ARLINGTON COUNTY VIRGINIA
EMPLOYEES' RETIREMENT SYSTEM

Board of Trustees Meeting Minutes
December 1, 2016

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

Voting Members Present:	Mr. Jon Kinney, President Mr. Richard Alt, Vice President Mr. Ken Dennis, Secretary (arrived 8:05 AM) Ms. Michelle Cowan, Treasurer (departed early)
Voting Members Absent:	Mr. Michael Brunner Ms. Sandy DeGray Mr. Peter Maier
Substitute Member Present:	Mr. Jimmie Barrett, Asst. Treasurer Mr. Alex Iams (arrived 8:03 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. Rob Gooderham, ACG Mr. Garry Musto, ACG Mr. Paul Massaro, T. Rowe Price Mr. Brad Meeker, T. Rowe Price Mr. Steven Finamore, T. Rowe Price Mr. Jason Ostroski, Clifton Larson Allen Mr. Brian Kiernan, Clifton Larson Allen Ms. Sara Teyema, Board Member Elect

CONSENT LIST

A motion to approve the consent list, consisting of the November 3, 2016 meeting minutes and Appreciation Resolutions for four Board members, was made by Mr. Barrett and seconded by Mr. Alt. The motion passed by a vote of 4-0, with Ms. DeGray, Messrs. Brunner and Maier absent, and Messrs. Dennis and Iams not yet present.

INTEREST RATE ON MEMBER CONTRIBUTIONS

A motion to set the crediting interest rate on member contribution account balances for 2016 at 0.908%, pursuant to Board policy, was offered by Mr. Barrett and seconded by Mr. Alt. The motion passed with a vote of 4-0, with Ms. DeGray, Messrs. Brunner and Maier absent, and Messrs. Dennis and Iams not yet present.

T. ROWE PRICE FLOATING RATE FUND REVIEW

As of October 31, 2016, annualized net investment returns of 4.0% since ACERS' initial investment (3/4/11) lagged the benchmark by 0.3%. A portion of the underperformance since inception is explained by the fund offering liquid access to a less liquid asset class with less volatility than the benchmark. Another reason is that the strategy has a more conservative exposure to credit than the benchmark. The strategy ranks in the first decile of its peer group since ACERS' original investment.

While Mr. Massaro acknowledged a substantial amount of uncertainty due to impending change in administrations, he noted that anticipated rising interest rates benefit the coupon rates on floating rate instruments in general. Sectors of concern include healthcare with expected changes to the Affordable Care Act and pressure on drug pricing as well as metals and mining while increased investment in infrastructure may provide an area of opportunity.

The Board discussed the merits of maintaining exposure to the strategy in light of the anticipated investment environment.

FY 2016 AUDIT FINDINGS AND CAFR SUBMISSION

Mr. Ostroski presented Clifton Larson Allen's report on the audit of ACERS' financial statement for the fiscal year ended June 30, 2016. Clifton Larson Allen issued an unmodified opinion that the financial statements are presented fairly, in all material respects, and in conformity with U.S. Generally Accepted Accounting Principles. He also noted that management was very cooperative and professional during the audit process.

Mr. Kiernan discussed financial highlights of fiscal year 2016, focusing on the new disclosures required by GASB Standard No. 72, Fair Value Measurement and Application.

Staff left the room and the Board had further discussions with Messrs. Ostraski and Kiernan. Upon staff's return, a motion was offered by Ms. Cowan and seconded by Mr. Dennis to approve the 2016 Comprehensive Annual Financial Report (CAFR) as submitted. This motion passed unanimously by a vote of 5-0, with Messrs. Brunner and Maier absent.

QUARTERLY INVESTMENT PERFORMANCE REVIEW

Mr. Gooderham reviewed the fund's performance for the quarter ended September 30, 2016. Fund returns for various time periods were:

(%)	Quarter	1 Year	5 Years	10 Years
Total Fund (Gross)	3.9	11.1	10.0	6.3
Total Fund (Net) *	3.8	10.8	9.7	5.9
Policy Benchmark**	3.3	10.2	9.1	5.6
CPI + 3.5% Annualized	0.9	4.8	4.6	5.1

** Gross returns adjusted downwards for current annual fee rate per annual fee review and analysis, assuming all fees deducted quarterly.*
***Effective 10/1/07: 40% Ru3000, 17.5% MSCI ACWI ex-US, 39% BC Universal, 1.5% Barclays TIPS, 2% T-Bills*

Net performance for the quarter and year outperformed the benchmark by 0.5% and 0.6%, respectively. Strong market returns during the quarter was attributable to a continuance of June 2016's end of month rally in global equities following heightened volatility resulting from the Brexit referendum. The year's net outperformance is primarily attributable to overweight allocations to domestic equity and to credit within fixed income.

