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Nebraska Retirement Systems Committee
January 26, 2018

[LB700 CONFIRMATION]

The Committee on Nebraska Retirement Systems met at noon on Friday, January 26, 2018, in Room 1525 of the State Capitol, Lincoln, Nebraska, for the purpose of conducting a public hearing on LB700 and gubernatorial confirmations. Senators present: Mark Kolterman, Chairperson; Brett Lindstrom, Vice Chairperson; Kate Bolz; Mike Groene; Rick Kolowski; and John Stinner. Senators absent: None.

SENATOR KOLTERMAN: We'll start. I know that Senator Groene as well as...everybody is supposed to be coming, so we'll start anyway. Welcome to the Nebraska Retirement Systems Committee hearing. My name is Senator Mark Kolterman, I'm from Seward and represent District 24, which is York, Seward, and Polk Counties. Our committee is made up, to my right, Senator Bolz who represents Lincoln, Senator Stinner who represents...

SENATOR STINNER: Scotts Bluff County.

SENATOR KOLTERMAN: ...Scotts Bluff County. Go ahead.

SENATOR LINDSTROM: Senator Lindstrom, District 18, northwest Omaha.

SENATOR KOLTERMAN: I just know where you're from.

SENATOR KOLOWSKI: Senator Kolowski, southwest Omaha.

SENATOR KOLTERMAN: And Senator Groene is from North Platte. He said he would be here. We have with us our page, Bailey, today, appreciate her. And our staff, we have Katie Quintero who's our committee clerk and...

KATE ALLEN: Kate Allen.

SENATOR KOLTERMAN: Kate Allen. Okay, we're here to conduct a hearing on...confirmation hearing for John Conley, Nebraska Investment Council and LB700. We'll take them in that order. Everything has been posted. We'd ask that you turn off your cell phones. If you want to testify in support, please come forward, or opposed. And we'll take you. We don't use the lights in this committee, normally. So, Mr. Conley, if you'd come forward, we'd appreciate it.

[CONFIRMATION]

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JOHN CONLEY: Sure, happy to. [CONFIRMATION]

SENATOR KOLTERMAN: Would you spell your name and say your name and then we'll move on. [CONFIRMATION]

JOHN CONLEY: Sure. John Conley, J-o-h-n C-o-n-l-e-y, from Omaha. [CONFIRMATION]

SENATOR KOLTERMAN: And you're here...your reappointment to the Nebraska Investment Council? [CONFIRMATION]

JOHN CONLEY: Yes, sir. I've served five years at this point and the reappointment is another five years. [CONFIRMATION]

SENATOR KOLTERMAN: And give us a little bit of your background. [CONFIRMATION]

JOHN CONLEY: Sure. I've been I think 44 years in the investment business now, a graduate of Nebraska Wesleyan and while there had an early start. And it's been a wonderful career, it truly has. It's certainly not over. But first ten years, roughly, in securities analysis with First Mid America, later as director of research of Charles Heider and Company, and then started my own investment management firm in 1986. And then about four years ago I merged that into Lincoln-based Smith Hayes Financial Services. And it, in turn, has merged into Great Falls, Montana-based...it's quite a large firm actually, a good-sized regional firm, D.A. Davidson. So it is my current employer and I am senior vice president with the firm. [CONFIRMATION]

SENATOR KOLTERMAN: And you've been on the Investment Council for five years now? [CONFIRMATION]

JOHN CONLEY: Yes, sir. [CONFIRMATION]

SENATOR KOLTERMAN: Appreciate what you're doing. Do we have any questions for Mr. Conley? Senator Stinner. [CONFIRMATION]

SENATOR STINNER: I would like to know from you, we've had this incredible runup in equities. In the face of probably three, maybe four, increases in interest rates I'm kind of interested, if you're sitting on the Nebraska Investment Council, is there strategies to help from that bottom-side risk? And what would those strategies be? [CONFIRMATION]

