

Minutes of the TCRS Board of Trustees meeting on December 16, 2013

The Board of Trustees of the Tennessee Consolidated Retirement System met on Monday, December 16, 2013 at 9:00 a.m. The meeting was held in Room 30 of the Legislative Plaza with Chairman David Lillard presiding.

Chairman Lillard asked Ms. Bachus to conduct an attendance roll call. The following members were present: Chairman David Lillard, State Treasurer; Mr. Tre Hargett, Secretary of State; Comptroller to the Treasury, Justin Wilson; Commissioner Rebecca Hunter, Department of Human Resources; Ms. Jill Bachus, Director of TCRS; Mr. Michael Barker, Ms. Patsy Moore, Mr. Bill Kemp, Mr. Ken Wilber, Mr. Harold Morrison, Mr. Kevin Fielden, Ms. Angie Judish, Mr. Gill Kendrick, Mr. Alfred Laney, and Mr. Bob Wormsley.

Approval of the September 27, 2013 Minutes of the Board of Trustees

On a motion by Comptroller Wilson and seconded by Commissioner Hunter, the minutes of the September 27, 2013 TCRS Board of Trustees meeting were unanimously approved.

Board of Trustees Committee Reports

Chairman Lillard mentioned the audit committee will meet immediately after the Board meeting for an information only meeting. Chairman Lillard briefly discussed a press release concerning an ongoing investigation with TBI about a former Treasury employee.

Chairman Lillard recognized Ms. Bachus to provide the administrative committee report. Ms. Bachus mentioned Mr. Fred Marshall provided the committee with an update on Concord. Ms. Bachus indicated the go-live date for Phase 6 is scheduled for April 2014.

Chairman Lillard reviewed the investment committee report. The investment committee considered and approved two strategic lending activities. Mr. Brakebill gave a report on assets and fund performance.

Investment Report

Mr. Brakebill began by reviewing the performance of the portfolio for the quarter ended September 30, 2013. Referencing information included in the Strategic Investment Solutions, Inc. report, he commented that the fund had ended the quarter with assets of \$38.8 billion, up from \$37.5 billion at the end of June 30, 2013. He also pointed out the significant recovery from the depths of the financial crisis when assets had fallen to \$22-\$23 billion. Mr. Brakebill noted that private equity investments continue to grow, totaling \$315 million during the quarter, up from \$273.1 million last quarter. He also noted that TCRS is now making strategic lending investments, which totaled \$150.8 million at the end of September, up from zero at June 30th. Finally, he pointed out that international emerging market investments totaled \$1.56 billion at the end of September, up from \$1.46 billion at the end of June. He indicated that private equity and strategic lending should continue to grow in the coming quarters as new investments are made

Mr. Brakebill informed the Board that the TCRS portfolio had returned 8.96% for the 12 months ended September 30, 2013. On a 3-year and 5-year, the fund returned 10.23% and 7.79%, respectively. Mr. Brakebill noted that the portfolio's 10-year return was 6.39% despite the impact of the financial crisis.

Mr. Brakebill pointed out that the fund's U.S. equity portfolio has risen 19.43% year over year, but had trailed its benchmark slightly. He also noted that the fund's international developed equity portfolio had added considerable value, increasing 25.4% year over year and slightly exceeding its benchmark. While equities had a banner year, fixed income had sold off. He mentioned that the fixed income portfolio, which had a longer duration, lost 3.5% but had exceeded its benchmark by 1.5%. He indicated that the real estate portfolio had generated decent returns on a 1-year (+10.16%) and 3-year (+11.73%) basis while 5-year returns were more tepid (+0.95%). Mr. Brakebill mentioned that the fund's private equity portfolio had done better than expected in spite of expected negative "j-curve" performance.

Mr. Brakebill next moved the discussion to key initiatives. He mentioned that the group had moved into its new office space without disruptions, that alternative asset allocation changes had been implemented, that specialty lending legal documents are almost complete, and that private equity and real estate due diligence has been active. Mr. Brakebill noted that 24 transaction specific investments are in process since the start of the fiscal year and have required a lot of time from the department staff, the Investment Committee, legal and the Treasurer. Mr. Brakebill pointed out that three to four transactions are in the closing process today.

