MINUTES
of the
FIRST MEETING
of the
INVESTMENTS AND PENSIONS OVERSIGHT COMMITTEE

August 19, 2020
Video Conference Meeting

The first meeting of the Investments and Pensions Oversight Committee (IPOC) for the 2020 interim was called to order by Representative Patricia Roybal Caballero, vice chair, on Wednesday, August 19, 2020, at 9:13 a.m. by video and audio conference via an online platform.

Present
Sen. George K. Munoz, Chair
Rep. Patricia Roybal Caballero, Vice Chair
Sen. Jacob R. Candelaria
Rep. Natalie Figueroa
Rep. Miguel P. Garcia
Sen. Gay G. Kernan
Sen. Steven P. Neville
Rep. William "Bill" R. Rehm
Rep. Tomás E. Salazar
Sen. John M. Sapien
Sen. Elizabeth "Liz" Stefanics

Absent
Sen. Gregg Fulfer

Advisory Members
Rep. Phelps Anderson
Sen. Roberto "Bobby" J. Gonzales
Sen. Mary Kay Papen
Rep. Sheryl Williams Stapleton
Sen. William F. Burt
Sen. Stuart Ingle
Sen. William H. Payne
Sen. James P. White

Staff
Anthony Montoya, Staff Attorney, Legislative Council Service (LCS)
Erin Bond, Research Assistant, LCS
Rebecca Griego, Records Officer, LCS
Carrie McGovern, Researcher, LCS

Handouts
Handouts and other written testimony are in the meeting file and posted on the legislature's website.

Wednesday, August 19

New Mexico Finance Authority (NMFA) Update and Small Business Recovery Act of 2020 (SBRA) (9:16 a.m.)

Marquita Russel, chief executive officer, NMFA, provided the committee with an update on the NMFA's activities as well as its efforts to implement the SBRA, recently passed during the June legislative special session. The presentation can be found here:

https://www.nmlegis.gov/handouts/IPOC%20081920%20Item%201%20NMFA%20-%20UPDATE%20and%20SBRA%20of%202020.pdf.

Questions and comments from committee members addressed the following:

- under the SBRA, in order for a small business to qualify, the business must show a loss of 30% or more of gross receipts for both April and May, which has caused issues for businesses that report less often than monthly or that did not qualify for both months. A member inquired whether the two months could be averaged, to which Ms. Russel replied that the statute is very specific and has no provision for averaging;
- the NMFA is allowed to use 1% of the balance of the Small Business Recovery Loan Fund to administer the SBRA, some of which it used to purchase third-party applications from Plaid, Formstack and Experian, although this was very limited in cost;
- to ensure that funds are spent in a lawful manner, certification at the time of closing states that funds must be used as stated in the SBRA;
- if a borrower has a loan in default, the NMFA will work with the client to make payments through a loan extension. According to Ms. Russel, the NMFA will not unreasonably withhold an extension;
- the amortization on principal is calculated over 36 months, and a borrower can prepay without penalty;
- a business is not required to give collateral to receive a loan; however, if a borrower goes out of business, there is likely no recourse for repayment;
- the NMFA's budget is set by its board of directors;
- a member cautioned against the possibility of tapping into the Public Project Revolving Fund in the 2021 session to help the state's solvency. Ms. Russel noted that should this happen, the demand for the fund will still remain, and fewer loans will be granted;
- to date, the NMFA has received 500 loan applications, 100 of which were denied. While a handful of projects have been funded, another 100 are in the closing stage. Ms. Russel stated that there were a few technical glitches, which have been fixed;
- it takes the NMFA three to five days to process an application, with an application taking 30 to 60 minutes to complete and another 30 to 60 minutes to review;

- the hospitality industry has submitted the highest number of applications and has been the most impacted by the COVID-19 pandemic. Ms. Russel said that she would provide the committee with a breakdown of how many restaurants, hotels, breweries and other hospitality businesses have sought SBRA loans when the data is available;
- to process the loans, the NMFA uses loan servicers, which consist of community development financial institutions, banks and credit unions throughout the state. Loan servicers receive $250 per application;
- all loan applications are submitted online, after which the NMFA assigns an application to a loan servicer. The NMFA pulls the credit information and does a final verification of the loan determination, while the loan servicer simply reports its findings. The NMFA bears the liability and the risk. A member wondered if it would be better to bypass the loan servicers to save money. Ms. Russel replied that loan servicers were added to the statute to provide more opportunities for businesses; in addition, if the NMFA had to process all applications, it would incur a longer turnaround time and would require more staff;
- application verification occurs online, and no face-to-face contact is necessary;
- personal credit information is not pulled, only business credit; while a credit score is not a criterion, the NMFA is looking at whether a business has a tax lien and has responsible credit behavior;
- regarding independent contractors and cottage industries, if these types of business are exempt from paying gross receipts, they do not report to the Taxation and Revenue Department, which reporting is a specific statutory requirement to receive a loan; and
- a loan recipient is required to make a payment one year after the loan is funded, with interest payments due annually for the first three years and the principal due at the end of the third year.

