

AGENCY NAME:	Retirement System Investment Commission		
AGENCY CODE:	E19	SECTION:	98



Fiscal Year 2015-16 Agency Budget Plan

FORM A – SUMMARY

RECURRING FUNDS (FORM B DECISION PACKAGES)	My agency is submitting the following recurring decision packages (Form B): Requesting a net increase in "Other" Funds. 49/6	
	For FY 2015-16, my agency is (mark "X"):	
	<input type="checkbox"/>	Requesting a net increase in recurring General Fund appropriations.
<input type="checkbox"/>	Not requesting a net increase in recurring General Fund Appropriations.	

CAPITAL & NON-RECURRING FUNDS (FORM C DECISION PACKAGES)	My agency is submitting the following one-time decision packages (Form C):	
	For FY 2015-16, my agency is (mark "X"):	
	<input type="checkbox"/>	Requesting capital and/or non-recurring funds.
<input checked="" type="checkbox"/>	Not requesting capital and/or non-recurring funds.	

PROVISOS	For FY 2015-16, my agency is (mark "X"):	
	<input checked="" type="checkbox"/>	Requesting a new proviso and/or substantive changes to existing provisos.
	<input type="checkbox"/>	Only requesting technical proviso changes (such as date references).
<input type="checkbox"/>	Not requesting any proviso changes.	

Please identify your agency's preferred contacts for this year's budget process.

	<u>Name</u>	<u>Phone</u>	<u>Email</u>
PRIMARY CONTACT:	Michael Hitchcock	737-7698	mhitchcock@ic.sc.gov
SECONDARY CONTACT:	Brian Wheeler	737-6843	bwheeler@ic.sc.gov

I have reviewed and approved the enclosed FY 2015-16 Agency Budget Plan, which is complete and accurate to the extent of my knowledge.

	<u>Agency Director</u>	<u>Board or Commission Chair</u>
SIGN/DATE:		
TYPE/PRINT NAME:	Michael Hitchcock	Edward Giobbe

This form must be signed by the department head – not a delegate.

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FORM B – PROGRAM REVISION REQUEST

DECISION PACKAGE	4916
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Provide the decision package number issued by the PBF system ("Governor's Request").

TITLE	Personal Services/Other Operating/Employer Contributions
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Provide a brief, descriptive title for this request.

AMOUNT	\$5,487,758.00
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What is the net change in requested appropriations for FY 2015-16? This amount should correspond to the decision package's total in PBF across all funding sources.

ENABLING AUTHORITY	SC Const. art. X, § 16; SC Code, Title 9, Chapters 1 and 16; Title 30, Chapter 4.
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What state or federal statutory, regulatory, and/or administrative authority established this program? Is this decision package prompted by the establishment of or a revision to that authority?

FACTORS ASSOCIATED WITH THE REQUEST	Mark "X" for all that apply:
	<input type="checkbox"/> (Base Adjustment) Allocation of statewide employee benefits.
	<input type="checkbox"/> (Base Adjustment) Realignment within existing programs and lines.
	<input type="checkbox"/> (Base Adjustment) Restructuring of agency programs – <i>requires pre-approval.</i>
	<input checked="" type="checkbox"/> Change in cost of providing current services to existing program audience.
	<input type="checkbox"/> Change in case load / enrollment under existing program guidelines.
	<input type="checkbox"/> Non-mandated change in eligibility / enrollment for existing program.
	<input type="checkbox"/> Non-mandated program change in service levels or areas.
	<input type="checkbox"/> Proposed establishment of a new program or initiative.
	<input type="checkbox"/> Loss of federal or other external financial support for existing program.
<input type="checkbox"/> Exhaustion of fund balances previously used to support program.	

RECIPIENTS OF FUNDS	Additional funding will be used both to recruit staff with specialized skills for investment management, oversight, operations, and reporting; and to acquire systems to improve investment management capabilities.
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What individuals or entities would receive these funds (contractors, vendors, grantees, individual beneficiaries, etc.)? How would these funds be allocated – using an existing formula, through a competitive process, based upon predetermined eligibility criteria?

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RELATED REQUEST(S) Decision package is not associated with other decision packages

Is this decision package associated with other decision packages requested by your agency or other agencies this year? Is it associated with a specific capital or non-recurring request?

MATCHING FUNDS Funds will not be matched

Would these funds be matched by federal, institutional, philanthropic, or other resources? If so, identify the source, amount, and terms of the match requirement.

FUNDING ALTERNATIVES Restricted - Other funds
Fund 42170000
RS Investment Commission Operating

What other possible funding sources were considered? Could this request be met in whole or in part with the use of other resources, including fund balances? If so, please comment on the sustainability of such an approach.

