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

December 8, 2016 – 1:30 p.m.

On December 8, 2016, the Board of Trustees of the Texas Municipal Retirement System (TMRS) convened for a meeting at 1:30 p.m. at TMRS Headquarters, located at 1200 North IH 35 in Austin, Texas, with the following members present:

Board of Trustees
Jim Parrish, Chair
Bill Phlipert, Vice Chair
Julie Oakley
Roel “Roy” Rodriguez
David Landis
Jim Jeffers

Present also were:

David Gavia, Executive Director
Eric Davis, Deputy Executive Director
TJ Carlson, Chief Investment Officer
Christine Sweeney, General Counsel
Robert Klausner, Klausner, Kaufman, Jensen & Levinson
Dan Wattles, Director of Governmental Relations
Leslee Hardy, Director of Actuarial Services
Debbie Munoz, Director Member Services
Scott Willrich, Director of Information Resources
Bill Wallace, Director of Communications
Rhonda Covarrubias, Director of Finance
Jesse Pittman, Project Manager
Sandra Vice, Director of Internal Audit
Leslie Ritter, Director of Human Resources
Kristin Qualls, Director of Public Equity
Chris Schelling, Director of Private Equity
Tom Masthay, Director of Real Assets
Jason Weiner, Director of Fixed Income
Dimitry Shishkoff, Director of Risk Management
Karen Jackson, Executive Assistant
Marcia Beard, RVK
Weston Kasper, RVK
Amy McDuffee, Aon Hewitt Investments
Brian Borton, StepStone
Joe Newton, Gabriel, Roeder, Smith & Company

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Also in attendance:

Michelle Mellon-Werch, Assistant General Counsel
Nick O’Keefe, Senior Staff Attorney
Madison Jechow, Assistant General Counsel
Michael Schaff, Assistant General Counsel
Tish Root, Legal Assistant
David Rodriguez, Regional Manager – City Services
Melanie Thomas, Editor
Carol Leung, Equities Investment Analyst
Chris Tindell, Private Equity Analyst
Cindy Morse, Investment Support Analyst
Debbie Farahmandi, Investment Operations Specialist
Peter Jeske, Project Specialist
Kate Reed, Compliance Officer
Eddie Schultz, Real Estate Analyst II
Rachel Cleak, Alternative Analyst
Melissa Jerkins, Quantitative Analyst
Carol Leung, Investment Analyst II
Paula Nguyen, Investments Accountant
Stacy White, Executive Assistant
Ariel Chou, Actuarial Analyst
Sean Thompson, Regional Representative – City Services
Ron Lewis, Ron Lewis & Associates
Bob Scott, City of Carrollton
Greg Shipley, Combined Law Enforcement Associations of Texas
David Crow, Arlington Professional Fire Fighters
Cody Hill, Arlington Professional Fire Fighters
George Kaufman, City of Garland
Keith Dagen, Government Finance Officers Association of Texas
Brad McCutcheon, Texas State Association of Fire Fighters
Kathleen Depweg, City of Arlington
Mitch Slaymaker, Texas Municipal Police Association
Michelle Kranes, Deputy Director, Pension Review Board
Andrew Clark, Speaker’s Office

Mr. Parrish called the meeting to order at 1:30 p.m. Ms. Oakley gave the invocation and the Pledge of Allegiance was recited.

1. **Consider and Act on Consent Agenda**

   Mr. Gavia stated that Staff had nothing to add to the consent agenda as presented. There were no changes suggested by the Board.

   Mr. Jeffers made a motion that the Board adopt the consent agenda as presented. Mr. Philibert seconded the motion, which passed 6-0.

2. **Executive Director Update – Governmental Relations**
Mr. Gavia introduced Mr. Wattles to present the overview of the Governmental Relations department. Mr. Wattles discussed the area of responsibilities and acknowledged that all areas of the organization participate in the governmental relations function. He reviewed his background and introduced Stacy White and explained her role.

Mr. Wattles discussed how his department coordinates TMRS’ interaction with the Texas Legislature. This includes bill tracking, bill analysis, preparation of legislative presentations, attendance at hearings and liaison with other legislative agencies including the U.S. Congress. He discussed Board-related support responsibilities, including coordinating the Minimum Education Training program for trustees.

