

GENERAL ASSEMBLY OF NORTH CAROLINA  
SESSION 2013

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HOUSE BILL 1209  
Committee Substitute Favorable 6/18/14

Short Title: Retirement Investment Accountability.

(Public)

Sponsors:

Referred to:

May 28, 2014

A BILL TO BE ENTITLED

AN ACT TO ENHANCE THE ACCOUNTABILITY AND TRANSPARENCY OF THE STATE RETIREMENT SYSTEMS' INVESTMENT PROGRAMS BY PROVIDING FOR AUDITED FINANCIAL STATEMENTS, PERFORMANCE REVIEWS, EXPANDED AND MODERNIZED REPORTING, A SUNSET ON THE CONFIDENTIALITY OF PROPRIETARY INFORMATION, RESOURCE FLEXIBILITY FOR THE INVESTMENT MANAGEMENT DIVISION, AND OTHER MEASURES.

The General Assembly of North Carolina enacts:

**SECTION 1.(a)** Article 6 of Chapter 147 of the General Statutes is amended by adding a new section to read:

**"§ 147-69.9. Third-party audit of Retirement Systems' investment programs.**

(a) In addition to all other audits and reports required by law, the State Treasurer shall prepare and issue, as of the end of each fiscal year, a set of financial statements regarding the investment programs for the Retirement Systems enumerated in G.S. 147-69.2(b)(8). These financial statements shall be audited by a commercial, independent third-party audit firm selected and engaged by the State Auditor based upon selection criteria developed by the State Auditor in consultation with the State Treasurer. The audit firm's report and the financial statements shall be provided to the General Assembly within six months after the close of the reporting period.

(b) Supplementary information accompanying the financial statements required by subsection (a) of this section shall include a discussion of the Retirement Systems' risk and returns compared to benchmarks, total management fees and incentives paid, and comparisons to peer cost benchmarks.

(c) Any associated costs of the audit required by this section shall be subject to the provisions of G.S. 147-69.3(f) and do not require appropriations to either the State Auditor or the State Treasurer in the Current Operations Appropriations Act."

**SECTION 1.(b)** This section becomes effective for audits and reports relating to the 2014-2015 fiscal year. For the 2014-2015 fiscal year, the requirements stated by subsection (a) of this section shall be met by an independent review of the Retirement Systems' pro forma financial statements. For the 2015-2016 fiscal year and thereafter, the audit requirement stated by this section shall take the form of an independent opinion concerning the Retirement Systems' initial financial statements. In order to allow for an opinion to be offered for the 2015-2016 fiscal year, the State Auditor shall select an audit firm no later than January 1, 2015, and, by June 30, 2015, the Treasurer shall separately account for any Retirement Systems' investment portfolios that are commingled with the Treasurer's other investment programs.



1           **SECTION 2.** Article 6 of Chapter 147 of the General Statutes is amended by  
2 adding a new section to read:

3 **"§ 147-69.10. Performance review of Treasurer's investment programs.**

4           At least once every four years, the State Treasurer shall engage a commercial, independent  
5 expert firm pursuant to G.S. 147-69.3(g) to evaluate the governance, operations, and  
6 investment practices of the State Treasurer in order to develop recommendations for  
7 improvement. The report of the expert firm shall be provided to the General Assembly when  
8 complete."

9           **SECTION 3.(a)** Article 6 of Chapter 147 of the General Statutes is amended by  
10 adding a new section to read:

11 **"§ 147-69.11. Reporting of Retirement Systems' investments.**

12           (a) Definitions. – The following definitions apply in this section:

- 13           (1) External investment manager. – The State Treasurer's counterparty or its  
14 affiliate given authority or discretion to make investment decisions  
15 concerning the investments that are not managed internally by the State  
16 Treasurer's staff.
- 17           (2) Incentive fees. – Any incentive compensation to an investment manager or  
18 investment vehicle that the Retirement Systems incur directly or experience  
19 indirectly as a reduction in distributions.
- 20           (3) Investment vehicle. – A limited partnership, limited liability company, trust,  
21 or other legal entity through which the State Treasurer invests.
- 22           (4) Management fees. – Compensation other than incentive fees paid to the  
23 investment manager or investment vehicle to compensate it for its  
24 management of funds that the Retirement Systems incur directly or  
25 experience indirectly as a reduction in distributions.

