

**MINUTES  
BOARD OF TRUSTEES OF THE  
INDIANA PUBLIC RETIREMENT SYSTEM**

**Meeting held at:  
One North Capitol  
1<sup>st</sup> Floor Conference Room  
Indianapolis, Indiana 46204**

**June 21, 2013**

**Board Members Present**

Ken Cochran, Chairman  
Brian Abbott  
Tim Berry  
Jodi Golden  
Deanna Oware (State Budget Agency designee)  
Kyle Rosebrough  
Mike Pinkham

**Others Present**

Ray Jones, IRTA  
Nancy Tolson, IRTA  
Meredith Maloney, Rivers Casino, Pittsburg  
Jim Masterani, Rivers Casino, Pittsburg  
Jim Baker, Unite Here  
Pete Keliuotis, Strategic Investment Solutions (SIS)  
Rich Dabrowski, Strategic Investment Solutions (SIS)

**Staff Present**

Steve Russo, Executive Director  
Steven Barley, Chief Operations Officer & Deputy Director  
David Cooper, Chief Investment Officer  
Anthony Green, Chief Legal and Compliance Officer  
Donna Grotz, Director of Strategic Initiatives and Administration  
Mike Hinline, Chief Information and Technology Officer  
Julia Pogue, Chief Financial Officer  
Teresa Snedigar, Director of Internal Audit  
Scott Davis, Investments, Director of Public Equity  
Brian Rogers, Investments, Director of Fixed Income and Real Assets  
Blair Webb, Investments, Investment Analyst  
Erin Hankins, Executive Assistant  
Katie Williams, Legal Analyst

Meeting called to order at 10:00 a.m. by Chairman Cochran.

I. **Approval of Minutes from April 26, 2013 Board of Trustees Meeting**

**MOTION** duly made and carried to approve the minutes from the April 26, 2013 Board meeting.

*Proposed by: Tim Berry*  
*Seconded by: Mike Pinkham*  
*Votes: 6 in favor, 0 opposed, 0 abstentions*

II. **Required Business**

In accordance with normal practice, written materials for the following matters were provided to the board members by mail in advance of the meeting.

A. **Strategic Plan Approval**

Donna Grotz presented the 2014-2016 INPRS Strategic Plan to the Board. Ms. Grotz reviewed the accomplishments made in Fiscal Year 2013, the 2013-2015 plan objectives, and various impacts to the 2013-2015 strategic plan. A board member asked how the plan is adjusted when goals are met or missed. Ms. Grotz replied that an assessment is made for each item and adjusted as needed.

Ms. Grotz then described the process for creating the 2014-2016 plan. She stated that a SWOT (Strengths, Weaknesses, Opportunities, and Threats) identification workshop was conducted with the executive staff, and that this information was used in the creation of the plan. Key enhancements to the updated plan included the adoption of two classifications, Strategic Objectives and Key Operational Requirements, to foster greater transparency. A board member asked if the metrics used in the strategic plan are the same as those reported to the governor's office. Ms. Grotz responded affirmatively that they are a subset.

Ms. Grotz presented the FY 2014 strategic and tactical priorities. She reviewed the introduction to the 2014-2016 plan, explained the addition of a new principle, and described the metrics used. Board members and staff engaged in a discussion of the history of the strategic plan and how the 2013 delays affected the goal dates.

**MOTION** duly made and carried to adopt the staff recommended INPRS 2014-2016 Strategic Plan.

*Proposed by: Mike Pinkham*  
*Seconded by: Jodi Golden*  
*Votes: 6 in favor, 0 opposed, 0 abstentions*

## B. FY 14 Budget Approval

Julia Pogue presented the Fiscal Year 2014 budget to the Board. She explained the FY 2014 budget drivers: modernization and enhancements; reorganization of the IT and Operations workforce; further management education and training; GASB (Governmental Accounting Standards Board) pension accounting changes; enhancement of member communication; and compliance with laws and regulations (e.g., IRS Plan C filing). Ms. Pogue then provided a chart showing the Administrative and Project Expense FY13 budget and FY13 forecast, and identified the specific items that were used to create the FY14 budget.

Ms. Pogue explained the key assumptions used to set the FY 14 Investment expense budget for management fees: 1) Public manager quarterly asset values were estimated using an annual growth rate of 6.75%; 2) Estimated private equity and private real estate asset values were provided by INPRS' consultants (based on each partnership's expected cash flows); 3) All managers were assumed to report fees. She stated that an increase in market value results in an increase in fees. Ms. Pogue then explained the changes in the Investment Expense budget from FY 2013 to FY 2014.

