

AGENDA ITEM DETAILS

- Subject:** Consideration of Consent Agenda – (Action)
- Minutes to the December 5, 2023 Joint Meeting of the Board of Trustees and Investment Advisory Committee
 - Minutes to the December 6, 2023 Audit Committee Meeting
 - Minutes to the December 6, 2023 Board of Trustees Meeting
 - Consideration of Internal Audit Administrative Items:
 - o Internal Audit Charter
 - o Audit Committee Charter
 - Texas Employees Group Benefits Program: Annual Non-Financial Performance Measure Update
 - Texas Employees Group Benefits Program: HealthSelect Medicare Plans Compliance and Operational Updates for Calendar Year Programs
 - TexaSaver Plan Compliance and Operational Updates
 - Quarterly Performance of TexaSaver Investment Options
 - Annual Review of Securities Lending Program

RECOMMENDED ACTION:

Move that the Board approve all items on the Consent Agenda as presented.

The Board may approve all items on the Consent Agenda through one motion. Trustees should review the materials related to the Consent Agenda prior to the meeting, and any trustee may request that an item be removed from the Consent Agenda in order to allow for full discussion of the item. Once there is a motion to approve the items on the Consent Agenda, trustees may ask simple questions, request clarification, or engage in brief dialogue regarding any item before voting.

The Consent Agenda includes the following agenda items as presented below:

Minutes to the December 5, 2023 Joint Meeting of the Board of Trustees and Investment Advisory Committee

The minutes to the Employees Retirement System of Texas Joint Meeting of the Board of Trustees and Investment Advisory Committee held on December 5, 2023 are included with this agenda item as **Exhibit A**.

Minutes to the December 6, 2023 Audit Committee Meeting

The minutes to the Employees Retirement System of Texas Audit Committee Meeting held on December 6, 2023 are included with this agenda item as **Exhibit B**.

Minutes to the December 6, 2023 Board of Trustees Meeting

The minutes to the Employees Retirement System of Texas Board of Trustees meeting held on December 6, 2023 are included with this agenda item as **Exhibit C**.

Consideration of Internal Audit Administrative Items:

The Internal Audit Charter is presented annually to highlight any changes in audit standards and to inform new Trustees of the standards by which the Internal Audit division operates. The Audit Committee Charter is presented to inform new Trustees of the purpose and responsibilities of the Audit Committee. No changes or updates were identified for the Internal Audit Charter (**Exhibit D**) or the Audit Committee Charter (**Exhibit E**) by the Internal Audit Director and these items are provided for informational purposes only.

Texas Employees Group Benefits Program: Annual Non-Financial Performance Measure update

Non-financial performance measures for the Group Benefits Program are provided annually to the board. These measures include assessments of network, how HealthSelect benefits compete in the marketplace, utilization, participant satisfaction and the progress towards goals identified for the Assess, Manage, and Prevent (AMP) Wellness initiative. These performance measures are included in **Exhibit F**. New and updated performance measures are provided in a separate agenda item.

For the most part, the plans are performing well when compared to targets. Measures that are not performing well against targets or require further discussion are included in another agenda item. The AMP measures continue to be aspirational with slow progress on annual PCP visits and condition program utilization. ERS hopes that new wellness program and communication campaign will make it easier for participants to engage with their health and benefits to move improve well-being and move the needle on AMP metrics.

Texas Employees Group Benefits Program: HealthSelect Medicare Plans Compliance and Operational Updates for Calendar Year Programs

The Employees Retirement System of Texas (ERS) manages health insurance benefits according to the Texas Employees Group Benefits Act as set forth in Chapter 1551 of the Tex. Ins. Code. The Texas Employees Group Benefits Program (GBP) provides access to competitive and comprehensive benefits. The GBP provides health insurance benefits to more than half a million state agency and higher education employees, retirees and their family members. ERS manages the GBP and optional benefits in a manner compliant with applicable regulations while offering the best value to members and participants. ERS manages this commitment by developing and actively administering effective vendor contracts.