Mr. Wattles highlighted the accomplishments of the Governmental Relation department. These include bill passage, Board training, legislative district reports and conducting and responding to surveys.

3. Legislative Committee Update

Mr. Wattles and Mr. Lewis began with a post-election update. Mr. Lewis discussed what he called the “Donald Trump” effect. Winning the election really did not impact statewide elections and very few seats changed. Texas should be well represented in the Trump administration.

Mr. Lewis reviewed various hot topic issues this session that could cause conflicts between the House and the Senate. School funding and Child Protective Services will both get a lot of attention. Pension issues will be a “battle ground” given the issues surrounding the cities of Houston, Dallas and Fort Worth. TMRS needs to be very vigilant regarding what may come our way.

Mr. Parrish asked what could come TMRS’ way. Mr. Lewis responded that Houston has a restructuring plan, but Dallas does not. Representative Dan Flynn, Chair of the House Pensions Committee knows there are several challenges facing his Committee. Currently, TMRS is not being looked at other than to say we are doing things correctly. Defined Contribution plans and all other options will likely be reviewed. Since TMRS has been successful, this may be why we could be looked at more closely.

Mr. Landis asked if SB 2 will be contentious (tax bill) and if it could possibly be an issue. Money is going to be tight which will cause contention and Mr. Landis noted that it could affect how cities balance their budgets, thus potentially, affecting benefits.

Mr. Wattles noted that a Defined Contribution bill (SB 151) has been filed affecting certain non-TMRS cities. Mr. Parrish noted that there seems to be a Defined Contribution bias on the part of the Pension Review Board (PRB) Chair, but TMRS has done a good job working with PRB staff.

Mr. Wattles discussed several issues have occurred on the federal level. There are several bills that continue to be filed, but have not passed due to “legislative grid lock”, but they may become active again.
4. Consider and Act on Legislative Agenda Items, Including Draft Legislation
Mr. Gavia discussed how the draft Return to Work bill was created, and that it was staff’s goal to determine if the draft legislation meets the Board’s goal.
Mr. Wattles gave an overview of the draft bill. One of the goals of the draft bill was when an individual returned to work for a reemploying municipality, the suspended payments would be tracked and upon re-retirement, the amount of the suspended payments would be re-annuitized without interest. Mr. Wattles noted several items that would have to be worked through. First, we had to determine how to handle the eight year gap exception to the return to work provision. The transition section of the draft bill provides that for retirees who already are or become eligible for the existing “8 year gap” provision before the effective date of the bill, but have not re-retired before the effective date of the bill, would still receive a lump sum payment of their suspended payments and would not have their annuity recalculated when they do re-retire. Second, the re-annuitization would only occur once and the reannuitization would be in the original form of the benefit. Finally, there is no guarantee that all the suspended payments would be recaptured since the payments are reannuitized, and that retirees may or may not live to their life expectancy based on TMRS’ mortality assumptions.

Mr. Wattles discussed the potential cost of the bill. The proposal affects a number of different departments within TMRS and also presents a number of unique challenges. The cost could range from approximately $272,000 to $800,000, depending on the effective date of the bill and whether development of the changes occur in-house or are contracted out to external vendors.

Mr. Rodriguez stated that since the Board’s original vote was not unanimous along with multiple other reasons, he moved that the Board’s previous action to move forward with the bill be tabled and that a bill not be advanced on this issue at this time. Ms. Oakley seconded the motion and stated she was not comfortable moving forward. She indicated that the work and efforts of the Advisory Committee, Staff and the Board are not lost. Mr. Landis agreed with this action.

Mr. Rodriguez made a motion that the Board not approve the proposed legislation. Ms. Oakley seconded the motion, which passed 6-0.

5. Consider and Act on Board Resolution for Legislative and Regulatory Matters
Mr. Gavia presented the draft resolution and noted the historical basis for its adoption. He explained that this resolution is slightly broader than in the past to give the Legislative Committee more room to act or react to issues that may arise during the session or from other legislative agencies.

