



ERS

EMPLOYEES  RETIREMENT
SYSTEM OF TEXAS

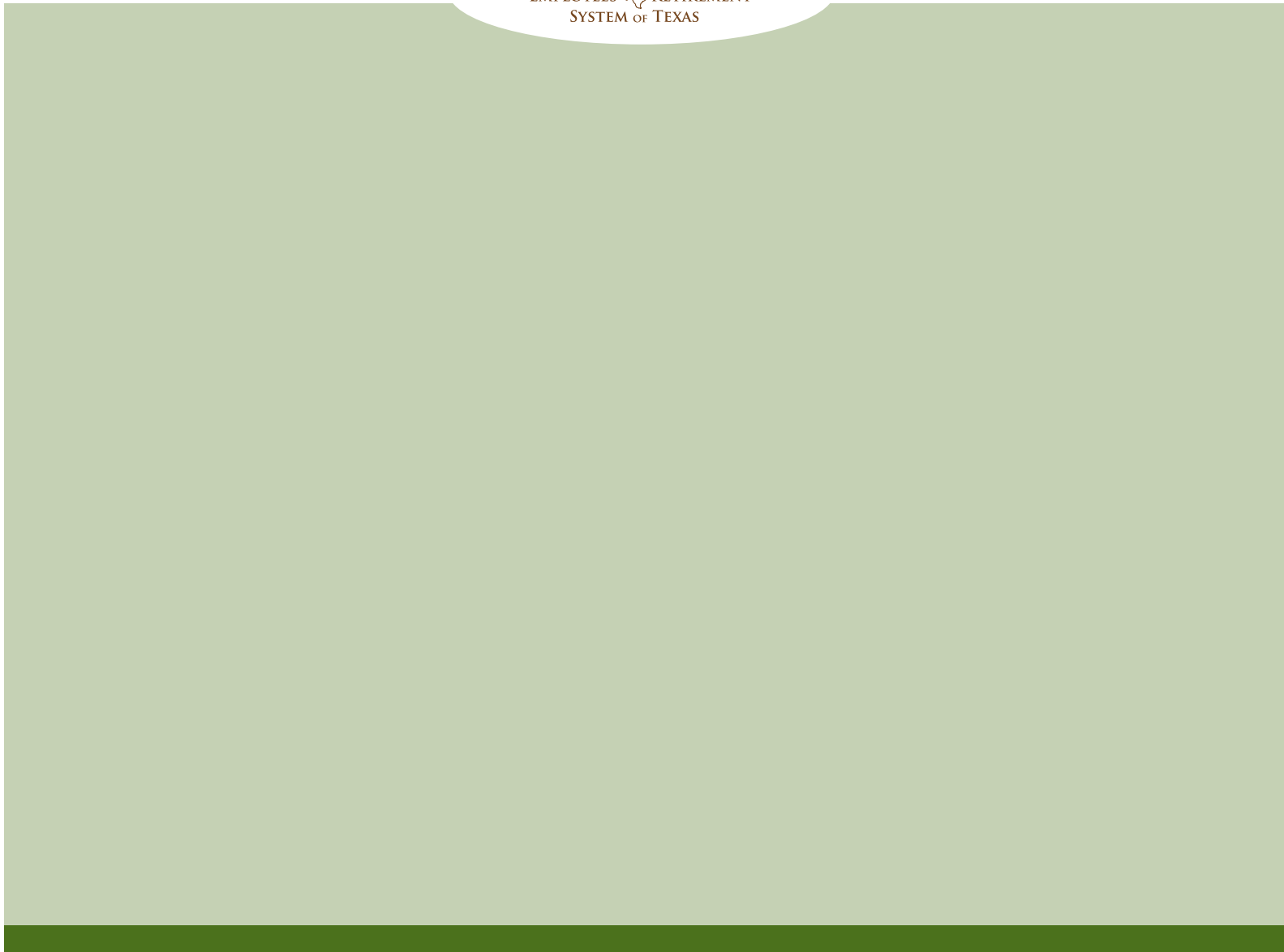


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**BOARD OF TRUSTEES MEETING
EMPLOYEES RETIREMENT SYSTEM OF TEXAS**

**February 24, 2015
ERS Board Room
ERS Building – 200 E. 18th Street
Austin, Texas 78701**

TRUSTEES PRESENT

Brian Ragland, Chair
Frederick E. Rowe, Jr., Vice-Chair
Doug Danzeiser, Member
Cydney Donnell, Member
Yolanda Griego, Member
I. Craig Hester, Member

ERS STAFF PRESENT

Ann S. Bishop, Executive Director
Porter Wilson, Executive Director Designate
Larry Zeplin, Chief Operating Officer
Paula A. Jones, General Counsel and Chief Compliance Officer
Tony Chavez, Internal Auditor
Bernie Hajovsky, Director of Enterprise Planning Office
Jordan Hajovsky, Director of Operations Support
Robert Kukla, Director of Benefit Contracts
Wendy McAdams, Director of Operations Support
Shack Nail, Deputy Director of Governmental Affairs
Ralph Salinas, Director of Human Resources
Marc Sundbeck, Manager of Enterprise Risk Management
Catherine Terrell, Director of Governmental Affairs
Tom Tull, Chief Investment Officer
Charles Turner, Chief Information Officer
Mike Wheeler, Chief Financial Officer
Ann Andersson, Legal Services
Brannon Andrews, Legal Services
Lori Blewett, Benefits Communications
Georgina Bouton, Benefit Contracts
Kelley Davenport, Executive Office
D'Ann Deleon, Benefit Contracts
Leah Erard, Governmental Affairs
Elizabeth Geise, Enterprise Planning Office
Gunther Goetz, Legal Services
Ginger Grissom, Benefit Contracts
Michelle Hinex, Enterprise Planning Office
Sharmila Kassam, Investments
David Lacy, Legal
Betty Martin, Investments
Patricia Maugham, Executive Office
Kyle Neely, Enterprise Planning Office
Lauren Russell, Benefit Contracts
Michelle Sneed, Enterprise Planning Office
Angelica Torres, Benefits Communications
MaryJane Wardlow, Governmental Affairs
Keith Yawn, Governmental Affairs

