ARKANSAS TEACHER RETIREMENT SYSTEM
BOARD OF TRUSTEES

MINUTES
October 3, 2006

The Arkansas Teacher Retirement System Board of Trustees held a regular meeting at 9:30 a.m., on Tuesday, October 3, 2006, in the Board Room of the ATRS Building at 1400 West Third Street in Little Rock, Arkansas.

Members of the Board Present:
John Fortenberry, *Chair*
Robin Nichols, *Vice Chair*
Dr. Richard Abernathy
Robert H. "Bunny" Adcock, Jr.
Monty Betts
Hazel Coleman
Lawrence Colston
Dr. Paul Fair
Beverly Leming
Linda Parsons
Ellen Terry

Staff Present
David Malone, *Executive Director*
Julie Cabe, *Deputy Director*
Kim Kight, *MPA*
Katherine Corcoran
Christa Clark, *Attorney Specialist*
Wayne Greathouse, *Deputy Director, Finance*
Gail Bolden, *Assoc. Director Operations*
George Snyder, *Internal Auditor*
Phillip McNeil, *Assoc. Director, Fiscal Affairs*
Suzanne Davenport, *Supervisor, Fiscal*
Donna Hobbs, *Personnel Manager*
Judy Brown, *Member Services Supervisor*

Members of the Board Absent:
Dr. T. Kenneth James
Gus Wingfield
Jim Wood

Others Present:
Rob Moritz - *Stephens Media*
Bobby Lester - *ARTA*
Mike Wickline - *AR Democrat-Gazette*
Betty McGuire, *former Board member*
Jim McGuire
Lloyd W. Black - *ARTA*
John Garrett - *Milliman Inc.*
Helen Holloway - *ARTA*
Mary Purselley - *ARTA*
Mary Ann Brown - *AR Dept. of Education*
Rodney O. Parks - *Merrill Lynch*
Richard Hutchinson - *AR Education Association*
Jody Carreiro - *Osborn, Carreiro & Associates*
Steve Osborn - *Osborn, Carreiro & Associates*

Linda W. Collins - *Lonoke County RTA*

I. Call to Order/Roll Call

John Fortenberry, Board Chair, called the meeting to order at 9:30 a.m., with a quorum present.

II. Adoption of Agenda

Mr. Fortenberry announced five additions to the agenda:

A. Revisions to Policy No. 1-11 (Legislative Committee Charter) would be considered during the Committee's report.

B The updated roster of Board Committees reflecting action taken on October 2 had been distributed and should replace Attachment No. 7 in the agenda packet.

C. Consideration of revised guidelines for Western Asset Opportunistic Yankee Portfolio and Wellington Non-U.S. Equity Portfolio in the Investment Committee report **(Resolution Nos. 2006-25a and 2006-25b – Revision of Guidelines)**.

D. The changes, noted in the October 2 meeting regarding the June 5-6, 2006, minutes, have been made and copies of the revised minutes have been distributed. The first item of business after the adoption of the agenda would be approval of these minutes.

Robin Nichols moved adoption of the agenda including the additions, with a second by Ellen Terry. The Board unanimously approved the motion.

III. Approval of Revised June 5-6, 2006, Board Minutes

Linda Parsons moved adoption of the revised minutes of the June 5-6, 2006, Board meeting, Ms. Terry seconded, and the Board unanimously approved.

IV. Report of the Investment Committee

A. Based on the recommendation of the Investment Committee, Ms. Nichols, Committee Chair, moved approval of the proposal to release the moratorium on Arkansas-Related Investment Program – Loans *(Attachment No.1)*. Hazel Coleman seconded, and the Board unanimously approved.

B. Ms. Nichols announced that the Investment Committee recommended ratification of the actions of the Executive Director, David R. Malone, in

continuing a property casualty insurance contract with Rebsamen Insurance. Monty Betts moved ratification of Mr. Malone's action and approval of the insurance contract with Rebsamen Insurance, Dr. Fair seconded, and the Board unanimously agreed.

C. Ms. Nichols reported that the Investment Committee had reviewed another proposal from Diamond State Ventures II (DSV-II) at their meeting on October 2. She reported that the committee voted three to two in favor of investing four million dollars with DSV-II, but rules require at least four votes to approve as a recommendation from the committee. After discussion of the staff's reasons for recommending the investment, Dr. Fair moved approval of a $4 million investment in DSV-II, Robert H. "Bunny" Adcock, Jr. seconded, and the Board approved on a vote of eight members for, one member opposed, and two members not voting.

