



THE HONORABLE CURTIS M. LOFTIS, JR.

State Treasurer

April 8, 2016

The. Honorable Joshua A. Putnam
Chair, Legislative Oversight Committee, Executive Subcommittee
P.O. Box 11867
Columbia, SC 29211

Dear Chairman Putnam,

I am in receipt of your letter of March 29, 2016, which requests the production on or before April 8, 2016 of certain documents relating to four different subject areas.

While we welcome the opportunity to work with the Legislative Oversight Committee to provide information helpful to its statutory mission, we are concerned about the focus and scope of this most recent request and its direction to a constitutional state officer. Certain of these requests inquire into areas which have been the subject of reviews by other legislative committees and we query whether the repetition of previous investigative efforts represents a good use of the time of this Subcommittee and the Treasurer's Office or of the taxpayer dollars which fund both.

Notwithstanding these concerns, we nonetheless provide these responses to the requests contained in your March 29th letter, together with binders containing responsive documents.

With respect to Requests 1-3 pertaining to South Carolina's credit rating, we agree that unfunded pension liabilities of approximately \$21.5 billion (more than 16 times the State's total general obligation debt) are a matter of significant concern. Consequently, we welcome the opportunity to work with the Committee to address this significant problem. However, Requests 2 and 3 ask for information which is not within the possession or control of the Treasurer's Office. S&P's proprietary rating process encompasses multiple financial categories in which the State is ranked on relative strengths and weaknesses. While S&P does not furnish any order of priority regarding issues of concern and the categories used in its ratings analysis, we are providing the Subcommittee with an excerpt from S&P's 2016 Rating Report for the State of South Carolina which discusses the effect of the State's unfunded pension liability on its credit rating. See Tab 1. This information was provided to the Treasurer's Office by S&P subject to certain confidentiality and non-disclosure restrictions. While we have been authorized by S&P to share this information with the Committee for its

use, we ask that you maintain the confidential and proprietary nature of this information by not making this S&P report excerpt publicly available.

With respect to Requests 4-5 pertaining to employees of the Treasurer's Office, we enclose documentation which provides substantive information responsive to these requests. *See* Tabs 2 & 3.

With respect to Request 6, we attach copies of all custody agreements from the time period covered by the request. *See* Tabs 4 & 5.

With respect to Requests 6-10 pertaining to the relationship between the Bank of New York Mellon (BNYM) and the Treasurer's Office, we note that these requests focus on issues litigated in a court action filed against BNYM in 2011. At the time that litigation was resolved by settlement in 2013, the settlement was reviewed and approved by the Attorney General, the State Treasurer, counsel for the State of South Carolina and by the presiding business court judge, the Hon. Clifton Newman. The Order approving the dismissal of the case contained the following judicial findings:

[T]his litigation has been hard-fought. During the over two year period it has been pending before this Court, the parties have filed and this Court has decided many motions, both procedural and substantive. In discovery, the parties have exchanged more than five million documents and taken over 35 depositions. . .

This Court has reviewed the Settlement and Mutual Release Agreement and queried counsel about the contents thereof. This Court is satisfied that all parties and Counsel are acting in good faith in the making of this settlement, that the signatories thereto have the full right and authority to enter into this settlement and to commit and to bind fully their respective parties, and that they reasonably believe and are correct that this Agreement and the payments and forward-looking credits, discounts and training it makes available to the State are, in fact, in the best interests of the parties and the citizens and retirees of South Carolina that benefit from this settlement.

(*See* Tab 6 at pp. 1-2.)

In 2014 and 2015, after the settlement was judicially approved and consummated, the Senate Finance Committee convened a Special Subcommittee to consider the BNYM litigation. For your convenient reference, we provide you with copies of the exhibits provided to that Senate Subcommittee by the Treasurer's Office. The exhibits include a securities lending chronology, the relevant securities lending agreements, litigation retention agreements relating to the litigation against BNYM, an analysis of the eventual settlement, and a copy of an affidavit given by former Treasurer Thomas Ravenel. (*See* Tabs 7-12).

