MINUTES
BOARD OF TRUSTEES OF THE
INDIANA PUBLIC RETIREMENT SYSTEM

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

November 2, 2012

Board Members Present
Ken Cochran, Chairman
Brian Abbott
Tim Berry
Jodi Golden
Adam Horst
Michael Pinkham
Kyle Rosebrough
Bret Swanson

Others Present
Pete Keliuotis, Strategic Investment Solutions (SIS)
Rich Dabrowski, Strategic Investment Solutions (SIS)
Ray Jones, IRTA
Andy Thomas, IRTA
Adam VanOzdol, Indiana Legislative Insight

Staff Present
Steve Russo, Executive Director
Andrea Unzicker, Chief Legal & Compliance Officer
Julia Pogue, Chief Financial Officer
Jeff Hutson, Chief Communication Officer
Teresa Snedigar, Director of Internal Audit
Mike Hineline, Chief Information and Technology Officer
David Cooper, Chief Investment Officer
Scott Davis, Investments, Director of Public Equity
Ben Fair, Investments
Tony Huang, Investments
Erin Hankins, Executive Assistant
Katie Williams, Legal Analyst

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

Mr. Cochran introduced new board members present: Kyle Rosebrough and Brian Abbott.

I. Approval of Minutes from September 14, 2012 Board of Trustees Meeting

MOTION duly made and carried to approve the minutes from the September 14, 2012 Board meeting.

Proposed by: ***Tim Berry***
Seconded by: ***Mike Pinkham***
Votes: ***6 in favor, 0 opposed, 2 abstentions***

II. Committee Reports

A. Appointments to Committees

Chairman Cochran discussed committee assignments and asked for feedback from the board. All were in agreement and Chairman Cochran finalized the appointments.

B. Investment Committee

Bret Swanson presented the INPRS Investment Committee report to the Board. On October 22, 2012, the committee met and discussed the following topics: major actuarial valuation assumptions and methods; compliance (there were no violations); performance review; department update; RFI timeline for annuity rate of ASA funds; IIF2 update; mid cap growth RFP update; absolute return strategy; and fixed income strategy.

III. 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. Actuarial Valuation & Contribution Rates

Steve Russo introduced the topic and invited Julia Pogue to make the presentation on actuarial valuation results to the Board. Ms. Pogue began with an overview of her presentation and an explanation of the board’s role in the decision making process. She reviewed the INPRS funding objectives: 1) achieve and maintain at least an 80% funded status; 2) have contribution rates equal to or greater than the ARC; 3) do not decrease contributions rates until funds reach 100% funded status; and 4) maintain stable contribution rates over time. She also stated that following an analysis of the new GASB rules, a formal funding policy will be presented to the Board for approval. Ms. Pogue summarized significant changes affecting INPRS since the June 30, 2011 valuation, which included: major actuarial assumption changes for all DB retirement plans; a market value of asset return in FY12 (0.7%) that was lower than assumed (7.0%); cost of living adjustments; excess reserve monies of $329M not included in June 30, 2012 valuation results, but reflected in future projections; and state appropriation of $19.6M for TRF 13th Checks that was also not included in June 30, 2012 valuation results, but reflected in future projections.

A high level executive summary given by Ms. Pogue identified factors used in the actuarial valuation. She explained the participant information for all INPRS funds used in the valuation. There has been a gradual increase over time of inactive-vested members. Efforts made to contact inactive-non-vested members and distribute funds to these members resulted in a significant reduction in numbers and therefore a savings in record keeper fees of about $1M.

Ms. Pogue gave an overview of INPRS asset reconciliation and explained the changes in market value of assets and actuarial value of assets. She then reviewed the changes in actuarial accrued liability for FY12.

Ms. Pogue gave an explanation of a chart detailing INPRS funded status as of the end of fiscal year 2012 and comparing the numbers to the end of fiscal year 2011. The aggregate unfunded actuarial accrued liability for pre-funded plans is $4,678.5M (81.2% funded status). The aggregate unfunded actuarial accrued liability for all INPRS plans (including the TRF Pre-1996 “pay-as-you-go” Account) is $16,222.4M (60.8% funded status). Board members asked clarifying questions about the numbers for various funds. Staff and other board members provided answers and explanations.

