



## Board of Trustees Meeting

August 29, 2018



Presented for Review and Approval

December 11, 2018

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**BOARD OF TRUSTEES MEETING  
EMPLOYEES RETIREMENT SYSTEM OF TEXAS  
August 29, 2018  
ERS Board Room  
ERS Building – 200 E. 18th Street  
Austin, Texas 78701**

**TRUSTEES PRESENT**

Doug Danzeiser, Board Chair  
Cydney Donnell, Board Vice Chair  
Ilesa Daniels, Member  
I. Craig Hester, Member  
Catherine Melvin, Member

**TRUSTEES ABSENT**

Jeanie Wyatt, Member – Excused by the Board

**ERS STAFF PRESENT**

Porter Wilson, Executive Director  
Cathy Terrell, Deputy Executive Director  
Paula A. Jones, Deputy Executive Director & General Counsel  
William Nail, Special Projects & Policy Advisor  
Jennifer Chambers, Director of Government Relations  
Tony Chavez, Director of Internal Audit  
Bernie Hajovsky, Director of Enterprise Planning  
Robin Hardaway, Director of Customer Benefits  
Diana Kongevick, Director of Group Benefits  
Wendy McAdams, Director of Operation Services  
Machelle Pharr, Chief Financial Officer  
Gabrielle Schreiber, Director of Procurement and Contract Oversight  
DeeDee Sterns, Director of Human Resources  
Kathryn Tesar, Director of Benefits Communications  
Chuck Turner, Chief Information Officer  
Keith Yawn, Director of Strategic Initiatives  
Nora Alvarado, Group Benefits  
Michelle Barron, Group Benefits  
Georgina Bouton, Group Benefits  
Carlos Chujoy, Investments  
Kelley Davenport, Executive Office  
Christi Davis, Customer Benefits  
D'Ann DeLeon, Group Benefits  
Blaise Duran, Group Benefits  
Leah Erard, Strategic Initiatives  
Beth Gilbert, Internal Audit  
Angelica Harborth, Group Benefits  
Darren Hughes, Investments  
Aaron Ismail, Investment Compliance Officer  
Sharmila Kassam, Deputy Chief Investment Officer  
Nancy Lippa, Office of General Counsel  
Aris Oglesby, Investments  
Jamey Pauley, Enterprise Planning Office  
Susie Ramirez, Executive Office  
Lauren Russell, Group Benefits  
Cheryl Scott Ryan, Office of General Counsel  
Robert Sessa, Investments  
Tommy Williams, Information Systems  
Lacy Wolff, Enterprise Planning Office

**ALSO PRESENT**

Nick Arnold, Humana  
Phil Dial, Rudd & Wisdom, Inc.  
Ruth Ann Eledge, Segal Waters  
Katy Fallon-Brown, Legislative Budget Board  
Elana Fowler, AFSCME Texas Retirees  
Aaron Haftl, Aon Hewitt  
Bill Hamilton, Retired State Employees Association  
Peter Jansen, CBRE  
Rick Johnson, Broaddus  
Jessica Karlsruher, Texas Public Employees Association  
Ashley Mann, House Appropriations Committee  
Chad Marsh, Endeavor  
Michael McCormick, Aon Hewitt  
Colleen McGlamry, UnitedHealthcare  
Chris Paxton, Optum Rx  
Lee Spangler, Blue Cross and Blue Shield of Texas  
Mallory Sumner, Blue Cross and Blue Shield of Texas  
Steve Voss, Aon Hewitt

## Meeting of the ERS Board of Trustees

### 1. CALL TO ORDER

#### 1.1 Call Meeting to Reconvene the ERS Board of Trustees

Mr. Doug Danzeiser, Chairman of the Board of Trustees of the Employees Retirement System of Texas (ERS), noting a quorum was present, called the meeting to order at 12:56 p.m. and read the following statement:

“A public notice of the ERS Board of Trustees meeting containing all items on the proposed agenda was filed with the Office of the Secretary of State at 8:41 a.m. on Monday, August 20, 2018, as required by Chapter 551 Texas Government Code, referred to as the Open Meetings Law.”

The Board of Trustees convened as a committee of the whole to consider the following Board agenda items.

### 2. MINUTES

#### 2.1 Review and Approval of the minutes to the May 23, 2018 ERS Board of Trustees Meeting (ACTION)

Mr. Danzeiser opened the floor for a motion on the approval of the minutes.

**Move** that the Board of Trustees of the Employees Retirement System of Texas approve the minutes to the meeting held on May 23, 2018.

Motion by Craig Hester, second by Catherine Melvin.

Final Resolution: Motion Carries

Aye: Craig Hester, Cydney Donnell, Doug Danzeiser, Ilesa Daniels, Catherine Melvin

### 3. BOARD RULES

#### 3.1 Review and Consideration of Proposed New Rule related to Mediation for Chapter 67 (Hearings on Disputed Claims) – (ACTION)

Ms. Paula A. Jones, Deputy Executive Director and General Counsel, presented the proposed rule amendments for Chapter 67, Hearings on Disputed Claims. These rules were proposed following the Sunset Commission's review of ERS and its recommendation to apply standard across-the-board requirements to ERS. Ms. Jones reported that one of the recommendations was to develop a policy to encourage the use of appropriate alternative dispute resolution procedures. Staff proposed a new rule in § 67.44 to permit ERS to offer mediation rights in contested administrative appeals when there are material facts at issue and there are remedies available under applicable law involving eligible claims for benefits, including disability retirement, long- and short-term disability insurance, dental PPO plan appeals and cases where ERS determines that a participant or dependent should be removed from the GBP in accordance with applicable laws, regulations, and/or plan requirements.

Ms. Jones informed the board that the notice of these rules was published in the July 27, 2018 issue of the *Texas Register* and no comments were received by ERS.

There being no further discussion or questions, Mr. Danzeiser opened the floor for a motion.

**Move** that the Board of Trustees of the Employees Retirement System of Texas adopt the proposed new rule to Chapter 67, Hearings on Disputed Claims, § 67.44 concerning Mediation, as presented in Exhibit A attached to this agenda item.

Motion by Catherine Melvin, second by Ilesa Daniels.

