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F I S C A L   I M P A C T   R E P O R T

		ORIGINAL DATE	02/09/10		
SPONSOR	SFC	**LAST UPDATED**	02/17/10	**HB**	
SHORT TITLE	Changes to State Investment Bodies			**SB**	18, 218, 238/SFCS /aSFL#1/aHTRC
				ANALYST	White

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

	FY10	FY11	FY12	3 Year Total Cost	Recurring or Non-Rec	Fund Affected
Total	NFI	$0.1	$0.1	$0.1	Recurring	SIC Operating Fund

(Parenthesis ( ) Indicate Expenditure Decreases)

Duplicates HB 289

SOURCES OF INFORMATION

LFC Files

Responses Received On Original Bill From
Attorney General's Officer (AGO)
State Auditor's Office (SAO)
State Land Office (SLO)
Educational Retirement Board (ERB)
Public Employee's Retirement Association (PERA)
State Investment Council (SIC)

SUMMARY

Synopsis of HTRC Amendment

The HTRC amendment to the SFC substitute for Senate Bills 18, 218, and 238 removes various sections and inserts language in order to mirror House Bill 289. These changes eliminate the following provisions from the original SFC substitute.

- Removal of the Governor from the SIC, and allowing the SIC to independently elect its own chair.
- Implementation of mandatory attendance requirements for all state investment an pension boards.
- Amendment of the gift act to prohibit any ex-officio elected official member of a state pension/investment board or candidate for such an office from accepting "anything of a value of more then twenty-five dollars" as a campaign contribution from current contract holders or potential contract bidders.
- Inclusion of language relating to gifts and campaign contributions to State Investment

Council (SIC) members and staff. The additional language was intended to statutorily impose the same ethical standards on the SIC as the Educational Retirement Board (ERB) and the Public Employees Retirement Association (PERA).

- Elimination of the transfer of full hiring and firing powers and responsibilities with respect to the State Investment Office to the Council. Currently the agency has four exempt positions which answer directly to the Governor. The original SFC substitute would have taken the SIO's power to "make purchases, sales, exchanges, investments and reinvestments of the assets of all funds" away and place such power solely with the SIC. The SIC would also have been charged with ensuring that the money under its management be "at all times handled in the best interests of the state," while simultaneously taking that responsibility away from the SIO. The SIO's duties relative to hiring external investment managers and contracting with other state agencies to invest money on their behalf were also eliminated and transferred to the SIC in the original SFC substitute. The original SFC substitute also allowed the SIC to delegate such responsibilities and duties to the SIO at its discretion.
- All provisions relating to the Educational Retirement Board (ERB) and the Public Employees Retirement Association (PERA) were also eliminated by the amendment.
- Requiring the SIC to appoint the SIO "with the advice and consent of the Senate." Under the amended legislation power to appoint and remove the officer would still be transferred to the SIC from the Governor however.

The amendment also changes language related to the makeup of the council. The amended legislation would increase the number of members from 9 to 11, as opposed to 10 in the original SFC substitute. The amended legislation would also slightly decrease the number of Governor's appointees who serve on the council. The bill would accomplish this by:

- eliminating three public members appointed by the governor with the advice and consent of the Senate;
- eliminating the State Investment Officer (SIO) as a member of the council;
- allowing the Legislative Council to appoint four public members with the advice and consent of the Senate, no more than two of which may be from one political party; and
- adding 2 additional public members appointed by the Governor with the advice and consent of the Senate.

Synopsis of SFL Amendment #1

Senate Floor Amendment number one to the SFC substitute for Senate Bills 18, 218, and 238 inserts language relating to gifts and campaign contributions to State Investment Council (SIC) members and staff. The additional language is intended to statutorily impose the same ethical standards on the SIC as the Educational Retirement Board (ERB) and the Public Employees Retirement Association (PERA).

Synopsis of SFC Substitute

The Senate Finance Committee substitute for Senate Bills 18, 218, and 238 make various changes to the makeup and or investment procedures and responsibilities of the three largest state investment agencies; the State Investment Council (SIC), the Educational Retirement Board (ERB), and the Public Employee Retirement Association (PERA). The substitute restructures the membership of the SIC as follows:

- The substitute eliminates the SIO and three public members appointed by the Governor and the State Investment Officer (SIO) from the SIC.
- The substitute adds to the SIC:
    - One public member appointed by the Senate President Pro-Tempore with the advice and consent of the Senate,
    - One public member appointed by the Senate Minority Leader with the advice and consent of the Senate,
    - One public member appointed by the Speaker of the House with the advice and consent of the Senate,
    - One public member appointed by the House minority leader with the advice and consent of the Senate, and
    - three public members nominated by the Governor and approved by the other seven members with the advice and consent of the Senate.