Ms. Oakley made a motion that the Board approve the resolution with amendments to be made to remove the language about the filing of return to work legislation and to reflect that the Board chose not to propose any changes to the current TMRS plan design at this time. Mr. Landis seconded the motion, which passed 6-0.
6. **Consider and Act on Legislative Committee Charter**
Ms. McDuffee presented the draft of the Legislative Committee Charter. She noted that this charter is consistent with other Board Committees.

Key responsibilities include: 1) to monitor and review federal and state legislative regulatory issues, 2) to review proposed potential legislation, and 3) assisting the Board in facilitating the System’s legislative and regulatory communications. This Committee would be required to report back to the Board; it would not be autonomous. The charter does permit the Board Chair and Committee Chair to speak or act on behalf of TMRS in certain circumstances.

Mr. Jeffers made a motion that the Board adopt the proposed Legislative Committee Charter as presented. Mr. Rodriguez seconded the motion, which passed 6-0.

7. **Consider and Act on Committee Appointment(s) and Reappointment(s)**
Mr. Gavia noted that since the committees have become more formalized, appointments or reappointments of Committee members will provide continued structure to the Committees. Mr. Parrish presented the current Committee assignments.

Mr. Philibert made a recommendation to the Advisory Committee on Benefit Design. He recommended that Mr. Landis serve as the Chair and Mr. Landis accepted.

Mr. Jeffers made a motion that the Board approve the appointments and reappointments to the following Committees for the calendar year 2017 with the recommendation that Mr. Landis serve as Chair to the Advisory Committee on Benefit Design:

- **Advisory Committee on Benefit Design**
  - Chair: David Landis
  - Vice Chair: Roy Rodriguez

- **Internal Audit Committee**
  - Chair: Jim Jeffers
  - Vice Chair: Julie Oakley

- **Compensation Committee**
  - Chair: Julie Oakley
  - Vice Chair: David Landis

- **Legislative Committee**
  - Chair: Jim Parrish
  - Vice Chair: Bill Philibert

Mr. Rodriguez seconded the motion, which passed 6-0.

8. **Consider and Act on Non-Core Fixed Income Manager Search Recommendation(s)**
Mr. Weiner and Mr. Kasper from RVK discussed how the Non-Core Fixed Income portfolio was constructed. In this search, managers were identified in the areas of corporate credit, structured products and direct lending. These proposed portfolios target specific investment
profiles that are expected to help achieve TMRS’ long term return and diversification objectives. The managers selected utilize best in class credit capabilities, complement the existing managers, and should improve the return profile and diversification of the Non-Core Fixed Income portfolio. They are managers that can tactically and strategically position their portfolios based on a relative value orientation predicated on their views of the economic and credit cycles. The manager search process focused on managers in areas of the portfolio that needed to be broadened and the standard process was followed. Four managers were selected for approval: Adams Street Private Credit Fund-A LP (Adams Street), Bain Capital Credit (Bain), GoldenTree Asset Management LP (GoldenTree) and Waterfall Eden Fund LP (Waterfall).

The first recommendation is Adams Street. Mr. Weiner reviewed the firm, their background and experience. TMRS would be a founding investor in the fund. Debt investments will include senior debt, unsecured debt. The risk of this fund is that it is a new fund with a team that was recently established, but that risk is mitigated by Mr. Bill Sacher’s, Partner and Head of Private Credit, proven experience of building out successful teams. In addition, the depth of the resources available from the broader Adams Street platform should further mitigate TMRS’ risk.

The next manager is Bain Capital. The firm is 100% employee owned and manages the full spectrum of credit strategies including leveraged loans, high yield bonds, distressed debt, direct lending, structured products, non-performing loans (NPLs) and equities. Bain employs a diversified investment approach which complements our more concentrated managers.

Golden Tree is a high conviction manager that builds concentrated portfolios relative to its peers. It has a disciplined fundamental value analysis investing only where there is a catalyst to realize value and a margin of safety that limits the risk of loss.

Waterfall is the final manager and they specialize in structured credit, namely high yield asset backed securities and loans. The team has deep experience and expertise with a five member Investment Committee charged with looking at thematic perspective, new sectors, large trades and European opportunities.

