Actions Taken by State Comptroller Thomas P. DiNapoli to Enhance the Common Retirement Fund's Policies and Procedures Following an Internal Review

April 5, 2017

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As Trustee of the New York State Common Retirement Fund, New York State Comptroller Thomas P. DiNapoli is committed to ensuring accountability and the highest standards of ethics, with absolutely no tolerance for self-dealing. In light of recent allegations of wrongdoing by a rogue employee as asserted by the United States Attorney for the Southern District of New York and the United States Securities and Exchange Commission (SEC), Comptroller DiNapoli ordered a comprehensive internal examination into the actions of the former employee, Navnoor Kang. This internal review was conducted by the Deputy Comptroller for Investigations and the Inspector General of the Office of the State Comptroller (OSC).

Based upon the findings of this internal examination, Comptroller DiNapoli immediately ordered new procedures for vetting potential investment staff and strengthened procedures and safeguards for the selection of brokers and the reporting of trading activities. The Comptroller also wrote to the federal authorities prosecuting Mr. Kang, urging them to aggressively pursue restitution and the return of any ill-gotten gains to the Common Retirement Fund (Fund or CRF).

All of the specific actions detailed below have been implemented.

While even the strictest controls may come up short against a sophisticated conspiracy to evade them, these new procedures will better safeguard the Fund, and the members of the New York State and Local Retirement System who rely upon it, from future acts of fraud. Fundamentally, the CRF is secure and has reached an all-time high estimated value of $186 billion.

Enhanced Pre-Employment Vetting Procedures for All Investment Professionals

Although vetting processes have been in place, those processes have been strengthened. To maximize assurance that all investment professionals employed by the Common Retirement Fund possess the right qualifications and integrity to do the job, Comptroller DiNapoli has directed that:

- All candidates, *prior to being interviewed*, must complete an application for employment listing all former employers, the name of the candidate's former supervisors, and the supervisors' contact information.

- All candidates must provide at least three professional references, one of whom must have been the candidate's most recent employer.

- Reference checks must be performed by appropriate CRF investment staff, as assigned by the Chief Investment Officer (CIO). This function *may not* be delegated to an outside entity.

- All former employers for whom the candidate has performed work relevant to the position for which the candidate is being considered during the past ten years must be contacted and asked, among other things, whether the employer would hire the candidate again.

Once a candidate's references have been checked, the candidate must be subject to a thorough background check overseen by the OSC Division of Human Resources and Administration using a qualified third-party vendor. This reference check must include:

- **Origin Search**, consisting of a multi-level review of the candidate's vital information to validate the candidate's identify and personal identifiers (e.g., date of birth, social security number, address history) and including a search of state and county criminal record databases and sex offender registries.

- **Credit Check**.

- **Global Scan**, consisting of, among other things:

  U.S. Treasury's Office of Foreign Assets Control (OFAC) Specially Designated
  Nationals (SDN) & Blocked Persons
  OFAC Sanctioned Countries, including Major Cities & Ports
  Non-Cooperative Countries and Territories
  Department of State Trade Control (DTC) Debarred Parties
  U.S. Bureau of Industry & Security (formerly BXA) -
  Unverified Entities List
  Denied Entities List
  Denied Persons List
  FBI Most Wanted Terrorists & Seeking Information
  FBI Top Ten Most Wanted
  INTERPOL Most Wanted List
  Bank of England Sanctions List
  Office of the Superintendent of Financial Institutions for Canada Sanctions List
  United Nations Consolidated Sanctions List
  Politically Exposed Persons List
  European Union Terrorism List
  World Bank Ineligible Firms.

- **FINRA (Financial Industry Regulatory Authority) Check,** including:

  Investment related violations and non-compliance
  SEC imposed sanctions.

Fresh Review of All Brokers and Ongoing Monitoring Process

To ensure that all broker-dealers (brokers) seeking to do business with the CRF are thoroughly scrutinized before being afforded the opportunity to execute trades on behalf of the Fund, that all brokers approved to execute transactions for the CRF are monitored on an ongoing basis, and that the CRF has a process in place to recruit and evaluate brokers on a continuous basis, Comptroller DiNapoli has memorialized the process for the continuous selection of broker-dealers authorized to execute fixed income and public equity trades for the CRF in a detailed broker selection policy. A consultant will assist with the process. The policy:

- Requires all broker-dealer firms seeking to do business or seeking to continue to do business with the CRF to apply to be added to the CRF-approved list of brokers and to respond to a questionnaire.

- Sets out a rigorous evaluation process that includes: consultant initial screening (currently Mosaic Consulting), a CRF review committee evaluation, formulation of recommendations by the Director of each asset class that will use the broker services, and CIO approval of a list, subject to final due diligence, including background checks performed on the firm, its key personnel, and the employees directly responsible for the CRF relationship.

- Provides that the consultant will monitor the brokers on the list on an ongoing basis, identifying any material changes reported by the brokers to the information provided on the questionnaires and any other significant events that would reasonably be expected to impact the ability of the broker-dealer to continue to execute transactions for the CRF.

- Requires that reports of any such material changes and significant events will be provided to the CRF review committee, which will formulate a recommendation to the CIO on whether a broker should remain on the list. The CIO will make the final decision, and provide notice to the committee and to the CRF Director of Compliance, who will make any changes that are required to the list.

- Directs that all CRF transactions be executed through an approved broker, unless the CIO expressly authorizes use of a broker not on the approved list for a transaction, with written notice to the Director of Compliance.

- Requires re-application by brokers on the list at least once every five years.

Restoration and Tightening of the Internal Controls Eliminated by the Rogue Employee

In response to Mr. Kang's deliberate actions to develop and implement seemingly appropriate processes for monitoring and reporting trades that enabled him to conceal his scheme, the Comptroller has directed certain measures to restore a robust system of internal controls, upon the recommendation of the Chief Investment Officer, and the CIO has implemented the following:

- Reinstitution of appropriate trade reports, both weekly and monthly, containing pertinent information – including broker names that are reviewed by either the CIO or Deputy CIO.

- Institution of volume reports to readily reveal trade volume as to each broker, which are shared with the CIO, Deputy CIO, Director of Operations, and Director of Compliance.

- Regular review by the Deputy CIO and the Director of Compliance of all trading reports for any spikes or anomalies, which should prompt immediate inquiry of justification for such spikes or anomalies.

- Annual review of all broker usage data by the CIO and Deputy CIO and a written explanation for any significant changes in broker traffic.

- Continued publication of all broker usage data in the Retirement System's Comprehensive Annual Financial Report.

Assertive Action to Promote Compliance with New York State Ethics Law by CRF Consultants, Advisors, Managers, and Brokers

The New York State Ethics Law imposes restrictions on gifts, which apply not only to the receipt of gifts by a public employee under circumstances in which it could reasonably be inferred that the gift was intended to influence him or her, or could reasonably be expected to influence him or her in the performance of official duties, or was intended as a reward for any official action on his or her part; *those restrictions extend as well to the offer or giving of such gifts by outsiders.* Specifically, Public Officers Law § 73(5) directs that, "No person shall, directly or indirectly, offer or make any such gift to a statewide elected official, or any state officer or employee, member of the legislature or legislative employee …."