Calendar year reporting. On an annual basis, staff provides a summary to the Board of the vendor's performance for those plans reporting on a calendar year basis -- the HealthSelectSM Medicare Advantage Plan (MA PPO) and HealthSelectSM Medicare Rx Plan. Additionally, **Exhibit H** provides the compliance and plan summaries for the optional benefit plans reporting on a calendar year basis. **Exhibit I** reports the enrollment for the applicable GBP plan.

Overall, contract compliance for the HealthSelect of Texas Medicare plans remains high. The vendors report adherence to contractual Performance Guarantees (PGs) using the Monthly Administrative Performance Report (MAPR). For calendar year 2023, the vendors reported one moderate noncompliance issue only.

UnitedHealthcare (Sierra Health)
HealthSelect MA PPO
Vendor Performance Overview, CY 2023

PG Severity	PG Category	Vendor Performance Results	PG Review Period	PG Performance Assessment Determination
1	Emergency Performance Guarantees (PG)	No noncompliant PGs	N/A	N/A
2	Critical PG	No noncompliant PGs	N/A	N/A
3	Moderate PG	1 moderate PG assessed	07/2023	98.51% accurate claims processing
4	Minor PG	No noncompliant PGs	N/A	N/A

UnitedHealthcare
HealthSelect Medicare Rx Plan
Vendor Performance Overview, CY 2023

PG Severity	PG Category	Vendor Performance Results	PG Review Period	PG Performance Assessment Determination
1	Emergency Performance Guarantees (PG)	No noncompliant PGs	N/A	N/A
2	Critical PG	No noncompliant PGs	N/A	N/A
3	Moderate PG	No noncompliant PGs	N/A	N/A
4	Minor PG	No noncompliant PGs	N/A	N/A

Plan Management

As part of plan management oversight, ERS:

- Ensures contracts requirements are met, services are performed timely, and financial interests are protected;
- Works with contracted vendors to provide a plan with comprehensive benefit offerings, wellness programs, and educational tools; and
- Evaluates the effectiveness and efficiency of GBP programs through data analytics, research and regular evaluation of best practices. Each program has its own eligibility rules and processing requirements.

Contracting and Vendor Performance Management

Each vendor contract defines the specific administrative services and deliverables to be performed in connection with the applicable benefit program. Staff monitors each vendor’s adherence to the contractual requirements, including PGs. Financial assessments may result if a vendor fails to meet the performance standards defined within the contract. **Exhibit G** provides an overview of the contract monitoring process.

Background/Analysis:

HEALTHSELECT MEDICARE PLANS

- **HealthSelect Medicare Advantage Plan, a preferred provider organization (HealthSelect MA PPO) (Medical Only)**

ERS has offered the HealthSelect MA PPO since January 1, 2012. On May 20, 2020, the ERS Board of Trustees awarded the HealthSelect MA PPO contract to UnitedHealthcare Inc. (Sierra Health)

following a competitive Request for Proposal (RFP) process. Sierra Health became the plan's insurer on January 1, 2021, with a contract period through December 31, 2026.

The HealthSelect MA PPO plan continues to provide the most cost-effective medical benefits for Medicare-enrolled GBP participants. Even with the ability to opt out of the plan, most participants remain in HealthSelect MA PPO as they become more familiar with the plan's favorable benefit coverage and lower dependent monthly contribution costs.

Plan eligibility. A retiree must have 10 years of service credit to be eligible for GBP retiree insurance. To enroll in the HealthSelect MA PPO medical plan, a retiree must provide ERS with his/her Medicare Beneficiary Identifier (MBI). All participants must be enrolled in Medicare Part A and Part B (primary coverage).

Plan design. The HealthSelect MA PPO provides fully-insured medical benefits to Medicare-enrolled retirees and their Medicare-enrolled dependents. The medical benefits are designed to provide coverage that is at least as comprehensive as that provided under HealthSelect of Texas[®]. ERS pairs the fully-insured HealthSelect MA PPO plan with the self-funded HealthSelectSM Medicare Rx plan administered by UnitedHealthcare.