FY16 Budget Proposal Summary

	<u>FY 16</u>	<u>FY 15 Approved</u>	<u>FY 15 Requested</u>
Total Personal Service	9,409,244	6,074,739	8,350,000
Operating Expense	6,345,369	4,649,800	4,650,000
Employer Contribution	2,054,520	1,596,835	1,920,000
Total Budget	17,809,132	12,321,374	14,920,000
Requested New FTEs	9	0	5
Total FTEs	51	42	47

SUMMARY

For FY2016, we are requesting 9 additional FTEs, which if approved, would bring our total to 51. A total FTE count of 51 will approach close to “full staffing” levels based on our current strategies and initiatives.

In addition to salaries and overhead (supplies, computers, etc.) for new FTEs, the Commission has acquired an administrator system and continues to seek a risk analysis and reporting system. These systems will improve investment management capabilities; allow us to acquire additional capabilities similar to our peers; and will mitigate risks. Each also fulfills recommendations of the Funston fiduciary audit. We also will engage a

consultant to conduct a Compensation Study and update the Commission's Compensation Policy and Performance Incentive Compensation (PIC) Plan per both Commission Policy and Funston Recommendation.

New Unclassified FTE Request Summary for FY15 – Totaling \$9,409,244.00

- Seek to recruit staff with specialized skills for investment management and oversight, operations, reporting and to continue addressing long-standing needs and Funston recommendations.
- **Requesting 9 Additional FTEs**—2 from prior year requests plus 7 additional for growth
- **4 new Investment staff:**
 - Carry-over: 1 Senior Officer (\$120K/yr range)
 - Additional: 2 Senior Officers (\$120K/yr range) and 1 Analyst (\$80K/yr range)
 - Planned Focus: Expand direct/co-investment capabilities, investment research and internal management
 - Primary Goals: Pursue attractive direct/co-investments, enhance internal management capabilities to increase expected returns with lower overall fees
- **5 new Operations staff:**
 - Carry-over: 1 Senior IT Applications Developer (\$100K/yr range)
 - Additional: 1 Reporting Performance Officer (\$60K/yr range)
 - Additional: 1 Human Resources Coordinator (\$50K/yr range)
 - Additional: 1 Legal Assistant/Paralegal (\$60K/yr range)
 - Additional: 1 Internal Audit Senior Consultant (\$85K/yr range)
- If approved, will approach “full staffing” based on current strategy/initiatives

Operational Request Summary – Totaling \$6,345,369.00

- Continue acquiring needed reporting and back office systems:
 - Improve investment management capabilities
 - Acquire additional capabilities similar to peers
 - Continue addressing Deloitte Risk Assessment recommendations, mitigate risks
- System requests—generally consistent with level “requested” in prior fiscal year:
 - Ancillary systems/services: Risk, Private Markets, Data Warehouse, Performance Analytics, other possible Fund Administrator services
 - Will pursue “modular” approach based on cost estimates and approved appropriation
 - As procurement process delays obtaining proposals, estimates used for budget
 - Continue to rely on PEBA for primary IT outsourcing
- Includes new FTE overhead per person (supplies and equipment, travel, etc.)
 - Plan to engage a consultant to update Compensation Study and review Commission's Compensation Policy and PIC Plan

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- Expect general inflationary increases
- Modest increase in rent

Additional Details-Investment Positions

Senior Private Markets Officer

- Aid in the development and implementation of the private markets program.
- Daily oversight for sourcing, assessing, and monitoring managers.
- The Senior Officer is expected to be a valuable contributor to the investment decision-making process and strategic asset class plan initiatives.
- Senior Officers have higher-level investment experience (10+ years).

Senior Diversifying Strategies Officer

- Aid in the development and implementation of the hedge fund and global tactical allocation program.
- Daily oversight for sourcing, assessing, and monitoring managers.
- The Senior Officer is expected to be a valuable contributor to the investment decision-making process and strategic asset class plan initiatives.
- Senior Officers have higher-level investment experience (10+ years).

Senior Real Estate Officer

- Aid in the development and implementation of the real estate program.
- Daily oversight for sourcing, assessing, and monitoring managers.
- The Senior Officer is expected to be a valuable contributor to the investment decision-making process and strategic asset class plan initiatives.
- Senior Officers have higher-level investment experience (10+ years).

General Investment Analyst

- The Investment Analyst will be responsible for assisting with asset class research, conducting due diligence and research on investment managers and strategies, and other projects, as requested.
- The analyst is expected to be a valuable contributor to the investment decision-making process and strategic asset class plan initiatives.
- The analyst will have 0-3 years of experience.

Additional Details-Operations Positions

Senior IT Applications Developer

- Assist IT Director with the integration of new reporting, analytics, risk systems and data warehouse capabilities
- Provide day-to-day support of technology needs for investment and operations staff
- Address programming needs of investment and operations staff for ad hoc and ongoing projects

Reporting Performance Officer: Fee Reporting Oversight

- Provide oversight of the Administrator’s collection and validation of fees.

