MINUTES
ARKANSAS TEACHER RETIREMENT SYSTEM
BOARD OF TRUSTEES-CALLED TELEPHONIC

Friday, July 20, 2018
10:15 a.m.
1400 West Third Street
Little Rock, AR 72201

ATTENDEES

Board Members Present
Jeff Stubblefield, Chair*
Danny Knight, Vice Chair*
Anita Bell*
Jason Brady, designee for Hon. Dennis Milligan*
Kathy Clayton*
Kelly Davis*
Susannah Marshall, designee for Candace Franks*
Andrea Lea, State Auditor*
Bobby Lester*
Robin Nichols*
Deborah Thompson*
Janet Watson*

Board Members Absent
Dr. Richard Abernathy
Johnny Key, Education Commissioner

***** ***via telephone***

ATRS Staff Present
George Hopkins, Executive Director
Laura Gilson, General Counsel
Rod Graves, Deputy Director
Rett Hatcher, Deputy Director
Manju, Director, Information Systems
Mike Lauro, Information Systems Manager
Jerry Meyer, Manager, Real Assets
Martha Miller, Staff Attorney
Kevin Odum, Attorney Specialist
Tammy Porter, Executive Assistant
Clint Rhoden, Director of Operations
Joseph Sithong, Software Support Analyst

Guest Present
Sean Barron, Simmons Bank
Michael Bacine, Franklin Park*

Reporters Present
Mike Wickline, AR DemGaz

I. Call to Order/Roll Call. Mr. Jeff Stubblefield, Chair, called the Board of Trustee meeting to order at 10:42 a.m. Voice roll call was taken. Dr. Abernathy, Mr. Black and Mr. Johnny Key were absent.

II. Adoption of Agenda

Ms. Nichols *moved* for *adoption* of the Agenda. Mr. Lester s*econded* the *motion,* and the Board *unanimously approved the motion.*

III. Executive Summary. The Executive Summary was provided for reference with no questions or expansions on the written summary.

IV. Investment Committee Report. Ms. Robin Nichols**,** Chair, gave a report on the Investment Committee Meeting.

A. Private Equity.

1. **Recommendation to Commit up to $30 Million Dollars in Thoma Bravo Fund XIII, L.P., a Private Equity Buyout Fund that Invests in Middle to Large Market Software Companies. Founded in 2007 and based in both Chicago and San Francisco, Thoma Bravo is a very experienced manager that acquires software companies in the U.S.** Mr. Michael Bacine presented that recommendation to commit $30 million dollars in Thoma Bravo Fund XIII, L.P. He stated that the firm is led by six principals, Orlando Bravo, Scott Crabill, Seth Boro, Holden Spaht, Carl Thoma, and Lee Mitchell. The principals have an average of 23 years each in the private equity industry and an average of 17 years each with the General Partner or its predecessor firm, Thoma Cressey Bravo. ATRS invested in Thoma Bravo Fund XI in 2014 and Thoma Bravo Fund XII in 2016. The general partner's four funds prior to Thoma Bravo Fund XII have generated returns ranging from 21% to 38% net IRR. Thoma Bravo Fund XII is still young but is on track to preform very well.

   The manager typically pursues a buy and build strategy seeking middle market and large companies where profitability can be significantly increased. Once operating improvements have been completed, Thoma Bravo seeks to make add-on acquisitions to rapidly grow portfolio companies to increase scale and attractiveness to strategic buyers. The general partner will primarily seek opportunities in the application, infrastructure and security software industries with a secondary focus on technology-enabled service industries. ATRS also invested in two Thoma Bravo Discover funds that employ a similar strategy in lower middle market businesses. This fund will provide additional investment opportunities in the software industry with a highly sought-after manager for ATRS. Both Franklin Park and ATRS staff recommend an investment in Thoma Bravo Fund XIII, L.P. with a commitment of up to $30 million dollars.

Mr. Hopkins stated staff concurs with the recommendation.

Ms. Nichols *moved* to *adopt* Resolution 2018-31, to Commit up to $30 Million Dollars in Thoma Bravo Fund XIII, L.P., a Private Equity Buyout Fund that Invests in Middle to Large Market Software Companies. The Board *unanimously adopted the Resolution*.

B. Arkansas Related

1. Recommendation to Make a Contingent Backup Commitment that Could Result in a Purchase of a Promissory Note of $150 Million Dollars Plus all Accrued and PIK Interest through a Promissory Note Purchase Agreement/Guaranty with Global Infrastructure Partners (GIP) to Purchase the Current GIP Promissory Note with Highland Pellets, LLC, a Wood Pellet Manufacturing Plant Located in the Pine Bluff Industrial Complex Adjacent to White Hall, Arkansas, in Exchange for a $15 Million Dollar Purchase Agreement Fee, with Imminent Need.

