

**Texas Emergency Services Retirement System  
Meeting Minutes of June 27, 2016**

McAllen Convention Center, 700 Convention Center Blvd, Room 101-C, McAllen, TX 78501

**Members Present:**

Frank Torres, Chairman  
Gracie Flores, Vice-Chair  
Jenny Moore, Secretary  
Dan Key, Trustee  
Dennis Rice, Trustee  
Don Shipman, Trustee  
Ron Larson, Trustee  
Steve Williams, Trustee

**Members Absent:**

Taylor Allen, Trustee

**Others Present:**

Kevin Deiters, Judy Johnson, Shirley Hays, Susannah Jones, William Langford, TESRS  
Jim Crowson, Assistant Attorney General, OAG  
Mark Fenlaw, Consultant, Rudd and Wisdom  
Jeff Chalk and Charles Hodges, Consultants, Milliman  
Nick Gaspari, Consultant, Harvest

---

Chairman Torres called the meeting to order at 10:00 a.m. and made welcoming remarks.

**1. Roll call of Board Members and Excusal of Absences**

Secretary Moore called the roll and announced that a quorum of the Board was present. Eight Trustees were present and Trustee Allen was absent.

A motion was made by Secretary Moore to excuse the absence of Trustee Allen, which was seconded by Trustee Williams and passed unanimously.

**2. Invitation for Public Comment**

Chairman Torres called for Public Comment. No Public Comments were made.

**3. Approval of Minutes for March 4, 2016**

Chairman Torres noted for the record that Mark Fenlaw of Rudd and Wisdom should have been included in the names of those attending the meeting.

A motion was made by Trustee Rice for the adoption of the minutes as amended, which was seconded by Vice-Chair Flores and passed unanimously.

**4. Approval of Minutes for June 9, 2016**

A motion was made by Secretary Moore for the adoption of the minutes as accepted, which was seconded by Trustee Shipman and passed unanimously.

---

## **5. Investment Matters – Gracie Flores, Committee Chair**

**Chairman Torres called upon Vice-Chair Flores to chair the agenda items covering investment items.**

### **5A. Harvest Fund Advisors Presentation.**

Mr. Chalk introduced Mr. Gaspari, who was representing Harvest Funds LLC (Harvest).

Mr. Gaspari presented an overview of his firm and his report of June 27, 2016, covering investment performance for the Board's *Master Limited Partnership* for energy and he answered questions from the Board regarding his firm and investment performance.

No action was taken during this agenda item.

### **5B. Investment Consultant Report on Asset Allocation and Investment Performance (Milliman)**

Mr. Chalk provided the Board with an overview of the report from Milliman entitled *Texas Emergency Services Retirement System Investment Review 1<sup>st</sup> Quarter 2016*.

The report's executive summary reported that at the end of the first quarter of 2016, the assets in TESRS were \$88.8 million. At \$24.8 million, international equity assets are 27.9% of the fund. Domestic equities hold \$37.0 million in assets and represent 41.6% of the portfolio while Fixed Income at \$23.6 million represents 26.6%. For the quarter, the Total Fund was up by 1.0%, which exceeded the Policy Index at 0.7%. Over the past twelve months, the fund is down 2.7%.

Using the three-year annualized returns, seven managers have exceeded or been in-line with their respective benchmarks and six managers are above the 50th percentile. The Total Fund has exceeded the Benchmark Policy Index over a three-year annualized period by 0.7%. Over five years, the fund has exceeded by 0.6% and six of its managers are above the 50th percentile. As a result, we conclude the Total Fund is in line with expectations.

Mr. Chalk discussed the four portfolio recommendations found on page 2 of the executive summary. He stated that there was no need to rebalance because the asset allocation was in line with the Board's investment policy. He briefly discussed the asset allocation study recommendations to reallocate international bonds into US core fixed income and reallocate small-cap core into small-cap value. (Note: This topic was the subject of Agenda Item 5C).

Mr. Chalk recommended to the Board that it consider alternatives to Atlanta Capital Management (ACM). He reported that ACM expanded the size and composition of its investment team last year but that the new team has under-performed the index and ACM just announced that the most senior member of the investment team, Richard B. England, CFA Managing Director and Portfolio Manager of Growth Equities, will retire from the firm on October 31, 2016.

As a result, Mr. Chalk stated that Milliman was changing its recommendation and is recommending that the Board commence a search.

In response to a question from Chairman Torres about the causes of the under-performance, Mr. Chalk cited poor stock selection and not a change in process as the primary cause of ACM's under-performance.

Vice Chair Flores expressed her concerns that ACM no longer offered downside protection that existed earlier in the year when higher quality large cap growth stocks were out performing; however, now we have the combination of underperformance and changes in fund managers.

