

HOUSE OF REPRESENTATIVES STAFF FINAL BILL ANALYSIS

BILL #: CS/CS/HB 1139 State Board of Administration

SPONSOR(S): State Affairs Committee and Constitutional Rights, Rule of Law & Government Operations Subcommittee, Stevenson and others

TIED BILLS: **IDEN./SIM. BILLS:** CS/CS/SB 110

FINAL HOUSE FLOOR ACTION: 119 Y's 0 N's **GOVERNOR'S ACTION:** Approved

SUMMARY ANALYSIS

CS/CS/HB 1139 passed the House on May 2, 2023, as CS/CS/SB 110.

The State Board of Administration (SBA) is responsible for managing investments for the Florida Retirement System (FRS) Pension Plan and for administering the FRS Investment Plan, which combined represent \$190.6 billion or 81 percent of the assets under management by the SBA. The SBA's ability to invest is governed by a "legal list" of the types of investments and the total percentage of funds that may be invested in each type. Currently, the SBA may invest 20 percent of any fund in alternative investments. The SBA may also invest up to 5 percent of any fund in investments not specifically listed on the legal list. However, before doing so, the SBA must present a proposed plan for such investment to the Investment Advisory Council. In addition, the SBA must maintain a list of scrutinized companies that boycott Israel and is prohibited from investing in such entities.

Unlike the FRS Pension Plan, the SBA does not manage investments for the FRS Investment Plan. However, the SBA is responsible for selecting and approving investment options and providers for the FRS Investment Plan. If an investment plan member is married and designates a primary beneficiary other than his or her spouse, the member's spouse must sign the beneficiary designation form to acknowledge the designation.

The bill authorizes the SBA to hold certain interests in real property through limited liability entities or joint ventures and issue securities and borrow money through such entities. The bill authorizes the SBA to invest up to 30 percent of any of its funds in alternative investments, which is an increase from the current maximum of 20 percent. The bill requires the SBA to divest the public fund from any company placed on the Scrutinized Companies that Boycott Israel List. The bill also reduces the information the SBA must report to the Investment Advisory Council in advance of making an investment not specially authorized by the legal list and instead allows for a "detailed analysis of the investment" for any such proposed investment activity.

The bill authorizes the SBA to develop one or more investment products to be offered under the investment plan as an alternative to those products currently offered by approved providers. If an investment plan member selects a primary beneficiary other than his or her spouse, the bill allows the SBA to waive the requirement that the member's spouse acknowledge such designation under certain circumstances.

The bill specifies that the SBA may not distribute certain investment plan benefits to a member found in court to have committed a specified prohibited act, similar to the current prohibition on the Division of Retirement for pension plan members.

The bill does not appear to have a fiscal impact on state or local governments.

The bill was approved by the Governor on May 24, 2023, ch. 2023-111, L.O.F., and became effective on that date.

I. SUBSTANTIVE INFORMATION

A. EFFECT OF CHANGES:

Present Situation

State Board of Administration

The State Board of Administration (SBA) is established by Art. IV, s. 4(e) of the Florida Constitution, and is composed of the Governor as Chair, the Chief Financial Officer, and the Attorney General, commonly referred to as “Trustees.” The SBA derives its power to oversee state funds from Art. XII, s. 9 of the Florida Constitution.

The SBA has responsibility for investing the assets of the Florida Retirement System (FRS) Pension Plan¹ and administering the FRS Investment Plan,² which combined represent approximately \$190.6 billion, or approximately 81.9 percent, of the \$232.9 billion in assets managed by the SBA, as of December 31, 2022.³ The pension plan is a defined benefit plan and the investment plan is a defined contribution plan that employees may choose in lieu of the pension plan. The SBA also manages over 25 other investment portfolios, with combined assets of approximately \$42.3 billion, including the Florida Hurricane Catastrophe Fund, the Florida Lottery Fund, the Florida Prepaid College Plan, and various debt-service accounts for state bond issues.

