

**South Carolina Public Employee Benefit Authority
Finance, Administration, Audit, and Compliance Committee
Meeting Minutes**

Tuesday, October 16, 2012

2nd Floor Conference Room
202 Arbor Lake Drive
Columbia, South Carolina 29223

Committee Members Present:

Mr. Steve Matthews, Chairman (in person)
Ms. Peggy Boykin (in person)
Mr. Art Bjontegard, Ex-officio (in person)

Others present for all or a portion of the meeting:

David Avant, Robbie Bell, Susan Brownlee, Stephen Van Camp, Justin Werner from the South Carolina Public Employee Benefit Authority (PEBA); Sara Corbett and Andrew Chernick from the South Carolina Retirement Systems Investment Commission; Daniel Brennan and Brian DeRoy from the State Treasurer's Office; Whitney Williams from Fred Allen and Associates; Will Kinney from Mullikin Law Firm; and Thomas Rey from CliftonLarsonAllen, LLP

I. Call to order and Adoption of Proposed Agenda

Chairman Matthews called the meeting to order at 2:00 p.m. Ms. Brownlee confirmed compliance with the Freedom of Information Act. Chairman Matthews noted those in attendance and then requested a motion and vote to adopt proposed agenda. Upon motion by Mr. Bjontegard and second by Ms. Boykin, the agenda was adopted.

II. Organization of FAAC Committee

Chairman Matthews introduced Mrs. Boykin's suggestion that the committee refer to best practices of other state boards for organization and procedures. Mrs. Boykin recommended contacting Texas Teachers Retirement and Wisconsin State Retirement systems to seek advice on organization, bylaws, etc. Mr. Bjontegard and Chairman Matthews concurred with Mrs. Boykin's suggestion.

III. Discussion of Need for PEBA Board Bylaws

Chairman Matthews initiated discussion of proposed bylaws which were drafted by PEBA's legal counsel, and consensus was reached to investigate where and what changes might be needed. PEBA staff and/or Mrs. Boykin were assigned the task of getting contacts and sample documents (mission statements, etc.). Mrs. Boykin asked whether the interim bylaws needed to be officially adopted until adopting a more permanent version. Chairman Matthews noted three important documents: 1) the statute and statutory summary; 2) obligations under fiduciary law; and 3) operational procedures/bylaws which would not be affected by changes in statute. Mr. Bjontegard mentioned he sent an email with suggested changes to the draft (staff left the meeting

room to retrieve a copy). There was brief discussion about making the Vice Chair position Chair-Elect, but this was abandoned, given that all terms will expire at the same time. Mr. Bjontegard asked that, if a board member is sued, would personally-incurred expenses be reimbursed from PEBA. Mr. Van Camp agreed to research the matter.

IV. Committee Procedures on Audit, Budget, and Financial Statements

Mr. Van Camp introduced Mr. Thomas Rey, of CliftonLarsonAllen, LLP. Upon question from Chairman Matthews, Mr. Rey confirmed the State Auditor's Office commissioned his services. Mr. Rey distinguished a fiduciary audit from a financial audit. He also confirmed for the committee that Generally Accepted Government Audit Standards (GAGAS) is the standard used for governmental audits. Chairman Matthews then asked several questions related to the procedures for developing and approving an operational budget. Mr. Van Camp, Ms. Nichols and Ms. Rumpfelt explained this process, noting the difference between the operational budget and the financial statements and that each financial statement component (insurance and retirement) has its own auditor. Mr. Rey explained that, if there would be a consolidated statement, the auditors would have to work together or one auditor would have to learn the other's work. Chairman Matthews asked whether there is a single preferred way. Mr. Rey explained, yes, most of the time, there is a single auditor for both sides. Mr. Bjontegard asked whether it is typical to use different auditors. Mr. Rey repeated that there is usually a single auditor. Upon question by Chairman Matthews, Mr. Rey confirmed an audit is not complete without its letter of representation. There was a brief discussion about issuing a letter of representation for investments without the authority/control over them. Mr. Rey confirmed that, without the controls, South Carolina's alternative investments were audited separately; they are higher risk. Mr. Rey explained that 90% of the alternative investment dollars and close to 100% of those managers were tested, which is a good baseline. Mr. Rey explained that most of South Carolina's alternative investments are audited annually by large, reputable firms, and the annual evaluations are their opinion as to the reasonableness of the managers' valuations. Mr. Rey explained more details of the valuation process, noting they are recorded at net asset value. Mr. Bjontegard asked how to ensure against performance bias from private managers to increase their fees, and Mr. Rey responded that they tend to be conservative. Mr. Bjontegard also expressed concern with private equity fund managers reporting their own performance numbers. Ms. Nichols presented Mr. Bjontegard with a list of all managers, who audited them and their opinions. Mr. Rey explained the process of testing private owned companies and that the Investment Commissions should be working with managers when anomalies occur. Upon question by Chairman Matthews, Mr. Rey confirmed it is PEBA's responsibility, not the Investment Commission's, to sign the representation letter and to be comfortable with what the Investment Commission is doing, which is still in development. Mr. Rey further explained that assessment of internal controls is a way to gauge how much testing is needed. Mr. Rey confirmed that, going forward, he can provide a management letter to the PEBA Board as to any deficiencies and/or best practices. Chairman Matthews asked where the PEBA Board can go for guidance to ensure PEBA staff knows and understands what is happening at the Investment Commission. Mr. Rey briefly explained how managers take their fees. Mr. Rey explained that most boards he works with have an investment committee with investment knowledge and/or training. He further explained the Investment Commission needs in-house expertise with the different types of assets, and the PEBA Board should have a basic understanding and be involved, in some way,