Final Resolution: Motion Carries

Aye: Craig Hester, Cydney Donnell, Doug Danzeiser, Ilesa Daniels, Catherine Melvin

3.2 Review and Consideration of Proposed Rule Amendments for Chapter 81 (Insurance) – (ACTION)

Ms. Robin Hardaway, Director of Customer Benefits, presented the proposed rule amendments for Chapter 81 concerning Insurance. Effective April 1, 2018, the Centers for Medicare & Medicaid Services (CMS) began issuing new Medicare cards, replacing social security number-based identification numbers with unique Medicare Beneficiary Identification numbers, known as an MBI. This change requires ERS to modify current Medicare retiree insurance enrollment processes. Ms. Hardaway stated that ERS must obtain the new MBI from new enrollees and confirm that number with CMS before new participants can enroll in the HealthSelect<sup>SM</sup> Medicare Advantage PPO and HealthSelect<sup>SM</sup> Medicare Rx programs.

The proposed amendment to Chapter 81.7 address retirees and Medicare-eligible retiree enrollments and Medicare-eligible dependents and their surviving dependents. The amendment clarifies that enrollment into the HealthSelect<sup>SM</sup> Medicare Advantage PPO for Medicare-eligible dependents and surviving dependents will occur after CMS confirms Medicare enrollment.

The next set of proposed amendments under § 81.7 similarly addresses enrollment into the HealthSelect<sup>SM</sup> Medicare Rx program for Medicare eligible retirees, Medicare eligible dependents, and Medicare eligible surviving dependents.

Ms. Hardaway announced that the notice of the proposed amendments to Chapter 81 was published in the July 27, 2018 Texas Register. There were no comments received by the deadline of August 27, 2018.

There being no further discussion or questions, Mr. Danzeiser opened the floor for a motion.

**Move** that the Board of Trustees of the Employees Retirement System of Texas adopt the proposed amendments to the sections of the Trustee Rules, 34 Texas Administrative Code (TAC), as described and incorporated in this agenda and as set forth in Chapter 81 (Insurance), by amending § 81.7 (Enrollment and Participation). The amendments are presented in Exhibit A of the agenda item.

Motion by Cydney Donnell, second by Catherine Melvin.

Final Resolution: Motion Carries

Aye: Craig Hester, Cydney Donnell, Doug Danzeiser, Ilesa Daniels, Catherine Melvin

#### **4. TEXAS EMPLOYEES GROUP BENEFITS PROGRAM UPDATE**

##### 4.1 Texas Employees Group Benefits Program Update

Ms. Diana Kongevick, Director of Group Benefits, introduced Blaise Duran, Director of Actuarial and Reporting Services, and Phil Dial of Rudd and Wisdom, Inc. to provide an update about the group benefits program. Mr. Duran reported that HealthSelect<sup>SM</sup> of Texas experienced a negative pharmacy trend during the first four months of plan year 2018. The unusual trend, where the plan paid less this year than the previous year for pharmacy, was due to the new pharmacy benefits manager contract. This lower trend has a one-time positive effect on the fund, where it re-sets the baseline. Since January, the trend has returned to norms more reflective of the program's history.

As in the first year of the Pharmacy Benefit Manger (PBM) contract with UnitedHealthcare (OptumRx), the first year of the HealthSelect medical third party administrator (TPA) contract resulted in lower-than-expected trend. This is largely due to the HealthSelect network's extremely competitive provider reimbursement rates. Mr. Duran reported that while utilization was less during the first part of the year, utilization returned to expected levels beginning in January 2018.

Ms. Kongevick reported that beginning this fall, ERS is expanding HealthSelect mental health provider access through Doctor on Demand and MD Live. Unlike the medical virtual visits, these are not urgent care visits, these are a way to increase access to providers for regularly scheduled visits to a therapist, psychologist or psychiatrist.

The virtual mental health visit is subject to the same copay and out-of-pocket expense as a visit to a mental health provider's office. Ms. Kongevick noted that the benefit is expected to be particularly valuable to those who live in rural areas, where access to mental health providers may be limited.

Mr. Duran provided an update on the 85<sup>th</sup> legislative initiatives:

- Rider 15 requires ERS to reduce freestanding emergency room plan costs. By September 1, 2018, the copay was increased for freestanding ERs from \$150 to \$300.
- Rider 18 requires the State's Health-Related Institutions (HRI) to reduce costs for HealthSelect plans.
- Article IX, § 10.7 requires the Health and Human Services Commission to collaborate with certain other state agencies on quality-based initiatives. Mr. Duran noted that a charter has been developed to formalize the goals, strategies, and operational details of what this would look like.
- Riders 14 and 16 require ERS to analyze Consumer Directed HealthSelect<sup>SM</sup> and review alternative plan design options.
- Rider 17 allows ERS to operate or contract with an onsite or near-site clinic as long as the approach is cost neutral and no funds are used to acquire or build the clinic. ERS is evaluating a pilot project for an on-site telemedicine clinic to be operated by Texas Tech University Health Sciences Center. This clinic will operate at one of the prisons and will provide an opportunity for prison guards and state employees who work at that clinic to access care through video conference with a nurse practitioner for urgent care services while at the workplace.

Ms. Kongevick reported that ERS recently formed an internal work group to discuss the components of a Group Benefit Funding Policy, including proposed goals for such a policy and an overall goal statement. The workgroup expects to have an agenda item at the December 2018 board meeting for discussion with the potential for board consideration at the May 2019 meeting.

Mr. Danzeiser stated that the health plan is currently in a very good financial position; however, he was interested in how staff and the board look at the plan in terms of future legislative funding requests under different circumstances or in connection with benefit plan design. Mr. Danzeiser asked if staff would bring the board recommendations only when the financial circumstances and changes need to be made to save the trust money or to bring up options when the funding is doing well. Ms. Melvin and Mr. Hester both agreed the board is interested in both being brought to the board.

Porter Wilson, ERS Executive Director, further reported that ERS has enhanced benefits over time. Ms. Kongevick gave illustrations of plan modernization in the past year, resulting in enhanced benefits. For the upcoming legislative session, staff are proposing to keep funding at the current levels for the next biennium, noting that the recently submitted set the base funding request at the FY19 level of funding.

This agenda item was presented for information and discussion purposes only. There was no further discussion or questions and no action was taken.

