
Minutes

A regular meeting of the Virginia Retirement System Board of Trustees was held on October 10, 2019 in Richmond, Virginia with the following members present:

Board Members Present

Mitchell L. Nason, Chair
Diana F. Cantor, Vice Chair
Hon. J. Brandon Bell, II
Wallace G. Harris, Ph.D.
W. Brett Hayes
William H. Leighty
O'Kelly E. McWilliams, III
Joseph Montgomery
Troilen G. Seward

Larry Kochard, Investment Advisory Committee Chair (by phone)

VRS Staff:

Patricia Bishop, Ron Schmitz, Jennifer Schreck, John Alouf, Suja Amir, Rory Badura, Parham Behrooz, Jeanne Chenault, Michael Cooper, Harriet Covey, Juanita Cribbs, Sara Denson, Barry Faison, Brian Goodman, JT Grier, KC Howell, Robert Irving, Wendy Jenkins, Ross Kasarda, LaShaunda King, Kristina Koutrakos, Matt Lacy, Chung Ma, Curt Mattson, Scott Mootz, Laurie Nelson, Walker Noland, Greg Oliff, Andrea Peeks, Caitlin Pelletier, Dan Whitlock, Cindy Wilkinson and Nick Zizzo.

Guests present were:

Latosha Johnson, Department of Planning and Budget; Elizabeth Peay, Office of Attorney General; Rick Fowler, Virginia Governmental Employees Association; Bea Snidow, Virginia Education Association; Michael Jay, House Appropriations Committee; Sarah Herzog, Senate Finance Committee; Jessica Ackerman, Virginia Municipal League; Jeremy Bennett, Virginia Association of Counties; Jenny Schoeller and Brian Deveney, Auditor of Public Accounts.

The meeting convened at 1:32 p.m.

Approval of Minutes

Upon a motion by Mr. Nason, with a second by Mr. Harris, the minutes of the June 13, 2019 meeting were approved.

Report of the Investment Advisory Committee

The Board received the report of the Investment Advisory Committee (IAC) meeting of August 13, 2019 and placed it on file.

The joint meeting of the Investment Advisory Committee (IAC) and the Investment Policy Committee (IPC) occurred on August 13, 2019. Mr. Schmitz provided a summary of the meeting, starting with the IAC election of the Vice Chair, William “Hance” West. Mr. Schmitz advised that staff provided an overview CIO report and asset and liability modeling (ALM) updates. Staff also presented proposed changes to the benchmarks and the mix of investment strategies for the Public Equity, Credit Strategies and Fixed Income programs.

Report of the Investment Policy Committee

The Board received the IPC report of August 13, 2019 and placed it on file.

Mr. Nason summarized the joint IAC and IPC meeting and noted that robust discussion was held throughout the ALM presentation. The IPC discussed and adopted Verus’s “Diversify” allocation mix as a reasonable long-term target.

Based on the results of the asset/liability study and an in-depth discussion, as well as the Investment Advisory Committee’s full support, the Committee recommended to the full Board the approval of the two actions outlined below.

Mr. Schmitz provided clarification on the two requests for board action.

On a motion from Mr. Nason, with a second from Ms. Cantor, the VRS Board of Trustees approved the following as amended:

Request for Board Action 2019-10-11: The Board approves changes to the benchmarks in the Defined Benefit Plan Investment Policy Statement for the following programs: Public Equity, Credit Strategies and Fixed Income. These changes are effective January 1, 2020.

On a motion from Mr. Nason, with a second from Ms. Cantor, the VRS Board of Trustees approved the following as amended:

Request for Board Action 2019-10-12: The VRS Board of Trustees approves the recommended changes to update the long-term Defined Benefit Plan Strategic Asset Allocation and Allowable Ranges to reflect the new Board target asset mix. The changes are effective January 1, 2020.

