

South Carolina Retirement System Investment Commission Meeting Minutes

Thursday, November 3, 2005

**Second Floor Conference Room
202 Arbor Lake Drive
Columbia, South Carolina 29223**

Commissioners Present:

Mr. James Powers, Vice Chairman
Treasurer Grady Patterson
Mr. Blaine Ewing
Mr. Allen Gillespie

Others present for all or a portion of the meeting: Nancy Shealy and Ashli Aslin from the South Carolina Retirement System Investment Commission; Anne Macon Flynn from the Budget and Control Board Office of General Counsel; Sam Wilkins and Joye Lang from the Budget and Control Board Office of Human Resources; Rick Patsy, Frank Rainwater, and Shakun Tahiliani from the State Treasurer's Office; Jay Love from Mercer Investment Consulting; Robert Dezube from Milliman Consultants and Actuaries; Keith Wood from Jamison, Eaton & Wood, Inc.; Peggy Boykin, Dianne Poston, Faith Wright, Tammy Davis, Travis Turner, Sarah Corbett, and Joni Redwine from the South Carolina Retirement Systems; Sue Sommer-Kresse from the College of Charleston; Broadus Jamerson from the South Carolina State Employees Association; Thomas Stanton from Stanton Consulting Group, Inc.; Travis Pritchett, Sam Griswold, Kent Phillips, and Wayne Pruitt from the State Retirees Association; Charley McDonald from the South Carolina Trooper's Association; and Horace Jackson, a state retiree.

I. CALL TO ORDER AND CONSENT AGENDA

Vice Chairman James Powers called the meeting of the South Carolina Retirement System Investment Commission (Commission) to order at 10:05 a.m. Chairman Reynolds Williams was unable to attend due to an unexpected scheduling conflict.

Vice Chairman Powers requested that the Commission consider adding an item to the proposed agenda relating to the implementation of the Interim Annual Investment Plan (AIP). Treasurer Grady Patterson expressed his reluctance to add items to the agenda after it had been posted. Vice Chairman Powers asked Ms. Nancy Shealy to briefly explain the issue. Ms. Shealy explained that the State Budget and Control Board (Board) adopted an Annual Investment Plan for Fiscal Year 2005-2006 and authorized its implementation. The Commission subsequently adopted the AIP, but explicit authority to implement the AIP was not addressed. She said on November 2, 2005, she received confirmation that implementation would occur on December 1, 2005, but it was too late to amend the proposed agenda prior to this meeting. Since the Commission was not scheduled to meet again until December 8, 2005, she recommended that the Commission consider the issue at this meeting to insure that the AIP would be

implemented in a timely manner. After thorough discussion, Mr. Blaine Ewing made a motion to adopt the proposed agenda as amended. The motion was seconded by Mr. Allen Gillespie and passed.

Vice Chairman Powers called for objections or amendments to the minutes from the Commission meeting on October 13, 2005. Mr. Ewing made a motion that the minutes be adopted as presented. Mr. Gillespie seconded the motion, which passed unanimously.

II. NOMINATIONS AND DISCUSSIONS OF RETIREE REPRESENTATIVE TO THE COMMISSION

Vice Chairman Powers recognized the candidates for the retiree representative to the Commission, Dr. Travis Pritchett and Dr. Thomas Stanton. Ms. Shealy discussed the required qualifications for the position as outlined by the State Retirement System Preservation and Investment Reform Act (Act 153) and verified that both Dr. Pritchett and Dr. Stanton were retired members of the South Carolina Retirement Systems (Retirement Systems). Ms. Shealy stated that both candidates appeared to be amply qualified to serve on the Commission. Ms. Shealy noted that, with the exception of the State Treasurer, no person may be appointed or continue to serve on the Commission if they are an elected or appointed officer or employee of the State or of any of its political subdivisions, including school districts. Ms. Shealy asked if either candidate currently served in such capacity, to which each replied that they did not.