To ensure that all consultants, advisors, managers and brokers with whom the Common Retirement Fund does business comply with these restrictions, Comptroller DiNapoli has directed that the following provisions be included in the appropriate legal documents with consultants, advisors, managers and brokers:

- The party will expressly acknowledge the restrictions on offering, making, or providing a gift to a state officer or employee under the circumstances set out in Public Officers Law § 73(5).

- The party will agree not to offer, make, or provide any gift to an employee of the Office of the State Comptroller.

- The party will agree to promptly report to the CRF Director of Compliance, the OSC Inspector General, and the OSC Special Counsel for Ethics any violations of the restrictions of which it becomes aware.

- Prior to the approval of any broker-dealer in the recruitment process, the party will be required to certify the provisions listed above, as well as to commit to provide training to its employees, to monitor compliance with these requirements, and to agree to submit to a background check.

- The annual CRF Compliance Questionnaire for Consultants, Advisors, and Managers has been amended to include a certification to the above.

Mandatory Refresher Ethics and Compliance Training for All CRF Staff

Although all OSC employees receive ethics training – a fact that the U.S. Attorney's criminal complaint acknowledges – the Comptroller has directed that all CRF staff attend mandatory refresher training. That training, which has been completed, included:

- Ethics – gifts and travel statutory and regulatory requirements; and examples specific to the Division of Pension Investment and Cash Management.

- Compliance – personal trading and insider trading prevention; compliance disclosures; new automated compliance management system.

- Travel Requirements and Restrictions – responsibilities of the traveler, supervisor and Finance Office; OSC's travel card program.

Affirmative Advocacy on Behalf of the CRF To Secure the Return of Any Ill-Gotten Gains

To ensure that any persons found to have engaged in wrongdoing, as alleged in the criminal indictment and the SEC civil complaint, do not benefit from such wrongdoing, Comptroller DiNapoli has written:

- To the Securities Exchange Commission, asking that any disgorgement of ill-gotten gains that may be secured from Mr. Kang and his co-conspirators be returned to the Common Retirement Fund.

- To Acting United States Attorney Joon H. Kim, asking that restitution to the Fund be included in any potential disposition of the criminal prosecution against Mr. Kang and his co-conspirators.

Diligent Efforts to Determine If the CRF Suffered Any Losses

The internal review conducted by OSC's Deputy Comptroller for Investigations and the Inspector General notes that whether the CRF suffered a loss as the result of Kang's alleged activities is uncertain and the amount of any loss is not readily calculable. The report, however, does suggest a process for attempting to answer that question. In furtherance of that suggested course of action, the Comptroller has directed that:

- All fixed income trade data during the two-year period when Mr. Kang was the Director of Fixed Income be provided to a third party to assess how the cost of executing those trades compared to contemporaneous trades made by others.

- If a pattern is found or suspected, a forensic advisory service be engaged to look deeper into the data to identify any potential losses.

- If possible losses are identified, Counsel is to determine if such losses may be recoverable in a civil action filed on behalf of the Fund.

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Report on the Investigation into the Hiring of Navnoor Kang and Other Related Matters

I. Introduction

On December 21, 2016, an indictment was unsealed in the United States District Court for the Southern District of New York charging Navnoor Kang (Kang), the former Director of Fixed Income for the New York State Common Retirement Fund (CRF or the Fund) and two private brokers with various counts of conspiracy to commit securities fraud, honest services fraud, and obstruction of justice.[1] The charges stemmed from Kang's alleged receipt of kickbacks and gifts in exchange for steering business towards his accomplices. Simultaneously, the United States Securities and Exchange Commission (SEC) unveiled a civil complaint against Kang and his co-defendants, charging them with various Exchange Act violations and seeking injunctive relief prohibiting them from engaging in this conduct and disgorging their profit from their illicit acts.[2] Both the Indictment and the civil Complaint detail Kang's scheme to circumvent the CRF's strict policies prohibiting his behavior and his efforts to conceal his acts after the fact from the federal authorities. The federal authorities further allege that Kang lied to the Fund about the circumstances of his discharge from his former employer, a brokerage firm, and that he had in fact been terminated for over 50 violations of that employer's compliance and ethics policies related to his acceptance of gifts. Later that day, the Comptroller directed the Inspector General and the Deputy Comptroller for Investigations to undertake a joint, comprehensive examination of the hiring of Kang and other matters meriting review. This memorandum consists of a summary of the factual findings of this investigation.

In order to complete this examination, within the limitations addressed below, all current and former CRF and Office of the State Comptroller (OSC) employees and other individuals involved in the hiring process were interviewed. Further, interviews were conducted of CRF management and staffers with information about the Fixed Income portfolio and processes and Kang's performance. All relevant documentation was reviewed within the CRF and OSC and from third parties as warranted including any available electronic information. All individuals voluntarily agreed to be interviewed. Also, in particular, the recruitment firm discussed in Section II of this report fully cooperated and voluntarily provided all information and documentation in its possession regarding the hiring process.

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[1] *United States v. Kang and Kelley*, District Court for the Southern District of New York, 16 CRIM 837. The federal indictment can be found at https://www.justice.gov/file/920006/download. Hereinafter, the indictment will be cited as "Indictment" followed by the referenced paragraph number(s) of that document.

[2] *United States Securities and Exchange Commission v. Kang, Schonhorn and Kelley*, District Court for the Southern District of New York, 16-CV-9829. The SEC complaint can be found at https://www.sec.gov/litigation/complaints/2016/comp-pr2016-272.pdf. Hereinafter, the complaint will be cited as "SEC Complaint" followed by the referenced paragraph of that document.

As the Comptroller directed, since first becoming aware of the existence of a federal probe in February 2016, OSC and CRF have assisted federal authorities in any way possible including providing any requested documentation or information and giving guidance and answering inquiries on an ongoing basis. For these actions, in the press release accompanying the indictment, United States Attorney Preet Bharara, "praised the investigative work" of the Office of Inspector General for the Office of the New York State Comptroller in the investigation.[3] Consistently, in conducting this examination, the Inspector General and the Deputy Comptroller for Investigations have continued to coordinate with the federal authorities and have taken no action which could potentially impair their efforts. Therefore, some investigative steps were not taken after consultation with those offices. Moreover, certain information has been excluded from this report as inappropriate for public dissemination given the ongoing prosecution and civil action.