ALSO PRESENT

Nick Arnold, Humana
Matt Absher, ADP
Tiffany Calderon, Humana
Phil Dial, Rudd & Wisdom, Inc.
Justin Emerson, CVS/Caremark
Kirk Lavalley, Delta Dental
Kim McLeod, UnitedHealthcare
Susanna Sachez, Invesco
Sara Tilley, ADP

Mr. Brian Ragland, Chairman of the Board of Trustees of the Employees Retirement System of Texas (ERS), called the meeting to order and read the following statement:

“A public notice of the Board of Trustees meeting containing all items on the proposed agenda was filed with the Office of the Secretary of State at 2:44 p.m. on Thursday, February 12, 2015 as required by Chapter 551, Texas Government Code, referred to as “The Open Meetings Law.”

Upon adjournment of the Audit Committee, the Board of Trustees convened as a committee of the whole to consider the following Board agenda items. Minutes to the February 24, 2015 Audit Committee Meeting are located under the Audit Committee agenda minutes.

IV. REVIEW AND APPROVAL OF THE MINUTES TO THE DECEMBER 4, 2014 MEETING OF THE BOARD OF TRUSTEES

Board of Trustee Chair, Brian Ragland opened the floor for a motion on the approval of the minutes to the Board of Trustees Meeting held on December 4, 2014.

MOTION made by Mr. Craig Hester, seconded by Mr. Doug Danzeiser and carried unanimously by the present members of the Board of Trustees of the Employees Retirement System of Texas to approve the minutes held on December 4, 2014.

V. REVIEW, DISCUSSION AND CONSIDERATION OF THE TEXAS EMPLOYEES GROUP BENEFITS PROGRAM:

a. Selection of the Administrators for the TexFlex Flexible Spending Account (FSA) Program and Qualified Transportation Flexible Benefit (QTFB) Beginning September 1, 2015 –

Mr. Rob Kukla, Director of Benefit Contracts introduced Ms. Georgina Bouton, Assistant Director of Benefit Contracts to present the next agenda item on the selection of administrator(s) for the TexFlex FSA.

Mr. Kukla began by giving the board a brief background on the FSA and stated TexFlex is a qualified plan under the Internal Revenue Code §125. The FSA is voluntary participation and employees are able to defer \$2,500 for medical expenses and \$5,000 for dependent childcare. At the May 2014 meeting, the board approved FSA program changes which included participant’s ability to carryover up to \$500 in unused plan funds into the next plan year. This involved eliminating the 75 day grace period which allowed participants additional time to encumber expenses after the policy year ended. The other change was participants who terminate employment with the state are no longer required to continue making monthly contributions to their TexFlex health care accounts after their termination.

Ms. Bishop asked Mr. Kukla to explain how ERS got to the \$500 carryover and Mr. Kukla responded by saying a survey was sent out to all the members asking if they would prefer to use a \$500 carryover or continue with the 75 day grace period. In all 13,000 members responded to the survey and 80% preferred the

\$500 carryover. Ms. Bishop reported one of the benefits to the state on this program is certain taxes are not required.

Mr. Kukla reported ERS entered into a three-year contract with PayFlex Systems for the administration of flexible benefits claims services under the TexFlex Program for September 1, 2008 through August 31, 2011. The contract was subsequently extended for a four (4) year period to expire on August 31, 2015. In addition to the FSA, ERS wants to explore the use of a Qualified Transportation Fringe Benefits (QTFB) plan which would add optional benefits to active employees. Under the IRS Code §132, QTFB contributions would be made on a pre-tax basis and operate from a savings standpoint. Employees could use pre-tax dollars to pay for qualified expenses associated with their daily commuting and parking fees and other mass transit services which might be incurred by the member in order to get them to work. If a member has money left over from a plan year, it can be carried over to the next.

Ms. Bouton reported the scope of services for the RFP would include the administrative services for the TexFlex FSA program as well as a QTFB benefit. The RFP was issued on July 28, 2014 seeking qualified vendor(s) to provide administrative services for the Health Care Reimbursement Account, Dependent Childcare Reimbursement Account, and/or QTFB plans. Ms. Bouton stated responses were due by September 18, 2014. ERS received five responses from: ConnectYourCare (CYC), ADP, Payflex, Wageworks, and UnitedHealthcare (UHC). She reported each of the five bids received provided for both the administrative services for the TexFlex as well as a separate bid for the administrative services of the QTFB plan.

Article 2 of the RFP disclosed 14 criteria as the basis for evaluating responses submitted by the vendors. These criteria have been grouped into seven major categories: compliance with RFP, proposal evaluation criteria for minimum & preferred, financial considerations, operational capabilities and services, contractibility, vendor service verification, and site visit. Ms. Bouton reported the bid proposals are evaluated based on the minimum and preferred criteria. Evaluation is done by a cross-divisional team comprised of subject matter experts throughout seven divisions within ERS (Benefits Communications, Customer Benefits, Information System, Finance, Legal, Internal Audit, and Benefit Contracts). The evaluation teams are assigned only those sections of the RFP for which they possess subject matter expertise. Ms. Bishop stated the Benefit Contracts division is designed and created to procure or manage the procurement as well as the monitoring of all benefits related to contracts.

