

MINUTES
BOARD OF TRUSTEES
OF THE TEACHERS' AND STATE EMPLOYEES' RETIREMENT SYSTEM

The regular quarterly meeting of the Board of Trustees was called to order at 9:30 a.m., January 26, 2017, by the Chair, Treasurer Dale R. Folwell. The meeting was held in the Dogwood Conference Room of the Longleaf Building at 3200 Atlantic Avenue, Raleigh, NC 27604. The Chair notified attendees that there would be a public comment period for organizations and individuals to address the Board.

Members Present

The Board members present were: Treasurer Dale R. Folwell, Lentz Brewer, Barbara Gibson, Greg Grantham, Terry McCann, Michael Mebane, LouAnn Phillips (on behalf of Superintendent Mark Johnson), Veronica Wright, and Van Dowdy.

Members Absent

The Board members absent were: John Aneralla, Greg Patterson, and Jack Brooks.

Guests Present

The guests attending were: Robert Curran, with the Attorney General's office; and, Michael Ribble, Larry Langer, Linda VanDeventer, Lisa Townley, and Susan Rosenbleeth (by phone) from Conduent Inc. (Buck Consultants).

Department of State Treasurer Staff Present

The staff members present were: Steve Toole, Cindy Aiken, Nick Byrne, Thomas Causey, Chris Farr, Jaclyn Goldsmith, Schorr Johnson, Michael Jackson, Fran Lawrence, Frank Lester, Laura Rowe, Kevin SigRist, Christina Strickland, Blake Thomas, Sam Watts, and Paula Woodhouse.

Introduction and Swearing In of Board Members

The Chair introduced a new member, Ms. Barbara Gibson, to the Teachers' and State Employees' Retirement System Board of Trustees. Ms. Gibson was sworn in and will serve as ex officio in her position as Director of the Office of State Human Resources. The Chair also gave an update on Board vacancies and pending appointments.

Ethics Awareness and Identification of Conflicts or Potential Conflicts of Interest

The Chair asked, pursuant to the ethics rules, about conflicts of interest of Board Members. Greg Grantham identified a potential conflict of interest related to the reemployment earnings discussion on the agenda based on his status as a rehired retiree who is working part-time for a school system. The Chair noted and confirmed that legal counsel was aware.

Approval of the Minutes from the October 27, 2016 Board Meeting

It was moved by Lou Ann Phillips, seconded by Lentz Brewer and carried unanimously that the minutes from the Board meeting held on October 27, 2016, be approved.

Approval of Resolution of Appreciation for the Service of State Treasurer, Janet Cowell

It was moved by Michael Mebane, seconded by Lentz Brewer and carried unanimously that the resolution of appreciation for the service of State Treasurer, Janet Cowell, be approved.

Approval of Resolution of Appreciation for the Services of Col. William Grey and Paula Woodhouse

It was moved by Greg Grantham, seconded by Van Dowdy and carried unanimously that the resolution of appreciation for the services of Col. William Grey and Paula Woodhouse be approved.

Retirement Systems Division Operations

The Chair recognized Thomas Causey, Deputy Director of Operations, and Michael Jackson, Chief of Member Services, for an update on benefit administration operations. Mr. Causey gave a report on operations metrics, indicating December 2016 was a good month in that Operations exceeded expectations from a metrics perspective.

Mr. Causey reported on the ORBIT Self-Service implementation, which will enhance the online experience when members access their retirement accounts... He stated that the staff will be working on enhancements for the Firefighters' and Rescue Squad Workers' Pension Fund in 2017. Mr. Mebane and Mr. Toole engaged in a dialogue regarding the overall security of Retirement data and servers.

