

Rhode Island State Investment Commission

Governance Review

Final Report Presentation

November 21, 2022



Agenda

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- Overview
- Findings and Recommendations
- Potential New SIC Charter
- Potential New Policies
- Recommendations
- Implementation Timing
- Implementation Priorities
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Overview

- Funston Advisory Services LLC (FAS) was engaged by the State Investment Commission in March 2022 to conduct a governance review.
- We were asked to:
 - Conduct an independent review of the Rhode Island State Investment Commission’s (SIC) investment governance, policies, and operations;
 - Evaluate SIC’s current governance policies and practices compared to peer/industry best practices; and
 - Identify opportunities for improvement.
- The governance review activities included:
 - Review of SIC’s governing statutes, policies, charters and governance practices;
 - Development of an InGov[®] peer benchmarking profile
 - Governance Effectiveness self-assessment survey completed by the Commissioners
 - Individual interviews with each Commissioner
 - Development of a final report with findings, conclusions, and recommendations and an implementation roadmap

Findings and Recommendations

- Finding: The SIC has been functioning well and has effective processes; however, many policies are not documented or are difficult to locate.
- Recommendations:
 - Adopt a Commission Charter that clearly defines the responsibilities and duties of the commission and policies that articulate the powers reserved for the commission and delegations to staff or third parties.
 - Develop and adopt a Governance Policy Manual that would include all relevant governing statutes, charters and policies of the SIC in one place.
 - Consider formalizing and adopting additional elements for inclusion in the investment policy statement.
 - Update the ESG policy to reflect the current practice of considering social and environmental considerations.
 - Consider adopting new policies in several areas.

Potential New SIC Charter

- A charter for the SIC would help clarify the responsibilities and duties of the SIC, the powers that are reserved for the SIC, and the delegations to the CIO and third parties.
- Potential SIC charter content could include:
 - Introduction and purpose
 - Duties and responsibilities
 - Commissioners
 - Governance and authorities
 - Commission officers
 - Conflicts of interest
 - Investments and funding
 - Risk management
 - Delegations to staff
 - Third-party advisors
 - Monitoring and reporting
 - Commission meetings
 - Charter review

Potential New Policies

Based upon peer practices, we recommend consideration of new or revised policies, as shown below, for inclusion in the Governance Policy Manual.

New/Revised Governance Policies (Many are currently in the Code of Ethics)

- Commission ethics and standards of conduct, including a compliance self-monitoring process
- Campaign contributions
- Conflicts of interest
- Confidentiality
- Commissioner orientation and continuing education
- Expense reimbursement
- Gifts and loans
- Indemnification and insurance
- External communications by Commission members
- Contacts with Commissioners during an RFP process
- Whistleblower/complaint handling and reporting
- Commission self-assessment
- Procurement

New Investment Policies

- Investment risk philosophy and policy
- Selection and termination process for external managers and advisors
- Due diligence standards
- Co-investment policy
- Securities litigation
- Personal trading
- Leverage policy

New Operational Policies

- Frequency of review of investment policies in the investment policy statement (e.g., annually, biennially)
- Process for providing annual feedback to the third-party advisors
- Frequency for a periodic review of administrative rules
- Communications policy
- Business continuity
- Risk management
- Vendor relationships
- Compliance
- IT governance

Recommendations

- The report included 28 additional recommendations for the SIC across eleven areas, including, by topic:
- **Commission Operations:**
 - Create a formal Vice Chair position to ensure there is a Commissioner designated to act in the place of the Chair in instances when the Chair is not available.
 - Develop a multi-year strategic policy agenda.
 - Improve oversight of the non-DB plan programs, i.e., OPEB Trust, Defined Contribution Plan, Deferred Compensation Plan, 529 Plan, including collaboration with the ERSRI Board regarding hiring of service providers and any changes to the plans.
 - Improve oversight of governance, audit and financial statements, and external evaluations.
 - Enable easier and user-friendly access to commission materials through an electronic portal with a repository (e.g., with SharePoint).
 - Consider an annual SIC retreat for more in-depth discussions.
 - Consider if a periodic, e.g., biennial, joint meeting or workshop with the ERSRI Board of Trustees would be beneficial to enhance consistency of asset-liability planning.