Following the initial round of clarifications, proposals from PayFlex and UHC had the lowest overall scores, and these proposals were not advanced for further consideration. Ms. Bouton reported the proposals from ADP, CYC, and WageWorks continued to be vetted through the evaluation process. By the end of this phase of the evaluation process, WageWorks bid ranked third and was not considered a finalist. The top two finalists identified were CYC and ADP.

Ms. Bouton informed the board the finalists were asked to participate in a face-to-face interview and to provide a best and final offer as well as a client list. ERS asked for a list of clients with FSA administrative services through each of these vendors, and a separate client list for the QTFB. Once ERS received those client lists, performance reference checks were made. Ms. Bouton reported all of the clients were complimentary of the services performed by the finalists.

The face-to-face interviews were held on January 14, 2015 and finalist interview sessions included presentations, key issue discussions and an opportunity for each respondent to highlight the strengths and unique aspects of their respective company. ERS staff conducted site visits at CYC and ADP to examine each of the finalist's customer service/operational and data center facilities. Throughout these site visits, ERS staff had a chance to ask a lot of questions and listen to the presentations from each of the organizations. Mr. Kukla also reported ERS found the site visits were informative and showed ADP has a consolidated operation effectively with all their administration in place whereas CYC is dispersed and has some outsourcing, particularly for back up support should claims or call center activities go beyond their expectation.

Mr. Kukla reported all things considered, ERS recommends the Board award the contract to ADP effective 9/1/2015. The board along with Mr. Kukla had various discussions on the explanation in determining the best value.

There being no further questions or discussion, the Board took the following action:

MOTION made by Ms. Yolanda Griego, seconded by Ms. Cydney Donnell, and carried unanimously by the present members of the board of Trustees of the Employees Retirement System of Texas and based on the information provided to ERS in response to the Request for Proposal, the evaluation process and results presented to the Board at this meeting, we have received sufficient information to determine the best value to the retirement system for the selection of a third part administrator of the flexible spending program, TexFlex. Therefore, I move that the Board of Trustees of the Employees Retirement System of Texas approve the selection of ADP to provide administrative services for the Health Care Reimbursement Account (HCRA), Dependent Care Reimbursement Account (DCRA), and Qualified Transportation Fringe Benefits (QTFB) plans available within the TexFlex Program, a cafeteria plan authorized and offered under the Texas Employees Group Benefits Program under a contract which will cover an initial four year term beginning September 1, 2015 through August 31, 2019.

I further move that the Board of Trustees of the Employees Retirement System of Texas authorize the Executive Director to negotiate and execute a contract with ADP with terms that are fully acceptable to ERS, and to authorize the Executive Director to thereafter administer the contract agreed to by the parties. In the event that a contract fully satisfactory to ERS is not timely executed with ADP, or if it appears to the Executive Director during the term of the contract that ADP will not be capable of performing the required administrative services for any plans or programs within the TexFlex Program to ERS' satisfaction, then the Board authorizes the Executive Director to resume contract negotiations with CYC, and to negotiate and execute contract terms with CYC that are fully acceptable to ERS, and to authorize the Executive Director to thereafter administer the contract agreed to by the parties.

b. Health Insurance Financial Status Update for the First Quarter Fiscal Year 2015 –

HealthSelect of Texassm (HealthSelect) is a self-funded point of service health benefit plan offered under the Texas Employees Group Benefits Program (GBP). About 84% of GBP health plan participants are enrolled in HealthSelect which offers health benefits coverage throughout Texas and the United States. Mr. Kukla informed the board ERS works very closely with the consulting actuaries, Rudd & Wisdom. ERS constantly monitors the financial performance of the health plans. Ms. Bishop reported ERS would spend down the contingency fund to \$100 million over the next biennium as stated in the appropriations request,.

Mr. Kukla reported the patient centered medical home (PCMH) program continues to pay dividends in helping to control costs. UHC reported PCMH participants cost 6% less than the rest of the HealthSelect population despite having similar health risk scores.

ERS contracted with Aon Hewitt to perform an audit of eligibility for all dependents added since the initial audit in 2011. The GAP audit was completed at the end of fiscal year 2014 and is expected to produce a net savings of \$8.7 million in fiscal year 2015.

Mr. Kukla proceeded to discuss bundled payments and stated ERS staff is currently investigating the use of bundled payments for certain procedures such as hip and knee replacements which often have significant variations in price from provider to provider. As part of the ongoing solution sessions where vendors can present potential cost saving opportunities to ERS staff, two companies have claimed providers often have inaccurate billings in which providers are sometimes overpaid for their services. Mr. Kukla stated these two companies presented potential solutions and ERS is in the process of issuing a Request for Proposal for these services.

There were no questions or further discussion, and no action was required on this item.

c. Discussion Regarding Ongoing Monitoring of HealthSelect TPA Performance –

Mr. Rob Kukla, Director of Benefit Contracts introduced Ms. Lauren Russell, Benefit Contracts Account Manager to present the next agenda item on the monitoring of the HealthSelect TPA performance. Mr. Kukla reported Benefit Contracts has a performance monitoring process for all the contracts tailored to the benefit plan such as financial performance, network, customer service, and claim processing just to name a few. Mr. Kukla reported monitoring methods include over 59 different contract monitoring tools such as, monthly financial reports, monthly administrative performance report and various meetings and operations. The monthly financial report is produced by the Underwriting, Data Analysis and Reporting Team and includes a review of revenue of income, claim payments and administrative costs.

On the 20th of every month ERS receives a Monthly Administrative Performance Report (MAPR). This report tracks adherence to several of the performance guarantees in the contract and includes a variety of items such as complaints and ID card delivery, phone call volume and service level statistics, network provider additions and terminations, and claim processing metrics and turn- around time.