The chair requested that the NMFA appear at subsequent IPOC meetings to provide updates on the types of businesses that received loans and, of those that were denied loans, the reasons for denial.

State Investment Council (SIC) Update and Recovery Programs (10:40 a.m.)

Steven K. Moise, state investment officer, SIC, Vince Smith, deputy state investment officer, SIC, and Charles Wollmann, director of communications, legislative and client affairs, SIC, provided the committee with an update of the SIC's activities and its participation in economic recovery programs related to the COVID-19 pandemic. The presentation can be found here:

https://www.nmlegis.gov/handouts/IPOC%20081920%20Item%202%20State%20Investment%20Council%20-%20IPOC.pdf.

Questions and comments from committee members addressed the following:

- with oil and gas production down, the corpus of the Severance Tax Permanent Fund (STPF) and the Land Grant Permanent Fund needs to be protected. There are many positive aspects to the renewable energy industry, but it will likely not replace oil and gas revenues;
- a likely scenario that is problematic is that the demand for oil will diminish;
- even with oil production down, the Land Grant Permanent Fund is still growing, and the State Land Office is projecting $1 billion flowing into the fund in 2020. However, it is difficult to predict beyond a few years how inflows to the fund will be affected;
- the SIC's New Mexico Recovery Fund, which is funded through the STPF and managed by Sun Mountain Capital, has to date awarded $25 million in eight loans, with $90 million lined up pending review;
- $50 million from the SBRA is available for local governments and is waiting to be deployed, but there is a chance that not all of the money will be used;
- a recently enacted law allows an increase from 9% to 11% in the amount of the STPF to be invested in New Mexico private equity and start-up businesses, which resulted in $100 million allocated to the New Mexico Recovery Fund;
- Sun Mountain Capital charges .5% on committed dollars over the first year, and for deployed dollars, .9%. The total expenses will not be known until all of the money is loaned out; however, Sun Mountain Capital is not charging carried interest;
- total venture capital investment returns in New Mexico are available in the SIC's most recent quarterly report; and
- a member asked if it would be a good idea to take all of the loans put out on the market and move them to the bond market to lower interest rates. Mr. Wollmann replied that a concern with this strategy is that the money has been deployed and will be tied up for several years. It is unknown what the rates of return will be, and some loans may wind up in default; this may result in the SIC having to take additional risk with other assets in its portfolio.

Educational Retirement Board (ERB) Update (1:03 p.m.)

Jan Goodwin, executive director, ERB, and Bob Jacksha, chief investment officer, ERB, gave the committee an overview of what has transpired at the ERB over the past several months. The presentation can be found here:

https://www.nmlegis.gov/handouts/IPOC%20081920%20Item%203%20Educational%20Retirement%20Board%20-%20Update.pdf.

Questions and comments from committee members addressed the following:

