



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

March 24, 2022 – 9:00 a.m.

The Board of Trustees of the Texas Municipal Retirement System (TMRS) convened for a meeting at 9:00 a.m. at the TMRS office, located at 2717 Perseverance, Suite 300, in Austin, Texas, with all Trustees present: Chair Jesús Garza, Vice Chair Bob Scott, Anali Alanis, Johnny Huizar, David Landis, and Bill Philibert.

Staff and consultants present included: David Wescoe (Executive Director), Michelle Kranes (Chief Service Officer), Christine Sweeney (Chief Legal Officer), Sandra Vice (Chief Administrative Officer), David Hunter (Chief Investment Officer), Michelle Mellon-Werch (Director of Communications), Anthony Mills (Director of City Services), Debbie Muñoz (Director of Member Services), Andi Focht-Williams (Deputy Director of Member Services), Leslee Hardy (Director of Actuarial Services), Kenneth Oliver (Actuarial Analyst), Dan Wattles (Director of Governmental Relations), Rhonda Covarrubias (Director of Finance), Nick O’Keefe (Deputy Chief Legal Officer), Michele Fullon (Investment Compliance Officer), Kelsey Baldwin (Senior Investment Attorney), Madison Jechow (Assistant General Counsel), Tom Masthay (Deputy Chief Investment Officer), Eddie Schultz (Senior Managing Director), Frank Atkins (Senior Investment Analyst), Eric Obermier (Director of Information Services), Chris Gillis (Network/Systems Administrator), Joe Newton (GRS), Ron Lewis (Ron Lewis & Associates), Alec Lewis (Ron Lewis & Associates), Marcia Beard (RVK), Spencer Hunter (RVK), Robert Klausner (Klausner, Kaufman, Jensen & Levinson), and Dr. Anthony Picchioni.

Mr. Garza called the meeting to order at 9:00 a.m.

Consent Agenda

1. Consider and Act on Consent Agenda.

Mr. Philibert moved that the Board adopt the Consent Agenda. Mr. Landis seconded the motion, which passed 6-0.

Board Organization

2. Consider and Act on Formation of Ad Hoc Board Committee.

Mr. Wescoe discussed establishing an Ad Hoc Board Committee to revise and update the TMRS Investment Policy Statement (IPS). The Board’s Bylaws allow the Board to create such a committee. Mr. Scott said Mr. Hunter had commented that the current IPS contained many

procedures in addition to policy and that the procedures need to be separated out. Mr. Scott also stated now is a good time to review the IPS because TMRS is reaching maturity in its asset allocations after having been invested only in fixed income assets before 2008.

Mr. Philibert moved that: (i) the Board create an ad hoc “IPS Review Committee” to work with staff on revising the IPS and then presenting the Committee’s recommended IPS changes to the Board for approval, (ii) a Committee charter is not needed, (iii) Bob Scott, as Chair, and Anali Alanis, as Vice Chair, be appointed as the two Committee members, and (iv) the Committee’s term continues until the Committee presents and the Board approves a revised IPS.

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

Executive Director Reports

3. Executive Director’s Report.

Mr. Wescoe presented his Executive Director’s Report. He discussed the Texas City Management Association clinic on February 24 in Granbury and meeting with representatives from the Combined Law Enforcement Associations of Texas. Mr. Wescoe discussed putting the prior TMRS office at 1200 North IH 35 on the market for sale and innovations at the new TMRS office that promote collaboration. He stated that TMRS now has 907 participating cities and discussed improvements in proactively marketing TMRS to eligible cities. He discussed promotions for employees in Member Services, Legal and Investments. Mr. Wescoe said that City Portal improvements, the most significant remaining part of the Pension Administration System Modernization project, are on schedule to be completed in 2022 and on budget.

4. Receive Senior Staff Quarterly Reports.

Ms. Vice presented staff reports for the first quarter of 2022. She highlighted recent cities that joined TMRS. She said that TMRS posted or mailed during the quarter more than 230,000 statements to Members and retirees, and that the statements have been updated to present information more clearly. Mr. Garza asked staff to consider if statements could be provided in Spanish upon request. Ms. Vice discussed work by Member Services and Information Services to make available new Internal Revenue Service W-4P forms ahead of the schedule requested by the IRS. Ms. Alanis asked if the W-4P form could be included as part of TMRS’ retirement packet. Mr. Garza asked about marketing by TMRS to unincorporated areas that are growing and may soon incorporate. Mr. Wescoe said City Services will focus first on existing cities that have not yet joined, and Mr. Wattles said there are 316 such cities. Ms. Sweeney said a city must be incorporated to join TMRS absent special legislation, such as the Dallas Police & Fire Pension System’s recent legislation to allow their staff to join TMRS.

