COMMISSION ON GOVERNMENT FORECASTING AND ACCOUNTABILITY

PENSION IMPACT NOTE

95TH GENERAL ASSEMBLY

BILL NO: **SB 1305, as amended by SA #1** March 29, 2007

SPONSOR (S): Schoenberg – Radogno, et al.

SYSTEM(S): All Systems

FISCAL IMPACT: SB 1305, as amended, does not directly impact any of the benefit provisions or funding of any of the affected public pension funds or retirement systems. It is unknown what impact, if any, the provisions relating to the selection and retention of investment advisors and consultants will have on the various pension funds.

SUBJECT MATTER: SB 1305, as amended, makes several changes to the Illinois Governmental Ethics Act, the Illinois Procurement Code, and the Illinois Pension Code as outlined in the Comments Section.

FISCAL IMPACT: SB 1305, as amended, does not directly impact any of the benefit provisions or funding of any of the affected public pension funds or retirement systems. It is unknown what impact, if any, the provisions relating to the selection and retention of investment advisors and consultants will have on the various pension funds.

COMMENTS: SB 1305, as amended by SA #1, makes the following changes:

Illinois Governmental Ethics Act

Board Member Disclosure of Economic Interests (State-funded Systems)

SB 1305, as amended by SA #1, requires board members of the five State-funded pension systems (SERS, SURS, TRS, GARS, JRS) and the Illinois State Board of Investment (ISBI) to file annual written statements of economic interest with the Secretary of State. Board members of the retirement systems and ISBI will be required to disclose any ownership interest in any entity doing business in the State of Illinois that exceeds $5,000 fair market value or $1,200 in dividends during the preceding calendar year or any position with that entity from which income in excess of $1,200 was derived during the preceding calendar year (excluding professional service entities). Board members will also be required to disclose the identity of any compensated lobbyist with whom the board member maintains a close economic association. Any board member who files a false or incomplete statement of economic interests shall be guilty of a Class A misdemeanor.

Board Member Disclosure of Economic Interests (Non-State Funded Systems)
SB 1305, as amended by SA #1, requires board members of all non-State funded public pension funds established under the Illinois Pension Code to file annual written statements of economic interest with the county clerk in the county which the pension fund's principal office is located. Board members will be required to disclose any ownership interest in any entity doing business with a unit of local government that exceeds $5,000 fair market value or $1,200 in dividends during the preceding calendar year or any position with that entity from which income in excess of $1,200 was derived during the preceding calendar year (excluding professional service entities). Board members will also be required to disclose any ownership interest exceeding $5,000 fair market value or $1,200 in dividend income during the preceding year in any entity which has applied to a unit of local government for any license, franchise or permit for annexation, or zoning or rezoning of real estate during the preceding calendar year. Any board member who files a false or incomplete statement of economic interests shall be guilty of a Class A misdemeanor.

Illinois Procurement Code

Designation of Pension Chief Procurement Officer
SB 1305, as amended by SA #1, requires each of the five State-funded retirement systems and the Illinois State Board of Investment (ISBI) to designate a pension chief procurement officer to oversee the selection and appointment of consultants made by the retirement systems and ISBI pursuant to their fiduciary duties.

Procurement Code Guidelines for Pension Fund Investment Activities
SB 1305, as amended by SA #1, places the function of selecting consultants by each of the five State-funded retirement systems and ISBI under the guidelines of the Illinois Procurement Code. Specifically, the bill places these activities under Article 35 of the Procurement Code, which governs the procurement of professional and artistic services. Hence, in selecting investment advisors and consultants, ISBI and the five State-funded retirement systems will be subject to the Procurement Code's requirements with respect to prequalification, evaluation, ranking, and selection of competitive bids for investment services.

Illinois Pension Code

Duties of Fiduciaries
Currently, the Pension Code defines a fiduciary as one who exercises discretionary authority or discretionary control over management of the pension fund, renders investment advice, or has any discretionary authority in the administration of the pension fund. SB 1305, as amended by SA #1, broadens the definition of a fiduciary to include any person who renders advice with respect to the selection of other fiduciaries.

Establishment of Goals for Utilization of Emerging Investment Managers
SB 1305, as amended by SA #1, mandates that all public pension funds under the Pension Code (with the exception of the Metropolitan Water Reclamation District pension fund and

Downstate Police and Fire pension funds) adopt a policy including quantifiable goals for the management of assets in specific classes by emerging investment managers on or before July 1, 2007.

Prohibited Transactions for Fiduciaries

SB 1305, as amended by SA #1, prohibits a fiduciary from knowingly causing or advising a pension fund to engage in an investment transaction with an investment advisor with whom the fiduciary has any financial interest or business relationship that would result in a pecuniary benefit to the fiduciary. The bill, as amended, makes this action a Class 3 felony.