Mr. Philibert moved that the Board approve the following:

(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 favorable background checks, if required below, and successful negotiation of the investment agreements:
<table>
<thead>
<tr>
<th>Name of Investment Manager, Investment Fund, or Fund Strategy</th>
<th>Asset Class Strategy</th>
<th>Initial Investment Allocation</th>
<th>Background Check Required (Yes or No)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Adams Street Private Credit Fund-A LP (Adams Street)</td>
<td>Direct Lending</td>
<td>$200 million</td>
<td>Yes</td>
</tr>
<tr>
<td>Bain Capital Credit, LP (Bain)</td>
<td>Relative Value Credit</td>
<td>$100 million</td>
<td>Yes</td>
</tr>
<tr>
<td>GoldenTree Asset Management, LP (GoldenTree)</td>
<td>Relative Value Credit</td>
<td>$200 million</td>
<td>Yes</td>
</tr>
<tr>
<td>Waterfall Eden Fund, LP (Waterfall)</td>
<td>Structured Products</td>
<td>$200 million</td>
<td>Yes</td>
</tr>
</tbody>
</table>

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

Mr. Landis seconded the motion, which passed 6-0.

9. **Consider and Act on Private Equity Manager Search Recommendation(s)**

Mr. Schelling reported to the Board that the Executive Director approved an $18.75 million co-investment of GSO COF III co-investment fund.

Mr. Schelling and Mr. Borton from StepStone Group stated that TMRS will be very close to its Private Equity pacing plan target. Mr. Schelling reviewed the manager search objectives and the process. This search focused on buy-out managers in the top quartile. One manager is recommended for approval, Incline Equity Partners.

Mr. Schelling reviewed the portfolio construction considerations that led to this manager search highlighting strategy considerations, manager implementation and geographic diversification. Incline Equity Partners will continue its strategy of investing in specialized manufacturing, business and industrial services and value-added distribution businesses operating in North America. They have an established and strong track record with three prior top quartile funds as well as a low loss ratio, just 5% across all funds. Risks include fund size which has been mitigated by fund discipline and modest turnover.

Mr. Landis moved that the Board of Trustees approve the following:

(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 favorable background checks, if required below, and successful negotiation of the investment agreements:
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<th>Name of Investment Manager, Investment Fund, or Fund Strategy</th>
<th>Asset Class Strategy</th>
<th>Initial Investment Allocation</th>
<th>Background Check Required (Yes or No)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Incline Equity Partners IV LP (Incline)</td>
<td>Buyout</td>
<td>$50 million</td>
<td>Yes</td>
</tr>
</tbody>
</table>

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

Mr. Philibert seconded the motion, which passed 6-0.

10. Consider and Act on 2017 System-wide Investment Pacing Plans
Mr. Carlson presented the 2017 System-wide Investment Pacing Plan (SIPP). Including committed allocations, TMRS is within its target ranges for all asset classes. He discussed the asset class reviews and turnover of managers that occur each year. The plan is constantly under review and subject to change as needed. Mr. Carlson highlighted the 2017 goals for each asset class and explained the expected shifts as well as the need for potential rebalancing and flexibility. He reviewed some of the Investment department projects in 2017 and beyond.

Ms. Oakley asked if the Board needs to take action on this SIPP or if it needs to be changed. Mr. Carlson gave a historical perspective on the reasons why it is adopted. Ms. Sweeney noted that flexibility can be added to the Board’s approval to prevent the need for additional action to permit a change.

Mr. Carlson noted that the Pacing Plan does include a footnote stating that, while every effort will be made to allocate these opportunities as presented, there are times when items may need to be moved. He also mentioned that the Pacing Plan is included in the Supplemental presentation to the Quarterly Staff Report that is provided to the Board each quarter. Ms. Oakley commented that it would be helpful if the Pacing Plans were available in one location so the Board could see at a glance how the Pacing Plan has evolved. Mr. Carlson indicated that he can provide the Pacing Plans to the Executive Office to upload to the Diligent Resource section for consistency.

