

Texas Emergency Services Retirement

Board Minutes of May 18, 2017

Courtyard Marriott 7809 E. Ben White Blvd, Austin Texas 78741

Members Present:

Frank Torres, Chairman
Jenny Moore, Vice-Chair
Dan Key, Trustee
Steve Williams, Trustee
Don Shipman, Trustee
Taylor Allen, Trustee
Courtney Gibson Bechtol, Trustee
Pilar Rodriguez, Trustee

*ADOPTED AS AMENDED
See page 4*

Members Absent:

Ron Larson, Secretary

Staff:

Kevin Deiters, Executive Director
Judy Johnson, Chief Financial Officer, CPA
Susannah Jones, Staff Services Officer
Shirley Hays, Contract Manager, CTCM
William Langford, Marketing Specialist

Others Present:

David Gordon, Assistant Attorney General
Jonathan D. Breth, CFP, AndCo Consulting, LLC
Jeffrey W. Rexford, Head of Business Development, Jackson Square Partners, LLC.
Jeffrey A. Hakala, CFA, CPA, Clarkston Capital Partners
Kurt P. Terrien, Partner, Clarkston Capital Partners
Michael B. Kinney, CFA, Westfield Capital Management
John. M. Montgomery, Managing Partner, Westfield Capital Management
Aaron A. Reed, CIMA, Kayne Anderson Rudnick Investment Management
Craig Stone, Portfolio Manager Kayne Anderson Rudnick Investment Management

Chairman Torres called the meeting to order at 8:03 a.m.

1) Roll Call

Vice-Chair Moore called the roll and announced that a quorum of the Board was present. Eight Trustees were present and Secretary Larson was absent.

2) Invitation for Public Comment

Chairman Torres called for public comment. No public comments were made.

3) Approval of Minutes for February 16, 2017

Vice-Chair Moore made the motion to adopt the minutes as presented. The motion was seconded by Trustee Shipman and unanimously adopted by the Board.

4) Small/Mid Cap Growth Equity Manager Finalist Presentations

a) Westfield Capital Management Co. Small/Mid Growth Equity Fund

Michael B. Kinney and John Montgomery made the presentation on behalf of Westfield Capital Management Co. and its Small/Mid Growth Equity Fund. Their presentation covered the structure of the firm; portfolio management; the investment process; and the historical performance for the portfolio.

b) Jackson Square SMID-Cap Growth Fund

Jeffrey W. Rexford made the presentation on behalf of Jackson Square and its SMID-Cap Growth Fund. His presentation covered the structure of the firm; portfolio management; the investment process; and the historical performance for the portfolio.

5. Small/Mid Cap Value Equity Manager Finalist Presentations

a) Clarkston Capital Partners Institutional Fund

Jeffrey A. Hakala and Kurt P. Terrien made the presentation on behalf of Clarkston Capital Partners and its Institutional Fund. Their presentation covered the structure of the firm; portfolio management; the investment process; and the historical performance for the portfolio.

b) Kayne Anderson Rudnick Investment Management SMID Quality Value Fund

Aaron A. Reed and Craig Stone made the presentation on behalf of Kayne Anderson Rudnick Investment Management and its SMID Quality Value Fund. Their presentation covered the structure of the firm; portfolio management; the investment process; and the historical performance for the portfolio.

6. Selection of a Small/Mid Cap Growth Equity Manager - Discussion and Possible Action

After discussion, Trustee Bechtol asked Mr. Breth for his recommendation. Mr. Breth recommended to the Board that it select the Jackson Square SMID-Cap Growth Fund.

Trustee Allen made the motion to select the Jackson Square SMID-Cap Growth Fund. The motion was seconded by Trustee Bechtol and passed unanimously.

7. Selection of a Small/Mid Cap Value Equity Manager - Discussion and Possible Action

After discussion by the Board, Vice-Chair Moore asked Mr. Breth for his recommendation. Mr. Breth recommended to the Board that it select the Clarkston Capital Partners Institutional Fund.

Trustee Shipman made the motion to select the Clarkston Capital Partners Institutional Fund. The motion was seconded by Trustee Allen and passed unanimously.

8. Investment Performance Report for the Quarter Ending March 31, 2017

Mr. Breth presented the AndCo Consulting's *Texas Emergency Services Retirement System Investment Performance - Period Ending March 31, 2017* report and he discussed the capital markets, the economy, and TESRS investment performance during the first quarter of 2017.

As of March 31, 2017, total assets were \$97.4 million. The net return for the quarter was 4.94%, which matched the Policy Index of 4.94%. Over the past twelve months, the Fund's net return was up 10.71%.

The asset allocation as of March 31, 2017 was:

- International Equities \$25.9 million 26.6%
- Domestic Equities \$42.9 million 44.2%
- Fixed Income \$23.8 million 24.5%
- Alternatives \$4.5 million 4.7%

Mr. Breth reported that the current asset allocation was within the acceptable range of the target and he did not recommend regarding rebalancing the portfolio.

No action taken.