Ms. Pogue discussed the FY 2014 budgeted capital expenditures and the risks and opportunities with the FY 2014 INPRS budget. She presented the FY 2014 detailed budget to the Board. Line item details for each area were included in the index. INPRS staff requested Board approval of the FY 2014 Budget as presented.

A board member asked about the effect of the ERM delay on the budget. Ms. Pogue and Mr. Russo discussed the offsets, savings, and expenses of IT projects. Ms. Pogue mentioned that the ASA-Only plan increased expenses. A discussion was had among board members and staff regarding costs from FY13 moving into FY14. A board member asked if investment managers did not report fees in the past. Ms. Pogue replied in the affirmative and a discussion was had on the topic. In response to a board member's inquiry, Ms. Pogue stated that the biggest concern regarding investment management fee reporting was the desire to separate expenses and income and sorting net fees. A board member asked if INPRS could require managers to provide detailed fee reports. Mr. Cooper stated that they are moving in that direction.

**MOTION** duly made and carried to adopt the staff recommended budget for Fiscal Year 2014.

<i>Proposed by:</i>	<i>Jodi Golden</i>
<i>Seconded by:</i>	<i>Tim Berry</i>
<i>Votes:</i>	<i>6 in favor, 0 opposed, 0 abstentions</i>

### III. Unfinished Business

#### A. ASA Annuities

David Cooper, joined by Pete Keliotis of Strategic Investment Solutions (SIS), presented information to the Board on the topic of Annuity Savings Account (“ASA”) annuity options. Mr. Cooper first provided background of the topic: the current retirement plan options, the ASA structure, and the ASA options at retirement (annuitize ASA balance through INPRS, leave ASA balance invested in existing INPRS options, or withdraw ASA balance). He gave a brief explanation of an immediate annuity. He then reviewed a timeline of the ASA Annuity Decision process and noted that a Board decision on which option to choose was needed by late July 2013.

Mr. Cooper then reviewed the four options for the management of future INPRS Annuity liabilities. The level of potential risk decreases with each option.

- Option 1: Status Quo – INPRS Annuity Rate = 7.50%
- Option 2: INPRS Annuity Rate = Defined Benefit Long Term Rate of Return (6.75%), which is set by the Board
- Option 3: INPRS Annuity Rate = Board Determined Market Based Rate
- Option 4: Utilize a 3<sup>rd</sup> Party Annuity Provider; Annuity Rate = Market Rate

A board member asked about how mortality tables are used in calculating the annuity rate. Ms. Pogue responded that PERF and TRF have been using different mortality tables, which results in different benefit amounts. She explained how the tables are used and stated that, no matter which option is selected, staff will recommend that the mortality tables be updated to reflect current mortality rates and to align PERF and TRF.

Mr. Cooper offered a review of the pros and cons, which were presented at the February 22, 2013, meeting, for each of the annuity options. The presentation of the cons for Option 3 resulted in a discussion among staff and board members. They discussed retirement timing and how the changing rate would affect member’s decisions about when to retire. Mr. Russo stated that setting the annuity quarterly would be best operationally for processing retirements and communicating rates with members. Mr. Cooper noted that a third party provider may change the rate weekly or daily if necessary.

Cons presented for Option 4 were: 1) INPRS would not have the ability to customize a third party annuity and 2) third party providers have a lower credit rating than the State of Indiana. Additional cons for Option 4 included possible challenges in member communication and that members would receive two separate payments for their pension and their annuity.

Mr. Cooper presented the scope, minimum qualifications, and distribution channels for the RFP for Option 4 that had been requested by the Board. The

RFP had two actual respondents: MetLife and Great West Financial. Using MetLife rate as an example, Mr. Cooper showed that the group rate would provide a benefit to members over the individual retail rate.

Mr. Cooper then presented additional information and two possible methodologies for the Board to consider for Option 3. He explained the potential rate methodology for Option 3a: The INPRS ASA Annuity Crediting Rate will be established quarterly on the last business day of the calendar quarter and will be effective for the second calendar quarter following that date (e.g. rate established on December 31 will be effective April 1 – June 30). It will be the lower of: 1) 10-Year United State Treasury Yield on the last business day of the calendar month + 1.50%; or 2) Lowest of the INPRS Target Rates of Return assumptions for the Retirement Fund, as approved by the Board. An example rate using Option 3a was compared to the market rate and used in a member benefit example. Mr. Cooper stated that a challenge for Option 3a would be communicating the changing rate to members and lagging behind the market changes.