Ms. Oakley made a motion that the Board approve the 2017 SIPP and authorize Staff to make changes in the implementation of the plan with notice given to the Board at the next meeting. Mr. Jeffers seconded the motion, which passed 6-0.

11. Consider and Act on Proposed Revision to Investment Policy Statement
Mr. Carlson noted that only two changes were made since the Investment Policy Statement (IPS) was presented at the October Board meeting.

The first change concerned co-investments. The co-investment language was moved to a general location instead of placing it in each individual asset class guidelines since it pertains
to all asset classes. The Executive Director’s authority to approve co-investments was moved to the Executive Director section of the IPS.

The second change involved the removal of descriptive language or language that was duplicative or no longer necessary due to the current status of the program.

Mr. Jeffers made a motion to approve the amendments to the IPS as presented. Ms. Oakley seconded the motion, which passed 6-0.

12. Consider and Act on Election of Board Officers
Mr. Gavia reviewed the historical background for the election of Board officers and noted that a formal policy is not in place. The Board has typically selected an Employee and an Executive trustee as Board officers with the Employee and Executive trustees alternating offices each year. However depending on when a Trustees is appointed, it may not always be feasible to always have an Employee and Executive Trustee sit as Chair and Vice Chair each year. In many cases, the Vice Chair has moved up to be the Chair the following year. However, Board By-laws do not prevent a Board member from serving as Board Chair or Vice Chair more than once.

Ms. Oakley made a motion to keep the current Chair and Vice Chair for 2017, Chair Jim Parrish and Vice Chair Bill Philibert. Mr. Rodriguez seconded the motion, which passed 6-0.

13. Executive Session
At 4:36 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 except Julie Oakley that were present before the executive session were still present. The meeting was opened to the public again at 5:50 p.m.

At 5:50 p.m. the meeting was recessed until 8:30 a.m. on Friday, December 9, 2016.

David Gavia
Executive Director

Jim Parrish
Chair, Board of Trustees
MINUTES OF THE
TEXAS MUNICIPAL RETIREMENT SYSTEM
Meeting of the Board of Trustees

December 9, 2016 – 8:30 a.m.

On December 9, 2016, the Board of Trustees of the Texas Municipal Retirement System (TMRS) reconvened for a meeting at 8:30 a.m. at TMRS Headquarters, located at 1200 North IH 35 in Austin, Texas, with the following members present:

**Board of Trustees**
- Jim Parrish, Chair
- Bill Philibert, Vice Chair
- Roel “Roy” Rodriguez
- David Landis
- Julie Oakley
- Jim Jeffers

Present also were:
- David Gavia, Executive Director
- Eric Davis, Deputy Executive Director
- Christine Sweeney, General Counsel
- TJ Carlson, Chief Investment Officer
- Robert Klausner, Klausner, Kaufman, Jensen & Levinson
- Rhonda Covarrubias, Director of Finance
- Leslee Hardy, Director of Actuarial Services
- Debbie Munoz, Director of Member Services
- Bill Wallace, Director of Communications
- Dan Wattles, Director of Governmental Relations
- Scott Willrich, Director of Information Resources
- Jesse Pittman, Project Manager
- Sandra Vice, Director of Internal Audit
- Leslie Ritter, Director of Human Resources
- Kristin Qualls, Director of Public Equity
- Chris Schelling, Director of Private Equity
- Tom Masthay, Director of Real Assets
- Jason Weiner, Director of Fixed Income
- Dmitry Shishkoff, Director of Risk Management
- Karen Jackson, Executive Assistant
- Marcia Beard, RVK
- Amy McDuffee, Aon Hewitt Investments

Also in attendance:
- David Rodriguez, Regional Manager – City Services
- Madison Jechow, Assistant General Counsel
- Adrienne Strong, Human Resources Generalist
- Melanie Thomas, Editor
Mr. Parrish called the meeting to order and the meeting was reconvened at 8:30 a.m. Ms. Oakley was not present at the start of the meeting.

14. **Consider and Act on New Appointments and/or Reappointments to the Advisory Committee on Benefit Design (formerly agenda item #18 on the Friday, December 9, 2016 agenda)**

Mr. Wattles noted this action is to appoint and reappoint representatives to the Advisory Committee on Benefit Design.