V. Approval of Revisions to Board Policy No. 1-11 (Legislative Committee Charter)

The Board reviewed the revisions to Board Policy No. 1-11 (Legislative Committee Charter) *(Attachment No. 2)* recommended by the Legislative Committee. Dr. Fair moved approval of the revised policy, Dr. Richard Abernathy seconded, and Board unanimously concurred.

VI. Discussion of Committee Reassignments

Mr. Fortenberry presented the revised Committee assignment list and rotation schedule *(Attachment No. 3)*. There were no questions or discussion.

VII. Report on Executive Director Search/Interviews

Mr. Fortenberry stated that the Board had interviewed three candidates and had a fourth interview scheduled in the afternoon during the Executive Session.

VIII. Resolution No. 2006-25: Recommendation of J. P. Morgan Strategic Property Fund Guidelines

Ms. Parsons moved adoption of **Resolution No. 2006-25** *(Attachment No. 4)* establishing the guidelines for J. P. Morgan Strategic Property Fund, Ms. Nichols seconded, and the Board unanimously approved the motion.

IX. Resolution No. 2006-25a: Recommendation of Western Asset Opportunistic Yankee Portfolio LLC Guidelines

Ms. Parsons moved approval of the revised guidelines in **Resolution No. 2006-25a** *(Attachment No. 5)*, Mr. Adcock seconded, and the Board unanimously concurred.

X. Resolution No. 2006-25b: Recommendation of Wellington Non-US Equity Portfolio Guidelines

Following discussion of the revised guidelines, Mr. Adcock moved approval of **Resolution No. 2006-25b** *(Attachment No. 6)*, Ms. Parsons seconded, and the Board unanimously approved the motion.

XI. Report on Actuarial Study by *Osborn, Carreiro & Associates, Inc.*

Jody Carreiro and Steve Osborn presented their study findings to the Board. They stated that the assumptions currently being made by ATRS actuaries, *Gabriel-Roeder,* were all reasonable, consistent, and appropriate. They had two suggestions: (1) To reconsider ATRS investment return assumption making it more conservative; and (2) to begin collecting more/better data on reciprocal salaries outside the ATRS system.

Brian Murphy of *Gabriel-Roeder* thanked Mr. Osborn and Mr. Carreiro for their report. Mr. Murphy said he believes the current investment return assumption of 8% is reasonable but will be reviewed again at the time of the next annual actuarial report. He agreed that Gabriel-Roeder would improve the process regarding reciprocity by beginning to keep more information on salaries.

At 10:15 a.m. Mr. Fortenberry called for a short break. The meeting reconvened at 10:30 a.m.

XII. Report on Operational Review of T-DROP by *Milliman Consultants & Actuaries*

John Garrett discussed the Operational Review of T-DROP report prepared by *Milliman Consultants & Actuaries*. After answering questions from the Board, he stated that he believed the current T-DROP plan was cost-neutral on a going-forward basis at the present time. He noted this conclusion could change in the future as a result of actions of the Legislature, the Board, or of future experience. He cautioned the Board that proposed IRS regulations could cause a problem with the current plan if those regulations become final.

XIII. Staff Reports:

A. Medical Board Reports – Michael Ray

Michael Ray presented the medical reports for the months of June, July, and August 2006. Ms. Parsons moved approval of the medical reports as presented, Ms. Nichols seconded, and Board unanimously agreed.

B. Personnel Report – Donna Hobbs

Ms. Hobbs presented the personnel reports for June through August 2006. Following discussion Ms. Parsons moved approval of the reports, Ms. Terry seconded, and the Board unanimously concurred.

C. Financial Reports – Phillip McNeill

Phillip McNeil presented the financial reports for the months of March, April and May. According to ATRS Policy No. 2-1, he reported that two charter schools had not paid their employer contributions to the system. He identified Haas Hall Academy of Farmington as having a plan in place to repay the sum of $50,0000 over the next two years. He further stated that the other school, identified as Focused Learning of Conway, plans to be paid-in-full within the next week.

D. No other staff reports required action.

XIV. Executive Director's Comments

David Malone had no comments.

XV. Executive Session on Personnel Matters

At 1:00 p.m. the Board entered into an executive session to interview a candidate for Executive Director and to discuss personnel matters. The meeting reconvened at 2:30 p.m. Ms. Coleman moved the reopening and readvertising of the Executive Director position, Mr. Adcock seconded, and the Board unanimously approved the motion.

XVI. Adjournment

Mr. Fortenberry adjourned the meeting at 2:45 p.m.

