

WEST VIRGINIA
SECRETARY OF STATE
KEN HECHLER
ADMINISTRATIVE LAW DIVISION

Form #3

FILED

AUG 16 3 32 PM '93

OFFICE OF WEST VIRGINIA
SECRETARY OF STATE

**NOTICE OF AGENCY APPROVAL OF A PROPOSED RULE
AND
FILING WITH THE LEGISLATIVE RULE-MAKING REVIEW COMMITTEE**

AGENCY: Wv State Board of Investments TITLE NUMBER: 113

CITE AUTHORITY WV Code 12-6-5 et seq.

AMENDMENT TO AN EXISTING RULE: YES NO

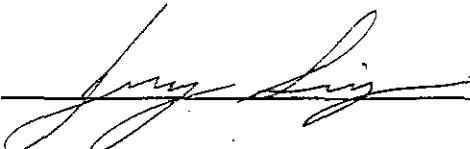
IF YES, SERIES NUMBER OF RULE BEING AMENDED: 2

TITLE OF RULE BEING AMENDED: Rule for the Administration
of the Consoildated Pension Fund

IF NO, SERIES NUMBER OF NEW RULE BEING PROPOSED: _____

TITLE OF RULE BEING PROPOSED: _____

THE ABOVE PROPOSED LEGISLATIVE RULE HAVING GONE TO A PUBLIC HEARING OR A PUBLIC COMMENT PERIOD IS HEREBY APPROVED BY THE PROMULGATING AGENCY FOR FILING WITH THE SECRETARY OF STATE AND THE LEGISLATIVE RULE MAKING REVIEW COMMITTEE FOR THEIR REVIEW.



9.20

Board Members:

Honorable W. Gaston Caperton, III
Governor/Chairman

Mr. John T. Poffenbarger
Executive Secretary/Member

Honorable Larrie Bailey
Treasurer/Member

Honorable Glen B. Gainer, III
Auditor/Member

Mr. Dwight Keating
Member

Mr. Richard Riederer
Member

Mr. William T. Tracy
Member



State of West Virginia
Board of Investments

Suite E-122
State Capitol
Charleston, WV 25305
Telephone: (304) 558-5000
Telefax: (304) 344-9284

Staff:

H. Craig Slaughter
Executive Director

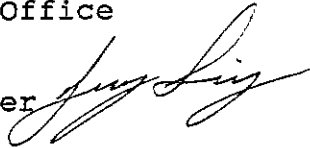
D. Jerry Simpson
Chief Operating Officer

Matthew E. Jones
Chief Financial Officer

Diana Will
Chief Investment Officer

Mark E. N. Asaad
General Counsel

To: Judy Cooper
Secretary of State's Office

From: Jerry Simpson
Chief Operating Officer 

Date: August 13, 1993

Subject: Filing of The Approved Rules for the Consolidated
Pension Fund

Attached for your review is all the material required concerning the filing of the approved rules for the "Administration of the Consolidated Pension Fund". It should be noted that these rules were filed on emergency basis (copy of memo attached) on June 18, 1993.

If you require any additional information, please call me at 558-5000.

Board Members:

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Diana Will
Chief Investment Officer

Mark E. N. Asaad
General Counsel

To: Marie Nickerson
Legislative Rule-Making Review Committee

From: Jerry Simpson
Chief Operating Officer

A handwritten signature in cursive script, appearing to read "Jerry Simpson".

Date: August 13, 1993

Subject: Filing of Rules for the Consolidated Pension Fund

Attached for your review are fifteen (15) copies of the material filed with the Secretary of State's Office concerning amendments to the rules for the "Administration of the Consolidated Pension Fund". It should be noted that these rules were filed on emergency basis (copy of memo attached) on June 18, 1993.

If you require any additional information, please call me at 558-5000.

Board Members:

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Executive Secretary/Member

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Mark E. N. Asaad
General Counsel

To: Marie Nickerson
Legislative Rule-Making Review Committee

From: Jerry Simpson
Chief Operating Officer *J.S.*

Date: June 18, 1993

Subject: Notice of an Emergency Rule

On this date, emergency rules were filed with the Secretary of State. These emergency rules are amended rules titled "Rules For The Administration Of The Consolidated Pension Fund". A copy of all documents are attached for your review.

If you require any additional information, please call me at 558-5000.

4. Explanation of Overall Economic Impact of Proposed Rule.

A. Economic Impact on State Government.

THESE PROPOSED RULES WILL CONTINUE TO ALLOW THE PENSION FUNDS OF THE STATE TO BE FULLY INVESTED AND ACCOUNTED FOR ON A MORE ACCURATE BASIS.

