

**MINUTES
of the
FIFTH MEETING
of the
INVESTMENTS AND PENSIONS OVERSIGHT COMMITTEE**

**December 2, 2011
State Capitol
Santa Fe**

The fifth meeting of the Investments and Pensions Oversight Committee (IPOC) for the 2011 interim was called to order by Senator George K. Munoz, chair, on Friday, December 2, 2011, at 9:15 a.m. at the State Capitol in Santa Fe, New Mexico.

Present

Sen. George K. Munoz, Chair
Rep. Henry Kiki Saavedra, Vice Chair
Rep. David L. Doyle
Rep. William "Bill" J. Gray
Sen. Timothy M. Keller
Rep. Larry A. Larrañaga
Sen. Carroll H. Leavell
Rep. Jim R. Trujillo
Rep. Luciano "Lucky" Varela

Absent

Sen. Steven P. Neville
Sen. Mary Kay Papen
Sen. John M. Sapien

Advisory Members

Rep. Donald E. Bratton
Sen. Carlos R. Cisneros
Rep. Miguel P. Garcia
Rep. Rhonda S. King
Rep. Patricia A. Lundstrom
Rep. Jane E. Powdrell-Culbert
Rep. Sheryl Williams Stapleton
Rep. Mimi Stewart
Rep. Richard D. Vigil

Sen. Tim Eichenberg
Rep. Roberto "Bobby" J. Gonzales
Sen. Stuart Ingle
Sen. William H. Payne
Rep. William "Bill" R. Rehm
Sen. John C. Ryan
Sen. Michael S. Sanchez
Rep. Shirley A. Tyler

Guest Legislators

Sen. Sue Wilson Beffort
Rep. Bill B. O'Neill

Staff

Tom Pollard, Legislative Council Service (LCS)
Doris Faust, LCS
Claudia Armijo, LCS

Guests

The guest list is located in the meeting file.

Handouts

Handouts and written testimony are in the meeting file and posted on the New Mexico Legislature web site.

Approval of Minutes

Because the committee will not meet again this year, the minutes for this meeting have not been officially approved by the committee.

Friday, December 2

Senator Munoz welcomed committee members and guests. He reminded members that the meeting was being webcast and asked them to introduce themselves, which they did.

Discussion of the Impact on the Severance Tax Permanent Fund (STPF) and Public Schools and Other Capital Projects Financed with Severance Tax Bonds of Proposals to Increase Severance Tax Revenue Flowing to the STPF

The committee members heard from a panel of experts regarding the impact on the STPF, public school construction and other capital projects financed with severance tax bonds of proposals to increase the severance tax revenue flowing into the STPF. The panel included Steven K. Moise, state investment officer, State Investment Council (SIC); David Abbey, chair, Public School Capital Outlay Council (PSCOC); Robert Gorrell, director, Public School Facilities Authority; Stephanie Schardin Clarke, director, Board of Finance Division, Department of Finance and Administration; Robbie Heyman, bond counsel, Sutin, Thayer & Browne, APC; Charles Wollman, director of communications, SIC; and Robert "Vince" Smith, deputy state investment officer, SIC.

Senator Munoz asked Mr. Gorrell to lead the presentation. To aid in the discussion, Mr. Gorrell provided a handout titled *State of New Mexico Public School Capital Outlay Council Public School Facilities Authority 2010 Annual Report*. He reminded committee members that, in response to fiscal conditions, the PSCOC did not fund any new school construction in 2010 and, overall, public school capital outlay decreased by 26% in 2010.

Mr. Gorrell provided a November 17, 2011 memorandum that contained an analysis of the *Outlook for PSCOC Project Economic Impacts to Maintain the Facilities Condition Index Rating*. The analysis provides a funding breakdown and estimate of the employment impacts of school construction funding, including PSCOC projects.

There was discussion about the rising insurance costs for coverage of public school structures. It was noted that the insurance costs keep increasing, even though many of the buildings have been renovated and updated. Mr. Gorrell noted that the older school structures depreciate faster than newer buildings and that this is a continuing problem.

In general discussion regarding the *Zuni* lawsuit, members and guest speakers discussed whether the public school funding formula needs to be reevaluated for needed changes. Members were advised that there is no real "end" to the lawsuit. Rather, in the court order, the state was directed to meet the needs of the schools with the greatest needs first. In 2006, after being reviewed by the court for compliance with its order, the judge said the state had been doing a good job in its efforts to remedy the inadequacies. Senator Munoz noted that staff would be requested to evaluate the funding formula and present their findings to the committee at a meeting in the next interim.

Mr. Moise, Mr. Wollman and Mr. Smith addressed the committee. Mr. Moise reminded the committee members of the newspaper articles and opinion pieces published earlier in the year regarding the long-term consequences of shrinking the corpus of the STPF. He noted that, due to the SIC's concerns over the long-term health of the STPF, the SIC held a meeting on the issue a week prior to the IPOC meeting. The meeting was attended by several legislators and other interested parties. Mr. Moise added that many believe that the intentions of the individuals responsible for the establishment of the STPF have not been continued in practice in recent years. Rather, the practices have changed to the detriment of the fund.

