

# Overview of Public Pension Plan Governance

November 2019



Although often overlooked or misunderstood, governance—defined as the systems and processes that comprise the oversight and control of an organization—plays an important role in the performance of a state or local government retirement system. Public retirement systems are established under state statutes, local ordinances, or both, and subject to fiduciary, investment, and administrative laws, which both grant authority to, and place restrictions on, entities responsible for one or more key areas of plan governance. This overview is intended to summarize the laws and rules that govern public plans, and the range of entities typically responsible for them. Common law trust laws, as well as the prudence and fiduciary standards required by them, also govern public pensions. Because every public retirement system and pension plan, including its governance structure, is unique, the description provided in this introduction is intended to illustrate typical arrangements and will not apply to every state, system and plan. Subsequent publications will address some of these unique or atypical governance arrangements.

## Key Takeaways

- Governance of public retirement systems is typically vested with a range of entities; those with a primary role include a legislative body, chief executive, public pension board of trustees, and key staff. An oversight committee or agency and other entities may also have a role.
- Key areas of retirement system governance—setting benefit levels, design and funding—in most cases are not delegated to public retirement system boards or staff, but rather are the responsibility of elected legislative bodies and the chief executive.
- Public retirement system boards and staff typically face restrictions in one or more key areas of governance that typically is assigned to them, including asset management, personnel policies, and the use of service providers.
- Every public retirement system is unique and systems should be measured in the context of their individual governance framework.

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## The Role of Legislative Bodies and Chief Executives

Two areas with a significant effect on the cost of a public pension plan and its funding level are the plan's design and financing structure.

A pension plan's design refers to the framework of the plan, defined by such characteristics as the age of eligibility to qualify for benefits, the rate at which benefits accrue, vesting requirements, required contributions from employers and employees; and others. A pension plan's design is the most important factor in the plan's cost, and normally is the responsibility of policymakers: state legislatures, city councils, and county commissions, etc. Recommendations for benefit design can also come from a variety of stakeholders, including governors, mayors, and other constituent group representatives.

### Typical Responsibilities Legislative Body

- Establishes retirement plan design
- Approves pension plan funding
- Establishes retirement system board structure
- Approves some or all retirement system board members

### Typical Responsibilities Chief Executive

- Proposes and approves or denies plan design
- Proposes and approves or denies plan funding
- Appoints some or all board members

Similarly, authority to fund the plan also lies mostly outside the authority of the public retirement system board. Although most states regularly pay their full Actuarially Determined Employer Contribution, some do not. Responsibility for funding a pension plan typically lies with a legislative body (e.g., the legislature, city council, county commission, etc.), accompanied by approval of the chief executive (e.g., the governor, mayor, etc.).

Among the most well-funded public pension plans in the U.S., commitment to timely and adequate actuarially determined contributions is the primary cause of the plan's healthy funding condition. Some boards in recent years have been given limited authority to effect employee or employer contribution rates, or both, but the vast majority of boards lack such authority.

In addition to responsibility for establishing and funding the plan, the legislative body and chief executive also ordinarily are responsible for creating the structure of the board that oversees administration of the retirement plan, and for selecting or approving, or both, some or all of the members of the board. Appendix A identifies the legislative committees or other entities in each state with jurisdiction or oversight over statewide retirement systems.

Statutes governing public retirement systems are approved by state legislatures and governors, and therefore also reflect the role of those entities in the public retirement system governance process.

