

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

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

April 27, 2012

Board Members Present

Ken Cochran, Chairman
Greg Hahn, Vice Chairman
Tim Berry
Jodi Golden
Adam Horst
Michael Pinkham
Bret Swanson
Cari Whicker

Others Present

David Thomas, Inspector General of State of Indiana
Pete Keliuotis, Strategic Investment Solutions (SIS)
Rich Dabrowski, Strategic Investment Solutions (SIS)
Jim Baker, Unite Here
Andy Thomas, IRTA

Staff Present

Steve Russo, Executive Director
Erin Hankins, Executive Assistant
Andrea Unzicker, Chief Legal & Compliance Officer
Katie Williams, Legal Analyst
Julia Pogue, Chief Financial Officer
Jeff Hutson, Chief Communication Officer
Teresa Snedigar, Director of Internal Audit
David Cooper, Chief Investment Officer
Brian Rogers, Investments, Director of Real Assets
DeAndra Ballard, Investments
Scott Davis, Investments, Director of Public Equity

Meeting called to order at 9:01 a.m. by Vice Chairman Hahn.

I. Board Education

A. Plan Design & Administration

Steve Russo introduced the topics to be covered in the Board Education portion of the meeting. Steven Barley began the presentation on Plan Design and the administration of pension plans by providing an overview of the Operations department of INPRS. Mr. Barley gave a history of the retirement process, summarized the re-engineering of the operations department, and mapped out the methods to process retirements for all funds. Mr. Barley presented the future model of the retirement process, goals for the Operations department, and plans for improved customer service.

Mr. Russo educated Board members on the current issues and trends in the public pension community using information compiled by NASRA Research Director, Keith Brainard.

B. Governance

Teresa Snedigar provided governance training to the Board. She defined fraud, discussed who is responsible for aspects of governance and fraud risk, identified five principles for governance, and highlighted the importance of “tone at the top”. Ms. Snedigar gave an overview of the fraud program, audit and risk oversight, and the plans to coordinate risk at INPRS. She concluded her presentation with an explanation of Board responsibility in the areas of governance and audit. A discussion was had among the Board and Staff regarding the audit committee and types of audit reports produced.

C. Ethics

Andrea Unzicker introduced David Thomas, Inspector General of the State of Indiana, to the Board. Mr. Thomas educated the Board on State of Indiana ethics requirements, contract guidelines, and potential conflicts of interest for board of trustee members.

D. Fiduciary Duties & Responsibilities

Ms. Unzicker introduced Pete Keliuotis and Rich Dabrowski from SIS. Messrs. Keliuotis and Dabrowski gave an overview of fiduciary issues for public fund trustees. They discussed the fiduciary duties to act solely on behalf of plan participants and to act with prudence, and reviewed special issues with respect to Defined Contribution Plans.

Staff and all visitors were dismissed for the Executive Session of the Board of Trustees.

II. Executive Session

An Executive Session was held at 12:12 p.m. pursuant to 5-14-1.5-6.1(b)(2)(B) and IC 5-14-1.5-6.1(b)(9).

As required by IC 5-14-1.5-6.1(d), the board hereby certifies that only subject matter related to IC 5-14-1.5-6.1(b)(2)(B) and IC 5-14-1.5-6.1(b)(9) was discussed.

Regular meeting called to order at 1:47 p.m. by Chairman Cochran.

Mr. Cochran recognized Board member Cari Whicker for her years of service to the TRF and INPRS Boards of Trustees.

III. Approval of Minutes from February 17, 2012 Board of Trustees Meeting

MOTION duly made and carried to approve the minutes from the February 17, 2012 Board meeting.

*Proposed by: Tim Berry
Seconded by: Adam Horst
Votes: 8 in favor, 0 opposed, 0 abstentions*

IV. New 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. Board Governance Manual Adoption of Revisions

Andrea Unzicker presented an executive summary of updates made to the Board Governance Manual. Updates were made to the Enterprise Risk Management Policy and its three major sections: Policy, Statement of Enterprise Risk Appetite, and the Board of Trustees Risk Oversight Charter. Updates to the Procurement Policy include addition of guiding Procurement Principles; small purchase guidelines; alignment with certain State language and policies for small purchases, negotiated bidding, and requests for information; and statutory requirements for investment real estate property management. Other updates to the Manual were based on Indiana Code changes and technical corrections.