Mr. Hopkins stated that the ATRS Board approved a commitment of up to $25 million dollars for 31% equity ownership of Highland at the July 19, 2016 meeting. The Board also approved a $26 million dollar loan to Highland at the September 8, 2017 meeting. Commissioning of the plant is nearing completion and plant production is ramping up. As the plant nears full commissioning and production increases, Highland is reviewing opportunities to refinance some of its existing debt.

The initial money for developing the plant and construction was provided by GIP. The GIP note is the senior secured note for the project. The GIP loan was intended for financing through the construction and commissioning phases of the plant and those phases are winding down. At the same time the commissioning has taken longer than originally expected from the original projections. The original projections and loan timelines put GIP in a position in the near future of requiring the equipment vendor to pay the loan if certain date hurdles were not met. Those older agreements have placed undue pressure on the equipment vendor, the investors, including ATRS, and on GIP. Negotiations have been underway for several weeks in order to eliminate the pressure the “put back” provision in the loan agreement has placed into the deal that jeopardizes the alignment of interest and the success of the plant. The desire of all parties to eliminate an unanticipated financial disruption due to longer than anticipated commissioning has provided ATRS an opportunity to be well compensated for undertaking the purchase/guaranty of a GIP loan that in all likelihood will be refinanced in less than 9 months. This would eliminate the obligation that would be undertaken to obtain the $15 million dollar purchase agreement fee. The Highland plant is in the final stages of being completed and production levels have been around 70% of the expected final production rates meaning the commissioning phase is almost over. More recent data shows production in the 90 to 95% range in the last few days. Highland had anticipated and planned to maintain its existing financing with GIP until sometime in 2018 and with commissioning and production reaching the final stages, Highland is already engaged in positive refinancing negotiations with new lenders.

The refinancing of the debt with GIP presents investment opportunities for ATRS. The catch point between the equipment vendor and GIP has the equipment vendor ready to step up to provide capital to the Highland project totaling $68 million dollars. The $68 million dollars to be provided by the equipment vendor would be used for the $15 million dollar premium that ATRS would receive to backstop the promissory note, to additionally fund the reduction of the GIP loan obligation by approximately $20 million dollars, providing funding to pay down an additional $15 million dollars on the $26 million dollar ATRS loan to Highland, to provide approximately an $8 million dollar debt service reserve and working capital fund for Highland to even better position the GIP loan, and $10 million dollars for Highland to complete all plant modifications that have been recommended by a nationally recognized timber products engineering firm that Highland has engaged to ensure the plant hits and maintains production at 100% of nameplate capacity.

The capital provided by the equipment vendor would be paid in tranches with part of the first payment of the $34 million dollar tranche used to pay the entire $15 million dollar ATRS purchase agreement fee, $10 million dollars used to pay down the GIP loan, and the remaining $9 million dollars being applied to the other plant requirements at Highland mentioned above. The remaining $34 million dollars of the total $68 million dollar payment by the equipment provider would be paid in four equal installments of $8.5 million dollars at intervals of 30, 60, 90, and 120 days. The payment stream of $8.5 million dollars would be prorated to the various categories listed in the above paragraph. At some point in the future, if the equipment vendor meets all terms and operational requirements, the equipment vendor would receive back about $7 million dollars from Highland that would be essentially retainage.

The plant operating even at 70% of capacity keeps Highland in a good financial position. The recommended plant modifications have been tested on one of the four lines at Highland in the last two weeks. That line has consistently operated at 100% of capacity. Another line that was carefully monitored has operated at approximately 70%. Using that operational insight, recent operation has shown the 90% to 95% results mentioned above. The expected cost of the modifications to bring the plant up to 100% of nameplate production is expected to cost less than $10 million dollars. This $10 million dollar allocation would also be used for a plant enhancement to double the capacity of a linear chip stacker and reclaimer to ensure chip storage during unseasonal weather and provide adequate contingency reserves. The doubling of the linear stacker also allows increased production since leaving wood chips on the yard longer reduces the moisture content of the chips so that drying time in the equipment is reduced to allow higher feed volumes and more production. The remaining $8 million dollars would be used for operating capital, additional debt service reserve, or as needed by Highland.