- an ERB statement of belief is that private assets are more likely to provide better outcomes in the long run compared to public securities, and this is reflected in its asset allocation;
- opportunistic credit investment includes private direct lending, high yield bonds, structured credit and regulatory relief trades with banks. This investment is governed by the Financial Accounting Standards Board, and most private asset managers have oversight boards;
- regarding private assets, there are some private asset managers that are domiciled overseas or have offices in other international markets, but most are United States companies; there is no prohibition on dealing with foreign companies;
- real assets include inflation-linked assets, infrastructure investments and timber, agriculture and water investments;
- 51% of the ERB's assets are in private assets. Of these, private equity and private real estate offer no liquidity, but other private assets offer varying degrees of liquidity. Since 2006, the ERB has been gradually increasing the percentage of private assets in its fund. A member expressed concern about investing so much in private assets because they have an eight- to 10-year return;
- the ERB is exploring the possibility of having the state issue pension obligation bonds, which have the most success when investment returns are at an all-time low, which is the case currently. Statutory changes would have to be made for this issuance to occur. These bonds could have an immediately positive impact on the ERB's funded ratio. Pension bonds are similar to school bonds, except that pension bonds are taxable and their interest rates are different;
- the state's credit rating has not been upgraded;
- the ERB's return-to-work statute sunsets on December 31, 2021, and its board has not taken a position on this. Ms. Goodwin said that it would be beneficial to devise new ways to keep people working as long as possible until retirement, instead of retiring and returning to work;
- currently, if a retired ERB member has 12 consecutive months of retirement, the member can return to work and work as much as the member wants, and contribution rates are 10.7% for the employee and 14.15% for the employer;
- a member suggested that the ERB look into the "California rule" that removes potential loopholes that can erode a pension system;
- a member asked how the ERB weighs investments in rising industries, such as renewable energy, versus declining industries, such as coal. While the ERB invests in both types of industries, its responsibility is to get the greatest return on investment, not to invest in companies with potential societal benefits;
- a member wondered if, in order to achieve parity between the two entities, the ERB and the Public Employees Retirement Association (PERA) should have their boards combined. Mr. Jacksha noted that this would require a constitutional amendment;

- the ERB's Investment Committee is composed of the chair of the ERB's board and two ERB board members appointed annually. The ERB's board recently decided that the ERB's investment staff will select managers and consultants; previously, the Investment Committee made this selection;
- if the state wants the ERB to be 100% funded in 30 years and does not want to increase employer contribution rates or issue pension bonds, benefits to current and future members may need to be cut. This could include reducing the multiplier for current and future members and capping the cost-of-living adjustments. An overhaul of the ERB for the next session has not been discussed, but employer contribution rates likely need to be increased;
- the returns from private and public assets can be found in the ERB's quarterly reports on its website;
- the ERB is searching for a manager to oversee the use of derivatives, i.e., futures and options, the use of which the ERB's board recently decided to allow. It is unknown what returns these derivatives will bring;
- the ERB assesses all asset categories on a quarterly basis;
- the ERB received funding in the 2020 legislative session for a new building, and the reason this funding was not cut is because it did not come from the General Fund;
- currently, the ERB has staff in two buildings, one it owns and one in which it leases space. When completed, the new building will house all employees, and the ERB will sell the building it owns for what should be much higher than the $4 million that it was appraised at 16 years ago;
- a member cautioned against setting investment policy based on social issues;
- a new building is needed now because it will enable the ERB to function most effectively. It will also allow ERB members to have more privacy when making financial decisions at the building;
- the chair requested the ERB to provide to the IPOC the board packet for the Investment Committee so that IPOC members can review what information and investments the Investment Committee is given and how decisions are made. Mr. Jacksha agreed to this request but asked that the information not be shared. The chair said that certain information can be redacted; and
- the chair asked how the ERB's board is functioning, to which the presenters replied that the board is collegial and speaks with one voice with the best interests of the beneficiaries in mind.

PERA Update (3:16 p.m.)

Wayne Propst, executive director, PERA, and Dominic Garcia, chief investment officer, PERA, provided the committee with an update of recent activities at the PERA. The presentation can be found here:

https://www.nmlegis.gov/handouts/IPOC%20081920%20Item%204%20Public%20Employees%20Retirement%20Association%20-%20Update.pdf.

Questions and comments from committee members addressed the following:

- currently, the PERA is housed in a rented space in Albuquerque and a Santa Fe building that it owns. The Retiree Health Care Authority (RHCA), whose main office is a leased space in Albuquerque, rents space in the Santa Fe building for its Santa Fe staff. Because the PERA's Albuquerque space is very small and on the fourth floor, which is problematic for its elderly clientele, the PERA was looking for a new space. As a result, the PERA and RHCA have decided to lease a building together in Albuquerque;
- a member suggested asking the Children, Youth and Families Department about the extra space it has in its new Albuquerque office;
- a member asked how the PERA's board of directors is functioning and how it makes investments, to which Mr. Propst replied that the board is developing a strategic planning process and is under strong leadership. Mr. Garcia noted that in January 2018, the PERA's board changed its governance from handling all investment decisions to making decisions regarding strategic asset allocation, setting benchmarks and setting a risk budget. PERA staff handles the delegation of implementing the risk budget and selects managers and reports these decisions back to the board; and
- the chair requested the findings from the PERA's audits at the next IPOC meeting.

Adjournment

There being no further business, the meeting adjourned at 3:56 p.m.