B. Economic Impact on Political Subdivisions; Specific Industries; Specific groups of citizens.

ALTHOUGH THERE ARE CURRENTLY NO LOCAL GOVERNMENT PENSION FUNDS INVESTED BY THE BOARD, THESE RULES WOULD INSURE THAT IS THIS WERE TO OCCUR AT SOME FUTURE DATE THESE FUNDS WOULD BE PROPERLY ACCOUNTED FOR.

C. Economic Impact on Citizens/Public at Large.

SEE 4A.

Date: _____

6/18/93

Signature of Agency Head or Authorized Representative

The general purpose of these rules is to aid in the implementation of the legislative findings and purpose set forth in Section One, Article One, Chapter Twelve of the Code, wherein the Board and the Treasurer are authorized to develop and maintain modern systems, consistent with sound financial practices, for the collection, disbursement, management and invest of public moneys. The rules of this series implement such legislative intent by prescribing procedures governing participation in, and administration of, the Consolidated Pension Fund to be administered by the Board, for the purpose of enabling the participating Pension Funds to maximize the return on their investments.

DATE: June 18, 1993

TO: LEGISLATIVE RULE-MAKING REVIEW COMMITTEE

FROM: West Virginia State Board of Investments

EMERGENCY RULE TITLE: Rules for the Administration of the
Consolidated Pension Fund

1. Date of filing: June 18, 1993
2. Statutory authority for promulgating the emergency rule:
Chapter 12-6-5
3. Date of filing of proposed legislative rule: June 18, 1993
4. Does the emergency rule adopt new language or does it amend or repeal a current legislative rule?
Amends current rules
5. Has the same or similar emergency rule previously been filed and expired?
No
6. State, with particularity, those facts and circumstances which make the emergency rule necessary for the immediate preservation of public peace, health, safety or welfare
The third extraordinary session of the 1990 Legislature
authorized the Board of Investments to invest in equities
(Code section 12-6-9(j)). The Board of Investments has selected
investment advisors and is now positioned to begin equity purchases.
These rule changes implement the provisions of this code section.

7. If the emergency rule was promulgated in order to comply with a time limit established by the Code or federal statute or regulation, cite the Code provision, federal statute or regulation and time limit established therein.

N/A

8. State, with particularity, those facts and circumstances which make the emergency rule necessary to prevent substantial harm to the public interest.

These rules only effect the participants in the consolidated pension fund.

WEST VIRGINIA ADMINISTRATIVE REGULATIONS
West Virginia State Board of Investments

Chapter 12-6
Series II
(1990)

Subject: Rules for the Administration of the Consolidated Pension Fund by the West Virginia State Board of Investments.

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FILED

WEST VIRGINIA ADMINISTRATIVE REGULATIONS
West Virginia State Board of Investments ~~Aug 16~~ 3 32 PM '93

Chapter 12-6
Series II
(1990)

OFFICE OF WEST VIRGINIA
SECRETARY OF STATE

Subject: Rules for the Administration of the Consolidated Pension Fund by the West Virginia State Board of Investments.

Section 1. General

1.01. Scope - These rules implement the provisions of West Virginia Code §12-6-1 et. seq. relating to the Consolidated Pension Fund established by §12-6-8(b).

1.02. Authority - West Virginia Code §12-6-5; §12-6-8.

1.03. Purpose - The general purpose of these rules is to aid in the implementation of the legislative findings and purpose set forth in West Virginia Code §12-1-1, wherein the Board is authorized to develop and maintain modern systems, consistent with sound financial practices, for the collection, disbursement, management and investment of public moneys. These rules and regulations implement such legislative intent by prescribing procedures governing participation in, and administration of, the Consolidated Pension Fund to be administered by the Board, for the purpose of enabling the participating Pension Funds to maximize the return on their investments.

1.04. Filing Date -

1.05. Effective Date -

1.06. Repeal of Former Rule - This legislative rule repeals and replaces WV 113 CSR2 "Rules for the Administration of the Consolidated Pension Fund by the West Virginia State Board of Investments" filed ~~April-13-1990~~ May 17, 1991 and effective ~~April-13-1990~~ May 17, 1991.