Relative to the TUCS universe of public plans, ACERS' performance was in the 18th, 41st and 23rd percentile on a one, five and ten-year basis, respectively. Ashford estimates the fund's diversified risk level at September 30, 2016 was 59, a decrease of 4 risk points versus June 30, 2016, primarily driven by the implementation of the risk reducing reallocation approved in July 2016. This compares to Ashford's estimated benchmark risk of 54 and the top of the policy risk band at 65.

LARGE CAP VALUE ANALYSIS & OPTIONS

Ashford Consulting presented an analysis on Focused Investors in response to a trustee request from the prior meeting.

The rationale for hiring Focused in November 2010 as a large-cap, high quality equity manager was reviewed. After analysis, Ashford concluded that hiring Focused was a good decision as: 1) the firm has executed their strategy and performed in line with expectations given market conditions and 2) has produced a $13 million gain versus initial funding sources as of 9/30/16. While performance has lagged over the past year, in part because of the concentrated nature of the portfolio and limited exposure to top performing sectors of the market, strategy performance remains above median and top quartile on a risk adjusted basis (Sharpe ratio) since inception. Ashford noted that Focused's fee is 3 bps above the median fee for this space, which concerned several Board members.

Ashford discussed two passive, risk neutral strategies for investing in this space with the goal of improved net of fee performance: 1) utilizing benchmark index funds and 2) using a sector weighted basket of ETF funds. Ashford was requested to provide additional analysis and bring specific alternatives to the February 2017 meeting for consideration by the Board.

FIXED INCOME REALLOCATION RECOMMENDATION

As a result of concerning organizational changes, Ashford recommended terminating Thornburg's $55 million account. Two options for reallocating the proceeds, which broadly maintained the fund's exposures to high yield and well below benchmark duration, were presented:

Option 1:

- $20 million to Vanguard Short Corporate Bond index fund
- $27 million to Mellon Capital High Yield Beta strategy
- $ 8 million to T. Rowe Price Floating Bank loan fund or

<u>Option 2:</u>

- $25 million to Loomis Sayles
- $23 million to T. Rowe Price Floating Rate bank loan
- $ 7 million to Vanguard Short Term Federal fund

Ashford noted that Staff suggested finding an option which utilized existing managers rather than establishing additional accounts with relatively small allocations. Potential transition costs were also discussed in light of the nature of Thornburg's holdings.

After discussion, Mr. Alt, seconded by Mr. Dennis, made a motion to authorize staff to take the actions necessary to terminate the Thornburg Multi-Sector Opportunistic Fixed Income mandate and to reallocate the final proceeds, on a pro-rata basis, as follows:

- $25 million to Loomis Sayles
- $23 million to T. Rowe Price Floating Rate bank loan
- $ 7 million to Vanguard Short Term Federal fund.

The motion passed by a vote of 4-0, with Ms. Cowan and Messrs. Brunner and Maier absent.

KEY INITIATIVES (UPDATE/OTHER BUSINESS)

- Ms. Stenroos noted that a draft of the annual Employee Newsletter, to be issued in January 2017 to retirees, was distributed to Board members for review. Members should communicate any comments directly to Ms. Stenroos.
- Mr. Zito noted the annual training will be held on Saturday, January 7, 2017.

INVESTMENT RELATED

A. Fund Balance for October
B. County Board Update (as of 9/30/16)
C. OPEB Quarterly Update (as of 9/30/16)

ADMINISTRATIVE ITEMS

A. Trip Report: Baltimore
B. Retirement Office Budget Variance Report
C. Calendar of Events

ADJOURNED

Mr. Dennis, seconded by Mr. Alt, offered a motion to adjourn the meeting. The motion passed with a vote of 4-0, with Ms. Cowan, Mr. Brunner and Mr. Maier absent. There being no further business, the meeting adjourned at 11:10 AM.

Respectfully submitted,
Susan Bomberg