

THE INVESTMENT COMMITTEE
OF THE
MARYLAND STATE RETIREMENT AND PENSION SYSTEM

MINUTES OF OPEN MEETING

September 20, 2016

The Investment Committee convened on Tuesday, September 20, 2016 at 9:03 a.m. in the 16th Floor Board Room of the State Retirement Agency, SunTrust Building, 120 E. Baltimore Street, Baltimore, MD.

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| Committee Members Attending: | Michael K. Barry David Brinkley James A. Bush, Jr. James “Chip” DiPaula Peter Franchot Kenneth Haines David Hamilton James Harkins Eric Brotman Stefan Strein | Sheila Hill Linda A. Herman, Co-Chair F. Patrick Hughes, Chairman Larry E. Jennings, Jr. Charles W. Johnson Nancy K. Kopp Theresa Lochte Richard Norman |
| Committee Members Not Attending: | Eric Brotman Stefan Strein | |
| Also Attending: | Victor Adekoya Phillip Anthony, MLIS Frank E. Benham (Meketa) Nathan Bowen, DBM Colleen Bower Kathy Brady, OAG Susanne Brogan Robert Burd, Deputy CIO Elizabeth Burton Antionette Butcher Rachel Cohen, OAG Melody Countess Eric Farls Chris Farrington, Pavilion Alternatives David Ferguson Anne Gawthrop Michael Golden Dimitri Grechenko Dana Johns Faina Kashtelyan | Larry Katsafanas Dean Kenderdine John Kenney Thomas Kurowski, Alex Brown Michelle Lowery Kent B. Miller, Brown Capital Mgmt. Mary Mustard (Meketa) Stephen Muturi Andrew Palmer, CIO Stephen Reilly David Rongione, Chief Internal Auditor, Internal Auditing Div. Michael Rubenstein, MLIS Jody Shaw, OAG Frederick “Beau” Smith Dana Tagalicod, MLIS Toni Voglino Brad Young, Pavilion Alternatives |

Mr. Hughes, Chairman, called the Investment Committee meeting to order at 9:03 a.m.

Item 1: Minutes

On a motion made by Mr. Harkins and seconded by Ms. Lochte, the Investment Committee unanimously approved both the May 6, 2016 and August 16, 2016 Special Investment Committee open meeting minutes.

Item 2: Pavilion Alternatives Group Report

Brad Young and Chris Farrington presented a market overview and private equity portfolio review to the board, and an update on firm developments which included Pavilion Financial Corporation's acquisition of Altius and merger with LP Capital Advisors to create Pavilion Alternatives Group.

Mr. Jennings requested charts provide a deeper analytical picture of the portfolio performance. Ms. Herman expressed interest in peer comparison reporting. Mr. Palmer will work with Mr. Jennings and Ms. Herman on making the private equity performance slides more consumable. Mr. Jennings will provide Mr. Palmer with examples of reports from other investment committees that he is on, that he feels may be more acceptable.

Mr. Farrington talked about the emerging manager program which started officially in 2011. He mentioned that Maryland is hosting an emerging manager conference featuring National Association of Investment Companies (NAIC) members on October 25th.

Mr. Hughes asked that future Pavilion reports provide more granular information on portfolio performance of the buyout and venture capital exposures and asked for clarification on the discrepancy in performance for emerging managers and the Private Equity portfolio.

Item 3: Meketa Reports

Meketa Investment Group presented the Second Quarter of 2016 performance update and current market overview to the Committee.

Mr. Jennings questioned the benchmark used for cash. Mr. Palmer responded that the cash returns include the earnings from the securities lending program. Mr. Palmer indicated that staff will work with State Street to show the performance of the cash equivalents investments relative to appropriate benchmarks and a total cash performance that includes the securities lending and any other income.

Ms. Mustard gave an activity update of the summary of work to date and potential future agenda topics which included education classes on private infrastructure and hedge funds. Mr. Hughes looks forward to a Hedge Fund primer and what is the role in the portfolio.

Item 4: Report from CIO

Mr. Palmer informed the Committee of ongoing projects including transition to the 2016 asset allocation, recruiting, resources, ETI investing (Senate Bill 982) and education initiatives.

Mr. Brinkley encouraged Mr. Palmer to meet with Department of Commerce regarding Senate Bill 982. Mr. Palmer informed the committee that he and staff have met with TEDCO which is part of the Department of Commerce. There is an RFI in process to select an external manager to run this program.

Treasurer Kopp asked if Staff could provide information that shows success in reducing fees with existing managers. Mr. Palmer indicated that staff can track fee reductions negotiated with existing managers, but this would be more difficult to quantify and track in negotiating improved economics and terms prior to contract execution.

Mr. Palmer reported that during the quarter there have been ongoing manager transitions. Mr. Hughes said that specific managers would be discussed in Closed Session. Mr. Palmer discussed Staff's estimate of the transaction costs associated with implementing the Asset Allocation targets adopted by the Board in September. Through January, Staff estimates transaction costs of between \$15 and \$20 million. Ms. Herman asked if Staff employed any transition managers in this process. Mr. Katsafanas replied that State Street was used for the full redemptions and the fixed income managers transitioned themselves to reflect the new benchmarks.

The Joint Committee on Pensions submitted an inquiry on "how the State Retirement and Pension System factors the growing risk of climate change into the pension fund's investments." Mr. Farls presented the response to the committee.