- **HealthSelect Medicare Rx Plan, prescription drug plan**

The HealthSelect Medicare Rx prescription drug plan provides prescription drug benefits to HealthSelectSM Secondary (Medicare-primary participants) and HealthSelect MA PPO participants.

Plan design. The HealthSelect Medicare Rx plan provides standard Part D coverage through a self-funded Employer Group Waiver Plan (EGWP) with secondary coverage through a self-funded wrap-around (Wrap) arrangement. The Wrap covers those prescription drugs not covered under Part D but available through the Wrap.

Due to Medicare Part D rules, a participant can be enrolled in only one Medicare Part D plan. Therefore, if a retiree elects to enroll in an alternate Medicare Part D plan and opt out of the HealthSelect Rx plan, there is no alternate HealthSelect prescription drug coverage available through the GBP.

Texa\$aver Plan Compliance and Operational Updates

Texa\$averSM 401(k) and 457 Program

The ERS Board of Trustees serves as both Trustee and Plan Administrator for the Texa\$averSM 401(k) and 457 Program (collectively known as the Texa\$aver program). The Texa\$aver program is a voluntary defined contribution program that aims to assist participants in accumulating supplemental assets for retirement, in compliance with Sections 401(k) and 457(b) of the Internal Revenue Code (IRC) and other governing statutes and regulations. The program provides participants with diversified investment choices to meet their varying levels of needs and risk tolerance. Participants can elect to use Texa\$aver investments to supplement the ERS-defined benefit retirement annuity.

During its May 22, 2019 meeting, the ERS Board of Trustees awarded the program's third-party administrative (TPA) services contract to Great-West Life & Annuity Insurance Company (Empower), and the investment advisory services contract to Advised Assets Group, LLC (AAG). Both contracts were awarded for six-year terms. AAG has rebranded and is now Empower Advisory Group, LLC (EAG).

Calendar year reporting. On an annual basis, staff provides a summary to the Board of vendor performance related to specific administrative services and deliverables defined within the contract's Performance Guarantees (PGs). Staff monitors each vendor's adherence to the contractual requirements, and assessments may result if a vendor fails to meet the PG standards defined within the contract. Empower reports adherence to contractual Performance Guarantees using the Monthly Administrative Performance Report (MAPR). EAG provides separate monthly reports reviewed by internal staff for documenting within a Monthly Monitoring Report (MMR).

Exhibit G provides a general overview of the contract monitoring process and a summary of vendor compliance is below. TexaSaver Program enrollment and contribution information for calendar year 2023 is provided in **Exhibit J**.

For calendar year 2023, vendor compliance remains high among both the TPA and advisory services contracts. Empower reported only one (1) instance of noncompliance with a PG category of Minor. EAG reported four (4) instances on noncompliance with a PG Category of Minor. Three (3) of the four (4) instances of noncompliance are pending further review of the metric’s methodology and have not been assessed to EAG at this time.

Empower
TexaSaverSM 401(k) and 457 Program
Vendor Performance Overview, CY 2023

PG Severity	PG Category	Vendor Performance Results	PG Review Period	PG Performance Assessment Determination
1	Emergency Performance Guarantees (PG)	No noncompliant PGs	N/A	N/A
2	Critical PG	No noncompliant PGs	N/A	N/A
3	Moderate PG	No noncompliant PGs	N/A	N/A
4	Minor PG	1 PG pending assessment	CY2023	Participant Satisfaction Rate 88.00% vs. \geq 90.00%

EAG
TexaSaver Advisory Services
Vendor Performance Overview, CY 2023

PG Severity	PG Category	Vendor Performance Results	PG Review Period	PG Performance Assessment Determination
1	Emergency Performance Guarantees (PG)	No noncompliant PGs	N/A	N/A
2	Critical PG	No noncompliant PGs	N/A	N/A
3	Moderate PG	No noncompliant PGs	N/A	N/A
4	Minor PG	1 PG assessed 3 PGs pending review	Jan, Feb, Mar	Q1: Interval Service Level (calls answered) 41.00% vs. \geq 80.00%
			Apr, May, Jun	Q2: Interval Service Level Pending review
			Jul, Aug, Sep	Q3: Interval Service Level Pending review
			Oct, Nov, Dec	Q4: Interval Service Level Pending review