5. Consider and Act on Matters Concerning the Sale of the TMRS 1200 North Interstate 35 Building.

Mr. Wescoe said TMRS retained Cushman & Wakefield to represent TMRS in the sale of the prior office building, and through that firm TMRS received a number of offers, which will be discussed in executive session.

Legal Reports

6. Consider and Act on Final Adoption of TMRS Rule Amendments – Chapter 129.

Ms. Sweeney asked the Board for final action on proposed rule amendments for Chapter 129 of TMRS' rules. This chapter relates to qualified domestic relations orders (QDROs), which are needed to pay TMRS benefits to a person other than a TMRS Member or retiree. In October, the Board approved publication of the proposed rule amendments. The proposed amendments were then submitted to the Governor's Office for review. After incorporating non-substantive changes requested by the Governor's staff and staff in the office of the Texas Register, the proposed rule changes were published in the Texas Register on Feb. 11, 2022. The public comment period expired on March 13, and no comments were received. If the Board approves a proposed Final Order for the rules, they will be published again in the Texas Register before they take effect. The proposed effective date for the rules, she said, is July 1, 2022, to allow time for education regarding the new rules.

Mr. Landis moved that the Board approve and authorize the Board Chair to execute the Final Order, adopt the repeal of the current Chapter 129 rules, and adopt the new Chapter 129 rules, to be effective July 1, 2022, after filing with the Secretary of State's *Texas Register* division, without changes to the proposed language as published. Mr. Scott seconded the motion, which passed 6-0.

7. Consider and Act on the State Office of Administrative Hearings Administrative Law Judge's Proposal for Decision in a Member Dispute Matter.

Ms. Sweeney requested that the Board make a final decision on a Proposal for Decision (PFD) from an Administrative Law Judge (ALJ) with the State Office of Administrative Hearings (SOAH) in a benefits matter where a Member appealed TMRS' determination. The ALJ's PFD supported TMRS' position found that the Member's non-vested account was cancelled by law after more than 5 years away from city service, and that the Member could not receive restricted prior service credit on that account after the account was cancelled. The Member was notified about the PFD and filed no objections to it. Ms. Sweeney presented a Final Order based on the PFD to the Board for consideration and stated staff recommended that the Board adopt the ALJ's PFD in whole.

Mr. Landis moved that the Board approve the proposed Final Order, and the Proposal for Decision from SOAH attached to the proposed Final Order as Exhibit A, which is incorporated into the Final Order by reference. Ms. Alanis seconded the motion, which passed 6-0.

Legislative Agenda

8. Review and Discuss TMRS Act Review Project and Potential Legislation Topics.

Ms. Sweeney told the Board that TMRS sought legislative changes to the TMRS Act three times since 2010. In 2011, Senate Bill (SB) 350 restructured three of TMRS's internal trust fund accounts into a single trust fund account. In 2019, SB 1337 made TMRS Act amendments to multiple administrative areas, and Ms. Sweeney discussed some highlights of those changes. In 2021, SB 1105 revised TMRS' statutes regarding retirees returning to work. Ms. Sweeney noted that three potential benefit topics have recently been considered by the Advisory Committee on Benefit Design regarding possible amendments to Cost of Living Adjustments options (COLAs), Updated Service Credit (USC) and COLA coverage links, and Supplemental Death Benefits (SDB) coverage links for Members and retirees. These topics remain under consideration. She then discussed seven prior administrative topics that were considered for legislation by staff and the Board in 2019 in preparation for SB 1337, but the Board decided not to pursue them in 2019 or in 2021. She said these seven administrative topics were not critical to TMRS operations.

Mr. Garza stated that a planned February Advisory Committee Meeting had to be cancelled due to weather. He said another Advisory Committee meeting will be scheduled before the Board considers action on the legislative proposals in May. Mr. Scott said that none of the seven administrative topics would justify legislation on their own, but they might be included in other legislation that might be pursued. Mr. Scott said that legislation should not be needed to address any statutory maximum affecting a city's rates given the current positive funding status for most cities.

Actuarial Services Reports

9. Consider and Act on 2021 Interest Credit Allocation to the Benefit Accumulation Fund and Interest Reserve Account.

Ms. Hardy asked the Board to approve the 2021 Interest Credit Allocation to the Benefit Accumulation Fund (BAF) and Interest Reserve Account. Mr. Newton presented GRS' recommendation to credit approximately 12.26% to the cities' accounts in the BAF.

Mr. Garza asked about the \$310 million reserve account, and Mr. Newton said that the reserve serves as a buffer as earnings on private market investment earnings until they are finally determined. Ms. Hardy said the reserve is based on prior practice, originally set at 1% of the TMRS fund, and experience with investments in private markets. Mr. Scott asked whether the positive investment returns would lower city rates. Mr. Newton said investment returns alone would reduce rates, but inflation at 7% also is a factor for rates, and the investment returns and inflation may offset each other, especially for cities with COLAs.