The Chair recognized Michael Jackson, Chief of Member Services, for a presentation on the metrics for Member Services. Mr. Jackson reported on metrics for imaging, email correspondence, and meetings and webinars conducted by the Retirement Counselors. He reported that the team is working on implementing virtual retirement counseling sessions and completed a successful test pilot in November. He reported that the call center was meeting the goal of 65 percent of incoming calls to be received within 30 seconds during the fall and winter last year. He commented that call volume increases substantially during tax periods, so they are anticipating a busy quarter. Mr. Mebane made the comment that he never ceases to be amazed at the quality of this group and the constant improvement.

The Chair recognized Nick Byrne, Deputy Director of Policy, Planning, and Compliance, to give an update on the Contribution-based Benefit Cap (CBBC) liabilities. Mr. Byrne reported that a total of 79 retirements have exceeded the CBBC since its inception, with a total cost of liabilities invoiced of \$7.6 million.

There was discussion around the early notification of employers of potential liabilities due to pensions exceeding the benefit cap. Mr. Byrnes stated that a monthly watch list is available to employers. The Treasurer offered his support for the law and stated that the intent is to change the behavior that creates additional pension liabilities.

Update on the Investment Advisory Committee (IAC) Meetings

The Chair recognized Michael Mebane to provide an update on the Investment Advisory Committee (IAC) Meetings. Mr. Mebane stated that one of the main topics raised in the most recent meeting was supplemental employment. Mr. Mebane stated that the IAC recommends that any Treasurer or CIO who is seeking supplemental employment should consult with the IAC and the Board prior to accepting supplemental employment. This recommendation was developed after several months of consideration and is designed to address potential conflicts of interest and to recognize the sole fiduciary status of the NC State Treasurer. The Chair stated that he is in favor of having standards in place that preserve the rights of future decision-makers and stakeholders. Mr. Mebane also reported that there is a

major effort to identify all fees and investment-related costs, how they factor into the valuation and how they compare with our peers. He noted that the returns perform very well compared with our peer groups. IAC is establishing its own equity management team along with a program that will give IMD the capacity to internally manage the portfolio. The program should be rolled out in the next 12 months and is designed to reduce overall investment management fees.

Increase in the Amount of Reemployment Earnings Before Suspension of Retirement Allowance

The Chair recognized Steve Toole, Retirement Systems Division Executive Director, for a presentation on the annual statutory increase in the compensation that may be earned by a re-employed beneficiary who is receiving either an early retirement benefit or a service retirement benefit, before suspension of a retirement allowance under G.S. §135-3(8)(c). Mr. Toole announced that the Consumer Price Index (CPI) was released on January 18, 2017 and recorded an increase of 2.1 percent for the period of January 1, 2016 through December 31, 2016.

It was moved by Van Dowdy, seconded by Lou Ann Phillips and carried unanimously that the amounts which may be earned before suspension shall be increased effective January 1, 2017, equal to the increase in the CPI of 2.1 percent, as published by the U.S. Department of Labor. Therefore, the maximum amount a re-employed retiree can earn without affecting his/her monthly retirement allowance is increased by the greater of 2.1 percent of the 50 percent compensation amounts or an adjusted amount of \$32,260, both effective January 1, 2017.

Overview of Retirement Systems Division's Legislative Agenda for 2017 Session of the North Carolina General Assembly

The Chair recognized Sam Watts, Policy Director, to provide an overview of RSD's legislative agenda for the 2017 session of the North Carolina General Assembly. Mr. Watts updated the Board that the Department submitted a budget request for two IT development positions that will assist with further expansion of ORBIT.

Mr. Watts presented the Department's agenda for the legislative session. He stated that there will likely be a Pension Integrity Act, which will strengthen existing structures to further prevent fraud, waste and abuse.

Mr. Watts discussed the Administrative Changes Act, regarding the ability to reinvest cost savings from the ORBIT system to implement other priorities.

After Mr. Watts' presentation, there was discussion on the long-term funding of the pension plans.