Plan Management

As part of plan management oversight, ERS:

- Ensures contracts requirements are met, services are performed timely, and financial interests are protected;

- Works with contracted vendors to provide educational tools and resources, customer service, and diverse investment options;
- Evaluates the effectiveness and efficiency of the program through data analytics, research and regular evaluation of best practices.

Quarterly Performance of TexaSaver Investment Options

The State of Texas established the TexaSaverSM 401(k) / 457 Program to attract and retain state employees and officials by offering participants an opportunity to increase their retirement income through voluntary investments. Participation in the program is voluntary and all investment decisions are directed by participants.

Since 2008, new state employees are automatically enrolled in the 401(k) program at 1% of their salary, although they may opt out. Unless they make an investment election, participants are defaulted into a retirement target date fund, for which the vintage varies according to their current age. Participants bear the investment risk associated with the products they select from the investment options offered within the program's lineup. This includes the risk associated with asset allocation. The Board does not bear any investment risk, but it has the fiduciary responsibilities of ensuring the program is well managed and acting in the best interest of program participants as outlined within the program's Investment Policy. Texas Government Code § 609.502(a) gives the ERS Board ultimate authority to determine which investment products are offered within the program's lineup.

To ensure that investment products remain suitable for the program, the Product Review Committee reviews each investment product on a quarterly basis in accordance with its charter. A document summarizing investment performance for the 4th Quarter of 2023 is attached in **Exhibit K**.

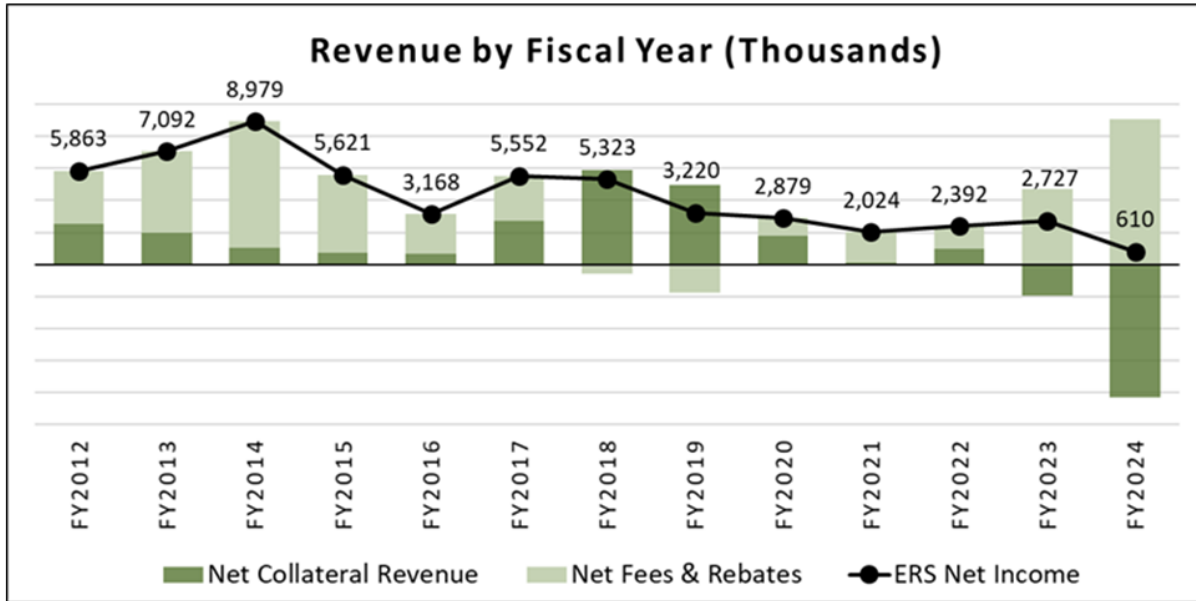
Annual Review of Securities Lending Program

In accordance with the ERS Investment Policy Statement, Section 4.15, and Texas Government Code, Section 815.303, in 2011 the Board of Trustees authorized staff to contract with Deutsche Bank AG (DB) to act as its securities lending agent. Since that time, DB has served ERS as an actively managed third-party lending agent separate from the custodian bank.