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JOHN CONLEY: It's an extraordinarily important question. Let me not try to be long winded with my answer, but try to...if I might try to simplify the investment business, I'd like to identify five asset classes: cash; short-term investments; longer-term fixed income investments would fall in the bond category; common stocks; real estate; and a fifth would be tangibles. So that might be 1968 Chevies, but more likely it is more like Rembrandt and van Gogh pieces of art, tangible pieces. There isn't an asset class that's cheap today and not one of those asset classes is called run and hide. So our role as the Investment Council is to try to make the most prudent investment decisions that we can and, frankly, not based necessarily on striving to achieve some rate of return, but it's what's the best rate of return that we can take at a level of risk that's appropriate. We have had huge runups in equity prices. Some of it may have been driven by recent tax legislation. But it raises the question of how do we protect ourselves in the down market? And I have private investment clients, that's what I do. I help manage, if you will, family resources. And going into a relationship, I always want my clientele to understand that we're going to have both good markets and we're going to have bad markets. We may well see a bad market, perhaps even a terrible market in the next couple of years. We don't know. What we do hope for is prudent judgment and good decisions. But the Investment Council is not in a position, nor do I believe it ever should be, to try to make dramatic swings, dramatic adjustments in the investment portfolio just to avoid what may or may not happen. At that point, it's speculation. We choose not to speculate. [CONFIRMATION]

SENATOR KOLTERMAN: Okay. Thank you. Any other questions? Hearing none, I would like to thank you for your dedication and appreciate the idea that you're going to run again, let your name stand. We do appreciate that. [CONFIRMATION]

JOHN CONLEY: Thank you, Senator. [CONFIRMATION]

SENATOR KOLTERMAN: So the way it works, we'll vote in Executive Session and we'll go to the floor with it, unless we have somebody that stands up and starts to sing or do something else, you have a good chance. [CONFIRMATION]

JOHN CONLEY: They may. Thank you very much to you all. [CONFIRMATION]

SENATOR KOLTERMAN: Yeah, thank you. Do we have any other proponents? Anybody in opposition to the appointment? Anybody neutral to the appointment? Hearing none, thank you. I'll close that hearing. Next, we have LB700. I'm going to open on that. Senator Lindstrom will take it from there. [CONFIRMATION]

SENATOR LINDSTROM: Very good. Good afternoon, Senator Kolterman. Whenever you're ready (inaudible). [LB700]

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SENATOR KOLTERMAN: Good afternoon, Senator Lindstrom. Members of the Retirement Committee, for the record my name is Mark Kolterman, M-a-r-k K-o-l-t-e-r-m-a-n. I represent Nebraska's 24th Legislative District, which includes Polk, York, and Seward Counties. I'm here today to introduce LB700. As the members of the committee know, we oversee the Nebraska Investment Council. Primary responsibility to the council relates to the investment programs of \$10.6 billion in defined benefit pension plans and \$2.7 billion in seven other retirement funds. The State Investment Officer and the University of Nebraska together approached me to introduce this technical correction for listing funds the council manages. As you see, the current language of the statute recognizes that the Board of Regents is responsible for managing the investment of the University Trust Fund. At the same time, the statute directs the council to include the same fund in the programs they invest. University Trust Fund consists of funds donated to the university and does not contain any funds derived from taxation. You will hear from the State Investment Officer that this was likely an oversight when the council was created and this bill simply corrects that technical oversight. It is my understanding that in the meantime the issue has been managed by an agreement between the Board of Regents and the council. This bill removes the obligation for the council to invest the University Trust Fund, which is overseen and managed by the Board of Regents. With that, I would hope that you advance this to the floor of the Legislature with a green vote. If you have any questions, I'd be glad to try and answer them. [LB700]

SENATOR LINDSTROM: Thank you, Chairman Kolterman. Any questions from the committee? Seeing none, thank you. We will now have proponents to LB700. [LB700]