Ms. Pogue stated that majority of other plans in the US are using an 8.0% assumed interest rate. An interest rate sensitivities chart compared three different interest rates (6.75% [INPRS’ current baseline], 7.5%, and 8.0%) and their affect on unfunded actuarial accrued liability and funded status for all INPRS plans. The chart revealed that if INPRS used an 8.0% assumed interest rate, the funded status of pre-funded plans would be 92.9%. Mr. Russo mentioned that INPRS’ assumptions are more conservative and assumptions do not change the amount paid out to members in benefits, but they drive the timing of when benefits are paid. Board members discussed the methodology of rate setting and stated that rate setting was connected to the investment strategy. Ms. Pogue stated that the goal is to reach 100% funded status for all plans while protecting the pension plan long-term. Mr. Russo added that failing to meet assumed rates hurts the long-term funded status of the plans.

Ms. Pogue presented the recommended contribution rates and appropriation amounts for 2014 and compared them to the approved rates from 2013. A chart showed the affect of the rates and amounts on the actuarial calculated rate

(ARC). A higher rate for the 1977 Fund will continue to be maintained in order to reach 100% ARC. The E,G & C Plan, Judges Plan, and PARF received money from the state surplus that is applied to reduce the contribution rate and appropriation amounts, resulting in the ARC not being met for 2014, yet exceeding the ARC for 2013.

Ms. Pogue then reviewed charts showing the PERF projection of total funded status, PERF projection of state contributions, and PERF projection of political subdivision contributions. She then reviewed charts showing the projection of funded status and projection of actuarially calculated contribution rate for the TRF 1996 account. Chairman Cochran asked for a brief overview and history of the TRF plans, which Ms. Pogue provided. Mr. Russo and other board members contributed to the explanation and discussion of TRF plans. A discussion was had on the importance of rate stability. Charts showing the projection of funded status and projection of contributions were presented for the 1977 Fund, JRS, EG&C, PARF, and LEDB.

Ms. Pogue provided history on the migration to a single rate (Composite Rate Group) for all PERF Political Subdivisions (PSDs). The CRG effective January 1, 2013 is 10.0%. Employers who were contributing more than 10.0% were brought down and for those below 10.0%, contribution rates were held to a maximum 1.5% increase year-over-year, therefore not all PSDs are at 10.0% yet. Approximately 70% of PSDs are currently included in the CRG. Based on actuarial valuations as of June 30, 2012, the recommended CRG contribution rate for PSDs is 11.2% effective January 1, 2014. Ms. Pogue explained that the 1.2% year-over-year increase was made of up: 0.8% due to the interest rate assumption change from 7.0% to 6.75%; 0.3% due to asset returns; and 0.1% due to mortality and other assumption and experience changes. Ms. Pogue then brought forth the INPRS staff recommendation to maintain the policy from the previous year and keep a maximum year-over-year increase of 1.5%. The employer rate would be capped at 11.2%. An additional 53 employers would be brought into the CRG, resulting in a total of 74% participation. Mr. Horst offered a summary of the discussion had and consideration by the investment committee on the topic. A discussion was had on the affect of the addition of political subdivisions to the Composite Rate Group, as well as the motivation for getting all employers into the CRG.

Ms. Pogue presented the staff recommendation for the Legislators' Defined Contribution Plan contribution rates. She first reviewed Indiana statute, which states the Board shall use the following rates in determining the LEDC crediting rate: 1) The rate at which the State makes contributions to fund the pension portion of a PERF member's retirement benefit and 2) The rate at which the State makes contributions to the Annuity Savings Accounts on behalf of State employees who are members of PERF. The recommended LEDC plan rate effective January 1, 2013 is 12.7% (based on 9.7% State contribution rate and 3.0% ASA rate). The recommended LEDC plan rate effective January 1, 2014 is

14.2% (based on 11.2% State contribution rate and 3.0% ASA rate). The recommended LEDC plan rate effective January 1, 2013 was discussed in the prior year's board meeting, but a vote was not taken then. Therefore the recommended 2013 rate was presented for a vote this year along with the recommended 2014 rate.

