

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

October 22, 2015

**Capitol Center
1201 Main Street, 15th Floor
Columbia, South Carolina 29201
Meeting Location: Presentation Center**

Commissioners Present:

Mr. Edward Giobbe, Chairman
Dr. Rebecca Gunnlaugsson, Vice Chair
Mr. Curtis Loftis, State Treasurer
Ms. Peggy Boykin, PEBA Executive Director
Mr. Allen Gillespie
Dr. Ronald Wilder
Mr. Reynolds Williams

Others present for all or a portion of the meeting on October 22, 2015:

Geoff Berg, J.P. Boyd, Corleon Brown, Betsy Burn, Andrew Chernick, Dori Ditty, John Farmer, Robert Feinstein, Mitchell Goldsmith, Michael Hitchcock, James Manning, Tricia Miller, Bryan Moore, Brittany Storey, Brian Wheeler from the South Carolina Retirement System Investment Commission; Clarissa Adams and Bert Cassell from the State Treasurer's Office; Suzanne Bernard and Tim McEnery from Aon Hewitt; Wayne Pruitt from the State Retirees Association of South Carolina, Karen Hermann, Jarad Nobles, Steve Yountz, Jay Collins and Tom Posey from ETV, and Andrea Taylor from Creel Court Reporting.

I. CALL TO ORDER AND CONSENT AGENDA

Chairman Edward Giobbe called the meeting of the South Carolina Retirement System Investment Commission ("Commission" or "RSIC") to order at 9:30 a.m. Chairman Giobbe referred to the proposed meeting agenda and asked for a motion to adopt the agenda. Dr. Ronald Wilder made a motion to adopt the agenda as presented, and Mr. Reynolds Williams seconded the motion, which was unanimously approved.

II. CHAIRMAN'S REPORT

Chairman Giobbe opened by recognizing Mr. Michael Hitchcock, Executive Director, to review proposed changes to the Commission governance policies. Mr. Hitchcock reviewed the proposed changes to Commission governance policies I and III, stating that the proposed changes clarify the relationship between the

Executive Director (ED) and the Chief Investment Officer (CIO), specifically in the event of a vacancy in the CIO position. The proposal includes a delegation by the Commission to the ED to conduct a search for a CIO and then recommend a candidate or candidates to the Commission for its consideration and approval. Discussion of the proposal ensued, including questions by Mr. Curtis Loftis regarding the extent of the delegation to the ED and how the search would be conducted, and questions from Mr. Williams as to whether one or multiple candidates would be presented to the Commission for consideration and approval. Mr. Hitchcock stated that he planned to present a CIO search plan to the Commission for approval and that he envisioned a collaborative process and offered to include clarifying language to that effect in the policies to reflect the discussion amongst the Commissioners. Mr. Hitchcock said that he would circulate new language to the Commissioners for review.

III. EXECUTIVE DIRECTOR'S REPORT

The Chairman asked Mr. Hitchcock to review the budget proposal. Mr. Hitchcock reviewed the proposal to be submitted to the Governor's office. After discussion Mr. Hitchcock briefly reviewed the management of FTEs over the previous year that led to the current proposal.

Dr. Wilder asked for information on the search for a new CIO. Mr. Hitchcock replied that both a job description and a RFP for a national search firm had been developed and that the latter had been submitted to the state procurement office.

Mr. Williams moved that the Commission authorize the ED to submit a proposed Fiscal Year 2017 detail budget substantially similar to the draft budget presented for inclusion in the Governor's annual budget. Dr. Wilder seconded and the motion passed four to one, with Mr. Loftis voting no.

IV. HUMAN RESOURCES AND COMPENSATION COMMITTEE REPORT

Dr. Rebecca Gunnlaugsson reported that the committee met on October 14, 2015 to consider a compensation policy designed by Towers Watson in collaboration with RSIC Staff. She noted that at the meeting there was a lot of concern raised over the ability to pay PIC on a regular basis with any stability. She said that the committee asked the staff to return with a proposal for an all-base compensation plan. The committee reconvened on October 16, 2015, and an all-base plan was presented and agreed upon by the Committee to present to the full Commission for discussion purposes. She asked Mr. Hitchcock to review both proposals.

Mr. Hitchcock reviewed the process of engaging the consultant and the process of gathering and analyzing the data for the study. He noted that two peer groups were created for analysis. Mr. Loftis asked for more information about the peer groups and Mr. Hitchcock said that he would provide it. Ms. Peggy Boykin asked to see

the comprehensive McLagan study and that which shows all the public pension funds. She said that RSIC should benchmark its compensation against its peer group and thus was concerned about the peer group used in the study. There was a lengthy discussion on what type of peer group should be used and how it would relate to the overall benchmark.

