
MEMORANDUM

TO: SUPPLEMENTAL RETIREMENT BOARD OF TRUSTEES
FROM: MARY BUONFIGLIO, DEPUTY DIRECTOR, SUPPLEMENTAL RETIREMENT PLANS
SUBJECT: GREAT WEST OPEN ACCOUNTS RECEIVABLE ITEM
DATE: DECEMBER 11, 2014

The purpose of this memorandum is to advise the Board of an accounting issue under review by the Plans' auditor, CliftonLarsonAllen. Staff partnered with Department of State Treasurer senior leadership and legal counsel to create a plan to research and resolve this issue in a manner consistent with our fiduciary duty to Plan participants. Staff does not recommend any Board action at this time. Formal auditor findings are anticipated to be presented at the March 2015 Board meeting.

Background

In July 2009, at the recommendation of Mercer Investment Consultants, a diversification strategy was initiated within the NC 401(k) and NC 457 Stable Value Portfolios. At that time, Prudential served as the sole investment manager of the NC 401(k) Stable Value Portfolio. The recommendation was adopted to diversify assets within both the NC 401(k) and the NC 457 Stable Value Portfolios, while maintaining Prudential as one of four portfolio managers. The existing portfolios were allocated to Prudential, Great West, Payden & Rygel, and PIMCO. Transition activities were coordinated between Mercer, State Street Global Services (the custodian), supplemental plans' staff, and the four portfolio management teams. Galliard was hired as a fully-delegated Investment Manager of both Stable Value Portfolios in September of 2010.

Issue

Upon receipt of assets within the NC 401(k), Great West opened an account receivable of approximately \$4.5 million. This receivable was opened in anticipation of the receipt of principal and interest pay downs associated with mortgage-backed securities. The anticipated paydowns were received by Prudential and never received by Great West. It is important to note that the research to-date indicates that the NC 401(k) is not "short" funds; the payment to the Plan was made in a timely fashion to Prudential following the 2009 transition. Due to this open account receivable, the crediting rate of the NC 401(k) Stable Value Portfolio has been overstated and must be corrected. In order to fully understand this error and its related financial implications, Staff has engaged the Plans' third-party independent auditor, CliftonLarsonAllen, to conduct a review of the 2009 transition and related activity in the subsequent years.

The parties involved in this issue (Great West, Prudential, and Galliard) have agreed to compensate the Plans for this audit and, utilizing agreed-upon methodology, compensate the NC 401(k) to prevent the reduction of the crediting rate, and pay back any fees taken in error based upon incorrect portfolio values.

Next Steps

CliftonLarsonAllen has initiated a consulting engagement to independently assess the events surrounding the 2009 transition and to provide the following work product:

- Verification of transition-related events.
- Independent determination of the dollar amount of the accounts receivable open accrual.
- Independent determination of the impact on the crediting rate, and the necessary payment to the portfolio to maintain the current crediting rate.
- Independent determination of the overpayment, if any, of participant fees and the dollar amount required to make participants “whole.”
- Independent verification of transition activities in subsequent years, and verification that the accounting methodology utilized was accurate and appropriate.

CliftonLarsonAllen has initiated their review and, barring unanticipated problems, anticipate providing a full report to the Board in the March 2015 meeting.