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Bill Analysis
Legislative Service Commission

H.B. 79

127th General Assembly
(As Introduced)

**Reps. Batchelder, J. McGregor, Fessler, Latta, Stebelton, Webster,
Uecker**

BILL SUMMARY

- Removes the requirement that the Administrator of Workers' Compensation make investments based on the prudent person standard and requires the Administrator to invest only in a list of permitted investments.
- Specifies limitations regarding the percentage of funds that the Administrator may invest in certain types of permitted investments.
- Requires the Workers' Compensation Oversight Commission to adopt a new investment policy within 90 days after the bill's effective date using the list of permitted investments.
- Removes the list of prohibited investments specified in current law.
- Removes the Administrator's authority to contract with outside investment managers for the purpose of investing the assets of the funds specified in the Workers' Compensation Law (R.C. Chapters 4121., 4123., 4127., and 4131.).
- Eliminates the requirements for criminal records checks for investment managers and business entities investing those funds.
- Removes the requirements that the Oversight Commission (1) vote to open an investment class, (2) adopt due diligence standards for investing in that class, and (3) report to the leaders of the General Assembly about those investments.

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CONTENT AND OPERATION

Changes to the investment authority of the Administrator of Workers' Compensation

Investment authority under current law

Continuing law allows the Administrator of Workers' Compensation to invest the surplus and reserve of the State Insurance Fund (hereafter SIF). The Administrator must make those investments (1) in accordance with statutorily specified fiduciary requirements and conflict of interest prohibitions (sec. 4121.126 and sec. 4121.127, not in the bill), (2) in accordance with the investment objectives, policies, and criteria established by the Workers' Compensation Oversight Commission, and (3) in consultation with the Bureau of Workers' Compensation Chief Investment Officer. Under current law, the Administrator must not engage in any prohibited investment activity specified by the Oversight Commission and must not invest in certain types of investments specified under current law. (Secs. 4121.121 and 4123.44.)

Current law requires the Administrator and other fiduciaries to discharge their duties with respect to the funds with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims, and by diversifying the investments of the assets of the funds so as to minimize the risk of large losses, unless under the circumstances it is clearly prudent not to do so. To facilitate investment of the funds, current law permits the Administrator to establish a partnership, trust,

limited liability company, corporation, including a corporation exempt from taxation under the Internal Revenue Code, 26 U.S.C. 1, as amended, or any other legal entity authorized to transact business in Ohio. Continuing law specifies requirements for purchasing and reporting on investments. (Sec. 4123.44.)

Investment authority under the bill

The bill removes the requirement that the Administrator make investments in accordance with the prudent person standard described above and removes the prohibition against investing in certain types of investments that are not commonly part of an institutional portfolio, lack liquidity, and lack readily determinable valuation. Instead, the Administrator must invest the surplus and reserve of the SIF in the classes of investments specified in the bill (see "**Permitted investments**," below). The bill also removes the ability of the Administrator to establish a partnership, trust, limited liability company, corporation, or other type of legal entity to facilitate the investment of the assets of the SIF. (Secs. 4121.121 and 4123.44.)

Permitted investments

The bill permits the Administrator, in accordance with the requirements described under "**Changes to the investment authority of the Administrator of Workers' Compensation**," above, to invest the surplus and reserve of the SIF in any of the following classes of investments:

(1) Bonds and mortgages on unencumbered real estate within Ohio or any other state worth 25% more than the sum loaned thereon, exclusive of buildings, unless such buildings are insured by some company authorized to do business in Ohio;

(2) Bonds, notes, debentures, and other such obligations secured by mortgages insured by the Federal Housing Administrator or the United States Secretary of Agriculture under Title I of "The Bankhead-Jones Farm Tenant Act" as amended;

(3) Loans to veterans guaranteed in whole or in part by the United States pursuant to Title III of the "Servicemen's Readjustment Act of 1944," 38 U.S.C. 693, as amended, provided such guaranteed loans are liens upon real estate;

(4) Legally authorized and executed bonds, notes, warrants, and securities that are the direct obligation of or are guaranteed as to both principal and interest by Canada, that are the direct obligation of or are guaranteed as to both principal and interest by any province of Canada, that are the direct obligation of or are guaranteed as to both principal and interest by any municipal corporation of

Canada having a population of 100,000 or more by the latest official census, and that are not in default as to principal or interest;

