

**ARLINGTON COUNTY VIRGINIA  
EMPLOYEES' RETIREMENT SYSTEM**

**Board of Trustees Meeting Minutes  
July 14, 2016**

The President of the Board, Mr. Peter Maier, called the meeting to order at 8:00 AM, in Conference Room 511C at 2100 Clarendon Boulevard.

Voting Members Present:            Mr. Peter Maier, President  
   Ms. Sandy DeGray, Secretary  
   Ms. Michelle Cowan, Treasurer  
   Mr. Michael Brunner  
   Mr. Jon Kinney

Voting Members Absent:            Mr. Richard Alt, Vice President  
   Mr. Ken Dennis

Substitute Member Present:        Mr. Jimmie Barrett, Asst. Treasurer  
   Mr. Alex Iams (arrived 9 AM)  
   Mr. Wayne Rhodes

Various Times:                        Mr. Daniel Zito, Executive Director  
   Ms. Randee Stenroos, Assistant Director  
   Ms. Katrina Milne, Investment Analyst  
   Ms. Susan Bomberg, Accountant  
   Mr. Garry Musto, ACG  
   Mr. Seth Yablonovitz, ACG  
   Mr. Shawn Driscoll, T. Rowe Price  
   Mr. Brian Dausch, T. Rowe Price  
   Mr. Brad Meeker, T. Rowe Price  
   Mr. Eric Conklin, Harvest  
   Mr. Anthony Merhige, Harvest  
   Mr. Jim McGovern, Franklin Park  
   Mr. Karl Hartmann, Franklin Park  
   Mr. Matthew Castaldo, Franklin Park

**CONSENT LIST**

A motion to approve the consent list, consisting of the June 2, 2016 meeting minutes, the cancellation of the August meeting and the rescheduling of the September meeting from 9/1/16 to 9/8/16, was made by Mr. Brunner and seconded by Mr. Barrett. The motion passed by a vote of 7-0.

## T. ROWE PRICE NATURAL RESOURCES REVIEW

Messrs. Driscoll, Dausch and Meeker reviewed ACERS' \$27.2 million investment in the New Era Fund, a mutual fund with the same objectives as the ACERS' former separately managed account in the T. Rowe Price Natural Resources strategy. The following summarizes the linked performance as of May 31, 2016.

(%)	Performance	Benchmark
1 Year	-7.2	-10.4
3 Year	-1.4	-5.1
5 Year	-2.9	-6.5
Since Inception (3/04)	7.4	5.8

Mr. Driscoll noted that the market environment for natural resources continues to be challenging with commodities, by his estimation, about six years into a bear market that could extend up to 20 years. Mr. Driscoll believes oil prices could drop into the teens and that renewable energy technology is maturing rapidly, presenting further challenges to fossil fuels along with potential investment opportunities. He noted that US specialty chemicals benefit from low energy prices and are a significant overweight in the strategy.

## HARVEST FUND ADVISORS

Messrs. Conklin and Merhige updated the Board on ACERS' \$76 million investment in Harvest. The following summarizes Harvest's net performance as of June 30, 2016.

(%)	Performance	Benchmark
Quarter	20.3	19.7
YTD	13.1	14.7
Since Inception (1/15)	-15.4	-15.9

Despite the absolute negative returns since inception, and the underperformance year-to-date, Mr. Conklin remains optimistic on the MLP space over the long term. Discussing the recent increased correlation between the investment performance of MLPs and the price of oil, Mr. Conklin noted that MLPs are essentially utilities specializing in moving natural gas, oil and other liquids at contracted rates with a volume driven business model that is independent of the price of oil. He stressed that MLP cash flows have remained robust over the last couple of years and that with global interest rates remaining low, he predicted MLP assets will be re-priced higher over time to reflect the stability of their cash flows.

## STRESS TEST AND ALLOCATION RECOMMENDATION

Mr. Yablonovitz continued the discussion of the market outlook and stress test analysis from the April and June 2016 Board meetings. He noted that ACERS' significant equity

overweight and corresponding fixed income underweight, particularly in investment grade securities, has benefited the fund over the past 8 years. However, based on the firm's current view and capital markets' assumptions, he recommended ACERS should consider trimming the fund's risk.