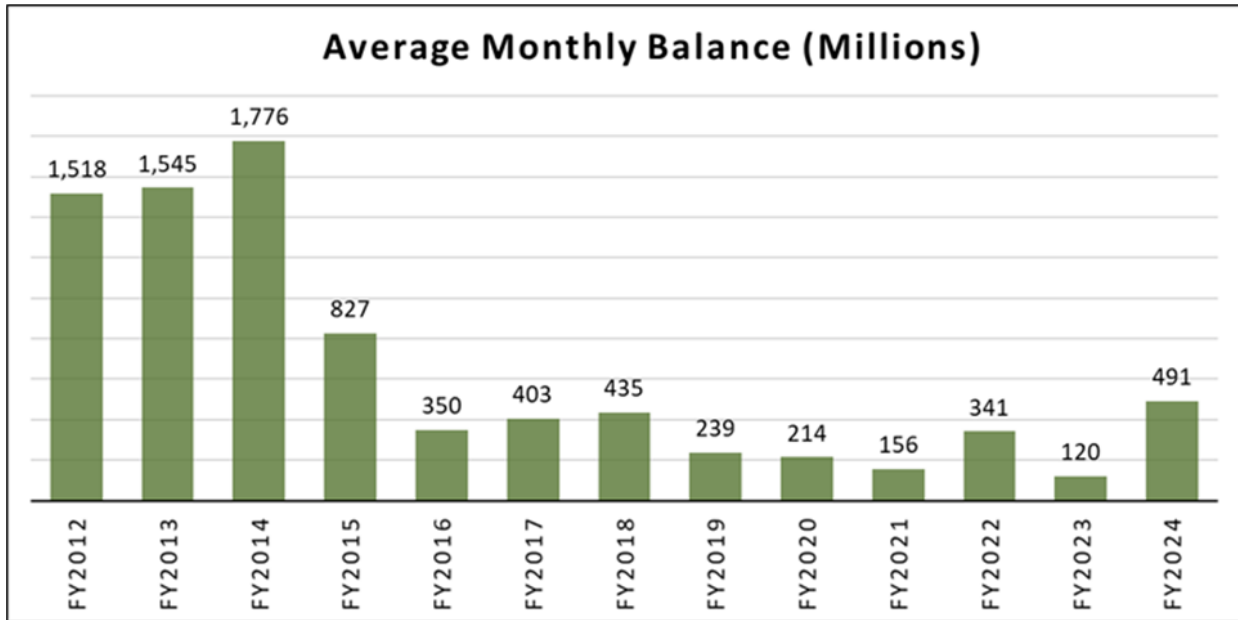
ERS retained DB to implement an intrinsic value program that lends only highly sought-after securities to a diversified group of borrowers and accepts only low risk collateral. Such a narrow approach earns higher average fees than more aggressive programs and produces attractive risk-adjusted returns without requiring additional capital or inhibiting the investment program. The drawback of such a conservative program is that lending volumes are typically small, which means that while the returns are attractive, the dollar amounts generated are relatively small.

OVERVIEW OF FINANCIAL RESULTS

For Fiscal Year 2023, the securities lending program earned \$2.7 million, an increase of approximately \$334,995 compared to the previous fiscal year. Net revenue for Fiscal Year 2024 through November 30, 2023, is \$609,517, approximately in line with the same period the previous fiscal year. Cumulative Trust net revenue from inception through November 30 is \$55.2 million.