#### 4.2 Consideration of Proposed Rates for HealthSelect<sup>SM</sup> Medicare Advantage PPO Plan for Calendar Year 2019 – (ACTION)

Ms. Kongevick presented proposed 2019 rates for HealthSelect<sup>SM</sup> Medicare Advantage, a preferred provider organization (MA PPO). She noted that the plan is highly valued and well received by retirees. The HealthSelect MA PPO is a fully insured PPO medical plan customized for retirees who participate in the Texas Employees Group Benefits Program (GBP). Ms. Kongevick reported that the cost of the plan is heavily subsidized by the federal government resulting in lower costs to retirees and to the program.

Mr. Blaise Duran reported that the HealthSelect MA PPO is a fully insured medical plan administered by Humana. Staff project the cost of prescription drug coverage for members under the HealthSelect Medicare prescription drug plan to be lower in FY19 than projections for FY18.



Mr. Duran reported that whenever evaluating a fully insured product for participation in the group benefits plan, ERS must comply with a rider in the General Appropriations Act which states that ERS cannot pay more for the fully insured coverage, than it would otherwise cost to cover these members and participants in the basic health plan.

To ensure compliance with the rider, the consulting actuary utilizes a theoretical cost index (TCI) model which estimates the costs that would be required to cover those HealthSelect MA PPO participants if they are enrolled in HealthSelect of Texas. Mr. Duran continued to state that to participate in the GBP, the HealthSelect MA PPO administrator must agree to charge premium rates that are no greater than 95% of the TCI in order to ensure savings of at least 5% as compared to the cost of coverage under HealthSelect of Texas.

Mr. Duran reported that the prescription drug coverage costs have decreased and there is no federal health insurance provider fee this year, as it has been waived. Based on these factors, staff propose a rate of \$140.92 for Medicare primary spouse coverage (nearly \$20 less than current cost) and \$281.84 for Medicare primary surviving spouse (nearly \$40 less than current cost). Mr. Duran reported an estimated \$200 savings for Medicare primary spouses enrolled in the MA PPO when compared to the cost of enrollment in HealthSelect. For the Medicare primary surviving spouse, the savings is over \$400.

There being no further discussion or questions, Mr. Danzeiser opened the floor for a motion.

**Move** that the Board of Trustees of the Employees Retirement System of Texas approve the Calendar Year 2019 plan rates as presented in this agenda item effective January 1, 2019 for the statewide HealthSelect Medicare Advantage PPO Plan offered under the Texas Employees Group Benefits Program.

Motion by Craig Hester, second by Catherine Melvin.

Final Resolution: Motion Carries

Aye: Craig Hester, Cydney Donnell, Doug Danzeiser, Ilesa Daniels, Catherine Melvin

#### 4.3 Consideration of Proposed Rates for Medicare Advantage Health Maintenance Organization Plan for Calendar Year 2019 – (ACTION)

Ms. Diana Kongevick, informed the board that the Medicare Advantage (MA HMO) is a fully insured plan. The cost of the plan is heavily subsidized by the federal government, resulting in lower costs to retirees and the plan. The plan is highly valued and well received, and enrollment continues to increase.

KelseyCare Advantage HMO is the only MA HMO currently offered under the Texas Employees Group Benefits Program (GBP) specific to those who reside in one of eight Houston-area counties. Ms. Kongevick noted that medical coverage is through KelseyCare Advantage, while prescription drug coverage is through the self-funded HealthSelect<sup>SM</sup> Medicare Rx plan administered by UnitedHealthcare. The service area will not change for CY19.

Mr. Blaise Duran reported that contribution rates comprise of three elements, the negotiated MA HMO premium for medical coverage, the projected HealthSelect Medicare Rx costs, and the health insurance provider fee. Staff project that the HealthSelect Medicare Rx cost is anticipated to be lower in CY19 and the federal health insurance provider fee has been waived for this year.

Mr. Duran informed the board that when determining appropriate premium rates for participating MA HMOs, ERS must comply with a rider in the General Appropriations Act. To ensure compliance with the rider, the consulting actuary utilizes a theoretical cost index (TCI) model. The premium rates are to be no greater than 95% of the TCI in order to ensure savings of at least 5% as compared to the cost of coverage under the HealthSelect of Texas.

Staff recommends a lower rate of \$122.38 for Medicare Primary spouse coverage, which is about \$14 less than last year's rate of \$244.76 and about \$30 less for a Medicare Primary Surviving spouse.

Mr. Duran said that members can go back and forth between the Medicare Advantage and the HealthSelect plan at any time throughout the year. Mr. Wilson added that eligible retirees make general

decisions about their benefits during annual enrollment and retirees can make decisions about their MA and HealthSelect plans on a month-to-month basis.

Mr. Danzeiser asked if there is information on the website showing the different premium rates. Ms. Kathryn Tesar, Director of Benefits Communications, confirmed the rates are on the website and added there are also seminars for people who are becoming eligible for Medicare.

There being no further discussion or questions, Mr. Danzeiser opened the floor for a motion.

**Move** that the Board of Trustees of the Employees Retirement System of Texas approve Calendar Year 2019 Medicare Advantage HMO contribution rates as presented in this agenda item for participation in the Texas Employees Group Benefits Program.

KS Plan Administrators, L.L.C., D/B/A KelseyCare Advantage MA HMO Plan to provide Medicare Advantage HMO medical-only coverage in the Houston application area which includes the counties indicated in Exhibit A of this agenda item.

Motion by Catherine Melvin, second by Cydney Donnell.

Final Resolution: Motion Carries

Aye: Craig Hester, Cydney Donnell, Doug Danzeiser, Ilesa Daniels, Catherine Melvin

4.4 Review and Consideration of Proposed TexaSaver<sup>SM</sup> 401(k)/457 Program Roth Fees – (ACTION)

Ms. Georgina Bouton, Assistant Division Director of Group Benefits, introduced Ms. Nora Alvarado, Director of Voluntary Income Plans, to assist in presenting a recommended change in the TexaSaver 401(k)/457 program fees. Ms. Bouton explained that this proposed change would be relevant to those participants having both pre-tax and post-tax contributions within the 401(k) or 457 account. ERS administers the TexaSaver 401(k) and 457 programs. It is a voluntary, tax-deferred supplemental retirement program to help state and eligible higher education employees with their personal retirement savings through elective payroll contributions. The program provides participants a way to complement their ERS pension and Social Security benefits. The board established a Roth contribution option in the 401(k) and 457 plans effective January 1, 2012. The Roth contribution option allows employees to designate all or a portion of their monthly TexaSaver contribution as an after-tax contribution. Ms. Alvarado further stated that the Texas legislature does not appropriate funds for the administration of the program and administrative expenses are fully paid by participants.

