

MEMORANDUM

To: House Financial Institutions and Pensions

From: Alan D. Conroy, Executive Director

Date: March 4, 2024

Subject: Opponent Testimony on HB 2739; Countries of Concern Divestment

On behalf of the KPERS Board of Trustees, I respectfully appear before the Committee today as an opponent to House Bill 2739.

House Bill 2739 establishes a requirement for State-managed funds, including the KPERS Trust Fund, to sell, redeem, divest or withdraw all publicly traded securities, held directly or indirectly in actively or passively managed investment funds of a “country of concern,” which is defined in the bill. The bill also prohibits future public or private market investments in countries of concern.

State funds would have one year to divest 50% of affected assets, unless a later date is more prudent based on fiduciary discretion. However, 100% of affected assets must be divested within two years.

In addition, no state agency may procure good or services from a company in a country of concern.

As defined by HB 2739, the list of countries of concern includes:

- China (including Hong Kong but excluding Taiwan)
- Cuba
- Iran
- North Korea
- Russia
- Venezuela

The provisions of HB 2739 sunset on July 1, 2029.

KPERS Investments History

Since 1961 when the Retirement System was created, the Legislature has delegated Trust Fund oversight and investment decisions to the Board of Trustees. The Board has carefully built the KPERS portfolio to provide the highest returns with the least amount of risk.



The KPERS Board of Trustees and all the Board’s investment managers are fiduciaries (highest moral, ethical, and legal standard) to our members. All investment decisions are made for the sole purpose of providing promised benefits. Adding statutory restrictions to investments impedes the Board of Trustees’ ability to make investment decisions and manage risk with the sole purpose of funding benefits. The constraints on KPERS investments could negatively impact the ultimate rate of return which translates into higher KPERS employer contributions by the State and local units of government.

The KPERS Board of Trustees and investment managers follow all federal laws regarding international investments. For example, no U.S. investments may be made within North Korea.

Current Holdings in Countries of Concern

Of the countries of concern listed in HB 2739, the KPERS Trust Fund only has holdings in China (including Hong Kong). As of January 31, 2024, KPERS had \$292 million in holdings China. Of the total, about \$257 million was in public market holdings subject to the divest requirements in HB 2739. The System currently has 13 holdings that are subject to divestment under HB 2739.

Over the past year, the KPERS Board of Trustees approved changes to the investment portfolio that reduced KPERS exposure to China. These changes were driven by economic and portfolio management considerations and were made on the advice of KPERS investment consultants and KPERS investment staff. In calendar year 2023, KPERS exited two international equity, commingled investment funds. One of these funds included passively managed investments to stocks across all industries in China. Exiting this fund eliminated KPERS passive exposure to China equities. The Board also adopted a new benchmark for the System’s international equity portfolio that excluded China. This change does not require divestment from China, but it does reduce the incentive for the System’s international equity managers to invest in China. Following these Board actions, exposure to China was reduced from \$611 million at the start of 2023 to \$292 million at January 31, 2024. KPERS currently hold 13 public market securities that will be subject to divestment under HB 2739. Prior to the Board action the Trust Fund had 800 China investments.

I have attached a *KPERS Fast Facts* on divesting KPERS’ investments in foreign adversaries. The document provides a high-level overview of the issue.

Technical Amendment

During review of the language in HB 2739, KPERS noted one potential amendment for consideration if the bill is moved forward. On page 3 of the bill as introduced, on lines 39 and 40 there is reference to “companies affiliated with a country of concern.” However, the meaning of “affiliated” is not defined.

For clarity and consistency with other parts of HB 2739, KPERS would request that language be changed to “a person owned or controlled by, or subject to the jurisdiction or

direction of a country of concern.” We can work with the Revisor’s on a balloon amendment if that is the will of the Committee.

Conclusion

With a history of prudent investment decisions, which follow from a well-established and disciplined investment policy and governance model, we do not believe a statutory divestment requirement is the appropriate approach for KPERS investments.

On behalf of the Board of Trustees, I respectfully request that HB 2739 not be passed. I would be pleased to answer any questions the Committee has.

KPERS FAST FACTS

Divesting KPERS' Investments in Foreign Adversaries

The fiduciary standard is our guiding principle and driving force. That means we put the interest of our members first in all that we do. It is the highest standard of care and accountability.

What Governs Investments?