Section 2. Definitions

For purposes of these rules, unless a different meaning clearly appears from the context;

"Board" means the West Virginia State Board of Investments;

"Code" means the West Virginia Code of 1931, as amended;

"Consolidated Pension Fund" means the investment fund managed by the Board and established pursuant to West Virginia Code §12-6-8(a);

"Participant" means all Pension Funds, entities or individuals contributing moneys or assets to the Consolidated Pension Fund;

"Pension Funds" means and includes the Workers' Compensation Fund; the Workers' Compensation Fund II; the Pneumoconiosis Fund; the State Teachers' Retirement System Fund; the Death, Disability and Retirement Fund for members of the Department of Public Safety's Division of Public Safety; the Public Employees' Retirement System Funds; the Judges' Retirement Fund; the Municipal Police Officers' Pension and Relief Funds; the Fire Fighters' Pension and Relief Funds and such other retirement or pension funds and systems established

on behalf of public employees of the State or of its political subdivisions and administered by the State;

"Securities" shall have the same meaning set forth in West Virginia Code §12-6-2;

"Select U. S. Government Agency Obligation" means any evidence of indebtedness issued by any of the following: the Government National Mortgage Association (GNMA), Resolution Trust Corporation Securities (RTC);

"U. S. Government Agency Obligation" means and includes any obligation of any United States government agency guaranteed as to the payment of both principal and interest, directly or indirectly, by the United States of America, including but not limited to the following: the Government National Mortgage Association (GNMA); the Federal Farm Credit Bank (FFCB); Federal Land Banks (FLB); the Federal Home Loan Mortgage Corporation (FHLMC); the Federal National Mortgage Association (FNMA); Federal Home Loan Banks (FHLB); Federal Intermediate Credit Banks; Banks For Cooperatives; Tennessee Valley Authority (TVA); United States Postal Service; Farmers Home Administration (FHA); Export-Import Bank; Federal Financing Bank; Student Loan Marketing Association (SLMA); Resolution Trust Corporation Securities (RTC); and Veterans Administration (VA); and

"U. S. Government Obligations" means any direct obligation of, or obligation guaranteed as to payment of both principal and interest by, the United States of America.

Section 3. Mechanics of Participation in the Consolidated Pension Fund

Pension Funds may participate in the Consolidated Pension Fund by making written or electronic requests to the Board of Investments. Written Requests for deposits or withdrawals shall state the amount which the Pension Fund wishes to make available for investment, or the amount which it wishes withdrawn, as the case may be. Such requests shall also contain other information which the Board of Investments considers necessary. The Board of Investments may require advance notice, as determined by the Board, for withdrawals of one million (\$1,000,000.00) or more.

Section 4. Accounting

4.01. Nature of Ownership - ~~Each Participant shall own a hundred percent (100%) interest in the pool in which its funds are invested.~~ Each Participant shall own an undivided interest in the portfolio of the Consolidated Pension Fund based on the Participant's prorata contribution of assets at any time. Ownership shall be expressed in terms of units. Each Participant, by completing and returning an "Account Request Form" to the Board of Investments, has consented to the methods of sharing gains and losses and all other accounting methods required or adopted by the Board.

4.02. Accounting System - The Board of Investments shall implement an accounting system based on generally-accepted accounting principals principles.

speculation, but for investment, considering the probable safety of their capital as well as the probable income to be derived.

(c) Permissible Investments - The Consolidated Pension Fund shall abide by West Virginia Code §12-6-9, as amended, and these rules and regulations with regard to permissible investments.

(d) Social Responsibility - To the extent that investments are consistent with all other standards established by the Board, selection of investments should consider the best interests of the people of the State of West Virginia.

(e) Custody - The Board shall designate and maintain custodian arrangements in its sole discretion and no investment advisor shall maintain custody of the securities of the Consolidated Pension Fund.

(f) Investment Advisors - The Board may select and contract with investment advisors who shall act in accordance with the terms and conditions specified by the Board and the applicable State and Federal laws.

(g) Investment Objectives - All pools within the Consolidated Pension Fund shall be subject to the investment objectives listed below in descending order of priority:

(1) Preservation of Capital - To preserve the capital investment in the Consolidated Pension Fund.

(2) Diversification - To diversify the investment of the assets of the Consolidated Pension Fund so as to minimize the risk of large losses.

(3) Rate of Return - To achieve a rate of return consistent with the rate of return objectives set by the Board.

(4) Stability - To maintain a high level of security in the Consolidated Pension Fund by minimizing risk and volatility insofar as possible within the rate of return objectives set by the Board.

(5) Turnover - To minimize transaction costs.

(6) Liquidity - To maintain sufficient liquidity to provide for all anticipated withdrawals or transfers and to invest in securities with sufficient marketability to provide for unexpected withdrawals.

(h) Investment Restrictions

(1) The Consolidated Pension Fund shall abide by the investment restrictions of West Virginia Code §12-6-10 and as further set forth by the Board.

(2) Not more than 20% of the portfolio of the Consolidated Pension Fund may be invested in any single industry sector. (The utility industry

shall be separated for the purpose of this restriction between telephone, electric, gas distribution, and similar segments.)