9. Investment Manager Watch List - Discussion and Possible Action

Mr. Breth reported that Pier Capital LLC was the only manager on the Watch List; however, he reminded the Board that Pier would no longer manage assets for the Fund after the Board's reallocation of the small-cap growth mandate to the small-mid cap growth mandate.

Trustee Shipman made a motion to remove Pier Capital LLC from the Watch List upon the reallocation of small-cap growth mandate to the small-mid cap growth mandate. The motion was seconded by Vice-Chair Moore and passed unanimously.

10. TESRS Cash Flow Projection (2017-2026)

Chief Financial Officer Judy Johnson presented a report on cash-flow projections for the Fund between 2017 and 2026. This was an informational presentation and no action was taken.

11. Written Investment Policy and Asset Allocation - Discussion and Possible Action

Mr. Breth provided an overview of proposed changes to the Written Investment and a revised asset allocation that:

- reduced international equity –developed markets from 21% to 15%;
- reduced international equity – emerging markets from 6% to 5%;
- increased core fixed income from 26% to 28%;
- reduced U.S. equity – Small Cap Core from 5% to 0%;
- reduced U.S. equity – Small Cap Growth from 5% to 0%;
- added U.S. equity – Small/Mid Cap Value 7.5%; and
- added U.S. equity – Small/Mid Cap Growth 7.5%.

After discussion by the Board, Trustee Shipman made a motion to adopt the Written Investment Policy and Asset allocation as presented. The motion was seconded by Trustee Allen and passed unanimously.

Trustee Allen made a motion to authorize the staff to rebalance the Fund according to the new asset allocation. The motion was seconded by Trustee Shipman and passed unanimously.

Trustee Allen made a motion to authorize the investment committee to conduct a search for a core real estate manager pursuant to the new asset allocation. The motion was seconded by Trustee Bechtol and passed unanimously.

12. Ethics Policy – Discussion and Possible Action

Executive Director Deiters provided an overview of the Board's *Ethics and Conflict of Interest Policy – April 2, 2014*. After discussion by the Board, Chairman Torres asked Mr. Deiters to place the Ethics policy on the August meeting agenda to provide Board members with additional time to review the policy.

13. Contract Administration and Management Policy - Discussion and Possible Action

The Contract Administration and Management was first considered at the February 16th, 2017 meeting; however, the Board delayed consideration of the Policy to enable the Attorney General's office to review and comment on the draft proposal.

Ms. Hays, CTCM, presented a revised draft Contract Administration and Management Policy that included a provision expanding the procurement processes to include the review of all draft contracts by the Attorney General's office. The Policy is required by the System's enabling statute and it contains provisions for establishing the need for contracts, the procurement process, the best value criteria and contract management.

Trustee Rodriguez made a motion to approve the Contract Administration and Management Policy as presented. The motion was seconded by Vice-Chair Moore and approved unanimously.

14. Board Travel Policy – Discussion and Possible Action

Mr. Deiters explained that the objective of the revised Board Travel Policy was to contain costs while enabling the Board to fulfill its fiduciary duties by conducting site visits or by attending educational conferences.

Trustee Rodriguez made a motion to adopt the Board Travel Policy as presented. The motion was seconded by Vice-Chair Moore and passed unanimously.

15. Proposed rule regarding service credit for eligible active military duty under the Uniformed Services Employment and Re-Employment Rights Act (proposal for publication) – Discussion and Possible Action

Outside Counsel Chuck Campbell presented proposed Rule §306.3 relating to qualified service credit under TESRS for eligible active military duty as required by Uniformed Services Employment and Re-Employment Rights Act (USERRA).

Mr. Campbell explained that a member is eligible under USERRA to receive up to five (5) years of qualified service credit in TESRS for the period while on active military duty. The member would need to receive an honorable discharge or release and return to his/her participating department within 90 days. The participating department would also need to make contributions (including both Part One and Part Two contributions) that would have been made during the period of military service.

The proposed rule also includes a 90-day “catch-up” period to allow departments to pay the required contributions for members eligible to receive qualified service credit under USERRA prior to the enactment of the rule.

Trustee Shipman asked Mr. Campbell if volunteers were covered by USERRA and if the System was required to comply. Mr. Campbell responded that that he did not research USERRA or case law to determine if TESRS had to comply with USERRA because TESRS was required to comply with USERRA by its state statute and by IRS requirements for qualified plans.

Mr. Deiters acknowledged the responsibility of TESRS to comply with USERRA and he asked Mr. Campbell if departments were required to comply with USERRA. Mr. Campbell responded that he did not believe that the departments were required to comply with USERRA and that TESRS did not have any responsibility regarding the compliance with USERRA by the departments.

Trustee Rodriguez asked Mr. Campbell if a department could elect not to pay the required contributions for a member returning from military service. Mr. Campbell said that a department would be required to pay for the contributions for a member whose status in the System was changed by the department to military leave at the time of the member’s termination.

After discussion, Trustee Shipman made a motion to publish the proposed Rule §306.3 on the Texas Register seeking public comment. The motion was seconded by Vice-Chair Moore and passed unanimously.

