

WASHINGTON STATE INVESTMENT BOARD
Audit Committee Meeting Minutes
May 24, 2012

The Audit Committee met in open public session at 9:03 a.m. at the Washington State Investment Board (WSIB) boardroom at 2100 Evergreen Park Drive SW, Olympia, Washington.

Committee Members Present: Steve Hill, Chair
Bill Longbrake (via teleconference)
George Masten
Bob Nakahara
Natasha Pranger (via teleconference)

Committee Members Absent: Senator Lisa Brown
Treasurer Jim McIntire

Others Present: Theresa Whitmarsh, Executive Director
Victor Moore, Chief Operating Officer
Gary Bruebaker, Chief Investment Officer
Shawna Killman, Audit Director
Rodney Reynolds, Internal Auditor
Patty Davis, Administrative Assistant

Steve Dietrich, Assistant Attorney General
Nolan Garrett, Intrinium Networks
Gary Blosser, Intrinium Networks
Mark Raker, Peterson Sullivan

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

Chair Hill called the meeting to order at 9:03 AM and took roll call.

APPROVAL OF THE MARCH 6, 2012, MINUTES

Mr. Masten moved to approve the March 6, 2012, Audit Committee meeting minutes. Ms. Pranger seconded the motion, and the motion carried unanimously.

EXTERNAL AUDIT – EXECUTIVE SESSION
IT Security Review and Compliance Audit

Chair Hill stated that the Committee would now go into executive session to consider financial and commercial information related to the investment of public trust or retirement funds because public knowledge regarding the discussion would result in loss to such funds or in private loss to the providers of this information. He said the executive session was expected to last until about 9:25 at which time the Committee will reconvene in open session.

[The Committee went into executive session at 9:05 a.m., and reconvened in open session at 9:25 a.m.]

Mr. Masten moved that the Audit Committee recommend the Board approve the IT Security Review and Compliance Audit. Ms. Pranger seconded the motion, and the motion carried unanimously.

EXTERNAL AUDIT

Financial Statement Auditor Independence Review

Ms. Killman noted the financial statements for all funds under WSIB management are audited annually by Peterson Sullivan LLP, an independent CPA firm. The upcoming Fiscal Year 2012 audit will be the Board's fourth audit under a five-year contract.

The Audit Committee Charter Policy 1.00.130 requires the Committee to review the independence of the external auditors by:

1. Obtaining statements from the auditors on relationships between the auditors and the WSIB;
2. Obtaining a listing of all services provided by the external audit firm from staff; and
3. Discussing the relationships with the auditors.

A letter from Peterson Sullivan regarding their independence from the WSIB, as well as a list of all services provided by Peterson Sullivan to the WSIB for the period from May 1, 2011, through April 9, 2012, were reviewed by the Committee.

Mr. Masten inquired if Peterson Sullivan performs audits for other state agencies. Mr. Raker confirmed they do audits for a few other Washington state agencies.

Mr. Nakahara inquired as to what type of relationship would infringe on Peterson Sullivan's independence and impede their ability to perform an audit.

Mr. Raker indicated that if there were any relatives of Peterson Sullivan among the Board members or staff, it would prohibit them from conducting an audit, or Peterson Sullivan performing day-to-day accounting functions, or making management decisions would also preclude them from confirming their independence from the Board.

Mr. Nakahara also inquired about potential conflicts with auditing WSIB partners. Mr. Raker indicated they would take a thoughtful look at the situation, and decline to participate if it could be viewed as a potential conflict

Mr. Masten inquired if all their contracts with state agencies were achieved through a competitive process. Mr. Raker confirmed that they were.

2011 Conflict of Interest Policy Compliance Review – Scope of Services and Auditor Appointment

In accordance with the Conflict of Interest Policy 2.00.100, Ms. Killman indicated the Board plans to have an annual Conflict of Interest Policy Compliance Review for calendar year 2011 performed by an external audit service provider.

The Board has a contract in place with Peterson Sullivan LLP that allows for non-audit services to be provided by the Contractor via a separate project work order. The proposed statement of work for the project work order was presented and has been reviewed by Peterson Sullivan. The proposed fee for this review is \$6,000, and represents a decrease from last year.

