I am writing in reference to the letter from M. Steve Yoakum, Executive Director of PSRS/PEERS to Mr. Martin White. I really think this letter should be "required reading" for every retired teacher. Steve is speaking the truth and it is very clearly stated. (The letter can be found at the end of this piece.)

Senate Bill 714 was third read Friday and incorporates into it Senate Bill 1050. Senate Bill 714 heads to the House this week. There are parts of Senate Bill 714 that are particularly "unsettling" to me.

In essence, there are three parts to this bill. The first and second parts, I do not have qualms about. They are: 1) Expansion of the State Auditor's responsibilities
2) Requires contributions from MOSERS which I think this should have been done in 1957. But, it is the third part that still gives me "angst". And, it is the reason why I think we should all be solidly opposed to this piece of legislation.

The third part is this: IT CREATES A STATE INVESTMENT BOARD. Now, on the surface this looks pretty innocuous. But, the "devil is in the details" as they say.

Here are my concerns:

1) Although PSRS/PEERS is not included in this legislation NOW, we all know Senate Bill 714 has to be debated and third read in the House. All it would take is the removal of "two little brackets" and PSRS/PEERS would be included in this piece of legislation.

2) Although PSRS/PEERS is not included in this legislation NOW, I am very suspicious that since our retirement fund is four times larger than MOSERS (See letter attached) that we are just too good of a "plumb" to be left alone. It would not be the first time someone has tried to take control of PSRS/PEERS. If not this year, why not another year. Our retirement fund has been "coveted" for many years by those in authority. We have a lot of money and state government knows it.

3) A State Investment Board, as is presently constituted in Senate Bill 714, would create a board where the Governor would approve appointees that were sent up to him. IF PSRS/PEERS were included in

this bill (currently it is NOT), we would lose the ability to vote for our own Board and those appointees would be approved by the Governor. If the Governor (whether Republican or Democrat or Independent or whatever) did not like the list, he simply refuses to approve and asks for another list. Sooner or later this is what happens: The board asks for a list of people the Governor will approve and THAT list is sent to that Governor.

4) Then, there is the possibility that when this bill reaches the final state, the conference committee, after it has passed both chambers that some language could be inserted that includes PSRS/PEERS. This happened on the federal level with the recent Congressional Health Insurance Reform; it can also happen to us on the state level. I am not saying that it will: but I will repeat that this bill is giving me "angst" as I watch its progress and debate. Powerful Senators seem intent on its passage.

5) Governor Jay Nixon has indicated that he will probably sign the legislation since he faces a 900 million deficit for next year and the inclusion of retirement contributions from MOSERS, The Missouri State Highway Department and The Missouri Highway Patrol will lessen that deficit by millions of dollars. So I think if this bill reaches his desk, I predict he WILL sign it. It will also give him the power to approve "appointees" to the State Investment Board and every governor, no matter what party, would like that.

6) I would like this bill a whole lot more if it did not set a PRECEDENT for a Missouri Investment Board (a high sounding name) that was at the ready to grab control of PSRS/PEERS at some future date-if not this session while in Conference Committee.

7) I have lived my life by a motto that I think applies in this case. It is this: "To be forewarned is to be forearmed".

Finally, I sincerely hope this bill in its present form is defeated even though it has many good parts to it. The PRECEDENT it sets is alarming.

Buck Smith MRTA Legislative Leader SEMO Unit

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March 3, 2010

Mr. Martin White
Email: m85white@gmail.com

Dear Mr. White:

Your recent email was forwarded to our office by the Missouri Retired Teachers Association. In response to your e-mail and the information received from Senator Crowell, we would like to furnish the following information:

Consolidation of PSRS/PEERS Investments with Other Public Pension Plans

SB 1050 was introduced by Senator Jason Crowell on Monday, March 1, to create the Missouri Public Trust Company. This company is authorized to manage the investment of the trust assets of the Missouri State Employees Retirement System (MOSERS) and the Missouri Department of Transportation and Highway Patrol Employees Retirement System (MPERS). Other Missouri public pension systems, except for the Public School Retirement System (PSRS), the Public Education Employee Retirement System (PEERS), and the Missouri Local Government Employees Retirement System (LAGERS), may contract with the company to act as trustee of their system's assets or to provide investment management or investment advisory services.