The average monthly lending balance for Fiscal Year 2023 declined \$221 million to \$120 million from a \$341 million average for Fiscal Year 2022. The majority of the decline in average balance was caused by actions taken by staff to restrict lending, in response to a rapid increase in the pricing of credit default swaps (CDS) on the program’s lending agent, which signaled market concerns with its credit quality that are described in more detail below.



RISK MANAGEMENT ACTIVITIES

Staff believes that ERS has appropriate risk mitigation features embedded in the securities lending program. The most important risk management features of the program are limiting collateral to fully indemnified assets, right-way risk, and indemnification.

- Collateral restrictions.** The program allows only overnight government repurchase agreements as collateral, and all borrowers must maintain at least 100% of the value of the securities borrowed in margin. ERS also has diversification requirements in place to ensure that the Trust is not over-exposed to any single borrower.

- **Right way risk.** Securities lending programs have historically experienced problems when the value of the invested collateral declines amid market downturns. Such challenges occur because borrowers have the right to return borrowed securities at any time and receive back their posted margin immediately regardless of the market price for the collateral. However, borrowed securities volumes also tend to shrink in financial downturns as borrowers return securities to get their cash back. Borrowers do so for a variety of reasons, including the need to raise cash to satisfy margin calls, to de-lever portfolios, or to meet redemptions. Borrowers may have credit concerns about the collateral pool or prime broker. Such tendency is generally regarded as “right-way risk” since it tends to reduce the size of the lending program as market risk increases.
- **Indemnification.** In addition to these protections, DB has agreed to indemnify ERS for both counterparty and collateral investment losses, which leaves ERS with only counterparty exposure to DB. ERS staff continuously monitors DB’s credit quality through market-based indicators such as Credit Default Swap (CDS) spread. Widening to various levels of implied default probabilities or particularly sudden swings has, in the past, prompted staff to curtail the program when the market indicated the potential for higher risk than the program is willing to bear for such a modest income stream.

DB’s CDS spread began in 2022 at 45 bps and increased steadily through the year, rising above 185 bps on October 11, 2023. That spread implies that the probability of default in the next year is greater than 3%. On that date and in consultation with the Risk Committee, staff instructed DB to increase the program’s minimum acceptable spread to lend an issue from an Overnight Bank Funding Rate (OBFR) of -9 bps to OBFR +500 bps, which effectively suspended the program. DB’s earnings release in the days that followed relieved market concerns, leading staff to reduce the lending hurdle to OBFR +0 bps on October 25. Staff monitors these risk metrics continuously, including via monthly reports to the Risk Committee, and is prepared to revisit the lending threshold if events warrant.



The chart above shows the history of DB’s CDS spread after it effectively restarted in May 2019 because of regulatory and structural changes. Its spreads have stabilized recently around the +90 bps level, which implies less than a ~2% probability of default in the next year.

Staff is currently comfortable with the risk and performance of the program and believes it is operating well despite the lower net revenue than was the case a decade ago.

ATTACHMENTS:

1. Exhibit A – Consideration of the Minutes to the December 5, 2023 Joint Meeting of the Board of Trustees and Investment Advisory Committee
2. Exhibit B – Consideration of the Minutes to the December 6, 2023 Audit Committee Meeting
3. Exhibit C – Consideration of the Minutes to the December 6, 2023 Board of Trustees Meeting
4. Exhibit D – Internal Audit Charter
5. Exhibit E – Audit Committee Charter
6. Exhibit F – GBP Annual Non-Financial Performance Measures
7. Exhibit G – GBP Vendor Contract Monitoring Overview
8. Exhibit H – GBP Optional Benefit Plans Updates and Compliance Overview for Calendar Year 2023
9. Exhibit I – GBP Calendar Year 2023 Enrollment Information
10. Exhibit J – Texa\$aver 401(k) and 457 Plans Enrollment
11. Exhibit K – 4th Quarter Review of Texa\$aver Investment Performance
12. Slides – Consent Agenda