

BILL ANALYSIS

C.S.H.B. 2731

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Pensions, Investments & Financial Services
Committee Report (Substituted)

BACKGROUND AND PURPOSE

According to the State Pension Review Board, more than two million retired government employees belong to the various public retirement systems in Texas. In recent years, the total unfunded liability in Texas public retirement systems has increased dramatically, and a significant percentage of the public pension funds are considered actuarially unsound, raising questions as to how well the public pension systems are managed. C.S.H.B. 2731 seeks to respond to these concerns by making several public policy changes that would address the sources of many of the problems surrounding public pensions in Texas.

RULEMAKING AUTHORITY

It is the committee's opinion that rulemaking authority is expressly granted to the State Pension Review Board in SECTIONS 1, 3, 5 and 7 of this bill.

ANALYSIS

C.S.H.B. 2731 amends the Government Code to require the State Pension Review Board to adopt rules and procedures for receiving and investigating a complaint against a person who provides management or investment services to a public retirement system alleging that the person violated or may have violated certain disclosure and filing requirements relating to potential conflicts of interest, certain prohibitions established under the bill's provisions, or a conflict of interest provision applicable under other law, or alleging that the person has been or may have been involved in criminal conduct relating to the services provided by the person to the system. The bill authorizes the board to refer a complaint to the attorney general for investigation and authorizes the attorney general to subpoena witnesses or books, records, or other documents relevant to such an investigation. The bill authorizes the attorney general, if as a result of an investigation the attorney general determines that a criminal offense has been committed, to refer the case to the appropriate law enforcement agency for prosecution.

C.S.H.B. 2731 authorizes the board, if a complaint is filed and the board determines it appropriate, to require a public retirement system to provide the board with a statement, not later than the 30th day after the date the system receives the request for a statement, detailing the system's method of selecting any person who provides the system with services relating to the management and investment of the system's assets. The bill exempts the Employees Retirement System of Texas, the Teacher Retirement System of Texas, the Texas County and District Retirement System, the Texas Municipal Retirement System, and the Judicial Retirement System of Texas Plan Two from this provision, provisions of the bill relating to required disclosure of certain potential conflicts of interest, and provisions of the bill relating to the submission of actuarial experience studies by a public retirement system to the board.

C.S.H.B. 2731 requires a member of the governing body of a public retirement system, an investment manager for a public retirement system appointed by contract, and any other person, including an investment consultant or advisor, providing services under contract to a public retirement system relating to the management and investment of the system's assets, to disclose,

not later than the 30th day after the date the person learns of the relationship, in writing to the public retirement system that the person or an immediate family member of the person, including the person's spouse, has a business, commercial, or other relationship that a reasonable person would find likely to diminish the person's independence of judgment in the performance of the person's responsibilities with respect to the management or investment of the system's assets, including a relationship in which the person or the person's immediate family member is employed by or participates in the management of a business entity or other organization receiving funds from the retirement system or owns or controls, directly or indirectly, an interest in a business entity or other organization receiving funds from the retirement system.

C.S.H.B. 2731 makes the failure by a member of a retirement system's governing body to disclose such a relationship a ground for removal from the governing body on which the person serves. The bill requires the board, if the board determines that such a person should be removed, to notify the appropriate appointing officer that a ground for removal exists. The bill makes the contract under which a person is appointed as an investment manager for a public retirement system or under which any other person provides management and investment services to the system voidable by the public retirement system if the person fails to disclose a relationship as required. The bill authorizes the retirement system's governing body to enter an order declaring the person ineligible to contract for business relating to the management or investment of the system's assets. The bill requires a person subject to the bill's disclosure requirements, at least annually on a date specified by the public retirement system, to file a statement with the system stating that the person is aware of the requirement to disclose material conflicts of interest and that the person is in compliance with the requirement.

C.S.H.B. 2731 requires the board, not later than January 1, 2012, to adopt rules relating to the types of relationships that must be disclosed and establishes that a person is not required to comply with the bill's provisions relating to the required disclosure of certain potential conflicts of interest before the 30th day after the date the board adopts rules required by that provision.

C.S.H.B. 2731 prohibits a member of the governing body of a public retirement system, an investment manager for a public retirement system appointed by contract, any other person, including an investment consultant or advisor, providing services under contract to a public retirement system relating to the management and investment of the system's assets, or a member of the immediate family of the person from accepting any benefit with an aggregate value in any calendar year of more than \$250 from any individual who enters into or seeks to enter into a contract with a public retirement system. The bill exempts from this prohibition food, lodging, and transportation related to attending a conference in Texas that is attended or expected to be attended by at least 50 individuals representing more than one public retirement system. The bill defines "benefit," for purposes of this prohibition, by reference to the Penal Code.