The total assets of the program are approximately \$3.1 billion with 8,872 Roth accounts as of through March 31, 2018.

The monthly administrative fees paid by the participants are structured on a tiered schedule that is based on the participant's account balance. Currently participants are assessed on a per account, per contribution type basis as reflected below in Table 1.

**Table 1  
TexaSaver Program Administrative Fees**

| Account Balance                     | Monthly Fee<br>(Per Participant, Per Account,<br>Per Contribution Type) |
|-------------------------------------|---|
| \$10.00 or less                     | No fee  |
| Between \$10.01 and \$1,000.00      | \$1.18  |
| Between \$1,000.01 and \$16,000.00  | \$3.99  |
| Between \$16,000.01 and \$32,000.00 | \$6.00  |
| Between \$32,000.01 and \$48,000.00 | \$8.17  |
| Between \$48,000.01 and \$64,000.00 | \$10.89   |
| \$64,000.01 or more                 | \$13.62   |

Administration fees may be offset by quarterly fund reimbursements made directly into participant accounts through revenue sharing agreements that ERS has with most of the TexaSaver funds.

Staff propose to eliminate the fee per contribution type which will benefit most participants who have both pretax and post-tax accounts, as it would eliminate the fee per Per Contribution Type.

The staff recommendation will simplify the administrative fee structure by eliminating the multiple administrative fees in an account when there are both traditional and Roth contributions. The objective is to have the monthly administrative fees assessed on a per participant, per account basis beginning October 1, 2018.

In a response to a from Mr. Danzeiser asking if most participants are contributing into two accounts, Ms. Bouton replied that there are about 1,660 participants that have both pretax and post-tax dollars in their 401(k) account.

There being no further discussion or questions, Mr. Danzeiser opened the floor for a motion.

**Move** that the Board of Trustees of the Employees Retirement System approve the proposed fee structure for the Texa\$aver Program, as presented in this agenda item, so that the monthly administrative fees are charged per participant, per Texa\$aver account, beginning on or after October 1, 2018.

Motion by Cydney Donnell, second by Craig Hester.

Final Resolution: Motion Carries

Aye: Craig Hester, Cydney Donnell, Doug Danzeiser, Ilesa Daniels, Catherine Melvin

## **5. BOARD OF TRUSTEES ELECTION**

### *5.1 Review and Consideration of the 2019 Board of Trustees Election Calendar – (ACTION)*

Bernie Hajovsky, Director of Enterprise Planning, presented to the board on the 2019 Board of Trustees election calendar. Mr. Danzeiser's term expires on August 31, 2019. Section 815.003(d) of the Texas Government Code states that before August 31 of each odd-numbered year, the Board of Trustees (Board) of the Employees Retirement System (ERS) of Texas is required to hold an election for the members and retirees of the system to nominate and elect a trustee. The board consists of three appointed members and three members elected by system members.

Mr. Hajovsky informed the board that any state employee who is actively contributing to the employee class is eligible to run for a position on the board. Employees at the Health and Human Services Enterprise and the Texas Department of Public Safety are ineligible to run in this particular election since those agencies are already represented on the board by elected Trustees. All contributing members, retired state employees receiving an annuity from ERS, and non-contributing members are eligible to vote in the election. Mr. Hajovsky reported that there were more than 340,000 eligible voters in the last election.

Eligible voters can vote by mail using a paper ballot that is sent to their home address on file, or online. If eligible voters have an email address on file, they receive a personalized, embedded link into the online ballot by email. Mr. Hajovsky noted that there were more than 10,000 voters during the 2017 election that cast their ballot via the email link electronically.

Mr. Hajovsky introduced the proposed schedule of key dates for the election. Those wishing to serve on the board must submit a petition of at least 300 unique signatures from eligible voters to be nominated as a candidate. Staff would certify that each candidate has received the correct amount of signatures from eligible voters. ERS hosts a candidate forum to give members and retirees the chance to ask questions of the candidates to learn their positions on benefits and retirement issues. The voting period would span five weeks. Once the voting period ends, the election administrator, Survey and Ballot Systems, compiles and validates the votes. The candidate that receives the most votes is the Trustee elect. There is no run-off election. The Trustee elect's term begins on September 1, 2019.

Staff recommends the Board of Trustees adopt the following calendar for the 2019 election as noted below.

## **Nomination Period**

Distribution of Nominating Petitions .....Friday, March 1, 2019  
Close Nominations at 5:00 P.M. ....Monday, April 1, 2019  
Certify Candidates; Select Ballot Order .....Thursday, April 18, 2019  
Candidate Forum .....Thursday, May 9, 2019

## **General Election**

Voting Begins .....Friday, May 10, 2019  
Close Voting .....Friday, June 14, 2019  
Executive Director Certifies Results .....Thursday, July 11, 2019

Mr. Danzeiser stated the cost of mailing paper ballots is fairly high and questioned if there is something that can be done to move towards electronic voting which would be a cost savings for the agency. Mr. Hajovsky noted that many election administrators promote electronic voting and there is a growing trend where many election administrators are moving away from the paper-based systems to fully electronic voting systems. Mr. Hajovsky also noted that in the most recent election 60% of voters cast their ballot via paper. Mr. Wilson chimed in to state that online voting has been an option for a number of election cycles and the change in the last election to provide the personalized email did increase the number of electronic votes.

There being no further discussion or questions, Mr. Danzeiser opened the floor for a motion.

**Move** that the Board of Trustees of the Employees Retirement System of Texas adopt the 2019 Board of Trustees Election Calendar as presented in this agenda item

Motion by Catherine Melvin, second by Craig Hester.