Recommendations (Continued)

- **Commission Development:**

- Conduct periodic Commission self-assessments that includes identification of continuing education priorities.
- Develop an onboarding program for newly-appointed Commissioners, including incoming State Treasurers, which includes governing statutes and Commission policies.
- Develop a structured Commissioner continuing education program with more frequent core education.
- Include actuarial and asset-liability management topics in Commissioner continuing education topics, including presentations by the ERSRI actuary.

- **Delegations:**

- Consider increasing delegations to staff for investment decision-making, with appropriate governance safeguards and controls in place, with the potential long-term objective of delegation of manager selection; short-term actions could include, for example:
 - Re-hiring of existing managers or general partners (“re-ups”); and
 - Portfolio allocations within the approved asset allocation.

Recommendations (Continued)

- **Commission/Chief Investment Officer Relationship:**
 - The SIC should provide input to the annual evaluation process for the Chief Investment Officer.
 - Ensure a succession plan exists for the Chief Investment Officer.
 - Review the results of exit interviews to identify ways to improve retention.
- **Use of Third-Party Service Providers:**
 - Consider engaging an independent third-party firm (e.g., CEM Benchmarking) to benchmark investment costs.
- **Strategic Planning:**
 - Direct staff to review the Treasury strategic plan with the SIC and obtain input from the SIC.
- **Investment Operations:**
 - Consider if operational due diligence with public market investments should be conducted.
 - Consider instituting a securities lending program.

Recommendations (Continued)

- **Human Resources:**
 - Develop a plan, with the Treasurer, to assist with staff transitions:
 - A staff development and succession plan; and
 - New employee orientation process.
 - The Treasurer’s Office should conduct periodic staff compensation benchmarking.
- **Risk:**
 - The Commission should articulate its risk appetite and risk tolerance.
 - Develop a process for monitoring vendor relationships for performance, risk, and compliance.
- **Independent Reassurance:**
 - With Treasury, consider how to best obtain internal audit services, either internal or outsourced, and develop an SIC charter for internal audit.

Recommendations (Continued)

- **Compliance:**

- The SIC should oversee compliance activities, with non-compliance incidents escalated to the Commission.
- The SIC / Treasury should have a compliance/ethics/fraud hotline that can be used by employees to report suspected compliance, regulatory, or ethical violations.
- Investment transactions and holdings compliance testing should occur at least monthly, if not daily.
- The SIC should consider if a document management system (DMS) to manage private market documentation would be beneficial.

Implementation Timing

- This review has over 30 recommendations and the SIC has limited resources to address implementation, so we have worked with staff to develop priorities and an implementation roadmap.
- Over the next six months, we propose the SIC implements the following three recommendations:
 - Develop and adopt a Commission charter;
 - Create a formal Vice Chair position; and
 - Review the results of exit interviews to identify ways to improve retention.
- We have prioritized an additional 24 recommendations for completion within a year.
- Six recommendations are likely to require more than a year to implement.

Implementation Priorities

- Eleven recommendations have been identified as highest priority:
 - Develop and adopt a Commission charter;
 - Develop and adopt a Governance Policy Manual;
 - Consider new investment policies for the investment Policy Manual;
 - Develop a multi-year strategic policy agenda;
 - Improve oversight of the non-DB plan programs;
 - Improve oversight of governance, audit and financial statements, and external evaluations;
 - Conduct periodic Commission self-assessments that includes identification of continuing education priorities;
 - Consider increasing delegations to staff for investment decision-making;
 - The Commission should articulate its risk appetite and risk tolerance;
 - With Treasury, consider how to best obtain internal audit services, either internal or outsourced, and develop an SIC charter for internal audit; and
 - Oversee compliance activities, with non-compliance incidents escalated to the Commission.

Next Steps

- SIC approval for staff to proceed to work on implementing the recommendations, with each individual item subject to SIC approval, as appropriate.
- Finalize and approve the new SIC charter.
- Create a formal Vice Chair position.
- Review the results of exit interviews to identify ways to improve retention.
- Begin work on the other recommendations, as appropriate.