Ms. Russell explained some of the examples of different types of items received on the MAPR. UHC reports on the total calls received which is broken down to member and provider calls. The MAPR also tracks several phone service levels such as the average speed of answer, which requires 80% of HealthSelect participant's phone calls are answered within 20 seconds. She also stated the blockage rate, which is the rate in which a member calls Customer Service and receives a busy signal, and the abandonment rate, which is the rate in which a participant terminates a phone call before reaching a Customer Service Representative are monitored. Ms. Russell reported the standard for both blockage rate and abandonment rate is 5%. Mr. Kukla noted this is just calls to our vendors and not the calls to Customer Benefits division at ERS.

Ms. Russell then noted the financial claims processing timeliness and both financial accuracy are measured on a monthly basis. In addition to tracking adherence to claims processing requirements in the MAPR report, ERS also hires an outside auditing firm on an annual basis to review the performance of the HealthSelect plan, and all other programs under the GBP. For fiscal year 2013 audit, ERS' outside auditing firm, Mountjoy Chilton Medley, measured 99.97% financial accuracy rate for UHC. Ms. Russell reported the fiscal year 2014 audit discussion is underway with a finalized project scope and expects to have the final report by the end of this year.

As part of the contracts monitoring process, Benefit Contracts holds bi-weekly operations and communications meetings. Ms. Russell reported these meetings occur both on-site and via conference call with the HealthSelect team. She noted progress on various open and outstanding items are reviewed which could include items such as benefit design review, communication projects, network activity and customer service trends. Ms. Russell informed the board the Benefit Contracts division handle calls, written correspondence, and any member issues raised which may be forwarded from various divisions within ERS. Benefit Contracts track member complaints and issues to ensure customer service trends and any sort of benefit reviews are identified and resolved timely.

Benefit Contracts division also receives reports on a quarterly basis which include anti-fraud activities, overpayment reports, member satisfaction survey scores, disease management initiatives, and wellness program activities.

Ms. Russell then proceeded to go over the survey results on the health insurance financial status update with the board. She stated the survey results are provided to ERS on a quarterly basis. The overall satisfaction with UHC continues to grow. Ms. Russell reported the overall satisfaction of UHC is 86.4%, for the last quarter of fiscal year 2014, which is a 4.3% increase from fiscal year 2013.

In a response to a question asked by Mr. Rowe wanting to know if there is a desired service satisfaction range, Ms. Russell stated there is a required standard all vendors are required to meet and UHC's is 80% or greater. Ms. Bishop then made comment there is a performance standard in the appropriations bill which ERS reports on. Ms. Bishop stated ERS is responsible for making decisions on the benefit design and not the third-party administrators.

Mr. Kukla informed the board of the annual executive review which summarizes the past year administrative and financial performance, healthcare trends and solutions to control healthcare spending. Mr. Kukla turned it over to Ms. Russell to discuss network management and stated Benefit Contracts receives regular emails from the network team at UHC with any sorts of new contracts signed or any potential terminations. Those go out to all of the directors to share with their appropriate staff. Mr. Kukla reported ERS receives a hospital based physician report every month and UHC is focusing on 314 unique groups in this category, of those 58% are emergency room physicians, to ensure our members, when they utilize an emergency room, particularly an in-network emergency room, are being treated by network physicians. Ms. Russell stated there has been a net addition of over 1,600 primary care physicians, 4,500 specialists, 1,400 other providers and over 43 new anesthesiology groups to UHC's network since 9/1/2012.

Mr. Kukla began to discuss complaints and grievances to the board and stated the most significant trend is the allowable amount grievance on anesthesia and seeing assistant surgeons charging rates higher than the surgeon. Mr. Kukla stated the assistant surgeon is a concern partly because there is no mechanism after the situation occurs to go through mediation like there is with the hospital-based physician.

Ms. Russell reported there are 31 specific contract requirements which currently govern the HealthSelect contract. Various items such as eligibility to file processing, communication materials review, quality and timeliness, phone service levels, claims processing time lines and website availability rate all ranked in severity. The items with the greatest ability to negatively impact GBP participants, if they're not met, carry the highest severity, and with them the highest performance assessment. This ensures GBP vendors make the members experience and their access to care the highest on their list of priorities.

Mr. Kukla reported there was an 11% savings in administrative fees with UHC. The reconciliation of claims had an accuracy rate of 99.987% from September 2012 through August 2014.

There were no questions or further discussion, and no action was required on this item.

VI. REVIEW AND DISCUSSION OF ELIGIBILITY AND COMPLIANCE FOR CALENDAR YEAR 2014 OF THE INVESTMENT ADVISORY COMMITTEE

Ms. Sharmila Kassam, Deputy Chief Investment Officer presented the agenda item on the Investment Advisory Committee (IAC) and the eligibility and compliance for calendar year 2014. Ms. Kassam reported the IAC was established at the discretion of the Board of Trustees and is comprised of at least five members and no more than nine members. The IAC members are selected based on their experience in the management of a financial institution or other business in which investment decisions are made or as a prominent educator in the fields of economics, finance or other investment related area. Texas Government Code §815.5091 through §815.5093 prescribe requirements for IAC eligibility and for the Board to annual review the eligibility of IAC members.

Ms. Kassam stated staff sent out compliance certification to all IAC members as part of the Board's annual review of the IAC compliance, and all certifications were returned without any issues noted. She also stated based upon ERS' review of the policy and statute requirements, all requirements for the IAC members have been met.

There were no questions or further discussion, and no action was required on this item.

VII. REVIEW AND DISCUSSION OF SECURITY AWARENESS AND PRACTICE UPDATE

Ms. Ann Bishop introduced Mr. Chuck Turner, Chief Information Officer to present to the Board an update on the security awareness practice. She stated it is very important for the Board to understand ERS' environment on security and how ERS takes very seriously the items of access to the members.

