

**MINUTES OF THE
TEXAS MUNICIPAL RETIREMENT SYSTEM
Meeting of the Board of Trustees**

May 18, 2017 – 1:30 p.m.

On May 18, 2017, the Board of Trustees of the Texas Municipal Retirement System (TMRS) convened for a meeting at 1:30 p.m. at the Lakeway Resort, located at 101 Lakeway Drive, Austin, Texas, with the following members present:

Board of Trustees

Jim Parrish, Chair
Bill Philibert, Vice Chair
Julie Oakley
Jim Jeffers
David Landis

Absent: Roel "Roy" Rodriguez

Present also were:

David Gavia, Executive Director
Eric Davis, Deputy Executive Director
TJ Carlson, Chief Investment Officer
Christine Sweeney, General Counsel
Leslee Hardy, Director of Actuarial Services
Debbie Munoz, Director Member Services
Scott Willrich, Director of Information Resources
Jesse Pittman, Senior Project Manager
Leslie Ritter, Director of Human Resources
Robert Klausner, Klausner, Kaufman, Jensen & Levinson
Chris Schelling, Director of Private Equity
Tom Masthay, Director of Real Assets
Jason Weiner, Director of Fixed Income
Sandra Vice, Director of Internal Audit
Karen Jackson, Executive Assistant
Marcia Beard, RVK
Joe Newton, Gabriel, Roeder, Smith & Company
Mark Randell, Gabriel, Roeder, Smith & Company
Amy McDuffee, Mosaic Governance Advisors
Brian Borton, StepStone Group LP
Tracy Harris, StepStone Group LP

Also in attendance:

Nick O'Keefe, Senior Staff Attorney
Pete Krnavek, Information Systems Manager
Chris Tindell, Private Equity Analyst
Cindy Morse, Investment Support Analyst

Debbie Farahmandi, Investment Operations Specialist
Peter Jeske, Project Specialist
Michael Schaff, Assistant General Counsel
Greg Shipley, Combined Law Enforcement Associations of Texas
Keith Dagen, Government Finance Officers Association of Texas
George Kaufman, City of Garland
Bob Scott, City of Carrollton
David Riggs, Texas State Association of Fire Fighters
Kathleen Depweg, City of Arlington

Mr. Parrish called the meeting to order at 1:31 p.m. and Mr. Landis gave the invocation.

1. Consider and Act on Adoption of Minutes from the March 30-31, 2017 Meeting of the Board of Trustees.

Mr. Gavia stated that Staff had nothing to add to the minutes as presented. Mr. Parrish requested a change noting that Ms. Oakley gave the invocation and not Mr. Parrish.

Mr. Jeffers made a motion that the Board adopt the minutes from the March 30-31, 2017 Meeting of the Board of Trustees with the requested change to the invocation. Mr. Philibert seconded the motion, which passed 5-0.

2. Consider and Act on Updated Beneficiary Forms and Other TMRS Forms

Mr. Gavia introduced Ms. Munoz to present the proposed changes made to the TMRS Beneficiary Forms. The TMRS Act states that members and retirees must designate beneficiaries on forms prescribed by the Board of Trustees and filed with the retirement system (Texas Government Code, Chapter 854 "Benefits"). That is, changes to certain TMRS forms must be approved by the Board before they can be put to use. In addition, the TMRS Legal Department has opined that, due to statutory provisions, Board approval is also required for the substance of the electronic forms.

Ms. Munoz explained the on-line beneficiary form process and presented six forms; four have been revised and two are new forms due to the on-line process. She summarized and highlighted the changes to the various forms which are either revised forms or replacements for existing forms.

If the Board approves these forms, Staff anticipates that the new and amended paper forms will be made available to cities, members, retirees, and payees as soon as practical after approval, and the new online designations will undergo testing and then be made available online in late June or early July.

Mr. Philibert made a motion that the Board (i) adopt the new and/or amended forms TMRS-BENE, TMRS-86, TMRS-7VOP, TMRS-24, TMRS-75, as presented, and the substance of the TMRS-EBENE form(s) to be generated by the new online processes, (ii) authorize the Executive Director and staff to continue using the existing forms, along with the newly approved forms, until such time as the Executive Director determines the use of the older versions of the forms is obsolete, and (iii) authorize the Executive Director, or his designee,

to make future non-substantive changes to the forms and the online processes for beneficiary designations as they deem necessary or desirable for the efficient administration of TMRS. Mr. Landis seconded the motion, which passed 5-0.