(5) Obligations issued, assumed, or guaranteed by the International Finance Corporation or by the International Bank for Reconstruction and Development, the Asian Development Bank, the Inter-American Development Bank, the African Development Bank, or similar development bank in which the President, as authorized by Congress and on behalf of the United States, has accepted membership;

(6) Specified bonds or other evidences of indebtedness that are issued by certain federal, state, or local governmental entities and are valid obligations of the governmental entity, if the governmental entity satisfies specified requirements relative to guarantees for payment of principal and interest and have a good payment history;

(7) Any bonds issued by or for federal land banks and any debentures issued by or for federal intermediate credit banks under the "Federal Farm Loan Act of 1916," 12 U.S.C.A. 641 and amendment thereto;

(8) Any debentures issued by or for banks for cooperatives under the "Farm Credit Act of 1933," 12 U.S.C.A. 131 and amendments thereto;

(9) Bonds issued under the "Home Owners' Loan Act of 1933," 12 U.S.C.A. 1461;

(10) The stock of a national bank located in Ohio, organized under the act entitled "An act to provide a national currency, secured by the pledge of United States stocks, and to provide for the circulation and redemption thereof," approved February 25, 1863, and acts amendatory thereof and supplementary thereto;

(11) First mortgage bonds of railroads upon which default in the payment of the interest coupons has not been made within three years prior to the purchase thereof by the Administrator;

(12) Legally authorized and executed bonds, notes, warrants, and other interest-bearing securities of any school district, water district, road district; or any special district of any state or of the District of Columbia if the district satisfies specified conditions relative to taxing authority and good payment history;

(13) Any securities described in section 77r-1 of the "Secondary Mortgage Market Enhancement Act of 1984," 15 U.S.C.A. 77r-1, subject to all of the limitations prescribed for (6) above for investments not guaranteed by the full faith and credit of the United States;



(14) Notwithstanding (13) immediately above, any of the following securities: (a) securities offered and sold pursuant to 15 U.S.C.A. section 77d(5), (b) mortgage related securities described in 15 U.S.C.A. section 78c(a)(41), or (c) securities issued or guaranteed by the Federal Home Loan Mortgage Corporation or the Federal National Mortgage Association;

(15) Bonds or other evidences of indebtedness, bearing or accruing interest, issued, assumed, or guaranteed by any solvent corporation, trust, partnership, or similar business entity organized and existing under the laws of Ohio or any other state, or of the United States, the Commonwealth of Puerto Rico, or of the District of Columbia, or of Canada or any province of Canada, upon which there is no existing interest or principal default, if specified conditions concerning bond rating and longevity of the business entity are satisfied;

(16) Stocks or limited liability company membership interests of any insurance, financial, investment, or investment management companies if the investment management companies are registered with the Securities and Exchange Commission under the "Investment Company Act of 1940," 15 U.S.C. 80a-1, as amended;

(17) Other stocks of any solvent corporation organized under the laws of Ohio or any other state, or of the United States, the District of Columbia, Canada, or any province of Canada, if the corporation paid a dividend or distribution during the preceding 12 months on the stock to be purchased, or if the corporation, together with its predecessor corporation, has been in existence for a period of at least five years;

(18) Tangible personal property or interests in that property for the production of income, provided that the Administrator must not invest in excess of 2% of the admitted assets of the SIF as of the preceding December 31 in such property or interests;

(19) In equipment trust obligations or certificates, security agreements, or other evidences of indebtedness entered into or guaranteed by any company operating wholly or partly within the United States or Canada, if that debt obligation is secured by a first lien on tangible personal property that is purchased or secured for payment thereof and that debt obligation is repayable within 20 years from the date of issue in annual, semiannual, or more frequent installments beginning not later than the first year after that date;

(20) Government money market funds;¹

(21) Negotiable promissory notes maturing in not more than six months from the date the note is issued, secured by collateral security through the transfer of any of the classes of securities described in the bill, with absolute power of sale within 20 days after default in payment at maturity;

(22) Repurchase agreements with and interest-bearing obligations of, including savings accounts and time certificates of deposit of a national bank of the United States, a commonwealth bank of Puerto Rico, a chartered bank of Canada, or a state bank, provided such bank is either a member of the federal deposit insurance corporation created pursuant to the "Banking Act of 1933," as amended, or the Canada deposit insurance corporation created pursuant to the act of Parliament known as the "Canada Deposit Insurance Corporation Act," as amended;

