

NEW MEXICO
PUBLIC EMPLOYEES RETIREMENT ASSOCIATION
AUDIT & BUDGET
COMMITTEE MEETING

November 10, 2015

This meeting of the Public Employees Retirement Board Audit & Budget Committee was called to order by Chair Stewart Logan at approximately 9:00 a.m. on the above-cited date in the PERA Building, Fabian Chavez, Jr. Board Room, 33 Plaza La Prensa, Santa Fe, New Mexico.

Following the Pledge of Allegiance, roll was called by Executive Director Wayne Propst and a quorum was established with the following members present:

Members Present:

Stewart Logan, Chair
Jackie Kohlasch, Vice Chair
John Reynolds

Member(s) Excused:

Tim Eichenberg

Other Member(s) Present:

Patty French
Dan Esquibel
Loretta Naranjo Lopez
Louis Martinez
Paula Fisher

Staff Members Present:

Wayne Propst, Executive Director
Susan Pittard, Chief of Staff-General Counsel
Jonathan Grabel, Chief Investment Officer
Greg Trujillo, Deputy Director
Renada Peery-Galon, ASD Director
Natalie Cordova, Chief Financial Officer
Judy Olson, Executive Assistant
Karen Risku, Deputy General Counsel
Jude Perez, Deputy CIO
Joaquin Lujan, Portfolio Manager
Kristen Varela, Portfolio Manager

Others Present:

Steve Cogan, REDW

Matt Doxtator, REDW

2. APPROVAL OF AGENDA

Mr. Reynolds moved to approve the agenda as presented. His motion was seconded by Ms. Kohlasch and passed by unanimous [3-0] voice vote.

3. APPROVAL OF CONSENT AGENDA

Chair Logan said he reviewed the minutes and found them accurate and complete.

Mr. Reynolds moved to approve the consent agenda. His motion was seconded by Ms. Kohlasch and passed by unanimous [3-0] voice vote.

4. CURRENT BUSINESS

A. Presentation: Internal Audit Report on Governance Fiduciary Responsibility and Training

Steve Cogan, Principal with REDW, commended the Board and management for undertaking the review of governance and training. The goal of the audit was to provide feedback and help the Board in its responsibilities to protect and oversee the retirement assets of PERA as well as assist the management and Board members as individuals.

Mr. Cogan explained their preparations to conduct the internal audit and the identified the best practice sources they reviewed and relied upon throughout the country.

Board Member and Committee Member Training

Matt Doxtator, REDW Senior Auditor, reviewed the different components of the audit and offered REDW's recommendations for this section:

- Creation of an education/training committee to ensure the identification of training opportunities as a collaborative process
- Formalized ongoing education for Investment Committee members
- Financial statement and risk management statement education for the Audit and Budget Committee members
- Training on standard practices

Mr. Doxtator recognized the expertise of PERA Board members and noted the audit recommendations address the long term.

Providing the management's response, CFO Natalie Cordova said there was agreement to continue collaborating with the Board. Staff will improve the tracking of training and advise the Board members of education opportunities. She said REDW's recommendations will serve the agency well to make sure management helps the Board to adhere to policies and procedures.

Mr. Cogan noted that it can be challenging to keep up with the training and documentation as a volunteer Board member. An increase in management's tracking and

involvement would address those issues.

Ms. French addressed the issue that arose with training for new Board members and said it was a scheduling issue that would be resolved in the future.

Gifts and Conflicts of Interest Reporting

Mr. Doxtator said that this review entails the State regulations as well as Board policy. There were lapses in documentation noted in the audit. Recommendations in this category included:

- Assigning specific responsibility to see that form reporting is adhered to
- Require vendors to report gifts
- Require annual acknowledgement of reading and complying with the Standards of Conduct

Responding for management, Ms. Cordova said an FTE will be designated to review gift reporting and financial conflict of interest forms with a final review by the Executive Director prior to submission. Staff agrees that all vendor contracts should require disclosures regarding gifts, etc. to be submitted on an annual basis.

Ad Hoc Evaluation Committee and Due Diligence Process

Mr. Doxtator said REDW's recommendations are all in line with best practices and are provided as a means of protecting the Board and IC members. Recommendations in this area included:

- Discontinue the inclusion of Board members in the due diligence and investment manager recommendation process
- Ensure that the Board's focus in investment manager selection follows the process established in the Investment Procurement Policy is followed
- Consider the implementation of a responsibility matrix to define the roles of the Board, investment managers, CIO and investment staff in key investment activities

Responding for management, Ms. Cordova said they agree with REDW's recommendations. These are good clarifying measures that will help protect the integrity of the process and reduce the Board's liability.

Ms. Naranjo Lopez said Board oversight is extremely important. Mr. Cogan agreed and said understanding the right questions to ask may require additional Board training.

