

MINUTES OF THE
ILLINOIS STATE BOARD OF INVESTMENT
MEETING HELD
Thursday, September 15, 2016 – 12:45 P.M.

Present:

Board Members

Marc Levine
Mark Cozzi
Ezequiel Flores
Steven Powell
Shari Greco Reiches
Treasurer Michael Frerichs
Justice Mary Seminara-Schostok
Comptroller Leslie Munger

Staff

William Atwood
Genette Bacon
Christopher Brannan
Johara Farhadieh
Karen Fitts
Tondalaya Lewis-Hozier
Katherine Pantano
Scott Richards
Alise White

Guests

Bank of New York Mellon
Dan Smith, Roby Snyder, Tony
Wilkins

Burke Burns & Pinelli
Sarah Boeckman

Illinois State Treasurer's Office
Jay Rowell, Garcia Rodrigo (via
telephone)

Loop Capital
Angela Myers

Meketa Investment Group
Frank Benham, Paul Crele, Ali Wallace

Nothern Trust
Kim Evans-Cole, Tom Eichenberger,
Gary Guibert, Rick Waddell

Public Attendees
Leando Lynch

State Retirement Systems
Tim Blair

Absent:

Board Members

Senator James F. Clayborne

ROLL CALL

Chairman Levine called the meeting to order at 2:10 p.m. Mr. Brannan called the roll and noted that a quorum was present.

REPORT OF THE CHAIRMAN

Chairman Levine referred members to the proposed schedule of Board Meetings for the 2017 calendar year (Official minutes contain attachment). Discussion ensued and the members determined that the meeting on the proposed schedule for March 16, 2017 should be moved to March 17, 2017. Including the discussed change, Comptroller Munger moved to approve the schedule of meetings. Trustee Reiches seconded and the motion passed unanimously.

CONSIDERATION AND APPROVAL OF PREVIOUS MINUTES

Trustee Cozzi moved to approve the open session minutes from the June 16, 2016 and July 22, 2016 Board meetings. Trustee Reiches seconded and the motion passed unanimously. (Official minutes contain attachment.) Ms. Boeckman noted that the Board also needed to approve the closed session minutes from June 16, 2016 and July 22, 2016 and that it was her recommendation that those closed session minutes remain closed as those minutes contain confidential issues that are still pending. Trustee Cozzi moved to approve the closed session minutes from June 16, 2016 and July 22, 2016. Trustee Reiches seconded and the motion passed unanimously.

CONSIDERATION AND APPROVAL OF STANDING COMMITTEES

Ms. Farhadieh provided the report of the Investment Policy Committee from its September 15, 2016 meeting. Ms. Farhadieh read through all of the motions approved by the Investment Policy Committee (set forth below). Ms. Farhadieh told the Board she had discussed with T. Rowe Price the impact on record-keeping fees if potentially replacing T Rowe Price as target date manager with Vanguard. T Rowe Price communicated that they would begin charging for loans and early distributions. Ms. Farhadieh pointed out that the amount of those fees was expected to be less than 20% of the fee savings of switching the target date manager to Vanguard as the Investment Policy Committee had recommended. Treasurer Frerichs asked how the changes to the deferred compensation investment options would impact MWDBE managers. Ms. Farhadieh stated that the changes would decrease assets under management by MWDBE managers in the deferred compensation plan by \$120 million. Trustee Munger moved to approve and ratify all actions taken by the Investment Policy Committee. Trustee Reiches seconded. The motion passed 7-1. Treasurer Frerichs noted that he voted no due to the impact on MWDBE managers.

Defined Benefit Plan Investments

1. The recommendation from ISBI Staff and Hamilton Lane regarding the investment of \$50 million dollars in Platinum Equity Capital Partners IV, L.P., subject to legal review and successful contract negotiations.
2. The recommendation from ISBI Staff and Courtland regarding the investment of \$50 million dollars in Harrison Street Real Estate Partners VI, L.P., subject to legal review and successful contract negotiations.

Defined Benefit Plan Manger Terminations

1. The recommendation of ISBI Staff and Meketa to terminate Lombardia's Non-US Large Cap Equity strategy and transition the assets to Ariel's International Equity portfolio.
2. The recommendation from Meketa and Investment Staff to terminate Decatur's Large Cap Equity portfolio and transition the assets to S&P 500.

