

NEW MEXICO EDUCATIONAL RETIREMENT BOARD

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October 20, 2017

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MINUTES OF THE

NEW MEXICO EDUCATIONAL RETIREMENT BOARD

REGULAR MEETING

October 20, 2017

1. CALL TO ORDER: QUORUM PRESENT

A Regular Meeting of the New Mexico Educational Retirement Board was called to order on this date at 9:10 a.m. in the Educational Retirement Board Conference Room, 6201 Uptown Boulevard, N.E., Ste. 203, Albuquerque, New Mexico.

Members Present:

Ms. Mary Lou Cameron, Chairwoman
Mr. H. Russell Goff, Vice Chairman
Mr. Larry Magid, Secretary
Mr. David Craig [sworn in later]
Dr. Donald W. Duszynski
The Hon. Tim Eichenberg, State Treasurer [left at 10:45 a.m.]

Members Excused:

None.

Staff Present:

Ms. Jan Goodwin, Executive Director
Mr. Rick Scroggins, Deputy Director
Mr. Bob Jacksha, CIO
Mr. Roderick Ventura, General Counsel
Mr. Mark Canavan, Real Estate and Real Assets Portfolio Manager
Ms. Norma Henderson, CFO
Mr. Alan Myers, Public Securities & Debt Portfolio Manager
Ms. Monica Lujan, Member Services Director
Ms. Lealia Nelson, Outreach Coordinator
Ms. Liz Lorang, Executive Assistant
Mr. Lawrence Esquibel, Chief Information Officer

Others Present:

Ms. Patricia J. Turner, Contract Attorney
Mr. Ryan Falls, Gabriel Roeder Smith
Mr. Allan Martin, NEPC
Mr. Sam Austin, NEPC
Ms. Judith Beatty, Recorder
[See sign-in sheet.]

b. Approval of Agenda

Mr. Goff moved approval of the agenda, as published. Dr. Duszynski seconded the motion, which passed unanimously by voice vote.

c. Approval of Minutes – September 18, 2017

Mr. Goff moved approval of the September 18 minutes, as submitted. Dr. Duszynski seconded the motion, which passed by voice vote, with Mr. Eichenberg abstaining.

d. Introduction of Guests

Mr. Martin introduced Sam Austin to the board. Mr. Austin recently joined NEPC as partner and member of its Public Fund team, and would be supporting Mr. Martin in working with the NMERB.

2. SWEARING IN OF NEW BOARD MEMBER – David Craig

Mr. Craig was sworn in as Board Member.

Mr. Craig stated that he was with the School Budget and Finance Analysis Bureau of the New Mexico PED and looked forward to serving on the board.

3. CONSENT AGENDA

a. Board Travel

Mr. Eichenberg cautioned the board that a plane ticket purchased through the State Purchasing Division's statewide price agreements is not necessarily the lowest and that a better deal can sometimes be found elsewhere.

Chairwoman Cameron congratulated Ms. Goodwin on her election last week to the national executive committee of NCTR (National Council of Teacher Retirement), an honor for the NMERB.

4. APPROVAL OF 2018 BOARD MEETING DATES

Mr. Eichenberg moved for approval. Mr. Magid seconded, and the motion passed unanimously by voice vote.

5. ERB COMMITTEE APPOINTMENTS

a. ARP Committee Appointments

Chairwoman Cameron requested approval of the following appointments to the ARP Committee: Larry Magid; Don Duszynski; David Craig.

Mr. Goff moved for approval. Mr. Eichenberg seconded, and the motion passed unanimously by voice vote.

b. Evaluation Committee Appointments

Chairwoman Cameron requested approval of the following appointments to the Evaluation Committee: Russell Goff; Larry Magid; Mary Lou Cameron.

Mr. Eichenberg moved for approval. Dr. Duszynski seconded, and the motion passed unanimously by voice vote.

c. Investment Committee Appointments

Chairwoman Cameron requested approval of the following appointments to the Investment Committee: Mary Lou Cameron; Russell Goff; Larry Magid.

Mr. Eichenberg moved for approval. Mr. Goff seconded, and the motion passed unanimously by voice vote.

d. Audit Committee Appointments

Chairwoman Cameron requested approval of the following appointments to the Audit Committee: Mary Lou Cameron; Tim Eichenberg; Russell Goff.

Mr. Magid moved for approval. Mr. Goff seconded, and the motion passed unanimously by voice vote.

6. JUNE 30, 2017 ACTUARIAL VALUATION REPORT: RYAN FALLS, GABRIEL ROEDER SMITH & COMPANY

Mr. Falls made this presentation, with the following highlights:

- Actuarial Funded Ratio is now at 62.9 percent.
- Unfunded Actuarial Accrued Liability is \$7.4 billion.
- Funding Period (Closed Group Valuation): 124.6 years.
- Funding Period (Open Group Projection): 61 years.

