

Department of Legislative Services
Maryland General Assembly
2019 Session

FISCAL AND POLICY NOTE
Third Reader - Revised

House Bill 821
Appropriations

(Delegates Barve and Grammer)

Budget and Taxation

State Retirement and Pension System – Carried Interest – Reporting

This bill requires the State Retirement and Pension System (SRPS) to report annually on the amount of carried interest on any assets in the system; the first such report must include data from fiscal 2015 through 2019. **The bill takes effect July 1, 2019.**

Fiscal Summary

State Effect: The State Retirement Agency can carry out the bill’s reporting requirements with existing resources. No effect on revenues.

Local Effect: None.

Small Business Effect: None.

Analysis

Current Law/Background: SRPS is subject to a fee cap of 0.5% of the market value of its assets, not including real estate or alternative investments, which are not subject to any fee cap.

By December 31 of each year, the SRPS Board of Trustees is required to report to the General Assembly the actual amount spent for investment management services during the preceding fiscal year.

Exhibit 1 shows the investment management fees reported for the prior two fiscal years, by asset class and type of fee. In fiscal 2018, SRPS investments returned 8.1% net of fees paid. For fiscal 2018, SRPS finished the year with assets of almost \$52.0 billion, so

investment management fees of \$372.0 million in that year represented about 0.72% of assets.

Exhibit 1
Investment Management Fees
State Retirement and Pension System
(\$ in Thousands)

	<u>FY 2017</u>			<u>FY 2018</u>		
	<u>Management</u>	<u>Incentive</u>	<u>Total</u>	<u>Management</u>	<u>Incentive</u>	<u>Total</u>
Public Equity	\$77,520	\$2,596	\$80,116	\$83,023	\$19,247	\$102,270
Fixed Income	10,300	220	10,520	12,555	4,351	16,906
Credit Opportunity	33,674	2,043	35,717	29,668	3,111	32,779
Real Return	22,284	3,174	25,458	16,504	2,323	18,827
Absolute Return	45,301	8,832	54,133	44,189	10,939	55,128
Private Equity	85,950	47	85,997	103,714		103,714
Real Estate	31,318	2,669	33,987	31,389	1,449	32,838
Currency Overlay	4,593	0	4,593	5,275	0	5,275
Other Investment Expenses	3,117	0	3,117	4,267	0	4,267
Total	\$314,057	\$19,581	\$333,638	\$330,584	\$41,420	\$372,004

Source: 2018 Comprehensive Annual Financial Report, State Retirement and Pension System

Carried Interest Transparency

In the past five years, calls for greater transparency in the reporting of carried interest have led to changes in the investment management industry. Carried interest is earned by investment managers in private markets (e.g., private equity, private real estate) and is the amount that a general partner (investment manager) retains as an ownership interest in the investment profits generated by the partnership. Carried interest typically represents 20% of the profits generated, but that proportion may be negotiated among the parties involved. As carried interest represents shared profits that are retained by the general partner rather than paid by the investor, it is not typically reported as investment fees paid.

Recently, several public pension plans, including the California Public Employees' Retirement System (CalPERS) and the Pennsylvania Public School Employees' Retirement System (PSERS) have released reports showing carried interest earned by general partners managing investments on their behalf. In addition, the Institutional

Limited Partners Association developed a reporting template that includes carried interest that has been endorsed by many investment managers and public pension funds (including SRPS).

In its initial report, CalPERS reported that general partners earned \$700 million in carried interest in fiscal 2015. PSERS reported that general partners earned \$5.17 billion in cumulative carried interest from 1980 through 2017. For calendar 2017, PSERS reported that general partners earned \$669 million in carried interest. Of note, PSERS indicated that it took 500 hours of staff and consultant time to generate the report on carried interest.

Additional Information

Prior Introductions: None.

Cross File: None.

Information Source(s): State Retirement Agency; *Governing*; Institutional Limited Partners Association; Pennsylvania Public School Employees' Retirement System; Department of Legislative Services

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