II. The Hiring of Navnoor Kang

A. The CRF Hires Korn Ferry International to Recruit and Vet Candidates

When the CRF's Chief Investment Officer (CIO) was appointed in August 2012, there were several key vacancies in the Fund. Additionally, relevant to this examination, the incumbent Director of Fixed Income was set to retire in 2014. The need for a fixed income portfolio manager was particularly pronounced because of a significant change to the Fund's approach to its fixed income portfolio. Specifically, the Fund had moved from its passive "buy and hold" approach to a more active tack. Yet, despite this change in vision and corresponding change in benchmarks, the Fund only employed two investment staffers on the long-term side, was still utilizing paper tickets to process trades, and employed no one with corporate credit experience or expertise to trade investment grade securities in-house, which would avoid external management and associated fees. Accordingly, CRF officials advised that in making this transition, bringing in an employee with corporate credit experience was essential. Based upon the need to expeditiously fill the Director of Fixed Income and other critical positions, it was determined that an outside executive recruitment firm with asset management expertise should be utilized.

In January 2013, the CRF issued a Request for Information (RFI) for professional search firms and eleven responses were received. Korn Ferry International (Korn Ferry) was selected. Korn Ferry is the largest executive search firm in the world, with offices in over 80 countries.[4] Korn Ferry was selected based upon its extensive experience in placing executives in asset management and specifically with public pension systems. In that regard, Korn Ferry boasted a Public Pension Funds Specialty Group within its Asset Management Practice with Financial Services that had successfully recruited for CALPERS, the largest public pension system in the nation, and had previously been utilized in the recruitment of the CRF's current CIO.

Pursuant to a contract executed on March 28, 2013, OSC retained Korn Ferry to provide services in the recruitment and vetting of candidates for seven positions in the CRF including a

[3] *See* https://www.justice.gov/usao-sdny/pr/former-portfolio-manager-new-york-state-common-retirement-fund-charged-pay-play-bribery.
[4] Korn Ferry was named the top-ranked executive recruitment firm in the country in 2015. (http://huntscanlon.com/top-50/) and 2016 (http://www.kornferry.com/press/korn-ferry-futurestep-ranked-as-the-no-1-provider-in-hro-todays-2016-rpo-bakers-dozen-list/).

Global Fixed Income Portfolio Manager. In sum, under the terms of its contract with the CRF, Korn Ferry agreed to develop an understanding of the CRF to create specifications – an ideal profile – for each position sought to be filled. Korn Ferry was then to identify suitable candidates through targeted research, a review of its database, direct sourcing and advertising. To ensure the process was all-inclusive, any resumes received by the Fund were to be forwarded to Korn Ferry to be included in its vetting. Korn Ferry then was contractually obliged to further "thoroughly interview qualified candidates to obtain a realistic understanding of their accomplishments, skill sets, behavioral characteristics, motivations, and growth potential." Korn Ferry further agreed to provide the CRF with the candidate's "unedited resume along with highlights of his/her background relative to the position description," and report progress though weekly update calls with CRF officials. Korn Ferry further guaranteed to "utilize their proprietary search assessment tool to gauge the relative strengths and weaknesses of finalist candidates." The contract was to expire six months later, in September 2014, with all positions filled. [5]

As set forth above, the SEC Complaint and Indictment allege that Kang deceived the CRF as to the circumstances of his termination from his prior employer, which allegedly was due to misconduct. In regard to reference checks, the CRF's contract with Korn Ferry provides: [6]

> **<u>Conduct Reference Checks for Successful Candidates</u>**
>
> Once a finalist candidate has been identified and a contingent verbal offer made, Korn/Ferry will facilitate references. Where requested by the CIO, Korn/Ferry will speak directly with individuals who are, or have been, in positions to evaluate the candidate's performance on the job. Korn/Ferry will rely on the information provided by those individuals, and will provide the CIO with written summaries of the conversations with these reference providers. Korn/Ferry will verify educational credentials and request the candidate to disclose all potential conflicts of interest to the CRF. If the CIO requests criminal background and/or credit checks on candidates, the costs for these services will be billed back to the CRF. Korn/Ferry does not warrant or guarantee the accuracy of information provided by these third parties.

Korn Ferry explained that "reference checks" included in its contract with the CRF entail more than simply contacting the individuals provided by the candidate. Because these individuals are presumably favorably inclined to the candidate, Korn Ferry attempts to "triangulate" by also contacting others who can be added to the list through sources and contacts the firm has developed. This is done in order to obtain a more "objective" view of the candidate's characteristics such as work style and reputation ("Past performance indicates future performance"). Korn Ferry also

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[5] Under the terms of the contract, a fully owned subsidiary of Korn Ferry which handles mid-level executive recruitment such as sought by the fund, managed the recruitment. For ease of reference, "Korn Ferry" with whom the fund contracted, will be used throughout this document.

[6] Similarly, on April 10, 2013, Korn Ferry conducted a "kick-off" meeting. Relevant to background checks, at this meeting, Korn/Ferry presented an agenda that included a diagram of the search process which, under "Assess Finalists", Korn Ferry detailed that "Full reference reports are submitted for finalist candidates."

researches the candidate through public sources (e.g., Google) to obtain any information in the public domain and any negative information obtained is noted to the client. In regard to contacting the former employers of a candidate, Korn Ferry officials stated that 99 percent or more of large employers will not provide any information beyond merely confirming salary and dates of employment. In regard to reporting misconduct, Korn Ferry officials interviewed categorically stated that in their combined experience over 50 years in the field they had never been told that type of information from a former employer, likely due to fear of lawsuit and institutional reputation. Indeed, the team leader stated that in her over 30 years, she had "never, ever" been given such information by a former employer.

B. Navnoor Kang Is Vetted and Hired

Korn Ferry advised that there is a global challenge when placing executives in public pension funds: the employer is seeking to employ executives in the asset management industry without paying market rate for such executives. Korn Ferry elaborated that, due to these salary constraints, the type of people who accepted these positions tended to either be experienced individuals who had made their fortunes and were seeking to do public service, or those seeking the opportunity to manage a larger portfolio than they would in private industry. A further challenge facing the CRF in particular, according to Korn Ferry and CRF officials, was attracting candidates to relocate to Albany, New York. These challenges were borne out in the search to fill the vacancies in the CRF. According to Korn Ferry's analysis, as of September 6, 2013, 231 candidates for the open positions had been screened by Korn Ferry. Of those, 142 had survived the initial resume review and been interviewed by Korn Ferry. Of these 142, 20 percent were unqualified, 40 percent had compensation issues, and 40 percent stated that they would not consider relocating to Albany.

In addition to advertising, in order to attract prospective qualified candidates to submit resumes, CRF staff informally spread the word to the professional community that the Fund was recruiting candidates for the open positions. Many resumes were received through these means which, under the terms of the contract, were forwarded to Korn Ferry for vetting. On July 12, 2013, a broker who had been doing business with the Fund for two decades under several firms emailed Kang's resume to a CRF official informing her that Kang was willing to relocate to Albany. The CRF official who received the resume stated that, although the broker praised Kang's abilities, the broker did not "push" Kang on her. In regard to his work history, although the CRF official did not have a distinct memory, the broker stated something to the effect that the market was bad and that Kang had been laid off. Based on the poor state of the fixed income market at the time coupled with her experience that people frequently move in the financial industry, the CRF official did not consider this unusual. As required by the contract, the resume was forwarded to Korn Ferry. No one at the Fund involved in the hiring process or otherwise had knowledge of Kang prior to his resume being sent by the broker or had any contact or communications with him prior to the interviews discussed below. For her part, the CIO was unaware of the identity of the brokerage firm who had forwarded Kang's resume until years later and had never heard of the specific broker who had initially emailed his resume.

