

**PUBLIC SAFETY PERSONNEL RETIREMENT SYSTEM
BOARD OF TRUSTEES OPERATIONS, GOVERNANCE POLICY and AUDIT COMMITTEE
MEETING**

October 22, 2014

MINUTES

Members Present: Mr. Greg Ferguson, Chairman, Trustee
Mr. Jeff McHenry, Member, Trustee
Ms. Randie Stein, Member, Trustee

Others Present: Mr. Jared Smout, Deputy Administrator
Ms. Ivy Voss, Assistant Attorney General
Mr. Robert Ortega, Local Board Training Coordinator/HR Manager
Mr. Don Mineer, Local Board Training Specialist
Ms. Leslie Clark, Senior Financial Accountant/Great Plains DBA
Mr. John Hendricks, Senior Investment/Financial Accountant
Ms. Bridget Feeley, Internal Audit and Compliance Officer
Mr. Sam Meier, IT Operations Manager
Mr. Jon Chase, Senior Systems Programmer
Mr. Marco Ceglie, Avant Strategies
Mr. Christian Palmer, Avant Strategies
Mr. Paul Hemmes, Systems Programmer
Ms. Michelle Pechan, Paralegal

1. Call to Order, Roll Call, Opening remarks.

*Mr. Gregory Ferguson
Committee Chairman*

The meeting was called to order by Chairman Ferguson at 10:00 a.m.

2. Presentation of the Month-to-Date Budget Report for FY 2015 and possible **Recommendations.**

*Mr. John Hendricks
Manager Finance and Accounting*

The total agency is estimated at the end of the fiscal year to be 5.14% over budget due to administrative and investment legal fees. Legal fees are projected to be over budget by \$301,300 at the end of the fiscal year which will be updated as more information becomes known. Administrative and investment legal fees will be reduced by about 50% due to in-house investment attorney and an Assistant Attorney General having been added to the staff. Personnel fees paid to ADOA are projected to be about \$40,000 for payroll processing.

3. 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

The Board Training staff continues to reach out to smaller boards and to assist those encountering problems. The training staff is working on the merger of the Parker, Lakeside, and Show Low Fire Districts into the Timber Mesa Fire and Medical District.

4. Presentation of the "Requests for Local Board Rehearing" Report for the current month.

Mr. Jared A. Smout
Deputy Administrator

There are two issues pending.

5. Review, discussion and possible **Action** regarding law firms' billings for legal services performed in September, 2014.

Mr. Jared A. Smout

The legal billings amounting to \$114,026.55 have been reviewed by appropriate in-house staff. A big portion is in the investment department and discussion was held regarding the fact this bill will be reduced in the future since in-house legal counsel has been hired. The committee discussed how other pension plans work regarding legal advice.

MOTION: 1-10/22/14	At 10:12 a.m.
Motion:	To approve the law firms' billings for legal services performed in September, 2014 in the amount of \$114,026.55.
Moved by:	Mr. McHenry
Seconded by:	Ms. Stein
Discussion:	None
In Favor:	Unanimous
Motion:	Passes

6. Report and **Recommendations** on the FY 2014 Compliance and Internal Audit Plan.

Ms. Bridget Feeley
Internal Audit and Compliance Officer

A review of travel and expense reimbursements has been completed and several issues have been addressed and corrected. These will be reviewed again in three to four months to see if the new processes are working as intended. Currently, the compliance staff is reviewing service purchases and the actuaries will be asked to review what they use to calculate the actual payments and they will be asked to comment upon the soundness of this process.

This month's focus will be reviews of contributions and management fees. The management fee review includes a written description of what is being done so the board can review it. The committee was asked to ratify if the written description of the review of the management fees reflects what was asked of the Internal Audit and Compliance Officer by the board.

MOTION: 2-10/22/14	At 10:18 a.m.
Motion:	The Committee recommended the Board of Trustees access the written description of the review process of management fees for possible ratification.
Moved by:	Ms. Stein
Seconded by:	Mr. McHenry
Discussion:	None
In Favor:	Unanimous
Motion:	Passes

Discussion was held about the number of management fee reviews to be accomplished and what amount of time would be required to do them. Also, it was hoped to be able, at some point in time, to align the legal fees connected with the management fees.

7. Written update on external communications efforts.

*Mr. Marco Ceglie
Mr. Christian Palmer
Avant Strategies*

Avant Strategies' assistance was sought for broadening media relationships for PSPRS. The representatives of Avant Strategies spoke about the communications efforts that have been made since July and they will begin giving monthly updates as to their efforts and the value they have provided. Negative information has been waning and efforts to broaden information regarding PSPRS staff, the Board of Trustees and other positive aspects will continue. The first challenge is clarity; the second is accuracy of information; and the third is to establish more positive media relationships. Efforts are being made to steer out of negativity, to dispel negative views of the agency, and to expand coverage in a wider area. Other efforts will be made to present and to clarify complicated information in an easier manner to understand and to be more proactive regarding PSPRS so their story is known.