Mr. Masten moved that the Audit Committee recommend the Board appoint Peterson Sullivan LLP to perform the calendar year 2011 Conflict of Interest Policy Compliance Review. Ms. Pranger seconded, and the motion carried unanimously.

INTERNAL AUDIT

Audit Recommendation Status Report

Ms. Killman presented the Audit Recommendation Status Report. Audit Committee Charter Policy 1.00.130 requires the Committee to review the responsiveness and timeliness of staff's follow-up activities related to prior audit recommendations. Ms. Killman reported that since the last quarterly report in March, staff resolved four of the five prior audit recommendations in the Real Estate and Tangible Assets areas. Internal Audit will review status of the remaining recommendation regarding travel expenses paid by outside sources directly to travel vendors, and report status to the Committee next quarter.

Mr. Longbrake commended staff on a job well done.

Fiscal Year 2013 Internal Audit Plan

Mr. Reynolds and Ms. Killman presented the Fiscal Year 2013 Internal Audit Plan. Project selections were made using a rigorous risk assessment process, as the Washington State Investment Board (WSIB) does not have the resources to audit all significant areas every year. From this process, the following eight audit areas were selected, and are in prioritized order:

1. Trade Processing, Confirmation, and Settlement
2. Public Equity Investments
3. Private Equity/Real Estate Back-Office Consultant
4. Budget Development and Management and Revenue Transfers In
5. Human Resources Management
6. Stock Distribution Manager
7. IT Security Follow-up - Outsourced
8. Computer Assisted Audit Techniques (CAATs)

Chair Hill requested an example of how Internal Audit will apply CAATs. Ms. Killman gave an example where WSIB vendor addresses are compared with WSIB employee addresses using computer programs developed by the State Auditor's Office. If any matches were found, Internal Audit would follow-up to ensure the vendor is a valid and independent from the WSIB.

Discussion ensued around the Internal Audit performance measure of completing 80 percent of planned audits. Chair Hill and Mr. Nakahara questioned whether it should instead be a goal of 100 percent, and if a situation arises that requires a reevaluation of audit items, they be brought to the Audit Committee for adjustment to the Audit Plan. Mr. Longbrake and Ms. Pranger feel the performance measure is appropriate. Mr. Longbrake suggested that if the 100 percent goal is not met, the Committee should ask if there are sufficient resources to achieve the goal. Ms. Killman stressed that the goal is always 100 percent completion. However, more urgent issues can arise that requires less critical audit items to be rescheduled to a later date. That then becomes part of the risk assessment for the next year. Mr. Masten felt the plan should be based on staff resources, and plan to achieve 100 percent. He agreed that the plan should be ambitious.

Members requested a quarterly update on status of the Audit Plan. Ms. Whitmarsh indicated management would add it as a standing agenda item so the Committee will receive a quarterly status report. Mr. Longbrake stressed that the review should look at the three and five-year cycle as well as the immediate timeline, and Ms. Pranger concurred.

Chair Hill reassured Internal Audit that the Committee believes they are hardworking and conscientious. His concern is regarding the appearance of not meeting 100 percent of the audit goals.

Mr. Longbrake inquired if there was any pressure from management to set the risk ratings. Ms. Killman assured him that the ratings were made in a collaborative method, and there was no undue pressure from management.

Mr. Longbrake also expressed his disappointment in the level of participation in the employee survey. He encouraged management to continue their efforts to increase participation by setting expectations for staff.

Mr. Longbrake expressed concern about the lower risk audit areas in the audit cycle plan that would be reviewed as time permits. Ms. Killman indicated that they expect the CAATs audits will aid them in providing more coverage.

Mr. Masten moved that the Audit Committee recommend the Board adopt the Fiscal Year 2013 Internal Audit Plan. Ms. Pranger seconded the motion, and the motion carried unanimously.

MANAGEMENT

Investment Referrals Quarterly Report

Ms. Whitmarsh offered the information for the members' reference. There were four new referrals, two of which were deemed unsuitable for the WSIB's investment strategy. The remaining two continue to be evaluated by the investment team. Ms. Whitmarsh indicated the referral process is working well and provides transparency for the WSIB.

There was no further business to come before the Committee and the meeting adjourned at 10:05 a.m.