In response to a question from Trustee Williams about ACM's performance during the past year, Mr. Chalk directed the Board's attention to page 10 that ACM was in the 21<sup>st</sup> percentile; however, they underperformed their benchmark.

Chairman Torres asked if the Board needed to take immediate action. Mr. Hodge replied that the Board had time to commence a search.

Trustee Williams asked Chairman Torres if the Board needed to take action today regarding ACM and not wait until August. Chairman Torres responded that the Board could take the action under agenda item 5H.

#### **5C. Asset Liability Study - Discussion and Possible Action (Milliman)**

Mr. Chalk provided a summary of reports entitled *Supplemental Asset Allocation* dated April 5, 2016. He explained that Options 7, 8, and 9 all had higher expected returns and lower risk than the current asset allocation. Each of these three options would increase the fund's allocation to domestic fixed-income by eliminating the international fixed-income class from the portfolio. Option 7 would increase the allocation to small-cap core; Option 8 would not change the allocation to small cap core; and Option 9 would move out of small-cap core and into small-cap values.

Vice-Chair Flores commented that the Investment Committee's concentrated on Option 9 during their review of the proposed because it increased expected returns by moving out of international fixed income and it reduced risk by replacing small-cap core with small-cap value. She concluded that the proposed change in the asset allocation would not have a significant impact on the long-term expected performance of the fund.

Mr. Chalk summarized Milliman's recommendation to the Board that it adopt Option 9. This would reallocate the current allocation of international fixed-income into domestic fixed-income and reallocate the current allocation of small-cap core into small-cap value. As a result, the Board would no longer have international bonds or small cap-core as an asset classes. The expected return would increase slightly and reduce risk as measured by standard deviation. The elimination of the allocation of small-cap core would also address the underperformance of Luther King.

Vice-Chair Flores stated that the Investment Committee agreed with the recommendation of the Investment Consultant to select Option 9.

Chairman Torres called for a motion to accept the Investment Consultant's recommendation to adopt Option 9 from the April 5, 2016 *Asset Liability Model and Study Supplemental Report*.

The motion was made by Trustee Shipman, which was seconded by Trustee Williams and passed unanimously.

#### **5D. Asset Allocation - Discussion and Possible Action (Milliman)**

Chairman Torres called for a motion to increase the Board's target allocation to domestic fixed income by 5% from 21% to 26% by eliminating the Board's exposure to international bonds and to authorize the Staff and the Investment Consultant to take all actions necessary to execute this reallocation.

The motion was made by Trustee Larson, which was seconded by Vice-Chair Flores and passed unanimously.

**5E. Issuance of Request for Proposal for a Small Cap Value Manager - Discussion and Possible Action (Milliman)**

Chairman Torres called for a motion authorizing the committee to initiate Requests For Proposal (RFP) for a Small Cap Value Manager and a Large Cap Manager.

A motion was made by Secretary Moore, which was seconded by Trustee Shipman and passed unanimously.

**5F. Investment Policy - Discussion and Possible Action (Milliman)**

Chairman Torres called for a motion to amend the Investment Policy.

Vice-Chair Flores moved to amend the Investment Policy by removing the allocation to International Bonds and to increase the allocation to Domestic Fixed Income from a lower limit of 21%, target of 26% and the upper limit of 31%. The motion was seconded by Trustee Larson and passed unanimously.

**5G. Update on Investment Consultant Request for Proposal (Kevin Deiters)**

Mr. Deiters provided an overview of his memorandum dated June 24, 2016 regarding the RFP for Investment Consultant and explained that he cancelled the RFP for Investment Consultant that was issued on June 13, 2016 over concerns about the proposed process. He indicated his intent to re-issue the RFP within 30 days.

No action was taken on this agenda item.

**5H. Investment Committee Recommendations to the Board – Discussion and Possible Action**

Chairman Torres called for a motion to keep Atlanta Capital, Luther King and Wells Fargo on Watch.

The motion was made by Trustee Rice, seconded by Secretary Moore and passed unanimously.

*Note: The Board went into recess at 11:56 a.m. for a lunch break. The Board reconvened at 12:45.*

**6. Actuarial and Audit Matters – Don Shipman, Committee Chair**

Chairman Torres called upon Trustee Shipman to chair the agenda items covering Actuarial and Audit matters.

**6A. Actuarial Assumptions for the 2016 Actuarial Valuation - Discussion and Possible Action (Rudd and Wisdom)**

Mr. Fenlaw provided an overview of his report entitled *Recommended Actuarial Methods and Assumptions for the August 31, 2016 Valuation* and he recommending to the Board that it update its mortality table and make no changes to Investment Return Assumption.

He explained that he and other public plan actuaries are concerned about the suitability of the *RP-2000 Combined Healthy Mortality Tables* for public pension plans and he recommended that the Board

continue to use the *RP-2000 Combined Healthy Mortality Tables* with an adjustment in the expected mortality improvement with projection to 2024.