Investment decisions for the pension plan are made by fiduciaries hired by the state. Under Florida law, an SBA fiduciary charged with an investment decision must act as a prudent expert would under similar circumstances, considering all relevant substantive factors. A nine-member Investment Advisory Council provides recommendations on investment policy, strategy, and procedures.⁴

The SBA’s authority to invest the funds, including FRS assets, is governed by s. 215.47, F.S., which provides a “legal list” of the types of investments and the total percentage that may be invested in each type of investment. The legal list guidelines provide that:

- No more than 80 percent of any fund may be invested in domestic common stocks.
- No more than 75 percent of any fund may be invested in internally managed common stocks.
- No more than 3 percent of equity assets may be invested in the equity securities of any one corporation, except to the extent a higher percentage of the same issue is included in a nationally recognized market index, based on market values, or except upon a specific finding by the SBA that such higher percentage is in the best interest of the fund.
- No more than 25 percent of any fund may be invested in specific instruments, such as certain bonds or other obligations of other states or of municipalities or other political subdivisions, notes secured by first mortgages insured or guaranteed by the Federal Housing Administration or the United States Department of Veterans Affairs, investment-grade group annuity contracts of the pension investment type, certain interests in real property, certain bonds or instruments issued by the government of Israel, foreign government general obligations, or other asset-backed securities.
- No more than 50 percent of any fund may be invested in foreign corporate or commercial securities or obligations.
- No more than 20 percent of any fund may be invested in alternative investments.

In addition, the SBA may invest up to 5 percent of any fund as it deems appropriate. However, before making such investments, the SBA must present a proposed plan for such investment to the

¹ S. 121.151, F.S.

² S. 121.4501(8), F.S. See also, R. 19-13.001, F.A.C.

³ State Board of Administration, *Performance Report Month Ending: December 31, 2022*,

<https://www.sbafla.com/fsb/Portals/FSB/Content/Performance/Trustees/2022/December%202022%20Monthly%20Trustee%20Report.pdf?ver=2023-03-15-152743-283> (last visited March 18, 2023).

⁴ S. 215.444(1), F.S.

Investment Advisory Council. The Investment Advisory Council is authorized to obtain independent investment counsel to provide expert advice with regard to such proposed investment activity by the SBA at the SBA's expense. The proposed plan must include the expected benefits and potential risks, methods for monitoring and measuring performance, a complete description of the investment, and assurances that sufficient expertise is available for the SBA to properly evaluate and manage the investment.⁵

Alternative Investments

To diversify its investments, the SBA invests in multiple asset classes: global equities, fixed income, real estate, cash equivalents, strategic investments, and private equity.⁶ As noted above, the SBA may not invest more than 20 percent of any fund in alternative investments through participation in alternative investment vehicles⁷ or in securities or investments that are not publicly traded and not otherwise authorized by the legal list. The use of alternative investment vehicles was first authorized in 1996 at a maximum of 5 percent of a fund.⁸ In 2007, the use was expanded to include a broader spectrum of alternative investments, including private equity funds, venture funds, hedge funds, and distress funds.⁹ In 2008, this maximum threshold was increased to 10 percent.¹⁰ In 2012, the threshold was again increased to 20 percent.¹¹

Currently, approximately 20 percent of FRS Pension Plan assets are invested in alternative investments, which is the legal limit. Due to the illiquid nature of alternative investments, typically including obligations that are contracted over multiple year periods, the SBA predicts it may have to forego new alternative investments that would enhance FRS investment returns.¹²

Scrutinized Companies that Boycott Israel

The SBA is required to maintain a list of companies that participate in a boycott of Israel.¹³ Current law defines the terms "boycott Israel" and "boycott of Israel" to mean refusing to deal, terminating business activities, or taking other actions to limit commercial relations with Israel, or persons or entities doing business in Israel or in Israeli-controlled territories, in a discriminatory manner. This definition does not include restrictive trade practices or boycotts fostered or imposed by foreign countries against Israel.

The SBA must provide notice to any company added to the list which informs the company that it may become subject to investment prohibition by the public fund.¹⁴ The notice must also inform the company of the opportunity to clarify its activities or cease the boycott of Israel. If after 90 days, the company does not cease its activities, the public fund is prohibited from acquiring direct holdings of the company.¹⁵

⁵ S. 215.47(6), F.S.

⁶ State Board of Administration, *Summary Overview of the State Board of Administration of Florida*, https://www.sbafla.com/fsb/Portals/FSB/Content/Topics/SBAOverview_20211025.pdf?ver=2021-10-28-120954-217 (last visited March 18, 2023).

⁷ "Alternative Investment Vehicle" means the limited partnership, limited liability company, or similar legal structure or investment manager through which the State Board of Administration invests in a portfolio company. S. 215.4401(3)(a)2., F.S.