Korn Ferry's recruitment and vetting under its contract with the CRF were administered by the head of its subsidiary and led by a team leader who had over thirty years of experience in asset management executive placement and particular expertise in placing public pension fund executives. The Korn Ferry team leader was responsible for quality control, sourcing strategy and client communications. According to Korn Ferry records, on July 16, 2013, the team leader "passed" on Kang – meaning his resume was not considered for further review at that time. Korn Ferry advised examiners that only their team leader would have reviewed the resume at that point in the process, but it is unclear why this decision to pass was made, as the team leader had no memory of the initial review when interviewed as part of this examination. Upon examination of Kang's resume during this investigation, a Korn Ferry official noted that Kang had earned a BA from Columbia University, and had worked for two of the most prestigious investment firms in the world, and said that he would consider Kang's resume as "interesting but need to pursue further" for the position had he reviewed it. When queried as to whether Kang's six month period of unemployment at the time of his interview should have been a flag, the Korn Ferry official stated that 2013 was a terrible year for fixed income and that 2012 had been a "horror show." Accordingly, "six months was not a long time to be on the beach" at that time.

On August 2, 2013, a phone conference was scheduled by the CRF with Korn Ferry. This call was spurred by the CRF's frustration at the state of the progress made at that point and the quality of the resumes it felt were being provided. The Korn Ferry official's "vague recollection" was that a decision was made after the meeting to re-look at candidates who had been previously disqualified but should be reconsidered because they were possibly using "too fine a filter". Accordingly, on August 9, 2013, the team leader took a "2nd look" at Kang's resume.[7]

Subsequent to this review, a decision was made to organize a phone screen with Kang which occurred on September 17, 2013. The phone screen was conducted by CRF executives and a member of the Division of Human Resources. This phone screen is the first time anyone from the CRF or OSC had ever interacted with Kang. When asked why he had departed his previous employer, Kang stated that he had been "laid off" because he was seeking to relocate to the East Coast to join his fiancée but that his former employer was laying people off in New York and there were no positions available for him. Given the state of the market, CRF officials reported that Kang's account seemed plausible. CRF officials further stated that Kang's credentials, especially his experience with corporate credit, were exactly what they were seeking in a candidate to lead the Fixed Income team as it transitioned to the active trading approach.

CRF officials further related that no other preferable candidates for the position were subsequently presented. In this regard, an examination of Korn Ferry records indicates that from the inception of the contract in April 2013 to December 2013, 78 candidates had submitted resumes for the Fixed Income position but only five, including Kang, survived Korn Ferry's review and were selected for telephone screening. Of the remaining four, one lacked the requisite corporate credit experience, one was too senior for the level of position sought to be filled, one was not pursued further after a telephone screen, and one was placed on hold after an in-person interview.

[7] The broker who had initially provided Kang's resume re-forwarded it on August 8, 2013 and it was again sent to Korn Ferry. Although the CRF official who received the resume did not recall the details, she was aware of the instigation for the August 2, 2013 meeting and remembered that Korn Ferry "was not finding anybody" and that the fund continued to spread the word of its search for good candidates.

A decision was made to conduct an in-person interview of Kang which was scheduled for December 4, 2013 and conducted by CRF officials in New York City. Kang was deemed to possess the expertise and background, particularly in relation to his experience with corporate credit, to bring focus to fixed income resources as the Fund started actively trading in-house. At this in-person interview, Kang was again asked about the reason for his departure from his prior employer and he provided the same account regarding his desire to move with his fiancée and the cutting of positions in New York, which to the interviewers was "plausible." Kang told them that he had been planning to join his fiancé in New York and had unwisely informed his former employer of this fact. The former employer determined that since he was leaving California and there were no positions in New York at the firm, they would not pay Kang a bonus for the prior year and would terminate his employment. CRF officials found Kang's account believable, as entities had been downsizing their fixed income teams and they had seen people terminated for many reasons in the industry.[8]

In order to verify the circumstances of Kang's termination from his previous employer, pursuant to the contract, the Korn Ferry team leader was asked to conduct reference checks.[9] Pointedly, the CIO stated that she asked staff to ensure that Korn Ferry checked with Kang's former employer regarding the reason for Kang's departure. On December 18, 2013, a CRF official memorialized the results of Korn Ferry's reference check in an email to other Fund officials stating: "I spoke with [Korn Ferry team leader] and she sent me the reference notes for Navnoor – she also told me that she checked the [former employer] departure and it all checked out – she knew someone that worked for [Kang's former employer] in NY and they said the firm was not doing as well as they expected so they may have to let some of the NY staff go so they didn't want to transfer anyone in from the west coast office to the NY office." When interviewed as part of this investigation, the Korn Ferry team leader had no memory of whom she had spoken with at Kang's prior firm in 2013 and could not recall what contact she had at that firm at that time. She did remember that the firm was going through a "hard time" in 2013.

The Korn Ferry team leader attached to an email to the CRF official a bullet point summary of her conversations with two of Kang's references: the President and CIO of a financial company not connected with the charges in the federal Indictment or Complaint and Deborah Kelley who (unbeknownst to anyone at the time) would later turn out to be Kang's co-conspirator. Notably, the individuals the Korn Ferry team leader chose to contact to complete her reference check were selected solely by the team leader presumably after discussions with Kang.[10] Indeed, Kang had not supplied any references to the CRF at this time and would not do so until over a month later as part of his employment application form.

[8] The SEC Complaint alleges that during his job interview with the CRF, "Defendant Kang lied about the reason he was terminated" by his former employer. SEC Complaint ¶ 29.

[9] This assignment is captured in a status update provided by Korn Ferry at that time which reads "12/11 [team leader] to check references."

[10] As part of the process, Korn Ferry's team leader is expected to communicate with both the candidate and the Fund as evidenced in the case of Kang by the dialogue over salary discussed below and other email exchanges.

At the next day's weekly meeting with Korn Ferry, it was determined that an offer should be extended to Kang, and after brief salary negotiations, Kang accepted the offer on December 30, 2013.[11]

Pursuant to standard OSC procedures, by letter dated January 10, 2014, Kang was supplied with various materials to review and return to Human Resources. Kang was required to complete and return an employment application and an authorization to conduct a criminal background check and credit check. Kang completed the requested material, which he hand-delivered on January 29, 2014. Notably, on his employment application, Kang checked "yes" in response to the question: "Were you ever discharged from any employment for any reason other than for lack of work or funds, disability or medical condition?" Despite the instructions that candidates who answered affirmatively to this question provide an explanation, Kang did not do so. In regard to previous employment, Kang listed three former financial industry employers and his time on the professional tennis tour. As to the listed firms, Kang provided the name of a supervisor, but left the boxes for "Reason for Leaving" and "Salary" blank. Under usual OSC practices for exempt class (at will) hires, these forms are examined by Human Resources personnel and any deficiencies noted to the hiring Division's personnel liaison. In regard to Kang's hire, this process was not followed because it was determined that reference checks had been contractually delegated to Korn Ferry.