26           (b) In addition to all other reports required by law, the State Treasurer shall prepare and  
27 make public a report on the fees and performance of external investment managers engaged for  
28 the Retirement Systems enumerated in G.S. 147-69.2(b)(8) as of the end of each fiscal year. A  
29 copy of each report shall be submitted within nine months following the end of the fiscal year  
30 to the State Auditor, the Joint Legislative Commission on Governmental Operations, the Chairs  
31 of the House of Representatives Appropriations Subcommittee and Senate Appropriations  
32 Committee, the Chairs of the House of Representatives and Senate Finance Committees, and  
33 the Fiscal Research Division.

34           (c) The State Treasurer's report shall include all of the following that are applicable,  
35 reported separately for each investment:

- 36           (1) The name, commitment amount, statutory classification, inception year, and,  
37 as applicable, either a statement that the investment is managed internally by  
38 the staff of the State Treasurer or the names of the external investment  
39 manager and the investment vehicle for that investment.
- 40           (2) The value of the State Treasurer's investment as of the fiscal year end.
- 41           (3) For each investment made pursuant to subdivisions (1) through (6) of  
42 G.S. 147-69.2(b) or sub-subdivisions a. and c. of G.S. 147-69.2(b)(8), the  
43 periodic net annualized time-weighted rate of return for that fiscal year and,  
44 since inception, reported net of fees.
- 45           (4) For each investment other than those described in subdivision (3) of this  
46 subsection, the net annualized internal rate of return and investment multiple  
47 for that fiscal year and, since inception, reported net of fees.
- 48           (5) For each investment other than those described in subdivision (3) of this  
49 subsection, the total cash contributions or other investments made and the  
50 total distribution received with respect to that investment for that fiscal year  
51 and since inception.

- 1           (6)   The dollar amount of the management fees and incentive fees incurred by  
2           the State Treasurer and paid to the external investment manager.  
3           (7)   For any fund-of-fund investment vehicles, the aggregate management fees  
4           and incentive fees for the underlying investment managers or investment  
5           vehicles used by the external investment manager.  
6           (8)   If any placement agent fees relating to the investment were directly or  
7           indirectly borne by the Retirement Systems, a list of the amount and type of  
8           those fees.

9           Portfolios of investments managed internally by the staff of the State Treasurer shall be  
10          reported on a portfolio-by-portfolio basis."

11           **SECTION 3.(b)** Chapter 132 of the General Statutes is amended by adding a new  
12 section to read:

13          "§ 132-1.14. Public records for Treasurer's investment programs.

14           (a)   Definitions. – The following definitions apply in this section:

- 15           (1)   External investment manager. – The State Treasurer's counterparty or its  
16           affiliate given authority or discretion to make investment decisions  
17           concerning Treasurer investments that are not managed internally by the  
18           State Treasurer's staff.  
19           (2)   Incentive fees. – Any incentive compensation to an investment manager or  
20           investment vehicle that the Retirement Systems incur directly or experience  
21           indirectly as a reduction in distributions.  
22           (3)   Investment vehicle. – A limited partnership, limited liability company, trust,  
23           or other legal entity through which the State Treasurer invests.  
24           (4)   Management fees. – Compensation other than incentive fees paid to the  
25           investment manager or investment vehicle to compensate it for its  
26           management of funds that the Retirement Systems incur directly or  
27           experience indirectly as a reduction in distributions.  
28           (5)   Person. – An individual, corporation, business trust, partnership, association,  
29           joint venture, or any other legal or commercial entity.  
30           (6)   Treasurer investment. – An investment for one or more of the investment  
31           programs established, managed, or operated by the State Treasurer pursuant  
32           to G.S. 147-69.3.