Kansas Statute & KPERS Policy

-  Sole benefit of members
-  No economic or social objectives
-  Highest return for lowest risk
-  Diversified investing

House Bill No. 2739 At-A-Glance

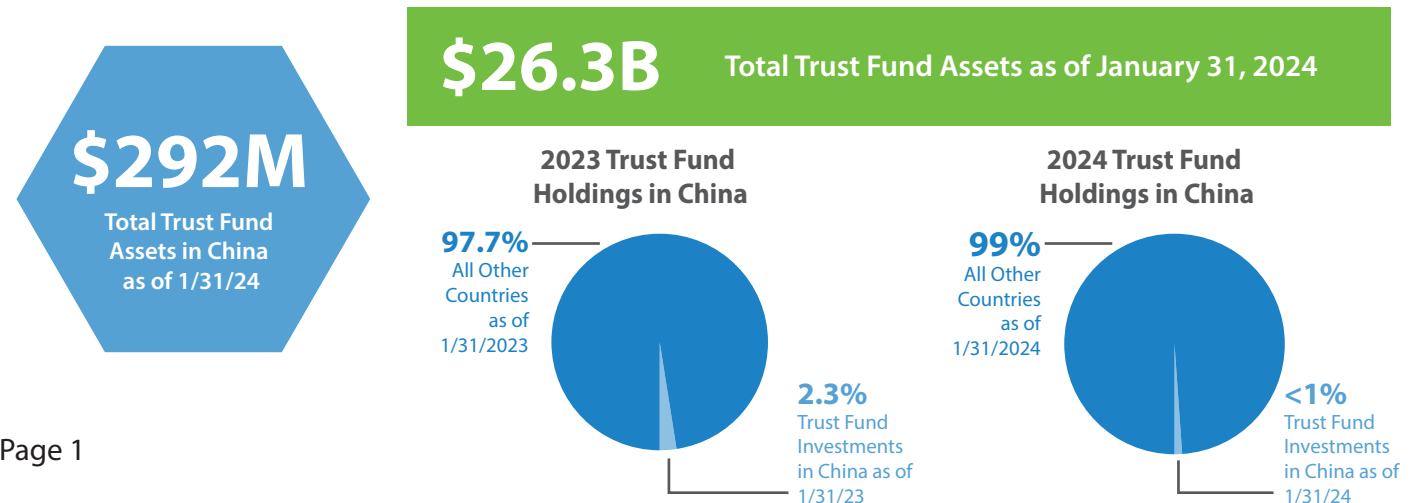
House Bill No. 2739 would enact the Countries of Concern Divestment and Procurement Protection Act, requiring State-managed funds, like the KPERS Trust Fund, to divest from investments with countries of concern.

Countries of Concern as Defined

Of the six countries noted in HB 2739, KPERS is currently investing only in China, which includes Hong Kong.

INVESTING IN:	China	Cuba	Iran	North Korea	Russia	Venezuela
	Yes	No	No	No	No	No

KPERS' Current Holdings in China

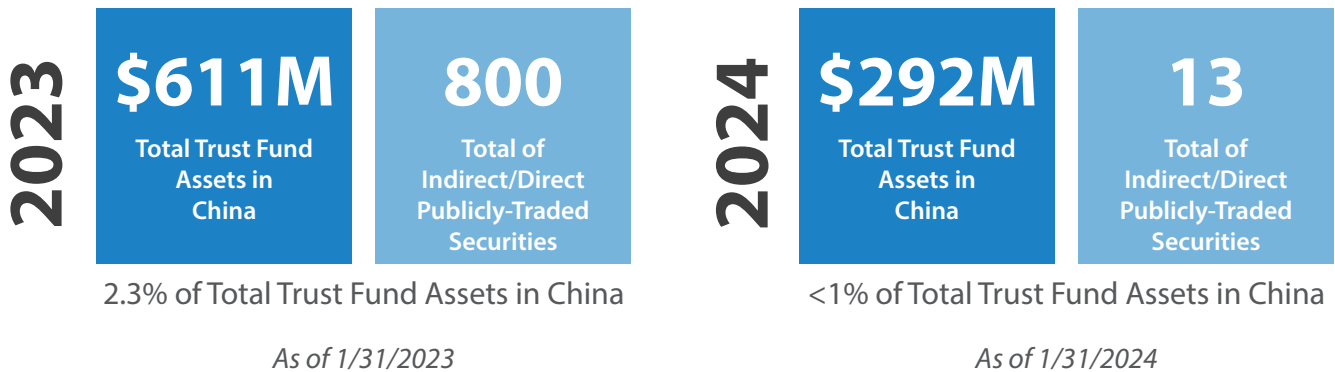


Recent Action to Manage Exposure to China

In 2023, the KPERS Board took steps that had the effect of reducing public market investment exposure to China:

- Divested from commingled International Equity funds, removing passive investments in China.
- Changed the International Equity benchmark to one that does not include China, reducing the incentive for investment managers to invest in China.

The number of public market holdings in China have declined from about 800 in early 2023 to 13 as of January 31, 2024.



Potential Impact of House Bill No. 2739



No New Investments in China

KPERS would not be allowed to make new investments in China as of the bill's effective date.

KPERS would also need to sell its publicly-traded holdings in China.

Any reduction in investment income would need to be made up through increased employer contributions.