Accordingly, three allocation options were presented for consideration, all of which yielded similar portfolio impacts in terms of expected risk, return and efficiency. The options included:

Option 1:

<b>Sources:</b>		<b>Uses:</b>	
<u>Mandate</u>	<u>\$m</u>	<u>Mandate</u>	<u>\$m</u>
Loomis Sayles	\$60	NTGI AGG Bond	\$150
Thornburg	\$20		
TRP Floating Rate	\$20		
Brahman	\$25.4		
Rutabaga	\$10		
Kiltearn	\$14.6		

Option 2a:

<b>Sources:</b>		<b>Uses:</b>	
<u>Mandate</u>	<u>\$m</u>	<u>Mandate</u>	<u>\$m</u>
Loomis Sayles	\$60	NTGI AGG Bond	\$150
Thornburg	\$20	Vanguard S&P 500	\$73.3
TRP Floating Rate	\$20		
Brahman	\$25.4		
Rutabaga	\$52.9		
Kiltearn	\$25		
TRP New Era	\$20		

Option 2b:

<b>Sources:</b>		<b>Uses:</b>	
<u>Mandate</u>	<u>\$m</u>	<u>Mandate</u>	<u>\$m</u>
Loomis Sayles	\$60	NTGI AGG Bond	\$150
Thornburg	\$20	Vanguard S&P 500	\$47.3
TRP Floating Rate	\$20		
Rutabaga	\$52.9		
Kiltearn	\$25		
TRP New Era	\$20		

Ashford stated its preferred option was 2b, while Staff favored 2a.

Mr. Brunner made a motion to authorize staff to take the actions necessary to implement option 2a above. Mr. Kinney made a friendly amendment to split the sources and uses portions of the transaction. The maker agreed and Mr. Kinney seconded the

motion. A discussion of the sizing of the Loomis and TRP New Era reductions ensued. The motion failed by a vote 1-2, with Messrs. Maier and Kinney dissenting and Ms. DeGray, Ms. Cowan, Messrs. Barrett and Rhodes abstaining.

Ms. Cowan, seconded by Mr. Brunner, made a motion to authorize staff to take the actions necessary to implement the sources outlined in option 2a above. The motion failed with a vote of 2-2, with Messrs. Maier and Kinney dissenting and Ms. DeGray, Messrs. Barrett and Rhodes abstaining.

Mr. Kinney then made a motion, seconded by Mr. Rhodes, to authorize staff to take the actions necessary to implement the following reductions:

**Sources:**

<u>Mandate</u>	<u>\$m</u>
Loomis Sayles	\$45
Thornburg	\$35
TRP Floating Rate	\$20
Brahman	Pending ACG recommendation by 7/27/16 or otherwise terminate the mandate
Rutabaga	\$53
Kiltearn	\$25
TRP New Era	\$10

The motion failed with a vote of 3-4, with Mr. Brunner, Mr. Maier, Ms. DeGray and Ms. Cowan dissenting.

Mr. Maier, seconded by Ms. Cowan, made a motion to authorize staff to take the actions necessary to implement option 2a with the following changes: lowering the Loomis Sayles reduction to \$53 million and terminating the TRP New Era mandate. Mr. Kinney made a friendly amendment to split the original motion into two, one regarding fixed income and the other equity. Mr. Maier accepted this as a new motion, which was seconded by Mr. Brunner. After discussion, the following fixed income reduction was proposed:

**Sources:**

<u>Mandate:</u>	<u>\$m</u>
Loomis Sayles	\$53
Thornburg	\$20
TRP Floating Rate	\$20

The motion passed unanimously by a vote of 7-0.

Next, Mr. Maier, seconded by Ms. Cowan, made a motion to authorize staff to take the actions necessary to terminate T. Rowe New Era mandate and implement the remainder of the equity reductions as included in option 2a above equity. The motion passed 5-2, with Ms. Cowan and Mr. Kinney dissenting.

Mr. Rhodes, seconded by Mr. Brunner, made a motion to authorize staff to take the actions necessary to implement the uses of option 2a above as presented. This motion passed by a vote of 5-2, with Mr. Kinney and Mr. Maier dissenting.