Rate of Return Assumption Overview and Background

Mr. Schmitz provided an overview of the investment rate of return assumption. He stated that migration to the new asset allocation would take time to achieve, resulting in the benefits of the new allocation not being realized immediately. He added that selecting a discount rate below the median expected long-term rate reflects a blended discount rate which incorporates near-term uncertainty in the markets. Historical investment return assumptions have targeted the median of the expected range of outcomes. The use of a blended rate targets a return slightly below the median, thereby increasing the probability of meeting plan assumptions. He concluded that due to the uncertainty surrounding the potential for, as well as the timing, length or severity of a near-term recession, a discount rate based on a blend of short- and long-term expectations warrants a lowering of the plans’ long-term investment

rate of return assumption. Mr. Badura provided clarification on the plan liabilities and the impact on contribution rates and the funded status.

Upon a motion by Mr. Nason, with a second by Ms. Cantor, the VRS Board of Trustees approved the following action:

Request for Board Action 2019-10-13: *The Board approves a reduction in the actuarial assumed rate of return from the current 7% to 6.75%, effective as of July 1, 2019, to be applied beginning with the 2019 actuarial valuations.*

Report of the Chief Investment Officer

Mr. Schmitz began his report by reviewing the New Investments and Terminations Report, the WaM Quarterly Summary Report and the Manager Referral Quarterly Summary Report with the Board.

Mr. Nason thanked Mr. Schmitz for his report.

Report of the Defined Contribution Plans Advisory Committee

The Board received the Defined Contribution Plans Advisory Committee (DCPAC) report of September 5, 2019 and placed it on file. Mr. Hayes stated that staff presented the Annual Investments Review, provided Administrative reports and gave communication updates. The next meeting of the DCPAC will take place on November 7, from 10:30 a.m. to 1:00 p.m. Mr. Hayes also advised that the ORPHE Annual Employer Update took place September 26, 2019. Further, staff will poll the DCPAC for 2020 meetings.

Report of the Audit and Compliance Committee

The Board received the Audit and Compliance Committee report of September 12, 2019 and placed it on file.

Mr. Leighty noted that staff discussed the Auditor of Public Accounts (APA) 2018 Assurances Review, noting that the APA has completed the Employer Assurances audit work. He also noted that two audit reports, the review of General Controls within the IT Client-Server Environment and the Group Life Insurance and Death Processing review, were submitted to the Committee. Mr. Leighty added that the following updates were discussed: Quarterly Review on Modernization Program, the Internal Audit Annual Progress Reports for FY2019, the Proposed FY2020 Audit Work Plan, the Quarterly Report on Fraud, Waste and Abuse Hotline Cases, Management's Quarterly Travel Expense and Per Diem Report and finally the Audit Director's Performance Evaluation.

Internal Audit Director Jennifer Schreck then reviewed the Annual and Long-Range Audit Plan Progress Report for FY 2019 and the Proposed Annual Audit Plan for FY 2020.

On a motion from Ms. Cantor, with a second by Mr. Montgomery, the Board approved the Annual Audit Plan for FY 2020.

On a motion from Ms. Cantor, with a second from Mr. Montgomery, the VRS Board of Trustees approved the following:

Request for Board Action 2019-10-14: The VRS Board of Trustees approves a 7% performance bonus for the Audit Director.

Mr. Nason thanked Mr. Leighty for his report.

Report of the Administration and Personnel Committee

The Board received the Administration and Personnel Committee report of September 9, 2019 and placed it on file.

Mr. Nason briefed the Board on the reappointment of William “Hance” West to the Investment Advisory Committee.

On a motion from Mr. Nason, with a second from Ms. Cantor, the VRS Board of Trustees approved the following:

Request for Board Action 2019-10-15: the VRS Board of Trustees reappoints William “Hance” West to the Investment Advisory Committee for a two-year term ending December 31, 2021.

Mr. Nason discussed the staff report on FY 2019 Agency Performance Outcomes and Operational Measures and the performance bonuses for eligible administrative and Investment Department operations and administration employees.

On a motion from Mr. Nason, with a second from Mr. Bell, the VRS Board of Trustees approved the following:

Request for Board Action 2019-10-16: The VRS Board of Trustees approves (i) the attainment of FY 2019 APOs and Operational Measures and (ii) a lump-sum bonus equal to 2.5% of salary for eligible administrative employees and eligible Investment Department operations and administration employees.

