1. Call to Order, Roll Call, Opening remarks ................................................. Mr. Gregory Ferguson

The meeting was called to order by Chairman Ferguson at 11:02 a.m.

2. Review, discussion and possible approval of the Operations, Governance Policy and Audit Committee Minutes from May 30, 2012 .......................................................... Mr. Gregory Ferguson

MOTION: 6-1-12 At 11:03 a.m.

Motion: To approve the minutes of the Operations, Governance Policy and Audit Committee from May 30, 2012.

Moved by: Mr. McHenry
Seconded by: Mr. Ferguson
Discussion: None
In Favor: Unanimous
Motion: Passes

3. Presentation of the Month-to-Date Budget Report for FY 2012 and possible Recommendations ................................................................. Mr. John Hendricks

Regarding the year end wrap-up, we were $387,000 over budget, but when you remove the litigation expenses, we were under by $33,000 stated Mr. Hendricks.
4. Written update on the progress of the Local Board Training Program and discussion and possible Recommendations regarding same. Mr. Robert Ortega, Local Board Training Coordinator and Human Resources Manager, Mr. Don Mineer, Local Board Training Specialist.

Mr. Ortega said an outreach program was conducted to inform individual boards and their members regarding laws and benefits.

5. Presentation of the Requests for Local Board Rehearing Report for the current month. Mr. Jim Hacking, Administrator.

Mr. Hacking indicated that this report will be a standard agenda item for each meeting; it will be used to track the status of outstanding or unresolved local board rehearing requests.

6. Review, discussion and possible Action regarding the June 2012 Kutak Rock billing for legal services performed in May 2012. Mr. Jim Hacking.

The Kutak Rock bill was $69,902 the bulk of which was investment related expenses. Mr. Hacking indicated that the billing had been reduced by $6,000 because of his objection to the magnitude of the charges related to the handling of a FOIA request related to a potential investment with a company called Red Kite.

MOTION: 6-2-12
At 11:21 a.m.
Motion: To recommend to the Board of Trustees the approval of the June 2012 Kutak Rock billing for legal services performed in May 2012.
Moved by: Ms. Stein
Seconded by: Mr. McHenry
Discussion: None
In Favor: Unanimous
Motion: Passes

7. Status report and possible Recommendation regarding fiduciary insurance for the PSPRS Board of Trustees. Mr. Jared Smout, Deputy Administrator.

Mr. Smout reported that upon further review, additional fiduciary insurance coverage is not needed. The insurance offered by the State of Arizona through ADOA should be quite sufficient for the needs of the Board and the staff. Because of our existing relationships with attorneys that are on the Attorney General’s approved list, we will most likely be able to stay with legal counsel of our choosing in the event of a lawsuit alleging breach of fiduciary duty. In addition, the state Administrative Code offers considerable protections that we do not want to jeopardize by seeking our own separate insurance coverage without ADOA approval. The penalty by ADOA for unauthorized purchase of insurance is 120% of the unauthorized purchase; moreover, the liability for the unauthorized purchase would be personal. Risk Management will back us up and we can use the Attorney General’s office plus outside counsel. Mr. Smout also pointed out that the state carries an excess insurance policy.
A suggestion was made to request a presentation by ADOA Risk Management regarding fiduciary insurance. This will be arranged for a future Board meeting.

8. Status report and Recommendation with respect to the PSPRS staff compensation review

Mr. Jim Hacking reported that Buck & Company will begin the process of staff compensation review in July; it should be completed within three months.

9. Presentation, discussion and possible Recommendations regarding modifications to the FY 2012/2013 PSPRS Administrative Budget

Mr. Hacking told the Committee members that certain modifications to the FY’13 administrative budget are needed. Since we cannot know how the court challenges to the pension reform bill will come out, we need to add an additional $40,000 for actuarial expenses in order for the actuaries to track the assets belonging to the retirees and various subsets of the active member participants. He also indicated that we have to accommodate slightly higher charges for the services of the part-time Assistant Attorney General.

