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SPRINGFIELD

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FILE NO. S-261

PENSIONS;
Illinois State Board of Investment
Nominee-commingling of assets

Honorable Carl F. Faust, Jr.,
Director
Illinois State Board of Investment
Room 1100, 160 North LaSalle Street
Chicago, Illinois 60601

Dear Director Faust:

On behalf of the Illinois State Board of Investment, (hereinafter referred to as I.S.B.I.) you requested an opinion on the legality of a nominee-custodial arrangement set up by Arthur Young & Company, the accounting advisor of the Board.

The problem involves the interpretation of P.A. 76-1829, passed June 21, 1969 and approved October 10, 1969.

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That act created the I.S.B.I. with authority to "manage invest and re-invest" securities and funds of the then existing State Employee's Retirement System, the General Assembly Retirement System, and the Judge's Retirement System "and to perform such other duties as may from time to time be authorized by the General Assembly."

Article 22A-109 provided for a nine man board with five ex-officio members including the State Treasurer, the Chairman of the Illinois Public Employees Pension Law Commission and the Chairmen of the three retirement systems covered, and four members appointed by the Governor with the approval of the Senate.

The board elected appointee Henry L. Pitts as Chairman, and pursuant to Section 22A-110 appointed you as Director. Under Section 22A-111 Arthur Young and Company was appointed as accounting advisor for the Board.

Though P.A. 76-1829 created a new board it must be recognized not as a new law but as an amendment to an existing statute-Chapter 108 1/2, the Pension Code.

In Apex Motor Fuel Co. vs. Barrett, 20 Ill. 2d, 395 our Supreme Court at page 399 said;

"portions of old law which are repeated in an amending act are regarded as a continuation of existing law rather than the enactment of new law on the subject."

To ascertain the powers and authority of the I.S.B.I. it is necessary to determine the intention of the General Assembly as shown by the 1969 enactments.

P.A. 76-1829 merely amended the Pension Code by transferring to the I.S.B.I. certain management and investment powers which had previously been vested by Chapter 108 1/2 in the boards of trustees of the three retirement systems. The administrative and investment powers of the three boards were covered in Section 2-127 and 2-135 for the General Assembly System, Sections 14-172 and 14-179 for the State Employee's Retirement System and Sections 18-135 and 18-141 for the Judge's Retirement System.

Two sets of amendments were made in 1969 to each of these articles. P.A. 76-741 passed May 6, 1969 and approved August 15, 1969 amended four sections of the General Assembly Retirement System including the investment powers in Section 2-135. P.A. 76-745 passed

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May 27, 1969 and approved August 15, 1969 amended six sections of the Judge's Retirement System, including the investment powers in Section 18-141. P.A. 76-747 and 748 passed June 21, 1969 and approved August 15, 1969 amended certain sections of the State Employee's Retirement System, though the investment powers were not mentioned.

Subsequently, P.A. 76-1829 passed June 21, 1969 and approved October 10, 1969 amended the Illinois Pension Code by removing all investment and securities management authority from the boards of the three systems and vesting those powers in the new board, I.S.B.I. which was created by adding Article 22A. No other powers of the three boards were affected in any way, and the three chairmen were to be ex-officio members of the I.S.B.I.

P.A. 76-1829 recites it is to amend Sections 2-135, 2-145, 2-147, 14-179, 14-185, 14-191, 18-141, 18-153 and 18-154 and to add Article 22A to the Illinois Pension Code. Sections 2-135, 14-179, and 18-141 covered the investment powers of the old boards and the other six sections

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covered necessary changes in the duties of the State Treasurer and the State Auditor resulting from the transfer of the investment authority to the I.S.B.I.

As to Sections 2-135, 14-179 and 18-141 the Act repeated the same investment powers as had appeared in the 1967 statute or in the May enactments by P.A. 76-741 and P.A. 745 mentioned above. To each section was added "As soon as possible and practicable following the effective date of this amendatory Act and, in any event, prior to July 1, 1970, the board of trustees shall transfer to the Illinois State Board of Investment, created by this Act, for management and administration, all investments owned by the system of every kind and character. Upon the completion of such transfer the authority of the board of trustees to make investments shall terminate. Thereafter all investments of the reserves of this system shall be made by such Illinois State Board of Investment, in accordance with the provisions of Article 22A of this Code."