On a motion from Mr. Nason, with a second from Ms. Cantor, the VRS Board of Trustees approved the following:

Request for Board Action 2019-10-17: The VRS Board of Trustees approves performance lump-sum bonuses for eligible administrative employees and eligible Investment Department operations and administration employees.

Next, Mr. Nason discussed the staff report on the year-end budget results for FY 2019 and an update on the FY 2020 budget, as well as the proposed budgets for FY 2021 and FY 2022.

On a motion from Mr. Nason, with a second from Ms. Cantor, the VRS Board of Trustees approved the following:

Request for Board Action 2019-10-18: The VRS Board of Trustees authorizes staff to request spending authority from the Department of Planning and Budget and legislature, as applicable, to execute planned initiatives for the next two fiscal years.

Mr. Nason noted that the Committee went into closed session to discuss benefits and compensation related to specific individuals.

On a motion from Mr. Nason, with a second from Ms. Cantor, the VRS Board of Trustees approved the following:

Request for Board Action 2019-10-19: The VRS Board of Trustees approves payment of an incentive amount of approximately \$4,088,248 for FY 2019 to VRS investment professionals as authorized by the Investment Professionals' Pay Plan.

On a motion from Mr. Nason, with a second from Mr. Bell, the VRS Board of Trustees approved the following:

Request for Board Action 2019-10-20: The VRS Board of Trustees approves a 5% performance bonus for the VRS Director payable on November 1, 2019 and a supplemental payment of \$75,000 made on or before December 31, 2019 as authorized in the 2019 Appropriation Act.

Mr. Nason praised the hard work of staff for its progress on Modernization and achieving agency goals.

Report of the Director

Ms. Bishop began her report by updating the Board on new coverage elections.

Ms. Bishop announced that VRS has won the Communicator Award of Distinction. Kelly Hiers was elected to the Board of the National Association of Government Defined Contribution Administrators (NAGDCA). She added that for the 37th consecutive year, VRS received an award for the Comprehensive Annual Financial Report (CAFR) and a Certificate of Achievement of Excellence in Financial Reporting for Governmental and Financial Reporting. The Popular Annual Financial Report (PAFR) also won the Government Finance Officers Association award.

Ms. Bishop then reviewed the FY 2020 Roadmap. She reported that VRS is still keeping track of the progress on the Cardinal payroll system. The host agency, the Department of Accounts (DOA), continues to evaluate its revised project schedule and it is slated to be completed in the Fall of 2021.

Ms. Bishop provided updates on operational and ongoing activities.

Litigation Update (Closed Session)

Mr. McWilliams moved, with second by Mr. Leighty, that the Virginia Retirement System Board of Trustees convene a closed meeting under the Virginia Freedom of Information Act for the purpose of consultation with legal counsel about actual or probable litigation pursuant to the exemption contained in Code of Virginia § 2.2-3711(A)(7).

Upon return to open meeting, Mr. McWilliams moved, with a second by Ms. Seward, the following resolution:

WHEREAS, the Virginia Retirement System Board of Trustees convened a closed meeting on this date pursuant to an affirmative recorded vote and in accordance with the provisions of The Virginia Freedom of Information Act; and

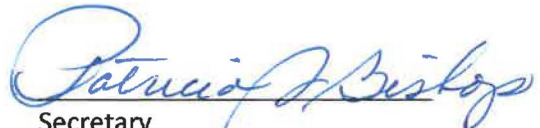
WHEREAS, Code of Virginia § 2.2-3712 requires a certification by this Committee that such closed meeting was conducted in conformity with Virginia law;

NOW, THEREFORE, BE IT RESOLVED, that the Board certifies that, to the best of each member's knowledge, (i) only public business matters lawfully exempted from open meeting requirements under this chapter were discussed in the closed meeting to which this certification resolution applies, and (ii) only such public business matters as were identified in the motion by which the closed meeting was convened were heard, discussed or considered by the Board.

