

**Regular Meeting  
Board of Trustees**

**August 13, 2002**

*The Board of Trustees of the Arkansas Teacher Retirement System reconvened on Tuesday, August 13, 2002, at 9:00 a.m. The meeting was held in the ATRS Board Room, 1400 West Third, Little Rock, Arkansas.*

**Members of the Board Present:**

Linda Parsons, Chair  
Charles Vondran, Vice Chair  
Winfred Clardy  
Hazel Coleman  
Charles Dyer  
Dr. Paul Fair  
John Fortenberry  
Ann Harbison  
Mary Harris  
Betty McGuire  
Raymond Simon  
Frank White

**Members of the Board Absent:**

Jimmie Lou Fisher  
Gus Wingfield

**Staff Present:**

Wayne Greathouse, Interim Executive Director  
Michael Ray, Interim Deputy Director  
Gail Blair, Manager, Data Processing  
Dena Dixon, Manager, Membership & Payroll  
Tammy Medlock, Administrative Assistant  
Hugh Roberts, Retirement Fund Investment Supervisor  
Bernice Smith, Manager, Accounting  
Barbara Waldrop, Manager, Pre-Retirement Education

**Others Present:**

Randy Abner, Optdata, Inc.  
Wesley Brown, Arkansas News Bureau  
Darrell Dover, Dover Dixon Horne, PLLC  
Tom Ferstl, Ferstl Enterprises  
Charles Knox, Arkansas Association of Educational Administrators  
Bobby Lester, Retiree  
Don Lewis, Optdata, Inc.  
Shirley Matheny, Retiree  
James McGuire, Guest of Betty McGuire

## **Others Present (Cont'd):**

Jan Meyer, Flake & Kelley Management  
Don Roberts, Arkansas Retired Teachers Association  
Carol Stapleton, Legislative Council  
Leonard Venable, Office of the State Treasurer  
Mike Wickline, AR Democrat-Gazette

## **VIII. Roll Call**

The minutes were recorded by Tammy Medlock of the Teacher Retirement staff.

## **IX. Adoption of Agenda**

The agenda item, "Next Regular Meeting Date(s)" was added to the agenda; the Retirement Village topic under "New Business" was moved to item B of the Real Estate Committee report; a new item "Travel Resolution," was added under "New Business." Mr. Vondran made a motion to adopt the agenda as revised. The motion carried.

## **X. Next Regular Meeting Date(s)**

Ms. Harbison made a motion to change the next regular meeting date(s) to October 21-22 2002. The motion carried.

## **XI. Public Comments on Agenda Items**

**Don Roberts, Arkansas Retired Teachers' Association (ARTA).** Dr. Roberts stated ARTA does not want T-DROP eliminated from ATRS, but desires the present program to be adjusted in the next legislative session.

## **XII. Investment Committee Report - Charles Vondran, Chair**

The next meeting of the Investment Committee is scheduled for Monday August 26, 2002, at 1:00 p.m. The Investment Committee meeting scheduled for Monday, October 21, will convene at 11:00 a.m.

## **XIII. Real Estate Committee Report – Tom Ferstl, ATRS Real Estate Manager**

**Alan Kilgore Purchase of Riley South.** Mr. Dover has prepared a draft proposal agreement.

**Northridge Renovations.** Mr. Dyer made a motion to approve \$250,000 for renovations to the Northridge facility. The motion carried. (*Attachment B – Revised Amount*)

**West Memphis Property.** Mr. Ferstl will request the seller correct the drainage problem before winter. He also indicated all extraordinary expenses incurred by ATRS to inspect the property would be billed to the seller.

**Jonesboro Property.** Mr. Fortenberry made a motion to approved Mr. Ferstl's recommendation to list the property with Flake & Kelley of Little Rock, and Halsey Real Estate in Jonesboro. The motion carried. Mr. Ferstl will negotiate realtor fees.

**Victory Building.** Mr. Ferstl reported 102,000 square feet are leased. By common consent, the board authorized Mr. Ferstl to dedicate space that would be leased to lobbyists.

**Leasing Agreement with Financial Centre II .** Mr. Ferstl reported there is no working agreement with Financial Centre II for the referral of Victory Building prospects. By common consent, the Board authorized Mr. Greathouse to pursue the matter.

**Retirement Village Final Invoices.** Dr. Fair made a motion to authorize Mr. Ferstl and Mr. Dover to investigate ATRS' liabilities and to make a recommendation to the Board. The motion carried. Ms. Parsons referred the issue to the Investment Committee.

**Lindsey Projects.** Dr. Fair made a motion to refer the project to the Investment Committee for consideration and final action. The motion carried.

#### XIV. Policies Committee Report – Dr. Paul Fair, Chair

##### A. Policy Changes

Page 33-42. **Election Policies.** The following sentence in paragraph one, page 34, under the heading, "Board of Trustees Composition," was revised to read, "Eleven members shall be elected to the Arkansas Teacher Retirement Board of Trustees, eight seven of whom shall be active members of the system with at least five years of credited service in force, one who is a member of a racial ethnic group and is either an active or retired member, and three who are retirant members retired from the system and reside in the State of Arkansas." Dr. Fair made a motion to adopt the policies as revised. The motion carried.

Page 29-30. **Draft Legislation Proposal (Policies Committee minutes July 15, 2002, Attachment A).** By common consent, the Board agreed the following would be stricken from the draft, "*Each trustee shall continue to serve until his successor is elected and has qualified.*" Dr. Fair made a motion to approved the draft as revised. The motion carried.

Page 27. **Real Estate Manager Limitations.** Dr. Fair made a motion to approve Item #4, "Real Estate Manager Limitations," recorded in the Policies Committee minutes of July 15, 2002. The motion carried.

Page 31-32. **Non-contributory Policy Change.** Dr. Fair made a motion to approve the policy change as presented. The motion carried.

B. Minutes of July 15, 2002.

Upon Mr. Fortenberry's request, the board by common consent agreed to strike the entire paragraph entitled, "Retirant Trustees," under the item "In other business" in the minutes.

**XV. Legislative Committee Report – Winfred Clardy, Chair**

A. Minutes of July 15, 2002

**XVI. Teacher Retirement System Reports**

A. Medical Board Summary Report – Michael Ray

Mr. Vondran made a motion to approve the report for June 12, 2002, as presented. The motion carried.

B. Personnel Report – Michael Ray

Mrs. Coleman made a motion to approve the report for August, 2002, as presented. The motion carried.

C. Membership & Payroll

D. Arkansas Related Investments

E. Investment Summaries

F. Financial Statements

**XVII. New Business**

A. ATRS Budget for 2003-2005

B. Discussion – New Salary for Executive Director

Mr. Greathouse reported the new salary for the Executive Director of \$150,000 would be introduced at the Joint Budget Committee meeting scheduled for October 16.

C. Discussion – Dinners Following Regular Board Meetings

Mr. Vondran made a motion that the system pay for board members and staff members, and money managers would pay for themselves and guests. The motion did not pass.

Mrs. McGuire made a motion that the Board returns to having dinners the first night of a Board meeting, and that money managers divide the cost of the meal. The motion did not pass.

Ms. Parsons indicated the item would be addressed again at the October Board meeting.

D. T-DROP Study Responses to RFP

Ms. Parsons assigned to the Oversight Committee the review and selection of a company to conduct the study.

E. Discussion – Alternative Investments Report

F. Travel Resolution (*Attachment C*)

Mr. Dyer made a motion to adopt the travel resolution for 2002 as presented. The motion carried.

**XVIII. Executive Director's Comments**

**In other business:**

**Executive Session.** The Board convened in executive session to discuss personnel and employing personnel. The Board reconvened in open session. No action was taken.

*As there was no further business to consider, Mr. Vondran made a motion to adjourn. The motion carried and the meeting adjourned at 1:00 p.m.*

*Linda Parsons*

\_\_\_\_\_  
Linda Parsons, Chair

\_\_\_\_\_  
Wayne Greathouse, Interim Executive Director,  
Secretary to the Board

10-23-02

\_\_\_\_\_  
Date

# ENNISKNUPP

## MEMORANDUM

August 8, 2002

To: Board and State of the  
Arkansas Teacher Retirement System

From: Steve Cummings, CFA  
Patrick J. Kelly, CFA

Re: Summary of Our Recommendations

We have made several recommendations that have been approved by the Trustees:

1. Terminate Zurich Scudder (replaced by Putnam)
2. Terminate Vanderbilt (replaced by Western Asset Management)
3. Adopt manager presentation guidelines

There are several recommendations we have made that were approved but we understand are being reconsidered:

1. Mitigate significant bias towards small-capitalization and value-oriented domestic stock
2. Introduce a domestic equity passive allocation of up to 40% (30% was approved) of that asset class
3. Reduce the number of domestic stock managers, namely:
  - a. Munder Capital
  - b. Invesco
  - c. Phoenix
  - d. Rothschild

Based on our recent review of the investment program, we have some additional recommendations at this time:

1. Reclassify some existing assets:
  - a. Nicholas Applegate's convertible bond portfolio as equity investment
  - b. Mezzanine financing as a component of alternatives
  - c. Diversified real estate (excluding Arkansas related) as a separate asset class
2. Modify the Statement of Investment Policy
3. Adopt guidelines for each manager portfolio
4. Adopt narrower rebalancing ranges and a rebalancing policy
5. Initiate manager reporting of soft dollar use



Arkansas  
Teacher  
Retirement  
System

*Attachment B*

1400 West Third, Little Rock, AR 72201  
Phone (501) 682-1517 or (800) 666-2877  
Website - <http://www.atrs.state.ar.us>  
Email - [info@atrs.state.ar.us](mailto:info@atrs.state.ar.us)

EMAIL

08/13/02 03:37 PM

From: Hugh Roberts

To: ATRS Board of Trustees

Cc: Wayne Greathouse, Tom Ferstl, Darrell Dover, Tammy Medlock

Subject: Budget for A & D Wings on Northridge

\*\*\*\*\*

Ladies & Gentlemen:

When I presented you with a figure for continued renovation at Northridge, I quoted you \$250,000.00. In looking over my notes this afternoon I discovered an error that was my fault. There are actually two parts to Mr. Kilgore's request. Listed below is each part of Mr. Kilgore's proposal along with the cost.