Mr. Magid asked why there is a renewed and critical focus on pension plans when there was virtually no attention being given to them three or four years ago. Mr. Falls responded that he thought the actuarial community has been slow to react to the downward trend in the economic environment, assuming it would eventually go back up. He commented, "It's starting to set in with everybody that this is the new norm." He added that there is a rising chorus of well-funded opponents to defined benefit pension plans who are aggressively lobbying legislators and other decision-making groups to get out of these DB plans and go into defined contribution plans.

Mr. Martin noted that the average defined contribution plan participant has less than \$100,000 in their DC account.

- Changes of assumptions generated a loss of \$823 million.
 - Decreased inflation assumption from 3 percent to 2.50 percent
 - Maintained real rate of return assumption of 4.75 percent
 - Decreased nominal investment return assumption from 7.75 to 7.25 percent
 - Decreased wage inflation from 3.75 percent to 3.25 percent
 - Decreased payroll growth assumption from 3.50 percent to 3.00 percent
 - Decreased the annual assumed COLA from 2.00 percent to 1.90 percent.
- Fair market value of NMERB assets increased from \$11.532 billion to \$12.509 billion. Total contributions of \$692 million, compared to \$693 million last year.
- Return of approximately 11.8 percent in FY 2017 (net of administrative and investment expenses)
- Actuarial value is now \$12.5 billion, compared to \$11.9 billion last year.
- Actuarial return was 8.2 percent in FY 2017, compared to 6.7 percent in FY 2016.

Mr. Craig moved to accept the Actuarial Valuation Report, as presented. Mr. Magid seconded the motion, which passed unanimously by voice vote.

7. INVESTMENT REPORTS: BOB JACKSHA, CIO

a. Custody Bank Contract

[Also reporting: Alan Myers]

Mr. Jacksha said the Investment Committee voted to recommend that the board approve staff's recommendation of a two-year extension of this contract.

Mr. Myers said the NMERB's contract with State Street Bank & Trust is over at the end of this fiscal year, and staff is recommending extension for another two years. The NMERB Investment Services Procurement Policy states that the board has the option to extend the custody bank contract for two years, with no limitation on the number of times that it can be extended.

Mr. Myers said the NMERB moved its custodied assets from JP Morgan to State Street in 2014. The expectation at that time was that the NMERB would receive better service from State Street, but they have fallen short of that expectation. He said NMERB feels it can negotiate with State Street, however, on ways of improving service going forward. Mr. Myers said the reason for not recommending a change is that the NMERB's Operations section is lacking a supervisor to spearhead a transition, and staff also is not convinced that a change would substantially improve custody services received anyway.

Mr. Martin added that there are only four banks of substance that could actually serve in this capacity, and all of them are under economic pressure and are having service issues. He said it is also tremendously difficult to go through an RFP process; rather, it is more advisable to get better service from an existing vendor than to take the risk of spending a lot of time and effort trying to find someone better and ending up being disappointed in that process.

Mr. Jacksha said he did not think it was worth the extra trouble to go through a lengthy and complex RFP process, and supported staff's recommendation.

Mr. Goff moved that the Educational Retirement Board approve a two-year extension of the custody bank contract with State Street Bank & Trust Company, subject to and contingent upon New Mexico State Law and Educational Retirement Board policies. Mr. Magid seconded the motion, which passed by voice vote, with Mr. Eichenberg voting against the motion.

b. Real Estate and Real Assets Policy Revision

[Also reporting: Mark Canavan.]

Mr. Jacksha said this proposed policy revision was presented to the Investment Committee in August, and the committee recommended approval of these changes.

Mr. Canavan said these revisions are intended to replace the current Investment Policy Statements for Real Estate, Natural Resources, and Infrastructure. The proposed Investment Policy Statement (IPS) streamlines all of these into one consistent format. In addition, the separate Natural Resources and Infrastructure IPS's have been consolidated into a single Real Asset IPS.

Mr. Canavan highlighted some of the changes:

Real Estate

- The RE target exposure was updated to 7 percent from 5 percent and the policy range to 0-14 percent from 0-10 percent.
- The benchmark for the RE portfolio was properly cited, changing the "NCREIF Index" to the "NCREIF Property Index."
- The Core, Value Add and Opportunistic Property Type descriptions were expanded for "residential" investments. The residential term is eliminated and two separate categories for "multifamily" and "senior housing" were added.
- "Commercial Mortgages" was eliminated as a Risk Type category. Categories are now Core, Value Add, Opportunistic, and Public Real Estate Securities.