## Retirement System Board and Staff Responsibilities

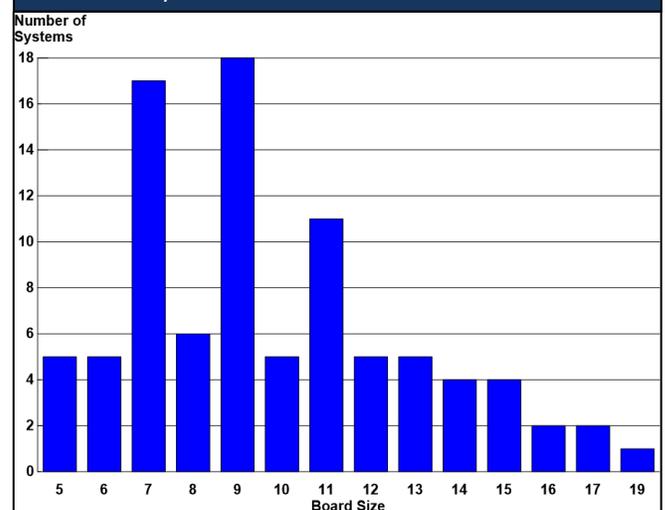
Public retirement system boards are the entity most commonly associated with governance of public retirement systems.

Boards are established to oversee the operations of the system, chiefly to ensure the system is fulfilling its statutory responsibilities related to retirement system functions. This oversight function requires conducting periodic meetings; hiring and firing of key staff members; approving a budget; setting staff compensation levels; and approving processes for procurement of professional services, though in some cases the legislature and/or chief executive also exert influence over or control some of these processes. In addition to ensuring the system is complying with legal responsibilities, boards also are expected to ensure that retirement systems are providing services in an appropriate and cost-effective manner.

Retirement system staff, and specifically top management positions, are ordinarily appointed by the system board and are responsible for carrying out the board's directives. As such, system managers serve as agents of the board, and high-level staff are considered fiduciaries to the plan (as described below).

Core retirement system staff functions include, among others, investment of the system's assets; administering plan benefits; financial accounting and auditing; actuarial measurement and analysis; managing information technology; communicating with stakeholders; managing service contracts and contractors; and human resources management.

Figure 1: Distribution of the number of trustees on public retirement system board



### *Typical Responsibilities* **Retirement System Board**

- Oversees administration of retirement plan
- Approves actuarial assumptions and methods
- Approves asset allocation and investment policy
- Hires and fires retirement system director and consultants

Although these are typical areas of responsibility, there is variation among the type and degree of authority individual system staff have over outcomes within these elements. For example, some retirement systems are not tasked with responsibility of managing assets, while other systems do have that responsibility.

Laws governing the size and composition of public retirement system boards vary widely. Methods of selecting board members can include: 1) election by the system's active and retired members, 2) appointment by the governor, legislative leadership, or other public officeholder, and/or 3) by virtue of holding another public office (ex-officio, such as state treasurers, comptrollers, public school superintendents, or their designees). Figure 1

identifies the distribution of public retirement system board size, and [a link to a listing of public retirement systems' board composition is found at the end of this document.](#)

Most public plan fiduciary laws pre-date the Employee Retirement Income Security Act (ERISA), the body of federal laws governing private pension plans. Although not subject to ERISA, public pension board members are, by definition, fiduciaries and they operate under rules consistent with general trust principles inherent in common law. These rules stipulate that board members shall operate a) solely in the interest of plan participants; b) for the exclusive purpose of providing benefits to participants and their beneficiaries; c) using the care, skill, and prudence that a prudent person or investor would use under like circumstances, etc.

In addition to fiduciary and prudence standards, public pension trustees also are subject to ethics standards and conflict of interest laws, and to numerous oversight and reporting requirements, such as open records laws, open meetings laws, financial reporting requirements, sunset requirements, audit standards, etc.

### *Typical Responsibilities* **Retirement System Staff**

- Administers retirement plan
- Recommends retirement plan design and funding policy
- Recommends actuarial assumptions and methods
- Recommends asset allocation and investment policy
- Recommends consultants

### ***Restraints on Board Authority***

Most public retirement system boards are subject to a range of restrictions in one or more areas of their key responsibilities. For example, many public retirement systems are subject to final legislative approval of their budget, and/or state rules governing their ability to hire, fire, and compensate personnel. Such restrictions affect a public retirement system's ability to compete for professional talent, for example, by restricting the amount a system may pay their investment professionals. Similarly, some states place limits on pension fund asset management such as restricting the portion of the portfolio that may be allocated to certain types of investments.