Changes to the Deferred Compensation Plan Investment Options

1. The recommendation of Meketa and ISBI Staff, to eliminate the *Active Large Cap Value* asset class allocation, and consequentially, terminate *LSV Value Equity* and map the applicable assets to *Vanguard Institutional Index*.
2. The recommendation of Meketa and ISBI Staff, to eliminate the *Passive Mid Cap Core* asset class allocation, and consequentially, terminate *Northern Trust S&P 400* and map the applicable assets to *Northern Trust Russell 2000*.
3. The recommendation of Meketa and ISBI Staff, to eliminate the *Active SMID-Cap Value* asset class allocation, and consequentially, terminate Ariel Investments and map the applicable assets to *Northern Trust Russell 2000*.
4. The recommendation of Meketa and ISBI Staff, to eliminate the *Active Small Cap Growth* asset class allocation, and consequentially, terminate Franklin Templeton and map the applicable assets to *Northern Trust Russell 2000*.
5. The recommendation of Meketa and ISBI Staff, to eliminate the *Active Non US Large Cap Growth* asset class allocation, and consequentially, terminate *INVESCO International Growth* and map the applicable assets to *Northern Trust MSCI ACWI ex. US index*.
6. The recommendation of Meketa and ISBI Staff, to eliminate the *Active Non US Small Cap Growth* asset class allocation, and consequentially, terminate *William Blair International Small Cap Growth* and map the applicable assets to *Northern Trust MSCI ACWI ex. US index*.
7. The recommendation of Meketa and ISBI Staff, to eliminate the *Active US Balanced* asset class allocation, and consequentially, terminate *Fidelity Puritan* and map the applicable assets to a similar target date fund.
8. The recommendation of Meketa and ISBI Staff, to eliminate the *Active Core Fixed Income* asset class allocation, and consequentially, terminate *T Rowe Price Bond Trust* and map the applicable assets to *Vanguard Total Bond Market Index*.
9. The recommendation of ISBI Staff and Meketa to select The Vanguard Group as the Target Date Fund provider for the DC Plan.

Justice Schostok provided the report of the Audit and Compliance Committee meeting from its September 15, 2016 meeting. Trustee Powell moved to adopt and ratify the report from the Audit and Compliance Committee as presented by Justice Schostok. Treasurer Frerichs seconded and the motion passed unanimously.

Mr. Brannan provided the report of the Executive Committee meeting from its August 11, 2016 meeting. Trustee Reiches moved to adopt and ratify the report from the Executive Committee as presented by Mr. Brannan. Chairman Levine seconded and the motion passed unanimously.

PRESENTATIONS BY DEFINED BENEFIT AND DEFERRED COMPENSATION CUSTODIAN RFP FINALISTS:

Mr. Atwood provided background on the searches conducted for custodians for both the DB Plan and DC Plan. He noted that Ms. Farhadieh lead the search for the DC Plan custodian, while Ms. White lead the search for the DB Plan custodian.

Chairman Levine moved to go into Executive Session pursuant to Section 2(c)(7) of the Open Meetings Act to discuss investment contracts with the DB Plan and DC Plan custodian finalists. Trustee Cozzi seconded and the motion was called to a Roll Call vote. All in favor were: Trustees Cozzi, Powell, Reiches, Flores, Treasurer Frerichs, Chairman Levine, Justice Schostok and Comptroller Munger. The motion passed unanimously.

Guests and Staff were excused from the meeting with the exception of Director Atwood, Ms. Farhadieh, Mr. Brannan, Ms. Boeckman, Ms. White, Mr. Richards, and Meketa representatives.

Trustee Cozzi moved to return to the open meeting. Justice Schostok seconded and the motion passed unanimously.

Northern Trust

After returning to the open meeting, representatives from Northern Trust, including Chairman and Chief Executive Officer Rick Waddel, were invited to join the meeting. Northern Trust representatives referred Members to their presentation. (Official Minutes contain attachment). Northern Trust representatives discussed the firm's custodian services capabilities, experience, investments in technology, as well as the firm's headquartered history and presence in Chicago and commitment to diversity. The Board Members thanked the Northern Trust representatives for their presentation.

Comptroller Munger exited the meeting.

Trustee Cozzi moved pursuant to Section 7(a) of the Open Meetings Act to allow Comptroller Munger to participate in the meeting via telephone due to her absence as a result of matters relating to her employment. Trustee Reiches seconded and the motion passed unanimously.

Bank of New York Mellon

Representatives from Bank of New York Mellon ("BONY") were invited to join the meeting. BONY representatives referred Members to their presentation. (Official Minutes contain

attachment). BONY representatives discussed the firm's experience with public fund clients, recently obtained clients (including Chicago Teachers), its developed technology and solutions, as well as its presence in Illinois. The Board Members thanked the BONY representatives for their presentation.

Trustee Cozzi moved to go into Executive Session pursuant to Section 2(c)(7) of the Open Meetings Act to discuss investment contracts with the DB Plan and DC Plan custodians. Justice Schostok seconded and the motion was called to a Roll Call vote. All in favor were: Trustees Cozzi, Powell, Reiches, Flores, Treasurer Frerichs, Chairman Levine, Justice Schostok and Comptroller Munger. The motion passed unanimously.

Guests and Staff were excused from the meeting with the exception of Director Atwood, Ms. Farhadieh, Mr. Brannan, Ms. Boeckman, Ms. White, Mr. Richards, and Meketa representatives.

Trustee Cozzi moved to return to the open meeting. Justice Schostok seconded and the motion passed unanimously.

After returning to the open meeting, Justice Schostok moved, consistent with the recommendation of Meketa and Staff to retain Northern Trust as custodian for the DC Plan. Trustee Powell seconded and the motion passed unanimously.