when hiring managers, and comfortable with initial and ongoing due diligence reports from the Investment Commission. David Avant noted that the Executive Director of PEBA now serves as a liaison on the Investment Commission, as an ex-officio member. There being no further questions, Chairman Matthews thanked Mr. Rey for his time and expertise.

Staff distributed a copy of Mr. Bjontegard's email regarding the draft. Mr. Bjontegard reviewed his suggestions for inclusions to the bylaws and operations. Meeting attendance was discussed briefly. Chairman Matthews asked whether the Board is statutorily permitted to sub-delegate duties, and Mr. Van Camp said he would investigate. Ms. Boykin suggested specifying responsibilities of a vice-chair. There was brief discussion about the Board's role and process with respect to the Agency Head Salary Commission.

Chairman Matthews recommended preparing a statement of procedures for the FAAC committee and any potential audit committee. Mrs. Sarah Corbett from the Investment Commission introduced herself and confirmed that they engaged Deloit and Touche to advise on due diligence issues. The commission recently adopted due diligence procedures and a checklist, which she will share with PEBA staff. She introduced Alan Chernick, Director of Audit and Compliance. Mrs. Corbett explained the Investment Commission will continue to revise and implement due diligence procedures and checklists in the coming months. Mrs. Corbett explained that she would be happy to take the suggestion back to Investment Commission management, that they sign the letters of representation going forward.

V. Review of Draft PEBA Operational Budget

Mr. Van Camp introduced Mrs. Karen Rumpfelt. She reviewed the budget and explained it is a composite of the two operating expenses for Insurance and Retirement. Upon question by Chairman Matthews, Mrs. Rumpfelt confirmed about 11 classified, administrative staff positions. Chairman Matthews asked, and Ms. Rumpfelt confirmed the IT positions were not part of administration, but under Other Operating expenses. There are about 88 authorized classified positions, with 2 unclassified. Chairman Matthews asked about "other operating expenses." Mrs. Rumpfelt explained that this includes IT personnel and equipment, consultants, actuaries, etc. Upon question by Mr. Bjontegard, Ms. Rumpfelt explained the Adoption Assistance Program. There were additional questions on the classified positions, and Ms. Rumpfelt agreed to provide the committee with additional details. Mr. Bjontegard asked the authorization trend for the operational budget, and Ms. Rumpfelt and Mr. Van Camp explained that has been flat and that it went down at some point for the Insurance side and that it comes out of the trust funds; it is not appropriated. Mrs. Nichols explained operating funds are transferred quarterly. Upon motion by Mr. Bjontegard and seconded by Ms. Boykin, the committee approved unanimously to refer the draft operating budget to the PEBA Board with recommendation for approval.

VI. Executive Session to Receive Legal Advice

Chairman Matthews asked whether it was necessary to hold executive session, given the earlier discussion in the main board meeting, and it was generally agreed executive session was not necessary. Chairman Matthews requested a motion to amend the

agenda to remove this item. The motion was made by Ms. Boykin, seconded by Mr. Bjontegard and carried unanimously.

VII. Adjournment

Chairman Matthews asked if there were any further items to discuss.

There being none, a motion was made, seconded and moved unanimously to adjourn at 3:35 p.m.