Mr. Turner reported to the board the Information Security Office (ISO) was formally created in 2007 with the hire of ERS' first Information Security Officer. The Information Security Officer is the primary point of contact for investigating and reporting on potential information security incidents. In 2010 ERS put out an information security manual and started investing in more tools and processes which allowed ERS to more effectively manage new processes and policies. In 2014 a transition was made in what the team does. They transitioned ISO from administrative activities to monitor, report and educate.

Mr. Turner stated one of the biggest initiatives in information security is data loss prevention, which includes unintentional release of member's information. Information Systems puts a great deal of investments into monitoring email, web and network traffic to prevent unintentional data loss. Storage is encrypted at rest on enterprise storage systems. The network and enterprise applications are periodically scanned. He also reported the hard drive on every ERS laptop and desktop is encrypted.

Multiple dashboards show different perspectives of the data to more readily identify anomalies or changing trends. Mr. Turner reported the ISO also monitors all of the active accounts, particularly the privileged accounts such as the DBAs, or the security administrators, who have access to a lot of information. Active monitoring is placed on these accounts so the ISO knows when and where they're being accessed. There is also monitoring of the secure file transfer protocol (sFTP) server. Mr. Turner reported anytime a member enrolls in a benefit, ERS has to inform the vendors, or the TPAs, the person needs to be in the system. The bulk of this data exchange with the vendors is on the sFTP server.

Mr. Turner briefly discussed the active dashboards such as data exchange monitoring, global view of ERS connections, detailed reporting of suspicious activity and fraudulent login detection. Remote connection monitoring maps and displays the source location of remote connections to ERS. This is compared to known connection patterns and expectations of Investment's travel.

Mr. Turner informed the board ERS has provided a tremendous amount of education to staff on the importance of information security. He reported ERS' culture has done well incorporating practices required in a constantly changing threat environment. As an example, he also reported IS completed a phishing campaign in October 2014 where they purposely sent out invalid "suspicious" emails to staff to see who would click on the link. He was glad to report a remarkably low number of staff clicked on the suspicious link.

Ms. Bishop asked Mr. Turner to briefly talk about Safe Harbor. She also mentioned ERS is compliant with Safe Harbor. Mr. Turner reported ERS did not have enterprise wide encryption at rest in 2013. Certain systems were encrypted because ERS knew there was sensitive information processing in those systems. When Safe Harbor was revised, IS reexamined how the information was used. Because of business processes, information needs to move to different applications or be accessed by multiple functional areas. The analysis determined the best approach was to do enterprise-wide encryption solution.

Ms. Bishop informed the board ERS has an agency-wide rapid response team so whenever there is an incident or suspected incident, the rapid response team is called in. It is a multiple discipline team of staff from all areas of the agency who come together, assess the issue, assess the potential and then all have their own responsibilities in terms of communications and evaluation which is monitored to the end. Ms. Marci Sundbeck, Director of Enterprise Risk Management, who is head of the agency-wide rapid response team, stated ERS has trained staff throughout the agency on how to recognize potential incidents and how to respond if they think an incident has occurred.

There were no questions or further discussion, and no action was required on this item.

VIII. DISCUSSION, CONSIDERATION AND TRAINING RELATED TO AGENCY CONTRACTING:

a. Reaffirmation of the Delegation of Authority for Agency Contracting and Procurements –

Paula A. Jones, General Counsel and Chief Compliance Officer notified the board Governor Gregg Abbott sent a letter to all state agencies on January 28, 2015 requesting compliance with certain contracting reforms contained within the recently filed Senate Bill 353 by Senator Jane Nelson. Governor Abbott specifically asked state agencies to begin complying with the following as of February 1, 2015:

- Disclosure and justification of no-bid contracts;
- Disclosure of possible conflicts of interest;
- Prohibition against contracts with business entities in which certain high-level agency leadership or staff have a financial interest;
- Contracts valued at more than \$1 million signed by Board Chair or delegated to the Executive Director;
- For procurements over \$5 million, notification to the Board and Executive Director regarding procurement method utilized and any potential issues relating to solicitation.

Ms. Jones reported ERS already has in place processes and procedures consistent with most of the items above and is currently evaluating other ways to enhance the processes and procedures regarding procurement. She also stated the Board has already delegated to the Executive Director the authority to execute and administer all contracts by ERS, regardless of the value. In the fiscal year 2015 approved operating budget, the Executive Director was authorized to negotiate, enter into and administer contracts on behalf of ERS. This delegation is consistent with the broad grant of authority found in ERS' Rules of the Board of Trustees (the "Rules"), Rule 65.1. In Rule 65.9, the Board of Trustees also delegated to the Deputy Executive Director the authority to perform any of the duties the Executive Director would have. Notwithstanding the existing authority, it was recommended the Board reaffirm the Executive Director's authority to negotiate, execute and administer contracts on behalf of ERS valued at more than \$1 million.

Ms. Jones stated she felt it was a good opportunity for the board to discuss who signs contracts on behalf of ERS in general, and whether or not it should just be the Executive Director, or should other staff be authorized to do so. Ms. Jones noted the Executive Director maintains the authority to execute any contract, and perhaps those under \$1 million could be delegated to other staff to execute based on certain dollar thresholds or other limitations with which the Board is comfortable.

Ms. Jones reported 285 contracts and related documents went through the legal division last fiscal year. There were also 27 private market-related transactions, 603 purchase orders up to \$25,000 in value, and 106 purchase orders were \$25,000 and more. Not all of these represented separate contracts. There was further discussion among the board and staff regarding the contracts process, and staff indicated additional information would be provided to the Board at a future meeting before discussing delegating contract authority to other staff.

