PERSONALLY SPEAKING

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LOUISIANA TEACHER RETIREMENT SYSTEM:
WHO'S IT *REALLY* WORKING FOR?

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The grand strategy of the Teacher Retirement System of Louisiana is to invest its portfolio of funds to "achieve maximum returns and minimize risk" (p. 29, 2012 annual report). A first-year college student in finance knows that it is literally impossible to maximize returns and minimize risk because returns are tied to risk. The greater the risk, the higher the returns.

In fairness, the reports also states that the System's assets are invested to "maximize the total return on investments within prudent parameters of risk" (p. 46). Whoever prepared this report needs to clean up this internal inconsistency and any muddled thinking that contributed to it. Much is at stake – asset holdings of nearly $14 billion that provide benefits for more than 152,000 retired and actively employed educators.

There would be little reason to dwell on this matter, were it not for several other problems in the TRSL annual report.

►No executive summary that in a few pages tells the reader in plain language the essentials of the System's performance.

► TRSL lists 33 investment advisors to whom it paid $30.5 million in FY 2012 (p. 69) but there is no reporting of the amounts paid to each of the 33 advisors.

►TRSL investments amounted to $13.908 billion at the end of FY2012, down from $14.227 billion in FY 2011, a loss of $319 million. At the same time the System paid out $70.3 million for investment expenses (pp. 27, 110).

►Nothwithstanding that loss, TRSL claimed a return of 0.1 percent (p. 84). This accounting slight-of-hand was achieved by not including advisor fees and alternative investment expenses that are rebated as asset gains are realized (p. 69). (Alternative investments include mezzanine, real estate, and private equity, both foreign and domestic). The report does not tell how rebates are calculated. One dollar rebated for every dollar of fees and expenses? Or something less than that?

► The System's target rate of return in FY2012 was 8.25 percent (p. 52). It is able to reach that target with investments like mezzanine financing in which funds are made available to an existing company with little due diligence on the part of the lender (TRSL) and little or no collateral on the part of the borrower. Returns can run as high as 20 to 25 percent if the borrower does not default.

► Compared to other public funds with at least $1 billion in asset holdings, TRSL's 0.1 percent performance in FY 2012 placed it in the 81st percentile. For the domestic equities class, the System's performance put it in the 85th percentile (p. 84). The higher the percentile ranking, the poorer the fund's performance.

►Over the last five years, the System's performance put it in the 78th percentile. During that period TRSL paid a total of $146.8 million in advisor fees and $266.2 million to cover alternative investment expenses. At the same time, it received $1.1million in commission rebate income (p. 110).

► The System retained two actuarial firms, one auditor, more than 18 IT consultants and vendors, more than six law firms, and nine medical examiners. Payments to these consultants are reported (p. 71) but as with its investment advisors no detail beyond the total and subtotals is reported.

► TRSL's ten largest debt holdings include bonds from Mexico, Malaysia, South Africa, Brazil, Russia, and Thailand (p. 82). No doubt these holdings are rationalized in terms of portfolio diversification.

► Perhaps most disturbing of all is that TRSL's unfunded liability climbed from $6.0 billion in FY 2007 to $11.0 billion in FY2012 (p. 96). If the System were to collapse today, that unfunded liability would exceed the $8.3 billion in general fund revenue available to State of Louisiana. Additional taxes would have to be imposed or member benefits slashed. In effect, the Louisiana taxpayer is betting that TRSL's investment strategy pays off much better than in FY2012. To dampen any fears to the contrary, the System took the unusual step of reporting an earned investment return of 14.5 percent for CY2012.

► The System suffered a net income loss on investments of $58.5 million in FY2012 (p. 83). If TRSL had invested just *half* of its portfolio in certificates of deposit paying just one percent, those assets would have earned roughly $70 million. Additional gains might have been realized through lower advisor fees and alternative investment expenses.

Is it necessary to have 33 financial advisors? Is it *prudent* to engage in mezzanine financing? Should TRSL buy bonds issued by countries like Russia, Thailand, Malaysia? Is TRSL's target rate of return of 8.25 percent reasonable at a time when the Federal Reserve has been suppressing interest rates? Are the TRSL staff and trustees able to provide the necessary oversight to assure that the System's assets are invested safely and its unfunded liability in the end doesn't bring down TRSL?

Who's TRSL *really* working for? Its members and Louisiana taxpayers, or its investment consultants and advisors?

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