(23) Certificates of deposit, savings share accounts, investment share accounts, stock deposits, stock certificates, or other evidences of indebtedness of a savings and loan association, provided all such evidences of indebtedness are insured pursuant to the "Financial Institutions Reform, Recovery, and Enforcement Act of 1989," 12 U.S.C.A. 1811, as amended;

(24) Bankers' acceptances and bills of exchange of the kinds and maturities made eligible by law for rediscount with the federal reserve banks, provided that the same are accepted by a bank or trust company incorporated under the laws of the United States or of this state or any other bank or trust company which is a member of the federal reserve system;

(25) Specified investments in business entities formed under the laws of a foreign jurisdiction² and specified investments issued by a foreign jurisdiction, subject to the limitations described under "***Limitations on permitted investments,***" below;

¹ The bill defines "government money market fund" as a fund that at all times invests in obligations issued, guaranteed, or insured by the federal government of the United States or collateralized repurchase agreements comprised of such obligations, and that qualifies for investment without a reserve pursuant to the purposes and procedures of the Securities Valuation Office of the National Association of Insurance Commissioners (sec. 4123.442(B)(3)).

² The bill defines "foreign jurisdiction" as a jurisdiction outside the United States, Puerto Rico, or Canada whose bonds are rated 1 by the Securities Valuation Office of the National Association of Insurance Commissioners (sec. 4123.442(B)).

(26) Investments denominated in foreign currency regardless of whether they are foreign investments, subject to the limitations described under "Limitations on permitted investments," below;

(27) Any securities or other property not permitted under the bill to the extent that the total amount of those investments do not exceed, in the aggregate, 6% of the total admitted assets of the SIF on the preceding December 31, within the limitations prescribed under "Limitations on permitted investments," below;

(28) Up to 5% of the total admitted assets of the SIF as of the preceding December 31 and within the limitations prescribed under "Limitations on permitted investments," below, in loans or investments³ in small businesses⁴ having more than half of their assets or employees in Ohio and in venture capital firms⁵ that meet specified requirements (sec. 4123.442(A)).

Limitations on permitted investments

For the purposes of investing in foreign investments described under (25) above and including investments denominated in foreign currency, the bill prohibits the Administrator from investing a sum exceeding in the aggregate 15% of its admitted assets as of the preceding December 31. The aggregate amount of investments held by the Administrator in a single foreign jurisdiction must not exceed 3% of the admitted assets of the surplus and reserve of the SIF as of the preceding December 31. The bill also prohibits the Administrator from investing in investments denominated in foreign currency a sum exceeding in the aggregate 10% of the admitted assets of that fund as of the preceding December 31. The aggregate amount of investments denominated in a single foreign currency held by

³ For the purposes of (28) above, the bill defines "investments" as any equity investment, including limited partnership interests and other equity interests in which liability is limited to the amount of the investment, but does not include general partnership interests or other interests involving general liability (sec. 4123.442(C)).

⁴ "Small business," under the bill, means any corporation, partnership, proprietorship, or other entity that either does not have more than 400 employees, or would qualify as a small business for the purpose of receiving financial assistance from small business investment companies licensed under the "Small Business Investment Act of 1958," 15 U.S.C.A. 661, as amended, and rules of the Small Business Administration (sec. 4123.442(B)).

⁵ "Venture capital firm," under the bill, means any corporation, partnership, proprietorship, or other entity, the principal business of which is or will be the making of investments in small businesses (sec. 4123.442(B)).

the Administrator cannot exceed 3% of the admitted assets of that fund as of the preceding December 31. (Sec. 4123.443(A) and (B).)

Under the bill the Administrator must not do any of the following:

(1) At any time, have invested a sum exceeding 5% of the admitted assets of the SIF as of the preceding December 31 in the bonds, notes, debentures, other evidences of indebtedness, and stocks of a particular corporation, trust, partnership, or similar business entity;

(2) At any time, own directly or indirectly more than 25% of the outstanding bonds, notes, debentures, other evidences of indebtedness, and stocks of any corporation;

(3) Own more than one-fourth of the capital stock of a national bank;

(4) Invest in or loan on the stocks and bonds of any railroad company to an extent exceeding one-fifth of the surplus and reserve of the SIF;

(5) In the aggregate, have an investment in and loan on all railroad property exceeding one-fourth of the surplus and reserve of the SIF;

(6) Have at any one time more than 10% of the assets of the surplus and reserve of the SIF invested in real estate and must not have at any one time more than 2% of those assets invested in any one real estate investment.