- Expand and refine current process for collecting manager fees.
- Ensure population and completeness in data repository.
- Work with Administrator to refine models to accommodate changing customs.
- Inventory, summarize, and group Investment Management Agreements or similar agreements for comparative purposes.
- Verify reasonableness and alignment with industry standard
 - Verify with RSIC Investment Team that fees paid are reasonable according to terms.
 - Analyze fee structures and assess reasonableness with industry standards.
 - Serve as resource during due diligence to assess reasonableness of proposed fee structure.

Human Resources Coordinator

- Schedules college recruiting fairs and attends, along with appropriate staff, to identify qualified intern and job applicants.
- Posts open positions and corresponds with job applicants to notify them of next steps.
- Arranges interview times, and as needed travel and lodging, for applicants.
- Provide initial telephone interview/screening to obtain work history, education, training, related job skills, salary requirements, etc. in order to refer qualified applicants to hiring manager for further consideration.
- Maintains records and files on recruiting activity and other HR/employee information. Reports EEO and other data as required.
- Conducts new hire orientations and enters new hire data into appropriate systems.
- Maintains organization charts and employee directory as well as personnel and other employee files.
- Coordinates and schedules training activity/events in support of training initiatives and career development plans as well as tracks/records training history information. Researches training program options to identify appropriate content and cost.
- Prepares and distributes training materials as needed.

Legal Administrative Assistance/Paralegal

- Provide an array of administrative and support services for RSIC's four lawyers and senior management, including:
 - Assistance with maintenance of hard copy and electronic files.
 - Assistance with conversion of historical hard copy records to electronic records
 - Assistance with maintenance of departmental calendars, tracking data bases, logs, etc.
 - Assistance with special projects (litigation support, group trust name change project, etc.)
- RSIC had a full time temporary employee providing this service during the period commencing late 2011 and ending in 2013. While the agency's intern pool has

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been available from time to time to provide limited assistance, RSIC Legal needs a dedicated resource to provide ongoing administrative and support services.

Internal Audit Senior Consultant

- Plan and perform financial, operational, and compliance related audits and/or reviews with minimal supervision.
- Perform walkthroughs of complex business processes and test the design and effectiveness of internal controls throughout the organization
- Document work and prepare observations and recommendations for corrective action and utilize and reference best practice audit tools and methodologies.
- Proactively communicate audit status and observations to audit management to ensure achievement of objectives.

Provide a summary of the rationale for the decision package. Why has it been requested? How specifically would the requested funds be used? If the request is related to information security or information technology, explain its relationship to the agency’s security or technology plan.

Calculations are based upon the goals of the Commission as illustrated in the Annual Investment Plan and the Statement of Investment Objectives and Principles. It also encompasses the recommendations of the Funston fiduciary audit. RSIC has not been authorized for its full request in previous years. Those prior requests along with projections beyond them are included in the current request. The total of the request reflects an agency close to “fully staffed” and operational for the foreseeable future and based upon the current Commission-approved strategic plan.

FY16 Budget Proposal Summary

METHOD OF CALCULATION

	<u>FY 16</u>	<u>FY 15 Approved</u>	<u>\$ Change</u>	<u>% Change</u>
Total Personal Service	9,409,244	6,074,739	3,334,505	54.89%
Operating Expense (requested)	6,345,369	4,649,800	1,695,569	36.47%
Employer Contribution	2,054,520	1,596,835	457,685	28.66%
Total Budget	17,809,132	12,321,374	5,487,758	44.54%
FTEs	51	42	9	21.43%

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	<u>Analysis of Major Changes in Budget (\$M)</u>	
	FY 15 approved budget	\$12.3
	Significant changes:	
	New 9 FTEs estimated salary	\$0.8
	Add'l PIC incl 6 hired FY 15 Inv FTEs	\$1.4
	Est staff salary performance increases	\$0.7
	Est Additional Temporary Employees	\$0.2
	Additional systems capabilities	\$0.7
	Retainage set aside	\$0.4
	Other, net	\$0.8
	Est increased employer contribution	\$0.5
	Total estimated budget increase	\$5.5
Total estimated FY 15 budget	\$17.8	

How was the amount of the request calculated? What factors could cause deviations between the request and the amount that could ultimately be required in order to perform the underlying work?

FUTURE IMPACT	<p>All of the Commission’s funding comes directly from the South Carolina Retirement System trust funds. There are no maintenance-of-effort obligations as a result of the proposed increase.</p> <p>The proposed increase will bring the Commission close to “full staffing” levels and will provide the Commission with additional investment, risk management and other systems that are necessary for a pension fund of our size (approximately \$29.8 Billion in investments around the world).</p>
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Will the state incur any maintenance-of-effort or other obligations by adopting this decision package? What impact will there be on future capital and/or operating budgets if this request is or is not honored? Has a source of any such funds been identified and/or obtained by your agency?