Presentation from Conduent (Buck Consultants) on the Boards' Assessment

The Chair recognized Linda VanDeventer of Conduent to present a report on the Boards of Trustees' Assessment. Paper copies were provided at the meeting due to sensitivity of the report. Mr. Toole commented that the assessment was requested by Treasurer Cowell, prior to leaving office and the Board survey was conducted in the fall of 2016.

Ms. VanDeventer commented that the report was at a high level and that the Board is cohesive and working well together. There were write-in remarks about how it has improved over the years. She

mentioned that while this Board is currently receiving and utilizing paper materials, the overall trend is moving to electronic and paperless formats.

Consult with the Boards of Trustees, Pursuant to N.C.G.S §143-318.11(a)(6) and (c)

It was moved by Michael Mebane, seconded by Lou Ann Phillips and carried unanimously that the meeting be closed pursuant to G.S. §143-318.11(a)(6) & (c).

Linda VanDeventer of Conduent presented a report to the Boards on the Executive Director Assessment that was conducted fall of 2016. After the discussion, it was moved by Greg Grantham, seconded by Terry McCann and carried unanimously that the meeting be reopened.

Actuarially Determined Employer Contribution (ADEC) Projections for State System

The Chair recognized Larry Langer and Michael Ribble, from Conduent, to present on the actuarially-determined employer contribution (ADEC) projections for the State System.

Mr. Langer presented the employer contribution rate projections for the system. The baseline projection presented was based on the December 31, 2015 valuation results and assumptions of an interest rate of 7.25 percent for all years and an investment return of 7.25 percent on market value of assets. Mr. Langer reported that the Employer Contribution Rate Stabilization Policy (ECRSP) sets the recommended employer contributions equal to 0.35 percent of payroll greater than the appropriated contribution during the prior year. However, contributions may not be less than the ADEC, and, contributions may not be greater than the contribution determined using the same assumptions used to calculate the ADEC, except for a discount rate equal to the 30-year Treasury rate as of the valuation date. Mr. Langer presented that the ADEC is projected to be greater than the prior year's appropriation, plus the 0.35 percent for all years through fiscal year 2022 under the ESCRSP adopted by the Board of Trustees on January 21, 2016.

Mr. Langer presented an alternate projection along with the baseline that shows a 6.0 percent investment return to reflect the estimated return of 6.0 percent for calendar year 2016.

There was discussion by the Board around the possibility of achieving a 7.25 percent rate of return and the Chair stated that the Board has the opportunity to have a more in-depth discussion in April.

Presentations on the 2018 Fiscal Year Alternatives for the General Assembly

Mr. Toole presented the 2018 fiscal year policy options and recommendations for the General Assembly for the Teachers' and State Employees' Retirement System, the Consolidated Judicial Retirement System, the Legislative Retirement System, the Disability Income Plan of North Carolina, and the National Guard Pension Fund.

Mr. Toole presented the fiscal alternatives for the Teachers' and State Employees' Retirement System. He stated that the most recent valuation report shows that the new ADEC of 10.08 percent is greater than the appropriated employer contribution rate in the state budget of 9.98 percent for fiscal year ending 2017. Therefore, the ECRSP results in a recommended contribution rate of 10.33 percent of payroll for fiscal year ending 2018, making the additional appropriation needed from the General Fund to be \$35.4 million.

Mr. Toole presented the fiscal alternatives for the Consolidated Judicial Retirement System. He stated that the most recent valuation reported that the new ADEC of 30.23 percent is greater than the state

budget of 29.46 percent for fiscal year ending 2017. Therefore, the state budget allocated from the General Fund will need to increase by \$539,000 to meet the new ADEC for fiscal year ending 2018.

Mr. Toole presented the fiscal alternatives for the Legislative Retirement System. He stated that the most recent valuation reported that the new ADEC of 18.27 percent is greater than the state budget of 18.22 percent for fiscal year 2017. Therefore, the state budget of allocated from the General Fund will need to increase by \$1,810 to meet the new ADEC for fiscal year ending 2018.