In addition to his application, on January 31, 2014, Kang submitted a notarized employment questionnaire to the Office of the State Comptroller swearing that his answers were true to the best of his knowledge. In this questionnaire, Kang averred that he was not the subject of any criminal investigation and that he had never "been discharged from employment . . . [or] resigned from any employment or business or professional association while charges were pending against [him] or during the course of any investigation." He further swore that he had never "been disciplined, admonished, cited or issued a formal warning by any professional or regulatory governing body, including, but not limited to, the SEC, the FINRA, [or] any state or federal securities or financial regulator." Kang further swore that there were not "any matters which may involve a conflict of interest or any problem in connection with [his] appointment to the position for which [he was] being considered, which [were] not fully covered by this questionnaire." Finally, Kang circled "NO" to the catch-all question: "Is there any event or matter in your past not reported in response to a prior question which, if it were public knowledge, might reflect adversely on you or this administration if you were appointed." Kang's questionnaire was reviewed and approved by the Division of Human Resources on February 13, 2014.

C. Events Subsequent to Kang's Hiring

In late July, 2015, approximately a year after Kang had assumed the Director position, Kang traveled with the CRF's CIO to California to meet with several firms including Kang's former employer as part of the CRF's search for strategic partners. The CIO recounted that Kang was greeted warmly at his former firm by high-ranking officials. These officials reminisced with

[11] Kang did not immediately assume the role of Director of Fixed Income. Rather, as intended when he was hired, he "shadowed" the then-current Director until her retirement in July 2014 so that she could train him and assess his capabilities. Upon her retirement, the former Director informed the CIO that Kang was ready to assume the responsibilities of Director and he was officially promoted on July 23, 2014.

Kang about his office-space at the firm. Further, these high-ranking officials inquired about the wellbeing of Kang's parents and asked whether Kang would still be in the area to attend a party that the firm was holding.[12]

Later that year (the precise date could not be determined but occurring after the late July meeting and before Kang's termination in February 2016), the CRF's CIO encountered one of the aforementioned high ranking officials of Kang's previous employer at an event. According to the CRF's CIO, this official mentioned, referring to Kang, that the CRF's CIO "had a great guy there" who had "made a mistake." He added that the firm "may have been too harsh on him, but you picked him up." The official further stated that Kang was "the type of guy with the benefit of hindsight [the firm] would have brought back." The high-ranking official would not expand upon the nature of Kang's "mistake." The CRF's CIO confronted Kang with the inconsistent account, and Kang informed her that while at his former employer he had rebuffed the advances of another official. Subsequently, Kang "made a mistake by forgetting to submit a voucher" and that official used his "failure to report a dinner" to "get rid of him." The CIO stated that she discussed Kang's account with a high-level staff member at the CRF and based upon the context – especially Kang's former employer's statements that they may have been "too harsh" on Kang, that his previous firm would have re-hired him, the manner in which Kang was received at the firm when they visited it, and the full details of Kang's account which she felt would only hesitantly be repeated – the CRF's CIO decided to monitor Kang's performance.

Starting in the fall of 2015, defects in Kang's managerial abilities became evident to the CIO and CRF executive management including his managerial style (i.e., inability to effectively communicate with and motivate staff) and administrative deficiencies (i.e., his failure to promulgate and abide by policies as discussed below). As discussed in Section III of this report, Kang was ordered by the CIO to issue appropriate policies and also, in late fall 2015, was admonished by the CIO regarding his performance as a leader. In February 2016, the Office of the State Comptroller was contacted by the SEC about a ski trip Kang had taken which was apparently paid for by a broker.[13] Based upon this information coupled with the ongoing issues regarding Kang's managerial abilities, the Office of the State Comptroller terminated Kang's employment.

III. Kang's Circumvention of CRF Policies and Procedures

A. Background

As stated in the criminal Indictment, Kang's alleged behavior was "strictly forbidden" by the CRF's policies and New York State law and the bribes he allegedly received "were paid secretly and without any disclosure" to the CRF.[14] As further averred, Kang was trained by the CRF on these prohibitions and certified that he was aware of the Fund's strict rules barring gifts

[12] The CIO's and Kang's warm reception at his prior employer is corroborated by emails from that firm's officials subsequent to their visit.

[13] It was not until the unsealing of the Indictment and the release of the SEC's Complaint that the CRF or the Office of the State Comptroller became aware of the full nature and extent of Kang's alleged acts. This trip was the only specific instance of an alleged improper gift known to the Fund prior to that date.

[14] Indictment ¶ 8; SEC Complaint ¶¶ 31-32.

and conflicts of interest.[15] Indeed, the Indictment alleges that Kang advised his co-conspirator that his acts were specifically forbidden by the CRF and conspired with his accomplice to conceal their acts from both the CRF and the conspirators' employers.[16] In the face of these clear prohibitions, the Indictment alleges that Kang circumvented the CRF's rules to steer trades to his co-defendants' firms and substantially increase the commission they earned in exchange for personal benefits. Specifically, Kang is charged with undermining the CRF's rules requiring that all transactions be conducted only through brokers approved by the CRF – which his accomplices' firms had not been – by conducting "pass through" or "step-out" transactions whereby an intermediary firm on the approved list acted as a go-between to effectuate the trade.[17] The Indictment further alleges that Kang eventually added the firms that employed his co-conspirators to the approved list and then exponentially increased the business directed towards those firms in exchange for unlawful gifts.[18] Part of this investigation examined how Kang was able to carry out his scheme and avoid detection by the CRF.

The investigation revealed that Kang was opportunistic and exploited a time where the fixed income portfolio and processes were in flux to apparently enrich himself. As set forth above, at the time of Kang's hiring, the CRF was transitioning its fixed income approach from a passive "buy and hold strategy" to an active strategy where the core portfolio of investment grade securities would be traded in-house. Contemporaneously, the CRF was transferring from an antiquated system of processing and reporting trade activity to an electronic system. As the new Director of Fixed Income, Kang was charged with leading this transition, but instead of designing processes consistent with his fiduciary obligations, Kang took advantage of this state of transition to commit and conceal his alleged crimes.

B. Approved Brokers

Generally, only brokers officially approved to do business with the CRF may be used by investment staff to conduct transactions. Historically, every three to five years, the CRF would engage in a broker review process culminating in the promulgation of lists of approved brokers for use by the Equity and Fixed Income teams. The particulars of this process evolved over time becoming more formalized over the years. At the time of the last such review, commenced in 2007 and concluded in 2008, two rounds of questionnaires were disseminated to interested firms for them to complete and return to a review committee at the CRF. The CRF committee then scored the submissions and compiled the approved lists: one for use by the Fixed Income team and a second to be used by the Equity team.