C.S.H.B. 2731 prohibits a public retirement system from knowingly employing or contracting with, either directly or indirectly, a former member of that governing body before the first anniversary of the date the individual ceased to be a member of the governing body.

C.S.H.B. 2731 makes a person who commits theft in relation to a service provided by the person to a public retirement system liable to the system for an administrative penalty in an amount not to exceed \$250,000 for each violation. The bill authorizes an action to be brought for such a violation regardless of whether a criminal conviction for theft has been sought or obtained against the person. The bill makes a person who commits a breach of the person's fiduciary duty in relation to a service provided by the person to a public retirement system liable to the system for an administrative penalty in an amount not to exceed \$500 for each violation or \$10,000 in the aggregate for all violations of a similar nature. The bill requires the amount of an administrative penalty imposed to be in an amount that is reasonably related to the harm to the public retirement system. The bill authorizes the attorney general to bring an action to recover the administrative penalty imposed. The bill establishes that the penalty is in addition to any other remedy provided by law. The bill defines "theft," for purposes of the provision relating to

an administrative penalty, by reference to the Penal Code.

C.S.H.B. 2731 decreases from \$100 million to \$10 million the minimum book value of the total assets of a public retirement system that makes such a retirement system subject to a statutory provision requiring periodic audits by an independent actuary of the system's most recently prepared actuarial valuations, studies, and reports. The bill limits the requirement for a quinquennial audit, by an independent actuary who meets certain criteria, of the actuarial valuations, studies, and reports of a public retirement system to a system with total assets the book value of which, as of the last day of the preceding fiscal year, is at least \$50 million. The bill authorizes the board, each calendar year, to select five public retirement systems with total assets the book value of which, as of the last day of the fiscal year, is at least \$10 million but not more than \$50 million, to complete such an audit. The bill authorizes the board, if a retirement system is unable to employ an independent actuary for purposes of completing the audit, to provide the service for a fee in an amount determined by the board. The bill makes a conforming change.

C.S.H.B. 2731 authorizes the board, no more than once every five years, to require a public retirement system with total assets the book value of which, as of the last day of the preceding plan year, is at least \$50 million to conduct and submit to the board an actuarial experience study. The bill authorizes the board to adopt rules to implement this provision and defines "plan year" for purposes of this provision.

C.S.H.B. 2731 requires the board, if the governing body of a public retirement system fails to file an annual financial report before the 10th business day after the final date by which the retirement system is required to file the report, to notify appropriate local media outlets before the fifth business day after that date. The bill requires the board, if, after local media outlets are notified of such a failure, the retirement system files the report or the board discovers that the board notified local media outlets by mistake, to notify the local media outlets not later than the fifth business day after that date of the receipt of the report or the discovery of its mistake. The bill requires the governing body of a public retirement system to require that all records, including the work papers involved in the preparation of the annual financial report, be retained in compliance with the records retention schedule adopted by the Texas State Library and Archives Commission applicable to all local governments.

EFFECTIVE DATE

September 1, 2011.

COMPARISON OF ORIGINAL AND SUBSTITUTE

C.S.H.B. 2731 differs from the original by requiring the State Pension Review Board to adopt rules and procedures for receiving certain complaints against a person who provides management or investment services to a public retirement system, whereas the original requires the board to adopt rules and procedures for receiving and investigating such complaints.

C.S.H.B. 2731 differs from the original by authorizing the board to refer a complaint to the attorney general for investigation, whereas the original authorizes the board or the attorney general to initiate an investigation if the board or the attorney general determines an investigation is appropriate.

C.S.H.B. 2731 omits a provision included in the original authorizing the board to enter into a memorandum of understanding with the attorney general to assist in an investigation and requiring the memorandum to specify the type, scope, and format of the investigative assistance provided by the attorney general.

C.S.H.B. 2731 differs from the original by authorizing the attorney general, if after an

investigation the attorney general determines that a criminal offense has been committed, to refer the case to the appropriate law enforcement agency for prosecution, whereas the original requires the board or the attorney general, if after an investigation the board or the attorney general determines that a criminal offense may have been committed, to make such a referral.

C.S.H.B. 2731 contains provisions not included in the original authorizing the board, if a complaint is filed and the board determines it appropriate, to require a public retirement system to provide the board with a statement detailing the system's method of selecting a person to provide asset management and investment services. The substitute contains provisions not included in the original exempting certain public retirement systems from this provision and the substitute's provisions for required disclosure of certain potential conflicts of interest and provisions for actuarial experience studies.