The bill expressly states that nothing in the provisions described immediately above authorizes the Administrator to use an investment in real estate primarily for recreational, agricultural, or mining purposes. (Sec. 4123.443(C) and (E).)

In the event that, subsequent to an investment in a small business or venture capital firm being made as described in (28) under "Permitted investments," above, a loan or investment is determined to have become qualified as a loan or investment described in (1) through (22) under "Permitted investments," above, the Administrator may consider such loan or investment as held under those investments and such loan or investment is no longer considered as having been made in accordance with (28) under "Permitted investments," above (sec. 4123.443(D)).

Changes to the investment policy

Current law

Under current law the Oversight Commission must establish objectives, policies, and criteria for the administration of the investment program for the Workers' Compensation System that include asset allocation targets and ranges, risk factors, asset class benchmarks, time horizons, total return objectives, and performance evaluation guidelines, and must monitor the Administrator's progress in implementing the objectives, policies, and criteria on a quarterly basis (sec. 4121.12(G)(6)). The Oversight Commission cannot specify in the objectives, policies, and criteria that the Administrator or employees of the Bureau of Workers' Compensation (BWC) are prohibited from conducting business with an investment management firm, any investment management professional associated with that firm, any third party solicitor associated with that firm, or any political action committee controlled by that firm or controlled by an investment management professional of that firm based on criteria that are more restrictive than the restrictions described in the Campaign Finance Law (R.C. Chapter 3517.). Current law requires the Oversight Commission to review and publish the objectives, policies, and criteria no less than annually and make copies available to interested parties. (Sec. 4121.12(G)(6).)

The Oversight Commission must prohibit on a prospective basis, any specific investment it finds to be contrary to its investment objectives, policies, and criteria and must prohibit investing assets of funds, directly or indirectly, in vehicles that target any of the following: coins, artwork, horses, jewelry or gems, stamps, antiques, artifacts, collectibles, memorabilia, or similar unregulated investments that are not commonly part of an institutional portfolio, that lack liquidity, and that lack readily determinable valuation (sec. 4121.12(G)(6)).

Current law requires the Oversight Commission to specify in the objectives, policies, and criteria for the investment program that the Administrator is permitted to invest in an investment class only if the Oversight Commission, by a majority vote, opens that class. After the Oversight Commission opens a class but prior to the Administrator investing in that class, the Oversight Commission must adopt rules establishing due diligence standards for BWC employees to follow when investing in that class and must establish policies and procedures to review and monitor the performance and value of each investment class. The Oversight Commission must submit a report annually on the performance and value of each investment class to the Governor, the President and Minority Leader of the Senate, and the Speaker and Minority Leader of the House of Representatives. Current law allows the Oversight Commission to vote to close any investment class. (Sec. 4121.12(G)(7).)

The bill

The bill requires the Oversight Commission to establish an investment policy using the classes of investments specified in the bill (see "**Permitted Investments**," above) for the Administrator to implement that includes the asset allocation targets and ranges, risk factors, asset class benchmarks, time horizons, total return objectives, and performance evaluation guidelines. Continuing law requires the Oversight Commission to monitor the Administrator's progress in implementing the investment policy on a quarterly basis (sec. 4121.12(G)(6)). Additionally, similar to current law, the Oversight Commission must review and publish the investment policy no less than annually and make copies available to interested parties and must prohibit, on a prospective basis, any specific investment it finds to be contrary to its investment policy (sec. 4121.12(G)(7) and (8)).

The bill eliminates the list of prohibited investments contained in current law. Also, the Oversight Commission is no longer subject, under the bill, to the limitations on campaign finance restrictions when establishing the investment policy (see "**Contracting with outside investment managers and consultants**," below). The bill also eliminates the requirements that the Oversight Commission (1) vote to open a class, (2) adopt rules specifying due diligence standards, and (3) submit an annual report to the Governor and the leaders of the General Assembly. Additionally, the bill removes the statement specifying that the Oversight Commission may vote to close a class. (Sec. 4121.12(G).)