On the other hand, Mr. Hacking pointed out that the budget can be reduced by $60,000 since there will be no need to purchase fiduciary liability insurance. Moreover, he indicated that, given what we know now about the FY’12 investment return relative to the benchmark return, we can further reduce the budget for the investment staff bonuses by $165,000 and related fringe benefits by an additional $28,000. That will result in a net reduction in the FY’13 budget relative to what was approved at the May meeting. The new budget total of $9.62 million will be significantly less than the budget for FY’12 and less than the actual expenditure level for FY’12.

10. Report on the factors impacting the financial status of PSPRS Plans including legal challenges to the various provisions of SB 1609

Mr. Hacking discussed the principal factors that will have negative impacts on the results of the actuarial valuations of the Plans when those valuations are completed in October. Among other things, he indicated that the funding ratios for the Plans will decline even more than expected because the System will fall far short of the actuarial assumed rate of return of 8%. In addition, we will have to factor in the impact of the additional unfunded liability associated with HB 2409, which the legislature approved for the PSPRS Plan this past session. Also, the changes in economic assumptions for the Plans that will begin to take effect during FY’13 will further erode the funding status of the Plan. All these factors will combine to put significant upward pressure on employer contribution rates that are already at very high levels. The new rates that will take effect on July 1st that are based on System FY’11 results will be 27.18% for PSPRS.
contributing employers, 11.31% for CORP contributing employers and 36.44% for EORP contributing employers whose rate is not subsidized. For those EORP employers whose contribution rate is subsidized, the percentage will be 20.87%. All these rates will increase for employer FY’14 once the results of the System FY’12 valuation results are known later this fall.

Regarding post retirement adjustments, Mr. Hacking indicated that PSPRS eligible beneficiaries would receive increases in two steps. However, because of the pension reform bill, neither CORP nor EORP beneficiaries will receive any adjustment this year.

A discussion was held regarding what would have happened if the pension reform bill SB 1609 had not been enacted. Last June 30 there was $274.5 million of excess returns which would have gone into the COLA reserves for the three Plans. After factoring in the cost of the payments that would have occurred last July 1st, there would still have been balances of $362 million in the PSPRS Reserve, $46 million in the CORP Reserve and $26 million in the EORP Reserve. Those balances would have been invested during FY’12 and would be available to finance post-retirement adjustments for the eligible beneficiaries of all three Plans this July 1st. But given that the pension reform bill put an end to any new in-flows of excess return assets to the Reserves, effective May 31, 2011, only PSPRS retirees will receive adjustments this July 1st. Of course if the courts rule that the changes to the COLA that were made by SB1609 are unconstitutional, the System will have to go back and undo the effects of those COLA changes.

11. Discussion and possible Recommendation that the Board of Trustees approve the revisions to the sections of the Governance Manual that have been reviewed and approved by the Committee

MOTION: 6-4-12
At 12:12 p.m.
Motion: To recommend to the full Board the approval of the revisions to the Governance Manual that were reviewed and approved by the Committee.
Moved by: Mr. McHenry
Seconded by: Ms. Stein
Discussion: None
In Favor: Unanimous
Motion: Passes

12. Report on the FY 2012 and FY 2013 Internal Audit Plans

Ms. Feeley stated that since the Audit Plan/Risk Assessment was not listed as an action item on the agenda, she will simply make a report of what she found. She told the Committee that based on the Risk Assessment; the System appears to be in very good shape regarding major controllable risks. This year an audit will be conducted on investment due diligence and an audit will be conducted to see if we are paying the correct management fees. She described the reasons for an audit schedule and said that every six months an area will be picked out for spot checks. A rotation schedule will be created for the audits.

13. Call to the Public.
This is the time for the public to comment. Members of the committee may not discuss items that are not specifically identified on the agenda. Therefore, pursuant to A.R.S. § 38-431.01(H), action taken as a result of public comment will be limited to directing staff to study the matter, responding to any criticism, or scheduling the matter for a later date for further consideration and possible recommendations to the Board of Trustees.

No members of the public wished to speak.

14. Schedule next meeting. *(Currently scheduled for Wednesday, July 25, 2012)*

15. Adjournment.

The meeting was adjourned at 12:26 p.m.

Gregory Ferguson, Chairman