Real Assets

- Consolidation of the Natural Resources and Infrastructure IPS's into Real Assets IPS.
- Consolidation into a single Real Assets CPI+4% benchmark.
- Property type exposure range maximum for energy was raised from 40 percent to 50 percent to better accommodate the range of opportunities (upstream and midstream) in this investment type.
- Geography references to northern and southern hemisphere was changed to U.S. and non-U.S.

Mr. Goff moved that the Educational Retirement Board approve the changes in the policies, as presented. Mr. Magid seconded the motion, which passed unanimously by voice vote.

c. Investment Committee Report

Mr. Jacksha summarized the discussion and action at yesterday's meeting, which was held at the NMERB's offices on Pacheco Street.

Mr. Jacksha said there are certain contracts that have to be reviewed and approved by the Investment Committee for extensions or continuation, depending on their nature. The committee plans to do this on a quarterly basis going forward.

-- Recommended the Board extend the State Street custody bank contract for another two years.

-- Reviewed the PanAgora (risk parity) contract and the BlackRock Aladdin software services contract, which the NMERB uses for its fixed income portfolio. The committee approved the continuation or extension of both contracts.

-- He and Kay Chippeaux made a presentation on CLO equity. Staff may bring a secondary transaction to the Investment Committee before the end of the year.

-- Reviewed the second quarter private equity report. Since-inception return is 13 percent on a dollar-weighted basis; the one-year return is close to 17 percent.

d. Other Investment Reports

Mr. Jacksha reported that Allan Martin made a presentation at yesterday's Investments and Pensions Oversight Committee on active versus passive investing, and internal versus external investing. Several committee members complimented Mr. Martin on the clarity of his presentation.

Mr. Jacksha also noted that Ms. Goodwin made a presentation earlier in the day on Return to Work, which was very well received.

Mr. Jacksha discussed a potential change to NEPC's scope of work in light of the new diversifying assets class that NMERB has added to the portfolio.

[Break.]

[Mr. Eichenberg left the meeting.]

8. DISABILITY RETIREMENTS: RICK SCROGGINS, DEPUTY DIRECTOR

Mr. Scroggins reported 12 approved and 10 in process new disability claims, 4 approved and 12 in process periodic disability claims and 1 approved and 1 in process disability COLA claim for the period August 1 – September 30, 2017.

Mr. Goff moved for approval of the Disability Retirements report. Mr. Magid seconded the motion, which passed unanimously by voice vote.

9. AGE & SERVICE RETIREMENTS: MONICA LUJAN, DIRECTOR, MEMBER SERVICES

Ms. Lujan reported a grand total of 359 retirements for the period August 1 – September 30, 2017.

Mr. Goff moved for approval of this report, as presented. Mr. Magid seconded the motion, which passed unanimously by voice vote.

Responding to Mr. Goff, Ms. Goodwin said Rule of 75 and Age 65 & 5 retirees now make up more than 60 percent of retirees each year. These are generally second career people; and since the normal cost of the NMERB retirement benefit for each person is their age at entry, there is more cost associated with these retirees. This creates a built-in inequity because the career people are effectively subsidizing the short-term people. She said one possible way of dealing with this, which she has preliminarily discussed with the stakeholder group, is moving to a tiered multiplier. Right now the multiplier is 2.35 for everyone, and one way to offset this greater cost for the short-term people is to have a multiplier for the first ten years of 1.35, with the next ten years at 2.35, and the final ten years at 3.35. Over the 30-year service length, that would average out to 2.35, but the shorter-term people would have a lower multiplier for their service to offset their higher cost.

Ms. Goodwin said staff will be putting together a proposal for the 2019 legislative session, and this would be one way of achieving 100 percent funding in much less than the 61 years currently projected in today's actuarial valuation report.

10. DIRECTOR'S REPORT: JAN GOODWIN, EXECUTIVE DIRECTOR

a. Retiree Health Care Update

Ms. Goodwin said the NMRHCA's new executive director, David Archuleta, is doing an excellent job.

b. Agency Activities

Ms. Goodwin stated that a three-page report of agency activities was in the packet for review. She said she is very pleased that the agency is down to just three vacancies out of a workforce of 68. She said NMERB is actively recruiting for two of them and scheduling

interviews. The third vacancy, created when Alan Myers moved into a portfolio manager position, is being upgraded.

c. State Tour

Ms. Goodwin reported that the NMERB is starting its state tour to talk to the members about why changes are necessary to the benefits prospectively so the NMERB can get to 100 percent funding in much less than 61 years. The tour begins on October 30 in Farmington and winds up on December 1 in Carlsbad.

d. Other

Return to Work

Ms. Goodwin reported that she and Rod Ventura made a presentation before the Investments & Pensions Oversight Committee yesterday, talking about Return to Work (RTW). The presentation was fairly well received. Ms. Goodwin said the RTW program, which is in statute, expires at the end of 2021. Although it originally started as a means of dealing with teacher shortages in rural schools, especially math, science, ESL and special education, it has mushroomed into something well beyond that, and there are administrators in Higher Ed that are participating as well as schools all over the state.