The Texas Municipal Police Association (TMPA) has nominated Kevin Lawrence, the organization’s Executive Director, to be their representative and Mitch Slaymaker, their Deputy Executive Director to be the designated alternate. The Arlington Professional Fire Fighters Association has nominated Cody Hill, a firefighter with the City of Arlington to succeed David Crow as the designated alternate to their current representative. Mr. Langley has also applied to serve a second, three-year term on the Committee.

The Advisory Committee Chair and Vice-Chair approved the nominations to move forward and the nominations also recognize the changes to the Charter in 2018.

Mr. Rodriguez moved that the Board approve the following:
• Appoint Kevin Lawrence to a 2-year term to expire on December 31, 2018 and appoint Mitch Slaymaker as an alternate representative for the Texas Municipal Police Association on the TMRS Advisory Committee on Benefit Design in the Group Class.

• Appoint Cody Hill as an alternate representative for the Arlington Professional Fire Fighters Association on the TMRS Advisory Committee on Benefit Design in the Group Class.

• Appoint Bryan Langley to a second, three-year term to expire on December 31, 2019 on the TMRS Advisory Committee on Benefit Design in the Individual Class.

Mr. Jeffers seconded the motion, which passed 5-0.

15. Chief Investment Officer Management Update, Including Governance, Personnel, Manager Update and Other Investment Related News or Matters (formerly agenda item #19 on the Friday, December 9, 2016 agenda)
Mr. Carlson announced that Michael Humphrey, co-founder of Courtland Real Estate Advisors, passed away suddenly. Mr. Humphrey was our account lead so TMRS will need to work through the associated account changes. Mr. Parrish requested a letter of condolence be prepared for the family.

Mr. Carlson informed the Board of the co-investment approved with GSO. Materials and information are provided in the Board package.

Mr. Carlson also notified the Board of the rebalancing of the Absolute Return category. The rebalance was from BAAM to the direct funds. Information regarding this $215 million rebalance is provided in the Board materials. One more rebalance is currently scheduled for April 2017.

16. Public Equity Asset Class Annual Review (formerly agenda item #20 on the Friday, December 9, 2016 agenda)
Ms. Qualls and Ms. Leung presented the annual Public Equity Asset class review. Ms. Qualls began by reviewing the asset class objectives. She reviewed the steps taken in the annual review process and the history of the public equity diversification. She presented the portfolio management structure which detailed each portfolio’s strategy type and portfolio benchmark.

Ms. Qualls reviewed the current allocation versus the target equity allocation with the current overweight for the total equity portfolio as the funding source for the Real Estate and Private Equity asset classes’ strategic target allocations. She also discussed the current U.S. and non-U.S. underweights in the active portfolio. Ms. Leung briefly discussed the public equity performance while Ms. Qualls provided more up-to-date performance numbers vs. the date of the report.

Ms. Leung reviewed the Investment Policy Statement (IPS) monitoring and portfolio review. The first review is to exceed an appropriate benchmark net of fees over rolling five year
periods. The second review is the manager rank in an appropriate universe of Managers possessing a similar style over rolling five year periods. All active managers do not have a 5 year track record, but the equity team determined all managers were within acceptance based on the qualitative evaluation.

Ms. Leung briefly mentioned the equity strategies that were reviewed for the 2016 review and provided information on the return/risk objectives for each of the active strategies. Ms. Leung also updated the Board on the equity market environment and the response of the different countries/regions of the global world performed both positively or negatively. She also discussed the drivers of slower economic growth going forward.

Ms. Qualls reviewed the highlights of 2016 for the public equity portfolio. In conclusion, all managers are performing in accordance with expectations and both TMRS and RVK concur that no changes are immediately needed. Staff will continue to work with managers on highlighted issues and will continue to evaluate potential changes to the equity passive/active structure in 2017. Staff will also need to determine the next steps for the Transition Management Program.

17. Investment Staff Quarterly Report/Asset Class Update (formerly agenda item #21 on the Friday, December 9, 2016 agenda)

Mr. Carlson began by reviewing the asset allocation and he noted that on a committed basis, we are near the target allocation. He reviewed the one-year and five-year performance numbers.