### ***Other Areas of Board Authority***

In addition to the responsibilities noted above, most public retirement system boards also have authority to set actuarial assumptions, which are projections about future demographic and economic events used to calculate the cost of the plan and to determine its financial condition. Actuarial assumptions that are especially consequential include the investment return assumption, the rate at which employer payrolls will grow, and the mortality assumption, which projects how long plan participants will live. Of all actuarial assumptions, the investment return assumption is the single-most impactful on the cost and funding level of the plan.

There are some exceptions to boards' authority to set actuarial assumptions; for example, in some states, including Florida, Minnesota, South Carolina, and Washington, authority to set the actuarial investment return assumption rests with the legislature or another entity external to the retirement system. A NASRA [issue brief on investment return assumptions](#) identifies (in its Appendix B) the entity responsible for setting the investment return assumption for selected state plans.

In recent years, a small number of state retirement system boards have been granted authority, via legislation, to make limited changes to the plan design or funding arrangement of the plan(s) overseen by the board. This authority is notable because it is unusual and, as previously discussed, these are governance elements typically reserved for legislative bodies and chief executives.

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## External Investment Entities

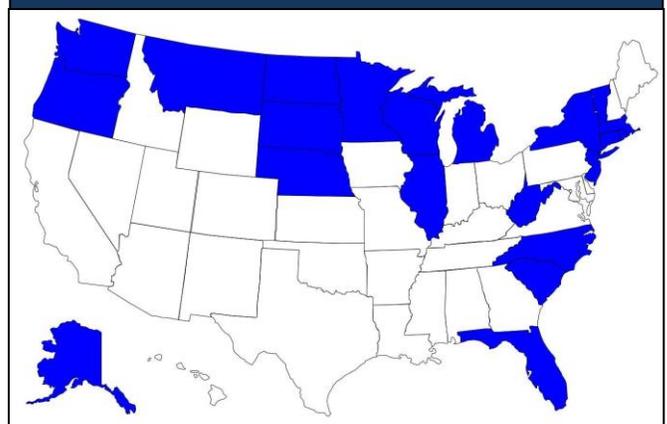
Most public retirement system boards are responsible for overseeing the management and investment of system assets, with this function typically delegated to an investment committee. These committees, which can include all or a subset of individuals on the system board, are generally tasked with developing investment strategies and monitoring investment processes.

Some other states divide the responsibility for overseeing administration of benefits from investing of assets, with the investment function performed by a state agency external to the retirement system. [A link to a compilation of public retirement system investment committees and other oversight entities is found at the end of this document.](#)

Three examples of separate investment entities include the Minnesota State Board of Investment, the Florida State Board of Administration, and the Massachusetts Public Retirement Investment Management Board. In each of these cases, the investment board focuses solely on investing the assets, while one or more separate boards oversee functions associated with administering plan benefits.

A third approach is used in three states—Connecticut, New York, and North Carolina—which constitutionally assign a sole fiduciary, elected statewide, to invest the system's assets. Figure 2 identifies states where some or all public pension assets are managed by an external agency or a sole trustee.

Figure 2: States in which some or all public pension assets are managed by a separate entity or sole trustee



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## Other Oversight Agencies

In addition to the stakeholders and entities identified previously, other statewide boards, agencies and legislative committees provide oversight of some or all retirement systems or retirement system functions in certain states. Some state agencies have wide ranging oversight responsibilities for state and/or local public retirement systems in their state. For example, the Texas Pension Review Board (PRB) is an independent state agency charged with reviewing state and local retirement systems' actuarial soundness and compliance with state law. The Ohio Retirement Study Council (ORSC) provides oversight of the state's retirement systems and

advises the legislature on matters pertaining to benefits, funding, investment, and retirement system administration.