Motion Carries

Aye: Craig Hester, Cydney Donnell, Doug Danzeiser, Ilesa Daniels, Catherine Melvin

## **6. COMPENSATION STUDY REVIEW**

### *6.1 Review and Discussion of the 2018 Compensation Study for ERS' Investment Professionals*

DeeDee Sterns, Director of Human Resources, stated that ERS regularly conducts compensation studies of the investment staff in order to fulfill a board directive that the system pay competitive market rates in order to recruit and retain the right personnel to invest the Trust. Assisting HR with the project is Jamey Pauley of Enterprise Planning Office. ERS contracted with Segal Waters Consulting to conduct the study this year. Ruth Ann Eledge reported on the study's findings.

Mr. Pauley reported that on November 9, 2017, ERS released an RFP to qualified vendors to provide a customized compensation study for positions within the Investments Division. The study was commissioned to evaluate the competitiveness of both pay and benefits for 53 non-administrative investment benchmark jobs. The 53 jobs represent 71 non-administrative positions within the Investments Division. Some of the job categories have multiple people in them.

Mr. Pauley informed the board that a contract for the requested compensation study was executed on March 1, 2018 with Segal Waters Consulting. On July 9, 2018 Segal Waters issued a final report to ERS which includes detailed findings regarding base pay, pay practices, paid leave, health benefits, retirement benefits, incentive compensation plans and total compensation.

Ms. Eledge provided an overview of the project methodology and findings. Segal Waters identified relevant peers who manage at least \$20 billion in assets, with similar jobs to ERS with a significant portion of the assets internally managed. A custom market survey was developed to collect, review, analyze and compare each benchmark job title. The comparison looked at the job duties and responsibilities, compensation, education, certifications, experience, tenure, specialized skills and benefits. The study developed salary recommendations based on the state compensation and classification pay guidelines and the ERS Policy and Procedure Manual.

The components that were included in the custom survey included direct pay, cash compensation, incentive plans, benefits, and retirement options. The survey identified comparable

employers, and collected data from those employers, as well as reviewing market data from the private sector including IBM Kenexa, Economic Research Institute and Willis Towers Watson to determine gaps in Total Compensation. At the end of the study Segal looked at the current grade assignments of positions within the state's compensation system and produced the final report documenting project methodology and findings.

The study calculated an adjustment for the cost of labor. The Economic Research Institute establishes a national index for cost of labor which looks at different geographic locations and establishes a relationship to a national index. The custom survey included an individual job summary that laid out the general responsibilities and requirements for that position, as well as the minimum qualifications.

Ms. Eledge stated there were 53 distinct positions that were identified to include in the survey. In the survey document there were questions in various different categories in compensation (salaries, pay ranges, merit plans, incentive compensation bonuses and incentive plan documents), benefits (paid leave, medical insurance, retirement), pay practices and organizational characteristics.

ERS' market position varies by benchmark job. The pay range midpoints were used to determine if individual benchmark jobs were at, above, or below market. Jobs with midpoints below 95% of market were identified as lagging the market and jobs with midpoints above 105% of market were identified as leading market. Overall the midpoint comparison is at 87% of the average in the market. Thirty-nine benchmark jobs have range midpoints that are below market. Seven (7) benchmark jobs were within the plus or minus 5%. While the salary midpoint is generally below the market average, the study showed that compensation rises above the market average when incentive compensation is included. Ms. Sterns said that staff would like to get additional information on this study result before making any recommendations related to the incentive compensation plan.

Ms. Sterns informed the board that staff's recommendation is to include funds in the FY19 budget to enable leadership to adjust certain salaries as needed to conform with the market. That money is included in the budget document that the board will consider in a separate agenda item. Staff will continue to use the information from the Segal Waters study, along with other market data, to guide salary decisions.

This agenda item was presented for information and discussion purposes only. There was no further discussion or questions and no action was taken.

## **7. INCENTIVE COMPENSATION PLAN**

### ***7.1 Review and Consideration of the ERS Incentive Compensation Plan – (ACTION)***

Ms. DeeDee Sterns presented the review and consideration of the ERS Incentive Compensation Plan (ICP). Ms. Sterns stated that the Board of Trustees reviews and considers the ICP on an annual basis. Staff review the document and present a draft of the document to the board during its May meeting. The draft will reflect any changes that the staff believe is needed to conform to the labor market and compensation plan standards and to improve plan administration. Ms. Sterns reported the plan was most recently amended and adopted by the Board on August 23, 2017.

The goal of the ICP is to communicate strategic performance priorities to participating employees, encourage sustained levels of high investment performance without undue risk, promote teamwork among employees, support the strategic and operational goals of ERS and to attract and retain key employees in a cost-effective manner.

Ms. Sterns reported that as part of the compensation study conducted by Segal Waters, staff gathered some ICP information to perform an additional review. Survey respondents were asked to provide copies of their plan documents. Not all respondents in the survey peer group offered an incentive plan. She also noted that staff determined additional time and data is necessary to thoroughly assess how ERS' ICP compares to the actual market.

Ms. Sterns noted that staff are not recommending any changes at this time to the plan document. Staff recommend that the board adopt, as part of the annual review of the plan, the ICP for Fiscal Year 2019 and the proposed plan document as submitted.

There being no further discussion or questions, Mr. Danzeiser opened the floor for a motion.

Move that the Board of Trustees of the Employees Retirement System of Texas approve the ERS Incentive Compensation Plan for Key Investment Professionals and Leadership Employees as presented in Exhibit A.

Motion by Cydney Donnell, second by Ilesa Daniels.

Final Resolution: Motion Carries

Aye: Craig Hester, Cydney Donnell, Doug Danzeiser, Ilesa Daniels, Catherine Melvin

## **8. ERS' OPERATIONAL ITEMS**

### 8.1 Review of 2018 ERS Accomplishments

Mr. Porter Wilson reviewed ERS' agency accomplishments for FY18. ERS had a successful year achieving progress toward four strategic goals. The first was supporting members' retirement income security in a number of ways. More than \$2.3 billion in payments for retirees and beneficiaries was issued and ERS developed the first Pension Program Funding Priorities and Guidelines document. ERS increased Texa\$aver participation by 5.7% and assets by 16.9% as of December 31, 2017 and retains 75.8% of participants who automatically enroll in the 401(k) Plan.

