

MEMORANDUM #35, 2011

Commonwealth of Massachusetts | Public Employee Retirement Administration Commission
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MEMORANDUM

TO: All Retirement Boards

FROM: Joseph E. Connarton, Executive Director

RE: Chapter 176 of the Acts of 2011: An Act Providing for Pension Reform and Benefit Modernization
(Governance Provisions)

DATE: December 2, 2011

As you know, Governor Deval Patrick has signed into law Chapter 176 of the Acts of 2011, “An Act Providing for Pension Reform and Benefit Modernization”. There are many aspects to this new law some of which impact the pension benefit structure and others which impact retirement board operations. The Public Employee Retirement Administration Commission (PERAC) is taking a two pronged approach to implementing the statute. Under separate cover we will provide you with a Memorandum outlining those provisions of Chapter 176 that bear primarily on benefit structure. This Memorandum will focus on those provisions dealing with retirement board operations or Governance. Please note that these Memos are introductory in nature. The Commission urges you to review the new law in detail.

Governance

A number of sections in Chapter 176 focused on the operations of retirement boards. These sections are an outgrowth of the Commission’s efforts in working with retirement boards and their representatives, legislators and governance experts over several years. Fundamentally, this approach can be broken down into several categories – Investment Regulation, Board Member Eligibility/Education/Reporting, Procurement Reform and Enforcement. This Memorandum will briefly review each section bearing on these general categories. During the course of the next several months PERAC, through the issuance of other Memos and Forms, will provide retirement boards with further direction.

Although a number of the sections of Chapter 176 take effect pursuant to dates specifically set forth in the new law, the Governance sections, with one exception noted below, become effective on February 16, 2012.

Investment Regulation

Section 2 and Section 40 of Chapter 176 dramatically alter the investment oversight function of PERAC. This is in keeping with the evolution of board practice in this area and with an added focus on Procurement reflected elsewhere in the new law.

PERAC will no longer be providing “Exemptions” or “Waivers” focused on individual investment managers. Under Chapter 176 boards will be required to submit documentation primarily dealing with certifying that the Procurement

Process has been followed, various disclosures from the vendor, certifications from the vendor and each board member that the process was not compromised, a certification that the investment is not prohibited by regulations and any consultant reports regarding the investment and the selected vendor.

Similar submissions are required when retaining an investment consultant.

Following review of this material, the Commission will, in instances where no issues of concern arise, issue an acknowledgement and the board may go forward. Such acknowledgement may be withheld if the Commission determines that such action is in the best interest of the retirement system.

Board Member

Several provisions of the new law relate to retirement board members. As noted, these include matters regarding eligibility to serve, education and financial disclosure.

Eligibility

Although there are several areas in which an individual is prohibited from serving on a board for failing to meet education requirements or file financial information, Sections 33 and 53 provide that, "No employee, contractor, vendor or person receiving remuneration, financial benefit or consideration of any kind, other than a retirement allowance or the statutory stipend for serving in the retirement board shall be eligible to serve on a retirement board; provided, however, that an employee of a retirement board may serve on a retirement board other than the retirement board by which the person is employed; and provided, further, that this paragraph shall apply only to individuals who first become members of a retirement board on or after April 2, 2012".

Education

This requirement is contained in the new Subdivision 7 of Section 20 of Chapter 32 added by Section 35 of Chapter 176. Although this section of Chapter 176 takes effect on April 2, 2012 the Commission will commence educational activities prior to that date in order to assist retirement board members in meeting these education requirements for calendar year 2012.

The law requires that during each term a retirement board member complete 18 hours of training. In each year a member must take a minimum of 3 hours of training. However, no more than 9 hours may be credited in any one year. There is no prohibition on a member completing more than 18 hours of training in the course of a term.

PERAC will provide board members with appropriate forms to file as statements of completion of education.

Failure to meet this mandatory requirement will prohibit the member from serving beyond the conclusion of the term for which the training requirement was not met.

PERAC is required to sponsor at least 9 hours of training which include, at a minimum, the topics of fiduciary responsibility, ethical conduct and conflict of interest. An additional 9 hours is to be related to topics prescribed by the Commission and provided by local, state, regional or national entities as it may determine.

A more detailed outline of the 2012 program will be available shortly.

Financial Disclosure

Sections 1 and 36 of Chapter 176 require that each board member file an annual "Retirement Board Member Statement of Financial Interest" with PERAC. Section 1 provides that these statements will be exempt from the Public Records Law and thereby not subject to public release. Section 36 provides that "...every member of a retirement board shall file a statement of financial interests for the preceding calendar year with the commission: (i) within 30 days of becoming a member of a retirement board; (ii) by May 1 of each year thereafter that the person is a member of a retirement board; and (iii) by May 1 of the year after the person ceases to be a member of a retirement board".