The amendments to the three sections relating to the State Treasurer stated he should hold such securities

so transferred "subject to the order and direction" of the I.S.B.I. The State Auditor was to honor vouchers "approved by the director of the Illinois State Board of Investment in accordance with the order and direction of said board."

As a successor by amendment to the powers of the three old boards, the I.S.B.I. necessarily had all investment authority previously vested in those boards plus such additional powers as were expressly or impliedly granted by P.A. 76-1829. It is evident the General Assembly intended to give the I.S.B.I. much broader and more flexible powers than those held by the old boards.

As noted above, the sections amended required transfer of all investments to the I.S.B.I for "management and control" and provided both the State Treasurer and State Auditor were to follow the "order and direction" of the new board on investments.

The new Article 22A in Section 101 stated the I.S.B.I was created "with authority to manage, invest and reinvest" all reserves and securities of the three systems.

Section 22A 106 provides:

"Manage': To invest, reinvest, exchange and to perform all investment functions with regard to reserves, funds, assets, securities and moneys which the board is authorized to invest, and to preserve and protect such reserves, funds, assets, securities and moneys, including, but not limited to, authority to vote any stocks, bonds or other securities and to give general or special proxies or powers of attorney with or without power of substitution. This term shall not include any functions, duties and responsibilities incident to the operation and administration of pension funds other than that of investments."

Section 22A 111 states "The board shall manage the investments of any pension fund for the purpose of obtaining a total return on investments for the long term."

To permit the new board to carry out these virtually unlimited powers, the General Assembly in Article 22A removed a number of restrictions which had formerly limited the investment powers of the old boards. The investment sections of each of the old boards provided "all investments shall be clearly marked to indicate ownership by the system and to the extent possible shall be registered in the name of the board." (Sections 2-135,

14-179 and 18-141) Section 22A 112, sub-paragraph 10 instead provides "All investments shall be clearly marked to indicate ownership by the system". As long as the investments are marked to show which system is owner, there is no restriction on the I.S.B.I. as to the name in which they may be carried.

The old language on registration of names, of course, appears in the amending part of P.A. 76-1829 because the sections to be repealed were necessarily set out in full. Even if the old provision had not been expressly repealed the old language has such a total and manifest repugnance to the language subsequently adopted in Article 22A that the old language cannot stand. (People ex rel. vs. Southern Ry. Co., 17 Ill. 2d 550, 557.)

Besides deleting the earlier express requirement on registration, the General Assembly has broadly increased the investment powers of the I.S.B.I. Before amendment, each Article provided "The assests of the system shall be invested as one fund." (Sections 2-153, 14-196, 18-160) Article 22A in Section 114(1) states the I.S.B.I

"may, for investment purposes, commingle all or a part of the invested assets of one or more pension funds under its jurisdiction and authority." To make commingling possible, it was of course necessary to remove any requirement of registration.

The investment authority of the I.S.B.I. is far greater than that granted any of the three systems under the repealed sections. Sec. 22A 112 requires three printed pages in the Session Laws to list the various categories in which investments can now be made.

Section 22A 113 provides that prior to July 1, 1970, the trustees of the three systems:

"...shall transfer to this board for management and investment all of their securities or for which commitments have been made, and all funds, assets or moneys representing permanent or temporary investments, or case reserves maintained for the purpose of obtaining income thereon. This transfer shall be receipted for in detail by the Chairman and director of the board.

The securities, funds and other assets so transferred to the Illinois State Board of Investment shall be placed in the custody of the State Treasurer who

shall serve as official custodian of the board, provide adequate safe deposit facilities therefor and hold all such securities, funds and other assets subject to the order of the board."