Mr. Cooper presented the potential rate methodology for Option 3b: The INPRS ASA Annuity Crediting Rate will be established quarterly on the last business day of the calendar quarter and will be effective for the second calendar quarter following that date (e.g. rate established on December 31 will be effective April 1 – June 30). It will be calculated based on: Lowest of the INPRS Target Rates of Return assumptions for the Retirement Fund, as approved by the Board, minus 3.00%. He stated that Option 3b would not be dependent on the changing 10-year US Treasury yield and would create a fixed rate; it would only change when the Board set a new long-term rate of return assumption. As with the previous option, an example rate using Option 3b was compared to the market rate and used in a member benefit example, which also showed the effect of using a rate other than 3.00% in the formula.

A board member asked if the annuitized funds would be invested separately from the DB funds. Mr. Cooper replied that his recommendation would be to leave the annuitized assets invested in the DB pool.

Mr. Cooper then referenced three bell-curve charts showing the probability of not achieving the ASA Annuity Crediting Rate for Option 3a/3b over one year, five years, and ten years; the risk decreases over time from 39% to 20%. He then discussed the impact of Options 3a and 3b on the funding status of the DB is not significant because the amount of money that is annuitize each year is about 1.00% of the total DB assets and the DB would be fully funded at the time the rate is set. However, the risk to the overall DB balance sheet is increased with these options. A discussion was had on the potential risk involving funded status, mortality tables, and other variables.

A board member asked about the expenses for Option 3 that could be charged to the ASA. A discussion was had on the topic and what INPRS would need to

consider. A board member then brought up issues such as plan flexibility and other options that third party vendors offer. A discussion was had on the legislative efforts to remove the ASA annuity option. Mr. Russo provided an update on past conversations he had with legislators on the topic. A board member stated that he had spoken with a legislator who had concerns about the risk carried by INPRS by maintaining the annuity option. Mr. Russo added that some legislators were concerned that the employer was bearing risk that the member should bear. Another board member asked about how the risk is transferred to employers. Mr. Russo explained how the cost to employers is calculated. A board member asked if the goal was to limit or eliminate risk. Mr. Cooper stated that moving all annuity options to a third party is the only way to completely remove risk from INPRS and the employers. Board members engaged in a discussion regarding risk, fiduciary duty of the Board, and methods for determining the annuity rate. Staff provided clarification on the options currently available to members at retirement.

A board member expressed disinterest in Options 1 or 4, desire for a slow transition to a new methodology, and preference for a yearly fixed rate. Another board member was not opposed to Option 3, leaned toward Option 4, desired to reduce risk, and questioned INPRS offering more than the market rate. A third board member asked about the amount of assets in the ASA, expressed disappointment in the lack of responses to the RFP for Option 4, and thought Option 3 and Option 4 were best. A fourth board member agreed and offered support for Options 3 and 4, stating that, if Option 3 was not too administratively burdensome on INPRS, it would provide the best rates for members. A fifth board member expressed their support of Options 3 and 4, mentioned that members already have the option to take their ASA to a third party, and discussed the lack of options available to members. A board member asked for clarification on members' current options for annuitizing with a third party provider. Mr. Cooper replied that members can do that, but would get a better rate if members invested as a group.

A board member stated that this was a significant decision for the Board to make and did not feel that the Board was ready to make that decision until further input was solicited from legislative leadership. A request was made for an additional meeting in July. Staff confirmed that members could call into a meeting via telephone to reach quorum. Staff also stated that the July deadline for a decision on the matter was needed to allow time to communicate with members.

Board members confirmed that they were available to meet in July. Staff encouraged board members to send them any questions about the various options. Mr. Russo provided information about upcoming PMOC meetings, the first one to take place in August. A board member asked if Option 3 would increase staff needs and/or budget. Mr. Russo replied that he would provide more information at the next meeting.

The Board and staff agreed to plan a meeting in July to continue the discussion and make a decision on the matter.

#### **IV. New Business**

##### **A. Financial Update**

Julia Pogue presented the INPRS financial update to the Board. This update included financial highlights as of April 2013, which was a good month for INPRS. However, the market drop in June will negatively affect second quarter earnings. She summarized the Fiscal Year 2013 actual and forecasted expenses compared to budget and provided an annual variance analysis for four specific areas: administration, projects, investments, and capital. Overall expenses were 10% lower than budgeted. Ms. Pogue gave an overview of the chart showing INPRS FY2013 Actual and Forecasted Change in Net Position. Detailed financial statements were also provided to the Board for their review.