(3) The Consolidated Pension Fund shall maintain a reasonable balance between the various classes of fixed income securities, without over-concentration.

(4) The Consolidated Pension Fund shall abide by the quality restrictions of West Virginia Code §12-6-9.

(5) Investment in financial futures contracts, options and other similar instruments shall be authorized for the sole purpose of performing hedges in order to reduce the risk associated with fluctuations in interest rates or market prices. Such investments shall be limited to direct obligations of, or obligations guaranteed as to the payment of both principal and interest by, the United States of America; namely, Treasury bills, notes, bonds and GNMA's. For purposes of these rules and regulations, the word "hedge" means taking a position in the futures or options market which is opposite and approximately equal to the one held in the cash market. This is a defensive strategy and shall only be used to protect the overall values of the various portfolios. Advance unanimous approval of the Board must be obtained

prior to each transaction in instruments of this type.

(6) Not more than twenty percent of the portfolio of the Consolidated Pension Fund may be invested in equities listed on the Standard and Poor's 500.

(7) The Board shall rebalance the portfolio between fixed income securities and equities within two weeks following the end of each calendar quarter based on the percentage of fixed income securities and equities in the portfolio on the last day of each quarter. All calculations to determine the balance between the fixed income portfolio and equities portfolio shall be made with the securities being valued according to general accepted accounting principles.

(8) The Board and its advisors shall purchase and sell equities on a best execution basis.

5.02. Investment Pools - The Consolidated Pension Fund is composed of various investment pools for the Pension Funds. It is the intent of the Board that the composite Consolidated Pension Fund meet ~~there-be-separate-portfolio-guidelines-for-the-administrator-of-each-investment-pool-in-addition-to-the-policies-objectives-and-restrictions-set-forth-in-Subsection 5.01.---The-Board-of-Investments-shall-administer-each-investment-pool-in-the-Consolidated-Pension-Fund-in-accordance-with-these-rules-and-regulations-and-as-may-be-further-prescribed-by-the-Board.---All-the-investment-pools-which~~

~~compose the Consolidated Pension Fund shall be required to meet individually the guidelines outlined in Tables I and II of this Rule. Due to the presently existing non-liquid investments contained in the portfolio on the effective date of these rules and regulations, the current investment portfolio may not be considered when applying the maximum limit on the obligations of any single private corporation for 5 years from these effective date of these rules and regulations.~~

5.03. Instructions for Use of Tables - The percentages in the "Minimum" column are the minimum percentages which the Board must maintain in each type of investment instrument. For example, the 15% figure in Table I, Line 1, means that a minimum of fifteen percent of the Investment-Peer Consolidated Pension Fund shall be invested in U. S. Government obligations. If the minimum percentage is "0", as in Table I, Line 2, the Board of Investments is not required to invest any moneys of the peer fund in instruments of that type.

The percentages in the "Maximum" column are the maximum percentages of the peer fund which may be maintained in each type of instrument. For example, in Table I, Line 1, the 100% figure in the "Maximum" column means that the Board may keep the entire peer fund invested in U. S. Government obligations. If the maximum percentage is "10", as in Table I, Line 4, this means that the Board of Investments is permitted to invest in instruments of that type up to a maximum of 10% of the peer fund.

In Table 1, the "Code Reference" column refers to the section of the West Virginia Code which authorizes the kind of instrument described under the "Instrument" column.

TABLE I.
GUIDELINES FOR DIVERSIFICATION
ACCORDING TO KIND OF INVESTMENT INSTRUMENT

	<u>Instrument</u>	<u>Code Reference</u>	<u>Minimum</u>	<u>Maximum</u>
1.	U. S. Government Obligation	§12-6-9(a)	15%	100%
2.	U. S. Government Agency Obligation	§12-6-9(b)	0%	85%
3.	Federally insured WV home mortgages	§12-6-9(d)	0%	10%
4.	Privately insured pools of WV home mortgages	§12-6-9(f)	0%	10%
5.	Corporate bonds, notes debentures, commercial paper and other evidence of indebtedness	§12-6-10(1) §12-6-9(g)	0%	75%
6.	Commercial paper and other corporate ob- ligations maturing in less than one year	§12-6-10(2) §12-6-9(g)	0%	20%
7.	Obligations of any single private corporation	§12-6-10(3)	0%	3%
8.	Fully collateralized WV certificates of deposit maturing in less than one year	§12-6-9(h)	0%	30%
9.	Repurchase agreements	§12-6-5(9)	0%	75%
10.	Reverse repurchase agreement	§12-6-5(10)	0%	15%
11.	Equity securities of Standard & Poors 500 Companies	§12-6-9(j)	0%	20%