Mr. Carlson reviewed Fixed Income, both Core and Non-Core. Both Core managers are out performing the benchmarks. Non-Core Fixed Income is just being funded so performance versus benchmarks is not meaningful.

Mr. Masthay discussed the Real Estate portfolio and reviewed the portfolio diversification, property type, geographic and sector diversification, and performance. He also discussed Real Return and noted there are no performance numbers since these are currently being funded.

Mr. Carlson reviewed Absolute Return. There are 15 managers in the direct portfolio and he discussed the diversification in the direct and BAAM aggregate portfolios.

There are 14 managers in the Private Equity Asset Class and Mr. Schelling discussed diversification by commitment as well as diversification across the three strategies.

Ms. Reed reviewed Compliance and noted no violation of the TMRS testing guidelines.

Mr. Shishkoff gave an overview of Risk Management. Total Risk is at 7.6% compared to a policy benchmark of 8.2% which is in line with historical forward looking levels. He discussed risk by asset class and compared the evolution of risk over time. On a total basis, the portfolio is running below both the benchmark and strategic target. Mr. Shishkoff
reviewed the distribution of the total portfolio across the globe. Mr. Philibert asked about the impact of the “sum of contribution of active manager decisions.”

Mr. Carlson concluded by stating that he is continuing to work to fill the last investment position.

Mr. Parrish asked if there was an area that TMRS could manage internally and reduce the number of managers. Mr. Carlson responded that this is being reviewed, but the analysis is not yet completed.

18. Consider and Act on Proposed 2017 Operating Budget (formerly agenda item #14 on the Friday, December 9, 2016 agenda)
Ms. Oakley joined the meeting at this time. Ms. Covarrubias began by reviewing Appendix H. This Appendix combines all the departmental projections and the estimates of expenses for the remainder of 2016. She discussed projects that were completed and compared funds budgeted to actual expenditures. We anticipate expending approximately 87% of the 2016 budget.

Ms. Covarrubias moved into Section 1 of the budget document and highlighted the accomplishments in 2016. She discussed the roll-outs on the Straight-through processing, the change in imaging systems, updates to the business continuity plans, Executive Workshops across the state, completion of the Asset/Liability Study and continued portfolio diversification.

Goal 1 was reviewed. It covers the actuarial retainer and funds for possible legislative studies. Goal 2 includes funds to continue with TMRS Direct, consulting fees for re-engineering of the city payroll process and continuation of the executive workshops. Funds in Goal 3 include an additional Internal Auditor and possible co-sourced audits. Goal 4 includes funds for additional employees and new projects.

The Executive Summary is in Section II of the budget document. The budget continues to be broken down into five general categories; the general categories as a percent of the total budget remain consistent with the prior year. Personnel Services is the largest category and it consists of nine new positions, a reduction in the TMRS retirement contribution rate, funds for merit increases, a one-time sick/vacation leave buy-out program, funds for temporary employees, and funds for the same employee benefits package. Ms. Oakley asked what the mechanism is for a budget amendment, specifically with regard to contingency funds. She would like for staff to come back to the Board and ask for an amendment to the budget as opposed to “building in” contingencies. Mr. Gavia discussed that “contingency” may be the wrong word and explained what those funds would be used for. Mr. Parrish asked for clarification on the request for temporary employees. Mr. Willrich reviewed the two areas where employees are needed, but may not be needed on a permanent basis.

The Professional Services category is the second largest area of the budget. It includes general and recurring funds for investment consultants, governance/strategic planning, governmental relations, disaster recovery and network security audit. The non-recurring
funds include consulting for city payroll process reengineering, an entity-wide Compensation Study and succession planning. New funds include a contingency for IT consulting for possible legislative changes, electronic records management projects, Lexmark Content upgrade and cloud strategy consulting.

The Rentals and Equipment Maintenance category includes mostly data processing needs; new software is detailed in Appendix D, which includes software for network virtualization (“Network Micro-Segmentation with VMware NSX” business case provided).

The Miscellaneous Section includes supplies as well as dues, subscriptions, publications and training.