3. Consider and Act on Results of 2016 Actuarial Valuation and Approval of 2018 Retirement Contribution Rates and Supplemental Death Benefit Contribution Rates. (formerly # 3 on the Friday, May 19, 2017 agenda)

Mr. Newton and Mr. Randall from GRS presented the results of the December 31, 2016 actuarial valuation. For cities with over five hundred employees, the average rate change was 0% (Section 1, EXHIBIT IV). The tough decisions made previously by the Board are now paying off. Even though the Unfunded Actuarial Accrued Liability (UAAL) increased, the Funded Ratio did improve over the previous year. This incremental improvement is what is expected.

Mr. Newton reviewed changes in the Aggregate Benefit Accumulation Fund highlighting non-investment experience. Mr. Randall reviewed the Summary of the Benefit Provision Changes reflected in the 12/31/2016 Valuation, noting the changes in the employee deposit rate, matching ratio, Updated Service Credit (USC) and Cost of Living Adjustment (COLA).

The Yields based on Market Value of Assets were reviewed as well as the Market and Actuarial Values of Assets and noted that in the future TMRS will likely experience more volatility than we are currently seeing.

Mr. Newton discussed contributions versus benefits and refunds. The negative cash flow is to be expected and it is in a very manageable range. The history of liabilities and assets was reviewed and described as being very stable. He discussed Funded Ratio Percentages, Projected Funded Ratios as well as the distribution of single equivalent amortization periods. The historical dollar weighted contribution rates and distribution changes in contribution rates by city were discussed.

The contribution rate Phase-In was reviewed and it was noted that most cities are paying the full rate even though they have a phase-in option. Measures of leverage were also discussed. As the ratio of assets and liabilities grow in relation to payroll and as the ratio of actives to retirees decrease, contribution rate volatility will increase.

Mr. Newton discussed the Sustainability Checklist. The checklist reviews a number of metrics, which taken as a whole, is indicative of the health of the retirement plan. A couple of items were noted: 1) longer term liability to payroll ratios will increase rate volatility and 2) higher funded ratios might lead to benefit enhancement pressure.

Overall, system-wide health continues to improve. With no changes in assumptions, the expectation is for increasing funded ratios over the next few valuations and continued stability in contribution rates.

Mr. Jeffers moved that the Board accept the December 31, 2016 actuarial valuation prepared by its consulting actuary and certify contribution rates for municipalities for 2018. Mr. Philibert seconded the motion, which passed 5-0.

4. **Securities Lending Considerations (formerly #3 on the Thursday, May 18, 2017 agenda)**
Mr. Weiner reviewed the history of the Securities Lending Program including the decision to terminate the program last year. Although Deutsche Bank continued to face organizational challenges, they have not had any program failures or major issues since we exited the program.

Due to competing initiatives, regulatory uncertainty, expected changes in security settlement cycles and other securities lending industry changes, Fixed Income Staff and RVK recommend postponing the analysis of restarting the securities lending program until 2018.

5. **Consider and Act on Private Equity Manager Search Recommendation(s) (formerly #4 on the Thursday, May 18, 2017 agenda)**

Mr. Schelling and Mr. Tindell presented the Private Equity Manager Search recommendation with Brian Borton and Tracy Harris from StepStone Group. The 2017 Private Equity search process timeline was reviewed as well as the search process objectives.

The manager search process was discussed. Two managers representing three funds were recommended as follows: Capital Partners Private Equity Income Fund III, L.P. (Capital Partners) Altaris Health Partners IV, L.P. (Altaris), and Altaris Constellation Partners IV, L.P. (Constellation).

The portfolio construction considerations were discussed including strategy diversification, manager implementation and geographic diversity. Mr. Schelling provided an Executive Summary of the Manager Recommendation.

The first recommendation was Capital Partners. They are an experienced investment team with no turnover. The three managing Directors have substantial experience in the U.S. lower middle market. The firm has an attractive strategy and differentiates itself by employing a low-debt capital structure to enable quarterly cash distribution to investors. Capital Partners has a loss ratio of 0%. Issues to consider include Fund II performance and mixed sourcing strategy. StepStone noted that both of these managers are incredibly selective of their investors, which is a testament to the staff's efforts.

The next recommendations were Altaris and Constellation. Altaris Capital Partners (ACP) is an investment firm focused exclusively on the healthcare industry. Both Altaris and Constellation will continue the Firm's strategy of investing in companies that operate across the healthcare industry, including pharmaceuticals, medical devices, services and IT sectors. The two co-founders and managing Directors have an average of twenty years working in private equity and an average of 28 years of relevant experience. Altaris has healthcare industry expertise and an impressive low loss ratio of just 6% across all funds. Issues to consider include a relatively small team, a largely unrealized Fund III and a significant fund size increase.