TABLE II

GUIDELINES FOR DIVERSIFICATION

ACCORDING TO QUALITY OF CORPORATE DEBT INSTRUMENTS

AUTHORIZED BY TABLE I

<u>Instrument</u>	<u>Minimum</u>	<u>Maximum</u>
1. Corporate bonds and notes rated "AAA" or equivalent	0%	100%
2. Corporate bonds and notes rate "AA" or equivalent	0%	50%
3. Corporate bonds and notes rated "A" or equivalent	0%	30%
4. Commercial paper rated in highest grade ("P-1" or equivalent)	0%	20%

Any corporate debt instrument that is downgraded following purchase may be liquidated at the Board of Investment's discretion if such downgrading puts the debt instrument out of compliance with Table II.

TABLE II

GUIDELINES FOR DIVERSIFICATION

ACCORDING TO QUALITY OF CORPORATE DEBT INSTRUMENTS

AUTHORIZED BY TABLE I

	<u>Instrument</u>	<u>Minimum</u>	<u>Maximum</u>
1.	Corporate bonds and notes rated "AAA" or equivalent	0%	100%
2.	Corporate bonds and notes rate "AA" or equivalent	0%	50%
3.	Corporate bonds and notes rated "A" or equivalent	0%	30%
4.	Commercial paper rated in highest grade ("P-1" or equivalent)	0%	20%

Any corporate debt instrument that is downgraded following purchase may be liquidated at the Board of Investment's discretion if such downgrading puts the debt instrument out of compliance with Table II.

Section 6. Miscellaneous

6.01. Minimum Amount of Investment - The minimum amount of investment in the Consolidated Pension Fund is One Thousand Dollars (\$1,000.00). There is no minimum time for which deposits will be retained.

6.02. Payment of Expenses from Earnings - The Board of Investments shall deduct expenses incurred in the administration of the Consolidated Pension Fund from the gross earnings of the fund monthly. Such fees shall be established by the Board on a pro rata basis.

6.03. Board Reports - The Board of Investments staff shall provide Board members a monthly financial statements prepared in accordance with Generally Accepted Accounting Principles and financial schedules report reflecting all purchases, and sales, and trades for each pool. ~~and also, a copy of the portfolio for each investment pool, reflecting the market value for each investment.~~

6.04. Authorized Financial Institutions and Brokers - The Board of Investments staff may not do business with any financial institution or brokerage firm that has not been approved by Board members. At the first Board meeting of each fiscal year, the Board of Investments staff shall provide Board members with a complete list of all financial institutions and brokerage firms for which the Boards staff request to transact business, currently on the approved list for their review and approval.

6.05 Reserve for Losses - The Board is authorized to establish, by appropriate accounting method, a reserve for loan losses. No interest shall be included in earnings calculations on any loans that are delinquent by sixty days or more, or for which the Board's staff determine collection to be doubtful.

WEST VIRGINIA ADMINISTRATIVE REGULATIONS
West Virginia State Board of Investments

Chapter 12-6
Series II
(1990)

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WEST VIRGINIA STATE BOARD OF INVESTMENTS

MINUTES

PUBLIC HEARING - CONSOLIDATED PENSION FUND RULES & REGULATIONS

July 22, 1993

The West Virginia State Board of Investments held a public hearing on proposed amendments to the Rules and Regulations for Consolidated Pension Fund on Thursday, July 22, 1993, at 1:00 P.M. in the State Capitol Complex Conference Center, Building 7 - Room B.

Jerry Simpson, Chief Operating Officer, WV Board of Investments, presided.

Others in attendance included:

Craig Slaughter, State Board of Investments
Matthew Jones, State Board of Investments
Diana Will, State Board of Investments
Mark Asaad, State Board of Investments
June Coffey, State Board of Investments
John D. Hoff, WV Association of Counties
Charles B. Williams, Public Employees Retirement System
Association
Glen B. Gainer III, State Auditor
Paul S. Mollohan, State Auditor's Office
Sam Cole, State Treasurer's Office
Don Adams, Division of Highways
Michael E. Sizemore, Legislative Auditor's
Ellen Quillen, Legislative Auditor's

Mr. Simpson called the meeting to order. He introduced the members of the State Board of Investments who were present including Mr. Asaad who served as Chairman of the meeting.

Mr. Asaad stated the rules for the hearing as follows:

- (1) Those who had registered to speak at the hearing would be allowed five minutes to make oral statements;
- (2) At the end of the oral statements the questions raised during the comments would be addressed; and
- (3) Any written comments delivered to the Recording Secretary during the meeting will be incorporated in the record.