Limitation on Contracts for Investment Consultants

SB 1305, as amended by SA #1, prohibits all pension funds established under the Pension Code and the Illinois State Board of Investment from awarding a contract for consulting services for longer than five years. The bill, as amended, also specifies that no contract for consulting services may be renewed or extended. Furthermore, the bill provides that at the end of the term of a consulting contract, the consultant may compete for a new contract under the guidelines of the Illinois Procurement Code (30 ILCS 50/35).

Procurement Code Requirements for Selection and Appointment of Consultants

SB 1305, as amended by SA #1, requires the five State-funded retirement systems to contract for investment services from consultants in accordance with the Illinois Procurement Code (30 ILCS 50/35). For non-State funded systems, the process of selecting investment advisors and contracting for investments services and consultants must be *substantially similar* to the method of selection required under Article 35 of the Procurement Code. The bill requires all bidders to disclose the names and addresses of entities that have a controlling interest in the entity making the offer, and also the names and addresses of persons who have ownership in the offering entity greater than 5%, or an amount that exceeds 60% of the Governor's annual salary ("key persons").

Requirements for Consultants

SB 1305, as amended by SA #1, requires a consultant who is neither a pension fund board member or employee to be one of the following on or after July 1, 2006: a registered investment advisor under the federal Investment Advisers Act of 1940; a registered investment advisor under the Illinois Securities Law of 1953; a bank; or, an insurance company.

Disclosure of Fees by Investment Advisors and Consultants

SB 1305, as amended by SA #1, requires all contracts entered into between all pension funds established under the Illinois Pension Code (including the Illinois State Board of Investment) and investment advisors or consultants to fully disclose all direct and indirect fees, commissions, penalties, and other forms of compensation, including reimbursement for expenses that may be paid by or on behalf of the investment advisor or consultant in connection with the provision of investment services. SB 1305, as amended, also requires that all investment advisors and consultants who currently provide investment services on a contractual basis must disclose to the board of trustees of the pension fund all direct and indirect fees, commissions, penalties, and other compensation paid by or on behalf of the investment advisor or consultant within 30 days after the effective date of this Amendatory Act. Additionally, the bill requires all boards of trustees to submit copies of their contracts with advisors and consultants to the Division of Insurance of the Department of Financial and Professional Regulation within 30 days of the appointment of the advisor or consultant.

Compliance with the Business Enterprise for Minorities, Females, and Persons With Disabilities Act

SB 1305, as amended by SA #1, requires all of the five State-funded retirement systems to comply with the Business Enterprise for Minorities, Females, and Persons with Disabilities Act with respect to selecting investment advisors and investment services. The Act sets a goal of awarding not less than 12% of the total dollar amount of State contracts to businesses owned by minorities, females, and persons with disabilities. The bill, as amended, also requires the boards of trustees of each system and the Illinois State Board of Investment to post on their respective websites the percentage of current investment contracts and those contracts awarded during the preceding five fiscal years to minority owned businesses, female owned businesses, and businesses owned by a person with a disability.

Limitation of Home Rule Powers

SB 1305, as amended by SA #1, contains a limitation and denial of home rule powers with respect to the provisions pertaining to the selection of investment advisors and consultants and fee disclosure. The bill specifies that home rule units may not regulate investment adviser and consultant contracts in a manner that is less restrictive than the provisions set forth in the bill.

Prohibition on Monetary Gain on Investments

SB 1305, as amended by SA #1, prohibits trustees and employees of the board of any retirement system established under the Pension Code or any employee of the Illinois State Board of Investment from having any direct interest in the income, gains, or profits of any investments made in behalf of the retirement system or State Board of Investment. Board members and employees of the board may not receive any compensation in connection with any investment. Violators will be guilty of Class 3 felony.

Fraud/Penalty for False Statements

SB 1305, as amended by SA #1, provides that any person who knowingly makes false statements or falsifies any records of a retirement system or the Illinois State Board of Investment is guilty of a Class 3 felony (currently a Class A misdemeanor).

Prohibition on Gifts

SB 1305, as amended by SA #1, prohibits board members and employees of all pension funds established under the Pension Code and the Illinois State Board of Investment from accepting or soliciting gifts from "prohibited sources." The bill, as amended, defines a "prohibited source" as a person who is seeking official action by the board of trustees of the pension fund or has interests that may be substantially affected by the performance or non-performance of the official duties of the board member or employee. Violators of the aforementioned provisions will be guilty of a Class A misdemeanor.

Prohibition on Contingent Fees

SB 1305, as amended by SA #1, prohibits retaining or employing a person solely for the purpose of influencing the outcome of the procurement of investment advice or services by a board of a pension fund established under the Pension Code or the Illinois State Board of

Investment. The bill, as amended, specifies that no person shall accept any commission or employment that is contingent upon a pension fund board's procurement decision. Violators will be guilty of a business offense and will be fined up to $10,000 and prohibited from conducting such activities for a period of three years.

SB 1305, as amended by SA #1, amends the State Mandates Act to require implementation without reimbursement.

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