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Nebraska Retirement Systems Committee
February 28, 2013

[LB77 LB138]

The Committee on Nebraska Retirement Systems met at 12:00 p.m. on Thursday, February 28, 2013, in Room 1525 of the State Capitol, Lincoln, Nebraska, for the purpose of conducting a public hearing on LB138 and LB77. Senators present: Jeremy Nordquist, Chairperson; Al Davis, Vice Chairperson; Danielle Conrad; Russ Karpisek; and Heath Mello. Senators absent: Rick Kolowski.

SENATOR NORDQUIST: Welcome to the Retirement Systems Committee. Please take a seat, and we're going to go ahead and get started. Good morning. I'm State Senator Jeremy Nordquist from District 7, which covers downtown and south Omaha, the Chair of the Retirement Systems Committee. Just a couple of housekeeping items. If you are testifying, there are sheets in the back corner. Please fill those out and deliver them to our committee clerk. There are also sheets if you want to indicate you support or opposition to a bill. And please silence your cell phone not to distract so we don't get that picked up in the audio. Please state and spell your name when you are testifying for the record. With that, to my left is our committee counsel, Kate Allen; to my far right, our committee clerk, Laurie Vollertsen; Matthew, our page today; Senator Karpisek was just in the room when we got started and snuck out. I don't know if he'll be back. I know Senator Davis will be joining us. Senator Kolowski has another engagement. We have Senator Heath Mello from District 5 and Senator Danielle Conrad from District 46. With that, we are going to go ahead and get rolling. Senator Krist, welcome. [LB138]

SENATOR KRIST: (Exhibits 1 and 2) Thank you, Senator Nordquist. Good afternoon, members of the Nebraska Retirement Systems Committee. For the record, my name is Bob Krist, that's B-o-b K-r-i-s-t, and I represent the 10th Legislative District in northwest Omaha along with a north-central portion of Douglas County which includes the city of Bennington. And I appear before you today in introduction and support of LB138. My introduction will be strikingly similar to the letter of intent because it is...encapsulizes the bill. The University of Nebraska Group Health Trust Fund presently holds more than \$143 million, including nearly \$27 million in General Fund appropriations. Section 85-128, 85-129, 85-131 of the Nebraska Revised Statutes clearly designate the State Treasurer as the custodian of the university funds, who is authorized to make disbursements therefrom. Regardless, the University of Nebraska created the trust fund without the approval or even knowledge of the State Treasurer, effectively removing hundreds of millions of dollars from appropriate as well as statutorily mandated executive oversight. It should be noted that the Legislature was also uninformed of the trust fund's existence, rendering similarly impossible any sort of legislative input or direction. LB138 remedies the ongoing mishandling of the trust fund. The bill creates a Group Health Trust Fund and directs the corpus of the trust fund to be transferred thereto. More importantly, LB138 places the Group Health Trust Fund under the express control of the State Treasurer, where that money should always have been. A couple of personal notes. The university did come in and talk with us about the issue.

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I'm sure they're not going to agree, and I know they will be here in opposition. We met with President Milliken and with the...I met with President Milliken and the State Treasurer, Don Stenberg. We had a wonderful meeting, and, I think, at that meeting, J.B. was very straightforward. He said: if you tell us to move it, we're going to move it, but don't tell us how to manage it. That's not what this is about. It's not about the ability of the regents or the university to develop trust funds, because they have that authority. It is about where it is. It is outside the state, being invested by Wells Fargo. I'll save my comments regarding that situation for my closing, and I will be here. I would entertain any questions if you have any. [LB138]

SENATOR NORDQUIST: Thank you, Senator Krist. Questions from the committee? Seeing none at this time. [LB138]

SENATOR KRIST: You have a letter passed out from Don Stenberg, State Treasurer, as well as an Opinion I'm sure that you will look at at your leisure from the Office of the Attorney General. And with that, I'll allow the next one. [LB138]

SENATOR NORDQUIST: Great. Thank you. We will entertain proponent testimony. Welcome. He might have stepped out. Maybe just hand it to Laurie and she'll get it distributed out. Thank you, Mr. Auditor. Welcome. [LB138]

MIKE FOLEY: (Exhibit 3) Thank you, Chairman Nordquist and members of the Nebraska Retirement Systems Committee. For the record, my name is Mike Foley, F-o-l-e-y, and I'm the Auditor of Public Accounts, here today in support of LB138. I recognize you're on your lunch break, so I'll be brief out of respect for your limited time. In April of 2010, the Legislature's Performance Audit Committee authorized my office to conduct a Performance Audit relating to the cost of health insurance for state employees. As part of that extensive process, we examined for comparative purposes the separate employee health plans offered by certain public entities, including the University of Nebraska. That audit revealed that the university had created on its own, without any express authority, statutory or otherwise, a separate group health trust fund with a local bank. The establishing of banking relationships is clearly within the authority of the State Treasurer. However, now that this banking relationship has been established, the university routinely funnels into the trust fund money collected to manage its employee health plan and to pay insurance claims. In addition, some \$27 million in General Fund appropriations were moved into the fund over the past seven years. As of June 30, 2011, the trust fund held about \$104 million; since then it's ballooned to about \$143 million. That is an extraordinary sum of money not to be under the proper custody of the State Treasurer. Because the committee's time is limited this afternoon, I won't belabor the details of why the audit report questioned the legality of the Group Health Trust Fund. For anyone interested, the report is available in its entirety on my Web site and you can read all of the details of why we came to that conclusion. What LB138 boils down to in its simplest form is the question of who's going to oversee