⁸ Ch. 199-177, Laws of Fla., authorized the SBA to invest up to 5 percent of a fund in private equity through participation in limited partnerships and limited liability companies.

⁹ Ch. 2007-98, Laws of Fla.

¹⁰ Ch. 2008-31, Laws of Fla., increased the threshold to 10 percent and expanded this limitation to authorize SBA to invest in securities or investments that are not publicly traded and are not otherwise authorized in s. 214.47, F.S.

¹¹ Ch. 2012-112, Laws of Fla.

¹² State Board of Administration, Agency Analysis of 2023 HB 1139 (March 18, 2023), on file with the Constitutional Rights, Rule of Law & Government Operations Subcommittee.

¹³ S. 215.4725, F.S.

¹⁴ "Public fund" means all funds, assets, trustee, and other designates under the SBA pursuant to part I of chapter 121, F.S. S. 215.4725(1)(e), F.S.

¹⁵ S. 215.4725(3), F.S.

FRS Investment Plan Funds

Unlike the FRS Pension Plan, the SBA does not manage investments for the FRS Investment Plan, which is the defined contribution plan. Instead, benefits accrue in individual member accounts that are member-directed and funded by employer and employee contributions and earnings.¹⁶ Accordingly, members bear the investment risks and reap the rewards from the investments in their accounts.¹⁷

The SBA is responsible, however, for selecting and approving investment options and providers for the FRS Investment Plan. “Approved providers” are private sector companies that are selected and approved by the SBA to offer one or more investment products or services to investment plan members. The SBA seeks to achieve the following long-term objectives for the investment plan:

- Offer a diversified mix of low-cost investment products that span the risk-return spectrum and give members the opportunity to accumulate retirement benefits;
- Offer investment options that avoid excessive risk, have a prudent degree of diversification relative to broad market indices, and provide a long-term rate of return, net of all expenses and fees, in order to achieve or exceed the returns on comparable market benchmark indices; and
- Offer members meaningful, independent control over the assets in their accounts.¹⁸

The investment plan features 19 funds, which include nine funds spread across five asset classes, 10 retirement date funds (that are mixtures of various asset classes), and a self-directed brokerage account.¹⁹ Investment management for these funds is outsourced to approved providers.

Designation of Beneficiaries

An investment plan member is authorized to designate one or more beneficiaries who, upon the member’s death, will receive any payable benefits from the member’s account.²⁰ The beneficiaries may be named sequentially or jointly. However, if the member is married and designates a primary beneficiary other than his or her spouse, the member’s spouse must sign the beneficiary designation form to acknowledge the designation.²¹

Forfeiture of Retirement Benefits

Article II, s. 8 of the Florida Constitution provides that “[a]ny public officer or employee who is convicted of a felony involving a breach of public trust shall be subject to forfeiture of rights and privileges under a public retirement system or pension plan in such manner as may be provided by law.”

Current law provides for the forfeiture of all rights and benefits, except for accumulated employee contributions, under any public retirement system²² by a public officer or employee²³ who is convicted before his or her retirement of the following specified offenses:

- Embezzlement of public funds.
- Theft from his or her employer.
- Bribery in connection with his or her public employment.
- Crimes related to the misuse of a public office.
- Any impeachable offense.

¹⁶ S. 121.4501(1), F.S.

¹⁷ See r. 19-9.001, F.A.C.

¹⁸ *Id.*

¹⁹ Florida Retirement System, *Investment Plan Investment Fund Summary*, https://www.myfrs.com/pdf/forms/invest_fund_summary.pdf (last visited March 18, 2023).

²⁰ S. 121.4501(20)(a), F.S.

²¹ S. 121.4501(20)(b), F.S.

²² “Public retirement system” means any retirement system or plan to which the provisions of part VII of ch. 112, F.S., apply, including the FRS.

²³ “Public officer or employee” means an officer or employee of any public body, political subdivision, or public instrumentality within the state. S. 112.3173(2)(c), F.S.

- Any felony committed with intent to defraud the public or the employing agency, and through the commission of which the member used or attempted to use his or her position's power, rights, privileges, or duties to profit, gain, or realize an advantage.
- Felony-level lewd or lascivious acts against a victim younger than 16, or felony sexual battery against a victim younger than 18, committed by using the member's powers, rights, privileges, or duties of the member's public position.²⁴

In addition, any FRS member who is adjudged by a court of competent jurisdiction to have violated any state laws against strikes by public employees, or who has been found guilty of violating such law forfeits all rights and benefits under the FRS, except for accumulated employee contributions.²⁵

The Division of Retirement within the Department of Management Services is prohibited from distributing benefits should a member be found in court to have committed one of the above prohibited acts.²⁶ The Division of Retirement distributes pension plan benefits, and the SBA distributes investment plan benefits.