There being no further questions or discussion, the Board took the following action:

MOTION made by Mr. Craig Hester, seconded by Ms. Yolanda Griego, and carried unanimously by the present members of the Board of Trustees of the Employees Retirement System of Texas that although the Executive Director is already authorized by the Board of Trustees to negotiate, execute and administer contracts on behalf of ERS, I move that the Board of Trustees hereby reaffirms the authority of the Executive Director to negotiate, execute and administer contracts on behalf of ERS that are valued at more than \$1 million.

b. Contract Training for Governing Bodies of Certain State Agencies –

Nancy Lippa, ERS Assistant General Counsel, informed the board at the December 4, 2014, board meeting about a new statutory training requirement. All members of the governing body of a state agency who

enter into contracts must complete at least one course of the training required by Texas Gov't Code §2262.0535 by September 1, 2015. The objective of the training is to provide governing bodies with a general understanding of the ethical and professional responsibilities related to State of Texas Purchasers and Contract Managers entering into contracts and oversight of awarded contracts. Ms. Paula A. Jones, ERS General Counsel and Chief Compliance Officer, informed the Board that although other staff is not required to take this training class, ERS staff involved in the contracting process are also taking this training concurrently with the Board.

At this time, the board and other ERS staff viewed a webcast of the pre-recorded training provided by the Office of the Comptroller of Public Accounts.

There were no questions or further discussion, and no action was required on this item.

IX. REVIEW AND DISCUSSION OF THE STATE OF ERS' UNFUNDED PENSION LIABILITY

Ms. Cathy Terrell, Director of Government Affairs and Jennifer Jones, Government Affairs Senior Program Specialist, presented the next agenda item on the state of ERS' unfunded pension liability. Ms. Terrell reported the pension plan is out of balance and the fund will not ever become sound unless funding or benefits are adjusted. Previous discussions have focused on either the revenue or the benefit options. Ms. Terrell informed the board of a few articles in the press, one from the *Austin American Statesman*, one from the *Dallas Morning News* editorial supporting pension funding, and a Moody's Report where there was a press release warning Texas to take care of the pension funds (or it could impact the state's bond rating).

Ms. Terrell reported the introduced budget for the House and Senate provided base funding only for the pension program and did not fund anything towards the requested exceptional item. The agency did get exceptional item funding for health insurance. She also reported the state has changed how funds will be allocated for retirement benefits from Fund 6.

Ms. Bishop stated ERS has presented information to both the House and Senate and doesn't expect to appear again before the Appropriations and Senate Finance Committees. Ms. Terrell stated in addition to all of the other moving factors related to employee benefits and pay raises, ERS does a mid-year actuarial valuation during the legislative session.

A sound plan has an equal balance of income and expenses. The income includes contributions and investment earnings and the expense is paid retirement benefits. Ms. Terrell stated the only way to lower expenses is to lower the amount of benefits being paid out. ERS has been asked by the legislature to come up with proposals for making the plan sound, through either revenue increases or benefit decreases. Since initial pension reforms in 2009, 37,000 participants are in Tier 2 benefits and 12,000 current participants who are in Tier 3 (which is the lowest level of benefits). There are 85,000 participants who will receive Tier 1 benefits.

Ms. Terrell discussed options which would grandfather, or exempt, certain employees who meet at least one of these criteria:

- Must be in Tier 1
- Are aged 50 or older or;
- Can combine age and creditable service to equal 70 or;
- Have at least 20 years of creditable service (or 15 years of LECO service);

Ms. Terrell noted under these grandfathering criteria if benefit modifications were made, 63% of active members could be affected by potential benefit changes.

Ms. Jones then explained how various potential retirement benefit changes might affect fund soundness, (see attached chart). Ms. Jones reported when GRS provided the analysis, they gave a full range of actuarial metrics typically seen in the valuation, like actuarial accrued liability, unfunded liability, and normal

cost. For the purpose of initial communications with policy makers and stakeholder groups, the focus on funding period is for a couple of reasons. One is ERS' actuary considers funding period the best metric to communicate where your plan is going. The other reason is Texas statute defines plan soundness as the ability pay off any unfunded liability within a 31-year period or less.

ERS requested the necessary funding in its Legislative Appropriation Request to make the fund sound without having to make any benefit changes.

Ms. Bishop and Ms. Paula Jones addressed Mr. Ragland's comment about what the board's role is with regard to legislation authorizing the ERS fund to provide post-retirement increases, including current law which requires ERS to provide a Cost of Living Adjustment (COLA) to some ERS retirees if the plan is sound before and after the COLA is paid.

Closing a Define Benefit plan can be done, but needs to be carefully planned as it can result in higher annual cost later on. If the state were to close the DB plan to new hires, Ms. J. Jones continued, the trust fund would deplete in 2038 compared to the current depletion date of 2063. Initially, direct appropriations for benefits would be \$3.9 billion in 2039 and it would remain above \$3 billion through 2053.

Ms. Terrell informed the board this agenda item was for informational purposes only and the material was developed at legislative request.

There were no questions or further discussion, and no action was required on this item.

X. EXECUTIVE DIRECTOR'S REPORT

(This agenda item was taken out of order and presented during the Joint Board of Trustees and Investment Advisory Committee meeting)

Ms. Ann Bishop proceeded with the next agenda item Executive Director's Report. Her report to the Board is included with these minutes as ¹Exhibit A

XI. EXECUTIVE SESSION – IN ACCORDANCE WITH SECTION 551.074, TEXAS GOVERNMENT CODE, THE BOARD OF TRUSTEES WILL MEET IN EXECUTIVE SESSION TO EVALUATE THE DUTIES AND PERFORMANCE OF THE EXECUTIVE DIRECTOR DESIGNATE OF THE EMPLOYEES RETIREMENT SYSTEM OF TEXAS; AND TO DELIBERATE THE APPOINTMENT, EMPLOYMENT, EVALUATION, REASSIGNMENT, DUTIES, DISCIPLINE, OR DISMISSAL OF ONE OR MORE PUBLIC OFFICERS OR EMPLOYEES. THEREAFTER, THE BOARD MAY CONSIDER APPROPRIATE ACTION IN OPEN SESSION.

