



JANET COWELL  
TREASURER

NORTH CAROLINA  
**DEPARTMENT OF STATE TREASURER**  
INVESTMENT MANAGEMENT DIVISION

KEVIN SIGRIST  
CHIEF INVESTMENT OFFICER

**VIA ELECTRONIC DELIVERY**

June 9, 2014

Dear Investment Advisory Committee Members:

Recently, the North Carolina Retirement Systems ("NCRS") investment program and the Department of State Treasurer ("Department") were the focus of a report and statements containing inaccuracies and unsupported allegations. The report was titled "North Carolina Pension's Secretive Alternative Investment Gamble: A Sole Fiduciary's Failed 'Experiment'" (the "BFS Report") and was issued by Benchmark Financial Services, Inc.<sup>i</sup> This letter is intended to share the Department's perspective on the BFS Report and address any concerns you might have about the status of the NCRS and the effectiveness of its investment program.

Throughout her entire term in office, Treasurer Cowell has proactively expanded investment reporting and engaged experts to independently review the NCRS investment program.<sup>ii</sup> One of the core values of the Department is to recognize and value the benefits of diverse ideas, perspectives and people. Further, the Department believes that regular transparent evaluations of the NCRS investment program are appropriate and essential to give stakeholders assurance that entrusted assets are being invested prudently, cost-effectively and in the sole interest of beneficiaries. Most recently, Treasurer Cowell convened the Investment Fiduciary Governance Commission, composed of industry experts, legislators and members of the NCRS, to independently review and recommend changes to the governance structure and operating model of the investment program.

While each independent review has identified areas for further improvement, they have also come to similar conclusions on the most important aspects of the NCRS investment program:

- The NCRS is one of the three best-funded systems in the country, unlike the retirement systems in many states that are struggling with significant weaknesses.<sup>iii</sup>
- A conservative investment program has produced good results. Through last calendar year, NCRS outperformed its stated performance benchmark over one, three, and five year periods. It has experienced weaker performance relative to peers, but this underperformance relative to peers is primarily attributed to NCRS' relatively lower risk.<sup>iv</sup> In relation to peers, NCRS has achieved strong risk-adjusted returns.<sup>v</sup>
- Investment management costs for NCRS are low compared to peers. In 2012, NCRS was in the 40th percentile of peer funds in total investment management cost, meaning that approximately

60% of peer funds have a greater total fund cost than NCRS. The median peer program pays 19% more in total fund cost than NCRS.<sup>vi</sup>

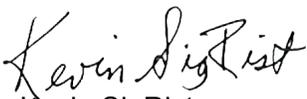
From this position of strength, the Department continues to actively pursue improved investment policies, processes, fees and contract terms. In doing so, our fiduciary duties require an objective approach to investment decision-making that diligently incorporates hard data, expert analysis, and the specific goals of the NCRS and its stakeholders. The BFS Report stands in stark contrast to this approach, as was documented by several commentators.<sup>vii</sup> The author of the BFS Report has also made unsupported public assertions:

- “ ‘The conclusion in the report, broadly, is that the pension fund is sick, it is suffering, it is failing to meet its objective,’ said Edward “Ted” Siedle, the consultant SEANC hired to write the report. ‘There is compelling evidence of wrongdoing.’ ”<sup>viii</sup>
- “ ‘The magnitude of the scam is 20 times greater than Madoff,’ Siedle said during a news conference, referring to jailed Wall Street financier Bernie Madoff, who is believed to have fleeced \$18 billion from investors.”<sup>ix</sup>

Appendix A, which is enclosed, addresses the BFS Report’s most troubling allegations, which are those that have the potential to create unfounded concerns regarding the stability of the NCRS and its investments. The BFS Report is not systematically organized and repeats many of its primary allegations multiple times in different contexts.<sup>x</sup> In order to structure a response, we have collected the allegations into eight primary categories and responded to each with citations to the appropriate documents.

If you have any questions about any of the BFS Report allegations or the Department’s responses, please contact me. The Treasurer and I look forward to working with you as we continue to build upon a strong NCRS investment program.

Sincerely,



Kevin SigRist  
Chief Investment Officer

cc: Pat McCrory, Governor  
Beth Wood, State Auditor  
Roy Cooper, Attorney General  
Elaine Marshall, Secretary of State  
Thom Tillis, Speaker, N.C. House of Representatives  
Phil Berger, President Pro Tempore, N.C. Senate

Enclosures:

- [Appendix A: BFS Report Allegations and Department of State Treasurer Responses](#)
- [Appendix B: Document Comparing BFS Report for North Carolina to BFS Report for Rhode Island](#)

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<sup>i</sup> The Benchmark Report was commissioned by the State Employees Association of North Carolina (“SEANC”). See [http://www.seanc.org/files/5113/9817/8618/North\\_Carolina\\_Pension\\_Fund\\_Forensic\\_Investigation\\_Report.pdf](http://www.seanc.org/files/5113/9817/8618/North_Carolina_Pension_Fund_Forensic_Investigation_Report.pdf).