Mr. Scott moved that the Board allocate, effective December 31, 2021:

- (i) a credit of 5% interest to each of the Supplemental Disability Benefits Fund and the Supplemental Death Benefits Fund, and
- (ii) a credit of approximately 12.26% interest to the Benefit Accumulation Fund, as well as maintain the initial Interest Reserve Account balance at \$310 million; and,

that the Board approve that any differences in the final versus estimated fourth quarter private investment fund valuation adjustments, as well as any adjustments that may be necessary to finalize net investment income for the year, be reflected in the final Interest Reserve Account balance as of December 31, 2021 and considered in the 2022 BAF interest credit determination. Mr. Huizar seconded the motion, which passed 6-0.

10. Consider and Act on Transfer from the Interest Reserve Account to the General Reserves Account.

Ms. Hardy recommended that the Board transfer \$7.5 million from the Interest Reserve Account to the General Reserves Account as a contingency plan in the event assets in the Supplemental Death Benefits Fund (SDB) become depleted due to the higher mortality rates associated with the global pandemic. Ms. Alanis asked if the recommended transfer was expected to be a short-term response or if this might be needed in future years. Ms. Hardy said death rates have fallen since December, so this is only for a contingency. She added that the money remains invested, the transfer is accounting only.

Mr. Landis moved that the Board transfer \$7.5 million from the Interest Reserve Account to the General Reserves Account, effective as of December 31, 2021. Ms. Alanis seconded the motion, which passed 6-0.

Internal Audit Reports

11. Report on Audit Committee's March 9, 2022 Meeting.

Ms. Focht-Williams reported on the Audit Committee's meeting on March 9, 2022. At the Committee meeting, she presented results of a consultant's annual review of information systems security and reviewed completed Internal Audit reports on Quality Assurance Review for Internal Audit and the 2022 Risk Assessment and Audit Plan. Ms. Vice congratulated Ms. Focht-Williams on her promotion to Deputy Director of Member Services and described the process for recruiting a new Director of Internal Audit. Ms. Vice said she expects to bring selected candidates to the Audit Committee for interviews at a special meeting in late April or early May so that a final recommendation can be presented at the May Board meeting.

12. Consider and Act on the 2022 Audit Plan.

Ms. Focht-Williams presented the 2022 Risk Assessment and Audit Plan for approval. She said she interviewed the Audit Committee members and TMRS senior staff regarding the plan topics, and most topics are unchanged, but an audit of Investments due diligence procedures was

recommended by the prior Committee Chair and will replace an audit of third-party vendors' data security. The Audit Committee reviewed and recommends the Plan to the Board.

Mr. Huizar and Ms. Focht-Williams discussed an audit regarding TMRS detecting and monitoring cybersecurity events, which Ms. Focht-Williams said remains in the Plan while an audit of third-party data security under TMRS contracts is being delayed. Mr. Scott asked if the cybersecurity audit will be done internally, and Ms. Focht-Williams said it depends on the new Director of Internal Audit's experience and strengths. Ms. Scott said he also would like an audit of third-party data security to remain on the list for future audit topics. Ms. Focht-Williams said that she will conduct the audit of Investments' due diligence procedures.

Mr. Landis moved that the Board approve the 2022 Audit Plan. Mr. Philibert seconded the motion, which passed 6-0.

Governmental Relations

13. Review, Consider and Act on the Board's Legislative Consultant.

Mr. Wattles introduced Ron Lewis, the Board's legislative consultant. Mr. Lewis discussed work that his firm has done for TMRS during changes in the legislature. Lewis said much of his work involved educating new legislative members about TMRS. Mr. Lewis presented a chart on five major bills that passed with support from the TMRS Board, and he said the TMRS Board had made good decisions on when to pursue proposed legislation.

Investment Reports

14. Chief Investment Officer Reports.

Mr. David Hunter reported that the TMRS Trust Fund returned 12.8% for 2021 and beat its asset allocation benchmark by 61 basis points. Mr. Hunter said the 61 basis points translates into about \$200 million additional assets. On a five-year basis the fund generated 8.94%, and on a ten-year basis, 7.69%, both of which beat benchmarks by 23 basis points. Mr. Hunter discussed reorganization of, and promotions within, the Investments team to put staff to their highest and best use. This structure, as well as the new offices, promotes collaboration. Mr. Hunter said that TMRS exposure to Russian investments was about \$65 million, which is less than 20 cents per \$100 of TMRS assets. Today, it is less than \$10 million. TMRS managers were working to reduce TMRS exposure to Russian assets in the fourth quarter of 2021. Asset allocation is close to target and progress toward the target was made during 2021. Global Equity, Private Equity and Real Estate classes helped to drive fund performance in the last five years. The asset allocation approved by the Board in July 2021 increased allocations to equity benchmarked assets, he said, yet risk remains in line with the most recent asset allocation study. New private market commitments of \$1.1 billion were approved in the fourth quarter split between Private Equity and Other Public and Private Markets (OPPM).