(This agenda item was taken out of order and presented during the Joint Board of Trustees and Investment Advisory Committee meeting)

At 4:49 p.m. on Tuesday, February 24, 2015, Mr. Brian Ragland, ERS Board of Trustees Chair, announced the ERS Board of Trustees would be going into executive session in accordance with Texas Government Code §551.074, to evaluate the duties and performance of the Executive Director Designate of the Employees Retirement System of Texas; and to deliberate the appointment, employment, evaluation, reassignment, duties, discipline, or dismissal of one or more public officers or employees. Thereafter, the Board may consider appropriate action in open session.

¹Exhibit A – page 12

At 5:42 p.m. on Tuesday, February 24, 2015, the Board of Trustees returned to open session and Mr. Ragland announced no action, decision, or vote was taken by the Board while in Executive Session. Mr. Ragland further stated he would entertain any motions from members of the Board.

MOTION made by Ms. Cydney Donnell, seconded by Ms. Yolanda Griego, and carried unanimously by the present members of the Board of Trustees of the Employees Retirement System of Texas to adjourn the meeting at 5:42 p.m.

XII. RECESS OF THE BOARD OF TRUSTEES – FOLLOWING A TEMPORARY RECESS, THE BOARD OF TRUSTEES WILL RECONVENE WITH THE INVESTMENT ADVISORY COMMITTEE TO TAKE UP THE REMAINING AGENDA ITEMS.

PUBLIC AGENDA ITEM - # 10

10. Executive Director's Report

February 24, 2015

Legislative Update

The House and Senate have appointed committees and begun the process of hearing testimony on bills. Senator Jane Nelson is the new chair of the Senate Finance Committee. In the House, the new House Appropriations Chair is Representative John Otto. The committees handling the bulk of the bills affecting ERS also have chairs. Senator Joan Huffman is the new chair of State Affairs, and Senator Kevin Eltife is the chair of Business and Commerce. In the House, Representative Dan Flynn is the chair of Pensions.

On February 5, ERS appeared before the Senate Finance Committee to testify on the proposed budget. On February 16, ERS appeared before House Appropriations to discuss their proposed budget. Both budgets provide base funding levels for the state retirement contribution, carrying forward the 7.5% contribution from the previous biennium, with a small allowance to account for potential new state employees. ERS will continue to work with the budget writers to find additional funding. On the GBP, both budgets include ERS's base request, as well as the exceptional item request to cover the estimated 6.9% cost trend.

ERS staff has visited with legislators and stakeholders to provide updates. On January 29, members of the Governmental Affairs division held a briefing with legislators and staff from the Central Texas delegation. In addition, a stakeholder briefing was held on February 3.

The summary of legislation with the potential to affect ERS programs filed so far in the 84th Texas Legislature is attached as Exhibit A.

Modernize Benefits Administration (MBA)

Modernizing Benefits Administration (MBA) is a multi-year project to evaluate and implement a course of action for replacing the existing Benefits Administration system and realigning processes and resources for member support of the Group Benefits Program (GBP). The goal of MBA is to determine the best possible option for providing eligibility and enrollment services to our members. The solution will enable ERS to deliver efficient customer service and allow for additional self-service features and functionality for members.

MBA was discussed at the August 2014 Board of Trustees meeting. Since then, the MBA team has collaborated to draft the Request for Proposal (RFP) for solutions to enable ERS to deliver efficient customer service and allow for additional self-service features and functionality for members. The RFP includes expectations for all current and future functionality. The team is currently reviewing the draft RFP for legal language and consistencies.

Due to size and scope of the MBA project, the RFP requires review by the Texas Contract Advisory Team (CAT), a team established by statute to assist state agencies in improving contract management practices. It is anticipated the CAT will engage the Quality Assurance Team (QAT) during its review. The QAT is an oversight committee charged with ensuring quality assurance reviews of technology projects for the State of Texas. We have adjusted the RFP timeline to include the estimated time required for this review and feedback. Based on the initial reviews, the QAT may have additional reviews during the implementation stages of the project.

Organizational Changes

I am pleased to announce Shack Nail assumed the role of Special Projects and Policy Advisor to the Executive Director effective February 2. Throughout his lengthy tenure at ERS, Shack has served in a number of roles, most recently as Deputy Director of Governmental Affairs. In his new role, Shack will coordinate policy

priorities, represent the Executive Office in constituent interactions, and communicate agency policy and programs to external stakeholders. Cathy Terrell, the Director of Governmental Affairs, now oversees the day-to-day administration of the Governmental Affairs Division.

I am also pleased to announce the creation of a new unit, the Enterprise Planning Office, within the Executive Office, also effective February 2. Bernie Hajovsky has transitioned into the role of Director of Enterprise Planning. Bernie began his career at ERS in 2005 and has served in the Office of Management Support (OMS) for the last two years. In his new role, Bernie oversees the Enterprise Program Management Office (EPMO) and OMS staff while coordinating enterprise-wide activities, which includes directing strategic planning and overseeing agency operational planning and budgeting. Bernie reports to the Chief Operating Officer.

As noted above, the EPMO joined the Executive Office effective February 2 to allow for better positioning of EPMO staff to broaden their role throughout the agency. Many projects require planning and coordination across multiple divisions, so the EPMO will transition under the Enterprise Planning Office to encompass all enterprise-wide projects. Kyle Neely continues in his current role as the manager of the EPMO.