Mr. Hitchcock said that the current compensation plan really is not workable despite it being benchmarked against the top decile of public plans which includes the big public firms. He said that the thought with the new proposal was to target the 75th percentile, and that would be for someone working at their optimal performance level. He said that they were open to other benchmarking methodologies but that his primary concern was the recruitment and retention of good talent. Mr. Hitchcock said that another concern for him was to have a compensation plan that the agency can actually implement consistently. Mr. Loftis discussed his experience in being on the compensation committee, going into detail about incentive components. Additional discussion ensued regarding the advantages and disadvantages of incentive compensation components and various benchmarking issues.

After additional discussion, Mr. Hitchcock said that his main goal was to have a compensation plan that could be delivered upon and that whether the plan included incentives or was an all-base plan that they would have an absolute performance component so that no one would benefit when the plan performed poorly. He added that by moving to an all-base plan the agency could focus much more on individual performance by members of the team while creating a team atmosphere focused much more on the strategic asset allocation, rather than tacitly trying to beat the benchmarks.

The Chairman said that his understanding was that compensation under the new proposals would be much more tied to the overall performance of the fund. Mr. Hitchcock confirmed and moved into an explanation of the proposed plans, beginning with the incentive compensation proposal. Mr. Loftis asked if the contributions and deductions were included in the 7.5% benchmark for 100% incentive compensation in the first new proposal. Mr. Hitchcock said that they were. Mr. Loftis asked if the proposal included the net outflow that was predetermined by statute, which has nothing to do with investment. Mr. Hitchcock said that the net outflow of benefit payments would have to be covered prior to the payment of any incentive compensation and that full incentive opportunity would be available at 7.5%. He continued to review the components of the incentive compensation proposal.

Dr. Wilder noted that the maximum ratios in the proposal were much lower than in the current policy. Mr. Hitchcock concluded his presentation of the incentive proposal. Dr. Gunnlaugsson said that because this incentive proposal was scaled back from the existing incentive plan that base pay would be raised as part of the

proposal. Mr. Hitchcock explained that aspect in more detail. Ms. Boykin said that she would like to see an example of that component in order to provide an accurate explanation to plan members. Mr. Hitchcock said that overall compensation for the investment team would decrease and decrease substantially compared to what it is now, especially in low performance years, but that he also must bear in mind the compensation parameters under which current employees were hired. He said that he was trying to balance the competing priorities. Mr. Hitchcock added that any increase in base compensation would occur over time and would be tied to performance.

Mr. Geoff Berg, Acting Chief Investment Officer, noted that eight recent departees left for a corporate environment and that made appropriate the inclusion of some corporate entities in the peer group.

Mr. Hitchcock said that regardless of whether the Commission chooses to adopt an all-base plan or the plan with incentive compensation, he intends to set a tone within the agency of high individual performance expectations through a robust employee management system, thus eliminating the ability of anyone to sit comfortably in their position.. Mr. Loftis asked if the choices were either the proposal with incentive compensation or the all-base plan. Mr. Hitchcock said that those were presented to the HRC Committee upon the committee's desire to move to an all-base plan. He said that his intention was to present both proposals to the Commission.

Dr. Wilder asked to hear the other point held by Mr. Berg. Mr. Berg explained the inherent difficulties with an incentive plan and his belief that such was not needed to motivate employees. He questioned the ability to accurately anticipate the difficulties of either paying the incentive in a suboptimal environment or breaking the covenant made to employees. He said that he preferred, for these reasons, to leave the incentive plan.

Discussion continued regarding the proposals and the merits of each. Mr. Berg noted that in the continuum of investor to allocator that RSIC is both. He said that pay is a motivating factor but career development also was a factor, and that is part of the plan laid out by Mr. Hitchcock. He said that the Commission should think philosophically about the right things to do that create the right environment, for a more fulsome compensation structure.

The Chairman declared a break from 11:12 a.m. to 11:22 a.m.

Mr. Hitchcock said that he planned next to discuss the proposal for the all-base pay plan and potentially specifics regarding impact on individual Staff members. Mr. Williams moved to go into executive session to discuss personnel matters pursuant to S.C. Code §§ 30-4-70(a)(1) and receive advice from legal counsel pursuant to S.C. Code § 30-4-70(a)(2), and to discuss investment matters pursuant

to S.C. Code §§ 9-16-80 and 9-16-320. Dr. Wilder seconded. The vote was unanimous.

Executive Session from 11:24 a.m. until 12:51 p.m.

The Commission reconvened in open session at 12:51 pm. It was noted that no action had been taken in executive session.

VII. ADJOURNMENT

There being no further business, the meeting adjourned at 12:51 p.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 Presentation Center at 1201 Main Street, Columbia, SC, at 5:02 p.m. on Wednesday, October 21, 2015.]