Mr. Moise reminded members that Bob Grant and John Bigbee, former legislators, addressed the SIC and have been on a campaign to increase the flow of dollars into the STPF. Mr. Grant and Mr. Bigbee presented information memoranda on the issue, which included historical facts about the fund, a recap of the deposits made to the fund from 2002 through 2011 and other pertinent information. Copies of the memoranda are located in the meeting file.

Mr. Smith presented the SIC's *Severance Tax Permanent Fund Analysis* handout dated December 2, 2011. He began with a discussion about what is statutorily mandated to be paid from the fund. He talked about possible changes to the flow of dollars into the fund and how those changes could impact the fund's balances. He noted that restoring the contributions to the STPF by 5% could impact the fund positively if done over a period of 20 or more years.

Mr. Smith directed the committee members' attention to the handout, which provides models depicting various scenarios for restoring the fund, including a status quo model depicting the projected value of the fund out to fiscal year 2031 if contribution rates remain the same.

Committee members discussed the inflation rate used for modeling the projected values of the fund. The inflation rate used by the federal government does not include such costly and necessary consumer items such as gasoline, members noted.

Ms. Clarke provided a handout titled *Severance Tax Bonding Program and Severance Tax Permanent Fund* in her presentation to the IPOC. She provided a brief history of severance taxes collected in New Mexico since 1937 and of the severance tax bonding program since 1959.

Ms. Clarke provided the following conclusions for the committee:

- Severance tax and permanent fund contributions are two competing uses of severance tax revenue, and both programs have positive consequences.
- Severance tax bonds finance capital improvements. If wisely spent, these improvements can make important contributions to the New Mexico economy.
- Permanent funds generate distributions that currently finance 11.6% of the general fund recurring revenue. This represents a large "down payment" on the state's government operations.
- Other possible uses of severance tax revenue could have positive effects on New Mexico's economy and include:
 - 1) lowering the tax burden on oil and gas producers;
 - 2) lowering taxes on other businesses and on New Mexico households; and
 - 3) spending the funds in some other way.
- Some states with oil and gas revenue make a direct distribution to households.

There was a discussion regarding the State Board of Finance's decision to give \$65 million to public schools. It was noted that the PSCOC certified the need for the funds to the State Board of Finance, which then directed the money to public schools. Members voiced concern over the process employed by the State Board of Finance and discussed whether that process usurps the powers and duties of the legislature to appropriate state funds. Some members requested information, including reports that detail the use of the funds.

Next, members discussed the impact of charter schools on the demand for public school capital outlay. Mr. Gorrell noted that charter schools have caused an increase in the demand for funds.

There was a discussion of a proposed senate joint memorial to study the impact of diverting money from the STPF. Some members expressed concern over the use of a memorial in lieu of actual legislation to achieve the intended study. Members discussed the issue and generally seemed in favor of a bill draft to address the issue. Senators Beffort and Munoz and Representatives Varela, Larrañaga and Saavedra all agreed to cosponsor legislation on the matter.

Before moving to the next agenda item, the committee, upon motion, voted without objection to approve the minutes from the committee's October 27, 2011 meeting.

Update on Education Trust Fund Investment Returns

Robert Watson, chair of the Education Trust Board, gave a presentation on the Education Trust Fund returns. He provided a handout highlighting the programs offered and their performance for the quarter ending September 30, 2011. Mr. Watson reminded the members that in 1997 the board began administering the Internal Revenue Service-approved 529 Plan, an education savings plan. When asked about the work of the board, Mr. Watson told the committee that the board has never had difficulty meeting a quorum and does everything necessary to provide public notice of its meetings. When questioned about the rating of the New

Mexico 529 Plan as an "F", Mr. Watson said he disagreed with the rating and he would rate the plan a "C+".

Mr. Watson noted that the board is in the process of hiring a new executive director and is also seeking his replacement as chair. He further said that the majority of the plans' assets are not held by New Mexico residents.

When asked about lawsuits related to the plan, Mr. Watson said that the Oppenheimer fund was over-leveraged. He said that the New Mexico 529 Plan got a good settlement and account holders would be receiving their payments as a result of the settlement shortly. When asked about other potential lawsuits, Mr. Watson said he does not know where the lawsuits are going. He added that he is suggesting that the board issue requests for proposals for at least five different account managers to manage the accounts.

Legislation Affecting the Educational Retirement Board (ERB) Proposed for Endorsement by the IPOC

Jan Goodwin, executive director, and MaryLou Cameron, chair, ERB, addressed the members regarding proposed legislation for the ERB. Ms. Goodwin began by telling members that the ERB had held several public meetings as part of its "Listening Tour" throughout the state. The meetings were intended to solicit public input regarding potential changes to the ERB statute affecting benefits and retirement qualifications.

Ms. Goodwin provided both a bill draft and an outlined proposal for changes recommended by the ERB. She explained that highlights of the proposed changes include a minimum retirement age of 55 years and a reduction in the cost-of-living adjustment (COLA) for all current, future and retired members. Additionally, the proposed changes would include a 10-year grandfathering provision providing a "safe harbor" for members set to meet retirement criteria within 10 years of the date the changes would become effective.

