

NORTH DAKOTA LEGISLATIVE MANAGEMENT

Minutes of the

LEGACY AND BUDGET STABILIZATION FUND ADVISORY BOARD

Thursday, April 25, 2013
Medora Room, State Capitol
Bismarck, North Dakota

Representative Keith Kempenich, Chairman, called the meeting to order at 3:05 p.m.

Members present: Representatives Keith Kempenich, Gary Kreidt; Senator Jerry Klein; Bank of North Dakota President - Eric Hardmeyer; Office of Management and Budget Director - Pam Sharp; Tax Commissioner - Cory Fong

Member absent: Senator Jim Dotzenrod

Others present: Darren Schulz, Retirement and Investment Office

Connie Flanagan, Retirement and Investment Office

Mark McKinnon, Raymond James & Associates, Inc.

It was moved by Representative Kreidt, seconded by Senator Klein, and carried on a voice vote that the minutes of the April 2, 2013, meeting be approved as distributed.

DISCUSSION REGARDING POOLING OF THE LEGACY FUNDS WITH OTHER FUNDS FOR INVESTMENT PURPOSES

Chairman Kempenich called on Mr. Darren Schulz, Interim Chief Investment Officer, State Investment Board, to lead a discussion regarding the possible pooling of money in the legacy fund with other funds for investment purposes. Mr. Schulz presented a discussion outline ([Appendix A](#)), including topics related to the current legacy fund investment policy statement, the advantages of pooling the legacy fund money with money in other funds, and the suggested modifications to the investment policy statement.

Mr. Schulz said the current legacy fund investment policy statement precludes the pooling of the legacy fund money with money in other funds. He said it would be beneficial to the legacy fund to allow the pooling of funds.

Chairman Kempenich presented the board with a definition of basis points ([Appendix B](#)) and a Legislative Council memorandum ([Appendix C](#)) that was presented to the board in October 2011. Mr. Schulz said one basis point is equal to one one-hundredth of a percent. He discussed the benefits of pooling investment funds. He said benefits include:

- Significant potential savings relating to trading costs because the investment in a pooled fund constitutes one trade.
- Pooled funds provide for the possibility of purchasing and selling securities more efficiently, which may result in lower brokerage costs. In

addition, a reduction in negative market impact cost may be realized when using pooled funds.

Mr. Schulz said transaction fees and trade settlement fees would be higher if investment funds are not pooled.

In response to a question from Representative Kempenich, Mr. Schulz said a variety of criterion is analyzed during the due diligence process of choosing an investment manager.

Mr. Schulz discussed the administrative efficiencies of pooling and provided information regarding the insurance pool participant funds, including the individual state fund balances and the asset class pools chosen for each fund. He said as added benefits to pooling, accounting for the funds is conducted at the pooled level with fewer transactions to reconcile, and in all instances, each fund pays its pro rata share of the actual expenses incurred.

Mr. Schulz discussed the insurance pool investment managers. He said, hypothetically, if the legacy fund were to participate in pooling with the current insurance pooled funds based on the asset class policy allocation that has been recommended by the advisory board, the Retirement and Investment Office anticipates the legacy fund's weighted average management fee would be 24 basis points with an additional 3 to 4 basis points for administrative and custodial fee purposes.

Mr. Schulz provided the advisory board with suggested modifications to the legacy fund investment policy ([Appendix D](#)). The modifications to the legacy fund investment policy are as follows:

- Section 3 is modified to state the correct section of the North Dakota Century Code.
- Section 6 is modified to clear the policy asset mix table of the original asset allocation policy for the implementation of the advisory board's recommended asset allocation policy and the addition of the State Investment Board's rebalancing policy.
- Section 7 is modified with the deletion of language precluding the legacy fund assets to be pooled with any other fund assets managed by the State Investment Board.
- Section 8 is modified with the deletion of language relating to broker relationships.

In response to a question from Senator Klein, Mr. Schulz said when fund assets are pooled, each fund continues to retain its own identity.

Mr. Fong suggested the advisory board approve the modifications to the legacy fund investment policy statement.

In response to a question from Representative Kreidt, Ms. Connie Flanagan, Fiscal and Investment Officer, Retirement and Investment Office, said the language pertaining to the State Investment Board's rebalancing policy was not included in the original policy statement and is suggested as a modification to maintain consistency of policy procedures.

It was moved by Mr. Fong and seconded by Mr. Hardmeyer to adopt the modifications to the legacy fund investment policy statement suggested by representatives of the Retirement and Investment Office, including modifications in:

- **Section 3 to correct the North Dakota Century Code reference.**
- **Section 6 relating to the asset allocation policy and the rebalancing policy.**
- **Section 7 to delete language precluding the pooling of fund assets.**
- **Section 8 to delete reference to broker relationships.**

Senator Klein suggested delaying consideration of adopting the policy statement modifications until the end of the meeting.

Ms. Sharp and Mr. Hardmeyer voted "aye." Representatives Kempenich and Kreidt, Senator Klein, and Mr. Fong voted "nay." **The motion failed.**

Chairman Kempenich called on Mr. Mark McKinnon, Raymond James & Associates, Inc., to discuss direct bond investing. Mr. McKinnon suggested the advisory board may wish to consider investing a portion of the money in the legacy fund within the state. He said the State Treasurer's office could be a potential investment management option.

In response to a question from Senator Klein, Mr. McKinnon said he is supportive of pooling the assets of the legacy funds.

In response to a question from Representative Kreidt, Mr. McKinnon said additional staff may be required within the State Treasurer's office if a portion of the legacy fund is to be managed by that office.

ADVISORY BOARD DISCUSSION AND STAFF DIRECTIVES

It was moved by Mr. Fong, seconded by Mr. Hardmeyer, and carried on a roll call vote that the Legacy and Budget Stabilization Fund Advisory Board adopt the modifications to the legacy fund investment policy statement suggested by representatives of the Retirement and Investment Office, including modifications in:

- **Section 3 to correct the North Dakota Century Code reference.**
- **Section 6 relating to the asset allocation policy and the rebalancing policy.**
- **Section 7 to delete language precluding the pooling of fund assets.**
- **Section 8 to delete reference to broker relationships.**

Representatives Kempenich and Kreidt, Senator Klein, Ms. Sharp, Mr. Fong, and Mr. Hardmeyer voted "aye." No negative votes were cast.

No further business appearing, Chairman Kempenich adjourned the meeting at 4:35 p.m.

Brittani S. Reim
Fiscal Assistant

Allen H. Knudson
Legislative Budget Analyst and Auditor

ATTACH:4