

There being no further business to be brought before the Board, the meeting adjourned at 12:10 p.m. Comptroller Munger thanked the Trustees and reminded them the next meeting was scheduled for April 21, 2015 at 10 a.m. in the Springfield Office with the videoconference location in the Bilandic Building.

Leslie Geissler Munger, Chairperson

Date: _____

ATTEST:

Timothy Blair, Executive Secretary

Date: _____