Discussion was held about the proposition for the City of Phoenix and the possible outcome as a result of the election if the proposition passes.

8. Presentation and discussion about the Purpose and History of the Public Safety Personnel Retirement System.

Mr. Jared A. Smout

The purpose of this agenda item, said Mr. Smout, is to have a constructive discussion about the purpose and history of PSPRS and why we have been different from ASRS, which is due to our administrative structure. Our purpose, based in statute, is to provide a uniform, consistent and equitable statewide program for public safety personnel who are regularly assigned hazardous duty in the employ of the state of Arizona and any political subdivision thereof where the administration of the System and the responsibility for making the provisions of the System effective for each employer are vested in a local board so that everyone would be responsible for their own system. This is the only plan like this in structure on the local level anywhere in the nation. Because of the unique structure, we have had some challenges recently as to where we fit in, how we should operate and how we should focus our attention.

Mr. Smout continued that it is his opinion that the System (the collective group of locally controlled entities) should not be viewed the same as the agency (the physical entity charged with ensuring that the System is uniform, consistent, and equitable). The System, as a whole, is represented and governed by the Board of Trustees (ARS § 38-848) who, through the Administrator and **“in accordance with the board’s governance policy and procedures and the budget adopted by the board”**, has employed the staff of the agency to carry out the collective purpose of the System (ARS § 38-848(L)(5)), that is, providing for a uniform, consistent, and equitable state-wide retirement program.

“As an independent trust fund whose assets are separate and apart from all other funds of this state” (ARS § 38-848(M)), the System’s funds are **not appropriated** and the System has been granted exemption from certain other state control in order to judiciously carry out its mandated purpose.

The State represents roughly 10% of the membership of the System and only 4% of the public safety employers. (If we include CORP and EORP, that number jumps to approximately 30% and 13%, respectively, yet still does not abscond the local administration structure.) Yet, frequent attempts to bring the System under more state control is inequitable, violating the statutory purpose of the System, and usurps the power and authority vested with the Board. Furthermore, only one position on the Board of Trustees is reserved for the State **“as an employer of public safety personnel”** (ARS § 38-848(A)(2)) and nothing more, thereby allowing the State a representative seat for its locally controlled agencies who are only a small part of the whole System.

Therefore, it is not wanting to be difficult or defiant, but rather out of duty that any attempt by the State perceived to overreach its authority and violate the statutory purpose of the System or usurp the authority of the Board, thereby compromising the integrity of this unique administration structure, has been and should rightly be met with concern by those charged to protect it. Therein lies the challenge in this 46-year relationship—to find and maintain a healthy balance between the unique administration structure of the System and the agency charged to oversee its statutory purpose.

9. Discussion and possible **Recommendations** regarding changes to the governing statements (mission, vision and values) of the System.

Mr. Jared A. Smout

Mr. Smout stated it is time to start changing the governing statements of the System since they no longer fit in order to lead the organization. We need more all-

encompassing guidelines in order to guide us at the top level and yet be able to apply it to lower levels. We need standards to govern our thoughts and behavior and we will begin this process.

10. Discussion and possible **Recommendation** regarding the use of legal counsel.

Mr. Jared A. Smout

For as long as the System has been in place and up until about a decade ago, the System used to have in-house legal counsel in the Assistant Administrator position to help interpret statute and give guidance in the day-to-day operations of the agency and also providing some guidance to the Fund Manager at the time. When that person left, reliance on outside counsel increased. As a result, the legal fees over the past decade have also increased due to the absence of this internal function. Additionally, the need for legal counsel in general was in greater demand due to the growth of the System and the growth of the agency that led to more complex issues needing attention. Moreover, during that same time the development and maintenance of governance policies and the increasing complexities of the changing investment portfolio, all of which had to be fulfilled by outside counsel, only added to those fees.

Now, however, we have in the Assistant Attorney General (only full-time since June) the internal function to help handle and deal with those same issues the Assistant Administrator had. Additionally, due to the growing complexities of our investment portfolio, the need for in-house investment counsel to help protect the interests of the Fund may have only presented itself within the past five years. Unfortunately, the search to find competent in-house investment counsel, who only began full-time in August, has taken just as long. By current indications, if the trend in decreased fees from August to September continues, it would seem that the combined efforts of our Assistant AG and in-house investment counsel have already begun to dramatically reduce our legal expenses (60% decrease in administrative, 40% decrease in investment, and 50% decrease in litigation fees).