PSRS/PEERS is still in the process of reviewing all the facets of this bill. While PSRS/PEERS is not currently included in SB 1050, we are extremely concerned about the creation of any type of private investment company and oppose the concept of a private investment company to manage public funds.

Proponents of the state investment board concept focus primarily on two issues: investment costs and boosting investment returns. Proponents have also suggested that the consolidation of investments would not result in some form of merging of the systems. This paper provides background information and facts on these issues.

Size of Missouri Retirement Funds

PSRS/PEERS is the largest public defined benefit plan in the state of Missouri and one of the 50 largest defined benefit plans in the United States. The total assets of PSRS/PEERS are greater than the total assets of all other defined benefit plans in the state. PSRS/PEERS had total assets of $26.6 billion as of December 31, 2009 while MOSERS had $6.9 billion, LAGERS had $3.7 billion and MPERS had $1.3 billion.

<u>Loss of Control Over Investments</u>

The proponents of an investment board have utilized a banking analogy: we do not need four banks when one would be more efficient. Additionally, under this structure, proponents have stated that "no other system will get the PSRS/PEERS money". While there could be one investment board (one bank) and all of the money could be accounted for separately, you may note that as banks consolidate, and get bigger, problems can occur. One need only look back to last year when the consolidation in the banking business (particularly at Citigroup and Bank of America) caused significant problems and ripples through the economy because they became too big, there was a loss of oversight, a loss of control and a failure in terms of risk management because there was too great a consolidation of power.

PSRS was established in 1946 as a Trust Fund for the teachers of Missouri. Today, every PSRS/PEERS member is part of an election process to select four members of the PSRS/PEERS Board. Those Board members represent the concerns of the membership. As when parents establish a trust fund for their children, they choose a trustee who will manage their money for the benefit of their children's future well-being. A parent would not choose a trustee that would not have a vested interest in ensuring their children's future success.

If investment consolidation were to be implemented, **it is a fact that the PSRS/PEERS membership would lose representation over their retirement funds**. The initial discussion of an investment board would provide for one representative from each retirement system on the board. Thus, PSRS/PEERS would have one representative (25% of the board from the Missouri systems) even though the PSRS/PEERS assets would represent 70% of the investment board assets. This is a significant and potentially damaging loss in fiduciary oversight for our membership. Thus, while proponents of consolidation say it would not lead to a merging of systems, an almost complete loss over the investment function by the membership through its duly-elected representatives has essentially the same devastating outcome for members of PSRS/PEERS.

<u>PSRS/PEERS is a Contributory System</u>

The membership of PSRS/PEERS provides contributions through deferred wages (payroll deduction) to help fund future benefit payments, while MOSERS (for example) does not require any contribution from its members. This results in substantial fundamental differences between the two plans. Of the $26.6 billion in combined assets for PSRS/PEERS, over $6.0 billion (nearly the same level of total assets as MOSERS) has been directly contributed by members of the Systems. While proponents of consolidation prefer to argue that all state retirement systems are paid for by tax payers, PSRS/PEERS is funded by deferred wages of our membership. PSRS members currently pay 13.5% of their salary for their retirement benefit. This is money that they are not able to use at their own discretion.

<u>Actuarial Soundness</u>

The actuarial funded ratios for the three largest Missouri defined benefit systems (PSRS/PEERS, MOSERS and LAGERS) as of June 30, 2009 were between 79.9% and 83%. Thus, from an actuarial standpoint, all systems are sound. Proponents of the investment board have stated that contribution increases would stop and benefits would stay the same if an investment board were created due to greater returns with lower costs. Again, this is not true. As stated previously, investment costs would be higher for PSRS/PEERS under the proposed structure. Contribution rates will continue to increase in the next year or two regardless of investment returns. And, most importantly, investment returns are not guaranteed so it is difficult to accurately predict future contributions or benefit structures based on moving the management of assets to a different entity.