Ms. Covarrubias reviewed the requested nine new positions and gave a brief overview of each position. Questions were presented regarding the need for an Assistant Director and Board discussion focused on the need for the new positions and the justification. The Board noted that these requests differ from last year’s projected personnel needs.

Ms. Covarrubias discussed the three-to-five year projections, noting future new personnel in Appendix F and major items/projects in Appendix G.

Mr. Willrich gave a presentation on the Information Technology (IT) Strategy. The strategy is to support the strategic plan and looks three to five years out. The strategy continually improves, ensures resiliency and will increase efficiency and reduce costs. Mr. Willrich explained how the software development group supports this high level strategy and noted various current and future projects.

Ms. Oakley moved that the Board adopt the 2017 Proposed Operating and Capital Expenditures Budget with the removal of the $100,000 contingency for IT consulting (for possible Legislative initiatives) and the reduction of “new” funds in the banking line-item from $1.3 million to $600,000 (based on a recent proposal received by TMRS management). Mr. Philibert seconded the motion, which passed 6-0.

19. **Consider and Act on Resolution Transferring Monies from Interest Reserve Account to Expense Fund (formerly agenda item #15 on the Friday, December 9, 2016 agenda)**

Ms. Covarrubias advised that we do anticipate having excess funds from the 2016 budget. The Board Trustees adopted a policy to maintain excess reserves in the Expense Fund of approximately 15% of the following budget year expenses.

Based on an analysis of the estimated 2016 operating expenses, we estimate remaining excess reserves of approximately $7.6 million at 12/31/2016.
Ms. Covarubias outlined the numbers as follows:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Budget</td>
<td>$30,100,000</td>
</tr>
<tr>
<td>Reserve to keep</td>
<td>$4,515,000</td>
</tr>
<tr>
<td>Excess to be used</td>
<td>$3,120,000</td>
</tr>
<tr>
<td>Transfer</td>
<td>$26,980,000</td>
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Ms. Oakley made a motion that the Board adopt a resolution to transfer $26,980,000 from the Interest Reserve Account in the Trust Fund to the Expense Fund to cover budgeted expenses for 2017. Mr. Jeffers seconded the motion, which passed 4-0. (Mr. Rodriguez and Mr. Landis had left the meeting at this time.)

20. **Consider and Act on Internal Audit Charter (formerly agenda item #16 on the Friday, December 9, 2016 agenda)**

Mr. Jeffers reviewed the amendments by the Internal Audit Committee to the Internal Audit Charter. The Charter was updated to remove references to the frequency for conducting risk assessments (#6) and developing the Internal Audit Plan (#7) as a result of discussions during the Nov. 21, 2016 Internal Audit Committee. Instead, these tasks will be performed at the frequency requested by the Committee. Also, minor edits were made to the Director of Internal Audit responsibility #13 for clarity.

Mr. Jeffers made a motion to adopt the Internal Audit Charter as presented. Ms. Oakley seconded the motion, which passed 4-0.

21. **Review and Discuss 2017/2018 Draft Audit Plan (formerly agenda item #17 on the Friday, December 9, 2016 agenda)**

Ms. Vice reviewed the Audit Plan’s development process. First, she conducted an agency-wide risk assessment. Ms. Vice worked with each department to identify the risk universe, describe the risks, and assign a risk score for the likelihood and impact of each risk event occurring. Second, risk scores for each auditable unit were sorted from high to low value and categorized as red (high), yellow (medium), and green (low) risks. Third, high risk units were selected for the 2017 to 2018 Audit Plan if they had no prior audit coverage during the last five years.

Ms. Vice discussed the Audit Plan elements and reviewed the Board’s next steps.

22. **Executive Director and Staff Reports**

Mr. Gavia presented a plaque to the Board Chair recognizing his service as Chair of the TMRS Board of Trustees for 2016.

23. **Call for Future Agenda Items**

There was no discussion at this time.

Mr. Philibert made a motion to adjourn the meeting. Ms. Oakley seconded, which passed 4-0.
The meeting was adjourned at 12:01 p.m.

David Gavia  
Executive Director

Jim Parrish  
Chair, Board of Trustees