A proposal was made by a Board member to have the Audit Committee preview the proposed changes to the Manual in advance of review by the full Board. A discussion was had on governance and audit. A decision was made to have all Board Governance Manual updates discussed by the Audit committee before bringing them before the Board for approval.

B. Financial Update

Julia Pogue recognized Steve Russo for his nomination and selection for the Central Indiana Chapter of the Association of Government Accountants 2012 award for Outstanding Service in State Government. Mr. Russo was recognized for his leadership in the successful merger of PERF and TRF, and the creation of INPRS (Indiana Public Retirement System).

Ms. Pogue presented the INPRS financial update to the Board. This update included financial highlights as of March 2012. Payouts and expenses were as expected. She summarized the Fiscal Year 2012 forecasted net position compared to the budget for four specific areas: administration, projects, investments, and capital.

C. FY13 Preliminary Budget

Ms. Pogue reviewed the preliminary budget for fiscal year 2013 to be approved by the Board at a later date. She presented the FY13 strategic plan goals and budget drivers, gave an overview of the budget categories, and reviewed capital expenditures from 2009 to 2013. New for FY13 budget is a breakout of ASA costs. Identifying administrative costs specific to the ASA will be useful for understanding and controlling costs and allow for possible charging of ASA administration to member accounts. The Board asked about the current practice and the possibility of adjusting the Guaranteed Fund rate to account for administrative costs. Staff explained current accounting practice and stated that the adjustment suggestion could be considered.

The Board asked for a chart showing historical budget trends. Ms. Pogue said Finance could prepare the chart. The Board asked about the proposal to provide online statements as default for members. A discussion was had among Board and Staff regarding member email contact and online account management.

D. Investments Update

David Cooper began the investment update with a review of the INPRS portfolio. Mr. Cooper presented the INPRS Asset Allocation: actual and target. He gave an

Economic update and an INPRS portfolio update. The peak to trough performance is showing continued improvement. In summarizing the DB Performance, Mr. Cooper said that it has been a good quarter; at end of this year the 10 year figure will most likely greatly improve; and we have had a positive start with risk parity. He compared the rates of return for Private Equity and Private Real Estate, compared the INPRS Historical Asset Class Returns from 2003 to present, and summarized the ASA Performance of PERF and TRF funds. Mr. Cooper reviewed the list of recent investments and terminations and gave an update on the Watch List.

E. FY13 Guaranteed Fund Rate Approval

Steve Russo summarized the discussion of the Guaranteed Fund (GF) Rate from the February 2012 Board Meeting and reviewed the applicable Indiana Code. He presented a staff recommendation that the board consider establishing a revised methodology for setting the GF rate at this meeting and recommended that broader discussions related to alternatives to the GF be tabled until the next meeting to allow staff time to engage consultant CapCities to assist Board and staff. A draft Statement Of Work (SOW) was presented to the Board. There was consensus to engage CapCities. Staff requested that Board members review the draft SOW and provide staff any suggested changes to the SOW no later than May 4, 2012.

David Cooper gave an overview of the PERF/TRF GF Rate History and the GF Reserves of PERF, TRF, and then combined as INPRS. The current low interest economic environment was highlighted. Mr. Cooper stated that INPRS should base GF rate setting methodology on the US Treasury rather than the GIC Index noting that GIC's are much less available in the market today. He emphasized that the investment staff and investment committee have been reviewing the difficulties in achieving a rate of return greater than the rate determined by the current methodology without assuming unjustified investment risk. The current methodology is "The crediting rate will be the 2-year GIC Index Rate compiled by T. Rowe Price, +/- 0.50%, taking into account the investment performance of the underlying assets, rounded to the nearest 0.25%." As Mr. Cooper introduced the proposed PERF and TRF GF Rate methodology, he stated that the underlying INPRS guaranteed fund portfolio benchmark's weighted average yield-to-worst should allow the current and proposed guaranteed fund rates to be attained with minimal risk to the plans, even with a moderate increase in interest rates.

Staff recommended that the Board adopt the following language for the PERF and TRF guaranteed fund programs:

The guidelines for setting the interest credit rate for the PERF and TRF guaranteed programs shall be:

The Guaranteed Fund interest credit rate will be established annually by the Board, normally at the Board's April/May meeting but no later than June 30th. It will be calculated by comparing:

"Current Yield" = Average of January, February, and March month-end 2-year US Treasury Note yields in the current year; and

"Prior Yield" = Average of January, February, and March month-end 2-year US Treasury Note yields in the prior year.