State agencies may exert oversight of a particular retirement system function. For example, the Louisiana Legislature established the Public Retirement Systems' Actuarial Committee (PRSAC) to review and study the actuarial assumptions, methods, and funding policies used by public retirement systems in the state. Similarly, the California Actuarial Advisory Panel (CAAP) was established to provide independent actuarial information to public retirement systems and other stakeholders.

Although oversight entities such as these typically have limited to no governance authority, many of them provide recommendations regarding plan design and financing, and they bring greater transparency to public retirement system operations, policies, and practices. A listing of state oversight agencies is included in Appendix A.

#### **Typical Responsibilities Oversight Boards and Commissions**

- Various responsibilities regarding oversight and monitoring of retirement system and pension plan operations and methods, including in some cases, responsibility for recommending or setting actuarial assumptions, actuarial methods, and approving funding

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## **Conclusion**

Authority to make the most consequential decisions regarding the long-term health of a public pension plan typically lies not with the retirement system board, but with policymakers, who enact the laws that establish the plan, its design and financing; and who authorize the public entities responsible for key areas of governance. Although boards, oversight agencies and system staff are delegated many governance responsibilities, they must operate within mandated restrictions, and they typically do not have authority to determine or adjust benefit levels or funding. Understanding a retirement system's governance framework is a vital first step toward properly evaluating a public pension plan, its condition, and the entities responsible for various policy outcomes.

## **Links to Resources**

- [Public retirement system board composition](#)
- [Composition of public retirement system board investment committees and external investment agencies](#)

### **Future Research**

Future research on this topic will examine the respective roles of each major public pension governing entity: retirement system boards, including the presence or absence of governance restrictions in place on the board; legislatures; governors; and retirement system staff. Future research also will focus on fiduciary duty: who is a fiduciary, who is not, and how fiduciary duty relates to governance.

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## Appendix A: Entities with Responsibility for Oversight of Statewide Retirement Systems

The operations of most statewide retirement systems are typically overseen by a board of trustees.

Information about board composition can be accessed here: [Composition of Public Retirement System Boards](#)

Deviations from this structure are noted for selected states in this resource.



State	Organization	House Committee	Senate Committee	Joint Committee	Notes
AL		Varies	Varies		
AK		Varies	Varies		
AR				Joint Committee on Public Employee Retirement and Social Security Programs	
AZ		Insurance	Finance		
CA	California Actuarial Advisory Panel <a href="https://www.sco.ca.gov/caap.html">https://www.sco.ca.gov/caap.html</a>	Public Employment and Retirement	Labor, Public Employment and Retirement		
CO				Pension Review Commission	A Pension Review Subcommittee is responsible for focusing on the financial health of CO PERA.
CT				Joint Appropriations Committee	
DC				DC Council Committee on Finance & Revenue	
DE				Joint Finance Committee	
FL	Department of Management Services <a href="http://www.dms.myflorida.com/">http://www.dms.myflorida.com/</a>	Government Operations Subcommittee	Governmental Oversight & Accountability		The <a href="#">Bureau of Local Retirement Systems in the Department of Management Services' Division of Retirement</a> monitors Florida's local government defined benefit pension plans for compliance with Florida law and Florida Administrative Code provisions. These responsibilities are divided between the Local Retirement Section and the Municipal Police Officers and Firefighters' Retirement Trust Funds Office.

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GA		Retirement	Retirement		
HI		Labor & Public Employment	Judiciary & Labor		
IA				Public Retirement Systems Committee	
ID		Commerce & Human Resources	Commerce & Human Resources		
IL		Personnel & Pensions	Licensed Activities & Pensions	Commission on Government Forecasting & Accountability	The state actuary is hired by the state auditor general and reviews the 5 state retirement systems' actuarial reports, assumptions, and state funding calculations. The State Department of Insurance collects reports for all funds and systems, with most of its efforts devoted to smaller local police and firefighter funds which operate independently.
IN		Employment, Labor & Pensions	Pensions & Labor		
KS		Pensions & Benefits	KPERS Select Committee	Joint Committee on Pensions, Investments, and Benefits	
KY	Public Pension Oversight Board <a href="https://kyret.ky.gov/About/Board-of-Trustees/Pages/Public-Pension-Oversight-Board-Materials.aspx">https://kyret.ky.gov/About/Board-of-Trustees/Pages/Public-Pension-Oversight-Board-Materials.aspx</a>	State Government	State & Local Government		
LA	Public Retirement Systems' Actuarial Committee <a href="https://www.doa.la.gov/Pages/prsac/Index.aspx">https://www.doa.la.gov/Pages/prsac/Index.aspx</a>	Retirement	Retirement		