Ms. Goodwin said she and Mr. Scroggins have done a lot of work to see if RTW really pays off financially for members. She said retirees have correctly pointed out that people are better off working longer than retiring, laying out, and then going back to work. Based on an analysis of the results, so long as someone lives to their mid-seventies, they are better off working longer; however, there is already a great deal of support in the legislature to extend RTW.

Ms. Goodwin asked the board to come up with a position on RTW so NMERB can include this in reports to committees and in testimony at the legislature. Chairwoman Cameron suggested that this topic be added to an upcoming work session agenda.

Cybersecurity

Ms. Goodwin said the NMERB should have a mechanism by which the board can discuss cybersecurity issues outside of open session as required by the Open Meetings Act. She noted that the State of California has an exception to their open meetings act that permits discussion on cybersecurity issues to take place in closed session. She said she would like to propose something like this for the State of New Mexico, and would like to add to that an exception to the Inspection of Public Records Act for cybersecurity-related documents. Because these changes would require legislative action, she said she has had a preliminary discussion with Sen. Sander Rue, who said he would be glad to sponsor such legislation.

Ms. Goodwin asked that this be added as a brief action item to the November 9 retreat agenda.

Ms. Goodwin said she has asked PERA to join the NMERB in this legislation. She added that she has sent an email to the Secretary of the Department of Information Technology, since this would apply to all state entities and all public entities within the state.

11. EXECUTIVE SESSION: 11:00 a.m.

- a. **Pending Litigation – Cooperative Educational Services v. New Mexico Educational Retirement Board and Jan Goodwin (session closed pursuant to NMSA 1978, Section 10-15-1(H)(7);**
- b. **Limited Personnel Matters – (session closed pursuant to NMSA 1978, Section 10-15-1(H)(2)) Compensation of Executive Director, Deputy Director, General Counsel and Chief Investment Officer and agency practices in regard to compensation**

Chairwoman Cameron moved that the board go into executive session pursuant to Section 10-15-1(H)(7) for purposes of discussing pending litigation, and pursuant to Section 10-15-1(H)(2) for purposes of discussing limited personnel matters. Mr. Magid seconded the motion, which passed on the following roll call vote:

For: Chairwoman Cameron; Vice Chair Goff; Secretary Magid; Mr. Craig; Dr. Duszynski.

Against: None.

12. ACTION FROM EXECUTIVE SESSION: 1:40 p.m.

Chairwoman Cameron moved that the board come out of executive session. The only items discussed during executive session were pending litigation and limited personnel matters, as set forth in the agenda. Mr. Magid seconded the motion, which passed on the following roll call vote:

For: Chairwoman Cameron; Vice Chair Goff; Secretary Magid; Mr. Craig.

Against: None.

Chairwoman Cameron asked contract attorney Patricia J. Turner to present a draft motion for the board to consider.

Ms. Turner read the following draft motion:

“The board directs contractor Canepa & Vidal P.A., Patricia J. Turner, to work with the Executive Director and other ERB staff to: (1) prepare budgetary evaluations and motions to

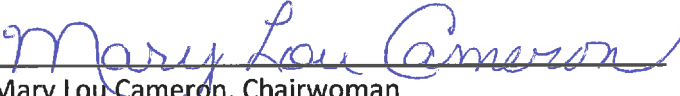
approve or reconfirm salary adjustments for the Executive Director, Mr. Scroggins, Mr. Jacksha and Mr. Ventura, as described in previous meeting minutes, and as may be amended due to budgetary considerations by the board at its December 8, 2017 meeting; and (2) to prepare options and alternatives, but not litigation, with the written documentation to effectuate the board's salary adjustment approvals as soon as possible."

Chairwoman Cameron so moved. Mr. Goff seconded the motion, which passed unanimously by voice vote.

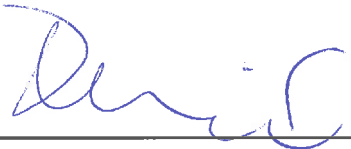
13. NEXT MEETING: FRIDAY, DECEMBER 8, 2017 -- ALBUQUERQUE

14. ADJOURN

Its business completed, the Educational Retirement Board adjourned the meeting at 1:40 p.m.


Mary Lou Cameron, Chairwoman

ATTEST:


Larry Magid, Secretary