In regards to the Investment Return Assumption, Mr. Fenlaw recommended to the board that it continue to use 7.75%. He noted his opinion that the 3 percent assumed annual rate of inflation; the estimated long-term investment expense, and the 7.75 percent annual rate of return net of investment-related expenses were reasonable.

Trustee Shipman called for a motion to accept the Rudd & Wisdom's recommendations for the actuarial assumptions for the next actuarial valuation.

The motion was made by Trustee Key, seconded by Vice-Chair Flores and passed unanimously.

**6B. TLFRRRA System Accrued Time, Discussion and Possible Action (Rudd and Wisdom)**

Mr. Fenlaw referred the Board to page 4 of a 2003 information booklet for members and prospective members that provided an interpretation of state law and administrative practice for providing credit for prior service.

He explained that the issue of accrued time has been raised by a member contesting the accuracy of the retirement benefit estimate in his benefit statement because the member's accrued time was not counted as qualified service. It was the member's position that the System needed to treat accrued time as qualified service because the current statute and Board rules did not address accrued time.

Mr. Fenlaw agreed that the current statute and rules do not address accrued time; however, the current statute does not invalidate how things were done in the past. He explained that the Senate Bill that passed in 2005 repealed the old law and established a new law that gave the Board more flexibility to adopt Board rules. The rules subsequently adopted by the Board did not invalidate any prior Board contracts or change the way prior service was granted in the past.

Mr. Fenlaw said that the Board would need to make a substantive change to address the member's request and he stated his opinion that this was not a change that he would support or that the Board should make because what the System has done has followed the state law that was in effect at the time. He reminded the Board that departments had the option to grant prior service when they entered the system but that they had to pay for it.

Mr. Fenlaw concluded his presentation by advising that the answer to the member's inquiry is that the System followed the law that was in effect at the time the member's department joined the system and that we are administering the program in the appropriate way.

In response to a question from Trustee Shipman, Assistant Attorney General Jim Crowson concurred with Mr. Fenlaw's position on the issue and he recommended that the Executive Director send a written response to the member.

Trustee Shipman asked Mr. Fenlaw and Mr. Crowson to work with the Executive Director on drafting a response.

No action was taken on this agenda item.

**6C. GASB 68 Audit Report (Weaver and Tidwell, L.L.P.)**

Trustee Shipman directed the Board's attention to the audit report from Weaver and Tidwell entitled *Texas Emergency Services Retirement System Report on Pension Information August 31, 2015* containing the GASB 68 disclosures that the System will need to make available to participating entities. The report discloses to the amount of each participating entities net pension liability and expected total pension expense for the year ended August 31, 2015.

In response to a question from Secretary Moore, Ms. Johnson advised that we would send the audit and this report to each participating department.

**6D. Actuarial and Audit Committee Recommendations to the Board - Discussion and Possible Action**

No action was taken on this agenda item.

**7. System Administration and Oversight Matters – Ron Larson, Committee Chair**

Chairman Torres announced to the Board that he renamed the Rules Committee to System Administration and Oversight Matters Committee because the committee would be responsible for rules and system administration.

Chairman Torres called upon Trustee Larson to chair the agenda items covering System Administration and Oversight.

**7A. Qualified Domestic Relations Orders - Discussion and Possible Action (Kevin Deiters)**

Trustee Larson opened the discussion on Qualified Domestic Relations Orders (QDROs) and turned the presentation over to Mr. Deiters. Mr. Deiters provided an overview of the letter from Outside Counsel Chuck Campbell entitled *Qualified Domestic Relations Orders and TESRS, dated June 17, 2016*, in which Mr. Campbell recommends to the Board that it adopt a model QDRO form.

Mr. Deiters concluded his presentation by describing the process followed by the Board in 2007 to adopt the provisions of Government Code Section 804 governing QDROs and the Model QDRO that was used by the System at the time.

**7B. Model Qualified Domestic Relations Order - Discussion and Possible Action (Kevin Deiters)**

Mr. Deiters provided an overview of the draft *Qualified Domestic Relations Order* that was drafted by Mr. Campbell and explained the process that would be followed.

In response to a question from Mr. Larson, Mr. Deiters responded that the Board did not need to adopt the Qualified Domestic Relations Order and Mr. Crowson concurred.

No action was taken on this agenda item.

**7B. 2016 Customer Service Survey Presentation (Susannah Jones)**

Trustee Larson called upon Susannah Jones to discuss the results of *2016 Customer Service Survey*.

Ms. Jones provided an overview of the survey that was conducted in March and April 2016 to determine the satisfaction of clients to the services provided by the Agency. She indicated that the respondents were pleased with the level of customer service provided by the Agency and reported an overall satisfaction rate of 100%.

No action was taken on this agenda item.