33           (b)   Notwithstanding G.S. 132-1.2(1) and subsection (d) of this section, all of the  
34          following information is a public record for each Treasurer investment:

- 35           (1)   The name, commitment amount, statutory classification, inception year, and,  
36           if applicable, the names of the external investment manager and the  
37           investment vehicle for that investment.  
38           (2)   The value of the State Treasurer's investment as of the fiscal year end.  
39           (3)   For each investment made pursuant to subdivisions (1) through (6) of  
40           G.S. 147-69.2(b) or sub-subdivisions a. and c. of G.S. 147-69.2(b)(8), the  
41           periodic net annualized time-weighted rate of return for that fiscal year and,  
42           since inception, reported net of fees.  
43           (4)   For each investment other than those described in subdivision (3) of this  
44           subsection, the net annualized internal rate of return and investment multiple  
45           for that fiscal year and, since inception, reported net of fees.  
46           (5)   For each investment other than those described in subdivision (3) of this  
47           subsection, the total cash contributions or other investments made and the  
48           total distribution received with respect to that investment for that fiscal year  
49           and since inception.  
50           (6)   The dollar amount of the management fees and incentive fees incurred by  
51           the State Treasurer to the external investment manager.

1           (7) For any fund-of-fund investment vehicles, the aggregate management fees  
2           and incentive fees for the underlying investment managers or investment  
3           vehicles used by the external investment manager.

4           (8) If any placement agent fees relating to the investment were directly or  
5           indirectly borne by the Retirement Systems, a list of the amount and type of  
6           those fees.

7           (c) In order to prevent other investment traders from utilizing knowledge of potential or  
8           pending Treasurer investment trades for personal gain, all records relating to trades made  
9           directly by the staff of the State Treasurer pursuant to G.S. 147-69.2(b)(6b) or the second  
10           paragraph of G.S. 147-69.2(b)(8) are not public record until 90 days after the transaction has  
11           closed.

12           (d) The following information shall not be public record until five years after the  
13           termination of an investment vehicle in which the State Treasurer has made a Treasurer  
14           investment and then shall become public record on that date:

15           (1) Information regarding the portfolio positions in which the investment  
16           vehicle invests.

17           (2) Capital call and distribution notices to investors of the investment vehicle.

18           (3) Information concerning other investors in the investment vehicle.

19           (4) The investment's private placement memorandum and other offering and  
20           marketing material, if marked confidential.

21           (5) The investment's contractual documents, to the extent stated in any clause  
22           that places a duty of confidentiality upon the State Treasurer.

23           (6) Any other information that constitutes a "trade secret" as defined in  
24           G.S. 66-152(3) and that was disclosed or furnished by an actual or potential  
25           external investment manager in connection with an actual or potential  
26           Treasurer investment."

27           **SECTION 4.(a)** G.S. 147-69.3(f) reads as rewritten:

28           "(f) The cost of administration, management, and operation of investment programs  
29           established pursuant to this section shall be apportioned equitably among the programs in such  
30           manner as may be prescribed by the State Treasurer, such costs to be paid from each program,  
31           and to the extent not otherwise chargeable directly to the income or assets of the specific  
32           investment program or pooled investment vehicle, shall be deposited with the State Treasurer  
33           as a General Fund nontax revenue program. The cost of administration, management, and  
34           operation of investment programs established pursuant to this section ~~and not directly paid~~  
35           ~~from the income or assets of such program shall be covered by an appropriation to the State~~  
36           ~~Treasurer for this purpose in the Current Operations Appropriations Act shall be reported to the~~  
37           General Assembly by June 15 of each year, providing the actual costs incurred for the previous  
38           fiscal year, the estimated costs for the current fiscal year, and the estimated costs for the next  
39           fiscal year."