Katherine Corcoran, Recorder

David Malone, Executive Director

John Fortenberry, Chair

Date Approved

ARKANSAS TEACHER RETIREMENT SYSTEM
1400 West Third Street
Little Rock, Arkansas 72201

RESOLUTION
No. 2006-25a

WHEREAS, the Board of Trustees of the Arkansas Teacher Retirement System desires to establish investment guidelines for Western Asset Opportunistic Yankee Portfolio LLC; and

WHEREAS, guidelines were originally adopted on August 5, 2003; and

WHEREAS, the revised guidelines attached to this resolution have been recommended by the System's consultant and staff and shall be effective on the date of funding;

NOW, THEREFORE, BE IT RESOLVED, that the Board of Trustees of the Arkansas Teacher Retirement System hereby approves the revised guidelines as attached for Western Asset Opportunistic Yankee Portfolio LLC.

Adopted this 3rd day of October 2006

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John Fortenberry, *Chair*
Arkansas Teacher Retirement System

ARKANSAS TEACHER RETIREMENT SYSTEM
1400 West Third Street
Little Rock, Arkansas 72201

RESOLUTION
No. 2006-25b

WHEREAS, the Board of Trustees of the Arkansas Teacher Retirement System desires to establish investment guidelines for Wellington Non-U.S. Equity Portfolio; and

WHEREAS, guidelines were originally adopted on February 3, 2004; and

WHEREAS, the revised guidelines attached to this resolution have been recommended by the System's consultant and staff and shall be effective on the date of funding;

NOW, THEREFORE, BE IT RESOLVED, that the Board of Trustees of the Arkansas Teacher Retirement System hereby approves the revised guidelines as attached for Wellington Non-U.S. Equity Portfolio.

Adopted this 3rd day of October 2006

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John Fortenberry, *Chair*
Arkansas Teacher Retirement System

POLICY TYPE: Governance Process

POLICY TITLE: Legislative Committee Charter

1. There shall be a Legislative Committee composed of five members of the Board appointed by the Board Chair, including the Board Chair who will serve as an ex officio voting member of the committee.

2. The committee shall meet as often as needed during the three-month prelegislative fall season and during the General Assembly sessions. At other times, the committee will meet on call by either the Committee Chair or the Executive Director.

3. The committee shall recommend to the Board for approval a spokesperson to present and support the Board's defined and adopted positions on legislative issues.

4. The purposes of the Legislative Committee shall be:

   A. To preview legislative proposals that will impact the Retirement System and its members.

   B. To suggest and develop legislative proposals for the benefit of the Retirement System and its members.

   C. To make recommendations to the Board for initiating or supporting legislative proposals or for opposing proposed legislation.

   D. To review and monitor enacted legislation relating to the Retirement System and its members. It shall be the ongoing responsibility of the Legislative Committee:

      i. To see that such legislation is properly incorporated into Retirement System policies and procedures, and

      ii. To monitor the effect of such legislation as it relates to current and future retirees.

   E. To monitor meetings of the Legislative Council and the Committee on Social Security and Retirement.

Authority: A.C.A §§24-7-301-305
Adopted: June 12, 2002
Amended: October 7, 2003
Removed from APA: December 6, 2005
Amended: October 3, 2006

ARKANSAS TEACHER RETIREMENT SYSTEM
1400 West Third Street
Little Rock, Arkansas 72201

RESOLUTION
No. 2006-25

WHEREAS, the Arkansas Teacher Retirement System desires to establish investment guidelines for JP Morgan Strategic Property Fund, the attached guidelines were developed by the system's consultant, Ennis Knupp and Associates, and reviewed and approved by the staff of ATRS.

NOW, THEREFORE, BE IT RESOLVED that the above-mentioned guidelines shall be effective on the date of funding and remain in force until new guidelines are recommended by the system's consultant and approved by the Board of Trustees of the Arkansas Teacher Retirement System.

FURTHER RESOLVED that the Board of Trustees of the Arkansas Teacher Retirement System approves the proposed guidelines for JP Morgan Strategic Property Fund.

Adopted this 3rd day of October 2006

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JOHN FORTENBERRY, *Chair*
Arkansas Teacher Retirement System

ARKANSAS RELATED INVESTMENT PROGRAM

CRITERIA/PROCEDURES

The Arkansas Related Investment Program was established by Act 412 of 1985 (A.C.A. §24-2-608). The purpose of the Act is to favorably impact the economic condition of and maximize capital investment in the State of Arkansas when appropriate investment alternatives are available. Such investments are subject to the Prudent Investor Rule.