The Board approved the resolution upon the following roll call vote:

Mitchell L. Nason: Aye
Diana F. Cantor: Aye
Hon. J. Brandon Bell, II: Aye
Wallace G. Harris: Aye
W. Brett Hayes: Aye
William H. Leighty: Aye
O'Kelly E. McWilliams, III: Aye
Joseph W. Montgomery: Aye
Troilen G. Seward: Aye

There being no further business, the meeting adjourned at 3:20 p.m.


Chair
Secretary

Report

The Investment Advisory Committee (IAC) held a joint meeting with the Investment Policy Committee on August 13, 2019 and took up the following matters:

APPROVAL OF MINUTES

The Committee approved the minutes of its April 11, 2019 meeting.

ELECTION OF IAC VICE CHAIRPERSON

The Committee elected William “Hance” West as the IAC Vice Chair.

CIO REPORT

Mr. Schmitz began his report with a market overview. Next, he discussed asset allocation and reviewed plan performance – which generally continues to be strong relative to benchmarks. He then discussed tracking error, information ratio and fund volatility – concluding that risk measures are all within Board-approved levels. Mr. Schmitz then reviewed the New Investments and Terminations Report with the Committee.

ALM UPDATE

The Committee was then updated on the status of the asset/liability study by Dr. Steven Peterson of VRS and John Meier of Verus Investments. Topics covered included, but were not limited to, deterministic projections, stochastic projections, 2008 – 2018 stress tests, and various scenario analyses. Updated possible long-term Defined Benefit Plan asset allocation and allowable ranges were also presented.

In addition, the Committee reviewed various assumed rates of return and the effects of each rate on funding.

Robust discussion was held throughout this presentation and the IAC endorsed the Verus’ “Diversify” allocation mix as a reasonable long-term target.

PROPOSED BENCHMARK and STRATEGY CHANGES

The respective Investment Program Directors presented proposed changes to the benchmarks and the mix of investment strategies within the Public Equity, Credit Strategies, and Fixed Income programs. The last asset/liability study suggested modifications of program investment mixes (Verus’ “Diversify” allocation) and these proposed benchmark changes more closely correlate to the new mix of investment strategies within each affected program.

A discussion was then held on the impact of the proposed benchmark changes on the total fund risk/reward aspect of the asset/liability study.

Thorough and detailed discussions took throughout this presentation.

IAC MOTIONS and CONSENSUS

After careful consideration and in-depth discussion, the IAC unanimously passed a motion, to be sent to the IPC, in full support of the benchmark and strategy changes presented at this meeting.

After additional discussion, there was consensus by the IAC members to fully support the long-term Defined Benefit Plan asset allocation and allowable ranges. Regarding a change in the assumed rate of return, the IAC members agreed that a potential change should be discussed further at the next Board meeting.

Submitted to the Board of Trustees on October 10, 2019.



Lawrence E. Kochard, Chair
Investment Advisory Committee

Report

The Investment Policy Committee (IPC) held a joint meeting with the Investment Advisory Committee on August 13, 2019 and took up the following matters:

APPROVAL OF MINUTES

The Committee approved the minutes of the following Brown Bag Lunch Meetings: November 20, 2018, December 13, 2018, February 14, 2019, May 13, 2019 and June 13, 2019.

CIO REPORT

Mr. Schmitz began his report with a market overview. Next, he discussed asset allocation and reviewed plan performance – which generally continues to be strong relative to benchmarks. He then discussed tracking error, information ratio and fund volatility – concluding that risk measures are all within Board-approved levels. Mr. Schmitz then reviewed the New Investments and Terminations Report with the Committee.

ALM UPDATE

The Committee was then updated on the status of the asset/liability study by Dr. Steven Peterson of VRS and John Meier of Verus Investments. Topics covered included, but were not limited to, deterministic projections, stochastic projections, 2008 – 2018 stress tests, and various scenario analyses. Updated possible long term Defined Benefit Plan asset allocation and allowable ranges were also presented. In addition, the Committee reviewed various assumed rates of return and the effects of each rate on funding.

Robust discussion was held throughout this presentation. The IPC discussed and adopted the Verus' "Diversify" allocation mix as a reasonable long-term target. In addition, the Committee agreed that the assumed rate of return could be lowered, however, determined that further discussion at the next Board meeting is warranted before a final decision.