Mr. Reynolds commented that the Board spends a great deal of time listening to investment managers that could be better used talking with staff and PERA's consultants.

Open Meetings Act and Retention of Communication

Mr. Doxtator said additional training and clarification of communication policies might be of benefit to the Board. The recommendations were drafted to help protect Board members and ensure that information is maintained to defend the Board's decisions.

- Create and implement a policy governing electronic communications
- Assign Board members PERA email addresses to conduct PERA business and create a policy to govern that use

- Conduct annual training on the Open Meetings Act, Public Records Act and Inspection of Public Records Act
- Consider the use of a time clock to ensure that agenda timelines are following during Board and committee meetings

Ms. Cordova said management concurs with the recommendations and trainings will be scheduled. PERA email addresses are now available for the Board members.

Deputy Director Trujillo said now that PERA owns its own domain, PERA.org, email addresses can be provided to the Board members.

Board Policy Documents and Committee Charters

Mr. Doxtator said the theme of relying on management continues in this item with managing the schedule of committee responsibilities through work plans and/or calendar. This would guide the actions of the committees. Recommendations were offered as follows:

- Assign the responsibility to an appropriate member of management to create and distribute work plans or calendars for the Board and each committee to ensure compliance with requirements in the Board Policy documents and committee charter
- Consider the use of the AICPA Government Audit Committee Toolkit Audit Committee Matrix to guide the activities of the Audit Committee
- Create and implement formal evaluation criteria for the Board and each of its committees
- Clarify who has legal and policy compliance responsibility
- Consider amending the IC Charter to define what decisions must be ratified by the Board, what reports must be provided to the Board and how often
- Amend the IC Charter to include a requirement that the charter be reviewed and updated at least annually
- Create a delegation of authority matrix to establish which Agency decisions require approval by the Board

Ms. Cordova stated that management agreed with the recommendations and will improve in its consistency in providing work plans. Management will work with the Board on establishing procedures to evaluate committees and review charters, etc. She said a feasible timeline to implement improvements should be within a few months of the 2016.

Ms. Naranjo Lopez said she would like further division between the independent auditor and management and noted a conflict could be perceived in that management hired the independent auditor. Ms. Cordova said the standards for independent auditors are very strict and two Board members participated in the RFP process selecting this firm.

Mr. Cogan said in most instances the Board is considered independent and through its audit committee takes the responsibility for appointing an independent financial statement auditor and for selecting and hearing from the internal audit function. He noted that PERA was in a better position in terms of independence because the auditors are not employees of management.

Human Resources and Employee Training

Mr. Doxatator said HR was included in the audit to review a commitment to competence which is demonstrated by how the agency hires, recruits, trains, evaluates and holds personnel accountable. He offered the following recommendations:

- Assign responsibility to ensure trainings are completed as required by job responsibilities
- Create a comprehensive training calendar which includes a refresher on the agency's Code of Conduct
- Ensure that background check requirements are clearly defined and enforced
- Designate an appropriate staff member to ensure that evaluations of exempt employees are performed annually
- Consider documenting whether the Executive Director was evaluated by the Board
- Assign responsibility for the periodic update of policies and create a rotating schedule
- Consider a global review of job duties, prioritization of key functions and responsibilities

Ms. Cordova said management agrees and said a training calendar is being developed to track all trainings including ethics and code of conduct trainings. Since July a policy committee is meeting on prioritizing and scheduling updates to PERA policies.

Board Comments and Questions

Ms. Naranjo Lopez asked whether the auditors considered that the Investment Committee be composed of all Board members and whether it was appropriate for the Chief of Staff to also hold the position of General Counsel. She asked whether any staff failed to meet the minimum qualifications within their positions. Mr. Doxtator said the audit did not review personnel resumes but instead focused on whether the individual understood what was expected of them in their position.

Stating she submitted hers, Ms. Naranjo Lopez expressed concern that the auditor was unable to obtain the evaluations of the Executive Director. Mr. Doxtator said they could follow up on that. Ms. Naranjo Lopez offered to forward hers to the auditors.

Ms. French said the last Executive Director evaluation occurred in an executive session, and she advised the Board at that time that she would consolidate the evaluations into one. She offered to forward the collective evaluation to the auditors.

Mr. Cogan said the report can be adjusted regarding that evaluation. Responding to Ms. Naranjo Lopez' concern regarding the IC membership, Mr. Cogan said it is best practice to have a subset of the Board serve on the committee. Regarding potential conflict of interest regarding chief of staff and general counsel, Mr. Cogan said that would require an evaluation of the specific roles and responsibilities.

Mr. Cogan said they could list concerns of Board and include them in a future audit.

Ms. Naranjo Lopez recommended that as a good reminder of policies and procedures all Board members should participate in the new member orientation. Ms.