<sup>ii</sup> Treasurer Cowell has commissioned three special reviews of the NCRS investment program since taking office: (A) The Ennis Knupp Independent Review and Evaluation of the North Carolina Retirement Systems (April 19, 2010); (B) The Hewitt EnnisKnupp report on Investment Management Division decision-making, compliance, and fees (May 22, 2013); and (C) A joint review with the Kellogg Huber law firm concerning placement agents (December 16, 2013).

<sup>iii</sup> “State of North Carolina Pension Overview,” Morningstar, Nov. 20, 2013, page 1, [Exhibit 1](#). “The State’s pension systems are strong,” commented Morningstar. Similarly, Standard and Poor’s named North Carolina the third strongest funded pension fund a July 16, 2013 report: “A Bumpy Road Lies Ahead for U.S. Public Pension Funded Levels,” *Standard and Poor’s*, July 16, 2013, page 4, [Exhibit 2](#).

<sup>iv</sup> Performance through September 30, 2013 was cited in “Investment Fiduciary Governance Commission Briefing Book,” Hewitt EnnisKnupp, January 23, 2014, pages 33-38, [Exhibit 3](#). As of December 31, 2013, NCRS’s total portfolio return, net of all fees and expenses, was 12.3% over one year, 8.7% over three years, 10.5% over five years, 6.6% over 10 years, and 5.9% over 15 years. See [Exhibit 4](#), taken from the performance update provided at the February 19, 2014 Investment Advisory Committee meeting. Performance figures are updated and posted on a quarterly basis on the Investment Management Division’s webpage, <https://www.nctreasurer.com/inv/Pages/Government-Operations-Reports.aspx>. The State’s Investment Advisory Committee receives each quarter a report containing additional technical detail; those reports are available along with the other Investment Advisory Committee meeting materials at <http://www.nctreasurer.com/inv/Pages/IAC-Reports.aspx>. Similarly, a high level of technical detail is reported annually in the investments section of the Treasurer’s annual report and two online supplements. Those documents can be found in [Exhibits 6, 7 and 8](#) and posted on the right-hand side of the Investment Management Division website, <https://www.nctreasurer.com/inv/Pages/default.aspx>.

<sup>v</sup> “Investment Fiduciary Governance Commission Briefing Book,” Hewitt EnnisKnupp, January 23, 2014, page 36, [Exhibit 3](#).  
<sup>vi</sup> *Id.* at page 41.

<sup>vii</sup> Examples of contemporaneous press coverage:

- “The 147-page report takes a shotgun approach, leveling numerous accusations and complaints steeped in inflammatory language.” David Ranii, “SEANC Report Harshly Criticizes NC Treasurer Janet Cowell,” *News & Observer*, April 22, 2014 ([Exhibit 5](#)).
- “Siedle’s claims far from finding ‘smoking gun.’” Editorial, *Triangle Business Journal*, April 25, 2014 ([Exhibit 5](#)).
- “[P]erhaps those who want the media’s attention feel compelled to use that kind of hyperbole. Fortunately for the state pensioners, Cowell has neither heisted nor secreted off with their money.” Scott Mooneyham, Capital Press Association, May 1, 2014 ([Exhibit 5](#)).
- “The report conducted by Benchmark Financial purports to be scathing indictment of the investment practices of North Carolina’s State Treasurer and calls for investigations by a collection of federal agencies. I’ve learned at least one thing from this 147-page report. If you make dozens and dozens of incorrect assertions, assumptions, and inferences, it is almost impossible for anyone to formulate a coherent response.” Andrew Silton, “Meditations on Money Management” blog, April 23, 2014 ([Exhibit 5](#)).

<sup>viii</sup> David Ranii, “SEANC Report Harshly Criticizes NC Treasurer Janet Cowell,” *Raleigh News & Observer*, April 22, 2014 ([Exhibit 5](#)).

<sup>ix</sup> Laura Leslie, “SEANC: Treasurer’s Handling of Pension Fund Warrants Criminal Probe,” WRAL (April 22, 2014), ([Exhibit 5](#)).

<sup>x</sup> In fact, numerous sections of the BFS Report use standard language pulled from previous reports by BFS directed at other states where BFS was engaged. In reviewing the BFS Report, we have identified at least ten instances where language from the report targeting Rhode Island was used in the North Carolina-oriented report. See [Appendix B](#).