MICHAEL WALDEN-NEWMAN: Good afternoon, committee members. Michael Walden-Newman, State Investment Officer with the Nebraska Investment Council. That's M-i-c-h-a-e-l W-a-l-d-e-n hyphen N-e-w-m-a-n. As was just stated by the Chair, when you look at the statutes that created the Investment Council in 1969, there was a sweep, you can appreciate, a statutory sweep of all state funds that rested with various state agencies and entities into the newly...to be created Nebraska Investment Council. And I believe that what happened is, is someone swept these funds into that enacting legislation and shouldn't have. And so the way the council, because we're mentioned in the statute...it says State Investment Officer, but when it says State Investment Officer it means the Nebraska Investment Council because they hire me and oversee my work. The Investment Council was named in that statute, when these are in fact private funds. So to get around the statutory language, most recently, now 11 years ago, the council entered into a management agreement, if you will, with the university where we essentially hired the university as a manager for these funds. And that agreement expired last year. And as you know, I've been here three years. So my take and our take as the council on this was, look, let's take this opportunity to take a few steps back here and see what the real issue is. And the real issue is not how to structure an agreement, the real issue is to come to you all and get a fix in the legislation to make it very clear who's responsible. And so we had an extension for one year of

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that agreement and are now here in front of you, as soon as we could, to get the language changed to take the council out of that and recognize what, in fact, is the current practice. And that is, that the university manages these funds. [LB700]

SENATOR LINDSTROM: Very good. Thank you. [LB700]

MICHAEL WALDEN-NEWMAN: I'd be happy to answer any questions you have. [LB700]

SENATOR LINDSTROM: Thank you. Any questions from the committee? I just have a quick question, sir, that as far as the allocation of these funds themselves, will they mirror what you're doing...are they in lockstep with what you're doing within the Investment Council now so the... [LB700]

MICHAEL WALDEN-NEWMAN: It's a good question, Senator, and the answer is, no. [LB700]

SENATOR LINDSTROM: Okay. [LB700]

MICHAEL WALDEN-NEWMAN: The University Foundation is actually managing those funds, they have their own allocation for that portfolio. [LB700]

SENATOR LINDSTROM: Okay. And they do similar to what you do with ATS mutual funds, other things, they're doing that on their side of the function? [LB700]

MICHAEL WALDEN-NEWMAN: And that's a great question for the university, too, Senator. Right. [LB700]

SENATOR LINDSTROM: Okay, very good. Thank you. Appreciate it. [LB700]

MICHAEL WALDEN-NEWMAN: Thanks. I'll be back in a few weeks with our annual report and we can talk investments, how's that? Thank you very much. Appreciate the help on this. [LB700]

SENATOR LINDSTROM: Thank you. Any other proponents? [LB700]

JOEL PEDERSEN: Good afternoon. My name is Joel Pedersen, it's J-o-e-l P-e-d-e-r-s-e-n. I'm general counsel at the University of Nebraska. We are here in support as a proponent of LB700 and very grateful for Senator Kolterman and the committee considering this. We are in this

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together with the State Investment Officer. This has been a technical correction we've needed at least since Michael got here and started paying attention. Between 1969 and the late '90s, there was a big gift. And so how was this oversight? In 1969, this was not a very big fund. It's not great size now, compared to your retirement assets. It's less than \$500 million. But the bottom line is in the late '90s, we got a substantial gift to this fund. The Board of Regents' policy is pretty clear. They have the foundation invest. And if you're giving by will or estate, we direct you as a Board of Regents in the General Counsel's Office to give that donation to the university through the University Foundation. That didn't happen in the instant...in the late '90s when the Othmer gift came and if you know, that's the Othmer Hall at 17th and Vine. The mortgage is paid for that building by this fund and there are other support items at the university, but that is what's in this trust fund. It's funds donated directly to University of Nebraska. And so the oversight part of this and how did that happen? We don't really know. But the size of the fund at that time was nothing compared to what it is today. And so we believe this technical correction, it obviates a need to have an agreement and it's a pretty simple fix at this point. And like I say, we're very grateful for Senator Kolterman introducing this, but we're even more grateful to work with the Investment Council and the State Investment Officer, because we truly are all together on this one. [LB700]

SENATOR LINDSTROM: Very good. Thank you. Any questions from the committee? Seeing none, thank you. [LB700]

JOEL PEDERSEN: Thank you. [LB700]

SENATOR LINDSTROM: Next proponent. Seeing none, we'll now move to opponents. Seeing none, any neutral testifiers? Also seeing none, Senator Kolterman waives closing and that will end the hearing on LB700. Thank you very much, everyone. [LB700]