##### **B. Investments Update**

David Cooper and Pete Keliuotis, from Strategic Investment Solutions (SIS), presented the investment update to the Board. Mr. Cooper began with a review of the INPRS Investment team imperatives: 1) Achieve 6.75% long-term rate of return assumption; 2) Achieve the return as efficiently and effectively as possible; and 3) Always have enough cash on hand to pay the bills. He provided an organizational chart showing all members of his team.

Mr. Cooper provided highlights of INPRS investments and the market. He mentioned that the fixed income portfolio has been revised based on conversations with board members in late 2012. The INPRS investment team hosted an annual A-team roundtable on June 5, 2013, with strategic partners. Mr. Cooper provided information on the INPRS portfolio and DB performance. He provided an economic and market update for the US, Europe, China, and Japan.

Mr. Cooper presented the INPRS asset allocation trends, which are in range and near targets. He reviewed the FY13 performance and noted that stocks have done exceedingly well. Mr. Cooper discussed monthly returns from January 2009 through April 2013. He reviewed the DB Performance chart, compared the rates of return for private equity and private real estate, and gave an update on risk parity performance. Mr. Cooper reviewed the ASA and target date funds performance.

To clarify a discussion from the last board meeting, Mr. Cooper presented information about ASA fee savings that occurred by combining the PERF and TRF investments. He stated that the new combined annual fee for INPRS is lower than that of the median peer group.

Mr. Cooper updated the Board on the pension relief and special death funds, which are performing on target and above the benchmark.

In reviewing the list of recent investments and terminations, Mr. Cooper explained that all changes were part of the restructuring of the fixed income portfolio. A board member asked for an explanation of the mandate revisions for fixed income investments. Mr. Cooper explained that the dollar amount did not change, but the investment strategy did change.

Mr. Cooper concluded with an update on the Watch List and explained how each manager on the list is monitored. He noted that, as of May 31, 2013, the equity managers on the list had outperformed the benchmark. Graphs and detailed reports were provided to the board.

### C. Executive Director Report

Steve Russo presented the Executive Director's report to the Board. He began with an update of the ASA-Only Plan. He stated that the Phase 1 go-live occurred as planned on March 1, 2013. The ERM ASA-Only Phase 2 is on track to go-live on July 12, 2013. Mr. Russo presented the retirement plan choices made by new hires as they reached the 60 day enrollment period (8.0% enrolled in the ASA-Only plan).

Mr. Russo provided a summary of an ERM system issue that resulted in anomalies to some member's estimated average compensation and service credit. He noted that existing manual quality controls were in place to ensure accurate benefit processing. He explained the timing for fixing the anomalies.

Mr. Russo provided a chart showing the release schedule for all projects within the INPRS IT modernization effort. Data fixes and bug fixes are released as part of normal weekly IT activity.

Mr. Russo presented the results of the Annual Employer Survey to the Board. He provided background and an overview of the participants and their response rate. Mr. Russo then reviewed the key findings of the survey in the following areas: ERM; satisfaction and attributes of INPRS as an organization; and overall findings. 95% of employers expressed overall satisfaction with INPRS and 90% of employers rated ERM use as very easy, easy, or somewhat easy. The survey results produced two recommendations: 1) INPRS could build on the success of the ERM Quick Reference Guides and on-line manuals and encourage those who have not used them to do so; and 2) Explore improvements to make managing the ERM exception queue easier.

Mr. Russo presented highlighted metrics for the Governor's and Board Dashboards. The 10 year actual return verses the actuarial target remains right at the target. Retirement processing and customer satisfaction remain in the

green. Mr. Russo stated that the recent retiree satisfaction metric volatility is stabilizing and trending upwards in the past three months. Investment returns vs. benchmarks, while green, are trending downward due to the challenging market environment for public equity active managers.

**V. Other Business as Requested by the Board**

No other business was requested by the Board.

**VI. Preliminary Agenda for September 13, 2013 Board Retreat**

Mr. Russo gave copies of the preliminary agenda for the September 2013 retreat to the Board members.

**VII. Adjournment**

**MOTION** duly made and carried to adjourn the June 21, 2013 Board meeting at 1:27 p.m.

<i>Proposed by:</i>	<i>Tim Berry</i>
<i>Seconded by:</i>	<i>Kyle Rosebrough</i>
<i>Votes:</i>	<i>6 in favor, 0 opposed, 0 abstentions</i>