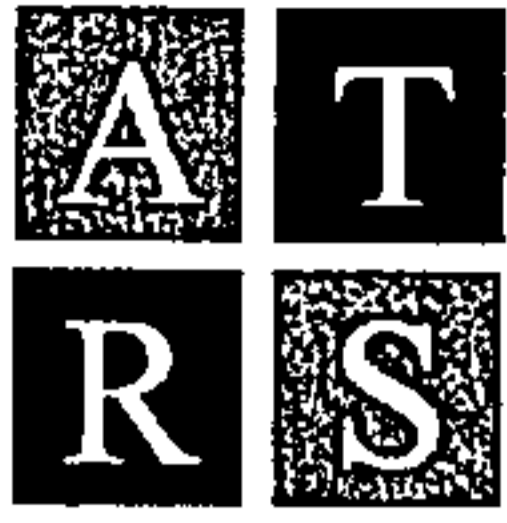
1. The cost of obtaining the Physical Plant/Mechanical Items for the two wings-\$234,780.00
2. Total for labor and materials needed by the contractor to install the items-\$212,974.00.

At the meeting today, the Board approved the additional \$250,000.00 I initially quoted. However, as you can see, the actual cost will be \$447,754.00.

I am asking each Board member to please respond to me by e-mail their approval or non-approval of the new amount. If you would like to see copies of the proposals, I'll be happy to fax or mail them to you. This figure is part of the overall cost of approximately \$1.8 million I quoted this morning. If the Board approves this, I will ask Tammy to include this in the minutes as an item approved by e-mail with full Board approval to be obtained at the next Board meeting. Wayne has already signed the agreement but I will not send it back to Mr. Kilgore until I have heard from you. The stipulation made by the Board as to no other approvals of renovations being done until a formal agreement is in place would still stand.

I sincerely apologize for this error and will do my best to be sure it does not happen again.

Hugh A. Roberts  
Retirement Funds Investment Supervisor



Arkansas  
Teacher  
Retirement  
System

*Attachment C*

1400 West Third, Little Rock, AR 72201  
Phone (501) 682-1517 or (800) 666-2877  
Website - <http://www.atrs.state.ar.us>  
Email - [info@atrs.state.ar.us](mailto:info@atrs.state.ar.us)

RESOLUTION

Board Expense Reimbursement  
For 2002

BE IT RESOLVED, *the members of the Board of Trustees of the Arkansas Teacher Retirement System are authorized reimbursement of expenses for attending trustee meetings in accordance with Act 1211 of 1995;*

NOW, THEREFORE, BE IT RESOLVED, *members of the ATRS Board of Trustees may attend and be reimbursed for any two (2) of the following conferences for the calendar year 2002:*

- National Council on Teacher Retirement (NCTR)
- Southern Conference on Teacher Retirement (SCTR)
- National Education Association (NEA) Forum on Retirement
- National Retired Teachers Association (NRTA) Pension Review

BE IT FURTHER RESOLVED, *trustees may be reimbursed expenses for attending two (2) additional retirement education conferences during the calendar year 2002.*

*ADOPTED this 13<sup>TH</sup> Day of August, 2002*

---

Linda Parsons, Chairman  
Arkansas Teacher Retirement System



**RESOLUTION 08.13.02**

**Board Expense Reimbursement For 2002**

BE IT RESOLVED, *the members of the Board of Trustees of the Arkansas Teacher Retirement System are authorized reimbursement of expenses for attending trustee meetings in accordance with Act 1211 of 1995;*

NOW, THEREFORE, BE IT RESOLVED, *members of the ATRS Board of Trustees may attend and be reimbursed for any two (2) of the following conferences for the calendar year 2002:*

- National Council on Teacher Retirement (NCTR)
- Southern Conference on Teacher Retirement (SCTR)
- National Education Association (NEA) Forum on Retirement
- National Retired Teachers Association (NRTA) Pension Review

BE IT FURTHER RESOLVED, *trustees may be reimbursed expenses for attending two (2) additional retirement education conferences during the calendar year 2002.*

*ADOPTED this 13th Day of August, 2002*

*Linda Parsons*

---

Linda Parsons, Chairman  
**Arkansas Teacher Retirement System**

**Regular Meeting  
Board of Trustees**

**August 13, 2002**

*The Board of Trustees of the Arkansas Teacher Retirement System reconvened on Tuesday, August 13, 2002, at 9:00 a.m. The meeting was held in the ATRS Board Room, 1400 West Third, Little Rock, Arkansas.*

**Members of the Board Present:**

Linda Parsons, Chair  
Charles Vondran, Vice Chair  
Winfred Clardy  
Hazel Coleman  
Charles Dyer  
Dr. Paul Fair  
John Fortenberry  
Ann Harbison  
Mary Harris  
Betty McGuire  
Raymond Simon  
Frank White

**Members of the Board Absent:**

Jimmie Lou Fisher  
Gus Wingfield

**Staff Present:**

Wayne Greathouse, Interim Executive Director  
Michael Ray, Interim Deputy Director  
Gail Blair, Manager, Data Processing  
Dena Dixon, Manager, Membership & Payroll  
Tammy Medlock, Administrative Assistant  
Hugh Roberts, Retirement Fund Investment Supervisor  
Bernice Smith, Manager, Accounting  
Barbara Waldrop, Manager, Pre-Retirement Education

**Others Present:**

Randy Abner, Optdata, Inc.  
Wesley Brown, Arkansas News Bureau  
Darrell Dover, Dover Dixon Horne, PLLC  
Tom Ferstl, Ferstl Enterprises  
Charles Knox, Arkansas Association of Educational Administrators  
Bobby Lester, Retiree  
Don Lewis, Optdata, Inc.  
Shirley Matheny, Retiree  
James McGuire, Guest of Betty McGuire

**ENNISKNUPP****MEMORANDUM**

March 28, 2002

To: Board and Staff  
Arkansas Teacher Retirement System

From: David Russell, CFA

Re: Recommendation to establish "Required Investment Manager Presentation Guidelines and Format"

One of EnnisKnupp's duties is to advise and assist ATRS in conducting and documenting their procedural prudence and due diligence. The duty to monitor and review investment managers is one of those tasks. ATRS currently has each of their investment managers make periodic presentations to the Board as part of their due diligence process.

We believe that the investment manager's presentation content should be established by the ATRS Board, not by the managers. In the absence of specific requirements, there is a natural instinct for investment managers to present what they think is important. This may not be the same information that is important and relevant to the ATRS Board. There is also a natural human tendency to accentuate the positive and omit or gloss over any negative information.

The investment manager's time in front of the ATRS Board is a scarce resource that should be carefully managed. It is imperative that the investment manager's communicate the maximum amount of information in the shortest amount of time. Manager's presentations should serve as an opportunity for the Board to review a wide range of key due diligence factors and their written materials should serve as documentation of the Board's ongoing due diligence process.

We recommend that the ATRS Board establish and adopt "Required Investment Manager Presentation Guidelines and Format" as outlined in the attached memo. Each of the elements covered in the attached memo have been carefully designed to assure that each manager's presentation covers, and documents in writing, key due diligence issues. This assures the Board that no key elements are overlooked and forces full disclosure by the managers. Not only is this process a "best industry practice" but the consistency of the reporting format also allows the Board to more easily compare and evaluate the investment managers.

# ENNISKNUPP

## MEMORANDUM

March 28, 2002

TO: All Investment Managers for  
Arkansas Teacher Retirement System

FROM: David A. Russell, CFA

RE: Required Investment Manager Presentation Guidelines and Format

Investment manager monitoring and due diligence is an important fiduciary responsibility. One of the primary methods used to meet this responsibility is your periodic presentation to the ATRS Board. In order to make your time with the Board as productive and informative as possible, the Board has adopted the following "Required Investment Manager Presentation Guidelines and Format."