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MA	Public Employee Retirement Administration Commission <a href="http://www.mass.gov/perac/">http://www.mass.gov/perac/</a>				
MD		Appropriations	Budget & Taxation	Joint Committee on Pensions	
ME				Joint Committee on Appropriations and Financial Affairs	
MI	Municipal Stability Board <a href="http://www.michigan.gov/localretirementreporting">www.michigan.gov/localretirementreporting</a>	Varies	Varies		
MO				Joint Committee on Public Retirement	
MN				Legislative Commission on Pensions & Retirement	
MS		Appropriations	Finance	Joint Legislative Committee on Performance Evaluation and Expenditure Review	
MT				State Administration and Veterans Affairs Interim Committee; Legislative Finance Committee	
NC			Pensions & Retirement and Aging		
ND				Employee Benefits Programs Committee	
NE		Appropriations	Retirement Systems		
NH		Executive Departments and Administration	Executive Departments and Administration		

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State	Organization	House Committee	Senate Committee	Joint Committee	Notes
NJ	Pension & Health Benefits Review Commission <a href="http://www.njleg.state.nj.us/committees/pension.asp">http://www.njleg.state.nj.us/committees/pension.asp</a>				
NM				Investments and Pensions Oversight Committee	
NV				Interim Retirement and Benefits Committee	
NY			Civil Service and Pensions Committee		
OH	Ohio Retirement Study Council <a href="http://www.orsc.org/?1">http://www.orsc.org/?1</a>				
OK	Oklahoma State Pension Commission <a href="http://okpension.ok.gov/index.html">http://okpension.ok.gov/index.html</a>	Business, Labor & Retirement Laws	Pensions		
OR				Joint Committee on Ways and Means	
PA		State Government	Appropriations		
RI		Finance	Finance		
SC		Ways and Means	Finance		
SD		Retirement Laws	Retirement Laws		
TN				Council on Pensions & Insurance	The TN Consolidated RS operates under the Tennessee Department of Treasury
TX	Texas Pension Review Board <a href="http://www.prb.state.tx.us/">http://www.prb.state.tx.us/</a>	Pensions	State Affairs		
UT				Retirement and Independent Entities Appropriations Subcommittee	
VA				Joint Legislative Audit and Review Commission	

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State	Organization	House Committee	Senate Committee	Joint Committee	Notes
VT	Public Retirement Study Committee <a href="http://www.vermonttreasurer.gov/content/retirement/Study-Committee">http://www.vermonttreasurer.gov/content/retirement/Study-Committee</a>	Government Operations	Government Operations		
WA	The Washington State Department of Retirement Systems is an administrative agency that administers pension and other benefits for state and local employees and teachers, and is not overseen by a board of trustees.			Select Committee on Pension Policy	The <a href="#">Pension Funding Council</a> is responsible for setting economic assumptions and pension contribution rates for the state's 11 pension plans. At least once every 6 years, the council administers an audit of the actuarial of the valuation used for rate setting.
WI				Joint Survey Committee on Retirement Systems	
WV	Municipal Pensions Oversight Board (31 police, 22 fire plans) <a href="http://www.mpob.wv.gov/Pages/default.aspx">http://www.mpob.wv.gov/Pages/default.aspx</a>			Joint Standing Committee on Pensions and Retirement	
WY				Joint Appropriations Committee	