

HOUSE BILL No. 2500

By Joint Committee on Pensions, Investments and Benefits

1-12

AN ACT concerning retirement and pensions; relating to the Kansas public employees retirement system and systems thereunder; alternative investments; amending K.S.A. 74-4921 and repealing the existing section.

Be it enacted by the Legislature of the State of Kansas:

Section 1. K.S.A. 74-4921 is hereby amended to read as follows: 74-4921. (1) There is hereby created in the state treasury the Kansas public employees retirement fund. All employee and employer contributions shall be deposited in the state treasury to be credited to the Kansas public employees retirement fund. The fund is a trust fund and shall be used solely for the exclusive purpose of providing benefits to members and member beneficiaries and defraying reasonable expenses of administering the fund. Investment income of the fund shall be added or credited to the fund as provided by law. All benefits payable under the system, refund of contributions and overpayments, purchases or investments under the law and expenses in connection with the system unless otherwise provided by law shall be paid from the fund. The director of accounts and reports is authorized to draw warrants on the state treasurer and against such fund upon the filing in the director's office of proper vouchers executed by the chairperson or the executive director of the board. As an alternative, payments from the fund may be made by credits to the accounts of recipients of payments in banks, savings and loan associations and credit unions. A payment shall be so made only upon the written authorization and direction of the recipient of payment and upon receipt of such authorization such payments shall be made in accordance therewith. Orders for payment of such claims may be contained on (a) a letter, memorandum, telegram, computer printout or similar writing, or (b) any form of communication, other than voice, which is registered upon magnetic tape, disc or any other medium designed to capture and contain in durable form conventional signals used for the electronic communication of messages.

(2) The board shall have the responsibility for the management of the fund and shall discharge the board's duties with respect to the fund

1 solely in the interests of the members and beneficiaries of the system for
2 the exclusive purpose of providing benefits to members and such mem-
3 ber's beneficiaries and defraying reasonable expenses of administering
4 the fund and shall invest and reinvest moneys in the fund and acquire,
5 retain, manage, including the exercise of any voting rights and disposal of
6 investments of the fund within the limitations and according to the pow-
7 ers, duties and purposes as prescribed by this section.

8 (3) Moneys in the fund shall be invested and reinvested to achieve
9 the investment objective which is preservation of the fund to provide
10 benefits to members and member beneficiaries, as provided by law and
11 accordingly providing that the moneys are as productive as possible, sub-
12 ject to the standards set forth in this act. No moneys in the fund shall be
13 invested or reinvested if the sole or primary investment objective is for
14 economic development or social purposes or objectives.

15 (4) In investing and reinvesting moneys in the fund and in acquiring,
16 retaining, managing and disposing of investments of the fund, the board
17 shall exercise the judgment, care, skill, prudence and diligence under the
18 circumstances then prevailing, which persons of prudence, discretion and
19 intelligence acting in a like capacity and familiar with such matters would
20 use in the conduct of an enterprise of like character and with like aims
21 by diversifying the investments of the fund so as to minimize the risk of
22 large losses, unless under the circumstances it is clearly prudent not to
23 do so, and not in regard to speculation but in regard to the permanent
24 disposition of similar funds, considering the probable income as well as
25 the probable safety of their capital.

26 (5) Notwithstanding subsection (4): (a) Total investments in common
27 stock may be made in the amount of up to 60% of the total book value
28 of the fund;

29 (b) the board may invest or reinvest moneys of the fund in alternative
30 investments if the following conditions are satisfied:

31 (i) The total of ~~such the annual~~ alternative investments investment
32 does not exceed more than ~~5%~~ 1% of the total ~~market value of~~ investment
33 assets of the fund. ~~If the total of such alternative investments exceeds~~
34 ~~more than 5% of the total investment assets of the fund on the effective~~
35 ~~date of this act, the board shall not invest or reinvest any moneys of the~~
36 ~~fund in alternative investments until the total of such alternative invest-~~
37 ~~ments is less the 5% of the total investment assets of the fund subject to~~
38 ~~the 5% limitation contained in this subsection. Nothing in this subsection~~
39 ~~requires the board to liquidate or sell the system's holdings in any alter-~~
40 ~~native investment held by the system on the effective date of this act,~~
41 ~~unless such liquidation or sale would be in the best interest of the mem-~~
42 ~~bers and beneficiaries of the system and be prudent under the standards~~
43 ~~contained in this section. The 5% limitation contained in this section shall~~