Members asked questions regarding the proposed changes and seemed concerned that the plan selected by the ERB was not one of the plans put forward to the public during the Listening Tour. Rather, the selected plan changes were offered to the ERB in late November 2011 by the New Mexico Association of Educational Retirees. Upon further questioning about the issue, Ms. Goodwin said that the provisions of the plan that were accepted by the ERB are consistent with the ERB membership input and other public input received by the ERB during the Listening Tour.

While all of the ERB's proposed retirement plan changes were not included in the bill draft before the committee, the ERB provided a detailed outline with the proposed changes, and the committee agreed to hear, review and vote on the proposal.

Legislation Affecting the SIC Proposed for the IPOC Endorsement

Senator Keller, Mr. Moise and Mr. Wollman presented legislative proposals for the committee's consideration. Among the proposals presented by the SIC was a bill to increase the

SIC's ability to invest in international equities. After discussion and questions from members, the committee endorsed several of the proposals, including:

- A bill to increase from 1% to 2% of the STPF allocation to the Small Business Investment Corporation (SBIC) and requiring that money allocated to the SBIC from the STPF that is not committed within three years of the allocation be returned to the STPF.
- A bill to change the membership of the SIC by replacing the elected officials with members appointed by those elected officials; removing the chief financial officer of a state institution of higher education; replacing the four members appointed by the New Mexico Legislative Council with one member each appointed by the president pro tempore of the senate, the minority floor leader of the senate, the speaker of the house of representatives and the minority floor leader of the house of representatives, all appointed with the advice and consent of the senate; and increasing from two to four the public members appointed by the governor, with the requirement that no more than two of the four be from the same political party. The bill also provides that the chair and the vice chair of the SIC be elected and changes the powers and duties of the SIC, the state investment officer and staff. Certain reporting deadlines are also changed by the bill.
- A joint resolution to amend Article 12, Section 7 of the Constitution of New Mexico to increase the standard of care exercised by the state investment officer in investing the Land Grant Permanent Funds and removing the constitutional limitation on investment of the funds in international securities, allowing that limitation to be set in statute by the legislature.
- A bill to impose a limit of 25% on the portion of the book value of the Land Grant Permanent Funds that may be invested in international equities at any single time. The bill would become effective upon the certification of the constitutional amendment discussed in the previous item, which would remove the constitutional limitation on international investing.

Legislation Affecting the ERB and the Public Employees Retirement Association (PERA)

Committee members held additional discussion regarding the ERB's proposed retirement plan changes and heard the final legislative proposals that would impact the PERA. Senator Munoz and Representative Stewart discussed possible legislative initiatives to enhance the solvency of the PERA. They were joined in the discussion by a panel of experts that included Kurt Weber, interim executive director, PERA, Daniel Ivey-Soto, executive director, New Mexico Clerks, LLC, Carter Bundy, legislative director, American Federation of State, County and Municipal Employees of New Mexico, Diego Arencon, president of Local 244, International Association of Firefighters, and Oscar Arevalo, fiscal services director from the Administrative Office of the Courts. A number of legislative drafts were reviewed and analyzed by the committee members. Some proposals were put forward for committee endorsement. Among them, the committee endorsed the following:

- A bill to amend the Judicial Retirement Act to provide that employer contributions to the judicial and magistrate retirement funds will come from the general fund and that the portion of civil docket and jury fees that have previously been deposited in the Judicial Retirement Fund be deposited instead in the general fund. This bill would also increase contributions to the Judicial Retirement Fund.
- A bill to allow retired PERA members to return to work temporarily as a precinct board members for a municipal election or an election covered by the Election Code without suspending their pension benefits.
- A memorial requesting the creation of a task force to evaluate the solvency of the municipal and state public safety members' retirement plans and to assess options and make recommendations to the IPOC no later than October 1, 2012 for changes in those plans in order to ensure their long-term solvency.
- A memorial requesting the PERA to assess options, recommend changes to its retirement plans to reduce unfunded retirement benefit liabilities, with a goal of bringing the ratio of fund assets to liabilities to 100% by 2041, and report the recommended changes to the appropriate interim committee by October 1, 2012.
- A bill to amend the Educational Retirement Act to establish a minimum retirement age of 55 for members retiring on or after July 1, 2022, to reduce the annual COLA for retirement annuity payments by 12.5% for existing and future retirees and to change member and employer contribution rates.

Other Legislation Proposed for the IPOC's Endorsement

The committee was provided with proposed legislation that would impact the State Treasurer's Office. Mark Valdes, deputy state treasurer, and Victor Vigil, deputy cash manager, State Treasurer's Office, described their proposed legislation to more clearly define the duties and responsibilities of the state treasurer with regard to receipt, payment and custody of state funds.

After a brief discussion, the committee voted to endorse a bill to clarify the duties and responsibilities of the state treasurer regarding the deposit and accounting of public money.

Having no further business, the committee adjourned at 4:55 p.m.