Ms. Pogue discussed the Annuity Savings Account Only (ASA-Only) Plan. She explained that effective February 1, 2013, all State new hires will have the option to elect to participate in the current DB hybrid plan or the new ASA-Only Plan. The member contribution rate for ASA-Only remains at 3.0% and will be paid by the State. The employer contribution rate will be the same as the DB contribution rate with two components: 1) the crediting rate to the member's ASA-Only account shall be at least 3.0% and not greater than the normal cost of the fund and 2) any amount not credited to the member's account shall be applied to the Unfunded Actuarial Accrued Liability (UAAL) of PERF. Mr. Russo explained normal cost and answered a board member's questions about the components and membership of the new plan. A board member brought up the Legislators' Defined Contribution Plan (LEDC) and compared it to the ASA-Only plan, pointing out the large difference in contribution rates. A discussion was had among staff and board members on the topic. It was noted that the discussion should not affect the board's vote on the ASA-Only plan, but was something to consider going forward. Mr. Russo mentioned that an internal legal review of the statutes regarding the LEDC contribution rate had been initiated and an update would be given to the Board in the December meeting. A board member stated that the board could approve the 2014 LEDC rate now, but would evaluate the rate after receiving results of the legal review.

Ms. Pogue presented the staff recommendation for ASA-Only contribution rate methodology. INPRS staff recommended the methodology for establishing the amount credited from the employer's contribution rate to the member's account for the ASA-Only Plan be the "Normal Cost (associated with the development of the State contribution rate) rounded down to the nearest 0.1%." Using this methodology and the FY2014 Calculated Normal Cost of 4.78%, 4.7% would be the rate recommended to credit member ASA-Only accounts beginning February 1, 2013 through fiscal year-end 2014 (June 2014). It was also recommended that the Board review this methodology every year as INPRS gains actual experience for the number of members who select the ASA-Only option. Clarification was made that the total contribution rate would be 7.7% (Employer contribution of 4.7% plus Member contribution of 3%). A discussion was had on enrollment, accommodating for new options available to members, and the uncertainty of how many new hires would choose the ASA-Only plan.

Ms. Pogue then reviewed the INPRS staff recommendation for contribution rates and appropriation amounts as detailed in the following charts:

INPRS Staff Recommended Contribution Rates for Fiscal Year 2013 (February 1 – June 30, 2013)	
ASA-Only Employer Crediting Rate	4.7%
ASA-Only Total Employer Contribution Rate	9.7%

INPRS Staff Recommended Contribution Rates for Fiscal Year 2014	
PERF State	11.2%
PERF PSD Composite Rate	11.2%
TRF 1996 Account	7.5%
ASA-Only Employer Crediting Rate	4.7%
ASA-Only Total Employer Contribution Rate	11.2%

INPRS Staff Recommended Contribution Rates for Calendar Year 2013	
LEDC Plan	12.7%

INPRS Staff Recommended Contribution Rates for Calendar Year 2014	
1977 Fund	19.7%
E,G,&C Plan	20.75%
LEDC Plan*	14.2%

**Subject to legal analysis and further board review.*

INPRS Staff Recommended Appropriation Amounts ($000's) for Fiscal Year 2014	
Judges Plan	$20,895
PARF	$1,174
LEDB Plan	$138

Questions were asked and a discussion was had on the timing of contribution rate changes (calendar year verses fiscal year) for employers.

MOTION duly made and carried to adopt the staff recommended contribution rates and appropriation amounts as detailed in the above charts and individual PSD Employer Rates reflected in the attachment presented to the Board.

Proposed by: ***Adam Horst***
Seconded by: ***Bret Swanson***

Votes: *8 in favor, 0 opposed, 0 abstentions*

Ms. Pogue concluded her presentation with a summary of the contribution rates and appropriation amounts estimated for the Fiscal Year 2015 State Budget.

IV. Unfinished Business

A. Private Equity Update: Indiana Investment Fund II (IIF2)

Mr. Russo introduced David Cooper and Pete Keliuotis to the Board and provided a brief overview of the investment department and relationship with outside consultants.

Mr. Cooper reviewed the current Indiana investment funds, provided background on the Request for Proposal process performed by SIS to select an investment firm to manage Indiana Investment Fund II (IIF2), and explained the timeline of the process.

Mr. Keliuotis provided a detailed explanation of the different investment options available for the IIF2 and the RFP process performed by SIS. The evaluation process encompassed a scoring matrix comprised of ten criteria: experience with similar mandates (customized and in-state); firm-wide private equity assets under management (minimum of $1 billion); performance (past success); investment process (well defined, consistent and appropriate for IIF2); organizational structure (stable, committed to private equity); investment professionals (team depth and history together); risk management; experience and knowledge of Indiana PE market and opportunities; terms and conditions; and understanding of the INPRS Investment Policy Statement.

