STATE OF DELAWARE
STATE BOARD OF PENSION TRUSTEES
AND
OFFICE OF PENSIONS
MCARDLE BUILDING
860 SILVER LAKE BLVD., SUITE 1
DOVER, DE 19904-2402

When Calling Long Distance
Toll Free Number 1-800-722-7300
E-mail: pensionoffice@state.de.us

Telephone (302) 739-4208
FAX # (302) 739-6129
www.delawarepensions.com

BOARD OF PENSION TRUSTEES
AUDIT COMMITTEE
PUBLIC MEETING MINUTES OF OCTOBER 18, 2013

Audit Committee Members Present
Helen R. Foster, Chair
Stephen Ritchie
Araya Debessay
Mark Finfrock
Robert L. Paretta
James Burke

Office of Pensions
David Craik
Wade Sallings
Jeffrey Hoover
Kathy Kunkle

Audit Committee Members Not Present
None

Ashford Consulting Group
Garry Musto
Sara Williams

KPMG
Joe Seibert
Arthur Ayres

Delaware Department of Justice
Ann Marie Johnson, DAG
Lisa Loikith, Pension Office Paralegal

1. OPENING COMMENTS

   The meeting of the Audit Committee of the Board of Pension Trustees was called to order by Helen R. Foster, Chair at 9:30 a.m.

2. APPROVAL OF THE MINUTES

   The Audit Committee reviewed the public minutes of the April 29, 2013 meeting.

MOTION made by M. Finfrock and seconded by S. Ritchie to approve the public minutes of the Audit Committee Meeting from April 29, 2013.

MOTION ADOPTED UNANIMOUSLY

The Audit Committee reviewed the executive minutes of the April 29, 2013 meeting.

MOTION made by A. Debessay and seconded by R. Paretta to approve the executive minutes of the Audit Committee Meeting from April 29, 2013.

MOTION ADOPTED UNANIMOUSLY

3. PENDING ITEMS (OLD BUSINESS)

No items to report.

4. KPMG'S PRESENTATION AND DISCUSSION OF FISCAL YEAR 2013 AUDITS

J. Seibert presented the 2013 audit results. KPMG completed the First State Independence Fund I, LLC (FSIF) audit for the year ending December 31, 2012. KPMG issued an unqualified opinion on October 16, 2013.

KPMG anticipates issuing an unqualified opinion on the Delaware Public Employees' Retirement System's (DPERS) financial statements pending receipt of legal confirmations, review of the Engagement by the Quality Control Review Partner, final review of the DPERS' Comprehensive Annual Financial Report (CAFR) and the signed Management Representation letter.

To maintain effective internal control over financial reporting, KPMG is required to report material weaknesses. No significant deficiencies were identified. There were special representations with reference to the wind-down of FSIF, but this is not unusual. J. Seibert indicated that a separate opinion is not required for internal controls (as would be needed for a SEC report), although they are reviewed for consistency.

M. Finfrock asked whether KPMG's review of internal controls is required to be as robust as for a public company. J. Seibert indicated that the same extensive review is not required. For DPERS, they need to have an understanding of internal controls and they may selectively conduct control tests in some areas, for example, disbursements, to insure internal controls are generally understood and working effectively. KPMG is looking for a balance between control risk and substantive procedures risk.

A. Debessay asked if auditors are not expressing an opinion on internal controls, how can we be confident that they are correct? J. Seibert responded that his work papers provide a record of his evaluation.

D. Craik asked KPMG about the State Auditor's role in the audit. Mr. Seibert replied that the State Auditor's are responsible for preparing the Request for Proposal and the Contract for the DPERS audit. The State Auditor's office selectively tests different departments within the state. Mr. Seibert was not sure the last time that the Auditor's Office reviewed the special procedures for the Pension Office. A governance suggestion was offered for management to give an overview at each committee meeting to give the committee some level of comfort regarding checks and balances and operational concerns.

With regard to the valuation of assets, Mr. Seibert explained that for critical accounting investments the numbers are reported using the Net Asset Value (NAV) which is a practical expedient for fair value. The NAV is appropriate for funds that are not intended to be traded or liquidated in a short period of time. KPMG has reviewed the processes and has determined that they are sufficient. The investment advisor (Ashford) has a robust process in place for evaluating NAVs .

KPMG reports there have been no changes to DPERS' Significant Accounting Policies. The Quality of Accounting Policies has been found to be high.