C.S.H.B. 2731 differs from the original, in a provision requiring disclosure to a public retirement system of a business, commercial, or other relationship that has the potential to diminish a person's independence in performing the person's duties with respect to the system's assets, by requiring that disclosure not later than the 30th day after the date the person learns of the relationship, whereas the original requires immediate disclosure.

C.S.H.B. 2731 contains provisions not included in the original requiring the board, if the board determines that a person should be removed from a position in a public retirement system, to notify the appropriate appointing officer that a ground for removal exists, and requiring the board to adopt rules relating to the types of relationships that must be disclosed.

C.S.H.B. 2731 differs from the original by prohibiting certain individuals and immediate family members from accepting any benefit with an aggregate value in any calendar year of more than \$250 from any individual who enters into or seeks to enter into a contract with a public retirement system and exempting food, lodging, and transportation related to attending a conference in Texas pertaining to public retirement systems from the prohibition, whereas the original prohibits a member of a public retirement system's governing body from accepting a gift, service, or other thing of value, including food, entertainment, and a promised future benefit, from another person doing business with or seeking to do business with the system. The substitute contains a provision not included in the original defining "benefit" for purposes of the prohibition.

C.S.H.B. 2731 differs from the original by prohibiting a public retirement system from knowingly employing or contracting with a former member of that governing body before the first anniversary of the date of the individual's departure from the governing body, whereas the original prohibits such employment or contracting before the second anniversary and does not specify that such employment or contracting is done knowingly.

C.S.H.B. 2731 differs from the original by making a person who commits theft in relation to a service provided to a public retirement system liable to the system for an administrative penalty, whereas the original makes a person who commits a breach of the person's fiduciary duty, fraud, theft, embezzlement, fraudulent conversion, unlawful appropriation, or misapplication of property in relation to such service liable to the state for a civil penalty. The bill contains provisions not included in the original authorizing an action to be brought for such a violation regardless of whether a criminal conviction for theft has been sought or obtained against the person; making a person who commits a breach of the person's fiduciary duty liable to the system for an administrative penalty in an amount not to exceed \$500 for each violation or \$10,000 in the aggregate for all violations of a similar nature; and requiring the amount of an administrative penalty to be reasonably related to the harm to the public retirement system. The substitute differs from the original by authorizing the attorney general to bring an action to recover an administrative penalty allowed by these provisions, whereas the original authorizes an action to recover a civil penalty imposed under these provisions. The substitute contains a provision not included in the original defining "theft" for purposes of the bill's provisions

relating to an administrative penalty.

C.S.H.B. 2731 omits provisions included in the original relating to computation of retirement benefits and relating to assumptions and methods used as the basis for a valuation of a public retirement system's assets and liabilities made by an actuary employed by the governing body of a public retirement system.

C.S.H.B. 2731 contains provisions not included in the original limiting a required quinquennial audit of the actuarial valuations, studies, and reports of a public retirement system to a system with total assets the book value of which is at least \$50 million; authorizing the board, each year, to select five public retirement systems with total assets of at least \$10 million but not more than \$50 million to complete such an audit; and authorizing the board, if a retirement system is unable to employ an independent actuary to complete the audit, to provide the service for a fee. The substitute differs from the original by making a conforming change related to these provisions.

C.S.H.B. 2731 contains provisions not included in the original relating to the submission of actuarial experiences studies to the board and omits provisions included in the original relating to requirements for making changes in contribution rates or benefit increases.

C.S.H.B. 2731 differs from the original by requiring the board, if the governing body of a public retirement system fails to file an annual financial report by the specified deadline, to notify local media outlets and requiring the board to notify the local media if the report is received or the board discovers it was mistaken about the failure to file, whereas the original authorizes the board, if the governing body of a public retirement system fails to file the annual financial report with the board within the prescribed time, to impose an administrative penalty in the amount of \$50 against each member of the governing body and the executive director or other person selected by the board of trustees to manage or administer the system.

C.S.H.B. 2731 differs from the original by requiring the governing body of a public retirement system to require that all records be retained in compliance with the records retention schedule adopted by the Texas State Library and Archives Commission applicable to all local governments, whereas the original requires the records to be retained for at least six years after the date the report is filed and to be made available to the board on request.

C.S.H.B. 2731 omits provisions included in the original relating to procurement of investment managers and other persons and contracts with investment managers and other persons and omits a saving provision included in the original.

C.S.H.B. 2731 contains provisions not included in the original requiring the board to adopt rules required by the bill's provision relating to disclosure of certain potential conflicts of interest not later than January 1, 2012, and establishing that a person is not required to comply with that provision of the bill before the 30th day after the date the board adopts the required rules.