Mr. Philibert moved that the Board:

- (i) Authorize the following allocation(s), each as proposed and in accordance with the TMRS Investment Policy Statement, with an initial investment allocation up to the amount set out below and at fees no greater than presented in the TMRS Staff memo, each individually contingent on final investment committee approval from StepStone, favorable background checks, if required below, and successful negotiation of the investment agreements:

| Name of Investment Manager, Investment Fund, or Fund Strategy | Asset Class Strategy | Initial Investment Allocation | Background Check Required (Yes or No) |
|--|----------------------|-------------------------------|---------------------------------------|
| Capital Partners Private Equity Income Fund III, L.P. (Capital Partners) | Buy-Out | \$70 million | Yes |
| Altaris Health Partners IV, L.P. (Altaris) | Buy-Out | \$50 million | Yes |
| Altaris Constellation Partners IV, L.P. (Constellation) | Buy-Out | \$12.5 million | Yes |

- (ii) Approve and incorporate by reference for all purposes the Board Standard Investment Authorizations for each such investment allocation.

Ms. Oakley seconded the motion, which passed 5-0.

6. Investment Staff Quarterly Report/Asset Class (formerly #5 on the Thursday, May 18, 2017 agenda)

Mr. Carlson presented the Investment Staff quarterly report and discussed the Investment portfolio asset allocation as of March 31, 2017, noting that progress is being made with the current allocation, commitments and targets. Net one year and five year performance by asset class was reviewed.

Each asset class was reviewed and included an overview of the asset class, managers selected to date, current versus target allocation, active versus passive allocation and performance. Mr. Carlson discussed the Non-Core Fixed Income benchmark mismatch.

The Real Estate Portfolio's diversification by property type, geographic distribution and sector was reviewed.

Mr. Carlson reported that the Real Return portfolio is being diversified away from just global linkers. Due to the varied nature of the Real Return space, the portfolio will include strategies across a variety of real asset types as well as a number of investment vehicle types

in order to maintain a diversified approach and that a benchmark change recommendation will be forthcoming to reflect that diversification.

Mr. Carlson gave an overview of the Compliance Program and discussed both automated and manual testing. The upcoming changes to the compliance methodology were highlighted.

The Risk Management program was reviewed and both the old method of reporting and new method of reporting were discussed. Mr. Carlson reported we are currently within risk tolerances across the entire portfolio. The total fund and asset class regional exposures were reviewed as well as risk evolution over time.

7. Chief Investment Office Management Update, Including Governance, Personnel, Manager Updates, Negative Interest Rates and Other Investment Related News or Matters (formerly #6 on the Thursday, May 18, 2017 agenda)

Mr. Carlson began with two Staff recognitions. Tom Masthay was recognized by Chief Investment Officer Magazine as one of their "Top 40 under 40" picks and Ms. deLivron was recognized by Institutional Investor as a Hedge Fund Rising Star. Ms. deLivron recently accepted a position at another firm and Mr. Carlson indicated we are recruiting for Ms. deLivron's position as well as the Operations and Performance Analyst.

In the first quarter, the Investment team took 367 manager meetings.

The transition to the State Street Enhanced Asset Owner Strategies (EAOS) plan was reviewed. The increased number of capital calls and the complexity of each were discussed. Due to the transition, all Operations Policies and Procedures are currently being reviewed. The EAOS Service Level Agreement is currently being reviewed line by line with EAOS Team. The best practices review is scheduled for June.

Mr. Gavia asked for an update on the pacing plan. Mr. Carlson noted the supplemental items are included in the Board materials. He discussed the reasons for not including the Non-Core Fixed Income Manager Search recommendation at this time as originally scheduled in the Pacing Plan.

8. Executive Session (formerly #7 on the Thursday, May 18 2017 agenda)

At 4:12 p.m., the Board entered into Executive Session, pursuant to Texas Government Code §§551.071 and 551.074 to consult with Legal Counsel to receive legal advice, and to discuss personnel matters. No action was taken during the Executive Session and all members of the Board that were present before the executive session were still present. The meeting was opened to the public again at 5:46

Mr. Landis moved that the Board adjourn the meeting. Mr. Jeffers seconded the motion, which passed 5-0. At 5:47 p.m. the meeting was adjourned.