The two core issues of actuarial valuation are 1) that the calculated census information given to the actuary is materially accurate and 2) KPMG internal actuaries review the results to be certain that the actuarial valuation makes sense. Key assumptions such as an interest rate of 7.5% are based off of a 2011 experience study done with a long term view. The interest rate and expected return rate are the same as the discount rate.

The Northern Trust Company's (NT) price testing should be synchronized with what KPMG expects. Small variations and tolerances will be accepted. KPMG will obtain a Service Organization Controls Report (SOC-1) of NT's internal controls.

KPMG reports there have been no noted disagreements with management, consultants, with other accountants, or litigation, claims, and assessments.

MOTION made by M. Finfrock and seconded by R. Paretta to move into Executive Session for the purpose of discussing confidential financial information, sensitive commercial information, and proprietary business information.

MOTION ADOPTED UNANIMOUSLY

MOTION made by R. Paretta and seconded by S. Ritchie to exit Executive Session.

MOTION ADOPTED UNANIMOUSLY

Mr. Seibert discussed the new GASB statements. GASB Statement No. 67 is effective June 30, 2014.

M. Finfrock asked who certifies on behalf of DPERs that the rate of return is adequate? Mr. Seibert responded it is the DPERs management's responsibility, after consultation with the Actuary and the Auditor.

A. Debessay asked what system is in place for Management to get notice of new standards. D. Craik and W. Sallings responded Management is aware due to webinars, conference calls, and GASB distributing information.

Mr. Seibert stated that the rate of return disclosure required under the new GASB standards will likely lower the rate of return reported with this calculation and a methodology will have to be used to compare across the board.

M. Finfrock asked if there is a need to go back and restate prior returns. Mr. Seibert responded it should be forward-looking for the most part but he will go back and look.

Each individual employer will be required to disclose their pro rata data. GASB suggests you use the projected future allocations of the plan, depending on the mix of employers.

A. Debessay expressed concern as to whether individual plans were reasonably funded. He stated they were normally 90% funded and inquired if any were 100% funded. D. Craik responded DPERS did have a plan over 100% funded. J. Burke stated some of the individual plans are 60% funded and asked if they need to be calculated. J. Siebert responded yes, the Closed State Police Plan is a pay-as-you-go plan.

Mr. Seibert discussed GASB Statement No. 68 where the information begins on 6/30/2014 and the information ends on 6/30/2015. The State has no pension liability on the books. Deferred inflows and outflows take into account the difference in actuarial assumptions versus what actually happened. GASB moved closer to a corporate world. There have been significant changes with how employers are dealing with this but not significant changes in statements.

Mr. Seibert indicated that the audit will be finalized in the next one or two weeks, and would be presented to the full Board.

5. FORTY-SECOND COMPREHENSIVE ANNUAL FINANCIAL REPORT (CAFR)

Mr. Seibert discussed the CAFR's financial statements. The Plan net position, employer and member contributions, net investment earnings, and pension benefits paid to retirees and beneficiaries all increased.

A. Debessay inquired on the difference between the New State Police Plan and the Closed State Police Plan. D. Craik explained the New State Police Plan is a new tier of police officers hired after January 1980.

Mr. Seibert remarked that Delaware does such a great job of reaching 100% of the annual required contribution every year.

6. FY13 CAFR KNOWN CHANGES FOR VERSION 3

W. Sallings discussed the changes.

7. PROPOSED FUTURE AUDIT COMMITTEE DATES

The audit entrance date is tentatively April 18, 2014 and the audit exit date is suggested for October 17, 2014.

8. DEPUTY ATTORNEY GENERAL REPORT

Deputy Attorney General Johnson had nothing to report.

9. NEW BUSINESS

W. Sallings asked KPMG if they want to review FSIF as the fund has wound down since June 30, 2013. Mr. Seibert replied this is up to the Audit Committee. The review is more analytical and KPMG did look at the subsequent receivables. There are two side pockets left.

W. Sallings asked would it make sense to test GASB Statement No. 68 to have the process in place before the effective date. D. Craik responded that DPERS will provide the actuary with employer ID numbers so they will have the necessary information. J. Burke asked if DPERS has notified the municipalities of the GASB 68 changes. D. Craik replied that if the municipality has a finance director, they will be aware of the changes.

At 11:25 a.m. there being no further business, MOTION was made by A. Debessay and seconded by R. Paretta to adjourn the meeting.

MOTION ADOPTED UNANIMOUSLY

Respectfully submitted,

Helen R. Foster, Chair
BOPT Audit Committee

cc: Audit Committee Members
Suzanne Grant
David Craik
Wade Sallings
Ann Marie Johnson