The three finalists with the highest scores (The Carlyle Group, Credit Suisse Customized Fund Investment Group (CFIG), and Hamilton Lane Advisors) were invited to make presentations at the SIS office on 10/26 and 10/29/12. Based on the SIS evaluation of all of the IIF2 candidates and the results from interviews, SIS recommended The Carlyle Group for the IIF2 mandate and to potentially take over management of some or all of the legacy funds, pending approval by INPRS and the other fund LPs. This recommendation is predicated upon the completion of final due diligence, legal review, and successful negotiation of terms and conditions.

MOTION duly made and carried to approve SIS' recommendation for the selection of The Carlyle Group for the IIF2 mandate and potential management of some or all legacy funds, pending approval by INPRS and other fund LPs.

Proposed by: *Bret Swanson*
Seconded by: *Jodi Golden*
Votes: *8 in favor, 0 opposed, 0 abstentions*

V. **New Business**

A. Financial Update

Julia Pogue presented the INPRS financial update to the Board. This update included financial highlights as of September 2012 with details about change in net position due to investments, contributions received, benefit payouts and benefit expenses. She summarized the Fiscal Year 2013 forecasted net position compared to the budget for four specific areas: administration, projects, investments, and capital. Ms. Pogue gave an overview of the INPRS FY2013 annual change in net position forecast and explained the purpose and process of developing the forecasted variances. Additional charts detailing financial information were provided to the Board.

B. Investments Update

David Cooper began with an update on the Request for Information timeline for annuity rate of ASA Funds. He gave background on the current ASA options at retirement and the current annuity rates. The RFI would solicit information from mostly insurance providers to learn how they set annuity rates and invest the funds. The RFI would also explore potential partnerships with providers. Mr. Cooper stated that he would update the Board on the RFI process and results. Mr. Russo suggested that the February 2013 board meeting may include an update.

Mr. Cooper reviewed the INPRS portfolio and mentioned that efforts are being made to merge the PERF and TRF ASA funds. In discussing the peak to trough performance, he stated that the past quarter was an all time high for INPRS defined benefit market value. Mr. Cooper then reviewed the INPRS asset allocation, actual and target, as of September 30, 2012, and the first quarter FY13 performance by comparing asset class contribution to total return. Mr. Cooper presented the economic update and stated that his greatest concerns are the US fiscal cliff and Europe.

Mr. Cooper discussed the CY 2012 performance of asset types in different economic environments, which demonstrates the need for diversification and risk management. He then reviewed the distribution of INPRS' monthly returns from January 2009 to September 2012.

In summarizing the DB Performance, Mr. Cooper mentioned that the ten year numbers will significantly change when 2003 rolls off. He compared the rates of return for private equity and private real estate and gave an update on risk parity performance. He then discussed the ASA performance of PERF and TRF funds and explained the options available to members. A discussion was had among board members and staff on the percentage of members who default or actively manage investment options for their ASA and how to better understand the choices of members. Mr. Cooper explained target date funds and the pension relief and special death funds and their performance.

Mr. Cooper referenced the list of recent investments and terminations and briefing explained the management process. Mr. Cooper gave an update on the Watch List and said that an RFP is in process for the mid-cap growth mandate.

C. Executive Director's Report

Mr. Russo updated the Board on the ongoing modernization efforts. He provided background, history, and a summary of the purpose of the Employer Reporting & Maintenance (ERM) project which went live in October 2012. The new Defined Benefit system (INPAS) project development remains on track, but the go-live date may be affected by a delay in ERM testing and the legislative requirement to launch ERM 2.0 ASA-Only plan on February 1, 2013. INPAS launch may be delayed until mid or late 2013. Mr. Russo presented the elements within each track of the ERM go-live process and discussed some current issues with the new system. Board members asked questions about the errors, employer feedback, resolution efforts, and how the errors were discovered. Staff responded that the errors were discovered by INPRS staff and employers within 24 hours and employers were contacted immediately. Board members expressed positive feedback with regard to the implementation and management of the new system.

Mr. Russo reported the Line of Duty death of Lake County Sheriff, Britney Muex.

Mr. Russo then presented metrics highlights for the Governor's and Board Dashboards. Some checks to members were delayed last month due to human error and the east coast hurricane.

VI. Other Business

No other business was brought forth.

VII. Preliminary Agenda for Next Board Meeting

The date of the next board meeting will be December 14, 2012. Orientations for new board members are on schedule. Mr. Russo stated that al committees will meet before the next meeting and those reports will be added to the agenda.

VIII. Adjournment

MOTION duly made and carried to adjourn the November 2, 2012 Board meeting at 12:37 p.m.

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