I. LOANS

A. LOAN APPLICATIONS - CRITERIA

The following criteria will be used by the Arkansas Teacher Retirement System to screen loan applications. Loan applications must conform to these criteria before they will be submitted to the Staff Review Committee. It should be understood that these criteria are minimum requirements and meeting them will not insure approval by the Staff Review Committee.

Loan applications will be considered only for projects located in the State of Arkansas.

I. Minimum Debt Ratio on Loans

TYPE	RATIO
A. Apartments	1.2
B. Hotel/Motel	1.4
C. Manufacturing/Retail	1.2
D. Medical/Health	1.2
E. Office Building/Retail	1.2
F. ADFA/Special Purpose Private Placements	1.2

II. Loan Size

Loans will be considered within a range from $1,000,000.00 to $50,000,000.00.

III. Terms

The terms of the loans will be 5 years, with an amortization of 15-

years to 20-years. In no case can amortization exceed the economic life of the assets. A 7-year call will be considered for variable rate requests.

IV. Interest Rate

The interest rate will be determined by market conditions and the merits of the project. The Staff Review Committee will establish an initial interest rate for the purposes of underwriting. The rate shall be no lower than seven and one-quarter percent (7.25%). Fixed rate requests will be 250 basis points over the 5-year U.S. Treasury Note.

Variable rate requests will be 225 basis points over the 5-year Treasury Note for 5-year calls, and 250 basis points over the 5-year U.S. Treasury for 7-year calls. The rate will be adjusted to maintain the original basis point spread every 12 months, from inception to call. Adjustments made from inception to call will not exceed 300 basis points, or the Arkansas usury maximum.

V. Prepayment Penalty

No additional payments may be made on the principal of the note, except that the maker, on any interest payment date, may prepay, in whole but not in part, the entire principal owed with accrued interest, plus prepayment fees in the manner as follows:

A. Seven-year calls: Five percent (5%) of the unpaid balance if prepaid during the first year.
   Five year call: Four percent (4%) of the unpaid balance if prepaid during the first year.
B. Seven year call: Four percent (4%) of the unpaid balance if prepaid during the second year.
   Five year call: Three percent (3%) of the unpaid balance if prepaid during the second year.
C. Seven year call: Three percent (3%) of the unpaid balance if prepaid during the third year.
   Five year call: Two percent (2%) of the unpaid balance if prepaid during the third year.
D. Seven year call: Two percent (2%) of the unpaid balance if prepaid during the fourth year.
   Five year call: One percent (1%) of the unpaid balance if prepaid during the fourth year.
E. No prepayment fee if prepaid after the fourth year.

VI. Fees

The loan applicant will be responsible for any fees incurred in obtaining a loan from the Arkansas Teacher Retirement System. These fees may include but are not necessarily limited to:

A. A check made payable to the underwriter of ATRS' choice in the amount of not less than $2,000.00.
B. Charges for any additional appraisals or reviews deemed necessary by ATRS.
C. All fees charged by the system's legal counsel pertaining to the loan document preparation and related to preparation for, and actual closing of, the loan.
D. Good Faith fee of 1% of the loan amount that will be due at the time of commitment and refunded at the time of loan closing.

All loans will be closed by an Abstract Company of ATRS' choice or at ATRS' counsel's office.

VII. Net worth

The combined net worth of the Borrowers must exceed the loan amount. If additional money is withdrawn to pay other debts then the Borrower's net worth must exceed the loan amount by 200%.

VIII. Loan To Value

The loan to value ratio must not exceed 80%. The net income should exceed debt service at the time of funding. If additional monies are withdrawn, then the loan to value must not exceed 65%. The occupancy rate should be in the 85% to 90% range. Funding is to pay off debt only.

IX. Debt To Equity

The debt to equity ratio must not exceed 4 to 1.

X. Appraisal

All loan applications must contain an appraisal performed by a State certified appraiser approved by the ATRS Supervisor/Real Estate. The appraiser must also have an appropriate certification from a recognized appraisal organization. The applicant is

responsible for verifying ATRS approval of the appraiser with the ATRS Supervisor/Real Estate.

XI. Assumption

The Investment Committee will consider a one-time assumption with a 2% fee. All expenses are to be paid by the assuming party. The assumption must meet all requirements of a new loan.

XII. Required Collateral

Any combination, or all of the following, may be required by ATRS before consideration of a loan request.

A. A first mortgage on all property involved in the project.
B. Lease and rent assignments.
C. Life insurance to key individuals. Insured amounts must be equal to two (2) years of loan payments.
D. If deemed necessary, disability insurance on certain professionals.
E. Personal guarantees of the individuals, general partners of partnerships, corporate officers, and major shareholders of corporations.
F. Certificate of Deposit.
G. Letter of Credit.