Both your oral presentation and written materials to the ATRS Board should contain complete information and affirmative statements for each of the following topics. Your presentation and written materials should be organized and presented in the same order as listed below:

1. **Organization and Product Overview.** Provide a brief overview of the current and historic ownership, management, and senior level staffing of your organization. Include your current assets under management, number of clients, and number of investment professionals you employ. Provide information regarding any change in the ownership and/or management structure of your firm in the past three years. Provide an overview of your investment mandate, your investment process, and portfolio management team.
2. **Performance.** Provide performance data relative to the agreed upon benchmark. Performance information should be shown on a calendar quarter-by-quarter basis, net of fees, with annual and cumulative (3-year, 5-year, and since inception, as applicable) summaries compared to the benchmark. Also include relevant portfolio characteristics compared to the benchmark. All data should be as of the most recent calendar quarter-end. You may provide more current up-to-date performance information as supplemental information.

3. **Client and Personnel Turnover.** Provide the number and size of all accounts that were gained or lost in the last three years. Provide the names of all investment professionals who either joined or left your firm in the last three years who were involved in the investment decision making process, research or client servicing function. In addition, please detail any other information about your staff that ATRS would consider material, such as reassignments of responsibility, prospective additions, etc.
4. **Risk Controls and Compliance.** Please describe the process you use to screen the portfolio for compliance with the client's investment policy. Review your overall portfolio constraints, risk controls and monitoring systems.
5. **Investment Guidelines.** Please provide an affirmative statement that your portfolio has been in compliance with all ATRS guidelines. If there have been any violations, disclose the violation and how it was resolved. Are there any provisions in the current ATRS investment guidelines or benchmarks that constrain or impair your investment process?
6. **Regulatory and Legal Issues.** Report on any and all SEC actions, pending or actual litigation, or any other events that ATRS would consider material.
7. **Additional Information.** Please provide any additional information or material that you feel would help ATRS to understand your firm, the investment management team, your investment philosophy, outcomes, the economy, or the market environment.

ATRS should receive 25 copies of your written presentation materials a minimum of 10 days before the meeting for distribution to the Board. Additionally, three copies of your presentation materials should be sent to EnnisKnupp.

If you have any questions regarding these requirements please feel free to contact me at: (312) 715-1700 or [d.russell@ennisknupp.com](mailto:d.russell@ennisknupp.com) Thank you.

**ENNISKNUPP****MEMORANDUM**

March 28, 2002

**To:** Board and Staff  
Arkansas Teacher Retirement System

**From:** David Russell, CFA  
Patrick Kelly, CFA

**Re:** Proposed Revisions to the Classification of Investments within the Overall Asset Allocation

The purpose of this memorandum is to address the classification of investments in the Arkansas Teacher Retirement System. There are three changes we are recommending:

- 1) The two mezzanine managers should be reclassified as alternative investments,
- 2) The alternatives asset class should be segmented to identify different strategies,
- 3) Timberland should be defined as real estate.

The exhibit on the following page details the proposed changes we recommend for the reclassification of investments.

The first proposed adjustment is to classify Blackstone Mezzanine Partners and DLJ Mezzanine investments as part of the alternatives asset class. These two managers do not construct bond portfolios designed to follow the movements of the public fixed income market, but rather make ownership investments or provide debt capital as a source of investment. Mezzanine capital is meaningfully more risky than most publicly traded debt. Although mezzanine financing is typically less risky than private equity, its shares similar characteristics to this asset class and we therefore, recommend classifying it as a mezzanine debt investment. It is without question an alternative type investment. Within the alternatives asset class, we recommend that the managers be classified into three categories: mezzanine debt, domestic private equity and foreign private equity.

Currently the target allocation to alternative investments includes real estate investments, which we feel should have its own target policy allocation that includes Timberland assets.

We feel the suggested remodeling of the asset allocation provides more clarity in the grouping of managers by investment type. Our upcoming Asset and Liability Study will assist in determining the target policy allocations to these asset class divisions going forward.

**Arkansas Teacher Retirement System**  
**Asset Class Remodel**  
**February 28, 2002**

**Original Classification**

	Market Value	Percent	Policy
Alliance Capital Management	\$313,752		
Munder Capital Management	271,147		
Oppenheimer Capital Management	455,788		
INVESCO Capital Management	381,574		
ICC Capital Management	373,118		
Rothschild Asset Management	230,535		
Eubel, Brady & Suttman	157,647		
Aetius Investment Management	158,471		
Trust Company of the West	92,185		
Daruma Asset Management	117,456		
Phoenix Council	90,025		
Kennedy Capital Management	275,961		
<b>Total U.S. Equity</b>	<b>\$2,917,570</b>	<b>40.4%</b>	<b>40.0%</b>
Brinson Partners	\$416,225		
Zurich Scudder	363,887		
AJB Govett	100,181		
<b>Total Non-U.S. Equity</b>	<b>\$880,293</b>	<b>12.2%</b>	<b>17.5%</b>
Regions Bank	\$600,519		
Vanderbilt Capital Advisors	258,513		
Loomis Sayles & Company	430,868		
Hyperion Capital Management	277,729		
Nicholas Applegate	308,483		
Blackstone Mezzanine Partners	25,283		
DLJ Mezzanine	25,249		
<b>Total Fixed Income</b>	<b>\$1,925,544</b>	<b>26.7%</b>	<b>25.0%</b>
DLJ Real Estate Capital I	\$29,056		
Westbrook Fund II	23,104		
Westbrook Fund III	77,305		
Westbrook Fund IV	17,967		
Olympus	42,382		
Hicks Muse Tate & Furst - III	65,906		
Hicks Muse Tate & Furst - IV	85,163		
Hicks Muse Tate & Furst - V	80,573		
Oakhill Capital Partners	36,581		
Westbrook Shp LLC	34,108		
Cypress	15,056		
Diamond State Ventures LP	1,000		
LJM2 Co-Investment LP	5,101		
DLJ Merchant III	54,182		
Hicks Muse Tate & Furst - 21st Century	11,601		
<b>Total Domestic Private Equity</b>	<b>\$389,271</b>	<b>5.4%</b>	
Doughty Hanson	\$61,450		
Doughty Hanson Tech I	9,908		
Doughty Hanson Euro Real Estate	11,316		
Cinven Funds	48,648		
Cinven Funds II	6,699		
Cinven Funds III	3,529		
<b>Total Foreign Private Equity</b>	<b>\$141,550</b>	<b>2.0%</b>	
<b>Total Alternatives</b>	<b>\$720,535</b>	<b>10.0%</b>	<b>10.0%</b>
Wachovia Timberland	\$85,000		
Wachovia Timberland II	145,269		
<b>Total Timberland</b>	<b>\$230,269</b>	<b>3.2%</b>	<b>1.5%</b>
Arkansas Related	\$514,754	7.1%	5.0%
Liquidity Account	\$27,136		
Cash	11,169		
<b>Total Cash Equivalents</b>	<b>\$38,305</b>	<b>0.5%</b>	<b>1.0%</b>
<b>Total Fund</b>	<b>\$7,228,570</b>	<b>100.0%</b>	<b>100.0%</b>

**Revised Classification**

	Market Value	Percent	Policy
Alliance Capital Management	\$313,752		
Munder Capital Management	271,147		
Oppenheimer Capital Management	455,788		
INVESCO Capital Management	381,574		
ICC Capital Management	373,118		
Rothschild Asset Management	230,535		
Eubel, Brady & Suttman	157,647		
Aetius Investment Management	158,471		
Trust Company of the West	92,185		
Daruma Asset Management	117,456		
Phoenix Council	90,025		
Kennedy Capital Management	275,961		
<b>Total U.S. Equity</b>	<b>\$2,917,670</b>	<b>40.4%</b>	<b>40.0%</b>
UBS Global Asset Management	\$416,225		
Zurich Scudder	363,887		
AJB Govett	100,181		
<b>Total Non-U.S. Equity</b>	<b>\$880,293</b>	<b>12.2%</b>	<b>17.5%</b>
Regions Bank	\$600,519		
Vanderbilt Capital Advisors	258,513		
Loomis Sayles & Company	430,868		
Hyperion Capital Management	277,729		
Nicholas Applegate	308,483		
<b>Total Fixed Income</b>	<b>\$1,876,112</b>	<b>26.0%</b>	<b>25.0%</b>
Blackstone Mezzanine Partners	\$25,283		
DLJ Mezzanine	25,249		
<b>Total Mezzanine Debt</b>	<b>\$50,532</b>	<b>0.7%</b>	
Hicks Muse Tate & Furst - III	65,906		
Hicks Muse Tate & Furst - IV	85,163		
Hicks Muse Tate & Furst - V	80,573		
Oakhill Capital Partners	36,581		
Westbrook Shp LLC	34,108		
Cypress	15,056		
Diamond State Ventures LP	1,000		
LJM2 Co-Investment LP	5,101		
DLJ Merchant III	54,182		
Hicks Muse Tate & Furst - 21st Century	11,601		
<b>Total Domestic Private Equity</b>	<b>\$389,271</b>	<b>5.4%</b>	
Doughty Hanson	\$61,450		
Doughty Hanson Tech I	9,908		
Doughty Hanson Euro Real Estate	11,316		
Cinven Funds	48,648		
Cinven Funds II	6,699		
Cinven Funds III	3,529		
<b>Total Foreign Private Equity</b>	<b>\$141,550</b>	<b>2.0%</b>	
<b>Total Alternatives</b>	<b>\$581,353</b>	<b>8.0%</b>	<b>10.0%</b>
DLJ Real Estate Capital I	\$29,056		
Westbrook Fund II	23,104		
Westbrook Fund III	77,305		
Westbrook Fund IV	17,967		
Olympus	42,382		
Wachovia Timberland	85,000		
Wachovia Timberland II	145,269		
<b>Total Real Estate</b>	<b>\$420,083</b>	<b>5.8%</b>	<b>1.5%</b>
Arkansas Related	\$514,754	7.1%	5.0%
Liquidity Account	\$27,136		
Cash	11,169		
<b>Total Cash Equivalents</b>	<b>\$38,305</b>	<b>0.5%</b>	<b>1.0%</b>
<b>Total Fund</b>	<b>\$7,228,570</b>	<b>100.0%</b>	<b>100.0%</b>