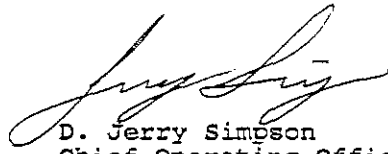
Consolidated Pension Fund

Mr. Asaad stated that any written comments regarding the rules for the Consolidated Pension Fund should be given to the recording secretary for incorporation into the minutes.

Mr. Jones stated that there were two main changes: (1) incorporation of administrative procedures for equities as allowed by State Statute and (2) clarification that, for the purpose of calculating the limitations on the amount of any particular type of asset that could be held, the total value of the consolidated pension fund would apply rather than the value of any one particular fund.

The attached is a summary of the comments made by the individuals who spoke and the Staff's responses.

The hearing was adjourned.



D. Jerry Simpson
Chief Operating Officer

Board of Investments
Public Hearing Held July 22, 1993
Consolidated Pension Fund Rules
Oral Comments and Questions Received

The following oral comments and oral questions were received and are presented below with the Board of Investments' staff reply where applicable. Many of the questions and comments received relate to the Board's plan to restructure the portfolios within the Consolidated Pension Fund. Although the changes made in these rules and regulations allow for a restructuring, the changes were not made specifically for the restructuring nor do they mandate that it occur. Conversely, they are made to address changes necessary for the full implementation of the investment program in equities as authorized by statute. Therefore, these rules should be put into effect regardless of any subsequent restructuring of the portfolios within the Consolidated Pension Fund.

Charles B. Williams - Public Employees Retirement System Association (PERSA)

1. Expressed PERSA's concern regarding the investment of Public Employees Retirement System (PERS) funds in equities. Implied that all funds should be invested in US Treasury Notes. PERSA doesn't want these funds to be at risk in any way since PERS is overfunded in excess of \$100 million.
2. Expressed PERSA's concern that the proposed rules and regulations may create a violation of the contractual agreement in force at the time of a PERS retirees' retirement.

RESPONSE

1. The question addresses the prudence of investing in equities. This question was debated by the legislature prior to the WV Code being amended to allow equities as a permissible investment.
2. The proposed rules and regulations in no way change the participant benefits which are statutorily defined. There is no violation of any statutory contract between the State and the retirees or current plan participants.

Don Adams - State Employee

1. Asked how the proposed consolidation of assets of the various retirement systems into a single pool came about?
2. Why was it needed?
3. As it relates to the ownership of the investment pool, how is each participants's pro rata contribution to be determined? If it is determined based upon the market value, what date is that market value to be determined?
4. If ownership is expressed in units, does the unit have value? If so, what is the value of the unit? Is the fund on the day of distribution going to be given X number of units or is it going to be given a single unit with a single value?
5. Upon valuation of the assets, there are going to be some adjustments to be made between the market value on the date of distribution of the unit and the book value that the investment pool is carrying; how are these adjustments to be handled?
6. When the Consolidated Pension Fund was created in March, 1979, adjustments were made on the books of the State Auditor and State Treasurer reflecting the current market value of the securities purchased from the various retirement funds. After the adjustments were made reflecting the purchase of the securities by the Board, all of the retirement funds reflected "losses". Is the same thing going to occur this time? If this is true, is the Board basically duplicating and diminishing the book value of the total portfolios a second time from March 1979 and, if not, are there plans to reverse the book entry of March 1979 and have a single diminishing of the book value of the assets?
7. How are the earnings going to be distributed? Is the Board going to distribute new units or portions of units? Is the portfolio going to be totally revalued on the date of distribution of earnings or is the Board just going to take the earnings and distribute them? What mechanism is going to be used to distribute the earnings?
8. Each of the pension funds have their own advisor; each of them have different goals; each of them have different strategies which they use. If the current pension fund investment pools are consolidated into one, is it the Board's idea to diminish all advisors down to one or is the Board still going to have multiple advisors for multiple funds that are within the one large pool. If this occurs, how does each of them maintain their individual strategies which they use and how is the Board going to work and intertwine these strategies? An example is that PERS is longer term because the earnings that are produced will meet current annuity requirements. Therefore

the goals and strategy used by the PERS advisor is much different than the Teachers' Retirement wherein they must use all earnings to meet their annuity payments. Therefore, the advisor's strategy for Teachers' Retirement is going to be entirely different than the strategy used by the advisor for PERS.

9. During the legislative session that has just ended, there was an attempt made to do something similar to this. The Legislature said "no". The Board's staff is now attempting by rules and regulations to do something that the Legislature said no to statutorily. I think that this will be to the disadvantage to PERS. They are the only one of the four pension funds that's actuarially sound, and every time something is done for the entire package it will benefit the others who are extremely underfunded to the detriment of PERS.