The bill requires the Oversight Commission to adopt an investment policy that meets the requirements described immediately above no later than 90 days after the bill's effective date. Under the bill, the investment objectives, policies, and criteria in existence on the bill's effective date remain in effect until the Oversight Commission establishes the new investment policy. Additionally, the bill specifies that it applies to investments made on or after the effective date of the investment policy adopted by the Oversight Commission pursuant to the bill (Sections 3 and 4).

Contracting with outside investment managers and consultants

Current law

Current law allows the Administrator to secure investment information services, consulting services, and other like services to facilitate investment of the surplus and reserve belonging to the SIF. If the Administrator elects to secure such services, the Administrator must pay the expense of securing such services from the State Insurance Fund (sec. 4123.44). The BWC Chief Investment Officer must establish and maintain a policy to monitor and evaluate the effectiveness of

securities transactions executed on behalf of BWC (sec. 4123.441). The Administrator cannot make any investments through or any purchases from, or otherwise do any business with, specified individuals who either were employed by BWC during the preceding three years or held a fiduciary, administrative, supervisory, or trust position, or any other position in which such person would be involved, on behalf of the person's employer, in decisions or recommendations affecting the BWC investment policy, and in which such person would benefit by any monetary gain (sec. 4121.126).

Current law prohibits the Administrator from entering into a contract with an investment manager for the investment of assets of BWC funds⁶ if any employee of that investment manager who will be investing assets of BWC funds has been convicted of or pleaded guilty to a financial or investment crime, as defined under current law.⁷ Similarly, current law prohibits an investment manager who has entered into a contract with the BWC for the investment of assets of BWC funds from contracting with a business entity for the investment of those assets if any employee of that business entity who will be investing assets of BWC funds has been convicted of or pleaded guilty to a financial or investment crime. The Administrator must have the Superintendent of the Bureau of Criminal Investigation and Identification conduct criminal records checks on the employees of an investment manager and business entity that will be investing the assets of BWC funds. (Secs. 109.579, 4123.444, and 4123.445, repealed by the bill.)

The bill

The bill prohibits the Administrator from securing investment information services, consulting services, or other like services to facilitate investment of the surplus and reserve belonging to the State Insurance Fund and from entering into a

⁶ "BWC funds" are those funds specified in the Workers' Compensation Law (R.C. Chapters 4121., 4123., 4127., and 4131. that the Administrator has the authority to invest, in accordance with the Administrator's investment authority under current law (sec. 4123.444(A)(1), repealed by the bill).

⁷ A "financial or investment crime" means any of the following offenses: (1) any criminal offense involving theft, (2) receiving stolen property, (3) embezzlement, (4) forgery, (5) fraud, (6) passing bad checks, (7) money laundering, (8) drug trafficking, or (9) any criminal offense involving money or securities, as set forth under specified chapters in Title 29 of the Revised Code that govern the following offenses: (a) arson and related offenses, (b) robbery, burglary, trespass, and safecracking, (c) theft and fraud, (d) gambling, (e) offenses against justice and public administration, (f) conspiracy, attempt, complicity, weapons control, and corrupt activity, (g) drug offenses, or (h) any other law of this state, or the laws of any other state or of the United States that are substantially equivalent to the offenses listed directly above.

contract with an investment manager to have that manager invest the assets of the State Insurance Fund (sec. 4123.44). The bill defines an "investment manager" as a person who makes investments on behalf of another person but is not employed by that person. "Investment manager" does not include a venture capital firm (sec. 4123.44). In prohibiting the Administrator from entering into such contracts, the bill correspondingly eliminates the criminal records check requirements and the prohibition against making investments through a person who was employed by BWC or who provided specified services to BWC during the previous three years (sec. 4121.126 and secs. 109.579, 4123.444, and 4123.445 (repealed by the bill)). The bill also removes the requirement that the BWC Chief Investment Officer must establish and maintain a policy to monitor and evaluate the effectiveness of securities transactions executed on behalf of BWC (sec. 4123.441). The bill specifies that a contract between the Administrator and an investment manager in existence on the effective date of the bill must expire in accordance with the terms of the contract, and the Administrator must not renew or extend that contract (Section 4).

HISTORY

ACTION	DATE
Introduced	02-27-07

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