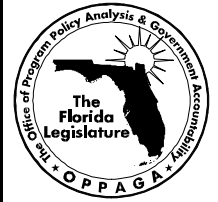




Office of Program Policy Analysis And Government Accountability



John W. Turcotte, Director

February 13, 1997

Follow-Up Report on the State Board of Administration's 1993-94 Investment Report

Report Abstract

The State Board of Administration has implemented four of our five recommendations and is in the process of implementing the remaining recommendation.

Purpose of Review

In accordance with s. 11.45(7)(f), F.S., this follow-up report informs the Legislature of actions taken by the State Board of Administration in response to our Report No. 94-48, which we issued May 8, 1995. This report presents our assessment of the extent to which the Department has addressed the findings and recommendations included in our report.

Background

The State Board of Administration performs a variety of investment activities including managing the Florida Retirement System Trust Fund (FRSTF), the Local Government Surplus Funds Trust Fund; State bond debt service accounts issues, Florida Lottery Lotto prize winner funds, and other various trust funds.

The law requires that the State Board of Administration provide the Legislature an annual report on its investment performance. The law further requires us to review the State Board's report and investment results.

Prior Findings

Our review found:

- The State Board of Administration's 1993-94 Investment Report contained some inaccurate information. The State Board of Administration's Investment Report indicated that there was a loss of approximately \$1.69 million for the real estate cash account. However, State Board staff had mistakenly classified a transfer of \$1.86 million as a loss. The real estate cash account actually experienced a gain of approximately \$175,000.
- The State Board of Administration had not developed policies for recognizing major reductions in the value of FRSTF assets. The State Board indicated that investments in a pooled real estate fund resulted in losses of approximately \$33 million in 1993-94. Documentation of this write-down consisted of a handwritten note, without any indication of the

loss being acknowledged by the Real Estate Asset Class Manager or the State Board's Executive Director.

- The State Board of Administration was primarily reporting investment results for a single year rather than on a long-term basis. The overall rate of return for fiscal year 1993-94 was 0.6%, which was below the investment objective of meeting the actuarial assumed rate of return (8%). However, long-term performance over 5, 10, and 15 years continued to exceed this objective.
- The State Board of Administration had developed written guidelines for investing in futures and options, but had not updated them since 1989. Further, guidelines had not been developed for investing in other types of derivatives.
- The State Board of Administration had not established written procedures and guidelines for staff to follow in monitoring and reporting on the use of derivatives. Monitoring can help assure investment guidelines are being followed.

Current Status

The State Board of Administration has implemented four of our five recommendations and is in the process of implementing the remaining recommendation.

Accuracy of Investment Report Information.

As we recommended, the State Board of Administration implemented procedures to ensure the integrity of data included in future annual investment reports.

Recognizing Major Reductions in the Value of FRSTF Assets.

As we recommended, the State Board of Administration adopted an accounting procedure for its staff to follow in recognizing major reductions in the value of FRSTF assets.

Reporting Investment Performance on a Long-Term Basis.

As we recommended, the State Board of Administration began to report its investment results over a period of 20 years. This provides the Legislature with better information on the SBA's achievement of its long-term investment objective of meeting the actuarial assumed rate of return over several business cycles.

Guidelines for Investing in Derivatives.

As we recommended, the State Board of Administration adopted guidelines for investing in various types of derivatives. These guidelines identify acceptable investment instruments and constraints on their use.

Monitoring the Use of Derivatives.

The State Board of Administration is in the process of completing written procedures for monitoring and reporting on the use of derivatives as a part of an internal risk management project.

This project was conducted in accordance with applicable evaluation standards. Copies of this report may be obtained by telephone (904/488-1023 or 800/531-2477), by FAX (904/487-3804), in person (Claude Pepper Building, Room 312, 111 W. Madison St.), or by mail (OPPAGA Report Production, P.O. Box 1735, Tallahassee, FL 32302). Web site: <http://www.state.fl.us/oppaga/>

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