David Gavia
Executive Director



Jim Parrish
Chair, Board of Trustees

**MINUTES OF THE
TEXAS MUNICIPAL RETIREMENT SYSTEM
Joint Meeting of the Board of Trustees and
Advisory Committee on Benefit Design**

May 19, 2017 - 9:00 a.m.

On May 19, 2017, the Board of Trustees of the Texas Municipal Retirement System (TMRS) convened for a meeting at 9:00 a.m. at the Lakeway Resort, located at 101 Lakeway Drive in Austin, Texas, with the following members present:

Board of Trustees

Jim Parrish, Chair
Bill Philibert, Vice Chair
Jim Jeffers
David Landis

Absent: Roel "Roy" Rodriguez
Julie Oakley

Advisory Committee Members

Cody Hill, Arlington Professional Fire Fighters Association
David Riggs, Texas State Association of Fire Fighters
Greg Shipley, Combined Law Enforcement Associations of Texas
Bonita Hall, Texas Municipal Human Resources Association
Greg Vick, Texas City Management Association
Kevin Lawrence, Texas Municipal Police Association
Wanda Heard, City of San Antonio
Michael Dane, City of San Angelo
Heidi Manti, Service Employees International Union

Present also were:

David Gavia, Executive Director
Eric Davis, Deputy Executive Director
Christine Sweeney, General Counsel
TJ Carlson, Chief Investment Officer
Rhonda Covarrubias, Director of Finance
Leslee Hardy, Director of Actuarial Services
Bill Wallace, Director of Communications
Dan Wattles, Director of Governmental Relations
Sandra Vice, Director of Internal Audit
Leslie Ritter, Director of Human Resources
Robert Klausner, Klausner, Kaufman, Jensen & Levinson
Karen Jackson, Executive Assistant
Marcia Beard, RVK
Amy McDuffee, Mosaic Governance Advisors

Also in attendance:

David Rodriguez, Regional Manager – City Services
Andi Focht-Williams, Senior Auditor
Keith Brainard, National Association of State Retirement Administrators
Gary Shilling, A. Gary Shilling and Company
George Kaufman, City of Garland

Mr. Parrish called the meeting to order at 9:00 a.m. Mr. Parrish requested that members of the Advisory Committee on Benefit Design introduce themselves and indicate which group they represent.

1. Pension Trends Presentation

Mr. Gavia introduced Mr. Keith Brainard, Research Director for the National Association of State Retirement Administrators. Mr. Brainard began with an overview of the statistics associated with public pension plans in the U.S. including assets, members, retirees and funding levels. He stated that TMRS is well funded. He noted funding levels for the country as a whole are improving and the national trend of reforms made across the country has stabilized many pension plans. Mr. Brainard discussed the stigma being attached to pension plans that are not making required contributions.

Public sector salary growth is improving, but still modest. Mr. Brainard reviewed revenues received by state and local governments and noted year-over-year the ratio of active members to retirees has been decreasing. The combination of low revenue, payroll and salary growth as well as declining active members can foretell funding issues for plans that are not currently well funded. Spending on public pension plans has been improving, but still is not to the level that is required to keep plans actuarially sound. Investment return assumptions were reviewed.

Mr. Brainard highlighted public pension plans in Texas. Employees in Texas are responsible for more of the financial cost of pension plan funding compared to the national average.

During this Legislative Session in Texas, two primary themes have been noted: the funding of retiree health care benefits for the Teachers Retirement System and addressing the pension plan funding problems in Dallas and Houston. Mr. Brainard reviewed current legislation for the Dallas and Houston Bill. He highlighted the Houston proposal for the pension plan funding and discussed it from the Pension Review Board's perspective.

2. Annual Economic Outlook Presentation

Dr. A. Gary Shilling was introduced by Mr. Gavia and was asked to provide an overview of the current economic conditions. Dr. Shilling began by discussing the expectations of the "Trump Bounce" and how investors are now reassessing the policies. He discussed how this assessment of the state of affairs translated into the pricing of commodities, the strength of the dollar and emerging markets, stock and bonds indices. Dr. Shilling feels that there is going to be some substantive improvement coming out of the election and he also feels that

we are going to see a period of rapid economic growth. There may be substantial deficits coming out it. The growth range should be 3% to 3.5%, but it will take some time. This is the first major theme.

The second major theme is globalization. Chinese growth has definitely slowed and in the United States, more jobs were lost than created. Dr. Shilling indicated that globalization has nearly ended.

The third theme is the aging of population. Dr. Shilling reviewed fertility rates and life expectancies in various countries and he also discussed the working population in comparison to total population. As populations age, there is a need for people to take care of the retirees. The United States is an exception since the population continues to grow, primarily due to immigration. The U.S. Labor Force participation rates were reviewed.