Under these provisions individuals who are members of a retirement board must, by May 1, 2012, submit a Statement of Financial Interests for 2011. Also, individuals who leave a retirement board after February 16, 2012 will be required to submit a Statement of Financial Interests by May 1, 2013 for 2012. Finally, individuals who served on a retirement board in 2011 but are not serving in 2012 must, by May 1, 2012 file a Statement of Financial Interest for 2011.

Those items that must be disclosed closely parallel several of the provisions of Chapter 268B with certain exceptions. Other employment, investments, loans, reimbursements, gifts, honoraria, and other items must be disclosed.

Failure to file a Statement or the filing of an inaccurate or incomplete Statement will result in removal of the person from the board and a prohibition on that person from serving on any board.

A more detailed outline of these requirements will be available shortly.

Chapter 268A Compliance Pledge

Section 41 of Chapter 176 requires each retirement board member upon the commencement of his/her term to file with the Commission "...a statement acknowledging the member is aware of and will comply with the standards set forth in Chapter 268A, this chapter (Chapter 32) and rules and regulations promulgated under this chapter." This form must be filed by any retirement board member beginning a term after February 16, 2012.

Procurement Reform

Sections 4 and 42 of Chapter 176 set forth a specific statutory process to be followed by retirement boards when procuring and contracting for certain services. It is important to note that, although this law requires the retirement board to adhere to that specific process, under Chapter 32, Section 23(3) board members, as fiduciaries, must meet the standard of a prudent expert in taking all actions related to procurement and contracting.

Due to the fact that these provisions come into effect on February 16, 2012, retirement boards must conclude any ongoing procurement (including the execution of a valid contract) prior to that date. Consequently, all procurements that have not resulted in an executed contract as of that date will be void and retirement boards must commence a new procurement process in compliance with the new law. Although these provisions are not law until February 16, 2012, please be advised that, in order to meet the requirements of 840 CMR 19.01(1),(2),(3),(7) and (11), retirement boards must comply with the new statute regarding all regulatory submissions made after December 31, 2011. PERAC will not process any such submissions in relation to investment services unless the provisions of Chapter 176 have been followed. Such an action is permissible under the provisions of Chapter 32, Section 23 (g) and PERAC Investment Regulations.

Many of the requirements contained in the statute are clear and this memo is not intended to be an exhaustive treatise on implementation. Retirement boards and their advisers should be able to conduct procurements under the new law with little additional effort beyond what has been required for years under the fiduciary duty noted above.

Applicability

The specific provisions of Section 23B of Chapter 32 apply to all contracts and procurements for investment, actuarial, legal and accounting services. Under paragraph (k) of that Section there are additional provisions relative to the procurement of services from an "investment service provider". These would include, but not be limited to, managers, partnerships, trusts, custodians, consultants, proxy services, securities litigation services and services related to the financial information (cash books, pooled fund statements, Annual Statements) the retirement boards must file with PERAC.

Paragraph (c) of Section 23B mandates that a contract for procurement of legal, investment, actuarial and accounting services must take place utilizing "...competitive sealed proposals, in accordance with this section."

Procurement File

Under paragraph (d) a retirement board that must “maintain a file on each contract” which retains “all written documents required by this section.” In addition, this paragraph addresses the issue of records retention by requiring that these documents “...be retained by the retirement board for at least 6 years from the date of final payment under the contract.”

Request for Proposals (RFP)

For all procurements covered by the statute the retirement board **must** “solicit proposals through a request for proposals”. That RFP must include, among other items set forth in paragraph (g) of Section 23B, the following:

- (1) The time and date for receipt of proposals, the address of the office to which the proposals are to be delivered and the maximum time for proposal acceptance by the retirement board;
- (2) The purchase description and all evaluation criteria that may be utilized;
- (3) All contractual terms and conditions.

Evaluation

The initial evaluation of the responses to the RFP is the responsibility of the retirement board. However, with respect to investment management services, the investment consultant may conduct the initial evaluation. That evaluation must be in writing and based **solely** on the criteria set forth in the RFP.

Each proposal is to be rated as highly advantageous, advantageous, not advantageous or unacceptable based on the evaluation criteria. The retirement board or investment consultant, if applicable, must state the reasons for the rating.

Each proposal is to be assigned a composite rating and the retirement board or investment consultant, if applicable, must state the reasons for the rating.