EXECUTIVE SUMMARY

In reviewing the ATRS U.S. equity portfolio, we made several important observations: ...

- There is a distinct value and small cap bias in the program. This can lead to extended periods of underperformance if this style falls out of favor. The value-bias has driven most of the component's out/under performance over the past five years.
- The bias is largely driven by the large number of value-oriented stock managers utilized and the allocations between these managers:

Value Managers*Large-Cap*

- Oppenheimer
- Invesco
- ICC Capital

*Mid-Cap*

- Eubel, Brady & Suttman
- Rothschild

*Small-Cap*

- Daruma
- Kennedy
- Phoenix Investment Counsel

Growth Managers*Large-Cap*

- Alliance
- Munder (core/growth)

*Mid-Cap**Small-Cap*

- Aeltus
- TCW

- There are redundancies among the individual styles of managers (i.e. 3 large value managers)
- The ATRS does not use any passive indexing in the U.S. equity component. This is unusual for a plan of this size.

Recommendations

- We recommend that you allocate between 30% and 40% to an index fund benchmarked to the Wilshire 5000 Index.
- We further recommend that you fund this allocation by terminating four U.S. equity managers:
  - **Munder Capital** - Their style plot is close to "core" and would be a prime candidate for replacement by an index fund. Their performance is sub-standard and it has had significant organizational and ownership challenges.
  - **Invesco** - Their mandate is large cap value, which somewhat duplicates the mandate of Oppenheimer and ICC, but with a much poorer track record.
  - **Phoenix** - There are three managers with small-cap value mandates and Phoenix has the least compelling performance.
  - **Rothschild** - There are two managers with mid-cap value mandates. Rothschild has the worst track record.



## EXECUTIVE SUMMARY

---

- Additional measures that can be taken to reduce the value bias are:
  - Allocate a portion of the passive investment to a Russell 1000 Growth Fund
  - Increase the amount of passive management
  - Add a complimentary growth manager

### Benefits of Indexing

- A significant degree of the value and small cap bias would be eliminated.
- Active risk would be reduced by 39% for a 30% allocation to an index fund (from 5.4% to 3.3%) or by 57% for a 40% allocation (5.4% to 2.3%) to an index fund. This will reduce the likelihood of severe underperformance versus the policy benchmark, creating negative attention and possibly financial consequences to the ATRS.
- The saving in direct fees would be approximately \$2.5 million for a 30% allocation or \$3.4 million for a 40% allocation to an index fund. These savings could be estimated as much as 50% higher if you added in the hidden costs of reduced trading costs and future manager turnover.

### Next Steps

A transition of this magnitude (approximately \$1.0 billion) can be completed in an efficient manner in a 4-week time frame. A detailed discussion of this transition is beyond the scope of this report, but we would like to discuss it further should our recommendations be accepted. It will also be necessary to conduct a passive index fund provider search.

## STRUCTURAL ISSUES

### Impact on the Total Fund

It is important to note that since U.S. equities are the largest asset class, the portfolio bias also strongly influences the total plan returns. While in 2000 and 2001 the value bias was a positive contributor, during 1997 (full year equity return data is not available), 1998 and 1999 growth was in favor and the value bias caused substantial underperformance:

### U.S. Equity Returns:

	Total Equity	Russell 3000 Index	Difference
1997 (6 months)	9.3%	11.9%	-2.6%
1998	19.2%	24.1%	-4.9%
1999	9.8%	20.9%	-1.1%
2000	-0.9%	-7.5%	8.4%
2001	-5.3%	-11.5%	6.2%

### Total Fund Returns:

	Total Fund	Benchmark	Difference
1997 (6 months)	5.3%	6.3%	-1.0%
1998	13.5%	18.4%	-4.9%
1999	17.7%	18.0%	-0.3%
2000	-1.7%	-4.9%	3.2%
2001	-3.5%	-6.1%	2.6%

### Recommendation

ATRS should work to eliminate the current value and small cap bias in the portfolio before another style and size rotation occurs. A systematic style and size bias is a structural issue that is under the direct control of the ATRS Board.

Maintaining the current value and small cap bias creates several risks:

- It will continue to periodically result in multi-year periods of substantial over- and under-performance. The under-performance cycle creates the potential for criticism. Additionally if ATRS's budget is subject to "adjustment" based on "objective performance criteria" by the Arkansas legislature, a three-year period like 1997-1999 could possibly have a significant adverse impact on the operating budget.
- The bias dominates investment manager's collective contributions to portfolio returns.
- It is a risk for which you are not compensated by higher long-run returns.

We will discuss alternatives to alleviate this bias later in the report. Alternatives to alleviate the style bias include:

- Add a growth index fund.
- Increase passive.
- Add complimentary active growth stock manager.

## STRUCTURAL ISSUES

---

### Recommendations

- We recommend that you allocate between 30% and 40% to an index fund benchmarked to the Wilshire 5000 Index.
- We further recommend that you fund this allocation by terminating four U.S. equity managers:
  - **Munder Capital** - Their style plot is close to "core" and would be a prime candidate for replacement by an index fund. Their performance is sub-standard and it has had significant organizational and ownership challenges.
  - **Invesco** - Their mandate is large cap value, which duplicates the mandate of Oppenheimer, but with a much poorer track record.
  - **Phoenix** - There are three managers with small-cap value mandates and Phoenix has the least compelling performance.
  - **Rothschild** - There are two managers with redundant mid-cap value mandates. Rothschild has the worst track record.

We provide a more in depth analysis on the individual managers in the last section of this report.

The termination of these four managers will generate approximately \$990 million dollars. This would represent approximately 33% of the U.S. equity portfolio. If a 30% target for an index fund is established the additional funds would be transferred to a growth mandate. If a 40% target for an index fund were established, additional funds would be raised by reducing the allocations of the remaining "value" managers. We highlight the impact these changes will have later on in this section.

### Benefits

- A significant degree of the value and small cap bias would be eliminated (but not all).
- Active risk would be reduced by 39% for a 30% allocation to an index fund (from 5.4% to 3.3%) or by 57% for a 40% allocation (5.4% to 2.3%) to an index funds. This will reduce the likeliness of severe underperformance versus the policy benchmark, creating negative attention and possibly financial consequences to the ATRS.
- The saving in direct fees would be approximately \$2.5 million for a 30% allocation or by \$3.4 million for a 40% allocation to an index fund. These savings could be estimated as much as 50% higher if you added in the hidden costs of reduced trading costs and future manager turnover.

A transition of this magnitude (approximately \$1.0 billion) can be completed in an efficient manner in a 4-week time frame. A detailed discussion of this transition is beyond the scope of this report, but we would like to discuss it further should our recommendations be accepted. It will also be necessary to conduct a passive equity investment provider in the circumstance an allocation to passive is made.

A series of exhibits follow that illustrate each of these benefits.

## STRUCTURAL ISSUES

## U.S. Equity Manager Structure

Managers	Current Structure	Proposed Alternative 1 30% Passive	Proposed Alternative 2 40% Passive
Aeltus	5.6%	5.6%	5.6%
Alliance	11.4	11.4	11.4
Daruma	4.0	4.0	3.3
EBS	5.0	5.0	3.4
ICC	12.5	12.5	9.9
Invesco	12.7	—	—
Kennedy	9.1	9.1	6.8
Munder	9.4	—	—
Oppenheimer	16.1	16.1	13.4
Phoenix	3.1	—	—
Rothschild	7.5	—	—
TCW	3.8	3.8	3.8
Wilshire 5000 Fund	—	30.0	30.0
Russell 1000 Growth Fund	—	2.6 <sup>1</sup>	12.5
<b>Total Equity</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>

The table above highlights our two proposed structures.