Mr. Farls discussed the System's current practices regarding climate change and how the System addresses climate change. One recommendation noted by Mr. Farls was to obtain an estimate of the portfolio's carbon footprint. Recognizing that information is incomplete and methodologies are still developing, Staff believes that beginning to measure the risk is a first step in managing the risk. Staff does not recommend policy targets for investments to reduce exposure to high carbon companies or to promote transformation (wind farms, solar, etc.) Staff does recommend an evaluation of the System's allocation to natural resources, infrastructure and commodities, in light of the Paris Accord, during the next asset allocation review with its general consultant.

Ms. Herman requested information on the System's exposure to the top 200 worst fossil fuel offenders per 350.org.

Item 5: Investment Policy Manual Amendments

The Investment Policy Manual was updated to reflect all items approved by the Investment Committee since the last update in March 2016, as well as adding clarifying language regarding personal trading by staff and the language related to OPEB (Other Post-Employment Benefits). The sections of the IPM that were updated include asset allocation, benchmarks, asset class ranges/constraints, staff trading in public securities and OPEB.

A red-lined version of the changes was included in the agenda packet and a clean version will be posted to the Agency website subject to final Board approval at the September 20, 2016 meeting.

ACTION

On a motion made by Ms. Herman and seconded by Ms. Hill, the Investment Committee unanimously approved the proposed changes to the Investment Policy Manual.

Item 6: ORP Update

Mr. Burd provided an update on the Optional Retirement Program. He informed the committee that in order to move from TIAA's existing individual contract structure to a new Retirement Choice contract, SPP §30-206 would need to be repealed and replaced with language that would allow the Board to enter into a group annuity contract. Mr. Burd indicated that legislation was recommended by staff and accepted by the Administrative Committee at its September 6, 2016 meeting. This proposed legislation would be included in the 2017 Board-requested legislative package that will be presented for approval by the full Board on September 20, 2016.

Mr. Burd also updated the committee on the Board's ability to add brokerage account options to allow greater investment choice flexibility for ORP participants. While the Office of the Attorney General advises that the Board has the authority under SPP §30-202 to offer a brokerage account option, staff would like to defer making a recommendation until the November 17, 2016 Investment Committee meeting as it considers the timing of implementation.

Ms. Herman asked that staff and Counsel take appropriate measures to protect the Board from potential liability resulting from participant brokerage accounts.

Item 7: Investment Reports

The Committee received the following investment reports:

- State Street Performance Reports
- Private Markets Performance Reports
- Quarterly TUCS Reports
- Securities Lending Report
- Division's FY17 Travel Plan - Update
- Quarterly ORP Performance Report
- New Hire Manager Report

On the Directors Desk:

- Broker Commission Reports
- OPEB-PHBT Update

On a motion made by Ms. Lochte and seconded by Mr. Bush, the Investment Committee voted without objection to go into closed session at 11:10 a.m. Ms. Cohen read the updated language for Item 8(d), Motion to meet in closed session.

(a) reviewing the closed session Investment Committee and special Investment Committee meeting minutes, pursuant to General Provisions Art., Section 3-103(a)(1)(i), the exercise of an administrative function;

(b) hearing a presentation by Investment Division staff of a Terra Maria Program restructuring pursuant to General Provisions Art., Section 3-305(b)(5), to consider the investment of public funds, and 3-305(b)(13), to comply with a specific statutory requirement that prevents public disclosure, namely, General Provisions Art., Section 4-335 preventing the disclosure of trade secrets and confidential commercial or financial information;

(c) discussing matters regarding the investment of public funds with staff, pursuant to General Provisions Art., Section 3-305(b)(5).

(d) discussing the System's investment and elimination of a position in a fund pursuant to General Provisions Art., Section 3-305(b)(5), to consider the investment of public funds; General Provisions Art., 3-305(b)(13), to comply with a specific statutory requirement that prevents public disclosure, namely, General Provisions Art., Section 4-335 preventing the disclosure of trade secrets and confidential commercial or financial information; General Provisions Art., Section 3-305(b)(7), to consult with counsel to obtain legal advice; and General Provisions Art., Section 3-305(b)(8), to consult with staff, consultants, or other individuals about pending or potential litigation;

(e) conducting an evaluation of the CIO's performance pursuant to General Provisions Art., Section 3-305(b)(1), consideration of a personnel matter.

CLOSED SESSION

Committee Members
Attending:

Michael K. Barry
David Brinkley
James A. Bush, Jr.
James "Chip" DiPaula
Peter Franchot
Kenneth Haines
David Hamilton
James Harkins

Sheila Hill
Linda A. Herman, Co-Chair
F. Patrick Hughes, Chairman
Larry E. Jennings, Jr.
Charles W. Johnson
Nancy K. Kopp
Theresa Lochte
Richard Norman

Committee Members
Not Attending:

Eric Brotman
Stefan Strein

Also Attending:

Victor Adekoya
Frank E. Benham (Meketa)
Colleen Bower
Kathy Brady, OAG
Susanne Brogan
Robert Burd, Deputy CIO
Elizabeth Burton
Antionette Butcher
Rachel Cohen, OAG
Melody Countess
Eric Farls
David Ferguson
Anne Gawthrop
Michael Golden
Dimitri Grechenko

Dana Johns
Faina Kashtelyan
Larry Katsafanas
Dean Kenderdine
John Kenney
Michelle Lowery
Mary Mustard (Meketa)
Stephen Muturi
Andrew Palmer, CIO
Stephen Reilly
David Rongione, Chief Internal
Auditor, Internal Auditing Div.
Jody Shaw, OAG
Frederick "Beau" Smith
Toni Voglino

Adjournment

There being no further business before the Investment Committee, on a motion made and seconded, the meeting adjourned.

Respectfully submitted,



Andrew C. Palmer
Chief Investment Officer