



THE HONORABLE CURTIS M. LOFTIS, JR.

State Treasurer

March 23, 2015

The Honorable Thomas Alexander
Gressette Building
Columbia, South Carolina 29201

Re: Senate Bill 527

Dear Senator Alexander:

I have reviewed the proposed legislation referenced above and wanted to follow up on my previous letter dated March 12, 2015 addressed to Senators Lourie and Bryant. That letter is attached for your convenience. In addition to the reasons cited therein as to why the current custodial framework of checks and balances should not be disturbed, I want to elaborate on the history and successes of the present system, as well as the reasoning and risks that could accompany the proposed changes.

First, the statutory reforms instituted by the General Assembly in 2012 have worked well, and the retirees and citizens of this State have greatly benefited from the changes. Those recent changes should be given ample opportunity to serve their intended purposes. Secondly, I have been a passionate watchdog since taking office and those enhanced oversight and transparency initiatives were not well-received by an establishment that preferred working behind closed doors. Despite some bumps in the road, it is clear my actions as statutory custodian have helped pave the way for a safer, more transparent investment approach that incorporates a tested system of checks and balances. The Office of State Treasurer, serving as the statutory custodian, has served the State well as a needed "check and balance" for over 70 years, and the following accolades and accomplishments evidence that the last four year of intense scrutiny of the system has enabled it to grow into one that more safely and efficiently manages the trust funds of South Carolina. As examples of recent changes:

- The SC Retirement System's reporting of investment management fees and related expenses was recently recognized as "the most transparent in the Nation;"
- The State's efforts with respect to financial reporting and disclosure, particularly the detailed disclosures regarding State pension trust funds and the ever-present issues surrounding the possible under-reporting of unfunded liabilities, have been applauded;
- The State's relationship with the credit rating agencies is outstanding, and my Office's steadfast commitment to transparency in all of the State's financial dealings is one of the

- pillars of trust upon which our stellar AAA Credit Rating is based (that pillar should not be eroded);
- The spirited and energized relationship between my Office and the RSIC has led to additional reforms at the administrative and corporate governance levels of RSIC.
 - Enhanced due diligence of investments;
 - Enhanced investment certification from RSIC corporate officers that includes specified responsibility and accountability;
 - The hiring of internal auditors, compliance officers, reporting and risk officers, and the creation of “Enterprise Risk Management Systems” and protocols (including the hiring of a dedicated “Enterprise Risk Management Systems Officer”);
 - The increased flow of information and disclosures between the agencies, the custodial bank and the public;
 - Improved sourcing, vetting, and approval processes for potential new investments; and
 - Written policies on conflicts of interest, third party placement agents, cash management, etc.

The positive accomplishments listed above are a result of RISC, the State Treasurer’ Office and the Legislature working together to build a better pension system. I respectfully urge you to consider the present system of checks and balances and see that the System is now well positioned to protect the State, its citizens and its deserving retirees from material instances of fraud, waste or abuse. RSIC, the State Treasurer, and PEBA each have a separate and distinct role in the system, and as such, each of these three entities has reciprocal fiduciary responsibilities to each other – in addition to their duties to the beneficiaries – thereby *reducing the likelihood* of fraud and error. Eliminating any one of these checks and balances and consolidating such authority or responsibility into one of the remaining entities is dangerous and creates an environment ripe for fraud and error.

It would be unwise to endorse such action.¹

Sincerely,



Curtis M. Loftis, Jr.
State Treasurer

1. In the constantly evolving global financial markets and their increasingly exotic investment vehicles (e.g. hedge funds, asset-backed securities, derivatives, etc.), is it ever prudent to eliminate a proven check and balance? Could additional oversight or the further segregation of duties have averted or prevented the multibillion dollar frauds committed against innocent shareholders, beneficiaries, and investors by, among others, Bernie Madoff, Enron, Lehman Brothers, HealthSouth, and WorldCom? More relevant to the situation at hand, could the pension scandals of California and New York been avoided with additional separation of duties and at least one more level of oversight?