In Alternative 1, the assets of terminated managers are transferred to a Wilshire 5000 Index Fund up to 30%. For purposes of style impact, we use a Russell 1000 Growth Index Fund for the assets of the terminated managers in excess of 30%. Therefore in our example, the total actual allocation is 32.6%.

In Alternative 2, additional assets are placed in the Russell 1000 Growth Index Fund from the value managers to further alleviate the small cap value bias. As was in the case in Alternative 1, we kept the excess assets from the terminated managers in the Russell 1000 Growth Fund to bring the actual allocation to passive up to 42.5%.

<sup>1</sup> Used for placeholder for new manager or can be implemented as actual investment, increasing total passive to 32.6%.

### **Others Present (Cont'd):**

Jan Meyer, Flake & Kelley Management  
Don Roberts, Arkansas Retired Teachers Association  
Carol Stapleton, Legislative Council  
Leonard Venable, Office of the State Treasurer  
Mike Wickline, AR Democrat-Gazette

### **VIII. Roll Call**

The minutes were recorded by Tammy Medlock of the Teacher Retirement staff.

### **IX. Adoption of Agenda**

The agenda item, "Next Regular Meeting Date(s)" was added to the agenda; the Retirement Village topic under "New Business" was moved to item B of the Real Estate Committee report; a new item "Travel Resolution," was added under "New Business." Mr. Vondran made a motion to adopt the agenda as revised. The motion carried.

### **X. Next Regular Meeting Date(s)**

Ms. Harbison made a motion to change the next regular meeting date(s) to October 21-22 2002. The motion carried.

### **XI. Public Comments on Agenda Items**

**Don Roberts, Arkansas Retired Teachers' Association (ARTA).** Dr. Roberts stated ARTA does not want T-DROP eliminated from ATRS, but desires the present program to be adjusted in the next legislative session.

### **XII. Investment Committee Report - Charles Vondran, Chair**

The next meeting of the Investment Committee is scheduled for Monday August 26, 2002, at 1:00 p.m. The Investment Committee meeting scheduled for Monday, October 21, will convene at 11:00 a.m.

### **XIII. Real Estate Committee Report – Tom Ferstl, ATRS Real Estate Manager**

**Alan Kilgore Purchase of Riley South.** Mr. Dover has prepared a draft proposal agreement.

**Northridge Renovations.** Mr. Dyer made a motion to approve \$250,000 for renovations to the Northridge facility. The motion carried. (*Attachment B – Revised Amount*)

**West Memphis Property.** Mr. Ferstl will request the seller correct the drainage problem before winter. He also indicated all extraordinary expenses incurred by ATRS to inspect the property would be billed to the seller.

# ENNIS, KNUPP & ASSOCIATES

---

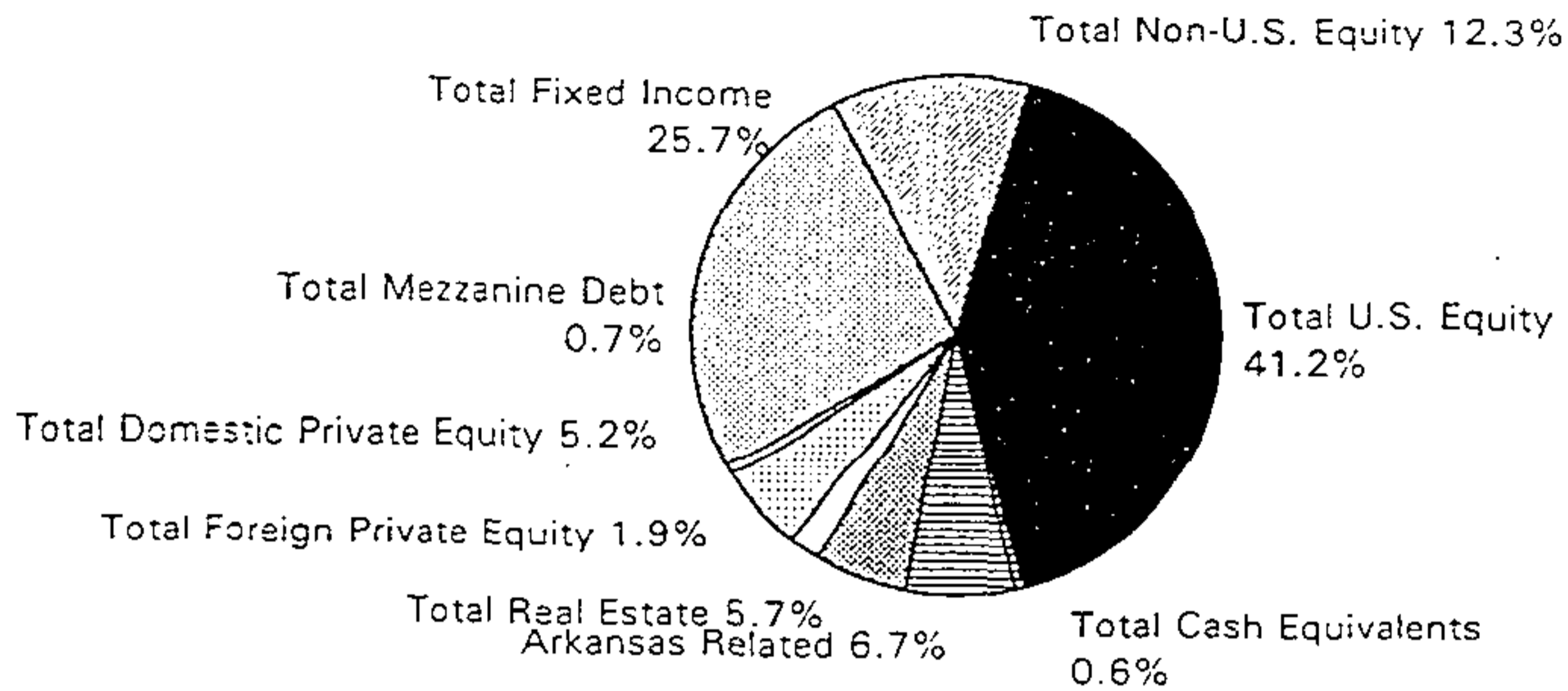
ARKANSAS TEACHER RETIREMENT SYSTEM  
PRELIMINARY UPDATE  
December 2001

# ARKANSAS TEACHER RETIREMENT SYSTEM

## PRELIMINARY UPDATE

## HIGHLIGHTS

### ASSET ALLOCATION AS OF 12/31/01



### RETURN SUMMARY ENDING 12/31/01

	1 Month	1 Year Ending 12/31/01	3 Years Ending 12/31/01	Since Inception	Inception Date
<b>Total Fund</b>	1.4%	-3.8%	4.1%	9.7%	2/29/96
Performance Benchmark*	0.8	-6.4	1.9	9.2	
<b>Total U.S. Equity</b>	2.9	-5.3	4.0	8.9	6/30/97
Russell 3000 Index	1.4	-11.5	-0.3	7.4	
<b>Total Non-U.S. Equity</b>	1.7	-17.3	-1.3	-1.5	6/30/97
MSCI AC World Ex-U.S. Free Index	1.3	-19.7	-3.9	-1.9	
<b>Total Fixed Income</b>	-0.3	3.9	5.9	6.5	2/29/96
LB Aggregate Bond Index	-0.6	8.4	6.3	7.2	

\*The descriptions of all benchmarks can be found in the appendix at the end of this report.

## ARKANSAS TEACHER RETIREMENT SYSTEM

## PRELIMINARY UPDATE

## PERFORMANCE SUMMARY

RETURN SUMMARY  
ENDING 12/31/01

	1 Month	1 Year Ending 12/31/01	3 Years Ending 12/31/01	Since Inception	Inception Date
Alliance Capital Management	0.4%	-22.9%	-6.5%	14.5%	6/30/91
S&P 500 Index	0.9	-11.9	-1.0	13.7	
Munder Capital Management	1.4	-14.2	-2.4	10.9	6/30/91
S&P 500 Index	0.9	-11.9	-1.0	13.7	
Oppenheimer Capital Management	0.5	-4.5	5.8	14.4	6/30/91
Russell 1000 Value Index	2.4	-5.5	2.7	14.5	
Invesco Capital Management	0.6	-3.0	-0.4	12.9	9/30/94
Russell 1000 Value Index	2.4	-5.6	2.7	15.3	
ICC Capital Management	4.0	-2.9	10.5	15.8	3/31/96
Russell 1000 Index	1.1	-12.5	-0.8	11.9	
Rothschild Asset Management	5.1	3.0	-	6.9	12/31/99
Russell Mid Cap Value Index	4.2	2.3	-	10.4	
Eubel Brady & Suttman	4.8	13.0	-	22.1	12/31/99
Russell Mid Cap Value Index	4.2	2.3	-	10.4	
Aetius Investment Management	4.6	-9.2	-	6.5	1/31/99
Russell 2000 Growth Index	6.2	-9.2	-	-1.2	
Trust Company of The West	5.3	-33.7	-	-6.2	1/31/99
Russell 2000 Growth Index	6.2	-9.2	-	-1.2	
Daruma Asset Management	7.7	15.9	-	15.4	7/31/00
Russell 2000 Value Index	6.1	14.0	-	19.1	
Phoenix Council	6.0	-12.0	-	-7.9	8/31/00
Russell 2000 Value Index	6.1	14.0	-	15.5	
Kennedy Capital Management	6.0	30.0	22.4	13.6	12/31/93
Russell 2000 Value Index	6.1	14.0	11.3	12.4	