At Vice Chairman Powers' request, Dr. Pritchett introduced himself to the Commission and discussed his education, career, credentials, and community involvement. Dr. Pritchett expressed his interest in acting as the retiree representative to the Commission, and stated that his academic and work experience gave him the knowledge necessary to contribute to the Commission's discussions. Dr. Pritchett stated that he was an active Member of the State Retirees Association Board, and, in that capacity, he represented members on issues related to health insurance and retirement benefits. Ms. Shealy noted that the primary focus of Dr. Pritchett's career had been in the area of insurance and asked him to discuss the correlation between his professional experience and investments and risk management as related to the responsibilities of the Commission. Dr. Pritchett confirmed that his main interest had been insurance, which included the study of retirement plans in conjunction with the employee benefit courses he taught at the University of South Carolina. Dr. Pritchett explained that he had studied and taught investment analysis, money and capital markets, and economics. Vice Chairman Powers thanked Dr. Pritchett on behalf of the Commission.

Dr. Stanton introduced himself to the Commission and provided an overview of his education, career, and qualifications. Dr. Stanton stated that he was skillful in matters involving the application of mathematics and investments and would enjoy the intellectual stimulation in working with the Commission. He stated that, if chosen, he would faithfully represent the interests of the state's retirees. Mr. Ewing asked Dr. Stanton whether the time commitment required of Commission members would be a burden to his work schedule. Dr. Stanton said meeting once a month should not present

a problem, but his availability to meet more frequently would depend on his work obligations. Vice Chairman Powers thanked Dr. Stanton on behalf of the Commission.

(Information relating to this matter has been retained in the Commission's files and is identified as Exhibit A.)

III. ADMINISTRATIVE MATTERS

Vice Chairman Powers recognized Mr. Sam Wilkins and Ms. Joye Lang from the South Carolina Budget and Control Board Office of Human Resources (OHR) for an update on the Chief Investment Officer (CIO) recruitment process. Mr. Wilkins provided the Commission with an updated timeline for the process and an overview of the costs of advertisements in various publications. Mr. Wilkins stated that a summary of the applicants should be available for the Commission's review prior to the January 2006 meeting. At that time the Commission may review the applications and determine how to proceed with the interview process. At Mr. Gillespie's suggestion, Mr. Wilkins agreed to work with Mr. Rick Patsy from the State Treasurer's Office (STO) to determine the feasibility of posting the position on the Bloomberg service. Ms. Lang agreed to explore posting the position on websites of local Chartered Financial Analyst Institute (CFA) chapters. Vice Chairman Powers thanked Mr. Wilkins and Ms. Lang for their assistance in the CIO recruitment process.

IV. OTHER BUSINESS

Vice Chairman Powers recognized Mr. Love of Mercer Investment Consulting, Inc. (Mercer), and Mr. Robert Dezube from Milliman Consultants and Actuaries (Milliman) for an update on the Asset Liability Modeling study (ALM). Mr. Love invited Mr. David Fraum from Mercer's Asset Liability Modeling group in Atlanta to participate in the discussion via telephone conference call. Mr. Love stated that the goal of the ALM would be to determine the most effective allocation for a plan's asset in the context of the liabilities. Messrs. Love, Fraum, and Dezube provided an overview of the considerations that would need to be addressed in the process of performing an ALM, including the ad hoc cost-of-living adjustment (COLA), the amortization period, and the contribution rate.

Mr. Love stated that the discount rate for the liabilities would be a critical factor to consider when conducting an ALM. Mr. Fraum stated that the Commission must consider whether or not there would be an expectation to move to a higher discount rate if the equity allocation increased. Mr. Gillespie asked whether the analysis could be completed using several different discount rates. Mr. Dezube stated that the model was quite complex and such an analysis would not be cost effective or timely.

Mr. Dezube stated that Milliman was in the process of completing the valuation for July 1, 2005, and recommended that the ALM be postponed until current figures are available. When asked about the cost involved in the ALM, Mr. Love stated that they would be able to provide a cost analysis at the next meeting. Vice Chairman Powers thanked Messrs. Love, Fraum, and Dezube on behalf of the Commission.

(Information relating to this matter has been retained in the Commission's files and is identified as Exhibit B.)

Vice Chairman Powers stated that the Commissioners received a copy of the agency's Fiscal Year 2007 budget as approved and submitted to the State Budget Office. Treasurer Patterson explained the budget process, and Ms. Peggy Boykin from the Retirement Systems stated that the Commission should expect to go before the House Ways and Means Committee for a budget hearing early in 2006.

