

# **Local Retirement Fund Investment Study Group**

Office of the State Auditor

Tuesday, August 31, 2010

2 p.m. to 4 p.m.

## **Members Present**

Howard Bicker, Minnesota State Board of Investment Executive Director

Edward Burek, Legislative Commission on Pensions and Retirement Deputy Director

Bruce Duncan, Excelsior Fire Relief Association President

Dave Ganfield, Apple Valley Fire Relief Association Administrator

Dave Matlon, Bloomington Fire Relief Association Treasurer

Rebecca Otto, State Auditor

Teri Richardson, Minnesota State Board of Investment Assistant Executive Director

J. Michael Stoffel, Duluth Teachers' Retirement Fund Association Executive Director

Gene Waschbusch, St. Paul Teachers' Retirement Fund Association Secretary-Treasurer

## **Members Excused**

Nyle Zikmund, Spring Lake Park, Blaine & Mounds View Fire Department Chief

## **Others Present**

Colleen Bollom, Minnesota Firefighter Pension Consultants Representative

Aaron Casper, National Insurance Services Representative

Aaron Dahl, Pension Analyst

Celeste Grant, Deputy State Auditor/General Counsel

Rose Hennessy Allen, Pension Director

Lucas Hinz, Pension Analyst

Jim Jensen, Pension Intern

David Kenney, Assistant Legal Counsel

Luke Kuhl, House Research Consultant

Brian McKnight, Wells Fargo Advisors Representative

Brian Rice, Minneapolis Police and Fire Relief Associations Representative

John Schutz, Wells Fargo Representative

Merle Waters, Wells Fargo Representative

The following motion was duly made, seconded and approved:

**RESOLVED** to require consent by a majority of Study Group members for proposals to move forward, although proposals and dissenting views that don't receive majority consent may be included in the Group's report.

**I. Call to Order**

Chair Auditor Otto called the meeting to order.

**II. Introductions**

The Study Group members and others that were present introduced themselves and identified the organization that they were representing.

**III. Study Group Purpose and Process Discussion**

Auditor Otto explained that all local retirement fund stakeholders were invited to participate on the Investment Study Group. Representatives from some funds are unable to attend the meetings, but will be receiving meeting materials and information via e-mail and have opportunities to share their thoughts. The members reviewed the purpose of the Study Group and noted that the Group is required to prepare a report to assess the effectiveness of current statutory prescriptions, options for change, and recommendations for consideration by the governor and the legislature during the 2011 legislative session.

The members also discussed the process for Study Group meetings. Auditor Otto suggested that consent by a majority of Study Group members be required for proposals to move forward, although proposals and dissenting views that don't receive majority consent could be included in the report. Bicker made a motion to adopt this process proposal. Stoffel seconded the motion, which was adopted unanimously.

The members reviewed the meeting schedule. Auditor Otto said that additional work will be conducted between meetings and additional meetings may be scheduled if necessary.

The members reviewed their contact information on the Investment Study Group membership list and confirmed that no changes were needed.

**IV. Discussion of Survey Results**

A survey was conducted before this first Investment Study Group meeting to gather feedback from the various stakeholders. A summary of the survey results was provided to the members. A list of the topic suggestions and survey comments were also provided, and discussed in detail by the Study Group. Some suggestions were technical, like cleaning-up outdated language and correcting statutory references. Other suggestions were substantive. Substantive suggestions included:

- Comparison of the Expanded List to SBI's Investment Authority  
Members of the Study Group expressed a desire that the expanded list of authorized investment securities found under Minn. Stat. § 356A.06, subd. 7, be updated to mirror the State Board of Investment (SBI)'s investment authority found under Minn. Stat. § 11A.24. Members representing the larger local pension plans stated that their investment returns are often compared to the SBI's investment returns, which isn't a fair comparison if the plans don't have the same investment authority. Burek explained the history of why separate lists were

created and that the two lists are still very similar. The members agreed to the concept of keeping separate lists for the SBI and for the larger local pension plans, but updating the expanded list for the local plans to mirror SBI's investment authority. Burek will work with the Revisor of Statute's Office to get a side-by-side comparison of the two lists. The Study Group agreed to review the comparison when it's available and decide which language from each list should be updated.

- **Prudent Person versus Prudent Expert Standard**

The members discussed a survey suggestion to hold executive directors of the large local retirement funds to the prudent expert standard, rather than the prudent person standard. The Study Group agreed not to pursue a change, as a prudent expert requirement would add significant cost to the funds.

- **Exchange Traded Funds**

The members discussed a survey suggestion to authorize exchange traded funds that invest in "other investments." Pension plans investing under the expanded list have authority to invest in exchange traded funds that are subject to the maximums, requirements, and limitations set forth in paragraphs (c) to (i) of the expanded list. "Other investments" are authorized under paragraph (k) of the list. An expansion of the exchange traded fund investment authority would be easy to do from a drafting perspective, but some members of the Study Group were concerned that an expansion would allow plans to invest in exotic or risky investments. The members agreed to revisit this topic at a future meeting.

The Study Group also discussed a survey suggestion to allow leveraged exchange traded funds. The members agreed not to pursue this topic as the investments were viewed as risky and seeking to authorize them would be controversial with the legislature at this time.

- **Mutual Funds**

The members agreed that the various mutual fund provisions need to be simplified. Auditor Otto said that the Office of the State Auditor would work on drafting simplified mutual fund language for the Study Group to review.

The Study Group also discussed restricting mutual fund investment authority so that pension plans can't invest in funds that sell short or are ultra-short funds. The members agreed to the concept of limiting these types of investments for small volunteer fire relief associations, but to consider authorizing the investments for the large local pension plans. One suggestion was to add a section to the expanded list that would authorize leveraged investments, up to a certain percent of the market value of the plan's portfolio. This topic will be revisited at a future meeting.

- **Limited List Investments**

The members discussed a survey suggestion to allow limited list plans to invest in debt investments that are within the top four, rather than top three, quality categories since they are all investment-grade debt. The members agreed to pursue this change.

- **Hedge Funds**

The Study Group discussed a survey suggestion to authorize hedge funds under certain conditions. Bicker expressed his reservations about hedge funds and cautioned the Study Group to proceed cautiously if pursuing a change. The members acknowledged that most likely none of the local pension plans would have enough money to invest in hedge funds directly. Some members were interested in authorizing hedge fund of funds investments. These types of investments may be less volatile, but may also have high fees. Other members shared their opinion that the Study Group should let some time pass to see how these types of investments perform before authorizing them. Cutting-edge investments may prove successful for a few years, but don't always perform well over time. The members agreed to revisit this topic at a future meeting.

**V. Review of Investment Provisions**

A review of the investment provisions was conducted in conjunction with the Study Group's discussion of the survey results and topic suggestions.

**VI. Other Business**

There was no other business.

**VII. Next Meeting**

Thursday, September 9, 2010  
2 p.m. to 4 p.m.  
Office of the State Auditor

**VIII. Adjournment**

Waschbusch made a motion to adjourn the meeting shortly after 4:00. Duncan seconded the motion that was adopted unanimously.