SENATE, No. 3473

STATE OF NEW JERSEY
217th LEGISLATURE

INTRODUCED NOVEMBER 9, 2017

Sponsored by:
Senator BOB SMITH
District 17 (Middlesex and Somerset)

SYNOPSIS
Restricts compensation of external managers authorized to invest assets of
State pension or annuity funds and requires disclosure thereof.

CURRENT VERSION OF TEXT
As introduced.
AN ACT restricting the compensation of external managers authorized to invest assets of State pension or annuity funds and requires disclosure thereof, amending P.L.1950, c.270.

BE IT ENACTED by the Senate and General Assembly of the State of New Jersey:

1. Section 13 of P.L.1950, c.270 (C.52:18A-91) is amended to read as follows:

13. a. The State Investment Council shall consult with the Director of the Division of Investment from time to time with respect to the work of the division. It shall have access to all files and records of the division and may require any officer or employee therein to provide such information as it may deem necessary in the performance of its functions. The council shall have authority to inspect and audit the respective accounts and funds administered through the Division of Investment. It shall formulate and establish, and may from time to time amend, modify or repeal, such policies as it may deem necessary or proper, which shall govern the methods, practices or procedures for investment, reinvestment, purchase, sale or exchange transactions to be followed by the Director of the Division of Investment established hereunder, except that the provisions of this subsection shall not apply to the operations account of Common Pension Fund L established pursuant to section 6 of P.L.2017, c.98 (C.5:9-22.10).

Notwithstanding any provision of the "Administrative Procedure Act," P.L.1968, c.410 (C.52:14B-1 et seq.) to the contrary, the council may adopt, immediately upon filing with the Office of Administrative Law such policies and regulations relating to the investment account, established pursuant to section 6 of P.L.2017, c.98 (C.5:9-22.10.), as are necessary to implement that section, which regulations shall be effective for a period not to exceed 12 months following adoption, and may thereafter be amended, adopted, or readopted by the council in accordance with the requirements of the "Administrative Procedure Act," P.L.1968, c.410 (C.52:14B-1 et seq.).

b. On or before January first of each year, and at such other times as it may deem in the public interest, the council shall report to the Governor, the Legislature, and the State Treasurer with respect to its work and the work of the Division of Investment. In addition to the reports specified above and in section 14 of P.L.1950, c.270 (C.52:18A-92), the council shall issue a report by

EXPLANATION – Matter enclosed in bold-faced brackets [thus] in the above bill is not enacted and is intended to be omitted in the law.

Matter underlined thus is new matter.
March 1 of each year on the investment activities for the prior State fiscal year, which shall include a summary of the current investment policies and strategies of the council and those in effect during the prior State fiscal year, a detailed summary for each financial product of the amount invested, performance benchmarks, and actual performance during the State fiscal year. The report shall be submitted to the Governor, the Legislature, and the State Treasurer, and shall be made available to the public through the official Internet site of the State. In addition, the council shall issue in the report a listing, in the aggregate and segregated by asset class, the investment returns achieved by the State-administered retirement system and retirement annuity funds under the council’s supervision by external managers. As part of any contract between the council and an external manager for the investment of State-administered retirement system funds and retirement annuity funds executed after the effective date of P.L. , c. (pending before the Legislature as this bill), the council shall require the external manager to disclose the rate and amount of fees charged by the external manager, which shall be based solely upon performance-based earnings which shall not include carried interest, incentive or profit-sharing fees. Performance-based earnings shall include refundable performance fees that best align the interests of external managers with the interest of the State-administered retirement system funds. Performance-based earnings shall focus on value-for-money, such as the ratio of fees paid to the value added, after fees and expenses and other costs, including administrative, legal and transaction costs, that may be referred to as management, consultant, or other pass-through costs, and are paid by the external managers, and shall maximize net-of-fee returns to the State-administered retirement system funds. The council shall include such rate and fees in the council’s report and shall submit the report to the boards of trustees of each State-administered retirement system mentioned in the report and to the Division of Pensions and Benefits, which shall post the report on its Internet website in the same location as other reports and analyses produced by the division.

c. The council shall hold a meeting each year that shall be open to the public, and shall accept comments from the public at such meeting. The matters that shall be open to discussion and public comment during this annual meeting shall include the investment policies and strategies of the council, the investment activities of the council, the financial disclosure statements filed by council members, and the certification of contributions filed by external managers, as well as other appropriate matters concerning the operations, activities and reports of the council.
d. An external manager shall be required to file a certification before being retained, and annually thereafter, that discloses the political contributions made, during the 12 months preceding the certification, by the manager or the manager's firm, or a political committee in which the manager or firm was active. The certification shall specify the political contributions made to candidates for elective public office in this State and any political committee established for the support of such candidates, and contributions made for the transition and inaugural expenses of any candidate who is elected to public office. As used in this subsection, "contribution" and "political committee" shall have the meaning set forth in "The New Jersey Campaign Contributions and Expenditures Reporting Act," P.L.1973, c.83 (C.19:44A-1 et al.). This certification shall be in addition to any other such disclosure required by law or executive order of the Governor.

2. This act shall take effect immediately and apply to new external manager retainer agreements or renewal of existing retainer agreements executed on and after the date of enactment.

STATEMENT

This bill requires that the compensation of external managers retained by the Division of Investments in the Department of the Treasury and authorized to invest assets of State pension or annuity funds to be based solely upon performance-based earnings. This restriction will apply to new external manager retainer agreements or renewal of existing retainer agreements. External manager agreements will not include carried interest, incentive or profit-sharing fees. Performance-based earnings that will be permitted must include refundable performance fees that best align the interests of external managers with the interest of the membership of State-administered retirement system funds.

The bill also requires the State Investment Council to include in its annual investment report a listing, in the aggregate and segregated by asset class, the investment returns achieved by the State-administered retirement system and retirement annuity funds under the council’s supervision by external managers. This report will also include disclosure of the rate and fees paid as compensation for external manager retainer agreements. The council’s report shall be submitted to the boards of trustees of each State-administered retirement system mentioned in the report and to the Division of Pensions and Benefits, which shall include the report on its Internet website.
State public pension funds rely on external investment firms for various services, including investment management of investments in the Alternative investment program. Alternative investments include hedge funds, private equity, real estate funds, real asset funds, opportunistic funds and global diversified credit funds. External managers of these funds maintain that they offer pension funds absolute return and volatility reduction in exchange for high management and performance fees that they charge. While external management services may be important for maintaining a balanced portfolio to ensure the health of pension fund investments, the fees that investment management firms can charge for their services can be exorbitant, sometimes arbitrarily so. Different classes of investment managers have developed their own pricing structures that may create the illusion of a natural market rate, while, in fact, managers charge what they believe investors will pay.

Under this bill performance-based earnings must focus on value-for-money, such as the ratio of fees paid to the value added, after fees and expenses and other costs, which are paid by the external managers, and must maximize net-of-fee returns to the State-administered retirement system funds.