Vice Chairman Powers asked Ms. Shealy and Mr. Love to provide information relating to the implementation of the AIP. Ms. Shealy explained that the Board previously adopted the AIP, including provisions to increase the equity target allocation to 50 percent of the total portfolio over the course of Fiscal Year 2006 in 2.5 percent quarterly increments. The Board also authorized implementation of the AIP in the most cost effective and efficient manner and authorized the Director of the Retirement Systems to execute contracts with transition manager(s) as recommended by Mercer and approved for legal sufficiency by the Board's Office of General Counsel. The Commission subsequently adopted the AIP, but did not address authorization for implementation. Ms. Shealy stated that the quarterly transition of assets provided in the AIP was anticipated on December 1, 2005, and she recommended that the Commission explicitly authorize the necessary steps to be taken to implement the AIP in a timely manner.

The Commission discussed the implementation process. Mr. Love explained that while the analysis for this transition had not been completed, transition managers often offer lower commissions because they could consider the entire transition and minimize costs by cross trading. Mr. Love and Ms. Shealy explained the process that the Board used for engaging transition managers, which had been adopted by the Board upon recommendation of the State Retirement Systems Investment Panel (Panel). Ms. Shealy noted that transition managers were required to assume fiduciary responsibility of the transition account during the process. She added that the Retirement Systems had used several transition managers based on an RFP Mercer issued in 2004 and that the managers were screened for quality of service and execution, their willingness to accept fiduciary responsibility, and contractual issues. Mr. Ewing asked if there were checks and balances, and Ms. Shealy replied that Mercer always analyzed the portfolio for transitions and had fiduciary responsibility in making recommendations. She added that Mercer, staff, and the STO, as custodian, monitor the transitions during the process.

In response to questions by the Commission, Mr. Love reviewed preliminary information about the transition. He noted that the allocation to Nicholas-Applegate Capital Management (NACM) would result in the Retirement Systems' account comprising approximately 29 percent of the total assets in the NACM Systematic Small Cap Growth strategy. Mr. Love stated, however, that since NACM had multiple strategies and significant assets under managers, Mercer was not concerned and recommended that the transition be implemented pursuant to the AIP.

After further discussion, Ms. Shealy recommended that the Commission consider authorizing implementation of the AIP as previously recommended by the Panel and authorized by the Board. Mr. Ewing made a motion to authorize the transition of assets to implement the Interim AIP in the most cost effective and efficient manner as recommended by Mercer and to authorize the Chairman of the Commission or his designee to execute a contract and any necessary documents with a manager(s) as recommended by Mercer, and upon approval for legal sufficiency by General Counsel, to transition the assets to implement the AIP. Mr. Gillespie seconded the motion, which passed unanimously.

Vice Chairman Powers advised that staff was in the process of planning a retreat for the Commission and the Panel in Wampee for the beginning of 2006. Ms. Shealy stated that Barton Waring from Barclays Global Investors (BGI) and representatives from Milliman would be invited to give presentations. She asked that Commissioners let staff know of any additional topics for discussion. Vice Chairman Powers noted that the next Commission meetings would be held on December 8, 2005, and January 19, 2005.

Ms. Shealy stated that the Commissioners received additional documents in their meeting packets as information, including a copy of the Comptroller General's travel reimbursement regulations, a document from the Retirement Systems outlining the chronology of events affecting the unfunded actuarial accrued liability, the Retirement Systems' Accountability Report for Fiscal Year 2005, and a copy of the Retirement Systems' financial statements as prepared by an independent auditor. Ms. Shealy noted that the Commissioners could expect the Comprehensive Annual Financial Report (CAFR) for Fiscal Year 2005 to be available in December.

Ms. Shealy stated that she had been working with a group from the National Association of Public Pension Attorneys (NAPPA) dealing with fiduciary liability insurance and insurance requirements for managers and consultants. Ms. Shealy noted also that she was working on proposed policies for the Commission including personnel policies, responding to FOIA requests, and other internal administrative guidelines, and she would forward those to the Commission when completed.

V. ADJOURNMENT

There being no further business, Vice Chairman Powers thanked everyone for attending the meeting. Upon motion by Mr. Ewing, which was seconded by Mr. Gillespie, the meeting adjourned at 12:00 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 2nd Floor Conference Room at 202 Arbor Lake Drive, Columbia, SC, on November 1, 2005.]