~~not have been violated if the total of such alternative investments exceeds 5% of the total investment assets of the fund as a result of market forces acting to increase the value of such alternative investments relative to the rest of the system's investments; however, the board shall not invest or reinvest any moneys of the fund in alternative investments until the total of such alternative investments is less than 5% of the total investment assets of the fund subject to the 5% limitation contained in this subsection as measured from the end of the preceding calendar year;~~

(ii) if in addition to the system, there are at least two other sophisticated investors, as defined by section 301 of the securities and exchange act of 1933;

(iii) the system's share in any individual alternative investment is limited to an investment representing not more than 20% of any such individual alternative investment;

(iv) the system has received a favorable and appropriate recommendation from a qualified, independent expert in investment management or analysis in that particular type of alternative investment;

(v) the alternative investment is consistent with the system's investment policies and objectives as provided in subsection (6);

(vi) the individual alternative investment does not exceed more than 2.5% of the total alternative investments made under this subsection. If the alternative investment is made pursuant to participation by the system in a multi-investor pool, the 2.5% limitation contained in this subsection is applied to the underlying individual assets of such pool and not to investment in the pool itself. The total of such alternative investments made pursuant to participation by the system in any one individual multi-investor pool shall not exceed more than 20% of the total of alternative investments made by the system pursuant to this subsection. Nothing in this subsection requires the board to liquidate or sell the system's holdings in any alternative investments made pursuant to participation by the system in any one individual multi-investor pool held by the system on the effective date of this act, unless such liquidation or sale would be in the best interest of the members and beneficiaries of the system and be prudent under the standards contained in this section. The 20% limitation contained in this subsection shall not have been violated if the total of such investment in any one individual multi-investor pool exceeds 20% of the total alternative investments of the fund as a result of market forces acting to increase the value of such a multi-investor pool relative to the rest of the system's alternative investments; however, the board shall not invest or reinvest any moneys of the fund in any such individual multi-investor pool until the value of such individual multi-investor pool is less than 20% of the total alternative investments of the fund;

(vii) the board has received and considered the investment manager's

1 due diligence findings submitted to the board as required by subsection
2 (6)(c); and

3 (viii) prior to the time the alternative investment is made, the system
4 has in place procedures and systems to ensure that the investment is
5 properly monitored and investment performance is accurately measured.

6 For purposes of this act, "alternative investment" means nontraditional
7 investments outside the established nationally recognized public stock
8 exchanges and government securities market. Alternative investments
9 shall include, but not be limited to, private placements, venture capital,
10 partnerships, limited partnerships and leveraged buyout partnerships; and

11 (c) except as otherwise provided, the board may invest or reinvest
12 moneys of the fund in real estate investments if the following conditions
13 are satisfied:

14 (i) The system has received a favorable and appropriate recommen-
15 dation from a qualified, independent expert in investment management
16 or analysis in that particular type of real estate investment;

17 (ii) the real estate investment is consistent with the system's invest-
18 ment policies and objectives as provided in subsection (6); and

19 (iii) the board has received and considered the investment manager's
20 due diligence findings submitted to the board as required by subsection
21 (6)(c).

22 (6) Subject to the objective set forth in subsection (3) and the stan-
23 dards set forth in subsections (4) and (5) the board shall formulate policies
24 and objectives for the investment and reinvestment of moneys in the fund
25 and the acquisition, retention, management and disposition of invest-
26 ments of the fund. Such policies and objectives shall include:

27 (a) Specific asset allocation standards and objectives;

28 (b) establishment of criteria for evaluating the risk versus the poten-
29 tial return on a particular investment;

30 (c) a requirement that all investment managers submit such man-
31 ager's due diligence findings on each investment to the board or invest-
32 ment advisory committee for approval or rejection prior to making any
33 alternative investment;

34 (d) a requirement that all investment managers shall immediately re-
35 port all instances of default on investments to the board and provide the
36 board with recommendations and options, including, but not limited to,
37 curing the default or withdrawal from the investment; and

38 (e) establishment of criteria that would be used as a guideline for
39 determining when no additional add-on investments or reinvestments
40 would be made and when the investment would be liquidated.