In sustaining competitive group benefits, the program had a very successful year due to the cost savings generated by the contracts for the new medical and pharmacy benefit managers. These savings help to sustain the program for all participants. In addition, staff developed a pilot community wellness program in Huntsville, which engaged two large Group Benefits Program (GBP) employers and community resources to work together to improve the health and wellness of Huntsville residents. Staff hired the first GBP Health Promotions Administrator to work with agency wellness coordinators and GBP plan administrators to expand health and wellness promotion programs and analyze the effectiveness of those programs. Mr. Wilson reported that ERS established and held the first meeting of the Group Benefits Advisory Committee which will meet twice a year. The committee will provide the Board with information from ERS participants, benefit experts, and professionals to ensure that state benefit offerings provide value to participants and employers. Mr. Wilson also reported that ERS increased its retirement enrollment in the HealthSelect Medicare Advantage PPO.

Mr. Wilson reported that to engage stakeholders for informed decision making, staff conducted in-house education conferences and promoted strategic outreach with primers on private equity and infrastructure. Staff also created an innovative, reader-friendly format for the GBP annual report which is sent to the legislature. Staff engaged stakeholder groups each quarter to request input on ERS' programs and share updates. Mr. Wilson noted that staff performed a thorough assessment of member publications working with an external consultant and began making suggested improvements. Engagements with members occurred through a variety of channels including: 102 benefits education events, 45 webinars, 424,454 phone calls, 3,300 on-site visits, 20,000 emails, 127,175 member requests and more than 370,000 pieces of incoming and outgoing mail.

Related to enhancing agency performance and accountability, Mr. Wilson reported that in the Survey of Employee Engagement, ERS achieved the highest ever participation rate from ERS employees. ERS implemented 16 of 19 projects related to Sunset Commission recommendations. ERS also instituted an independent investment compliance function and improved agency processes and procedures, including implementation of direct deposit of state and member contributions and an automated travel system to streamline authorizations and reimbursements. Staff developed a comprehensive space plan to accommodate staff during construction of the new building, and contracted with appropriate professionals as part of the redevelopment of the annex and zoning changes from the City of Austin. Mr. Wilson informed the board that improvement of the Records Management Program included enhancements of the training program.

This agenda item was presented for information and discussion purposes only. There was no further discussion or questions and no action was taken.

## 8.2 Review of Building Development Project

Mr. Porter Wilson provided an update on the design build process currently underway as part of the space planning and building redevelopment project. ERS continues to work with the selected design-build firm, Ryan Companies, and architectural firm, STG, in the pre-construction and design process. The newly constructed building will replace the current ERS “annex” building. The new building will address current and future space needs for ERS, and will have excess capacity that ERS can lease to third-party tenants to generate revenue. Business model projections show that the lease revenue from the new building will cover the cost of construction, and generate a return for the Trust.

An initial design, called the “Edge”, was initially selected and approved. The design/build team then began work to further develop the design during the Schematic Design phase. The Schematic Design was approved at the end of July 2018. The building features an offset core, which allows large floorplates that are attractive to commercial tenants. Other design decisions included parking, access for tenants, customers and freight, and ERS space needs. It was determined that ERS office space would take up a portion of the fifth floors of the new building with a sky-bridge connection between the existing ERS building and the new building. The design build team continues to refine the structure and design and is scheduled to complete 100% Design Drawings in November. From there, the team will develop a guaranteed maximum price for construction. The Board will consider that proposal at their December 2018 meeting.

The City of Austin approved ERS’ rezoning change in June 2018 from a general commercial services and commercial liquor sales district to the Central Business District. This allows ERS to maximize the height potential on the site. The site is subject to the city’s Capitol View Corridors. The ERS team has been working with Austin Energy to locate the key electrical systems that will be required for the new building. ERS received the Capitol View Corridor Elevation Determination and have submitted an application for a site development permit based on the amount of work to be done in the city’s right-of-way.

After a Request for Qualifications (RFQ) process, ERS selected NV5 to serve as the independent architect engineer for the duration of the project. This is a requirement under state law when a design build process is underway. Mr. Wilson informed the board that ERS will be publishing an RFQ in the fall for an independent engineer for construction materials, engineering, and testing and inspection service. This is another requirement of state law. Mr. Wilson then introduced Peter Jansen with CBRE to discuss the marketing of the building. ERS selected CBRE as the real estate brokers for the project. Mr. Jansen reported on the marketing activities and tenant outreach that CBRE has done to date. Mr. Jansen said that the Austin market is incredibly active right now, and tenant activity has led to an unbelievable compression and limited availability in the office market right now. He said the firm is very excited to take this building to market.

Bob Sessa, ERS Director of Real Estate, introduced Chad Marsh of Endeavor Real Estate Group. Endeavor has been in the Austin market for 20 years and has done some prominent projects such as the Domain. The firm is not involved in the ERS project. Mr. Marsh provided an assessment of the current Austin real estate market and future prospects for the Central Business District and Austin innovation district. Austin continues to be a sought after location for commercial tenants, based on Endeavor’s market data and analysis. Endeavor’s data shows that of the 6.7 million square feet of office space that has been delivered in the Austin market since 2014, 91% is leased and about 9% is out for execution. Another 3.9 million square feet is currently under construction and 54% of that space has been pre-leased.

Mr. Marsh said that ERS has an advantage in the market because of its long term investment perspective. The building will be located in a part of town that is becoming more relevant and attractive to tenants due to its proximity to the University of Texas, the medical school, state government and the central business district. He believes that a lot of different users will be interested in the ERS development. Mr. Marsh advised the board that designing a retail space on the ground floor of the building is attractive to potential tenants and often key to energizing a particular part of the city, which bodes well for this part of the city.

This agenda item was presented for information and discussion purposes only. There was no further discussion or questions and no action was taken.

8.3 Consideration and Approval of the ERS Fiscal Year 2019 Proposed Operating and Capital Budgets – (ACTION)

Mr. Porter Wilson presented the ERS Fiscal Year 2019 Proposed Operating and Capital Budgets for board approval. The budget includes the FY19 major initiatives for which funding is requested within the budget. Initiatives include providing information to the 86<sup>th</sup> Texas Legislature on the pension plans, the Texas Employees Group Benefits Program and other ERS programs and operations. Investment staff will continue to develop the directional growth portfolio and develop an opportunistic credit asset class as part of the asset allocation. Staff will conduct a two-year review of the 2017 Board approved pension trust assumed rate of return for board approval in August of 2019. Mr. Wilson reported that staff are developing an informal video series about how ERS invests for its members and retirees. He also stated that a solicitation for a third-party administrator for the TexaSaver 401(k)/457 program will be conducted. Another initiative for 2019 is expanding access to mental health services by activating virtual visits for mental health, as well as developing goals and structure for the group benefits wellness program and continuing to pursue innovative cost containment ideas and programs for the group benefit program.