PROPOSED BENCHMARK AND STRATEGY CHANGES

The respective Investment Program Directors presented proposed changes to the benchmarks and the mix of investment strategies within the Public Equity, Credit Strategies, and Fixed Income programs. The last asset/liability study suggested modifications of program investment mixes (Verus' "Diversify" allocation) and these proposed benchmark changes more closely correlate to the new mix of investment strategies within each affected program.

A discussion was then held on the impact of the proposed benchmark and strategy changes on the total fund risk/reward aspect of the asset/liability study.

Robust discussion was held throughout this presentation.



IPC RBAs

Based on the results of the asset/liability study and an-depth discussion, as well as the Investment Advisory Committee's full support, the Committee recommends the approval of the following actions to the full Board:

Request for Board Action: *The Board approves changes to the benchmarks in the Defined Benefit Plan Investment Policy Statement for the following programs: Public Equity; Credit Strategies; and, Fixed Income. These changes are effective January 1, 2020. (Upon further review by staff since the last meeting, additional changes to the benchmarks may be necessary. Staff plans to review proposed changes at the November IAC meeting, and will bring revisions to the Board of Trustees at its November 20, 2019, meeting.)*

Request for Board Action: *The VRS Board of Trustees approves the recommended changes to update the Defined Benefit Plan Strategic Asset Allocation and Allowable Ranges to reflect the new long-term Board target asset mix. The changes are effective January 1, 2020. (Note that the dates in the RBA for the Defined Benefit Plan Asset Allocation have been updated to clarify the inception date of the previous long-term target asset mix.)*

Submitted to the Board of Trustees on October 10, 2019.

A handwritten signature in black ink, appearing to read 'Mitchell L. Nason', written over a horizontal line.

Mitchell L. Nason, Chair
Investment Policy Committee

Report

The Defined Contribution Plans Advisory Committee met on Thursday, September 5th, and took up the following matters:

INVESTMENTS

Annual Investments Review

Staff provided an overview of the DCPAC duties and responsibilities as it relates to investments. Staff's annual investments review included a review of the total DC plans assets overseen by the Investment Department as well as highlights from staff's annual report covering the investment programs for the unbundled and bundled DC plans investment programs. Staff informed the Committee that staff will share recommended changes to the two DC investment policy statements at its next scheduled meeting on November 7, 2019. Staff noted it had no suggested changes to the DC Plans Investments Belief Statements.

ADMINISTRATION

Administrative Reports and Communication Update

Staff provided an overview of monthly reports, specifically highlighting the following:

- (1) The total assets and number of accounts under management in the second quarter of 2019;
- (2) New plan adoptions and transition of assets for second quarter 2019, and a historical overview of plan adoptions and transitions to the COV 457 and Cash Match Plans;
- (3) 2019 NAGDCA Leadership Award for Hybrid Voluntary Contributions Initiatives;
- (4) Review of total assets in the COV 457 and Virginia Cash Match Plans for the second quarter of 2019;
- (5) An overview of COV 457 and Virginia Cash Match plans contributions, withdrawals and net cash flow for the second quarter of 2019;
- (6) Review of total assets in the Hybrid Retirement Plan for the second quarter of 2019, including the assets and accounts in the Hybrid 401(a) Cash Match Plan and Hybrid 457 Deferred Compensation Plan;
- (7) An overview of cash flow from the defined contribution component of the Hybrid Retirement Plan, including contributions, withdrawals and net cash flow for the second quarter of 2019;
- (8) An update on the Hybrid 457 voluntary contribution elections and participation rates, including the auto-escalation population and number of participants with the maximum voluntary contributions;
- (9) An update on Auto-Escalation 2020 employer communication and outreach efforts;

- (10) An overview of the positive initial pilot of a summer meeting series for hybrid plan school division employees to address the challenges of connecting with teachers due to their classroom and other afterschool responsibilities; and
- (11) Annual review of asset retention initiatives, including an overview of asset retention metrics for the unbundled plans, distributions and withdrawals and ongoing communication and engagement efforts for active and separated participants.