**7C. Report on Pension System Activities (Shirley Hays)**

Trustee Larson called upon Contract Manager, Shirley Hays.

Ms. Hays presented a summary of her report entitled *FY 2016 TESRS Third Quarter Overview Report* covering call volumes, mail volumes, web inquires, and certain work flow measures such as the number of members added and terminated. The report indicates there were 3,950 active members, 2,233 vested terminated members, and 3,080 retired members during the quarter.

No action was taken.

**7E. Chief Financial Officer Report (Judy Johnson)**

Trustee Larson called upon Chief Financial Officer, Judy Johnson.

Ms. Johnson began her presentation by discussing the Appropriated Fund Budget and reporting that the Agency has spent \$503,451 or 66% of the annual budget of \$758,139. She expects to complete the fiscal year with a balance of \$12,970.

Ms. Johnson provided an overview of the Base Reconciliation process that the Agency submits to the LBB regarding actual and expected expenditures for FY 2016 and FY 2017. She reported that the Agency is in discussion with the LBB about exceeding the employee cap of 10 by one full-time equivalent employee; however, the Agency is in compliance with the provisions of Article IX of the appropriations act that allow agencies to exceed their employee cap by 10 percent.

For the Board's Non-Appropriated Fund Budget for FY 2016, Ms. Johnson reported that the current budget of \$852,992 reflects the increase approved by the Board for the Garcia and Richmond Contracts. Year-to-date expenditures of \$483,909 represent 56.7% of the budget and expect to complete the fiscal year under budget by approximately \$32,344.

Ms. Johnson reported that the System transferred \$500,000 in May because expenditures during the quarter (\$1.37 million) exceeded Contributions (\$900,000). For the fiscal year-to-date, a total of \$1.65 million has been drawn down under the budget authority of \$2 million.

Ms. Johnson concluded her presentation by reporting the receipt of department contributions in the amount of \$2,510,666 (include through May) and pension payments in the amount of \$3,904,955 through June.

Mr. Deiters asked if the Board needed to include investment management fees in the Board budget. Ms. Johnson replied that we needed to track investment management fees for cash flow purposes; however, it was not necessary to include them in the Board Budget. Trustee Shipman commented that investment fees could be provided as a separate informational item.

**7F. Board Budget - Discussion and Possible action (Judy Johnson)**

Trustee Larson turned over the meeting to Chairman Torres.

No action or changes were made.

**7G. Discussion and possible approval of Evaluations and Rules Committee recommendations to the Board**

No action was taken on this agenda item.

**8. Strategic Plan - Discussion and Possible Action (Kevin Deiters)**

Chairman Torres called upon Mr. Deiters to discuss the Agency Strategic Plan.

Mr. Deiters began his presentation with an overview of the state strategic planning and budgeting process and he provided an overview of the Agency Strategic Plan for Fiscal Years 2017 to 2021.

Chairman Torres called for a motion to approve the Agency Strategic Plan and to authorize the Executive Director to make non-substantive changes as needed.

A motion was made by Trustee Larson to approve the Strategic Plan, seconded by Trustee Shipman and passed unanimously.

**9. Legislative Appropriations Request Process Overview - Discussion and Possible Action (Kevin Deiters)**

Chairman Torres called upon Kevin Deiters to provide an overview of the Legislative Appropriation Request.

Mr. Deiters advised the Board that the Legislative Budget Board had not distributed instructions and that we would share the instructions with the Board upon our receipt. He advised the Board of his intent to only ask for base funding with no additional funding or additional employees.

Mr. Shipman recommended that the Agency attempt to keep 11 employees. Mr. Deiters responded that would seek guidance from the LBB on the matter.

Chairman Torres stated that he and Mr. Deiters met with the Governor's office last week and were advised against requesting exceptional items in the LAR.

The Board discussed the need to cancel the proposed meeting in El Paso that was scheduled for the end of August. After discussion, it was the consensus of the Board to meet in Austin during the first week of August.

No action taken on this agenda item.

**10. Executive Director's Report – Kevin Deiters**

In response to questions from Mr. Shipman about the status of the database up-grade, Mr. Deiters agreed to provide the Board with an assessment of the status of the project by the middle of July.

Chairman Torres agreed to Mr. Shipman's request to include the system upgrade as a future agenda item..

**11. Training for TESRS Board Members - Discussion and Possible Action**

No action was taken on this agenda item.



**12. Request for future agenda items and meeting dates**

Chairman Torres noted that the Board will meet on August 2 in Austin.

**13. Adjourn**

Chairman Torres called for a motion to adjourn.

A motion was made by Secretary Moore, which was seconded by Trustee Shipman to adjourn the meeting at 2:57 p.m. and passed unanimously.

Minutes Approved By:

  
\_\_\_\_\_  
Signature: Secretary Moore

8-2-2016  
\_\_\_\_\_  
Date: