

**Joint Legislative Audit and Review Commission
of the Virginia General Assembly**



**Special Report:
Certain Personnel Issues at the
Virginia Retirement System**

**JLARC Staff Briefing
Trish Bishop
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VRS Oversight Act

- **Section 30-78 *et seq.* of the *Code of Virginia* requires JLARC to oversee and evaluate VRS on a continuing basis**

- **Areas for review and evaluation include:**
 - **structure, governance, administration, and management**
 - **actuarial policy and actuarial soundness**
 - **investment practices, policies, and performance**

Background

- **On June 24, 2005, the Retirement System Oversight Subcommittee of JLARC directed staff to complete a special study of two personnel issues at the Virginia Retirement System (VRS):**
 - **the potential conflict of interests of a member of the Board of Trustees relative to his interest in seeking the Chief Investment Officer position, and**
 - **the handling of the former director's severance agreement**

Study Methods

- **To complete this review, JLARC staff**
 - reviewed Board and committee minutes, memoranda, email, contracts, and personnel and financial records
 - conducted interviews with members of the Board of Trustees, the VRS staff, staff of the Office of the Attorney General, and the search firm hired to conduct the CIO search
 - conducted a review of relevant sections of the *Code of Virginia*

- **Staff of the Auditor of Public Accounts assisted with the review of payroll records and other supporting documentation**

Chief Investment Officer (CIO) Search

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- VRS is currently conducting a search for a new CIO
- A selection committee has been created to review the candidates for the position
- The six members of the selection committee are members of either the Board of Trustees or the VRS Investment Advisory Committee (IAC)

Conflict of Interest Raised About Search Committee Member

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- **The search committee hired an outside firm to conduct the CIO search**
- **All candidates are to be reviewed by the search firm and then brought forward to the committee**
- **In reviewing internal candidates with the committee, the search firm discussed a member of the search committee as a potential candidate**
 - **Counsel and the search committee raised concerns about a member of the committee seeking the position**
 - **Committee resolved to preclude current Board and IAC members from consideration**
 - **The individual being considered resigned from the search committee and elected not to apply for the position**

Concerns Addressed by the Committee

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- **The selection committee acted promptly and appropriately to resolve the situation**
- **The process raises a general concern about the process for hiring staff in leadership positions**
- **The approach of turning to a member of the Board of Trustees to fill an open staff position was used by VRS to fill the director position in 2002**

Recommendations

- **The Board of Trustees should adopt a policy prohibiting members of the Board or the Investment Advisory Committee from being eligible for any full-time position at VRS for one year after the end of service on the Board or the Committee. If the Board chooses not to enact such a policy, the General Assembly may wish to restrict the practice by statute.**

Recommendations

- **The members of the Board of Trustees and the Investment Advisory Committee should commit to ongoing training by the VRS counsel on the requirements of the Conflicts of Interests Act and the Board of Trustee's Governance Policy.**
- **Counsel and senior VRS staff must also exercise their professional responsibility to ensure Board compliance with the Act.**

Severance Agreement for the Former Director

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- **The Board chairman executed a severance agreement for the former director in December 2004**
 - **Gross amount of severance was \$263,122, the equivalent of two years' salary**
 - **Agreement also provided for the purchase by VRS of six months of service valued at \$3,289**

- **The chairman may have believed that he had authorization to act for the Board, but statute is clear on the duty and authority of the chairman**

Authority of the Board Chairman Is Limited

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- **Section 51.1-124.20 (D) of the *Code of Virginia* enumerates the chairman's duties. The chairman shall**
 - **preside over meetings of the Board,**
 - **communicate on behalf of the Board to outside entities interested in the Retirement System, and**
 - **perform additional duties as set by resolution of the Board**

- **The limitation on the authority of the chairman was one of the primary reforms of the system in response to the 1993 JLARC report**

The Board Did Not Authorize the Severance Agreement

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- The Board can delegate authority to the chairman and committees, but it must do so by resolution in an open meeting
- The Board did not consider or adopt a resolution directing the chairman to execute a severance agreement with the director and never approved the final severance package in open session
- Seven of the eight Board members interviewed for the review indicated that they were not aware of the details of the agreement
- Since the severance agreement was executed without authorization, it may be invalid

Severance Agreement Appears Unwarranted

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- For eligible employees who are involuntarily separated from employment with the Commonwealth, the Workforce Transition Act (WTA) provides for
 - either a transitional severance benefit of up to a maximum of 36 weeks' salary or
 - extra retirement credits
- The severance agreement for the former director provided for two year's salary
- Normally, severance is not provided when a State employee retires
- Since the director was retiring and had served in his position only three years, the additional benefit of two years of severance appears unwarranted

Recommendation

- **The Board of Trustees of the Virginia Retirement System should act promptly to either recover the funds paid to the former director but never authorized by the Board, or authorize the severance benefits as provided for in the termination agreement dated December 1, 2004.**

Original Employment Contract Provision Had Lapsed

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- **The original contract for the employment of the director**
 - was executed in February 2002
 - called for severance of up to two years salary for the first two years of the agreement
 - did not provide for severance beyond the initial two-year period

- **There was no obligation for severance as part of a termination agreement:**
 - The original provision for severance had lapsed
 - A revised employment contract, which included severance, was negotiated but never executed
 - The director was retiring, and had served three years

Lack of Oversight by the Board

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- **The Board did not properly monitor the process under which the director terminated his service**
- **While the former chairman appears to have erred in executing the agreement without the full knowledge and authorization of the Board, the Board failed to discharge its duty to inquire about, understand, and monitor the termination of the director**

Lack of Severance Policy

- **VRS does not have a policy on the provision of severance for employees who serve at the pleasure of the Board**
- **VRS employees, including the director, are eligible for the benefits provided under the Workforce Transition Act (WTA)**

Recommendation

- **The Board of Trustees should adopt a policy of the use of severance pay for VRS employees.**

- **The policy should establish:**
 - **the purpose of severance,**
 - **when severance may be offered, and**
 - **the appropriate amounts that may be offered.**

Handling of the Severance Agreement Was Inconsistent with FOIA

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- **Section 2.2-3705.8 of the *Code of Virginia* requires the disclosure of contracts between a public body and its officers or employees**
- **Both the original contract with the former director and the severance agreement were marked as confidential**
- **The VRS staff were directed not to discuss the agreement**
- **Staff indicated that they thought the agreements were protected from disclosure, because they were personnel records**

Recommendation

- **The members of the Board of Trustees, the Investment Advisory Committee, and the VRS staff should be trained by VRS counsel on the requirements of FOIA.**
- **The Board should express its sense by resolution that the Board, its committees, and the VRS staff will always comply with the requirements of the Act.**
- **Whenever Board or committee actions could conflict with FOIA, the VRS director, the CIO, and counsel should promptly advise the Board or committee of the requirements of the Act.**

Conclusion

- **In the early 1990s, various actions of the VRS Board of Trustees worked to erode the public's confidence**
- **The reforms enacted in 1994 provided a foundation for**
 - **strong leadership**
 - **effective communication, and**
 - **sound stewardship of public funds**
- **Each member of the Board has a duty to discharge their responsibilities in a manner that will prevent the Board's ability to govern from being called into question, and take an active interest in the important policy decisions of the Board**

Conclusion

- **The director, the CIO, and other VRS staff should provide guidance to the Board to ensure compliance with laws and regulations**
- **Board and VRS management need to encourage a more open environment of communication with staff**
- **Within this more open environment, staff need to exercise their professional responsibilities and bring to the attention of management and the Board any concerns about compliance with statute and regulations**