After the completion of the last such review in 2008, a widely shared sentiment developed that the system could be vastly improved and that a less static selection system was advisable. Particularly, in addition to being "laborious" and substantially diverting staff time from their primary duties of actively managing Fund assets, it became clear that three to five years was too long a period to wait for a review. This concern was underscored by the global financial crisis that ensued immediately after the creation of the list, which dramatically affected the status of financial

[15] Indictment ¶¶ 10-12; SEC Complaint ¶¶ 33-34.
[16] Indictment ¶¶ 17-19; SEC Complaint ¶ 13-14.
[17] Indictment ¶ 20.
[18] Indictment ¶ 21.

institutions. Accordingly, it became evident that an on going review by an outside firm specializing in the area would be more effective and practical. As noted in the 2013 Final Report of Funston Advisory Services' "Fiduciary and Conflict of Interest Review" of the CRF: "The CRF has not conducted an equities broker search since 2008, but should do so more frequently to better assure best execution. A continuous selection process is a practice amongst peer funds and was identified by the CRF trading staff as an option worth considering."

At the time Kang assumed the position of Director of Fixed Income in July 2014, there were 19 approved brokers on the fixed income list. In addition to the general understanding that a continuous review of approved brokers was advisable, the existing list was considered not only "stale" but also inadequate for the Fund's ability to engage in the new active fixed income strategy.

Prior to Kang's assuming the role of Director, the beginnings of a broker selection process for Fixed Income had been initiated with an eye towards implementing a continuous review process through an outside vendor. The concept was for interested vendors to answer a questionnaire posted online, which was to be supplied to the firm hired to conduct the rolling vendor review. In June 2014, Kang directed that an email be sent to approximately 90 firms along with an application form to gauge each firm's interest in becoming approved brokers. If interested, the solicited brokers were to provide general pedigree information (i.e., address, primary contact) and the types of coverage potentially provided. Approximately 40 submissions from different firms were received as a result of the canvass, but, as discussed below, an outside vendor had yet to be engaged to conduct the envisioned continuous review, and there is no evidence that any substantive screening or analysis of these responses occurred.

In late October 2014, Kang approached a high-ranking CRF official about adding eight new brokerage firms to the approved list, including the two firms that employed his eventual accomplices, stating in an email, "[t]hese are the brokers that would add a lot of value immediately and ones we really need. Most of them have publically traded debt and all are large institutions with balance sheet." The official responded that she would examine past practice on adding brokers.

According to the CRF's 2009 "Long and Short Term Fixed Income Investments Policy, Procedures, Reporting and Control Guidelines" then in effect, in order to be approved, brokers were required to meet three general minimum qualifications:

1. Good financial condition based on the financial statements submitted during the Broker review or as requested by PICM [Pension Investment and Cash Management Division];
2. Acceptable standards of record keeping including timely and accurate confirmation; and
3. Acceptable record of timely delivery and payment on trades.

The policy then provides: "The Chief Investment Officer authorizes additions and deletions to the approved broker and direct issuer lists as recommended by the Fixed Income Investment Officers. The Fund uses a selection device (i.e., questionnaire) to assist in the evaluation of brokerage service providers. The Chief Investment Officer must authorize transactions with dealers not on the approved list."

On November 6, 2014, a memorandum was submitted to the CIO and signed that day approving the addition of the eight brokers. The memorandum states, after listing the brokers to be approved:

> The current list of approved brokers for fixed income has not been updated since 2009 and lacks the full complement of coverage needed to effectively trade the portfolios. These additional brokers will enable staff to address the immediate needs of access to additional liquidity, best execution, and more complete asset class coverage. These firms all meet the requirements the Fund currently sets for broker selection including net capital positions, breadth of coverage, depth of trading and sales staff and experience trading with large institutional clients.
>
> The global equity and fixed income teams are beginning the process of issuing a request for Proposals by Invitation (RFI) to select a firm to manage the broker selection process. The brokers listed above will be added to the approved list immediately upon your [the CIO's] approval but will be required to go through the full due diligence process following the procurement of this firm. The procurement is scheduled to begin later this month.[19]

Consistent with the final paragraph of the memorandum, the same day the CIO approved the addition of the eight new brokers, she also signed a memorandum approving the issuance of a RFI for the purpose of selecting a firm to manage the broker selection process for the entire CRF. The memorandum states that the hiring of such a firm "would result in a more efficient process for the selection of brokers and will allow the investment officers to concentrate on managing and trading portfolios. This new process will allow CRF to keep its broker list current by adding brokers that meet its criteria as needed instead of waiting years for a new broker search. The selected firm will also monitor the current lineup of brokers to insure that there are no significant changes in net capital, major regulatory violations or any other concerns at the brokerage firms." Under the time frame outlined in the memorandum, a contract with the selected broker review firm would be finalized and executed in February 2015, four months later. Kang informed the CRF that he had vetted the proposed firms and that they met the minimum criteria set forth in CRF policy. In retrospect, it is unknown what, if any, background investigation Kang conducted as to these eight newly approved brokers.[20]

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[19] Similarly, once approved by the CIO, the memorandum was transmitted to the CRF's compliance team with the note: "We are going to begin the process for the broker search but in the meantime due to trading needs [the CIO] has approved some additional brokers for the fixed income team."

[20] Although neither of the firms which employed Kang's coconspirators met the qualifications when the 2008 review was conducted, CRF officials advised that the change in fixed income strategy would have significantly affected a 2014 assessment. Particularly, while the 2009 review in regard to fixed income negatively scored brokers with more limited coverage or niche operations, under a more active approach, this disadvantage would not apply. CRF officials further apprised that the most critical component of broker analysis is an assessment of net capital. Based upon SEC filings, these two firms reported assets well over the generally applied threshold for approval at that time and research has unearthed no other information concerning their record keeping or prompt delivery which may have caused them to be deemed unacceptable under the 2009 qualifications. Nor has research unearthed any

In March 2015, the RFI still not having been issued, Kang sought to add an additional 14 firms as approved brokers. None of these brokers is charged in connection with Kang's scheme. Of note, when the list was submitted to the CIO by a Fund official, it was stated: "The addition of these dealers will mitigate the risk of missing opportunities and will expand the liquidity available to the CRF which is necessary and consistent with a portfolio of this size. It is important to note that as we initiate a formal broker review, all existing approved dealers as well as prospective ones will go through the review process." Upon examination, the CIO specifically inquired whether any further actions were required to protect the Fund and was advised that as long as the Director of Fixed Income, Kang, believed that the firms "would come through the traditional standard broker review without any issues," approval was acceptable. After Kang declared that the firms would pass muster, the CIO repeated the need to expeditiously issue the RFI for a broker search firm.