XIII. The following documents are required for a complete loan application.

A. A current appraisal – by a certified, ATRS-approved appraiser.
B. An environmental clearance report on hazardous or toxic materials on the site.
C. Alta mortgage title insurance and boundary survey.
D. Term sheet, which reflects loan amount, terms of amortization, project summary, and any other relevant information.
E. A copy of all leases.
F. A current rent-roll.
G. Two to five years of operating statements (balance sheet and income statement prepared by a CPA).
H. Color photographs of the property, both interior and exterior.

I. Current, signed, personal financial statements of all borrowers must not be over six months old and must be prepared by an accounting firm.

J. Resumes and bank references on all borrowers.

K. Financial projections of the project.

L. Franchise agreement (if franchised).

K. History

XIV. Exceptions

The Investment Committee on an individual basis must approve exceptions to the Staff Review Committee procedures.

XV. If the loan request involves both a loan and an equity venture or purchase and passes the Staff Review Committee, the following will be required before the loan can be presented to the Investment Committee. It is the applicant's responsibility to contact the Real Estate Underwriter and discuss the following requirements after the request has been through the Staff Review Committee.

A. An Engineering report is to be completed and reviewed by the Real Estate Underwriter.

B. An Environmental study, at a level to be determined by the Real Estate Underwriter, is to be completed and reviewed by the Real Estate Underwriter.

BORROWERS SHOULD BE AWARE THAT ATRS IS A STATE AGENCY AND IS GOVERNED BY THE FREEDOM OF INFORMATION ACT. BORROWERS' RECORDS CAN BE MADE PUBLIC UPON A PROPER REQUEST SENT TO THE AGENCY.

B. LOAN APPLICATIONS – STAFF REVIEW COMMITTEE/INVESTMENT COMMITTEE PROCEDURES

The initial loan request package will be prepared and presented to the Arkansas Teacher Retirement System based on criteria for the Arkansas Related Investments Program provided to the broker, as set forth in I.A. Loan Applications - Criteria.

The package will be submitted to the ATRS Supervisor/Real Estate for initial screening. The Supervisor will critique the package to see that it meets the

criteria set forth by ATRS. This critique will be performed strictly for the purpose of notating any policy violations or obvious weaknesses. The package will then be presented for consideration to the Staff Review Committee consisting of the ATRS Director, ATRS Supervisor/Real Estate and the Deputy Director of Finance. The package will be screened for very basic requirements, such as Arkansas location or ownership, net worth, loan to value and debt service. The Staff Review Committee will also determine the interest rate.

If the Staff Review Committee approves the package to be underwritten, the broker will be notified. At that time, the borrower is required to send a check for not less than $2,000.00 to ATRS. The package and check will be delivered to an ATRS approved underwriter with no interest in the loan request package by ATRS for review and recommendation. The underwriter will perform the necessary due diligence to ensure that all information provided to the System is accurate. This will include, but not be limited to, appraisals, environmental reports, engineering reports if required, additional financial statements, tax returns, etc.

If the loan request package receives a positive recommendation from the underwriter, the broker will be notified and the package will be scheduled for presentation at the next scheduled Investment Committee meeting. (See I.A.XV for additional requirements if the loan request involves both a loan and an equity venture or purchase). An executive summary of all material that has been acquired will be mailed to the members of the Committee and all underlying material will be available for inspection by Committee members.

The ATRS staff and the underwriter will present the investment, along with a recommendation, to the Investment Committee and, if necessary, to the Board of Trustees.

A loan in the amount of $5 million or less must receive the approval of the Investment Committee only; a loan in an amount over $5 million must receive approval from the ATRS Board of Trustees following a recommendation by the Investment Committee.

Following appropriate approval of a loan, a Commitment Letter will be sent to the borrower outlining all the provisions of the loan agreement. If the borrower agrees to the provisions of the Commitment Letter, the Letter will be signed and returned to ATRS with a check for 1% of the loan amount which will be held in escrow by ATRS' contracted attorneys until closing. Once the loan is closed, this 1% will be refunded to the borrower.

The ATRS Supervisor/Real Estate will work with ATRS' contracted attorneys to complete the due diligence and documents necessary to close the

transaction. Closing of the transaction will be handled by ATRS' contracted attorneys.

II. PURCHASE OF REAL PROPERTY

Currently under moratorium.

Criteria and procedures will be developed.

III. SALE OF REAL ESTATE INTERESTS

Criteria and procedures are being developed.