RESPONSE

- 1 - 7. Questions 1 - 7 relate to the mechanics of how the portfolios of Consolidated Pension Fund would be restructured and are not related to the public hearing on the rules and regulations. Answers to these questions are briefly summarized as follows.
 - . The plan to restructure the Consolidated Retirement Fund was adopted by the Board of Investments at its June 9, 1993 meeting as recommended by the staff. The primary purpose for the restructure is to diversify the risk associated with having a single investment advisor assigned to a particular retirement or trust plan. Through this restructuring, each of the retirement plans and trust plans can benefit from the investment results generated through the various investment advisory styles of the different managers.
 - . The proposed restructuring plan includes a money market fund for which units of ownership will be purchased on a constant dollar basis. Contributions and withdrawals from the money market portfolio will be allowed on a daily basis. A fixed income pool with multiple investment advisors will be periodically priced based on current market values of the assets within the portfolio. Contributions and withdrawals will be allowed as often as the portfolio is priced. The unit value determined will include any income earned but not yet distributed as of the date of the pricing. This is to ensure that any contributions or withdrawals fairly reflect any earned but not distributed income.

- . As of the effective date of the restructuring, each individual plan's assets which are to be contributed into the fixed income pool will be valued at their market value. Units of ownership will be distributed based on an arbitrary starting value of \$100.00 per unit. In contrast to the 1979 formation of the pools, each individual plan will maintain its historical cost. The difference between the historical cost and the market value at the date of the restructure will be reflected as an unrealized gain or loss at the plan level. Subsequent withdrawals from the fixed income pool will generate a realized gain or loss at the plan level based upon the plan's average per unit cost in comparison to the market unit value at the date of the withdrawal.
 - . Earnings will be distributed and reinvested in the money market fund on a daily basis. The earnings will be distributed based upon the plan's proportional balance of the total fund. Earnings of the fixed income pool will be distributed based on units of ownership at the date the Board's staff declare the dividend. We currently anticipate declaring a dividend on a monthly basis with the dividend being reinvested at the closing price on the date of declaration.
8. Again, this question goes to the restructuring of the portfolio issue. These rules are necessary regardless of whether the restructuring is achieved. Nevertheless, the plan for restructuring was discussed. As previously noted there will be multiple investment advisors assigned to the fixed income pool and the money market pool. The asset allocation responsibilities will be administered by the Board's staff in allocating funds between the money market fund and the longer term fixed income pool as well as the equity pool. This allocation process is primarily done based on cash flow forecasting projections provided to the Board by the retirement systems and the Bureau of Employment Programs. The investment advisors do not employ a particular investment strategy because they manage one fund versus another fund. They have an investment strategy that they apply to the funds regardless of the particular plan's actuarial soundness. This statement is supported by analyzing the investment strategy of Investment Advisors, Inc. who is the investment advisors on the Workers' Compensation Fund and the Public Employees Retirement System Fund. The same investment strategy is employed on these funds even though Workers' Compensation is the most actuarially unsound plan of all the seven pension and trust funds within the Consolidated Pension Fund and PERS is the most actuarially sound plan.

9. The Board of Investments' staff does not believe that any changes in the rules and regulations in any way relate to any legislation that was introduced during the 1993 Legislative session. Mr. Adams did not elaborate on any particular point on this issue.

Sam Cole - Representing Treasurer Larrie Bailey

1. I had several concerns that are basically the same as those covered by Don Adams. I would simply say that the Treasurer would concur in the questions that Mr. Adams has asked with major emphasis on his concerns on the consolidation of all the investment pools.

John Hoff, WV Association of Counties

1. I would first like to just raise a question that arose in my mind some time ago, and I think the Attorney General has reached an opinion that has helped to answer the question. When the Legislature in August, 1990 created the defined contribution plan for teachers and then changed the permissible investments for the Board, did they change the contracts that were then in existence between the State of WV and the Judges Retirement System, Teachers' Retirement System, Department of Public Safety Retirement System and PERS? I think I have an answer for PERS; but my question is; as fiduciaries, why would not the Board of Investments try to find out what those contracts are? Are they inviable? Can you diminish the investments? In other words, are they controlled by something more than 12-9? The Attorney General just said yes they certainly are and they are unconstitutional with regards to PERS; and I think that is an important question that must be answered for all of your investments.
2. I brought a hypothetical illustration (see exhibit 1) to show what the impact of Section 4.01 would have on PERS. The main thrust of this illustration is that PERS is the most solvent of the Boards, and does not need any money that is coming in now - in fact another \$100 million is added each year after they pay all the benefits to the retirees. Those monies ought to be invested long term - and can be and have been invested long term - and this table is on fixed investments and not the equities. I have made some assumptions, one that for each dollar you put in assets you get one unit in holdings. I have probably got more money in short-term investments here for PERS - about \$500 million - than really ought to be there based on its need. But the other retirement systems have some more immediate needs and you can't chance long-term investments and the whims of the market and the losses you take if you have to start cashing them in early and selling them. So what this shows is that, in my hypothetical example, we would transfer \$25,000 a day in interest from PERS to the

other units that are on my illustration. That comes to \$9.2 million a year.

