

SUBJECT: Continuing Teacher Retirement System authority to invest in hedge funds

COMMITTEE: Pensions, Investments and Financial Services — favorable, without amendment

VOTE: 9 ayes — Murphy, Vo, Capriglione, Flynn, Gervin-Hawkins, Gutierrez, Lambert, Leach, Wu

0 nays

2 absent — Longoria, Stephenson

WITNESSES: For — Timothy Lee, Texas Retired Teachers Association; (*Registered, but did not testify*: Dannie Silcox, Texas Association of Taxpayers)

Against — None

On — Jerry Albright and Brian Guthrie, Teacher Retirement System; (*Registered, but did not testify*: Brad Gilbert, Teacher Retirement System)

BACKGROUND: Government Code sec. 825.3012(a) defines "hedge fund" as a private investment vehicle that:

- is not registered as an investment company;
- issues securities only to accredited investors or qualified purchasers under an exemption from registration; and
- engages primarily in the strategic trading of securities and other financial instruments.

Sec. 825.3012(b) allows the Teacher Retirement System to invest up to 5 percent of its total investment portfolio in hedge funds. Sec. 825.3012(b-1) increases that percentage to 10 percent for funds invested before September 1, 2019.

DIGEST: HB 1612 would continue the authority of the Teacher Retirement System (TRS) to invest not more than 10 percent of its total investment portfolio

in hedge funds. It would eliminate a Sunset date of September 1, 2019 for this authority.

The bill would take immediate effect if finally passed by a two-thirds record vote of the membership of each house. Otherwise, it would take effect September 1, 2019.

**SUPPORTERS
SAY:**

HB 1612 would allow the pension system for retired teachers to continue using hedge funds to diversify its investment portfolio and reduce risk during periods of declining global equities. TRS has been investing in hedge funds since 2001. In 2011, the Legislature increased the cap on TRS hedge funds from 5 percent of its total investment portfolio to 10 percent. That authority is scheduled to expire this September, at which time the cap would drop back to 5 percent. Currently, TRS has 8 percent of its portfolio invested in hedge funds.

A common misconception is that hedge funds are risky investment vehicles. In reality, they are not an asset class but rather a business model that encompasses a variety of investment styles aimed to make money in all market conditions. During the 2008 stock market downturn, TRS hedge fund investments helped mitigate against greater losses.

TRS has negotiated favorable fee structures for the external managers it hires for its hedge fund investments. A 2010 report from the State Auditor's Office said that the TRS external manager program and its hedge fund portfolio are managed by the TRS Investment Division with due professional care and should be permitted to continue as deemed appropriate by the TRS Board of Trustees.

**OPPONENTS
SAY:**

No concerns identified.