The RFI was eventually issued in November 2015 and a contract signed with the prevailing vendor effective March 2016. When various CRF officials were asked to explain the delay in issuing the RFI and executing the contract, they responded that in light of staffing limitations other important matters arose in the interim which were triaged ahead of the RFI.

C. Trade Processing and Reports

In addition to the change in philosophy towards an active trading approach, a second modification was in process at the time of Kang's assumption of his position as Director which minimized his chances of detection. Namely, starting prior to Kang's employment, Fixed Income was moving from an antiquated paper ticket system for processing trades to an electronic paper-less medium utilizing the Bloomberg system in an effort to mitigate risk of error and streamline the process.

Under the paper ticket system, trades were documented by hand on a form and required two signatures: one from the investment officer confirming the trade and one by the Director of Fixed Income approving the trade. In addition to listing the details of the security involved in the trade (price, etc.) the paper ticket also included the name of the broker involved in the transaction. As he assumed responsibilities as Director of Fixed Income, Kang was tasked with continuing the work of his predecessor in devising the procedure for processing and approving trades electronically. The procedure Kang developed, and which was approved by management, involved investment staff who had executed a trade receiving an electronic confirmation. The trader was then to review the details and, if accurate, confirm the trade. This confirmation substituted for the paper approval by the investment officer. After secondary confirmation by the OSC Accounting Office, the trade would be released to the Fund's custodial bank. At the end of each trading day, Accounting was to send the Director of Fixed Income an electronic report of trades consummated that day for approval. The Director's review of this report substituted for the second signature on the paper ticket.

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existing negative available information about Kang's confederates at that time which should have raised concerns. Therefore, these firms may have met the qualifications for approved brokers in 2014.

Although there is nothing inherently improper or suspicious about this process in general, Kang manipulated the procedure he conceived to conceal his actions. First, by design or fortuity, Kang eliminated a record contemporaneously documenting the identity of the broker utilized in each transaction prior to the completion of the trade. Second, unlike the practice of his predecessor and the practice on the Equity side of the Fund, Kang, as Director of Fixed Income, traded himself as opposed to merely reviewing and approving the trades of his subordinates. Under the new system, no one approved the trades Kang personally made. Third, the investigation revealed that Kang regularly negotiated trades – including, but not limited to, trades with his co-conspirators – and then directed subordinate staff members to confirm the transaction under the parameters dictated. Specifically, Kang would apparently instruct the broker he was negotiating with to send the electronic confirmation to a subordinate investment officer and the investment officer was then directed by Kang to approve the trade as presented. Although there is nothing improper or contrary to policy about the Director trading or directing subordinate staff to complete a substantially ministerial task, Kang used the new trading process not only to steer business to his accomplices, but also to create the false impression that most of these transactions were conducted by investment staff and then approved by him.

Kang's manipulation of the electronic trade process had ripple effects that he capitalized on to further conceal his alleged criminal activity. CRF management advised investigators that trends in broker usage which should prompt further inquiry would not necessarily be noticed when viewed on a daily basis. Rather, to discern patterns, a longer time frame is required: weekly or monthly. Prior to Kang's arrival, Fixed Income investment staff would prepare a weekly summary of the trades for the preceding week culled from the paper tickets for that period. This weekly report, which was sent to the CIO and others, included the information from the week's paper tickets including the identity of the involved brokers.

This weekly report took on additional significance under the new active approach to fixed income. Under the buy and hold strategy, the Fixed Income team was required to obtain the CIO's approval before entering into any "buy programs" or if they intended to sell a security. Because buying and selling were to become commonplace under the new approach, during the period between Kang's acceptance of employment and his start date at the CRF and in anticipation of his joining the staff, the then-Director obtained permission from the CIO to buy and sell securities within the current strategy and provide the CIO with trade details on a weekly basis. When he assumed his position as Director in July 2014, Kang eliminated this weekly report, stating that an electronic equivalent would be developed using data culled from Bloomberg. This report was not reinstituted until spring 2015, after some fixed income trading activity "hit the basket,"[21] prompting management to demand a weekly report. Shortly thereafter, at the instruction of the CIO, additional information was added to the report to demonstrate sufficient liquidity. Notably,

[21] The CRF is permitted to invest the assets of the Fund in specific types of investments enumerated in several sections of the New York State Retirement and Social Security Law. One provision, commonly referred to as the "basket clause," provides that up to 25 percent of the Fund's assets may be invested in investments not specifically authorized by any other statute so long as "the trustee or trustees of a fund shall make such investments with the care, skill, prudence and diligence under circumstances then prevailing that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims." As investments made under this provision are capped, the CRF continually monitors investments falling within this section to ensure its best use for the benefit of the Fund.

when Kang designed the renewed report to be generated using data from the Bloomberg system, he omitted the field showing the identity of the broker used in the listed trades.

Additionally, prior to Kang's arrival, Fixed Income staff would produce a monthly volume report demonstrating the business each broker was conducting with the Fixed Income team based upon par value. This report was developed years earlier as a Fixed Income substitute for the monthly commission report generated by the Equity team. Fixed Income staff advised investigators that they developed the volume report because, unlike in the equity realm, calculating commission on fixed income transactions is complicated and a commission report was not a reliable indicator of broker activity.[22] Instead, the team developed the volume report as a more accurate picture of the business conducted with the various approved brokers. Kang eliminated this monthly report when he became Director. When queried by staff, Kang would state that he would eventually create an electronic substitute using the Bloomberg system, but he never revived the report.

Further, although the Fund had switched to an active approach for Fixed Income, it launched this new approach absent new trading guidelines reflective of this new strategy. Kang eschewed the provisions of the then-existing guidelines requiring a minimum number of broker bids to be reviewed, including MWBE brokers, declaring to investment staff that the existing rules were part of the discarded "buy-and-hold" approach and that abiding by them hurt the Fund's bargaining position. Although Kang was tasked with developing new guidelines for the active strategy when he became director, either by design, apathy or some combination of each, he delayed promulgating any despite repeated direction to do so by the CIO and CRF executive management.[23] Finally, frustrated by Kang's repeated failure to complete guidelines, on September 21, 2015, the CIO suspended all fixed income trading stating: "For several months now, we have been requesting that formal trading guidelines be established for the fixed income portfolio since the portfolio is actively managed. Because this has not been provided, you must cease all active trading immediately by COB today. Trading will be reinstated once guidelines have been submitted and agreed upon." In the succeeding weeks, Kang worked with the Deputy CIO to contact private and public pension funds and construct new guidelines based upon best practices. The new guidelines were issued in the first week of October 2015 and trading was recommenced.