In addition, we note that the 2014-15 Appropriation Act (Part 1B, § 105 F50.13) required the Public Employee Benefit Authority (PEBA) to prepare and submit to the Senate Finance Committee and House Ways and Means Committee a report on the settlement of the BNYM litigation. This report was prepared by an independent out-of-state law firm engaged by PEBA. We are advised that the cost of preparing this report was in excess of \$100,000, which was paid by PEBA using public funds. The Treasurer's Office is informed and believes that the attorneys engaged by PEBA were tasked with conducting a comprehensive and extensive review of all matters related to the litigation and its settlement. As part of its findings, the PEBA-commissioned report (a copy of which is also being provided to the Subcommittee) "[d]id not draw any conclusions regarding the likely outcome in the litigation had it been tried to conclusion," as the independent law firm concluded that "[i]t is simply impossible to predict how the State's claims would have fared at trial or what amount of damages would have been awarded had the State prevailed on any of its claims." (See Tab 13 at p. 16.)

We trust that this previously compiled information and the analyses and reports conducted by other judicial, legislative and independent private evaluators is a sufficient response to Requests 6-10. We note that assembling a completely original response to these requests as currently drafted would require extensive staff time and expense, as much of the litigation-related material remains in the hands of outside counsel and other entities outside the Treasurer's office and some of the requests seek information which must be reviewed to prevent disclosure of information potentially protected by attorney-client privilege or potentially subject to confidentiality provisions under the terms of the BNYM settlement agreement. Moreover, some of the requested information was not part of the litigation process and must be assembled, analyzed and developed. As is demonstrated by the responses to Requests 4-5, the Treasurer's office is leanly staffed without excess personnel time to dedicate to tasks beyond their core responsibilities. Consequently, compilation of such information cannot be performed on a tight schedule. Should the attached documents be deemed insufficient to meet the Subcommittee's request and should it insist on a full and original response to these requests, we estimate that the compilation of all responsive documents could not be prepared before September 15, 2016, would incur costs of at least \$50,000, and will require a special allocation to cover this expense.

With respect to Requests 11-12, pertaining to excessive fees paid by the Retirement System Investment Commission, the Treasurer's Office welcomes the opportunity to work with the Committee to address this significant problem. However, although the Treasurer is a statutory member of the RSIC, S.C. Code § 9-16-315(A)(2), documents relating to the fees incurred by RSIC are not within the control of the Treasurer. Detailed information concerning fees paid by the RSIC are in the care and custody of that entity, which we note is also the subject of review by the Legislative Oversight Committee. Furthermore, the production of a response to these requests would require examination of fee agreements for hundreds of managers dating back approximately ten years. Accordingly, the preparation of such a response would be extremely costly and time consuming.

However, the Legislative Audit Council recently released a December 2015 report commenting on investment fees incurred by RSIC as a result of its investment strategy. We are providing copies of this report and its executive summary. The Legislative Audit Council concluded that fees had increased from 0.1% of assets in 2005 to 1.6% of assets in 2014. (*See* Tab 14, Legislative Audit Council RSIC Report Summary at p. 6.) The Audit Council noted that although the RSIC reports the fee and expense ratio for its portfolio, it does not report ratios by investment category and it recommends that it be required to do so. (*See* Tab 15, Legislative Audit Council RSIC Report at 22 & 24). We concur in this recommendation.

We believe that this response and the extensive materials provided herewith materially answer the substance of the inquiries posed by the Subcommittee in your March 29th letter. We look forward to meeting with the Subcommittee on April 14, 2016 and will be prepared at that time to address those matters that have been noticed in the published agenda.

Sincerely,

Signature Redacted

Clarissa T. Adams
Chief of Staff
SC State Treasurer

CTA/lmd

cc: The Honorable Laurie Slade Funderburk
The Honorable Wm. Weston J. Newton
The Honorable Robert Q. Williams
Committee staff