

MEMORANDUM #39, 2011

Commonwealth of Massachusetts | Public Employee Retirement Administration Commission

Five Middlesex Avenue, Suite 304, Somerville, MA 02145

Ph 617 666 4446 | Fax 617 628 4002 | TTY 617 591 8917 | www.mass.gov/perac

Domenic J. F. Russo, *Chairman*

Auditor Suzanne M. Bump | Alan Macdonald | James M. Machado | Donald R. Marquis | Robert B. McCarthy |

Gregory R. Mennis

Joseph E. Connarton, *Executive Director*

MEMORANDUM

TO: All Retirement Boards

FROM: Joseph E. Connarton, Executive Director

RE: Chapter 176/Contracts

DATE: December 15, 2011

The Public Employee Retirement Administration Commission (PERAC) has provided retirement boards with two memoranda that focused on a general overview of Chapter 176 of the Acts of 2011 (PERAC Memo #35 - 2011 and PERAC Memo #36 - 2011). As the retirement community transitions to the new statute, we will be disseminating other memoranda and advisories. PERAC recognizes the complexities and challenges of the new law and its impact on longstanding practices of the retirement boards.

Statutory Language

The statutory language in the new Section 23B applies to "...every retirement board contract for the procurement of investment, actuarial, legal and accounting services." It is important to note that, although this law requires the retirement board to adhere to the specific process of that section for contracts related to the listed services, 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 for services. Thus, in contracts for procurement for other services such as software, investigation, and medical services, retirement board members must meet the fiduciary standard.

Among other things, Chapter 176 addresses procurement and contracts. In particular, with respect to contracts, Section 23B of Chapter 32 requires that "...all contracts shall be in writing and the retirement board shall make no payment for a service rendered prior to the execution of a contract" and also requires that "...a retirement board shall not award a contract for a term exceeding five years, including any renewal, extension, or option...".

It should be noted that, although the vendor selected for the performance of a discrete task such as the completion of an actuarial valuation must be chosen in accordance with the provisions of Section 23B, the contract related to that task generally will not contain a term that would run afoul of the five year rule.

Contract Review

An initial review of the contracts that the retirement board presently has in force with vendors will enable a determination to be made as to the new law and its impact on existing relationships.

Existing Written Contracts - Term 5 Years or Fewer

An existing written contract with a term of five years or fewer **will remain** in effect until the end of its term at which point Section 23B will apply. For example, two years ago the retirement board executed a written contract with a vendor for a five year term. That contract is not affected by the new law, however, at the conclusion of the five year term (three years) the new law must be followed. In this context, the provisions of Section 23B pertaining to extension, options and renewal of contracts do apply, and the contract cannot be extended beyond the five year term even though it was entered into prior to February 16, 2012. The term "extension" applies to amendments to the contract that increase the total number of years resulting in a period longer than a five year term and, thus, any such amendment is not consistent with the statute.

Existing Written Contracts - No Term

Please be advised that failure to have a written contract containing a term of five years or fewer in place on February 16, 2012 will put the retirement board in violation of Section 23B. Consequently, those retirement boards with a written contract that does not contain a term **should consider amending** any such contract to bring it into compliance with Section 23B. The process of amendment for this purpose also provides an opportunity for the retirement board to review and, if warranted, seek to change other provisions of the agreement. In the event that no such amendment is negotiated the retirement board must conduct a competitive search. Unless a retirement board conducts such a competitive search and executes a written contract before February 16, 2012 establishing a term of no longer than five years, it will be necessary to conduct a search under Section 23B as soon as possible after that date. That search must result in the execution of a written contract with a term of five or fewer years. In those circumstances PERAC will allow the continuation of existing contracts until the Section 23B process is completed. The retirement board will not be found to be in violation of Section 23B provided it concludes its Section 23B search by July 1, 2012.

Trusts, Commingled Funds or Mutual Funds

In some circumstances the structure of investment vehicles may be a trust, commingled fund or mutual fund which allows for regular commitment and liquidation of the investment. The underlying documents establishing the structure will be open - ended as to term. In order to meet the five year maximum requirement under Section 23B, the retirement board should, as part of the motion authorizing the investment, include language stating that the commitment to the entity is for a maximum period of five years. In addressing existing relationships such a motion should be adopted as soon as possible.

No Written Contract

In the event that a retirement board is being provided services without a written contract no further payments may be made under any such arrangement and the retirement board must conduct a competitive search for such services. Consequently, unless a retirement board conducts a competitive search and executes a written contract before February 16, 2012 establishing a term of no longer than five years, it will be necessary to conduct a search under Section 23B as soon as possible after that date. That search must result in the execution of a written contract with a term of five or fewer years.

Termination of a Contract

The term of years set forth in statute does not preclude the retirement board from entering into a contract that allows either party to terminate the contract prior to the term ending. The five year provision is a maximum length and it does not prevent the parties from negotiating termination provisions within that time frame.

Maximum Term of a Contract

The law provides that the maximum term for a contract is five years. Thus, prior to the conclusion of that period, a search must be completed under Section 23B regardless of the level of satisfaction the retirement board may have with the services provided by the vendor.

PRIM

A question has been raised relative to the applicability of Section 23B to retirement board relationships with the Pension Reserves Investment Trust Fund (PRIT). Investment in PRIT by a retirement board is specifically authorized by Chapter 32, Section 23. As a result, there is no prerequisite for a retirement board to invest in PRIT and Section 23B does not apply to investment by retirement boards in the PRIT Fund.

As noted, PERAC recognizes the complexities of the new law and, although this memorandum does not necessarily address all the issues pertaining to procurement and contracts embodied therein, we hope that this will assist retirement boards and vendors during this transition period.

Thank you for your continued cooperation in this regard.