41 The board shall review such policies and objectives, make changes con-
42 sidered necessary or desirable and readopt such policies and objectives
43 on an annual basis.

1 (7) The board may enter into contracts with one or more persons
2 whom the board determines to be qualified, whereby the persons under-
3 take to perform the functions specified in subsection (2) to the extent
4 provided in the contract. Performance of functions under contract so
5 entered into shall be paid pursuant to rates fixed by the board subject to
6 provisions of appropriation acts and shall be based on specific contractual
7 fee arrangements. The system shall not pay or reimburse any expenses of
8 persons contracted with pursuant to this subsection, except that after
9 approval of the board, the system may pay approved investment related
10 expenses subject to provisions of appropriation acts. The board shall re-
11 quire that a person contracted with to obtain commercial insurance which
12 provides for errors and omissions coverage for such person in an amount
13 to be specified by the board, provided that such coverage shall be at least
14 the greater of \$500,000 or 1% of the funds entrusted to such person up
15 to a maximum of \$10,000,000. The board shall require a person con-
16 tracted with to give a fidelity bond in a penal sum as may be fixed by law
17 or, if not so fixed, as may be fixed by the board, with corporate surety
18 authorized to do business in this state. Such persons contracted with the
19 board pursuant to this subsection and any persons contracted with such
20 persons to perform the functions specified in subsection (2) shall be
21 deemed to be agents of the board and the system in the performance of
22 contractual obligations.

23 (8) (a) In the acquisition or disposition of securities, the board may
24 rely on the written legal opinion of a reputable bond attorney or attorneys,
25 the written opinion of the attorney of the investment counselor or man-
26 agers, or the written opinion of the attorney general certifying the legality
27 of the securities.

28 (b) The board shall employ or retain qualified investment counsel or
29 counselors or may negotiate with a trust company to assist and advise in
30 the judicious investment of funds as herein provided.

31 (9) (a) Except as provided in subsection (7) and this subsection, the
32 custody of money and securities of the fund shall remain in the custody
33 of the state treasurer, except that the board may arrange for the custody
34 of such money and securities as it considers advisable with one or more
35 member banks or trust companies of the federal reserve system or with
36 one or more banks in the state of Kansas, or both, to be held in safe-
37 keeping by the banks or trust companies for the collection of the principal
38 and interest or other income or of the proceeds of sale. The services
39 provided by the banks or trust companies shall be paid pursuant to rates
40 fixed by the board subject to provisions of appropriation acts.

41 (b) The state treasurer and the board shall collect the principal and
42 interest or other income of investments or the proceeds of sale of secu-
43 rities in the custody of the state treasurer and pay same when so collected

1 into the fund.

2 (c) The principal and interest or other income or the proceeds of sale
3 of securities as provided in clause (a) of this subsection (9) shall be re-
4 ported to the state treasurer and the board and credited to the fund.

5 (10) The board shall with the advice of the director of accounts and
6 reports establish the requirements and procedure for reporting any and
7 all activity relating to investment functions provided for in this act in order
8 to prepare a record monthly of the investment income and changes made
9 during the preceding month. The record will reflect a detailed summary
10 of investment, reinvestment, purchase, sale and exchange transactions
11 and such other information as the board may consider advisable to reflect
12 a true accounting of the investment activity of the fund.

13 (11) The board shall provide for an examination of the investment
14 program annually. The examination shall include an evaluation of current
15 investment policies and practices and of specific investments of the fund
16 in relation to the objective set forth in subsection (3), the standard set
17 forth in subsection (4) and other criteria as may be appropriate, and rec-
18 ommendations relating to the fund investment policies and practices and
19 to specific investments of the fund as are considered necessary or desir-
20 able. The board shall include in its annual report to the governor as pro-
21 vided in K.S.A. 74-4907, and amendments thereto, a report or a summary
22 thereof covering the investments of the fund.