PRIORITIZATION	<p>RSIC will pursue remaining IT needs as quickly as possible. The addition of investment versus operations staff simply will reflect the ability to find the best candidates as soon as possible.</p>
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If no or insufficient new funds are available in order to meet this need, how would the agency prefer to proceed? By using fund balances, generating new revenue, cutting other programs, or deferring action on this request in FY 2015-16?

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INTENDED IMPACT

In the Fiscal Year Ending June 30, 2014, the Commission’s investment decisions resulted in a 15.99% Plan Return, which significantly exceeded the 14.26% Policy Return. This translates to an outperformance of 102 basis points or an additional \$270 million for the Retirement System trust funds due to the active management of the portfolio by RSIC employees. Over the past five years, investment staff have been instrumental in creating over \$1 Billion of outperformance, net of fees. With the additional proposed budget allocation, the Commission will seek to build upon this record, and will endeavor to produce superior long term, risk-adjusted investment results for the trust funds.

As of 6/30/14	Plan Returns ¹	Policy Returns ¹	Outperformance (Bps)	Cumulative Investment Gain (\$) ²	Cumulative Outperformance (\$) ²
One Year	15.29%	14.26%	102 BPS	\$4,034	\$270
Two Years	12.61%	11.16%	145 BPS	\$6,547	\$754
Three Years	8.37%	7.51%	86 BPS	\$6,633	\$680
Five Years	11.48%	9.98%	150 BPS	\$13,720	\$1,797

¹Returns greater than one year are annualized
²Dollar values in millions

- “Policy Returns” represent hypothetical return if assets invested passively (indexed) with weights per AIP allocations
- Reflects additional value of investment staff decisions

What impact is this decision package intended to have on service delivery and program outcomes, and over what period of time?

PROGRAM EVALUATION

The Commission’s mission is to manage the assets of the South Carolina Retirement System trust funds in a prudent manner in order to secure the Fund for the sole benefit of Plan participants. The Commission has met or exceeded the statutorily set assumed rate of return over the long term while maintaining a reasonable level of risk. RSIC’s “disclosure of total external management fees is the most complete in the industry”, according to Funston. Funston also noted that, “there are no red flag indicators of malfeasance or misfeasance...consistent with the finding of the SIG (State Inspector General)”.

How would the use of these funds be evaluated? What specific outcome or performance measures would be used to assess the effectiveness of this program?

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FORM D – PROVISO REVISION REQUEST

NUMBER	NEW
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Cite the proviso according to the renumbered list for FY 2015-16 (or mark "NEW").

TITLE	Administrator Retention
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Provide the title from the FY 2014-15 Appropriations Act or suggest a short title for any new request.

BUDGET PROGRAM	
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Identify the associated budget program(s) by name and budget section.

DECISION PACKAGE	
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Is this request associated with a decision package you have submitted for FY 2015-16? If so, cite it here.

REQUESTED ACTION	Add
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Choose from: Add, Delete, Amend, or Codify.

OTHER AGENCIES AFFECTED	NONE
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Which other agencies would be affected by the recommended action? How?

SUMMARY	<p>25% of each payment made to the Retirement System Investment Commission's Investment Administrator will be retained by the Investment Commission.</p>
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Summarize the existing proviso. If requesting a new proviso, describe the current state of affairs without it.

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EXPLANATION	<p>To ensure the Investment Administrator performs satisfactorily.</p>
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Explain the need for your requested action. For deletion requests due to recent codification, please identify SC Code section where language now appears.

FISCAL IMPACT	<p>\$600,000 is the total minimum retainage to be held during the first two years (\$300,000 per year) of the contract period. Funds in the Investment Commission’s operating budget funds are considered “other funds.”</p> <p>Payment for services is made quarterly at a cost of \$300,000. \$75,000 of each quarter’s payment is retained by the Investment Commission. After a period of two years, the Investment Commission may remit the retained amounts to the vendor upon satisfactory performance. The Investment Commission may also continue to collect retained amounts after the first two years if the Commission deems it necessary.</p>
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Provide estimates of any fiscal impacts associated with this proviso, whether for state, federal, or other funds. Explain the method of calculation.

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Of the funds authorized to RSIC, up to 25% of the annual amount invoiced for its administrator system may be retained for the purpose of ensuring the performance of the administrator. The retained funds must be held by the agency until the verification of satisfactory performance. All undistributed funds in the Investment Commission's retainage account will be carried forward to the next Fiscal Year.

**PROPOSED
PROVISO TEXT**

Paste FY 2014-15 text above, then bold and underline insertions and strikethrough deletions. For new proviso requests, enter requested text above.