ORPHE Update

- (1) Total ORPHE assets for the second quarter 2019, and assets by plan provider (DCP, TIAA, and Fidelity);
- (2) ORPHE-eligible enrollments and new hire provider selections in the second quarter 2019;
- (3) An update on ORPHE 2020 initiatives, including an overview of the implementation timeline as well communication and outreach initiatives planned in the fall.

OTHER BUSINESS

There was no other business to come before the Committee.

PROPOSED 2019 MEETINGS

The next meeting of the DCPAC will take place on November 7th, from 10:30 a.m. to 1:00 p.m. Also, for those who are interested, the ORPHE Annual Employer Update is scheduled for September 26, 2019, but is not a meeting of the DCPAC. The DCPAC will also poll for 2020 meetings.

That concludes my report to the Board.

Submitted to the Board of Trustees on October 10, 2019.



Brett Hayes, Chair
Defined Contribution Plans Advisory Committee

Report

The Audit and Compliance Committee met on September 12, 2019 and discussed the following:

EXIT ON THE AUDITOR OF PUBLIC ACCOUNTS (APA) 2018 EMPLOYER ASSURANCES REVIEW

The APA reported it has completed the Employer Assurances audit work. This audit covers the data VRS prepares and supplies to employers and their auditors to support required financial reporting over pension plans and other post-employment benefits (OPEBs) under Governmental Accounting Standards Board (GASB) Statements No. 68 and No. 75. All resources for employers will be available within the next week on the VRS website.

AUDIT REPORTS

The Committee received two audit reports.

- The review of *General Controls within the IT Client-Server Environment* determined VRS's IT client-server architecture is effective and secure. Opportunities for enhancement of certain policies and procedures were discussed within the report.
- The review of *Group Life Insurance and Death Processing* noted these activities are handled timely, accurately, and in accordance with established guidelines and procedures.

QUARTERLY REVIEW ON MODERNIZATION PROGRAM – PHASE 4

Management presented its status report on the Modernization Program - Phase 4. Management highlighted VNAV system performance since the April Go-live activities, noting:

- system availability has been good,
- ramp-up activities are considered complete,
- all disbursements continue to run as scheduled,
- RIMS remains as inquiry only, with unneeded environments being deleted, and
- quality monitoring and operational support activities continue.

Further, management noted the remaining functionality of online retirements will be finalized by the end of the fiscal year.

Internal Audit presented its Quarterly Review and indicated agreement with management's representations regarding the Modernization Program – Phase 4 overall schedule, budget, and scope. Internal Audit acknowledged management's efforts and continued work.

INTERNAL AUDIT ANNUAL PROGRESS REPORTS FOR FISCAL YEAR 2019

The Committee received the following updates:

Annual Report on the Audit Recommendation Follow-Up System (ARFUS)

The Committee received the Annual Report on the Audit Recommendation Follow-Up System (ARFUS) as of June 30, 2019. ARFUS contained seven internal recommendations for the fiscal



year, three of which were tested and released (one with comment). As of June 30, 2019, there were four outstanding recommendations in ARFUS.

Internal Audit Annual Report

The Audit Director provided the Committee with a summary of the Department's accomplishments over the past year as well as an overview of the Department's initiatives and challenges for the coming year. She recognized the contributions of the internal audit team.

The Audit Director explicitly confirmed to the Audit and Compliance Committee that the VRS Internal Audit Department and its staff are organizationally independent of the activities they examine and possess the appropriate qualifications to meet the needs of the approved audit plans. The Audit Director also discussed the Department's conformance with the IIA's *Standards* and upcoming external quality assurance review to further validate its conformance.

Annual and Long-Range Audit Plan Progress

The Audit Director presented the annual audit plan results for the fiscal year ended June 30, 2019, along with the status of the long-range audit plan for the four years ending June 30, 2020.

The Audit Director noted that as of the conclusion of the third fiscal year of the long-range plan, modifications have been made to the remaining plan to accommodate the changing risk environment, adjustments to the Modernization Program – Phase Four schedule, and unplanned resource constraints.

Specifically, changes have been made to the timing and/or duration of certain examinations, including the addition of new projects, deferral of some projects to a period outside of the currently approved long-range plan and the consolidation of other projects within the existing long-range plan.