Any revisions to a proposed plan for providing services should be obtained by negotiation prior to awarding the contract. It should be noted that any such revision that is agreed to by the retirement board that diminishes the rights of the retirement board as originally proposed may result in a violation of fiduciary duty.

In the event that the initial evaluation is conducted by the investment consultant the consultant **must** review evaluations of **all** the proposals with the retirement board and provide each member with the initial evaluation of each proposal.

Decision

The retirement board shall determine the most advantageous proposal from a responsible and responsive offeror taking into consideration price and the evaluation criteria. An award may be conditioned on “...successful negotiation of the revisions specified in the evaluation...” Any omission of a revision so specified must be explained in writing.

Negotiation

As noted, the retirement board or its duly designated agent, subject to the approval of the retirement board, may negotiate all terms of the contract not deemed mandatory or non-negotiable. If, after negotiation, the retirement board determines that it is in the best interest of the retirement system not to award the contract to that vendor, it may determine the proposal which is next most advantageous from a responsible and responsive vendor and may negotiate terms of the contract with that vendor.

Disclosures

On or before January 1 of **each year** and as part of the RFP process all contractors or prospective contractors must file annual disclosures with the retirement board and PERAC. These include disclosure of arrangements for compensation paid or to be paid to a contractor or a related person in connection with the services the contractor provides to the retirement board or any other client; disclosure of compensation in whatever form paid or expected to be paid by the contractor or a related person to others in relation to the services provided to the retirement board or any other client;

and disclosure of any conflict of interest that the contractor may have that may interfere with the ability of the contractor to provide unbiased and objective services to the retirement board.

Cancellation/Rejection

The retirement board may cancel an RFP or reject in whole or in part any and all proposals if it determines that cancellation or rejection serves the best interests of the retirement system. The reason (s) for the cancellation must be stated by the retirement board in writing.

Vendor/Board Forms

In accordance with the new law, proposals submitted to a retirement board must include a Vendor Certification Form by which vendors certify under the pains and penalties of perjury that the proposal “has been made and submitted in good faith and without collusion or fraud with any other person.”

In addition, each retirement board member must certify to PERAC under the pains and penalties of perjury “that, to the best of the members knowledge and belief, this proposal has been made and submitted in good faith and without collusion or fraud with any person.”

Term

No contract may be awarded for a term exceeding 5 years, however, a retirement board may participate in a limited partnership, trust or other entity with a term for a longer period “...as part of an investment of system assets.” As a result, all contracts entered into by a retirement board must explicitly state a term consistent with the new law.

Written Contracts

All contracts must be in writing and no payment may be made for a service rendered prior to execution of a contract.

Penalties

A contract made in violation of these provisions is not valid and the retirement board may not make any payments under such a contract.

Any person conspiring to cause a contract to be solicited or awarded in violation of these provisions will pay to the retirement board not more than \$2,000 for each violation. In addition, such a person will pay the retirement board double the amount of damages sustained by the retirement board as a result of the violation.

As noted above, the provisions of the new law pertaining to procurement are clear, concise and easily understood. During the course of its educational efforts the Commission will review various aspects of procurement best practices, however, retirement boards in concert with their attorneys and consultants should be able to implement the law as written.

Enforcement

Section 38 of Chapter 176 authorizes PERAC to debar contractors and vendors thereby excluding such contractors and vendors from “contracting or subcontracting with a retirement board”.

Debarment may be imposed for a number of reasons including:

1. Conviction or final adjudication by a court or administrative agency of the following:

- (a) a criminal offense related to obtaining or attempting to obtain a contract or subcontract or the performance of such a contract or subcontract;
- (b) a criminal offense involving embezzlement, theft, forgery, bribery, falsification or destruction of records, receiving stolen property or other offenses indicating a lack of business integrity or

honesty;

- (c) a violation of state or federal antitrust laws;
- (d) a violation of Chapter 268A (the State Ethics Law);
- (e) a violation of Chapter 32.

1. Substantial evidence of any of the following:

- (a) providing false information in connection with obtaining or trying to obtain a contract;
- (b) failure to comply with record keeping and accounting requirements of law or regulation;
- (c) failure to perform or unsatisfactory performance;
- (d) submission of an inaccurate disclosure statement;
- (e) failure to disclose certain compensation;
- (f) any cause affecting the responsibility of a vendor which the Commission determines to be serious and compelling enough to warrant debarment.

As noted within, additional guidance will be provided on the “non-governance” aspect of Chapter 176 of the Acts of 2011.

Thank you for your cooperation in this matter.