23 (12) (a) An annual financial-compliance audit of the system, includ-
24 ing any performance audit subjects which are directed to be included in
25 such annual audit by the legislative post audit committee, performance
26 audits of the system as prescribed under the Kansas governmental op-
27 erations law, and such other audits as are directed by the legislative post
28 audit committee under the Kansas legislative post audit act shall be con-
29 ducted. The annual financial-compliance audit shall include, but not be
30 limited to, a review of alternative investments of the system with any
31 estimates of permanent impairments to the value of such alternative in-
32 vestments reported by the system pursuant to K.S.A. 74-4907, and
33 amendments thereto.

34 (b) In accordance with this subsection (12), the annual financial-com-
35 pliance audit may include one or more performance audit subjects as
36 directed by the legislative post audit committee. In considering perform-
37 ance audit subjects to be included in any financial-compliance audit con-
38 ducted pursuant to this subsection (12), the legislative post audit com-
39 mittee shall consider recommendations and requests for performance
40 audits, relating to the system or the management thereof, by the joint
41 committee on pensions, investments and benefits or by any other com-
42 mittee or individual member of the legislature. Commencing with the
43 financial-compliance audit for the fiscal year ending June 30, 1998, the

1 legislative post audit committee shall specify if one or more performance
2 audit subjects shall be included in the financial-compliance audit con-
3 ducted pursuant to this subsection (12), in addition to such other subjects
4 as may be directed to be included in the financial-compliance audit by
5 the legislative post audit committee. Except as otherwise determined by
6 the legislative post audit committee pursuant to this subsection (12), com-
7 mencing with the financial-compliance audit for the fiscal year ending
8 June 30, 1998, one or more performance audit subjects specified by the
9 legislative post audit committee shall be included at least once every two
10 fiscal years in a financial-compliance audit conducted pursuant to this
11 subsection (12). The legislative post audit committee may direct that one
12 or more performance audit subjects are to be included in a financial-
13 compliance audit conducted pursuant to this subsection (12) not more
14 than once during a specific period of three fiscal years, in lieu of once
15 every two fiscal years.

16 (c) The auditor to conduct the financial-compliance audit required
17 pursuant to this subsection (12) shall be specified in accordance with
18 K.S.A. 46-1122, and amendments thereto. If the legislative post audit
19 committee specifies under such statute that a firm, as defined by K.S.A.
20 46-1112, and amendments thereto, is to perform all or part of the audit
21 work of such audit, such firm shall be selected and shall perform such
22 audit work as provided in K.S.A. 46-1123, and amendments thereto, and
23 K.S.A. 46-1125 through 46-1127, and amendments thereto. The audits
24 required pursuant to this subsection (12) shall be conducted in accord-
25 ance with generally accepted governmental auditing standards. The fi-
26 nancial-compliance audit required pursuant to this subsection (12) shall
27 be conducted as soon after the close of the fiscal year as practicable, but
28 shall be completed no later than six months after the close of the fiscal
29 year. The post auditor shall annually compute the reasonably anticipated
30 cost of providing the financial-compliance audit pursuant to this subsec-
31 tion (12), subject to review and approval by the contract audit committee
32 established by K.S.A. 46-1120, and amendments thereto. Upon such ap-
33 proval, the system shall reimburse the division of post audit for the
34 amount approved by the contract audit committee. The furnishing of the
35 financial-compliance audit pursuant to this subsection (12) shall be a
36 transaction between the legislative post auditor and the system and shall
37 be settled in accordance with the provisions of K.S.A. 75-5516, and
38 amendments thereto.

39 (d) Any internal assessment or examination of alternative investments
40 of the system performed by any person or entity employed or retained
41 by the board which evaluates or monitors the performance of alternative
42 investments shall be reported to the legislative post auditor so that such
43 report may be reviewed in accordance with the annual financial-compli-

1 ance audits conducted pursuant to this subsection (12).

2 Sec. 2. K.S.A. 74-4921 is hereby repealed.

3 Sec. 3. This act shall take effect and be in force from and after its
4 publication in the statute book.

5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25
26
27
28
29
30
31
32
33
34
35
36
37
38
39
40
41
42
43