French agreed and said that was the reason the orientation was to be held during the retreat.

Ms. Kohlasch said she spoke to the auditors earlier and had her concerns addressed.

Mr. Esquibel asked about the contracted scope of work under which REDW performed this service.

Mr. Esquibel asked how much weight the auditors gave to facts versus comments/opinions and whether the recommendations were derived from facts or comment/opinions. Mr. Cogan said it is REDW's intention for all of their findings to be based on fact. He said if REDW hears the same comments from a number of people that suggest, for example, additional training in a particular area would be prudent for the organization then that also is observed as a fact.

In particular, Mr. Esquibel asked where the facts were to sustain that deliberations were occurring outside of a quorum and said he found it troubling that was within an audit report. Mr. Cogan said this concern was raised as a theme by a number of staff and Board members, thus REDW recommended additional training was appropriate and helpful. Mr. Cogan said if there is specific language or sentence phrasing that is objectionable, he was willing to rework that area.

Mr. Esquibel said without actual factual data the theme could be promulgated by those with an "ax to grind." Mr. Cogan said it was their professional sense that there was enough of a theme to, not accuse, but recommend additional training, education and awareness as an appropriate response to the feedback received. Based on their conversations there is an opportunity for education, learning and further awareness.

In response to Mr. Esquibel's question regarding management's response, Mr. Doxtator said they were provided by management and unaltered in their presentation within the report.

Mr. Jimenez cautioned against badgering the auditors.

Mr. Esquibel requested a definition of PERA's governance structure. Mr. Cogan commented that the PERA has a process under state statute as an elected board and as result the Board may be lacking experts in investments, government financial statements, government audits, accounting, and benefit plan administration. The Board addresses this deficiency through training and education which is helpful and appropriate. However, in the context of creating a legacy the Board may want to consider a process where the Board through its structure appoints experts in the above mentioned items.

Mr. Doxtator said reviewing the governance structure includes determining whether the board is independent, committees are independent and the makeup of the committees is consistent with best practices or the statutes. The management structure is also reviewed for who they report to and who they have oversight of. The report does not offer an opinion regarding governance, rather it compares best practice criteria used for evaluation purposes. Mr. Cogan identified the organization best practices that were referenced within the report.

Ms. Cordova said management collaborated in developing responses.

Mr. Esquibel asked about Board members participating in due diligence and Ms. French said in her 12 years as a Board member it has always been done.

In response to Mr. Esquibel's questions about meeting timelines, Mr. Cogan said these are recommendations that REDW feels would be helpful to the Board's efficiency.

Ms. Cordova offered to provide the RFP as well as the contract as requested by Mr. Esquibel. Chair Logan said he promoted the notion of an independent outside auditor.

Ms. Naranjo Lopez said she attended a conference in 2014 that focused on how to effectively use internal audit committee. She had requested training on that.

Mr. Martinez said he strives to be diligent, a responsible leader and represent the membership by providing his experience in government. The Board's role is that of leadership. He said some of the phrases within the report require rewording. Best practices should be seen as a manner in which to guide the Board.

Mr. Cogan said the intent of the report was for the Board to use it as a tool to improve.

Mr. Jimenez thanked the auditors for outlining some of the agency's deficiencies and for their recommendations on improvements. He congratulated them on a succinct report and said he hoped the Board would be able to take the criticism and move forward. He commended staff for their brave recommendations. He expressed his disappointment in the Board's lack of courage to move forward and instead critiquing the audit process. He asked the Chair what the plan was to address these items and why it was not an action item.

Chair Logan said as a preliminary report it was not ready for action. Ms. Cordova said procedurally, audits are not action items and are provided as information items. Mr. Jimenez said the Board should be diligent in taking action on the recommendations that came forward.

Mr. Logan said he welcomed the opportunity for the Board to work on the issues as presented within the audit.

Ms. Fisher appreciated the audit report and was said she was confident the Board would follow up on the recommendations.

Ms. French said the audit brought to light some very important issues, that as Board chair she anticipated discussing at the next retreat.

Chair Logan said the goal was to obtain a thoroughly independent report and he felt that was accomplished. It was obvious from the report that the Board wants what is best

for the fund.

Mr. Propst said in his career he has seen many audit reports and the one presented by REDW is one of the best. He also recognized Ms. Cordova's fine work on this report and senior staff for their participation.

Chair Logan said he had additional comments and concerns that he would address with Ms. Cordova.

5. **OTHER BUSINESS**

None was presented.

6. **ADJOURNMENT**

Having completed the agenda, Chair Logan adjourned this meeting at approximately 11:05 a.m.

Approved by:



Stewart Logan, Chair
Audit & Budget Committee

ATTEST:



Wayne Propst, Executive Director