40           **SECTION 4.(b)** G.S. 147-69.3 is amended by adding a new subsection to read:

41           "(g1) The State Treasurer is authorized to appoint employees possessing specialized skills  
42           or knowledge necessary for the proper administration of investment programs created pursuant  
43           to this section. Notwithstanding the restrictions on the establishment of new employment  
44           positions contained in G.S. 143C-6-6(a), the State Treasurer may create those positions  
45           authorized under this subsection solely in the interest of the beneficiaries of the various  
46           investments authorized under G.S. 147-69.1 and G.S. 147-69.2, incurring only costs that are  
47           appropriate and reasonable."

48           **SECTION 4.(c)** G.S. 147-69.3(i2) reads as rewritten:

49           "(i2) In order to promote achievement of long-term investment objectives and to retain  
50           key public employees in the Investment Division, with investment functions, the State Treasurer  
51           is authorized to establish market-oriented compensation plans, including bonuses for the Chief

1 ~~Investment Officer and Investment Directors~~ salaries and performance-related bonuses, for  
2 ~~employees possessing specialized skills or knowledge necessary for the proper administration~~  
3 ~~of investment programs, who shall be exempt from the classification and compensation rules~~  
4 ~~established by the Office of State Human Resources. The bonuses may design and~~  
5 ~~administration of those compensation plans shall be based on compensation studies conducted~~  
6 ~~by a nationally recognized firm specializing in public fund investment compensation and the~~  
7 ~~Pension Plan performance compensation. The salaries compensation and other associated~~  
8 ~~employee benefits shall be apportioned directly from the investment program. The Treasurer~~  
9 ~~shall report the salaries and bonuses paid to the Joint Legislative Commission on Governmental~~  
10 ~~Operations annually."~~

11 **SECTION 4.(d)** G.S. 126-5 is amended by adding a new subsection to read:

12 "(c12) Except as to G.S. 126-13, 126-14, 126-14.1, and the provisions of Articles 6, 7, 14,  
13 15, and 16 of this Chapter, the provisions of this Chapter shall not apply to employees of the  
14 Department of State Treasurer possessing specialized skills or knowledge necessary for the  
15 proper administration of investment programs and appointed pursuant to G.S. 147-69.3(g1) or  
16 compensated pursuant to G.S. 147-69.3(i2)."

17 **SECTION 5.(a)** G.S. 147-69.3 is amended by adding a new subsection to read:

18 "(h1) The State Treasurer shall adopt, publish, and regularly review investment policy  
19 statements for each investment program created pursuant to this section. The investment policy  
20 statements shall include, but are not limited to, descriptions of investment objectives, roles, and  
21 responsibilities, permitted types of investments, risk management and control activities,  
22 implementation guidelines, and evaluation criteria necessary to measure investment  
23 performance of the applicable funds."

24 **SECTION 5.(b)** G.S. 147-69.3(i) reads as rewritten:

25 "(i) The State Treasurer shall report at least twice a year to the General Assembly,  
26 through the Finance Committees of the House of Representatives and the Senate, on the  
27 investment programs created under this section. The Treasurer shall present the reports to a  
28 joint meeting of the Finance Committees. The chairs of the Finance Committees may receive  
29 the reports and call the meetings. The Finance Committees may meet during the interim as  
30 necessary to hear the reports from the State Treasurer. The State Treasurer's report and  
31 presentation to the Finance Committees shall include all of the following:

- 32 (1) A full and complete statement of all moneys invested by virtue of the  
33 provisions of G.S. 147-69.1 and G.S. 147-69.2.
- 34 (2) The nature and character of the investments.
- 35 (3) The revenues derived from the investments.
- 36 (4) The costs of administering, managing, and operating the investment  
37 programs, including the recapture of any investment commissions.
- 38 (5) ~~A statements~~summary of the investment policies for the revenues invested.
- 39 (6) Any other information that may be helpful in understanding the State  
40 Treasurer's investment policies and investment results.
- 41 (7) Any other information requested by the Finance Committees."