<u>Investment Returns</u>

Investment performance is very time-period dependent. MOSERS had better investment returns than PSRS/PEERS for the last ten years and PSRS/PEERS had better investment returns than MOSERS for a preceding ten-year period. Performance has varied year-by-year over the last twenty years, with PSRS/PEERS outperforming in some years, and MOSERS outperforming in others. Differences in investment returns between the two systems can be expected because the investments of each fund are structured under a different risk tolerance. For example, PSRS/PEERS have historically utilized a lower risk portfolio primarily because PSRS members have a sizable contribution rate and because they do not receive social security. MOSERS members are covered by social security and make no contribution into their System.

The Board of PSRS/PEERS determines the amount of risk they are willing to take with their members' retirement accounts. Attempts to boost investment returns through greater risk-taking is most likely not in the best interest of the membership. Furthermore, if the assumption of greater risk in the pursuit of higher returns becomes appropriate, the current Board of PSRS/PEERS can elect to make that decision. It should not be made by those who are solely interested in minimizing the State's obligations to fund public pension plans.

To gain perspective, consider that if MOSERS takes more risk and is paid for the risk (higher investment returns), the state contribution into the retirement system declines. If MOSERS takes more risk and the markets are negative (lower investment returns), the state contribution to the retirement system increases. Alternatively, if PSRS/PEERS takes more investment risk and the markets are negative (lower investment returns), the school district contribution to the retirement system increases AND the contribution from the Missouri educators' paycheck increases.

Perhaps the most important factor to consider when projecting future returns is to heed the SEC-mandated disclaimer: *"Past performance is not indicative of future results."*

<u>The Proposed Consolidation Would Raise Investment Expenses for PSRS/PEERS</u>

Investment expenses are hard dollar costs that will be paid whether a fund provides good investment returns or poor investment returns. Stated differently, investment expenses are guaranteed to be paid every year while investment performance is not guaranteed.

Proponents of an investment board have stated that, "by being able to cut overhead costs by not having to pay for duplicate investment staffs, there would be a reduction in contribution rates for teachers". **This is not true**. Total internal investment staff expenses for PSRS/PEERS in fiscal year 2009 were less than 7 one hundredths of a percent of total assets ($1.7 million). Thus, even if the investment staff at PSRS/PEERS were eliminated entirely, it would have virtually no impact on the contribution rate.

Proponents of the investment board have also stated that combining investment staffs will cut costs, similar to combining banks. This may be true as long as the larger bank (PSRS/PEERS) takes over the smaller bank. However, most discussions have centered on the PSRS/PEERS investments being managed under the MOSERS investment structure. This will directly increase costs to Missouri's educators and impact contribution rates.

The MOSERS internal investment staff expenses were almost double that of PSRS/PEERS in fiscal year 2009 ($3 million versus $1.7 million) despite managing approximately one-fourth of the assets. MOSERS has 50% more internal investment staff than PSRS/PEERS and a substantially higher salary structure. While this is a significant difference, it is not material enough to create a contribution rate difference on a fund of $26.6 billion.

Most importantly, the real expense would occur in asset management fees. MOSERS total investment management expenses and fees were 0.81% (or 81¢ for every $100 under management) in fiscal year 2009 while the PSRS/PEERS total expenses and fees were 0.45%. On a portfolio the size of PSRS/PEERS, this would increase management fees by tens of millions of dollars per year which could **increase** contribution rates. In fact, if PSRS/PEERS incurred the level of investment management expenses and fees paid by MOSERS, nearly $100 million of extra costs would have been incurred by PSRS/PEERS.

The PSRS/PEERS website www.psrsmo.org discloses all financial information. Additionally, investment information is updated on a quarterly basis.

Again, while PSRS/PEERS is not included in the current legislation, we are extremely concerned with the creation of any type of private investment company to manage public funds. If you wish to contact your legislator and voice your opposition to the concept of a private state investment company to manage public retirement system funds, we would suggest that you contact them when they return from spring break on March 15th. To find your legislator, go to http://www.senate.mo.gov/llookup/leg_lookup.aspx.

If you should have additional questions, please feel free to contact our office.

Sincerely,

M. Steve Yoakum
Executive Director