The Asia phenomenon is the fourth theme and this is principally driven by exports. The Asian economy is not consumer driven.

The last theme is inflation. Inflation and deflation were reviewed especially during periods of war and peace. Prices of goods are declining due to globalization, but service prices are increasing. The odds are for low inflation in the future and this low inflation will translate to lower interest rates.

3. **Overview of the 85th Legislative Session, Presentation of Legislative Committee Report and Discussion of Filed and Proposed Legislation, Including Solicitation of Board Direction to the Legislative Committee and Staff on Selected Matters, if desired (formerly #4 on the Friday, May 19, 2017 agenda)**

Mr. Wattles thanked the Advisory Committee for their service and input prior to the Session. There are only ten days left in the 85th Regular Legislative Session. Of the 7,000 bills that have been filed, TMRS is tracking 384 bills, which is a 25% increase from the previous Session. Of the 385 bills, 55 are pension-related bills which is a 30% increase over the previous legislative session.

The Budget has been the primary focus and there has been concern expressed about the Senate and House being able to come to agreement.

Mr. Wattles reviewed the pension bills and discussed the status of the Dallas Police and Fire pension bill as well as the bill affecting the three City of Houston pension systems.

Regarding the bills that directly affect TMRS, House Bill 3056 (Meyer) would allow the City of University Park to adopt an ordinance allowing the City to enroll "first hired" fire fighters into TMRS and effectively close their TLFRA plan. For this to occur, University Park must complete the applicable process outlined in the bill before October 1, 2018. The bill has been passed out of the Senate State Affairs Committee and is headed to the Senate floor.

The other bills that directly affect TMRS are not procedurally viable. With regards to the ethics bills discussed at the March Board meeting, of the eight bills that proposed to suspend

the annuity of members or retirees who have committed certain felonies while in office, only one bill has passed both chambers which is SB 500 (Taylor). Mr. Wattles also discussed two other bills authored by Senator Huffman, SB 509 which is the investment reporting bill and SB 936 (Huffman) which proposes to create a joint interim committee composed of three senators appointed by the Lt. Governor and three house members appointed by the Speaker of the House to study various retirement plan alternatives to defined benefit plans.

Mr. Wattles reviewed the HB 4016 commonly referred to as the “dead peasants” bill and noted that this bill is procedurally no longer viable. However, the bill will be tracked until the session is over.

4. **Executive Director Update (formerly #5 on the Friday, May 19, 2017 agenda)**

Mr. Gavia introduced Mr. Wallace to discuss the recognition for Transparency in Reporting that TMRS received from the Center for State and Local Government Excellence. TMRS was one of five pension plans in the country that were recognized for “promoting best practices in health and retirement benefits, workforce planning and strategies to attract, retain, and develop talent.” Mr. Wallace stated the recognition was the result of a team effort across all TMRS departments, including Finance, Actuarial Services, Legal, Governmental Relations, Communications, Investments, Information Systems and the Executive Staff.

The report was prepared by Joshua Franzel and Elizabeth Kellar of the Center for State and Local Government as well as Paula Sanford of the University of Georgia. Keith Brainard and Alex Brown of the National Association of State Retirement Administrators also provided input. Mr. Wallace described the process of the study and the meetings that took place between TMRS Staff and Mr. Franzel.

The study addressed compliance with the Government Finance Officers Association and other standards where applicable. Eighty-three systems were sampled across the United States and Mr. Wallace highlighted the number of systems that offer various actuarial reports, funding policies, investment information, basic benefit information, and financial/actuarial information to their members.

Five systems were recognized as “exemplary” and TMRS was included. Mr. Wallace described the characteristics of an exemplary system as well as the four notable strengths of TMRS.

Past recognition of TMRS included being named Public Plan Sponsor of the Year for 2009 by Plan Sponsor Magazine. In the Texas State Comptroller Report for 2012, TMRS was one of only three plans that received “all green,” or passing marks, on their scorecard for meeting benchmarks for funded ratio, amortization, and contribution practices.

The Board thanked Staff and the Advisory Committee for their hard work.

5. **Call for Future Agenda Items(formerly #6 on the Friday, May 19, 2017 agenda)**

No items were discussed.

Mr. Philibert made a motion the meeting be adjourned. Mr. Landis seconded the motion, which passed 4-0. The meeting was adjourned at 10:55 a.m.



David Gavia
Executive Director



Jim Parrish
Chair, Board of Trustees