15. Receive Fourth Quarter 2021 Investment Compliance Report.

Mr. O’Keefe introduced Ms. Fullon, TMRS’ Investment Compliance Officer. She reported that during the fourth quarter, TMRS and its investment managers were in compliance with all testable parameters in the Investment Policy Statement after review of more than 2,000 compliance tests.

16. General Investment Consultant Quarterly Report.

Ms. Beard said RVK’s report focuses on the fourth quarter 2021. This report focuses on the positive performance in 2021, she said, and is preliminary until statements are audited to update private assets. In the quarter, TMRS outperformed its actual allocation benchmark by 53 basis points, and for the trailing year outperformance was 61 basis points. In each period through 10 years, TMRS outperformed its return assumption of 6.75%. Under TMRS investment policy focused on the five-year return, TMRS outperformed its actual allocation benchmark by 23 basis points. TMRS is close to its strategic target allocation, and Ms. Beard said the strategic target allocation would have returned 9.83% in the past five years, so the allocation is moving in the right direction. Within asset classes, TMRS beat class benchmarks in five of seven classes, and OPPM is very close to its benchmark. Total Equity trails the benchmark, she said, but during positive market returns following the pandemic active managers have struggled to beat index benchmarks. Mr. Spencer Hunter said markets have changed in 2022, and volatility resulting from the Russian war and commodity prices have caused the global equity benchmark to move down about 6.5% so far this year. Both equity and fixed income assets are moving down at the same time, which is not common, he said.

Board Education

17. Board Education: Global Equities Asset Class.

Mr. Atkins provided an overview of Global Public Equities, which is intended to provide capital appreciation over time, which historically has been achieved by owning stocks for the long-term. TMRS has held this class for about 14 years, and its average annual return is about eight percent, which has added about \$7.5 billion to the Trust Fund. This asset class has done this while being the primary source of funds for investments into other asset classes. The class includes both actively and passively managed holdings and is diversified by geography, company size and industry. The class is highly regulated and generally has low fees compared to other classes. Mr. Garza asked how fees can remain low in such a complex asset class, and Mr. Hunter said that TMRS uses passive management for most equity holdings and limits active management to certain sectors where it is more likely that active managers can bring higher returns.

Mr. Atkins discussed the breakdown in this class between large companies and mid-size to small companies. Mr. Hunter said this class has the largest allocation, 35%, in the TMRS portfolio with a return assumption higher than all but Private Equity. The objective is to beat the Investment Policy Statement benchmark, but the class has not done so for the 1-, 5- and 10-year periods. Current passive strategies have outperformed the benchmarks, and six managers currently beat their strategy-specify benchmarks (such as the Russell 2000 for U.S. small companies) but not the overall benchmark. That means, he said, there are tilts in TMRS’ portfolio in its active strategies

causing it to be underweight to U.S. and International large companies and overweight to emerging markets and mid-sized to small companies. Mr. Hunter said staff are discussing with RVK and Northern Trust how to adjust those tilts to improve net returns and reduce tracking errors and fees.

Mr. Scott said that while asset allocation is the primary driver of return, there is a lot of opportunity within asset allocation to further enhance returns. The Board asked for 35% in global equities, he said, but it did not specify where to allocate the 35% within that category. Mr. Hunter said the biggest area for improvement was in public equities, and the next biggest was in non-core fixed income, although TMRS has done fairly well in that category.

Executive Session.

18. Executive Session.

The Board went into Executive Session at 11:24 a.m. The meeting reconvened in Open Meeting at 2:26 p.m. No action was taken during the Executive Session. All members of the Board who were present before the Executive Session were present.

After returning from Executive Session, Mr. Garza called back Agenda Item No. 5, Consider and Act on Matters Concerning the Sale of the TMRS 1200 North Interstate 35 Building.

Mr. Landis moved that the Board authorize the Executive Director to negotiate and enter into all agreements necessary for the sale of the TMRS 1200 North Interstate 35 Building (its legal street address being 708 E. 12th Street) to the buyer recommended by TMRS' agent, Cushman & Wakefield. Mr. Philibert seconded the motion, which passed 6-0.

Future Board Agenda Items

19. Call for Future Agenda Items.

There were no future agenda items. Mr. Garza adjourned the meeting at 2:28 p.m.



Jesús A. Garza
Chair, Board of Trustees



David B. Wescoe
Executive Director