3. As fiduciaries - as you are by extension of the job given to the Consolidated Public Retirement Board and the people they represent - can you, as fiduciary, create such a system? So the purpose of my illustration here is to say you are setting up something that I question its legality. Our eyebrows go up when we see you use the phrase "sharing losses" because the contract made in 1961 with PERS for fixed investments is very safe with U.S. Treasuries. You know you don't have to pay any fees if you use the 800 number and call Richmond and invest in U.S. Treasuries. That ought to be a factor in the total amount of net earnings that any fund is going to make and any dollar invested is going to make, and that is what you have to pay out in investment fees and consulting services.
4. We are quite concerned about not tracking this money separately and not getting the very best investment for the longest term that you can, and we know that the PERS money has been invested in that manner and has done quite well, and it is the only fund right now that I know of that is over 100 percent actuarially sound.

RESPONSE

1. The Board of Investments' staff does not believe that there is a violation of any fiduciary responsibility through the allocation of investment assets into equities. The matter of the Attorney General issuing an abstract opinion stating that the investment of equities for the Consolidated Pension Fund is unconstitutional will be addressed by the Board at a subsequent meeting.
2. There are many flaws in the hypothetical illustration presented by Mr. Hoff. Primarily Mr. Hoff has included money market assets with longer term fixed income assets which is not the nature of the restructuring. He has also grossly misstated the asset allocation for the various maturities. The actual restructuring does take into account market valuation and unrealized gains and losses which are not included in Mr. Hoff's example.
3. Mr. Hoff's question primarily challenges the investment strategy employed by the Board of Investments' staff and Board members through our contractual relationship with professional money managers. We do not believe there is any validity to his analysis that the creation of such a system is in any way illegal. In the contrast, this system of restructuring enhances the potential return for any particular plan and by diversification reduces the risk associated with any one plan. These are the goals of every fiduciary.

4. Mr. Hoff's statement is inaccurate. The plans' account balances will be separately accounted for and a statement showing their beginning and ending balances along with any changes i.e. contributions, withdrawals, distributions of earnings, or change in the unrealized appreciation or depreciation of their units will be provided to them on a monthly basis. Again, Mr. Hoff is making a subjective analysis that the proposed restructuring, although unrelated to the rules and regulations, will in fact be to the detriment of PERS which is not the staff's belief.

Paul Mollohan - State Employee

1. I would like to confirm what Mr. Adams has said about the investment guidelines for combining the retirement systems. I feel it is an abandonment of the fiduciary responsibility that the Board has by taking PERS, which is completely solvent, and shortening the terms of the investments which will reduce interest income for PERS. In effect transferring those funds to the Teachers' Retirement System.
2. I have a problem that there's no guidelines in the rules about the record date of the payment of the reinvestment of the dividend interest income or whatever the case may be - the valuation of the securities in relation to the number of units. Is there going to be a record date and payment date? What is the disposition of the funds paid prior to the payment date?
3. I just feel that this is the wrong direction for the Board to take in light of the Attorney General's opinion concerning investment in equities.
4. This is just another "nail in the coffin" of PERS and at the expense of Teachers. The Teachers' Retirement System is barely making it. The legislated appropriations in the last couple of years have fallen off from what the Legislature had previously committed themselves to appropriate. Which means that they even have to potentially point their investments toward a shorter term.

RESPONSE

1. Mr. Mollohan's analogy that the restructuring will be to the detriment to the PERS fund is inaccurate for the reasons previously stated. To reiterate, the investment advisors generally do not manage the funds based on the actuarial soundness of the plan but rather manage a pool of money based on the investment strategy that they believe will generate the most value on those assets. There are of course, exceptions but they do not apply here as the funds are currently being funded sufficiently to maintain positive cash flows.

2. The Board will have detailed policies relating to the record date for the declaration and reinvestment of investment earnings as well as policies for the valuation of securities. As previously mentioned, the unit value will include any earned but undistributed income at any particular date. These details are not set forth in the rules because we follow GAAP in this regard and GAAP rules are always subject to change or interpretation.
- 3 - 4. No response to these statements.

Auditor Glen Gainer III

I want it noted on the record that I am one of only two Board members that are either here or represented by a representative.