16. Proposed amendment to Rule §310.6 Local Contributions (proposal for publication) – Discussion and Possible Action

Mr. Campbell explained that the proposed amendment to Rule §310.6 Local Contributions was intended to provide the Board with more flexibility regarding the assessment of Part 2 Contributions and to clarify when contributions are assessed during periods of medical, disability or military service. The proposal does not change the minimum contribution rate for active members (Part 1) or any additional amount assessed for the unfunded liability (Part 2).

Trustee Rodriguez made a motion to publish the proposed Rule §306.3 in the Texas Register seeking public comment. The motion was seconded by Trustee Williams and passed unanimously.

17. Proposed amendment to Rule §310.8 Billings (proposal for publication) – Discussion and Possible Action

Mr. Deiters explained that the proposed Rule §310.8 would change the frequency of billing departments from quarterly to semi-annually and is intended to increase the efficiency of the System and reduce the amount of time spent by the Agency and participating departments in membership reconciliations, payments and collections. If the rule is enacted, departments would be billed in February and August.

Trustee Key expressed concern that some departments would delay the enrollment of new members in the System.

Mr. Deiters agreed with the concern raised by Trustee Key and pointed out that under the proposed rule that instead of just either the Local Board Chair or the administrative head of the department, the local board would be responsible for not only enrolling members into the System but also certifying by action of the local board the accuracy of the Membership Roster Report (MRR). The MRR would be become a required report and those departments that fail to submit a certified MRR would be subject to administrative penalties.

Trustee Williams made a motion to publish the proposed Rule §310.8 in the Texas Register seeking public comment. The motion was seconded by Trustee Key and passed unanimously.

18. Executive Director's report on administrative and financial activities of the System

Mr. Deiters reported to the Board regarding the operations of the agency during the third quarter of FY 2017. His report included an overview of the Agency's Legislative Appropriation Request, the State hiring freeze, agency database project update, and the recruitment of new departments.

This was an informational presentation and no action was taken

19. Authority to issue a request for proposal for accounting services- Discussion and Possible Action

Mr. Deiters requested the Board's authority to seek proposals from accounting firms interested in

serving as the System's accountant. He expressed concern about the agency's reliance on a single staff member for critical pension and investment accounting.

Chairman Torres asked for an explanation of how outsourcing critical accounting functions would improve the sustainability of the accounting program while maintaining the integrity of accounting records. He expressed concern that the proposal might actually increase risk to the program.

CFO Johnson explained that the agency CFO would oversee the activities of the contract CPA firm and that a regional firm would have the sophistication and depth needed to meet the assorted demands of the program. She also explained another benefit of outsourcing the accounting functions is that that the CFO could focus on internal audit and improving Agency processes.

Mr. Deiters responded to the Chairman's question by stating his opinion that the outsourcing of pension and investment accounting to an established CPA firm would reduce the risk to the System that currently exists with its reliance upon a single employee and the potential for an extended vacancy in the CFO position.

Trustees Williams and Shipman acknowledged the risks associated with the Agency's reliance upon a single employee for critical accounting functions; however, they would prefer the Agency to use available general revenue funds to finance the contract instead of solely relying upon non-appropriated funds.

Mr. Deiters agreed to commit available general revenue funds to the project and seek additional funding for the next Legislative Appropriation Request.

Trustee Bechtol made the motion to authorize the Executive Director to issue a Request for Qualifications for outside accounting services. The motion was seconded by Trustee Williams and approved unanimously.

20. FY 2017 Board Non-Appropriated Budget - Discussion and Possible Action

CFO Johnson provided an overview of Board's Non-Appropriated Budget as of February 28, 2017. She reported that we were at the mid-point of the fiscal year and that expenditures fiscal year-to-date reflected 42 percent of the Board's annual budget.

Mr. Deiters requested \$75,000 from non-appropriated funds to enhance cyber-security. This would include operating system and database software upgrades; implementing multi-factor authentication; testing the programming code; and conducting penetration testing.

After discussion, Trustee Williams stated his opinion that the Board had a fiduciary responsibility to protect the security of member information and he made a motion for the Board to allocate no more than \$75,000 in non-appropriated funds for cyber-security. The motion was seconded by Vice-Chair Moore and approved unanimously.

21. Board Educational Opportunities – Discussion and Possible Action

Chairman Torres encouraged Board members to attend the TexPERS conference in San Antonio during August. This was an informational presentation and no action was taken.

22. Request for future agenda items and meeting dates

Chairman Torres requested the Board to contact Mr. Deiters if they had items they would like on the August 17-18th meeting. Mr. Deiters identified the following items for the meeting

- Rules Adoptions
- FY 2018 Budgets
- Legislative Update
- Presentations from real estate investment firms
- Presentations from accounting firms
- Executive Director Evaluation

23. Adjourn

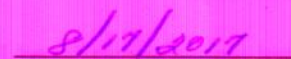
Chairman Torres requested a motion to adjourn at 5:15 pm.

The motion was made by Trustee Williams, seconded by Vice-Chair Moore and passed unanimously.

Minutes Approved By:



Ron Larson, Secretary



Date: