



**Thursday, March 9, 2023
Audit Committee Meeting**

9:00 A.M.

**In Person at the Washington State Investment Board
2100 Evergreen Park Drive SW, Olympia, WA 98502**

OR

The link to join can be found at www.sib.wa.gov/meetings.html

Main Governing Board

1. Call to Order/Roll Call (9:00a)

2. Adoption of Minutes (9:00-9:05)

A. Adoption of the December 6, 2022, Minutes

3. External Audit (9:05-9:10)

A. Financial Statement Auditor Independence Review

4. Internal Audit (9:10-10:00)

A. Audit Recommendation Status Report

B. Internal Audit Report – Contract Payments

C. Internal Audit Report – Personal Investments and Trading System

D. Audit Plan Quarterly Status Report - Fiscal Year 2023

5. Management (10:00-10:20)

A. Annual Investment Compliance Report

B. Quarterly Investment Referral Report

6. Break (10:20-10:30)

7. Management cont. (10:30-11:45)

A. 2022 Year-End Proxy Voting Reports and 2023 Proxy Season Preview

8. Other Items (11:45-11:50)

9. Executive Session (11:50-12:10)

A. Audit Director Performance Evaluation

10. Adjourn (12:10p)

**WASHINGTON STATE INVESTMENT BOARD
Audit Committee Meeting Minutes
March 9, 2023**

The Audit Committee met in open public session via Teams video conferencing available to participants and members of the public at <https://www.microsoft.com/en-us/microsoft-teams/join-a-meeting?rtc=1>, Meeting ID: 295 390 860 318, Passcode: qyNfYd; Dial-In Number 1-360-726-3322; Phone Conference ID: 986 359 061#.

Committee Members Present: Treasurer Mike Pellicciotti, Chair
Tracy Guerin
Joel Sacks
Sara Ketelsen
Liz Lewis
Bill Longbrake
George Zinn

Committee Members Absent: None

Also Present: Allyson Tucker, Chief Executive Officer (CEO)
Chris Hanak, Chief Investment Officer (CIO)
Kristina Taylor, Chief Financial Officer (CFO)
Marie Steffen, Audit Director
Susan Iselin, Internal Auditor
Greg Henderson, Investment Compliance Manager
Shawna Killman, Investment Operational Due Diligence Officer
Isaac Williamson, Investment Compliance Officer
Bridget Murphy, Corporate Governance Officer
Rhonda McNavish, Assistant Senior Investment Officer – Public Equity
Stacy Conway, Executive Assistant
Lisa Devlin, Administrative Assistant

Brad Berls, Eide Bailly LLP
Gordon Seymour, Glass Lewis
Brianna Castro, Glass Lewis
Fassil Michael, Institutional Shareholder Services (ISS)
Tor Jernudd, Attorney General’s Office
Jesse Yoder, Attorney General’s Office

CALL TO ORDER

Chair Pellicciotti called the meeting to order at 9:06 a.m. and took roll call. All Committee members listed as present were able to fully participate in the meeting.

ADOPTION OF THE DECEMBER 6, 2022, MINUTES

Chair Pellicciotti moved to adopt the December 6, 2022, meeting minutes. Ms. Guerin seconded, and the motion carried unanimously.

EXTERNAL AUDIT

Financial Statement Auditor Independence Review

Ms. Steffen and Mr. Berls reviewed the independence of the Board’s annual external financial statement audit firm, Eide Bailly. Ms. Steffen provided an overview of the statement of independence received by Eide Bailly and the list of payments that were made to the firm by the WSIB between February 1, 2022, and February 1, 2023. She noted that the payment made in this scope reflected a true-up of prior payments based on a review of billing rates. Mr. Berls discussed Eide Bailly’s tenure with the WSIB, effectiveness of conducting audits virtually, and plans to resume onsite audit work.

Chair Pellicciotti and Mr. Berls discussed a recent change to the relationship between the Office of the State Treasurer (OST) and Eide Bailly. The OST has contracted with Eide Bailly to provide internal audit services. Both Chair Pellicciotti and Mr. Berls expressed their desire to make this disclosure in good faith and Mr. Berls stated there is no impact to Eide Bailly’s independence from the WSIB.

INTERNAL AUDIT

Audit Recommendation Status Report

Ms. Iselin reported on one audit recommendation relating to cash receipting, which was completed over the quarter. Internal Audit verified the updated operating procedures, and the recommendation is closed.

Internal Audit Report – Contract Payments

Ms. Iselin presented the results of the Contract Payments internal audit engagement. The engagement was added to the Fiscal Year (FY) 2023 Audit Plan after a discrepancy was discovered. The audit focused on hourly-rate contract payments and the process and controls over payment processing. Overall, the audit concluded that processes and controls are in place to assist with ensuring contract payments are accurate and paid in accordance with contracted rates. The payments tested complied with approved contract rates and were processed in compliance with applicable policies. There were two audit recommendations relating to strengthening internal controls. Management agreed with the recommendations, and the action taken to address the recommendations was reviewed and verified as complete.

When asked what would be considered a high-level audit recommendation, Ms. Iselin discussed areas of higher risk based on the likelihood of occurrence or the materiality of the impact, to include high overpayments, payments not properly tracked in the accounting system, and invoices not monitored appropriately.

Internal Audit Report – Personal Investments and Trading System

Ms. Steffen presented the results of the Personal Investments and Trading System internal audit engagement. The audit included a review of both the processes and controls related to the agency’s personal trading system and functions, as well as compliance with Board policies, to include required training, certifications and attestations, and personal investment compliance reporting. Overall, the audit concluded that the WSIB adequately maintains and monitors the agency’s personal trading program and functions that assist employees and Board members in complying with Board and Administrative policies relating to personal investments and trading. Overall, the WSIB complies with Board and Administrative policies relating to the required training, certifications and attestations, and personal investment compliance reporting.

There were four audit recommendations that would serve to strengthen internal controls, improve documentation, and ensure compliance with policies. Management agreed with the recommendations and identified a timeline for completion. Action relating to two of the recommendations was taken and verified by Internal Audit. Internal Audit will review the remaining recommendations over the next quarter.

Discussion ensued regarding the Public Disclosure Commission’s Statement of Financial Affairs (Form F-1), the WSIB’s processes relating to tracking completion of the Form F-1 filings, and the maintenance of the WSIB’s restricted list in the personal investment compliance system designed to ensure compliance with Board and Administrative policy.

Audit Plan Quarterly Status Report – FY2023

Ms. Steffen reported on the status of the FY2023 Audit Plan. She noted changes to reporting dates for two audits and stated that all audits on the FY2023 plan are anticipated to be completed.

MANAGEMENT

Annual Investment Compliance Report

Mr. Henderson introduced the investment compliance team and provided an overview of the annual reporting requirements of the investment compliance program to the Audit Committee. He reviewed the responsibilities of investment compliance and explained various regulatory reporting required of the WSIB. Discussion ensued regarding a newly implemented Financial Crimes Enforcement Network (FinCEN) regulation related to overseas banking rules.

Mr. Henderson presented an overview of market documentation related to tax compliance and tax reclaims. In addition, he reviewed the daily compliance program and 2022 testing results.

Ms. Killman presented a summary of the WSIB's operational due diligence (ODD) activities. She explained that Real Estate intermediaries are reviewed on a 2-year cycle and the underlying real estate operating company independent control assessment reports are submitted to the WSIB for review. She addressed who performs control reviews on behalf of the intermediaries and the materials under review. She outlined other ongoing real estate intermediary monitoring, 2022 real estate ODD observations, and anticipated focuses for 2023 ODD reviews. In addition, Ms. Killman highlighted ODD activities related to public market manager searches and System and Organization Control (SOC) reports submitted by certain WSIB service providers annually. When asked, she stated that there have been no issues with service providers submitting SOC reports. She concluded her remarks with a review of private markets compliance testing and noted that the results were positive in 2022.

Mr. Williamson discussed gift reporting analytics, reviewed the compliance monitoring requirements of the personal trading policy and the WSIB's restricted list, and reviewed personal trading pre-clearance procedures and 2022 statistics.

Mr. Henderson reviewed the required training for staff and Board members related to the personal investments policy, new account reporting criteria, and other policy reporting requirements. He noted that there was 100 percent compliance in 2022 for annual attestations by staff and Board members, and timeliness, as it relates to new account reporting, is an area of focus for 2023.

Ms. Smith addressed FinCEN regulations and reiterated that the WSIB follows state laws on where to deposit funds. In addition, manager contracts include a requirement that they comply with all applicable laws and regulations.

Investment Referral Quarterly Report

Ms. Tucker provided the quarter's investment referral report and reviewed the purpose of the report, referring to the underlying policy.

[The Committee recessed at 10:20 a.m. and reconvened at 10:30 a.m.]

CORPORATE GOVERNANCE

2022 Year-End Proxy Voting Reports and 2023 Proxy Season Preview

Ms. Murphy introduced Mr. Seymour and Ms. Castro to present recent and emerging U.S. stewardship trends. Mr. Seymour provided an overview of recent U.S. regulatory updates including Securities and Exchange Commission (SEC) Proxy Advice Rules; changes to Form N-PX, which requires filers to disclose say-on-pay votes; and other evolving environmental, social, and governance (ESG) disclosure requirements. He reviewed recent Department of Labor developments relating to proxy voting and ESG investing and discussed federal and state level anti-ESG measures.

Discussion ensued regarding the potential impact on the WSIB of recent regulatory changes. Mr. Seymour opined that, broadly, the finance industry is gradually moving toward increased transparency and disclosure on ESG issues, and that agency ESG and stewardship activities should align with investment activities.

Ms. Castro presented a review of U.S. annual shareholder meetings and vote outcomes for director proposals, say-on-pay proposals, and shareholder proposals (SHPs). She stated that the top drivers of majority opposition in the director proposals category were generated by gender diversity concerns. Say-on-pay support levels remained consistent, with high levels of support on environment and social SHPs. She presented a preview of key trends for 2023, and she discussed the steady progress being made on board gender diversity and the overall improvement in diversity disclosure by S&P 500 and Russell 1000 companies. Ms. Castro reviewed Glass Lewis policy changes related to gender diversity for Russell 3000 companies and other Glass Lewis policy statements relating to disclosure of diversity metrics and diversity in underrepresented communities.

Discussion ensued regarding Glass Lewis' follow up actions after failed proposals, the frequency of Glass Lewis recommendations against directors, consequences if a director fails to receive majority support, and company engagement practices to ensure recommendations are being heard.

[Ms. Guerin left the meeting at 11:00 a.m.]

Ms. Murphy presented the calendar year 2022 year-end proxy voting results, as well as asset stewardship program updates and forward-looking priorities. She highlighted that director elections made up over two-thirds of votes on proxy resolutions, and the remaining votes were split between say-on-pay, auditor ratification, SHPs, and mergers and acquisitions. She discussed specific results related to voting on directors and compensation, noting that the WSIB voted against, or “withheld” from, 9.7 percent of the director nominees up for approval in 2022, which was up from 7.1 percent in 2021. She reviewed WSIB policy changes relating to binding gender diversity on boards requirements that were enacted in 2019 and 2023, and she expanded on voting outcomes when the WSIB opposed directors based on the 2019 changes. Ms. Murphy commented that the WSIB will continue to vote against directors when appropriate, and she opined that accountability has increased at the board level, with increased focus on meeting attendance, responsiveness to SHPs, climate-related matters, and on say-on-pay concerns.

Ms. Murphy discussed trends related to SHPs, explaining that support levels rose for compensation related SHPs, declined slightly for environmental and governance SHPs, and declined significantly for social-related resolutions. She attributed some of the decline of social-related SHPs to “anti-social” proposals that are presented as beneficial, but are actually regressive in nature, skewing the data outcomes.

Discussion ensued regarding “anti-social” proposals and the ability to hold companies accountable. Ms. Murphy opined that the nuances of SHPs are increasing and becoming more detailed. The WSIB will continue to vote proxies according to investment and proxy policy and data, with a nuanced understanding of the substance of the SHPs. She explained that she utilizes direct peer communication and applicable resource groups to assist with the flow of information and as a reference to how industry peers are responding to changes. When asked how the Board can best support the alignment of policies, proposals, and votes, Ms. Murphy stated that the evolving Climate and Diversity, Equity, and Inclusion (DEI) Blueprints will act as a guide to align policies and the investment process with proxy voting over time. She remarked on the Asset Stewardship program priorities, trends, and areas of focus in 2023, highlighting that engagement and alignment of proxy voting policy with the Climate and DEI Blueprints will be a priority.

Mr. Michael presented the WSIB’s international investment managers’ proxy voting activity and a review of key global trends in 2022. He highlighted board quality, compensation, economic factors, and shareholder rights as the four categories analyzed. Overall, managers are diverging from vote recommendations at a reasonable level and each manager appears to be

scrutinizing issues and votes to align with their respective investment strategies. He reviewed forward looking global trends for 2023 and noted that climate change, say-on-climate, and diversity resolutions are on the rise. When asked, he explained that there are more short-term resolutions because companies feel issues can be addressed easier and with less uncertainties. To measure environment and social metrics over the long-term the metrics need to be appropriate and reliable to test.

Ms. McNavish presented the Public Equity unit's qualitative assessment of the ISS non-U.S. manager review. Overall, staff concluded that the ISS analysis demonstrated that non-U.S. investment managers are voting their proxies consistent with their investment philosophies and processes. She described the three categories of managers: passive; active, tending to vote with management; and active, tending to vote against management. She highlighted Brandes, an active deep value emerging markets manager that tends to have a lower alignment with management and ISS. Deep value managers may be looking at companies that are out of favor or turnaround stories and they will vote their independent views. In the area of director elections, they were stricter than ISS. In that area there may be a higher threshold for Board independence.

[Ms. Guerin joined the meeting at 11:50 a.m.]

OTHER ITEMS

There was no further business to come before the Committee.

EXECUTIVE SESSION

Chair Pellicciotti announced that the Committee would go into executive session to discuss the performance of a public employee. The executive session was expected to last approximately 10 minutes, at which time the Committee would reconvene in open session to adjourn the meeting.

[The Committee went into executive session at 12:01 p.m.]

Audit Director Performance Evaluation

[The committee reconvened in open session at 12:20 p.m.]

The meeting adjourned at 12:21 p.m.