The following chart summarizes the final reallocation as authorized by the Board:

<b>Sources:</b>		<b>Uses:</b>	
<u>Mandate</u>	<u>\$m</u>	<u>Mandate</u>	<u>\$m</u>
Loomis Sayles	\$53	NTGI AGG Bond	\$150
Thornburg	\$20	Vanguard S&P 500	\$73
TRP Floating Rate	\$20		
Brahman-Terminate	\$25		
Rutabaga-Terminate	\$53		
Kiltearn	\$25		
TRP NRIS-Terminate	\$27		

Note: Amounts are rounded; actual allocation to uses will be prorated amount of market values of sources at time of redemption

## **PRIVATE EQUITY FUNNEL AND FEE STRUCTURES**

Mr. Castaldo reviewed Franklin Park's five stage investment activity funnel and highlighted the number of funds reviewed since the firm was retained in March 2013. Mr. McGovern noted that early performance for ACERS' private investment portfolio is outperforming the corresponding S&P 500 Total Return Public Market Equivalent.

Mr. Hartmann discussed the fee structures and mechanics of private equity in detail including management, transaction and monitoring fees, offsets, claw backs and carried interest. Example calculations were presented. Franklin Park's process for monitoring private equity fees was also discussed.

## **KEY INITIATIVES UPDATE/OTHER BUSINESS**

Staff:

- Recommended a change to language concerning alternative investments and liquidity in the Investment Policy Statement (IPS), specifically to define illiquid investments as those without full redemption rights on a maximum 45 business days' notice, up from 31 days. This change will be included on the consent list for September.
- Noted the inclusion of a new manger summary reports, developed by Katrina Milne, in the Board package. Trustees liked the report and asked that minutes from the managers' prior visits be included in future versions.
- Recommended adding Able Noser to the stable of transition managers to execute complex deals, noting that fees are event based only. Mr. Maier, seconded by Mr. Barrett, made a motion to authorize staff to negotiate and execute a transition management agreement, subject to acceptable legal review, with Able Noser. The motion passed with a vote of 6-0, with Ms. Cowan absent.
- Discussed a recent visit to Los Angeles to visit current manager Focused and two private equity firms of interest.

- Updated the Board on the status of the Arsenal investment, noting that Arsenal will most likely request an extension when the term expires in August 2016; this would require Board approval.
- Noted Ashford did a training session on July 13 concerning valuation techniques in general and how they are employed by ACERS' active managers.

**CLOSED SESSION**

A motion was offered by Mr. Maier, seconded by Mr. Brunner, and passed 6-0 with Ms. Cowan not present, to enter into closed session for discussion, consideration or interviews of prospective candidates for employment; assignment, appointment, promotion, performance, demotion, salaries, disciplining or resignation of specific public offices, appointees or employees of any public body pursuant to Virginia Code §2.2-3711 (A)(1) and for discussion or consideration of medical and mental health records excluded from this chapter pursuant to subdivision 1 of §2.2-3705.5. The closed session began at 11:33 AM.

The Board returned to open session at 11:40 AM. On a motion by Mr. Maier, seconded by Mr. Barrett, and carried by a vote of 6-0, the voting recorded as follows:

<u>Member</u>	<u>Vote</u>
Mr. Barrett	Aye
Mr. Brunner	Aye
Ms. DeGray	Aye
Mr. Kinney	Aye
Mr. Maier	Aye
Mr. Rhodes	Aye

The Board certified that only public matters lawfully exempted from open meeting requirement by Virginia law and identified in the motion convening the closed session were heard, discussed or considered by the Board.

After the Board reentered open session, a motion was offered by Mr. Maier, seconded by Ms. DeGray, to set the Executive Director's FY2017 salary at \$225,000. The motion passed by a vote of 6-0 with Ms. Cowan absent.

**INVESTMENT RELATED**

- A. Fund Balance Report (May)
- B. June 1, 2016 Training Session Minutes

**ADMINISTRATIVE ITEMS**

- A. Inventory Listing
- B. Calendar of Events

## **ADJOURNED**

Mr. Brunner, seconded by Mr. Barrett, offered a motion to adjourn the meeting. The motion passed with a vote of 6-0, with Ms. Cowan not present. There being no further business, the meeting adjourned at 11:45 AM.

Respectfully submitted,  
Susan Bomberg