The availability of this additional capital places Highland and ATRS in a favorable position. ATRS is paid $30 million dollars, $15 million dollars (up to $5 million will be recallable by Highland for any contingency) to reduce the $26 million dollar ATRS loan, and $15 million dollars for the contingent promissory note purchase agreement/guaranty. The amount ATRS would have to pay to acquire the promissory note is reduced $20 million dollars at close. That is $20 million dollars plus interest that is no longer a liability to the equity owners of

Highland, including ATRS. An extra $8 million dollars is provided to Highland to cover all loan payments that further protects ATRS and adds value to ATRS as an equity owner. Finally Highland gets an improved plant that should ramp up to full nameplate capacity within a fairly short period of time, estimated to be 6 months. The additional chip storage that the agreement funds gives Highland chip storage to operate even under severely wet or inclement periods that occasionally shut other similar facilities down and enhances production. The total linear stacker chip storage capacity at Highland would be 33,000 tons. The stored wood chips are what are fed into the equipment to create wood pellets. The contingency reserve on the plant modifications and the increased capacity of the reclaimer provides a very strong cushion to implement the improvements.

As to input to the plant, Highland has had great success in obtaining wood fiber at lower cost than originally projected in its production modeling. The purchaser of the wood pellet production has provided Highland assurances that its offtake agreements are in good stead with the view of the offtake purchaser to maintain its long term offtake agreements well into the future. ATRS is agreeing to purchase the GIP note at par value if that ever happened. That par value will be at least $20 million dollars less due to a pay down on the note at closing. In addition very positive negotiations are underway to refinance all or a substantial sum of the GIP note within a year. Once the note is refinanced, the ATRS contingent purchase agreement is voided since the note would be paid off in the refinancing. ATRS would have no repurchase obligation on any new promissory note.

To incentivize Highland to eliminate the purchase/guaranty obligation of the GIP note, Highland has agreed that if the GIP note is not refinanced by August 1, 2019, then the ATRS equity in Highland moves from 31% to 36% with the other equity owners being diluted on a prorata basis. Based on current discussions with potential lenders, refinancing the GIP note within a short amount of time is appearing to be very positive with a lower anticipated interest rate than the current 10.5% interest rate on the GIP note.

Ultimately a longer than anticipated commissioning period provided others the incentive to improve Highland's plant capabilities, to improve the debt and equity position of Highland while providing ATRS $30 million dollars including $15 million dollars for what is expected to be a short term contingent loan purchase obligation. The commissioning now has the plant operating at a reasonable capacity with third party engineering allowing the plant to quickly reach nameplate capacity with ATRS in a position to obtain more equity if refinancing of the GIP note is not completed on a time schedule as anticipated. The total transaction involves $68 million dollars. This executive summary contains the expected allocation of the $68 million dollars to resolve the issues concerning the commissioning period. The $15 million dollar payment to ATRS for the promissory note purchase agreement/guaranty will not be modified however there may be some modification to the remaining allocation amounts based upon updated information to best finalize the transaction.

ATRS staff has worked over the past several months to analyze this potential promissory note purchase agreement with GIP. Simmons Bank (Simmons) was also hired to perform due diligence on the proposed investment. The recommendation of Simmons and ATRS staff is a commitment of up to $150 million dollars plus all accrued and PIK interest for a promissory note purchase agreement/guaranty with GIP for the current promissory note with Highland Pellets, LLC, the parent company of the wood pellet manufacturing plant located in the Pine Bluff Industrial Complex adjacent to White Hall, Arkansas. The investment will provide ATRS a $15 million dollar payment to ATRS for the contingent agreement, a $15 million dollar payment on the existing ATRS note and the potential for ATRS to acquire more equity in the plant based on the timing of the refinancing of the Highland debt. Plus the other payments either enhance the value of the equity of ATRS or provide funding to pay the debts of Highland. The resolution for this proposed investment, like others of this type, allow for distributions from the investment to be reinvested or recalled by the investment using the same process as in other investments. Since the only close for this investment opportunity is expected to take place before the next scheduled meeting of the Arkansas Legislative Council (ALC), Imminent Need is being requested.

Mr. Hopkins stated staff concurs with the recommendation.

Ms. Nichols *moved* to *adopt* Resolution 2018-32, to Make a Contingent Backup Commitment that Could Result in a Purchase of a Promissory Note of $150 Million Dollars Plus all Accrued and PIK Interest through a Promissory Note Purchase Agreement Guaranty with Global Infrastructure Partners (GIP) to Purchase the Current GIP Promissory Note with Highland Pellets, LLC, a Wood Pellet Manufacturing Plant Located in the Pine Bluff Industrial Complex Adjacent to White Hall, Arkansas, in Exchange for a $15 Million Dollar Purchase Agreement Fee, with Imminent Need.The Board *unanimously adopted the Resolution*.

V. Adjourn.

Mr. Knight moved to *adjourn* the Board Meeting. Ms. Nichols *seconded* the *motion*, and the Board *unanimously approved the motion.*

Meeting adjourned at 10:47 a.m.

George Hopkins,
Executive Director

Mr. Jeff Stubblefield, Chair
Board of Trustees

Tammy Porter,
Recorder

Date Approved