2015 Board of Trustee Election Update

ERS certified the candidates for the 2015 Trustee Election at a meeting held on February 11. There were three candidates certified: Jerry McGinty (Texas Department of Criminal Justice), Louri O'Leary (Texas Secretary of State), and Ilesa Daniels (Texas Health and Human Services Commission). Trustee candidates will answer voter questions as part of a forum to be held in the ERS auditorium on March 5. The forum is an opportunity for ERS members and retirees to ask questions and hear the candidates' positions on state employee benefits and retirement issues. The forum will be live-streamed for our Internet audience, and a recording will be available on our website for those who are unable to attend or view the event on March 5. Voting runs March 6 through April 10. The election results will be announced on May 6.

Investments Update

Highlights:

ERS co-sponsored an Emerging Manager Conference with Teacher Retirement System January 22. More than 700 investment professionals attended. ERS took the opportunity to reiterate its commitment to Emerging Managers with a number of representatives participating from the Investment Division.

Honorable Mentions:

Robert Lee III was nominated for the Next Generation CIO award at aiCIO's Industry Innovation Awards. He was also recognized in the Class of 2014 Forty Under Forty list.

Tom Tull made the aiCIO list for the Power 100 Institutional Investment Elite for 2014.

State Employee Charitable Campaign Awards

Participating ERS employees generously donated \$37,363.00 to our 2014 ERS State Employee Charitable Campaign resulting in the campaign receiving the **Largest Per Capita Gift award** and the **Rising Star: Most Improved Campaign award** (in the category of agencies with 300 to 499 employees.)

Additional information

Largest per Capita gift = Total Amount of Donations/Total number of Agency Employees = \$120.00

Rising Star = 25% increase from previous year

STAFF RECOMMENDATION:

This agenda item is provided for informational and discussion purposes only. No action is required.

ATTACHMENT – 1

Exhibit A – Filed Legislation Affecting the Employees Retirement System of Texas 84th Texas Legislature,
Regular Session

**Filed Legislation Affecting the Employees Retirement System of Texas
84th Texas Legislature, Regular Session**

Bill	Author	Summary	February 10, 2015
GENERAL APPROPRIATIONS BILLS			
		Retirement: <ul style="list-style-type: none"> • ERS – State contribution rates of 7.5% for both years of biennium; plus an additional state agency contribution at the rate of 0.5% of base payroll • LECOSRF – 0.5% state contribution rate for both years of biennium • JRS 2 – 15.66% state contribution rate for both years of biennium • JRS 1 – Fully funded 	
SB 2	Nelson	Group Health Plan: <ul style="list-style-type: none"> • Funded sufficiently to potentially avoid benefit changes through FY 2017 	
HB 1	Otto	<ul style="list-style-type: none"> • Maintains current 100% member and 50% dependent state contribution • Maintains 1% of base payroll contribution from participating state agencies and higher education institutions • Requires ERS to provide reports regarding the bidding and administration of the HealthSelect contract to LBB and SAO. Other Benefits: <ul style="list-style-type: none"> • Public Safety Benefits (Chapter 615) – Fully funded • Retiree Death Benefits – Fully funded 	
RETIREMENT			
<i>Retirement - Elected Class</i>			
HB 131	Simpson	Fixes elected class annuity at 2% of \$125,000 for members entering the class on or after 9/1/2015.	Filed 11/10/14
SB 110	Taylor	Suspends or reduces annuities of elected officers on final conviction of a felony or certain misdemeanors related to the officer's official duties.	Referred to State Affairs 1/27/15
SB 115	Taylor	Prohibits ERS from withholding as confidential the name or amount of annuity of a retired member of the legislature.	Referred to Business & Commerce 1/27/15
HB 408	Turner, Chris	Prevents certain members of the elected class from transferring service to the employee class, or from retiring from the employee class while still in elected office.	Filed 12/01/14

Bill	Author	Summary	February 10, 2015
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HB 425	Fallon	Makes elected officials ineligible to receive an annuity if convicted of bribery, embezzlement, or perjury.	Filed 12/02/14
HB 681	Sheets		Filed 1/05/15

Retirement - Employee Class

HB 442	Gonzales, Larry	Allows beneficiaries to have all or part of an employee's or retiree's death benefits be payable directly to a funeral director or establishment.	Filed 12/04/14
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HB 585	Fallon	Limits the maximum retirement annuity amount for new employees hired after August 31, 2015 to the amount of the gross salary of an active duty General or Admiral of the US armed forces.	Filed 1/05/15
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HB 701	Allen, Alma	Provides an immediate 10% COLA, effective 9/1/15, plus a 4% annual COLA for annuitants. Also provides a supplemental payment equal to the lesser of the monthly annuity or \$2,000, payable in January '16.	Filed 1/14/15
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SB 465	Taylor	Suspends or reduces annuities of Texas Juvenile Justice Department employees on final conviction of a certain offenses against a minor student.	Referred to State Affairs 2/10/15
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CHAPTER 615
(Survivor benefits for officers killed in the line of duty)

SB 436	Lucio	Increases lump sum survivor benefit from \$250,000 to \$500,000, and doubles the monthly benefit paid to surviving minor children.	Referred to State Affairs, 2/09/15
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INSURANCE

Insurance - Coverages

SB 194	Ellis	Requiring HIV tests to be a part of routine blood work.	Referred to Health and Human Services 1/27/15
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SB 264	Ellis	Allows dependents of the wrongfully imprisoned to participate in the GBP.	Referred to State Affairs 1/28/15
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Bill	Author	Summary	February 10, 2015
<i>Insurance - Plan Design/Funding</i>			
HB 966	Crownover	Requires ERS to establish a voluntary consumer-directed health plan in the form of a high deductible health plan (HDHP) with a Health Savings Account (HSA) as an alternative to HealthSelect with coverage to begin	Filed 01/27/15
SB 482	Hancock	September 1, 2016.	Referred to State Affairs 2/10/15