RETURN SUMMARY  
ENDING 12/31/01

	1 Month	1 Year Ending 12/31/01	3 Years Ending 12/31/01	Since Inception	Inception Date
Brinson Partners	1.0%	-14.6%	-1.1%	6.9%	6/30/93
MSCI World Ex-U.S. Index	0.6	-21.4	-4.5	4.5	
Zurich Scudder	1.7	-23.3	-3.1	6.6	6/30/93
MSCI EAFE Index	0.6	-21.4	-5.1	4.3	
AIB Govett	4.6	-5.9	1.0	-4.2	6/30/94
Performance Benchmark	1.3	-19.7	-2.7	-6.1	

RETURN SUMMARY  
ENDING 12/31/01

	1 Month	1 Year Ending 12/31/01	3 Years Ending 12/31/01	Since Inception	Inception Date
Regions Capital Management	-0.6%	8.1%	6.0%	6.4%	2/29/96
Intermediate Gov't/Credit	-0.6	9.0	6.4	6.8	
Vanderbilt Capital Advisors	-0.7	6.0	3.8	5.2	6/30/97
LB Aggregate Bond Index	-0.6	8.4	6.3	7.6	
Loomis Sayles & Company	-1.2	6.5	5.2	6.4	6/30/97
LB Aggregate Bond Index	-0.6	8.4	6.3	7.6	
Hyperion Capital Management	-0.4	8.3	6.2	6.4	3/31/97
Mortgage Index	-0.4	8.2	7.0	7.9	
Nicholas Applegate	2.0	-11.3	10.4	12.9	11/30/98
Performance Benchmark	1.2	-5.3	7.7	9.5	



## ARKANSAS TEACHER RETIREMENT SYSTEM

## PRELIMINARY UPDATE

## ASSET ALLOCATION

## ASSET ALLOCATION AS OF 12/31/01

(\$ in thousands)

	U.S. Equity	Foreign Equity	Fixed Income	Real Estate	Alternatives	Cash	Total	Percent of Total	Policy
Alliance Capital Management	\$345,753	--	--	--	--	\$345	\$345,099	4.7%	
Munder Capital Management	281,857	--	--	--	--	2,560	284,417	3.9	
Oppenheimer Capital Management	477,238	--	--	--	--	10,737	488,025	6.6	
Invesco Capital Management	373,631	--	--	--	--	11,953	385,584	5.2	
ICC Capital Management	377,525	--	--	--	--	1,897	379,422	5.1	
Rothschild Asset Management	222,800	--	--	--	--	4,315	227,115	3.1	
Eubel Brady & Suttman	151,557	--	--	--	--	609	152,166	2.1	
Aeltus Investment Management	165,294	--	--	--	--	4,587	169,881	2.3	
Trust Company of The West	113,402	--	--	--	--	3,338	116,741	1.6	
Daruma Asset Management	113,972	--	--	--	--	6,533	120,605	1.6	
Phoenix Council	91,863	--	--	--	--	928	92,811	1.3	
Kennedy Capital Management	263,155	--	--	--	--	7,158	270,313	3.7	
<b>Total U.S. Equity</b>	<b>2,983,117</b>					<b>55,062</b>	<b>3,038,179</b>	<b>41.2</b>	<b>40.0%</b>
Brinson Partners	--	\$424,917	--	--	--	\$2,178	\$427,095	5.8%	
Zurich Scudder	--	359,333	--	--	--	18,113	377,451	5.1	
AIB Govett	--	95,628	--	--	--	3,049	98,677	1.3	
<b>Total Non-U.S. Equity</b>		<b>879,878</b>				<b>23,345</b>	<b>903,223</b>	<b>12.3</b>	<b>17.5%</b>
Regions Capital Management	--	--	\$536,789	--	--	\$11,975	\$548,764	8.1%	
Vanderbilt Capital Advisors	--	--	260,985	--	--	--	260,985	3.5	
Loomis Sayles & Company	--	--	425,122	--	--	10,053	435,175	5.9	
Hyperion Capital Management	--	--	273,020	--	--	5,572	278,592	3.8	
Nicholas Applegate	--	--	315,754	--	--	6,135	321,889	4.4	
<b>Total Fixed Income</b>			<b>1,862,630</b>			<b>33,735</b>	<b>1,896,415</b>	<b>25.7</b>	<b>25.0%</b>
Blackstone Mezzanine Partners	--	--	--	--	\$23,225	--	\$23,225	0.3%	
DLJ Mezzanine	--	--	--	--	25,249	--	25,249	0.3	
<b>Total Mezzanine Debt</b>					<b>48,474</b>		<b>48,474</b>	<b>0.7</b>	
Hicks Muse Tate & Furst - Fund III	--	--	--	--	\$64,603	--	\$64,603	0.9%	
Hicks Muse Tate & Furst - Fund IV	--	--	--	--	84,664	--	84,664	1.1	
Hicks Muse Tate & Furst - Fund V	--	--	--	--	80,573	--	80,573	1.1	
Oakhill Capital Partners	--	--	--	--	36,531	--	36,531	0.5	
Westbrook Shp LLC	--	--	--	--	34,108	--	34,108	0.5	
Cypress	--	--	--	--	15,056	--	15,056	0.2	
Diamond State Ventures Lp	--	--	--	--	1,000	--	1,000	0.0	
LJM2 Co-Investment L.P.	--	--	--	--	5,101	--	5,101	0.1	
DLJ Merchant III	--	--	--	--	52,241	--	52,241	0.7	
Hicks Muse Tate & Furst - Century Fund	--	--	--	--	9,213	--	9,213	0.1	
<b>Total Domestic Private Equity</b>					<b>383,140</b>		<b>383,140</b>	<b>5.2</b>	
Doughty Hanson	--	--	--	--	\$61,450	--	\$61,450	0.8%	
Doughty Hanson Tech I	--	--	--	--	7,843	--	7,843	0.1	
Doughty Hanson Euro Real Estate	--	--	--	--	9,411	--	9,411	0.1	
Cinven Funds	--	--	--	--	59,973	--	59,973	0.8	
<b>Total Foreign Private Equity</b>					<b>138,677</b>		<b>138,677</b>	<b>1.9</b>	
DLJ Real Estate Capital II	--	--	--	\$29,056	--	--	\$29,056	0.4%	
Westbrook Fund II	--	--	--	24,941	--	--	24,941	0.3	
Westbrook Fund III	--	--	--	78,634	--	--	78,634	1.1	
Westbrook Fund IV	--	--	--	17,967	--	--	17,967	0.2	
Olympus	--	--	--	42,382	--	--	42,382	0.6	
Wachovia Timberland	--	--	--	145,269	--	--	145,269	2.0	
Wachovia Timberland II	--	--	--	85,000	--	--	85,000	1.2	
<b>Total Real Estate</b>				<b>423,249</b>			<b>423,249</b>	<b>5.7</b>	
<b>Arkansas Related</b>				<b>\$495,381</b>			<b>\$495,381</b>	<b>6.7%</b>	<b>5.0%</b>
Liquidity Account	--	--	--	--	--	\$30,635	\$30,635	0.4%	
Cash	--	--	--	--	--	10,503	10,503	0.1	
<b>Total Cash Equivalents</b>						<b>41,138</b>	<b>41,138</b>	<b>0.6</b>	<b>1.0%</b>
<b>Total Fund</b>	<b>\$2,983,117</b>	<b>\$879,878</b>	<b>\$1,862,630</b>	<b>\$918,630</b>	<b>\$570,291</b>	<b>\$153,280</b>	<b>\$7,367,876</b>	<b>100.0%</b>	<b>88.5%</b>
<b>Percent of Total</b>	<b>40.5%</b>	<b>11.9%</b>	<b>25.3%</b>	<b>12.5%</b>	<b>7.7%</b>	<b>2.1%</b>	<b>100.0%</b>		

# ARKANSAS TEACHER RETIREMENT SYSTEM

## PRELIMINARY UPDATE

## APPENDIX

### DESCRIPTION OF BENCHMARKS

**Total Fund** - The Performance Benchmark for the Total Fund represents the performance of the asset class benchmarks as a weighted average of the Target Policy Allocations set forth by the investment committee. Currently as of October 1, 2001, the benchmark consists of 40% of the Russell 3000 Stock Index, 17.5% of the MSCI All-Country World Ex-U.S. Stock Index, 25% of the Lehman Brothers Aggregate Bond Index, 10% of the Alternative Policy made up of the Russell 3000 + a 2% premium per year, 1.5% of the NCREIF Southeast Timberland Index, 5% of the EnnisKnupp Real Estate Index and 1% of the EnnisKnupp STIF Index. The EnnisKnupp Real Estate Index is used in place of the NCREIF Index for periods since December 31, 2001, due to availability of returns. Returns since August 1, 1998 through September 30, 2001, consist of 40% of the Russell 3000 Stock Index, 17% of the MSCI All-Country World Ex-U.S. Stock Index, 28% of the Lehman Brothers Aggregate Bond Index, 7.5% of the Alternative Policy benchmark of the Russell 3000 + a 2% annual premium, 1.5% of the NCREIF Southeast Timberland Index, 5% of the EnnisKnupp Real Estate Index and 1% of the EnnisKnupp STIF Index. Returns prior to July 31, 1998, consist of the actual allocations to the seven different asset classes included in the Arkansas Teacher Retirement System over time. The benchmarks used for each asset class are noted below.