However, that should not displace the purpose and desire for outside fiduciary counsel the Board has chosen to retain. **The challenge now is to return to the balance once shared over a decade ago between these two roles of internal and external counsel.** Indeed, because of the unique administrative structure of the System, it would behoove the Board to keep outside counsel so as to not create any unfavorable balance toward any one entity within the System, namely the State. Outside fiduciary counsel is the attorney for the System (the collective group of entities represented by the Board of Trustees) and in that role represents all their interests, not just the State's. By statute, the Attorney General serves as the chief legal officer of the State (ARS § 41-192(A)), which may put the Assistant AG assigned to our agency at odds with the interests of the System from time-to-time. Furthermore, although the AG may have authority to represent political subdivisions and municipalities in certain restricted instances, those same political subdivisions and municipalities have the right to withdraw the authority of the AG to represent them (ARS 38-192(A)(5)). Therefore, again, because of the unique administration structure of the System, retaining separate outside counsel may be in the best interests of the System, which essentially is a cooperative-type pension fund for political subdivisions and municipalities, with a few state agencies.

Chairman Ferguson stated many local boards do not realize the structure of the PSPRS. Mr. Smout replied we need to do a better job in educating the local boards. We have the

responsibility to oversee this and to protect the System since the original purpose for the way it was set up was great. We have begun the process as to informing the local boards as to how contribution rates are determined and people should be trained regarding this process along with actuarial support, especially the decision making people.

Discussion was held regarding how the attorney general's office approves attorneys. Events that have occurred in the last couple of weeks and the progress that has been made will be discussed in Executive Session. Also discussed was having a written summary regarding all of our legal matters and the actions.

11. Discussion and possible **Recommendations** regarding the use of Employment Agreements.

Mr. Gregory Ferguson

The Chairman of the Board has asked us to develop a consistent policy for Employment Agreements. Mr. Smout informed the committee he has compared all of the employment agreements and has shared with the committee the differences in those agreements. Ms. Stein inquired as to whether or not the fiduciary counsel is the same as the investment counsel and what do we need to do to break those two apart. Mr. Smout responded that would need a statutory change and suggested a one line item for each thing. Ms. Stein stated she does not understand why the internal auditor is not on this list since the function is to report to the Board and not to the Administrator. Who has the authority to have a contract versus being an employee? We need to be cognizant of the flow of business with the administrator and determine how to have this work smoothly. Discussion was held regarding a possible rewrite of section §§ 38-848(O) Ms. Stein added we need to look at standardizing contracts. Discussion was held about retention bonuses and to seek advice on industry practices.

12. Discussion and possible **Recommendations** regarding proposed legislation.

Mr. Jared A. Smout

Legislation is proposed in order to alleviate any IRS issues with the transition from a defined benefit plan to a defined contribution plan. Discussion was held about details of a proposed Administrative Bill.

MOTION: 3-10/22/14	At 11:31 a.m.
Motion:	The recommend to the Board of Trustees to move ahead with the IRS bill.
Moved by:	Ms. Stein
Seconded by:	Mr. McHenry
Discussion:	None
In Favor:	Unanimous
Motion:	Passes

13. Update and discussion on the progress of efforts with the ADOA in relation to the MOU.

Mr. Jared A. Smout

Three areas of focus in regard to the MOU are: personnel review which has been completed in draft form; GAO audit – the report should be given to us at the end of the month for our comment; and MOU – each item has been addressed.

14. Update, discussion and possible **Recommendation** on the RFP for fiscal 2015 external financial auditor.

Mr. Jared A. Smout

Three firms were invited to respond to the RFP and the best approach would be to extend the contract again to Heinfeld Meech for continuity especially with the implementations required by GASB. Discussion was about changes, if any, in the Heinfeld Meech staff and the committee will research if the state has a list of qualified external auditors. Staff has recommended awarding the contract to Heinfeld Meech with a one year option for the future fiscal year as needs are presented.

MOTION: 4-10/22/14	At 11:45 a.m.
Motion:	To recommend to the Board of Trustees to award the contract to Heinfeld Meech for Fiscal Year 2015 in the amount of \$148,935.
Moved by:	Mr. McHenry
Seconded by:	Ms. Stein
Discussion:	None
In Favor:	Unanimous
Motion:	Passes

15. 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.

There was no response to the Call to the Public

16. Schedule next meeting. (*Currently scheduled for Wednesday, November 19, 2014*)

The next meeting will be held on Wednesday, November 19, 2014.

17. Adjournment.

The meeting was adjourned at 11:47 a.m.

Mr. Greg Ferguson, Chairman