Effect of the Bill

SBA Investment Authority

The bill amends the SBA's investment authority to authorize the SBA to hold certain interests in real property and related personal property through limited liability entities or joint ventures. Specifically, these subsidiary interests will be empowered to hold the SBA's investment mortgages and related instruments that are secured by real property, and instruments that contain provisions for equity or income participation or with provisions for convertibility to equity ownership, and interests in real property related collective investment funds.

In addition, the SBA and its affiliated limited liability entities and joint ventures may issue securities and borrow money through loans or other financial obligations, including bonds, equity securities, and other security instruments, any of which may be unsecured, or secured by investments in real property or related cash flows, guaranteed by the related fund, or governed by financial covenants. The proceeds of such loans or financing obligations may be loaned to or otherwise used as a source of funding for affiliated limited liability entities or joint ventures.

The bill reduces the specified information the SBA must give to the Investment Advisory Council in advance of making an investment not specifically authorized by the legal list and instead allows for a "detailed analysis of the investment" for any such proposed investment activity.

The bill authorizes the SBA to invest up to 30 percent of any of its funds in alternative investments, which is an increase from the current maximum of 20 percent.

The bill makes conforming changes and updates certain out-of-date terminology to reflect current industry terminology by updating the term "corporation" to "entity" and "common stock" to equity securities."

Scrutinized Companies that Boycott Israel

The bill requires the SBA to divest its holdings from companies placed on the Scrutinized Companies that Boycott Israel List. If after 90 days following the public funds' first notice to the company that the company may become subject to investment prohibition or divestment, the company continues to boycott Israel, the public fund must sell, redeem, divest, or withdraw all publicly traded securities of the

²⁴ S. 112.3173, F.S.

²⁵ S. 121.091(5)(h), F.S.

²⁶ S. 121.091(5)(k), F.S.

company from the public fund within 12 months after the company's most recent appearance on the Scrutinized Companies that Boycott Israel List.

The bill allows the SBA to cease divestment from or reinvest in certain scrutinized companies if clear and convincing evidence shows that the value of all assets under management by the public fund becomes equal to or less than 99.50 percent, or 50 basis points, of the hypothetical value of all assets under management by the public fund, assuming no divestment for any company had occurred.

The bill requires the SBA to provide a written report to each member of the SBA Board of Trustees, the President of the Senate, and the Speaker of the House of Representatives in advance of the divestment, which sets forth the reasons and justification for its decision to divest in a scrutinized company.

The bill also amends the definition of the terms "boycott Israel" and "boycott of Israel" to include taking adverse action, including changes to published commercial financial ratings, risk ratings, and controversy ratings based on nonpecuniary factors, to inflict economic harm on Israel or persons or entities doing business with Israel or in Israeli-controlled territories. The bill specifies that these terms include trade practices that are prohibited by federal regulations issued in compliance with federal law but does not include trade practices that are preempted by federal law.

FRS Investment Plan

The bill authorizes the SBA, consistent with its fiduciary responsibility, to develop one or more investment products to be offered under the investment plan as an alternative to those products currently offered by approved providers.

The bill removes the requirement that a member's spouse sign the beneficiary designation when a member designates a primary beneficiary other than his or her spouse. Instead the bill requires the spouse to be notified and acknowledge that he or she has not been so designated. However, the bill authorizes the SBA to waive this requirement under certain circumstances. Specifically, the SBA may waive the requirement when the spouse either cannot be located or fails to affirmatively acknowledge the designation and the member submits an affidavit that explains the facts and circumstances and requests a waiver.

Forfeiture of Retirement Benefits

The bill specifies that the SBA may not distribute investment plan benefits to a member found in court to have committed one of the specified acts prohibited in the statute.

II. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT

A. FISCAL IMPACT ON STATE GOVERNMENT:

1. Revenues:

None.

2. Expenditures:

None.

B. FISCAL IMPACT ON LOCAL GOVERNMENTS:

1. Revenues:

None.

2. Expenditures:

None.

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

None.

D. FISCAL COMMENTS:

None.