Mr. Brakebill noted that tactical allocation during the quarter was relatively neutral as asset allocation changes are underway. He commented that an investment policy amendment had been made and that there will likely be more policy changes and updates in 2014. Mr. Brakebill mentioned that TCRS was close to hiring a new Director of Private Equity and that Daniel Crews continues to act as Interim Director. He also commented that an executive search was underway for a new Director of Real Estate and the department is in early stages of the interview process. He indicated that he expected formal interviews to begin in January.

Mr. Brakebill indicated that he is as confused as anyone about the rise in the markets. Earnings are up only 4-5%, so the rise in stock prices has been mostly valuation driven. There is a lot of momentum heading into the end of the year with lots of questions about the outlook for 2014. The Fed's strategy related to the taper remains a key concern and that there has been a lot of discussion about that.

Real Estate Advisors

Mr. Brakebill described that TCRS uses Real Estate Advisors to source deals and that the department will have the choice on whether to move ahead with those deals or not. TCRS has relied on its real estate consultant, The Townsend Group ("Townsend"), to identify and vet potential advisors. Townsend sent out questionnaires to 34 potential advisors, which the department narrowed down to seven, ranking each one. Mr. Brakebill did note that TCRS already has a separate relationship with five of these advisors. At the end of the vetting process, the department had decided to hire all seven, subject to approval by the Board of Trustees.

Treasurer Lillard asked if there was a motion to approve the selected Real Estate Advisors. Mr. Kemp made a motion, and Mr. Wormsley seconded the motion. A roll call was taken, and the motion was unanimously approved.

Investment Policy

Mr. Brakebill mentioned that there are certain technical cleanups that the department is looking to make to the Investment Policy. One such issue involves exchange traded funds (ETFs). Mr. Brakebill described an ETF and how it differs from stocks and mutual funds. He mentioned that the policy change in question clarifies the issue around ownership limits of ETFs.

Treasurer Lillard mentioned that ETFs had not been invented when the Investment Policy was created. He then pointed out that, based on how ETFs differ from stocks, that ETFs should not be subject to the 5% holding limitation. Treasurer Lillard said changes like this are an evolving process for TCRS.

Treasurer Lillard asked if there was a motion to approve to the amendment to the Investment Policy. Mr. Wormsley made a motion to approve, which was seconded by Mr. Laney and Mr. Hargett. A roll call was taken, and the motion was unanimously approved. Treasurer Lillard thanked Mr. Brakebill for his presentation.

Actuarial Valuation

Chairman Lillard introduced Mr. Justin Thacker from Bryan, Pendleton, Swats, and McAllister to review the actuarial valuation. Mr. Thacker noted the purpose of the valuation is to determine employer contribution rates and to examine the financial health of the plan. Next, Mr. Thacker presented highlights of the actuarial valuation.

As determined by the July 1, 2013 actuarial valuation the contribution rate for teachers will be 9.04%, the rate for state employees will be 15.14%, and for state judges and attorneys general the rate will be 22.87%. The hybrid benefit plan goes into effect July 1, 2014.

On a motion by Mr. Barker and seconded by Commissioner Hunter, the Board unanimously approved the new contribution rates for teachers, state employees, and state judges and attorneys general. This motion also included providing staff with the authority to adjust the amortization period used in calculating employer rates for political subdivisions not to exceed 30 years.

Adjournment

Chairman Lillard announced the completion of the business at hand and asked if there was any other business to come before the Board.

On a motion by Mr. Laney and seconded by Mr. Barker, the Board unanimously approved the TCRS Board of Trustees meeting be adjourned.

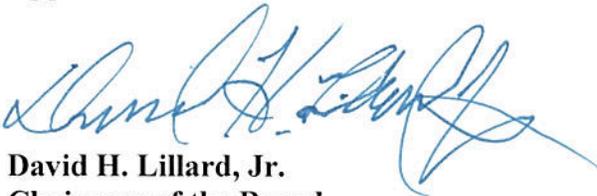
With no other business, the Board of Trustees adjourned at 10:20 a.m. on December 16, 2013.

Respectfully Submitted,



**Jill Bachus
Director, TCRS**

Approved:



**David H. Lillard, Jr.
Chairman of the Board**