PROPOSED FY 2020 AUDIT WORK PLAN

The Committee received the proposed audit plan for fiscal year 2020, which is a component of the long-range plan. The Audit Director discussed adjustments to the annual plan as pulled from the long-range plan to better align available resources with the organizational risks. The Committee approved the plan as presented.

QUARTERLY REPORT ON FRAUD, WASTE AND ABUSE HOTLINE CASES

Two alleged Fraud, Waste and Abuse Hotline complaints reported to Internal Audit via the Office of the State Inspector General during the period of May 1, 2019 through July 31, 2019 were presented to the Committee. The complaints alleged retirement benefit fraud and abuse of the long-term disability program. Both allegations were determined to be unfounded; therefore, the cases were closed.

MANAGEMENT'S QUARTERLY TRAVEL EXPENSE AND PER DIEM REPORT

The Committee received management's quarterly travel expense and per diem report.

MISCELLANEOUS UPDATES

The Committee received the following updates:

Results of Agency Performance Outcomes and Agency Operational Measures

Internal Audit reviewed management's representations regarding the Agency Performance Outcomes and Operational Measures for the fiscal year ended June 30, 2019, noting nothing came to its attention that indicated that the outcomes and measures were not appropriately represented as satisfied for the fiscal year.

Internal Audit's Review of Investment Incentive Compensation

Internal Audit completed its review of the Investment Department's proposed incentive compensation amounts and determined they were accurately computed in accordance with the authorized pay plan.

Quality Assurance Review

The Audit Director noted Internal Audit is currently undergoing a quality review by an outside party relative to the department's conformance with the International Standards for the Professional Practice of Internal Auditing. The review's results will be available later in the year.

Proposed Committee Meeting Schedule for the 2020 Calendar Year and Next Meeting

The Audit Director discussed proposed meeting dates for 2020 and will be reaching out soon to finalize them with Committee members.

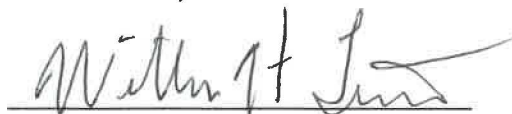
The Committee's next meeting is scheduled for December 12, 2019 at 10 a.m.

AUDIT DIRECTOR'S PERFORMANCE EVALUATION

The Committee met in closed session to review the Audit Director's performance for the fiscal year ended June 30, 2019.

Request for Board Action: Before you is a Request for Board Action to approve a bonus for the Audit Director. The Committee recommends that the Board approve this RBA. I ask for a motion for the Board to approve this request.

Respectfully submitted to the Board of Trustees on October 10, 2019.



Mr. William H. Leighty, Chair
Audit and Compliance Committee

Report

The Administration and Personnel Committee met on September 9, 2019 and discussed the following:

APPROVAL OF MINUTES

The Committee approved the minutes of its June 12, 2019 meeting.

REAPPOINTMENT OF INVESTMENT ADVISORY COMMITTEE MEMBER

The Committee recommends the reappointment of William “Hance” West to the Investment Advisory Committee for a two-year term ending December 31, 2021.

Request for Board Action: *The Board reappoints William “Hance” West to the Investment Advisory Committee for a two-year term ending December 31, 2021.*

REVIEW AND APPROVE ATTAINMENT OF FY 2019 APOS AND OPERATIONAL MEASURES

Mr. Cooper presented a report of the FY 2019 Agency Performance Outcomes (APOs) and Operational Measures to the Committee. He advised that staff had successfully met the goal of completing four (4) of the five (5) identified APOs and noted that the only item not completed in its entirety was APO #3, which required the completion of three technology projects that comprise the remainder of Phase 4. Those projects have been added to the FY 2020 APOs adopted at the June Board meeting. Staff surpassed the stated goal of meeting or exceeding the performance target for thirteen (13) of the sixteen (16) Operational Measures, successfully completing fifteen (15). Mr. Cooper noted that the only measure not accomplished related to disability retirement processing timeframes that were affected by the transition from RIMS to VNAV.