- *If the "Current Yield" is lower than the "Prior Yield":*
 - *The interest credit rate will be set to the "Current Yield," rounded to the nearest basis point.*
- *If the "Current Yield" is higher than the "Prior Yield":*
 - *The interest credit rate will be set to the average of the "Current Yield" and the "Prior Yield," rounded to the nearest basis point.*

MOTION duly made and carried to approve the staff recommended methodology as stated above.

*Proposed by: Greg Hahn
Seconded by: Bret Swanson
Votes: 7 in favor, 0 opposed, 0 abstentions*

Mr. Cooper presented the staff recommendation for the proposed PERF and TRF guaranteed fund crediting rate for FY 2013. Staff recommended that the Board adopt the following:

The interest credit rate for the PERF and TRF guaranteed programs shall be 0.28%, effective on July 1, 2012.

MOTION duly made and carried to approve the staff recommended Guaranteed Fund rate of 0.28% effective on July 1, 2012.

*Proposed by: Bret Swanson
Seconded by: Jodi Golden
Votes: 7 in favor, 0 opposed, 0 abstentions*

F. Executive Director's Report

Steve Russo presented the Executive Director's report. He gave a legislative update, summarizing bills that were enacted (SEA 127, SEA 128, HEA 1003, HEA 1123, and HEA 1376). He then updated the Board on the ongoing modernization efforts. The Employer Reporting & Maintenance (ERM) project is delayed until October 2012 to allow for a longer "soft open" for employers and programming of additional functionality. The new Defined Benefit system (INPAS) project remains on track. Mr. Russo gave a CAFR update, stating that the FY 2011 PERF and TRF CAFRs were awarded Government Finance Officers

Association (GFOA) Certificates of Achievement for Excellence in Financial Reporting. A consolidated INPRS CAFR is planned for FY 2012. Mr. Russo presented metrics highlights for the Governor's and Board Dashboards, as well as key metrics from the INPRS Scorecard for Operations, Communications, Finance, Investments, and Audit departments.

G. Other Business

Motions were made relating to matters discussed by the Board during the Execution Session.

MOTION duly made and carried to approve INPRS as lead plaintiff in litigation filed against SAIC, Inc.

Proposed by: Mike Pinkham
Seconded by: Bret Swanson
Votes: 7 in favor, 0 opposed, 0 abstentions

MOTION duly made and carried to approve 6% salary increase to INPRS Executive Director, Steve Russo, based on the job evaluation discussed during the Executive Session.

Proposed by: Adam Horst
Seconded by: Greg Hahn
Votes: 7 in favor, 0 opposed, 0 abstentions

Mr. Russo proposed a compensation plan for INPRS Investment Staff. He reviewed the history and goals of the investment department and emphasized the importance and cost saving potential of internal investments management. Mr. Russo gave an overview of the current compensation structure and the risk of high turnover of staff members. He compared INPRS investment staff salaries to those of other public pension plans: 80% of INPRS salaries are at or below the 25th percentile as compared to other plans in the Midwest region. He noted that approximately 50% of public plans provide performance based incentive compensation to their investment professionals.

Mr. Russo proposed (1) to establish separate base-pay bands for investment professionals at INPRS and (2) to replace the standard pay for performance program with a unique incentive compensation component for investment professionals. He proposed Investments' Base Pay Bands for employee types with midpoints set to 50th percentile of comparable Midwest externally managed public pension funds. Three steps for implementation were also proposed: Step 1) Immediately increase base salaries to the 25th percentile (Min) for each band; Step 2) Raise base salaries toward 50th percentile (Mid) over the next 3 to 5 years based upon individual performance; and Step 3) Annually review and update base pay bands. Mr. Russo presented the INPRS Investment Incentive Plan objectives (reward performance, recruitment and retention) and guiding principles. He proposed elements for the incentive plan rewards, including

drivers, reward factors, and a reward formula. Mr. Russo concluded the presentation with other provisions for the incentive compensation plan and several example scenarios.

MOTION duly made and carried to support the Executive Director's decision to establish separate base-pay bands for investment professionals and the establishment of a incentive compensation plan for INPRS Investments staff.

Proposed by: Adam Horst
Seconded by: Jodi Golden
Votes: 7 in favor, 0 opposed, 0 abstentions

V. Adjournment

MOTION duly made and carried to adjourn the April 27, 2012 Board meeting at 3:30 p.m.

Proposed by: Bret Swanson
Seconded by: Adam Horst
Votes: 7 in favor, 0 opposed, 0 abstentions