42 **SECTION 6.** G.S. 147-69.3(j) reads as rewritten:

43 "(j) Subject to the provisions of G.S. 147-69.1(d), the State Treasurer ~~shall~~ may adopt  
44 any rules necessary to establish, operate, conduct, and carry out the provisions of all activities  
45 related to the investment programs established pursuant to this section."

46 **SECTION 7.(a)** G.S. 128-29.1 is repealed.

47 **SECTION 7.(b)** G.S. 147-69.2(b) reads as rewritten:

48 "(b) It shall be the duty of the State Treasurer to invest the cash of the funds enumerated  
49 in subsection (a) of this section in excess of the amount required to meet the current needs and  
50 demands on such funds. The State Treasurer may invest the funds as provided in this  
51 subsection. If an investment was authorized by this subsection at the time the investment was

1 made or contractually committed to be made, then that investment shall continue to be  
2 authorized by this subsection, and none of the percentage or other limitation on investments set  
3 forth in this subsection shall be construed to require the State Treasurer to subsequently dispose  
4 of the investment or fail to honor any contractual commitments as a result of changes in market  
5 values, ratings, or other investment qualifications. For purposes of computing market values on  
6 which percentage limitations on investments in this subsection are based, all investments shall  
7 be valued as of the last date of the most recent fiscal quarter.

8 (1) Investments authorized by G.S. 147-69.1(c)(1)-(7).

9 (2) General obligations of other states of the United States.

10 (3) General obligations of cities, counties and special districts in North Carolina.

11 (4) Obligations of any company, other organization or legal entity incorporated  
12 or otherwise created or located within or outside the United States, including  
13 obligations that are convertible into equity securities, if the obligations bear  
14 one of the four highest ratings of at least one nationally recognized rating  
15 service when acquired.

16 (5) Repealed by Session Laws 2001-444, s. 2, effective October 1, 2001.

17 (6) Asset-backed securities (whether considered debt or equity) provided they  
18 bear ratings by nationally recognized rating services as provided in  
19 G.S. 147-69.2(b)(4).

20 (6a) In addition to the limitations and requirements with respect to the  
21 investments of the Retirement Systems set forth in this subsection, the State  
22 Treasurer shall select investments of the assets of the Retirement Systems  
23 such that investments made pursuant to subdivisions (b)(1) through (6) of  
24 this section shall at all times equal or exceed twenty percent (20%) of the  
25 market value of all invested assets of the Retirement Systems.

26 (6b) Investments pursuant to subdivisions (b)(1) through (6) of this section may  
27 be made directly by the State ~~Treasurer~~Treasurer, through investment  
28 companies registered under the Investment Company Act of 1940,  
29 individual, common, or collective trust funds of banks and trust companies,  
30 group trusts and limited partnerships, limited liability companies or other  
31 limited liability investment vehicles that invest primarily in investments  
32 authorized by subdivisions (1) through (6) of this subsection, or through  
33 contractual arrangements in which the investment manager has full and  
34 complete discretion and authority to invest assets specified in such  
35 arrangements in investments authorized by subdivisions (b)(1) through (6) of  
36 this section, provided for each indirect investment, the investment manager  
37 has assets under management of at least one hundred million dollars  
38 (\$100,000,000).

39 "...."

40 **SECTION 8.** Section 1 of this act becomes effective July 1, 2014, and applies as  
41 provided in Section 1(b) of this act. Section 3 of this act becomes effective July 1, 2014, and  
42 the reporting requirements required by that section apply to the reports for the 2013-2014 fiscal  
43 year. Section 5 of this act becomes effective July 1, 2014, for the Retirement Systems  
44 enumerated in G.S. 147-69.2(b)(8) and becomes effective July 1, 2015, for the other investment  
45 programs created pursuant to G.S. 147-69.3. The remainder of this act becomes effective July  
46 1, 2014.