Notably, although Kang eliminated any documentation and manipulated procedures to hide his alleged illicit acts, this is not to say that fixed income investments were not monitored during Kang's tenure or that best execution was not energetically sought by the Fixed Income team. To the contrary, Kang regularly met formally and informally with CRF executive management to discuss fixed income strategy and activity. Investment staff also participated in regular all-staff meetings (originally twice a week and eventually daily) where fixed income activity was discussed with senior management. Moreover, a review of Kang's communications and calendar reveals innumerable discussions with Fixed Income staff and CRF management on specific trades, pricing and general portfolio strategy. Similarly, Fixed Income staff confirmed that they routinely

[22] *See* Richard Best, "How Brokers are Compensated for Selling Bonds," Investopedia, 12/10/15, http://www.investopedia.com/articles/financial-advisors/121015/how-brokers-are-compensated-selling-bonds.asp.

[23] Kang's electronic calendar contains a "To Do" task he created for himself on August 6, 2014 to be completed that day, reading: "Review Policy Manual", referring to the Fixed Income policy manual then in effect. As of the date of his termination, the status of this task remained "overdue."

discussed individual trades with Kang including best execution and portfolio strategy. Additionally, fixed income strategy and performance were reviewed and discussed by the Comptroller's Investment Advisory Committee.[24] Moreover, there is abundant evidence that other members of the Fixed Income team regularly, vigorously negotiated with brokers to obtain the most advantageous trades for the Fund.

D. Step-Outs/Business with Kang's Co-Defendants

According to the Indictment and SEC Complaint, prior to Kang's addition of his co-defendant's firms to the CRF's approved broker list, Kang steered trades to his co-defendants by using a third-party-approved broker as a middleman. This tactic (known as a "pass through" or "step out" transaction) was not regularly utilized by the Fund and, as used by Kang, circumvented the CRF's rule on approved brokers. Fixed Income investment staff advised that prior to Kang's tenure they would infrequently identify a security that would be a good investment for the Fund but not available through any approved broker. In these rare instances, staff would attempt to purchase the security using an approved broker to locate a second broker to conduct the transaction at best execution. Instead of using this technique in rare instances for the benefit of the Fund based upon a particular security sought, Kang apparently used an approved broker as a middleman to circumvent Fund policy and provide business to his co-conspirators. As per his normal tactic, Kang would explain to investment staff that he was utilizing this technique as part of the new active approach and that the middleman provided the CRF with the best value.

Once Kang's confederates' firms became approved brokers, they, like other approved brokers, would directly contact investment staff with trade ideas. Of note, several investment officers stated that upon his becoming Director, Kang stopped the practice of making the CRF's Fixed Income portfolio regularly publically available, declaring that the Fund was hurting its bargaining position, particularly under the new active approach, by revealing its position to brokers and the market. While the portfolio was still posted annually on the Bloomberg system, this material became dated over the year and Kang prohibited ongoing distribution. Notwithstanding his stance, one of Kang's co-defendants informed an investment officer after Kang had been terminated that Kang had disclosed the portfolio. With this knowledge, during the course of this investigation, several staffers also noted retrospectively that both co-defendants appeared to have better knowledge of the Fund's holdings than other brokers. While absent the ability to interview Kang or his co-defendants it is impossible to determine if Kang provided them with advantageous information and, if so, how regularly, his actions at a minimum gave the perception of favoritism prohibited by the CRF's policies and New York State law.

[24] The Comptroller's Investment Advisory Committee, comprising prominent investment professionals appointed by the Comptroller pursuant to Section 423 of the Retirement and Social Security Law, advises the Comptroller on general investment issues, reviews the investment policy statement and any amendments, and reviews and provides a recommendation to the Comptroller on the proposed asset allocation plan developed by the Chief Investment Officer. The Investment Advisory Committee also periodically reviews the strategic plan of each Common Retirement Fund asset class, and monitors the Common Retirement Fund's risk profile, investment activity and performance on a periodic basis.

E. Possible Loss to the Fund

The criminal Indictment and the SEC Complaint allege that Kang violated federal law and his fiduciary obligations to the Fund by receiving benefits for directing business to his co-defendants. Although the Indictment alleges that the Fund paid higher commissions on certain step-out trades, neither the Indictment nor the Complaint allege whether the CRF suffered a loss as a result of Kang's activity. This is unsurprising as the amount of loss, if any, is not an element of the crimes and violations for which he is charged. Moreover, even if the Fund suffered no loss, if Kang violated the law, he deserves punishment commensurate with his betrayal of the public trust.

Whether the Fund suffered a loss and, if so, the amount of such loss, due to Kang's actions is not readily calculable and beyond the scope of this report. Federal authorities to date have been unable to provide the Fund with an amount of any potential loss. Moreover, Kang and his co-defendants, who would know whether the specific trades covered by the complaint were inflated or if Kang's scheme instead centered on steering business to them which would have been distributed amongst other brokers, are not available to be interviewed this office.[25] Further, the records of the firms who employed Kang's co-defendants that would reveal the amount of any mark-up on any trade are similarly inaccessible for purposes of this examination.

CRF officials and others have explained that to make such a determination, suspect trades would need to be segregated from other trades. Examination would then have to be conducted to determine whether those securities or other comparable securities were traded on the market at the time of each suspect trade. If there are comparable transactions, the price negotiated by the Fund would have to be compared with other trades to determine if it appears within a reasonable range. If no comparable transaction can be identified contemporaneous with the suspect trade, valuation becomes even more difficult. Moreover, to truly understand whether the suspect trades eventually benefitted or damaged the Fund, examination must be conducted of the performance of the security subsequent to the purchase or sale including, on the buy side, whether the Fund retained the security and collected interest or sold the security and, if so, at what profit or loss. Whether the trades were unnecessary and the related question of opportunity cost – whether the Fund forewent a trade in order to pursue the suspect trade – is even more difficult to determine, especially in light of the major change in philosophy to active trading upon Kang's arrival.

These factors are presented to outline the challenges of attempting to explore the existence of any possible loss to the Fund given Kang's actions and the available information. Whether loss to the Fund can be meaningfully calculated, and if so at what expense, is a matter beyond the scope of this investigation.

[25] Although a comprehensive review is not feasible as part of this examination, there is evidence of Kang bargaining for better prices for the Fund with brokers including with his co-defendants.

IV. Conclusion

This report constitutes the factual findings of this examination as to the process by which Kang was hired and how he avoided detection.[26] In addition to the serious criminal charges he now faces, Kang's alleged actions violated unambiguous CRF polices and New York State law. Kang was trained on these applicable laws and rules and certified that he understood them. Unfortunately, Kang proved to be resourceful and was able to circumvent these policies by conspiring with outside brokers and taking advantage of a transitional stage of the CRF's Fixed Income operations. No system can perfectly insulate an organization against premeditated criminal action deliberately designed by a person in a position of trust to circumvent existing safeguards. This is especially true of one conspiring with outside individuals to deceive and to conceal their actions. These findings are provided to present information for potential remedial action as to the CRF's policies and practices to attempt to further protect the Fund from future potential criminal enterprises.

[26] As set forth above, investigators consulted with the federal authorities and took no actions which could potentially interfere with ongoing federal proceedings, which included refraining from any investigative steps or the public reporting of any information which could jeopardize these proceedings.