In continuing with the major initiatives, staff will continue to conduct outreach to group benefit program participants for feedback on insurance programs, conduct Summer and Fall enrollment for members, and conduct the Board of Trustees Election. Staff will complete implementation of Sunset Commission recommendations and policy changes. ERS will also evaluate, select and implement a new benefits administration services vendor to upgrade system functionality for benefits eligibility and enrollment, replacing a system that was implemented in 2000. Staff will continue to enhance data quality and data analytics capabilities. The budget also includes funds to relocate staff from the annex into existing space in the main ERS building to prepare for new building construction. ERS will also conduct an enterprise risk management assessment, develop and implement plans to address opportunities identified in the Survey of Employee Engagement, and evaluate and refine the agency's succession plan. Mr. Wilson then turned the presentation over to Ms. Machel Pharr, Chief Financial Officer, to walk the board through the specifics of the 2019 budget.

Staff is proposing an increase of \$3.9 million, or 4.9% for a total of \$82.3 million for the FY19 operating budget. A majority of the budget, 62%, is used for salary and salary-related expenses. Salary and salary related increases include a proposal to add six new positions. The six positions equate to five and one-half full time employees because staff proposed to add one of the positions mid-year. The positions include one in the Investments division focused on research/expansion of hedge funds, one in the Group Benefits division for grievance administration, one in the Customer Benefits division for the Business Integration Team, one for the Information Systems division for IT asset management, one for the Operations Support division for facility and property project management, and one for Office of Procurement & Contract Oversight division for contract management and oversight, scheduled to be funded mid-year.

Ms. Pharr reported that \$289,000 is included as a result of the investment salary compensation study and \$5.45 million in the budget for payments as part of the incentive compensation plan. Significant reductions in the initial budget included the cost of renting on computer software equipment by \$310,000 and eliminating one-time costs of \$94,000 for professional consulting related to communication projects, and an executive search contract, as well as building improvements of \$150,000 related to the freight elevator.

Significant drivers that are not related to salaries included in the 2019 budget are an increase for investment consultants (\$457,000), insurance audit services (\$219,000), postage (\$190,000) and consulting services (\$130,000). Staff also expect an increase in actuarial services for Fiscal Year 2019.

Ms. Pharr announced that staff are anticipating moving forward with a contract for the Benefits Administration Services (BAS). Staff are proposing to continue to use the \$315,000 included in the 2018 operating budget, plus an additional \$207,000 from the Fiscal Year 2019 for independent validation and verification and project management services related to the project. Also included in the proposed 2019 budget is \$225,000 for systems for procurement and contract management oversight.



In the proposed 2018 capital budget, staff are including approximately \$11.1 million which is related to the new building, consulting and architectural services as well as \$550,000 for renovation of the existing building. Ms. Pharr announced that a budget adjustment will be presented to the board at its December meeting for the design/build building contract award recommendations.

Mr. Hester questioned what lead to ERS being under budget for Fiscal Year 2018 by over \$3 million. Ms. Pharr responded that some of it is due to vacant positions and turnover. The largest contributing factor were projections for incentive compensation plan payouts that were above actual payout based on Trust performance. She noted that ERS doesn't budget 100% of salaries for the three larger divisions. She stated that positions have tended to be filled for longer and have had fewer turnovers during this past year. The overall vacancy trend used for 2019 is 2%. Any money not spent in a fiscal year remains in the Trust.

Ms. Melvin praised Ms. Pharr and staff for going through a very mindful exercise each year to look for cost savings.

Mr. Hester then asked the board to consider in addition to the budget, a \$300,000 compensation pool that management could use for employees that are not covered under the incentive compensation plan for Fiscal Year 2019.

There being no further discussion or questions, Mr. Danzeiser opened the floor for a motion.

**Move** that the Board of Trustees of the Employees Retirement System of Texas approve the fiscal year 2019 Proposed Operating Budget, including the addition of a compensation pool in the amount of \$300,000 to be used at the discretion of the Executive Director for retention and recruitment of staff not eligible for the Incentive Compensation Plan and the Capital Budget for the Employees Retirement System that Texas has presented, and authorize the Executive Director to administer the operating and capital budgets as necessary for the efficient and effective administration of the system, and authorize the transfer of interest account as required to fund the operating and capital budget.

Motion by Craig Hester, second by Cydney Donnell.

Final Resolution: Motion Carries

Aye: Craig Hester, Cydney Donnell, Doug Danzeiser, Ilesa Daniels, Catherine Melvin

## 9. EXECUTIVE DIRECTOR REPORT

### 9.1 Executive Director Agency Update

**Fiscal Year 2019-2023 Strategic Plan** – ERS uses an interactive biennial process for developing the agency's strategic plan and updating guidelines for long-term goals, initiatives and spending to support the ERS mission and address critical needs. Staff reaffirmed the agency mission: ERS offers competitive benefits to enhance the lives of its members. ERS maintained the same four strategic goals related to the pension, insurance, stakeholder engagement and agency performance and accountability.

**Legislative Appropriation Request for Fiscal Year 2020-2021** – The State set ERS' base-level funding for each year of the 2020-2021 biennium at the projected 2019 levels. The retirement and group benefit programs were exempt from a mandated 10% budget reduction that other state agencies were subject to when doing their appropriations request. Funding requests above the base funding levels are considered exceptional items and must be itemized, prioritized, and justified in the Legislative Appropriation Request.

ERS requested additional funding for the pension program to the actuarially sound contribution rate. The ERS retirement fund requires 23.33% of payroll in order to be considered actuarially sound. The additional funding for the 2020-2021 biennium would be around \$531 million. The Law Enforcement and Custodial Officer Supplemental (LECOS) retirement program has a \$75.6 million additional funding need for biennium to become sound and the Judicial Retirement System 2 requires a 23.98% contribution rate to become sound, which would be around \$1.4 million.