Pursuant to this mandatory provision the State Treasurer accepted the securities and funds and entered into a contract with the First National Bank of Chicago to be custodian of said assets of the three funds and to provide adequate safe deposit facilities therefor. The State Treasurer assumed the custodial expense. It had been the practice of the State Treasurer to make similar custodial arrangements with banks as to each of the three funds, though that action was not specifically authorized in the earlier statutes.

The General Assembly expressed its approval of such arrangements in Section 22A 111 which stated the I.S.B.I. could make such custodial arrangements with national or state banks in Illinois.

Section 22A 110 provides:

"The board may adopt such rules and regulations (not inconsistent with this Article) as in its judgment are desirable to implement and properly administer this Article. A copy thereof shall be filed with the Secretary of State."

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Sections granting somewhat similar general powers to establish rules and regulations were included in each of the other systems, but of course, not limited solely to securities management and investment authority. (See Sections 2-143, 14-176, and 18-150).

It is my conclusion that the nominee-partnership arrangement and safeguards described in the attachments to your letter is within the broadened authority granted the I.S.B.I. in P.A. 76-1829.

In reaching my conclusion, I have taken the following considerations into account. In giving effect to the intention of the legislature, the Illinois Supreme Court has found it proper to consider the occasion and necessity for the law. L. & N.R. Co. vs. Industrial Board, 1918, 282 Ill. 136; The People vs. Fox, 1915, 269 Ill. 300. Also, the Supreme Court has given recourse not only to language used in a particular statute, but also to reasons motivating its enactment and the purpose to be accomplished. Moyer vs. Board of Education, 1945, 391 Ill. 156.

The clear and convincing language of Paragraph 22A 106, in granting to the Illinois State Board of Investment the power to "perform all investment functions with regard to reserves, funds, assets, securities and moneys" gives rise to the conclusion that the General Assembly intended the Illinois State Board of Investment to have all such necessary powers to implement the grant of this authority. Without the necessary powers to implement its purpose, the Illinois General Assembly's intention would be frustrated.

Further, I have also looked at contemporary circumstances in the securities market place. Courts, in seeking to arrive at intentions of legislatures with regard to legislation, consider it proper to look at existing circumstances and contemporary conditions. First National Bank vs. Wedron Silica Co., 1933, 351 Ill. 560; Bowman vs. Industrial Commission, 1919, 289 Ill. 126.

I have, therefore, taken official notice of the majority of the transfer agents of listed and unlisted corporations. In numerous circumstances, transfer agents require the execution of stock powers by each and every one of the members of boards similar to the I.S.B.I. To call upon all

members of that board on each and every occasion where a common stock was bought or sold to execute stock powers would seriously impair and frustrate the purpose of the enabling legislation. Stocks could not be bought and sold quickly, and delivery would sometimes be held up for a period of 30 to 60 days depending upon the individual requirements of each transfer agent. The I.S.B.I. would be seriously handicapped in trading equity securities. It could not be done, and thus the intention of the General Assembly would be thwarted. However, these circumstances are remedied by the use of a nominee. By using a nominee, the I.S.B.I. is enabled to have the full faith and credit of a large financial institution to guarantee good title of each of its securities, and obviates the necessity of the execution of many stock powers by its members. The use of a nominee would thus put the I.S.B.I. on equal footing with other high volume trading investors who likewise call upon the full faith credit of financial institutions to guarantee good title as a nominee.

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I do not see any inconsistency or conflict between the provision (Paragraph 22A 112) requiring that all investments be clearly marked to indicate ownership by the particular pension fund and the provision (Paragraph 22A 114) authorizing the Board, for investment purposes, to commingle the invested assets of the pension funds. The language of these two provisions is clear and unambiguous and each provision must be given full force and effect. Requirement that all investments must be clearly marked to indicate ownership by the particular pension fund does not prohibit or mean an investment cannot be made by using more than one pension fund. That provision which requires the investments to be clearly marked to indicate ownership of the system relates to the bookkeeping records of the I.S.B.I. Since the statute expressly authorizes commingling, it is concluded that the Board is authorized to commingle the assets for investment purposes in accordance with and in compliance with these two provisions in the Illinois Pension Code.

Very truly yours,

A T T O R N E Y G E N E R A L