

**WASHINGTON STATE INVESTMENT BOARD**  
**Audit Committee Meeting Minutes**  
**December 6, 2011**

The Audit Committee met in open public session at the Washington State Investment Board (WSIB) boardroom at 2100 Evergreen Park Drive SW, Olympia, Washington.

Committee Members Present:      George Masten, Acting Chair  
                                         Steve Hill, Chair (via teleconference)  
                                         Senator Lisa Brown  
                                         Bill Longbrake  
                                         Treasurer Jim McIntire (via teleconference)  
                                         Bob Nakahara (via teleconference)  
                                         Natasha Pranger

Others Present:                      Theresa Whitmarsh, Executive Director  
                                         Shawna Killman, Audit Director  
                                         Kris Logan, Investment Accounting Controller  
                                         Rodney Reynolds, Internal Auditor  
                                         Kate Sandboe, Corporate Governance Officer  
                                         Patty Davis, Administrative Assistant  
                                         Steve Dietrich, Assistant Attorney General  
                                         Ray Holmdahl, Peterson Sullivan  
                                         Bob McCormick, Glass Lewis  
                                         Mark Raker, Peterson Sullivan

[Names of other individuals attending the meeting are listed in the permanent record.]

Acting Chair Masten called the meeting to order at 9:02 a.m. and took roll call.

**ADOPTION OF THE SEPTEMBER 7, 2011, MINUTES**

**Ms. Pranger moved to approve the September 7, 2011, Audit Committee meeting minutes. Senator Brown seconded the motion, and the motion carried unanimously.**

**MANAGEMENT**

**2011 Year-End Proxy Voting Report**

Ms. Sandboe presented the 2011 Year-End Proxy Voting Report. For the first 10 months of the year, the WSIB voted almost 3,000 proxy ballots, covering more than 27,000 individual proxy issues. By far the greatest number of votes cast was in director elections, followed by ratification of auditor, and advisory vote on executive compensation, or “say-on-pay and “say-when-on-pay,” new requirements under the Dodd-Frank Wall Street Reform and Consumer Protection Act.

In 2012, the WSIB’s proxy voting priorities will be controlling executive compensation, the election of directors by majority vote, shareholder proposals on political contributions and reporting, and annual election of directors.

Mr. McCormick, Glass Lewis, presented strategy for 2012 proxy voting and background information on the previous proxy voting issues.

Mr. Longbrake inquired if the WSIB's voting had a noticeable impact on companies and their practices. Ms. Sandboe stated that it will have an impact because when companies file their proxy materials with the Securities and Exchange Commission in 2012, they will be required to address the results of their say-on-pay vote.

[Treasurer McIntire arrived at 9:06 a.m. via teleconference]

Treasurer McIntire stated that the votes are advisory and companies can choose to ignore them. He inquired to what degree did companies disregard the proxy votes and if there were consequences. Mr. McCormick stated that there could be shareholder lawsuits and a possible shareholder vote against company directors the following year.

Regarding the WSIB's non-U.S. proxies, staff reminded committee members of the research and discussions earlier this year before the Committee agreed to have our global equity fund managers vote the proxies according to their voting guidelines, but with additional oversight by WSIB staff. As part of that review, staff sent fund managers a list of the WSIB's 10 largest international holdings and asked them to report how they voted at those meetings. Of the five managers who held shares to vote for the WSIB, staff found the biggest contrast in how the WSIB would have voted compared to how our fund managers voted was in the election of directors.

Staff said concerns about those voting differences are outweighed by the amount of engagement fund managers do with company management regarding governance issues. Mr. Longbrake inquired if the engagements they have with management make any difference in the long run. Ms. Sandboe will continue tracking the issue and results.

Mr. Masten inquired whether Dodd-Frank has enforcement authority. Mr. McCormick stated that there was no provision for that, but the shareholders could apply pressure to companies to comply. Mr. Longbrake inquired who finances the shareholder lawsuits. Mr. McCormick indicated that law firms usually take those cases on a contingency basis, with the hope that the company pays the fee. Mr. Longbrake asked if more lawsuits should be expected, and Mr. McCormick stated yes.

Senator Brown stated she appreciates the work WSIB is doing with regard to proxy voting. She noted that improvements in companies' governance practices occur very slowly, and that the pace of changes can often be quite frustrating.