The Committee recommends the approval of the following action to the full Board:

Request for Board Action: *The VRS Board of Trustees approves (i) the attainment of FY 2019 APOs and Operational Measures and (ii) a lump-sum bonus equal to 2.5% of salary for eligible administrative employees and eligible Investment Department operations and administration employees.*

REVIEW AND APPROVE PERFORMANCE BONUSES FOR ELIGIBLE ADMINISTRATIVE AND INVESTMENT OPERATIONS AND ADMINISTRATION EMPLOYEES

Mr. Cooper discussed the proposed performance bonuses for eligible administrative and Investment operations and administration employees. The RBA includes a 4% bonus to employees who received a rating of “exceptional” and a 2% bonus to employees who received a rating of “exceeds” on their FY 2019 performance evaluation. The bonus amount is based on their salary as of June 30, 2019.

The Committee recommends the approval of the following action to the full Board:

Request for Board Action: *The VRS Board of Trustees approves performance lump-sum bonuses for eligible administrative employees and eligible Investment Department operations and administration employees.*



REVIEW REVISED BOARD'S CODE OF ETHICS AND STANDARDS OF CONDUCT POLICY

Mr. Cooper briefed the Committee on the recommended amendments to the Board's Code of Ethics and Standards of Conduct Policy. After discussion, the Committee agreed to postpone the RBA until the November meeting pending clarification of certain definitions in the policy.

BUDGET UPDATE (YEAR END RESULTS)

Ms. Peeks gave a presentation of the year-end results for FY 2019 and an update on the FY 2020 budget, as well as the proposed budgets for FY 2021 and FY 2022. Ms. Peeks advised that approximately two-thirds of the budget proposals for FY 2021 and FY 2022 concern necessary enhancement of IT services; namely migration to a cloud environment, strengthening existing IT security, fraud detection and prevention systems, and replacement of end-of-life systems and hardware. The majority of the remaining budget proposals address tools and staffing needs of the Investment Department to develop strategies and maximize returns, as well as staffing to enhance the agency's in-person and online customer responsiveness. Ms. Peeks concluded by noting that, compared to its peers as reported by CEM Benchmarking, Inc., VRS is spending less in total pension administration costs while providing optimal service to members and retirees.

REVIEW AND AUTHORIZE BUDGET REQUEST TO THE DEPARTMENT OF PLANNING AND BUDGET

Following Ms. Peeks' presentation, the Committee recommended approval of the following action to the full Board:

Request for Board Action: *The VRS Board of Trustees authorizes staff to request spending authority from the Department of Planning and Budget and legislature, as applicable, to execute planned initiatives for the next two fiscal years.*

INFORMATIONAL ITEM: APPROVE INTERNAL AUDIT DIRECTOR'S PERFORMANCE BONUS

Mr. Cooper advised that the Audit and Compliance Committee will review the Audit Director's performance at its meeting on September 12, 2019 and provide a recommendation via RBA to the Board of Trustees regarding a performance bonus at its October 10, 2019 meeting.

COMPENSATION AND BENEFITS (CLOSED SESSION)

The Committee went into closed session to discuss benefits and compensation related to specific individuals.

Upon returning to open meeting, the Committee recommended the approval of the following actions to the full Board:

Request for Board Action: *The VRS Board of Trustees approves payment of an incentive amount of approximately \$4,088,248 for FY 2019 to VRS investment professionals as authorized by the Investment Professionals' Pay Plan.*



The Committee noted that the amount presented in the RBA is an approximate amount that may be amended before being presented to the Board. The RBA has been amended to reflect the Committee's action.

Internal Audit reviewed the proposed investment incentive compensation for the fiscal year that ended June 30, 2019 and found that the aggregate amount, as well as the amended payment amounts, were accurately computed in accordance with the Investment Professionals' Pay Plan.

Request for Board Action: *The VRS Board of Trustees approves a 5% performance bonus for the VRS Director payable on November 1, 2019 and supplemental payment of \$75,000 made on or before December 31, 2019 as authorized in the 2019 Appropriation Act.*

Submitted to the Board of Trustees on October 10, 2019.



Mitchell L. Nason, Chair
Administration and Personnel Committee