Trustee Powell moved to select Northern Trust as custodian for the DB Plan. Trustee Cozzi seconded and the motion was called to a Roll Call vote. All in favor were: Trustee Cozzi, Trustee Flores, Treasurer Frerichs, Comptroller Munger, Trustee Powell, Trustee Reiches, and Chairman Levine. Justice Schostok opposed the motion. The motion passed 7-1.

REPORT OF THE DEPUTY EXECUTIVE DIRECTOR-INVESTMENTS

Ms. Farhadieh referred the Board Members to their presentation materials, "DC Communication Timeline re Participant Fee." (Official Minutes contain attachment.). Ms. Farhadieh discussed various future communications to DC Plan participants regarding updates to participant fees.

REPORT OF THE DIRECTOR OF OPERATIONS, ACCOUNTING AND AUDIT

Ms. White referred Members to their presentation materials, "Actual vs. Projected Budget Forecast as of 06/30/2016." (Official Minutes contain attachment). Ms. White discussed how the expenditures for the fiscal year ended 06/30/2016 were under the budgeted amount. Ms. White stated that she does not foresee a material change in expenditures for the coming year. Chairman Levine thanked Ms. White for her hard work on the DB Plan custodian search process.

REPORT OF THE EXECUTIVE DIRECTOR

Mr. Atwood asked Chairman Levine that the Consideration and Approval of the Remote Work Policy be removed from the meeting agenda. Chairman Levine granted Mr. Atwood's request. Mr. Atwood referred members to their presentation materials, "Merit Compensation Policy" (Official Minutes contain attachment.) Mr. Atwood summarized the policy as drafted would provide merit compensation up to a percentage previously approved by the Board to certain members of ISBI Staff based on annual supervisor evaluations. Discussion ensued amongst the members. Trustee Cozzi asked whether the Board would approve each individual merit

compensation payment. Justice Schostok noted additional fiduciary considerations if the Board became involved in specific Staff member compensation decisions. Comptroller Munger noted that merit compensation builds compensation without a pensionable basis but emphasizes the importance of performance evaluations. Trustee Powell stated a concern that standards could loosen for paying merit compensation down the road and would like that each payment to be disclosed to the Board. Mr. Brannan stated that he would update the policy to clarify that the Executive Director would disclose all merit compensation payments to the Board, and that all payments made over a certain percentage of an individual's salary would require Board approval. No motion was made to approve the Merit Compensation Policy, with an updated draft to be presented at the next Board Meeting.

Mr. Atwood referred members to their presentation materials, "Illinois State Board of Investment Pension Fund Asset Allocation Review and Risk Analysis." (Official Minutes contain attachment.) Mr. Atwood discussed how the State Employees Retirement System and the Judges Retirement System each decreased their return assumptions from 7.25% to 7.0% and from 7.0% to 6.75%, respectively. The presentation materials prepared by Meketa showed minor proposed adjustments to the asset allocation in order to keep the same probability of achieving the return assumptions, or how leaving the asset allocation at its current status would yield a slightly increased probability in achieving the return assumptions.

Mr. Atwood pointed out that Meketa was recommending the creation of a 4% Opportunistic Debt allocation because investments were being made in that asset class across the portfolio and having a dedicated category was appropriate. Chairman Levine pointed out that such investments were being made in real estate, private equity and hedge funds and he believed this change would improve transparency. Chairman Levine pointed out that the 4% was being offset by 1% reductions to private equity, real estate, high yield/bank loans and emerging market debt, all categories that have or may have overlap with opportunistic debt. Justice Schostok moved to adopt the proposed updated asset allocation as recommended by Meketa. Chairman Levine seconded and the motion passed unanimously.

Mr. Atwood then asked that the Board authorize the Executive Director with the help of Staff to conduct a search for a communications adviser to assist with media communications as well as communications to DC Plan participants. Trustee Powell made a motion to authorize Mr. Atwood to conduct a search for a communications adviser. Trustee Reiches seconded and the motion passed unanimously.

REPORT OF THE GENERAL COUNSEL

Mr. Brannan discussed various items that the Staff will be working on in the coming months, including a reformatted Investment Policy, a Statement of Powers Reserved outlining the scope of the Board's exclusive authority, and a Vendor Contact Policy to provide the Board Members a consistent procedure and practice when interacting with current and prospective vendors.

REPORT OF FIDUCIARY COUNSEL

Ms. Boeckman discussed recent developments regarding the Illinois Freedom of Information Act and its application to Board matters. Ms. Boeckman noted that private communications discussing ISBI business may be information subject to FOIA disclosure.

NEW BUSINESS/OLD BUSINESS

None.

PUBLIC COMMENT

None.

NEXT MEETING AND ADJOURMENT

Chairman Levine stated that the next meeting of the Board would be scheduled for December 15 at 1:00 P.M., official notices to be distributed at a later date. At 4:43 p.m., there being no further business to come before the Committee, Trustee Powell moved to adjourn the meeting. Trustee Cozzi seconded and the meeting was adjourned.

Respectfully submitted,

William Atwood, Executive Director