### **Investment Referrals Quarterly Report**

Ms. Whitmarsh offered the information for the members' reference. There are no new referrals to report. Ms. Whitmarsh indicated the process is working well and provides transparency for the WSIB.

### **Revisions to Conflict of Interest Policy 2.00.100**

Mr. Dietrich presented three proposed revisions to the Conflict of Interest Policy, 2.00.100. He explained that the changes were proposed to address several recurring issues that have arisen over the past couple of years. The proposed changes to Policy 2.00.100 would:

1. Explicitly authorize the approval authority to issue written investment approvals that cover a specified category of "other investments";
2. Explicitly authorize a Board member or employee to delegate the submission of investment approval requests or required investment reporting to another person; and

3. Clarifies that any former Board member or Executive Director who held his or her position in the preceding calendar year is required to file PDC Form F-1 or F-1a.

Mr. Hill inquired whether the financial reporting obligation applied only to the Board. Mr. Dietrich stated that the reporting requirements are in statute and apply to all state officers.

**Ms. Pranger moved that the Audit Committee recommend the Board approve the revised Conflict of Interest Policy 2.00.100. Senator Brown seconded the motion, and the motion carried unanimously.**

## **INTERNAL AUDIT**

### **Internal Audit Report 2012-03 - Disbursements**

Mr. Reynolds informed the members that Internal Audit has completed the review of the Board's disbursements as outlined in the *Fiscal Year 2011-2012 Internal Audit Plan*. The objectives were to determine whether:

1. The WSIB is complying with requirements related to disbursements, including procurement, processing and payment;
2. Control procedures are in place and operating to assist with ensuring compliance and safeguarding state assets; and
3. Controls limit personnel to only the electronic access necessary to perform their assigned job duties.

This report does not contain any audit recommendations. Ms. Pranger inquired about the total number of transactions. Mr. Reynolds will provide Ms. Pranger the information.

### **Audit Recommendations Status Report**

Ms. Killman presented the quarterly Audit Recommendations Status Report. Of the five outstanding items, three were resolved since the last report to the Committee in September. The Real Estate Investment File Organization update was completed, and two recommendations related to the improvement of controls around contract monitoring were implemented. The two remaining audit recommendations will be followed up on by Internal Audit over the next quarter, and status reported back to the Committee in March.

## **EXTERNAL AUDIT**

### **Fiscal Year 2011 Independent Auditors' Report**

Ms. Logan introduced Mr. Raker and Mr. Holmdahl from Peterson Sullivan. Mr. Holmdahl reviewed the required communications and presented the Fiscal Year 2011 Independent Auditors' Report. Peterson Sullivan provided opinions on each of the six separate financial reports. No audit adjustments to the financial statements were made. No disagreements in processes were identified. Peterson Sullivan reconfirmed their independence to the WSIB.

Mr. Nakahara inquired if there were any improvements to be made by the WSIB. Mr. Raker stated that he did not see any need for changes to the WSIB's procedures. Mr. Nakahara inquired if they expected any new pronouncements and if so, would they require additional resources.

Mr. Holmdahl stated that there were none that would affect the WSIB. Mr. Longbrake inquired if there had been any non-material past adjustments, and Mr. Holmdahl stated there had not been any adjustments. Mr. Longbrake inquired if the valuation procedures used by the Board's alternative asset managers were considered reasonable and prudent, and Mr. Holmdahl responded yes; he is

confident that the standards are being met. Ms. Logan advised the members that a valuation RFP has been issued. Beginning January, 2012, a consultant will evaluate the WSIB's entire valuation process over the alternative assets.

#### **CONFLICT OF INTEREST POLICY COMPLIANCE REVIEW**

Mr. Raker, Peterson Sullivan, presented the results of the 2010 Conflict of Interest Policy Compliance Review. In the areas of gift reporting, travel paid by outside sources, personal investments, and training, there were no findings. In the area of filing the required Statement of Financial Affairs forms, Mr. Raker noted one employee filed late. Mr. Longbrake remarked that the report indicated there were four late filers, and Mr. Raker clarified that the initial report provided is in the process of being updated as new information became available, and would be reflected in the revised report.

There was no further business to come before the Committee and the meeting adjourned at 10:22 a.m.