The substitute also imposes an attendance requirement on SIC and ERB members determining that an absence at three consecutive meetings shall be grounds for removal from the council or in the case of ERB, notice of resignation. The substitute also requires all three investment boards to allow for public comment at each of their meetings. Additionally, SIC monthly investment reports would be required to be published monthly on both the Department of Finance and Administration (DFA) and legislative websites.

The substitute amends the gift act to prohibit any ex-officio elected official member of a state pension board or candidate for such an office from accepting "anything of a value of more then twenty-five dollars" as a campaign contribution from current contract holders or potential contract bidders.

The proposed legislation also requires the SIO to be appointed by a majority of the SIC with the advice and consent of the Senate instead of the Governor. The SIC would also be granted full hiring and firing powers and responsibilities with respect to the State Investment Office. Currently the agency has four exempt positions which answer directly to the Governor. The substitute also takes the SIO's power to "make purchases, sales, exchanges, investments and reinvestments of the assets of all funds" away and places such power solely with the SIC. The SIC is also charged with ensuring that the money under its management be "at all times handled in the best interests of the state," while simultaneously taking that responsibility away from the SIO. The SIO's duties relative to hiring external investment managers and contracting with other state agencies to invest money on their behalf are also eliminated and transferred to the SIC. However, the substitute does allow the SIC to delegate such responsibilities and duties to the SIO.

The substitute adds language to existing statute which explicitly identifies SIC, ERB, and PERA council/board members as fiduciaries for their respective funds. This language also explicitly identifies investment managers as fiduciaries.

The proposed legislation would also permit the investment agencies to contract with their own custodial bank. Currently the State Board of Finance (BOF) enters into one contract on behalf of all state investment agencies.

Lastly the substitute sets up alternative investment advisory committees at each agency if any separate alternative investment asset class exceeds ten percent of the respective fund's value.

The committees shall consist of five members each, one of which will be the SIO/Chief Investment Officer and four other members to be appointed by the full council or board. At least one member, but no more than two members, of the full council or board shall be a member of the advisory committee. The advisory committees are charged with making recommendations to the full council or board with respect to investment matters and decisions related to their respective alternative asset class.

FISCAL IMPLICATIONS

This legislation would create a minor impact on the SIC operating budget related to additional printing and administrative costs, as well as additional per-diem payments to the increased amount of public members. These additional costs are expected to be minimal.

The substitute may also have additional operating impact on SIC with regard to granting it the ability to RFP and contract with its own custodial bank. The agency's operating budget is currently not funded with any general fund appropriations, and thus this provision would have no direct general fund impact. Currently the State Board of Finance (BOF) contracts with one custodial bank on behalf of all state investment agencies. As BOF is currently in the process of awarding a new four-year custodial bank contract, it is unclear if and when these additional operating impacts will occur.

SIGNIFICANT ISSUES

Recently the state's investments have seen a great deal of turmoil both from a performance standpoint and a reputational standpoint. The proposed legislation addresses a few of these issues by proposing a number of different changes to the council's makeup and council member conduct requirements. Some of the proposals in the substitute are also included in an Independent Operating and Fiduciary Review (IOFR) performed by institutional investment advisor Ennis Knupp and Associates on behalf of the Legislative Council and State Board of Finance. However, there are a number of recommendations made in the IOFR which are not included in the amended legislation which were included in the original SFC substitute.

The amended substitute changes the governance of the SIC. The IOFR stated with respect to SIC that the Governor's current "amount of influence is greater than that of most other funds," and should be "balanced by including legislative appointees on the Council or increasing the number of ex-officio members who are not part of the executive branch." If the substitute were enacted, the Governor would still appoint more members than any other source and therefore the board would remain arguably unbalanced. Under the proposed legislation the makeup of the SIC would be such that:

- 5 of 11 members will be the Governor and direct Governor appointees,
- 4 of 11 members will be legislative appointees, and
- 2 of 11 members will be ex-officio elected officials.

If the proposed legislation is enacted, the Governor would remain chairman of the council. The IOFR performed by Ennis Knupp reported that national best practices are for council members to independently elect a chairman and vice-chairman from amongst themselves as opposed to having a de-facto chair set in statute.

Therefore if the amended legislation were enacted, the SIC would still be operating outside of national best practices and contradict numerous findings in the Ennis Knupp IOFR. This has the potential to create the risk that further turmoil and suspicion, from both a performance and reputational perspective, will continue to accompany these agencies at the potential cost of hundreds of millions of taxpayer and retiree dollars.

OTHER SUBSTANTIAL ISSUES

The substitute inserts new language into Subsection C of 6-8-3 NMSA 1978 explicitly stating that the member appointed as the CFO of a New Mexico higher education institution "shall serve at the pleasure of the governor." It is unclear why such language is either necessary or prudent given the findings of the Ennis Knupp IOFR.

WHAT WILL BE THE CONSEQUENCES OF NOT ENACTING THIS BILL

If the SFC substitute for Senate Bill 18, 218, and 238 is not enacted, state investment agencies could continue to statutorily operate outside the realm of national best practices.

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