**U.S. Equity** - The Russell 3000 Stock Index.

**Non-U.S. Equity** - The MSCI All-Country World Ex-U.S. Index.

**Fixed Income** - The Lehman Brothers Aggregate Bond Index.

**Arkansas Related** - The EnnisKnupp Real Estate Index.

**Alternatives** - The Russell 3000 Stock Index plus 2.0% per year.

**Timberland** - The Southeast Timberland NCREIF Index.

**Cash Equivalents** - The EnnisKnupp Short Term Investment Fund (STIF).

**AIB Govett International Benchmark** - Since January 1, 2001, the benchmark consists of the MSCI All-Country World Ex-U.S. Stock Index. Prior to December 31, 2000, the benchmark consists of the MSCI Emerging Markets Index.

**Nicholas Applegate Performance Benchmark** - The performance benchmark for the Nicholas Applegate portfolio currently consists of 90% of the CSFB Convertible Securities Index and 10% of the Salomon High Yield Index.

**EnnisKnupp Real Estate Index** - A capitalization-weighted average of 27 open- and closed-end real estate funds representing approximately \$20 billion in assets.

**EnnisKnupp Short-Term Investment Fund (STIF) Index** - An average of the returns of six major banks' commingled short-term investment funds.

## ARKANSAS TEACHER RETIREMENT SYSTEM

## PRELIMINARY UPDATE

## APPENDIX

## DESCRIPTION OF BENCHMARKS

Lehman Brothers Aggregate Bond Index - A market-value weighted index consisting of the Lehman Brothers Corporate, Government and Mortgage-Backed Securities Indices. The Index also includes credit card-, auto- and home equity loan-backed securities, and is the broadest available measure of the aggregate U.S. fixed income market.

Lehman Brothers Intermediate Government/Credit Bond Index - A market-value weighted index consisting of the Lehman Intermediate Government and Intermediate Corporate Index.

Lehman Brothers Mortgage Index - A market value-weighted index consisting of the mortgage pass-through securities of Ginnie Mae (GNMA), Fannie Mae (FNMA) and Freddie Mac (FHLMC).

MSCI All-Country World Ex-U.S. Index - A capitalization-weighted index of stocks representing 47 developed and emerging country markets, excluding the U.S. market.

MSCI Europe, Australasia, Far East (EAFE) Non-U.S. Stock Index - A capitalization-weighted index of stocks representing 22 developed and emerging country markets in Europe, Australia, Asia and the Far East.

MSCI World Ex-U.S. Stock Index - A capitalization-weighted index of stocks representing 21 developed stock markets in Europe, Asia and Canada.

Russell 3000 Index - An index that measures the performance of the 3000 stocks that make up the Russell 1000 and Russell 2000 Indices.

Russell 1000 Index - An index that measures the performance of the largest 1,000 stocks contained in the Russell 3000 Index.

Russell 1000 Value Index - An index that measures the performance of those Russell 1000 companies with lower price-to-book ratios and lower I/B/E/S growth forecasts.

Russell 2000 Index - An index that measures the performance of the smallest 2000 companies contained in the Russell 3000 Index.

Russell 2000 Growth Index - An index that measures the performance of those Russell 2000 companies with greater price-to-book ratios and greater I/B/E/S growth forecasts.

Russell 2000 Value Index - An index that measures the performance of those Russell 2000 companies with lower price-to-book ratios and lower I/B/E/S growth forecasts.

Russell Mid Cap Value Index - An index that measures the performance of those Russell 1000 companies with lower price-to-book ratios and lower forecasted growth values.

S&P 500 Stock Index - A capitalization-weighted stock index consisting of the 500 largest publicly traded U.S. stocks.

Wilshire 5000 Stock Index - A capitalization-weighted stock index representing all U.S. common stocks traded regularly on the organized exchanges. The Index is the broadest measure of the aggregate U.S. stock market.

April 9, 2002

## REPORT- Real Estate Investment Manager

- (1) Received a request from Jim Hathaway to sign a contract with Crafton, Tull, and Associates, an engineering firm for a fee "to be determined".

I did not do so, due to the open-ended nature of the contract. It appears that on 12/12/01 Bill Shiron signed a contract with J. Hathaway for \$25,000 for consulting services in regard to the Highfill property. It also appears that on 12/13/02 the ATRS Board agreed to approve for the Highfill Land Team, which he takes to mean engineering.

I need some guidance, do you want me signing contracts with no specified amounts and do you assume that you have budgeted a total of \$50,000 toward the Highfill Land Team ???  
These all happened before my time!!!!

- (2) Management Contract signed with Kilgore on Riley Properties... all has 30 day cancellation clause. Kilgore has taken over management and now requests that we set up a "construction account" to cover needed renovation costs associated with the Riley North facility. I suggest that \$100,000 be placed in a joint ATRS/Kilgore construction account so that the renovation process might go forward at that location, and that outstanding invoices against that facility be paid for the past labor and materials.
- (3) Both myself and our law firm are in serious need of an accurate accounting report on the Riley Properties from when they were first acquired by ATRS to the present. The necessity of properly answering the Holman lawsuit has made this accounting report a serious as well as the need to be able to ascertain who has not been paid for past labor materials.
- (4) I have asked Darrel Dover to advise all contracted parties involved in the Chenal Retirement Village to formally understand that we are closing that project and that they have been so advised. Have shown the property to a prospective purchaser, do not know how serious they are, but have also gotten our offer to sell out there on the internet.  
  
We have new aerial photos of both the Chenal Project and of the Victory Bldg. These can be made available to prospects over the internet. (see attached)
- (5) Do we want to make offer to purchase "leased Lots" immediately North of the Ark-La building....owner made an offer to sell which I ignored due to the high amount, should I counter-offer ????
- (6) State Building Service has asked that we consider a loan to the State, on a property that they wish to purchase to consolidate their position around the Capitol. I am requesting that you give me the authority to deal directly with Mr. Laman in the future, as I firmly believe that an Amicable working relationship with that agency is to the benefit of ATRS.

MEMORANDUM

**ENNISKNUPP**

April 10, 2002

To: Board and Staff  
Arkansas Teacher Retirement System  
From: Steve Cummings, CFA  
David Russell, CFA  
Re: Recommendation Clarification

At the suggestion of staff, we wish to clarify our recommendation regarding the use of passive investment strategies (index funds) for the ATRS. In our report on U.S. Equity, we discussed at length the advantages of index funds as a core component of the investment program. During our presentation to the Board we recommended that at least 30% of the ATRS domestic stock assets be allocated to an index strategy.

In all aspects of this analysis and discussion, we are referring to traditional indexation (as opposed to enhanced indexation). The traditional indexation we are recommending involves the use of products that strive to match the performance of a given index. Enhanced indexation is a style of investing that is more like active management than passive management and one that we are not currently recommending the trustees consider. If there is interest on the Board to learn more about enhanced index strategies, we would be happy to prepare a report on that topic.

**Jonesboro Property.** Mr. Fortenberry made a motion to approved Mr. Ferstl's recommendation to list the property with Flake & Kelley of Little Rock, and Halsey Real Estate in Jonesboro. The motion carried. Mr. Ferstl will negotiate realtor fees.

**Victory Building.** Mr. Ferstl reported 102,000 square feet are leased. By common consent, the board authorized Mr. Ferstl to dedicate space that would be leased to lobbyists.

**Leasing Agreement with Financial Centre II .** Mr. Ferstl reported there is no working agreement with Financial Centre II for the referral of Victory Building prospects. By common consent, the Board authorized Mr. Greathouse to pursue the matter.

**Retirement Village Final Invoices.** Dr. Fair made a motion to authorize Mr. Ferstl and Mr. Dover to investigate ATRS' liabilities and to make a recommendation to the Board. The motion carried. Ms. Parsons referred the issue to the Investment Committee.