ERS did not request any exceptional item funding request for the 2020-2021 biennium. The program will have sufficient funding at FY19 base levels, due to the program savings from the contracts for medical and pharmacy benefit administration.

**Survey of Employee Engagement Results** – the ERS employee response rate was exceptional at 92%. ERS' overall score was 401, an increase of 10 points over the 2016 rate of 391. Scores above 400 are the product of a highly engaged workforce. The survey is designed to assess the overall climate at ERS with the results below:

Atmosphere: Safe and free of harassment.  
Score: 431 – substantial strength. (2016 Score: 420)

Ethics – Employees are ethical in their behavior and ethical violations are appropriately handled.  
Score: 429 – substantial strength (2016 Score: 424)

Fairness: Employees believe that equal and fair opportunity exists for them and others.  
Score: 407 – strength. (2016 Score: 396)

Feedback: The opportunity to provide information so improvements can occur.  
Score: 356 – although lower than other categories, still considered a strong and desirable score. (2016 Score: 352)

Management: The extent to which ERS leadership is accessible, visible and effectively communicate.  
Score: 389 – strength. (2016 Score: 382)

**Summer Enrollment for Plan year 2019** – The enrollment period was from June 25 – July 27, 2018. ERS mailed out 268,901 personal benefit enrollment statements, 51,598 members made coverage changes, and ERS and ACT received 10,612 enrollment phone calls. ERS conducted Summer Enrollment fairs around the state, along with webinars to allow members to receive important benefits information and ask questions.

**Fall Enrollment for Plan Year 2019** – Retirees enrolled in Medicare can make benefits changes for themselves and their families. The enrollment period is from October 29 – November 16, 2018. Enrollment fairs will be held in most major cities and webinars for those who are not able to attend a fair in person.

## 10. EXECUTIVE SESSION

10.1 Executive Session – In accordance with Section 551.074, Texas Government Code, the Board of Trustees will meet in executive session to evaluate the duties, performance and compensation of the Executive Director of the Employees Retirement System of Texas. Thereafter, the Board may consider appropriate action in open session.

Mr. Danzeiser stated it was 4:07 p.m. on August 29, 2018. In accordance with Section 551.074, Texas Government Code, the ERS Board of Trustees will meet in executive session to evaluate the duties, performance, and compensation of the executive director of the Employees Retirement System of Texas. Thereafter, the Board may consider appropriate action in open session.

Upon returning from executive session, Mr. Danzeiser announced it was 6:07 p.m. on August 29, 2018, and the Board is now in open session. No action, decision, or vote was taken by the Board while in executive session. Mr. Danzeiser then stated he will entertain any motion from members of the Board at this time.

Ms. Donnell acknowledged Mr. Wilson for his considerable progress on achieving the strategic directions for the agency and how much time he has devoted to the agency and care of its operation.

**Move** that the Board of Trustees of the Employees Retirement System of Texas award the ERS Executive Director, Porter Wilson, an increase in his annual compensation of 5% of his Fiscal Year 2018 annual salary effective September 1, 2018. Further move that the Executive Director be awarded the maximum Incentive Compensation Plan award for which he is eligible based on his participation in the

Incentive Compensation Plan for the Fiscal Year 2018, for the qualitative 75% of his 50% which reflects his leadership and management accomplishments for the year, and for the quantitative, 100% of his 50% which is based on trust fund performance.

Move that the Board of Trustees of the Employees Retirement System of Texas affirm that effective September 1, 2018, Porter Wilson, ERS Executive Director, is approved to participate in the ERS Incentive Compensation Plan (ICP) for key investment professionals and leadership employees as a leadership employee with a maximum award percentage available of 100% of his salary in accordance with the terms of the plan. Further move that Mr. Wilson's performance goals for the Plan Year 2019 should reflect 50% of his possible award under the ICP as a quantitative goal based on relative trust fund performance. And 50% of his possible award under the ICP should be a qualitative goal reflecting his overall agency leadership, management, communications, policy matters, staff development and implementation of the agency strategic initiatives as reflected in the board approved operating budget for fiscal year 2019.

Further move that the Board of Trustees of the Employees Retirement System of Texas use the agency initiatives identified in the fiscal year 2019 operating budget and approved by the board to evaluate the executive director's job performance by measuring the initiatives against the accomplishments reported in fiscal year 2020 operational budget.

Motion by Cydney Donnell, second by Craig Hester.

Final Resolution: Motion Carries

Aye: Craig Hester, Cydney Donnell, Doug Danzeiser, Ilesa Daniels, Catherine Melvin

## **11. BOARD CHAIR ELECTIONS**

### 11.1 Election of Chair and Vice-Chair of the ERS Board of Trustees for Fiscal Year 2019 – (ACTION)

Texas Government Code, Title 8, Section 815.201, provides that the Board shall elect new officers from its membership. As a result of such an election, the newly elected Chair and Vice-Chair of the ERS Board of trustees will each serve a one-year term beginning September 1, 2018 and ending August 31, 2019.

Ms. Melvin thanked Chair Danzeiser for his service as chair over this past year.

**Move** that the Board of Trustees of the Employees retirement System of Texas elect Craig Hester as Chair and Ilesa Daniels as Vice-Chair of the ERS Board of Trustees for one-year terms beginning September 1, 2018 and ending August 31, 2018.

Motion by Catherine Melvin, second by Cydney Donnell.

Final Resolution: Motion Carries

Aye: Craig Hester, Cydney Donnell, Doug Danzeiser, Ilesa Daniels, Catherine Melvin

## **12. CALENDAR**

### 12.1 Confirm date for the next Joint meeting of the ERS Board of Trustees and Investment Advisory Committee, the next meeting of the Board of Trustees, and the next meeting of the Audit Committee

Mr. Danzeiser reminded the board the next meeting is scheduled for Tuesday, December 11, 2018 and Wednesday, December 12, 2018. Mr. Wilson also noted this was the last meeting held in the ERS Board room due to building renovation. The December meeting will be held at the Teacher Retirement System of Texas office.

## **13. ADJOURNMENT**

### 13.1 Adjournment of the ERS Board of Trustees meeting

The Board of Trustees adjourned at 6:14 p.m. on August 29, 2018.