

**South Carolina Retirement System Investment Commission
Audit Committee Meeting Minutes**

September 18, 2012

**15th Floor Conference Room
1201 Main Street
Columbia, SC 29201**

Committee Members Present:

Mr. Allen Gillespie
Mr. Reynolds Williams

Others present for all or a portion of the meeting on Tuesday, September 18, 2012: Andrew Chernick, Sarah Corbett, Robert Feinstein, Hershel Harper, Monica Houston, Adam Jordan, James Manning and Nancy Shealy from the South Carolina Retirement System Investment Commission (“RSIC”); Michael Chung from Deloitte and Touche (“Deloitte”); Bill Leidinger from the State Treasurer’s Office; Tammy Nichols from the South Carolina Retirement System; Wayne Pruitt from the State Retirees Association.

I. Call to Order – Mr. Allen Gillespie, Chairperson called the meeting of the RSIC Audit Committee (“Committee”) to order at 9:07 a.m. A quorum was present.

II. Approval of Minutes – Mr. Gillespie introduced Mr. Andrew Chernick, Audit and Compliance Director and Ms. Monica Houston, Audit and Compliance Officer to the Committee. Mr. Reynolds Williams made a motion to approve the minutes from the April 11, 2012, Committee meeting, which was seconded by Mr. Gillespie and approved unanimously.

III. Overview of Internal Audits – Mr. Michael Chung from Deloitte explained the internal audit process. He added that all of the recommendations from Deloitte are attainable by RSIC and many initiatives are already underway. He noted that an overall theme throughout the report is the need for technology and resources. Mr. Chung went on to give an overview of the sections of the report: due diligence framework, valuation, and cross-trades.

Regarding due diligence framework, Mr. Chung said the report focuses on the technology and reporting that will help facilitate the investment process. Regarding valuation, Mr. Chung noted that there are certain procedures that RSIC can undertake particularly during the due diligence process in order to gain more comfort over the valuation of the investments. Finally, regarding cross-trades, Mr. Chung explained that cross-trading was viewed relative to the impact such transactions have on the valuation and hence the effect on financial reporting.

In response to Mr. Chung’s comments relative to valuation, Mr. Gillespie made inquiry regarding RSIC’s rights on Strategic Partnership investment committees; he asked whether RSIC retained input and control over the audit and valuation function. Mr. Hershel Harper, Chief Investment Officer responded that the answer could be different for each Strategic Partnership depending upon when they were executed but that typically what has been built in is the ability to hire a third party valuation consultant. He further noted that almost all of the Strategic Partnerships have a valuation committee to oversee the valuation process. Ms. Sarah Corbett, Deputy Chief of Staff noted that there are several components of a manager’s valuation process that RSIC should be a part of, adding that if there are any changes or exceptions to valuation policies, RSIC needs to investigate those instances and understand the reasoning. Mr. Chung and Ms. Corbett noted, discussed, and placed emphasis on the value of developing documentation standards and

utilizing a risk based approach in reviewing the investment valuations to improve operational efficiency.

Referring to the Audit Report sent to the Committee in advance of the meeting, Mr. Chung continued to review the recommendations made by Deloitte. Mr. Chung reiterated that RSIC's technology infrastructure should be developed in order to create the efficiencies necessary to perform all of Deloitte's recommendations.

Mr. Gillespie asked Mr. Chung if the report's recommendations are too restrictive regarding the necessity of historical performance and therefore do not allow for RSIC to invest in new managers. Mr. Chung explained that while Deloitte's recommendations are just an example, he does believe the guidelines could be adaptable to allow for an investment in a new manager. Mr. Harper added that while there should be a set of rigid due diligence guidelines, Staff should understand that there will be changes and additional standards for new managers. Ms. Corbett added that a new manager would fit into the due diligence guidelines, but would then affect the risk-based framework accordingly (i.e., a new manager would have a higher risk rating than a manager with a long historical track record).

Ms. Corbett noted that Mr. Harper has approved the Initial Due Diligence Guidelines.

Mr. Williams asked what the Committee needs to present to the Commission at the next meeting on September 20, 2012. Ms. Houston explained that the Internal Audit staff wanted to know what the Committee desired to bring to the full Commission, but added that the key aspects should be to explain that an Internal Audit Report has been done, and what management's next steps are going to be.

Ms. Nancy Shealy suggested the Committee should summarize the report and any further actions, and simply provide the full report to the Commissioners for their own information. Mr. Williams agreed.

Mr. Gillespie inquired specifically about the audit coverage of the cross trades. Mr. Chung indicated that the review performed looked at the process, not the detail, of the transactions and indicated that such falls under the umbrella of the due diligence process as it relates to valuation of the transaction. Mr. Harper elaborated on his knowledge of one specific cross trade noting that the process in that instance was to use an independent third party for valuation.

Mr. Harper briefly commented on management's response and action plan to the recommendations. Emphasis was placed on the organization's need for additional human capital and technology resources to adequately mitigate the risks identified. He discussed RSIC's current efforts in the area of technology, as well as prior accomplishments of the staff that addressed the areas of concern.

IV. Review of Risk Assessment Dashboard – Mr. Chernick provided a brief background on the Dashboard and its purpose. He discussed the progress to date of the items/tasks listed on the Dashboard. Ms. Corbett added color to developing operational infrastructure noting that this was one of the most critical items to focus on as it laid the foundation for all that the organization does. She provided details on the current efforts to build out the operational infrastructure through implementation of a contact management system, a private markets system, and a data hub. It was noted by Mr. Adam Jordan, Acting Chief Executive Officer that these systems were all that the organization could implement under the current budget. Mr. Williams made note that the Risk Assessment Dashboard provides a good summary that one can quickly comprehend and he requested it be enhanced to easily identify items/tasks that have been completed.

A brief discussion regarding Commissioner' responsibilities and governance of Strategic Partnerships followed. Mr. Gillespie made the initial inquiry with Mr. Jordan providing input as to where Commissioners may find some of the requested information on the secure portal. Mr. Harper also responded by briefly providing historical background and perspective on the strategic partnership arrangements as well as management's current efforts and thought process.

V. Audit Committee Composition – A brief discussion was held related to the recent change in the number of people on the Committee from three to two. Mr. Gillespie elaborated on concerns he had and his desire to change the composition back to three. Mr. Williams responded and indicated that such a decision was necessitated by the Commission's current Governance Policies. It was noted that a proposed revision of the Governance Policies was on the upcoming Commission Meeting Agenda. The item was deferred pending outcome of the proposal at the coming September 20th Commission meeting and voting on such at the November Commission meeting.

V. Executive Session to Review Investment Matters pursuant to SC Code §9-16-80 and §9-16-320 – Mr. Williams made a motion to enter executive session to discuss matters related to Strategic Partnership Investments as a result of the Deloitte audit, which was seconded by Mr. Gillespie. Mr. Chung, Mr. Chernick, Ms. Houston, and subsequently Ms. Corbett were asked to attend the executive session. The Committee recessed into executive session for purpose of discussing investment matters that could affect the Portfolio. Upon returning from Executive Session, Mr. Williams noted that no action was taken.

V. Adjournment – There being no further business, on motion duly made and seconded, the meeting was adjourned at 11:37 a.m.

[Staff Note: In compliance with S.C. Code Ann. §30-4-80, public notice of and the agenda for this meeting were delivered to the press and to parties who requested notice and were posted at the entrance, in the lobbies, and near the 15th Floor Conference Room at 1201 Main Street, Columbia, SC, on September 14, 2012.]