Mr. Toole presented the fiscal alternatives for the Disability Income Plan of North Carolina. He stated that the most recent valuation reported that the new annual required contribution (ARC) is 0.14 percent of payroll, which is lower than the 0.38 of payroll for fiscal year ending 2017. Therefore, the General Assembly could lower the contribution rate without negatively impacting the funding of the plan.

Lastly, Mr. Toole presented the fiscal alternatives for the North Carolina National Guard Pension Fund. He stated that the most recent valuation reported that the new ADEC of \$8,923,153 is greater than the state budget of \$8,517,073 for fiscal year ending 2017. Therefore, the state budget allocated from the General Fund will need to increase by \$406,080 to meet the new ADEC for fiscal year ending 2018. Mr. Toole presented two policy options for the Board: 1) to recommend an increase to the current appropriation to fund the ADEC; or, 2) to recommend an increase to the current appropriation of \$2 million above the ADEC. Increasing the appropriation of \$2 million above the ADEC would provide an accelerated payment schedule that would pay off the unfunded liability of this plan in approximately 7 years (opposed to the current 12 year amortization). The Board discussed the overall funded status of the Fund, how the increase in contributions will affect the funding status, and amortization schedule.

Mr. Toole noted that the decision for the Death Benefit Plan is being deferred to April 2017.

Application of Charter School to become a participating employer in the Teachers' and State Employees' Retirement System

Mr. Toole presented the application from The North Carolina Leadership Charter Academy, Inc., (doing business as The NC Leadership Academy), for participation in the Teachers' and State Employees' Retirement System. Mr. Toole reported that the North Carolina Leadership Academy has complied with the requirements of North Carolina G.S. §135-5.3. Additionally, he reported that the audit report and financial statements demonstrated that the school is capable of meeting the financial obligations of participating in the retirement system.

It was moved by Lou Ann Phillips, seconded by Mr. Brewer and carried unanimously that the North Carolina Leadership Academy become a participating employer in the Teachers' and State Employees' Retirement System, effective February 1, 2017.

Public Comment

The Chair recognized Ardis Watkins, State Employees Association of North Carolina (SEANC). SEANC supports the Treasurer's deep dive into the investments. SEANC supports the 10.33 percent employer contribution rate. SEANC requests the Board delay the COLA decision until later this month.

Setting of 2018 Employer Contribution Rates and making recommendations to the North Carolina General Assembly

It was moved by Michael Mebane, seconded by Terry McCann, and carried unanimously that the following contribution rate recommendations be approved for presentation to the North Carolina General Assembly: increase the current employer contribution rate appropriation of 10.08 percent to 10.33 percent to fund the ADEC for the Teachers' and State Employees' Retirement System; increase the appropriation of 29.46 percent to 30.23 percent to fund the ADEC for the Consolidated Judicial Retirement System; increase the current appropriation of 18.22 percent to 18.27 percent to fund the ADEC for the Legislative Retirement System; lower the employer contribution rate of 0.38 percent to 0.14 percent of payroll for the Disability Income Plan of North Carolina; and, increase the current appropriation to \$2 million above the ADEC for the North Carolina National Guard (to accelerate the payment schedule to pay off the unfunded liability).

Closing Comments

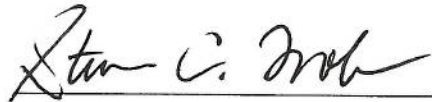
The Chair asked if there were any closing comments from board members. Hearing none, the Treasurer commented on the importance of funding the retiree health benefit plan and reducing investment related management fees by \$100 million. He stated that if these objectives are not achieved, then other areas, such as education and transportation, will be impacted long term.

State System Adjournment

There being no further business before the Board, the meeting was adjourned at 12:47 p.m., without objection.

A handwritten signature in blue ink, reading "Dale H. Hull, Jr.", written over a horizontal line.

CHAIR

A handwritten signature in black ink, reading "Stan C. Webb", written over a horizontal line.

SECRETARY