**Lindsey Projects.** Dr. Fair made a motion to refer the project to the Investment Committee for consideration and final action. The motion carried.

#### XIV. Policies Committee Report – Dr. Paul Fair, Chair

##### A. Policy Changes

Page 33-42. **Election Policies.** The following sentence in paragraph one, page 34, under the heading, "Board of Trustees Composition," was revised to read, "Eleven members shall be elected to the Arkansas Teacher Retirement Board of Trustees, eight seven of whom shall be active members of the system with at least five years of credited service in force, one who is a member of a racial ethnic group and is either an active or retired member, and three who are retirant members retired from the system and reside in the State of Arkansas." Dr. Fair made a motion to adopt the policies as revised. The motion carried.

Page 29-30. **Draft Legislation Proposal (Policies Committee minutes July 15, 2002, Attachment A).** By common consent, the Board agreed the following would be stricken from the draft, "*Each trustee shall continue to serve until his successor is elected and has qualified.*" Dr. Fair made a motion to approved the draft as revised. The motion carried.

Page 27. **Real Estate Manager Limitations.** Dr. Fair made a motion to approve Item #4, "Real Estate Manager Limitations," recorded in the Policies Committee minutes of July 15, 2002. The motion carried.

Page 31-32. **Non-contributory Policy Change.** Dr. Fair made a motion to approve the policy change as presented. The motion carried.

B. Minutes of July 15, 2002.

Upon Mr. Fortenberry's request, the board by common consent agreed to strike the entire paragraph entitled, "Retirant Trustees," under the item "In other business" in the minutes.

**XV. Legislative Committee Report – Winfred Clardy, Chair**

A. Minutes of July 15, 2002

**XVI. Teacher Retirement System Reports**

A. Medical Board Summary Report – Michael Ray

Mr. Vondran made a motion to approve the report for June 12, 2002, as presented. The motion carried.

B. Personnel Report – Michael Ray

Mrs. Coleman made a motion to approve the report for August, 2002, as presented. The motion carried.

C. Membership & Payroll

D. Arkansas Related Investments

E. Investment Summaries

F. Financial Statements

**XVII. New Business**

A. ATRS Budget for 2003-2005

B. Discussion – New Salary for Executive Director

Mr. Greathouse reported the new salary for the Executive Director of \$150,000 would be introduced at the Joint Budget Committee meeting scheduled for October 16.

C. Discussion – Dinners Following Regular Board Meetings

Mr. Vondran made a motion that the system pay for board members and staff members, and money managers would pay for themselves and guests. The motion did not pass.

Mrs. McGuire made a motion that the Board returns to having dinners the first night of a Board meeting, and that money managers divide the cost of the meal. The motion did not pass.

Ms. Parsons indicated the item would be addressed again at the October Board meeting.

D. T-DROP Study Responses to RFP

Ms. Parsons assigned to the Oversight Committee the review and selection of a company to conduct the study.

E. Discussion – Alternative Investments Report

F. Travel Resolution (*Attachment C*)

Mr. Dyer made a motion to adopt the travel resolution for 2002 as presented. The motion carried.

**XVIII. Executive Director's Comments**

**In other business:**

**Executive Session.** The Board convened in executive session to discuss personnel and employing personnel. The Board reconvened in open session. No action was taken.

*As there was no further business to consider, Mr. Vondran made a motion to adjourn. The motion carried and the meeting adjourned at 1:00 p.m.*

*Linda Parsons*

\_\_\_\_\_  
Linda Parsons, Chair

\_\_\_\_\_  
Wayne Greathouse, Interim Executive Director,  
Secretary to the Board

10-23-02

\_\_\_\_\_  
Date



# ENNISKNUPP

## MEMORANDUM

August 8, 2002

To: Board and State of the  
Arkansas Teacher Retirement System

From: Steve Cummings, CFA  
Patrick J. Kelly, CFA

Re: Summary of Our Recommendations

We have made several recommendations that have been approved by the Trustees:

1. Terminate Zurich Scudder (replaced by Putnam)
2. Terminate Vanderbilt (replaced by Western Asset Management)
3. Adopt manager presentation guidelines

There are several recommendations we have made that were approved but we understand are being reconsidered:

1. Mitigate significant bias towards small-capitalization and value-oriented domestic stock
2. Introduce a domestic equity passive allocation of up to 40% (30% was approved) of that asset class
3. Reduce the number of domestic stock managers, namely:
  - a. Munder Capital
  - b. Invesco
  - c. Phoenix
  - d. Rothschild

Based on our recent review of the investment program, we have some additional recommendations at this time:

1. Reclassify some existing assets:
  - a. Nicholas Applegate's convertible bond portfolio as equity investment
  - b. Mezzanine financing as a component of alternatives
  - c. Diversified real estate (excluding Arkansas related) as a separate asset class
2. Modify the Statement of Investment Policy
3. Adopt guidelines for each manager portfolio
4. Adopt narrower rebalancing ranges and a rebalancing policy
5. Initiate manager reporting of soft dollar use



Arkansas  
Teacher  
Retirement  
System

*Attachment B*

1400 West Third, Little Rock, AR 72201  
Phone (501) 682-1517 or (800) 666-2877  
Website - <http://www.atrs.state.ar.us>  
Email - [info@atrs.state.ar.us](mailto:info@atrs.state.ar.us)

EMAIL

08/13/02 03:37 PM

From: Hugh Roberts

To: ATRS Board of Trustees

Cc: Wayne Greathouse, Tom Ferstl, Darrell Dover, Tammy Medlock

Subject: Budget for A & D Wings on Northridge

\*\*\*\*\*

Ladies & Gentlemen:

When I presented you with a figure for continued renovation at Northridge, I quoted you \$250,000.00. In looking over my notes this afternoon I discovered an error that was my fault. There are actually two parts to Mr. Kilgore's request. Listed below is each part of Mr. Kilgore's proposal along with the cost.

1. The cost of obtaining the Physical Plant/Mechanical Items for the two wings-\$234,780.00
2. Total for labor and materials needed by the contractor to install the items-\$212,974.00.

At the meeting today, the Board approved the additional \$250,000.00 I initially quoted. However, as you can see, the actual cost will be \$447,754.00.

I am asking each Board member to please respond to me by e-mail their approval or non-approval of the new amount. If you would like to see copies of the proposals, I'll be happy to fax or mail them to you. This figure is part of the overall cost of approximately \$1.8 million I quoted this morning. If the Board approves this, I will ask Tammy to include this in the minutes as an item approved by e-mail with full Board approval to be obtained at the next Board meeting. Wayne has already signed the agreement but I will not send it back to Mr. Kilgore until I have heard from you. The stipulation made by the Board as to no other approvals of renovations being done until a formal agreement is in place would still stand.

I sincerely apologize for this error and will do my best to be sure it does not happen again.

Hugh A. Roberts  
Retirement Funds Investment Supervisor



*Attachment C*

1400 West Third, Little Rock, AR 72201  
Phone (501) 682-1517 or (800) 666-2877  
Website - <http://www.atrs.state.ar.us>  
Email - [info@atrs.state.ar.us](mailto:info@atrs.state.ar.us)

RESOLUTION

Board Expense Reimbursement  
For 2002

BE IT RESOLVED, *the members of the Board of Trustees of the Arkansas Teacher Retirement System are authorized reimbursement of expenses for attending trustee meetings in accordance with Act 1211 of 1995;*

NOW, THEREFORE, BE IT RESOLVED, *members of the ATRS Board of Trustees may attend and be reimbursed for any two (2) of the following conferences for the calendar year 2002:*

- National Council on Teacher Retirement (NCTR)
- Southern Conference on Teacher Retirement (SCTR)
- National Education Association (NEA) Forum on Retirement
- National Retired Teachers Association (NRTA) Pension Review

BE IT FURTHER RESOLVED, *trustees may be reimbursed expenses for attending two (2) additional retirement education conferences during the calendar year 2002.*

*ADOPTED this 13<sup>TH</sup> Day of August, 2002*

---

Linda Parsons, Chairman  
Arkansas Teacher Retirement System

**RESOLUTION 08.13.02**

**Board Expense Reimbursement For 2002**

BE IT RESOLVED, *the members of the Board of Trustees of the Arkansas Teacher Retirement System are authorized reimbursement of expenses for attending trustee meetings in accordance with Act 1211 of 1995;*

NOW, THEREFORE, BE IT RESOLVED, *members of the ATRS Board of Trustees may attend and be reimbursed for any two (2) of the following conferences for the calendar year 2002:*

- National Council on Teacher Retirement (NCTR)
- Southern Conference on Teacher Retirement (SCTR)
- National Education Association (NEA) Forum on Retirement
- National Retired Teachers Association (NRTA) Pension Review

BE IT FURTHER RESOLVED, *trustees may be reimbursed expenses for attending two (2) additional retirement education conferences during the calendar year 2002.*

*ADOPTED this 13th Day of August, 2002*

*Linda Parsons*

---

Linda Parsons, Chairman  
**Arkansas Teacher Retirement System**