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more than \$143 million in public funds. State statute already says that the Treasurer is the custodian of all university funds. However, by creating the Group Health Trust Fund, the university not only circumvented that law but also effectively removed from any state oversight whatsoever an extraordinary sum of public money. So long as the university is permitted to maintain the Group Health Trust Fund in its present form, no effective central management or control of that money is possible. As a matter of fact, prior to my office's audit report, neither the Treasurer nor the Legislature had knowledge of the fund's existence. And that's not a criticism of the Treasurer or the Legislature; there was simply no way for you to have known this. Without LB138, the university will continue to set aside and spend in virtual secrecy the more than \$100 million already in the fund. There will be no way to ensure that this money, which the audit report shows conclusively as to be far in excess of what it needs to be, is managed efficiently, much less that it's actually used for employee health insurance purposes. Fortunately, Senator Krist has provided the Legislature with an opportunity to bring a measure of accountability and transparency to this health fund. Passage of the bill will allow the fund to be formally established with the State Treasurer will be empowered to safeguard it in coordination with the state's investment officer. I applaud Senator Krist for bringing the bill and encourage you to advance this important legislation. Thank you very much. [LB138]

SENATOR NELSON: Thank you, Mr. Foley. Questions from the committee? Senator Conrad, please. [LB138]

SENATOR CONRAD: Thank you, Auditor Foley. Nice to see you, as always. [LB138]

MIKE FOLEY: Thank you. [LB138]

SENATOR CONRAD: Just a quick follow-up in regards to some of the issues before the body and before this committee on these related topics. Have you had a chance to review the legislation forwarded to the full body for consideration that emanated from the Legislative Performance Audit Committee in regards to additional accountability and oversight on this issue? [LB138]

MIKE FOLEY: Was that the LB620, I think it is? [LB138]

SENATOR CONRAD: I'm sorry, I don't remember the number off the top of my head. [LB138]

MIKE FOLEY: I think that might be the bill you're referring. [LB138]

SENATOR CONRAD: Okay. [LB138]

MIKE FOLEY: And I think that's a good bill and... [LB138]

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SENATOR CONRAD: Okay. [LB138]

MIKE FOLEY: ...I see it's moving forward and I'm pleased to see that. [LB138]

SENATOR CONRAD: Yes, and that was my question to you, was how did you see that interfacing with this piece of legislation? [LB138]

MIKE FOLEY: I think that's an important component of it... [LB138]

SENATOR CONRAD: Okay. [LB138]

MIKE FOLEY: ...to make sure that the...not only the university but also DAS would come forward and explain where they are with the health insurance plans, because these are self-funded plans, as you know. And to make sure that they're reporting properly to the Legislature and where we are with those plans, what the rates are, what the premiums are, the claims history, the fund balances, and all that kind of information. [LB138]

SENATOR CONRAD: Okay. [LB138]

MIKE FOLEY: I think we should be regularly apprised of it. [LB138]

SENATOR CONRAD: Because it seems to me, in reviewing the materials in advance of this hearing, that there may be some honest disagreement about some of the underlying legal issues, but we're all in agreement that from a policy perspective we want to move towards increased accountability and oversight. [LB138]

MIKE FOLEY: Yes, yes. [LB138]

SENATOR CONRAD: And so I just wanted to make sure that that was your position as well and to see if maybe there was another vehicle to address those issues. [LB138]

MIKE FOLEY: Yes, thank you, Senator. [LB138]

SENATOR CONRAD: Okay. Very good. Thank you. [LB138]

SENATOR NORDQUIST: Thank you. Any additional questions? Senator Davis. [LB138]

SENATOR DAVIS: Thank you. Thank you, Mr. Chairman. So, Auditor Foley, the revenue that's in this, it comes from the university system and is to fund their healthcare, is that correct? [LB138]

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MIKE FOLEY: Well, it comes from the employee portion of the premium; it comes from the employer's portion that the university funds from General Funds and tuition dollars and so forth; and it also comes from General Fund appropriations which were moved into the fund. And of course earnings on the fund would accrue... [LB138]

SENATOR DAVIS: And so there's never been any report of this money to the state Auditor? [LB138]

MIKE FOLEY: No. I don't think...outside of the university, I don't believe any of us were aware of that fund until we did this audit. [LB138]

SENATOR DAVIS: Thank you. [LB138]

SENATOR NORDQUIST: Okay. Thank you. Any additional questions? Seeing none, thank you. [LB138]

MIKE FOLEY: Thank you, Senators. [LB138]

SENATOR NORDQUIST: Next proponent. Welcome. [LB138]

DON STENBERG: Mr. Chairman, members of the committee, for the record, my name is Don Stenberg, S-t-e-n-b-e-r-g, and I'm the State Treasurer of the state of Nebraska. The situation of the University of Nebraska Group Health Trust Fund came to my attention as a result of the work of the Legislature's Performance Audit Committee and the State Auditor's audit of the university health fund. Senator Krist has already offered a copy of a letter that I sent to him that outlines my response to a number of arguments the university has made. I'm not going to go into all of those, but I'd refer the committee to those for the points that I don't make here today. I think that the history of the legal relationship of the State Treasurer to the University of Nebraska is a very important consideration here with LB138. Since the founding of the university in 1869, state law--which is now codified as Section 85-128 of the Nebraska statutes--has provided as follows, quote, the State Treasurer shall be the custodian of all the funds of the university, unquote. Then in 1907, more than 100 years ago, the Nebraska Legislature specifically provided, quote, the State Treasurer shall be the treasurer of the state university. And that's today Nebraska statute 85-129. And just to make sure that this was clearly understood, the Legislature added 85-131, which provides, quote, disbursements from the university funds shall be made by the State Treasurer, unquote. So there's a very long history of more than 140 years that the State Treasurer is the custodian of the funds of the university and more than 100 years the Treasurer of the state of Nebraska has been the treasurer of the university by state statute. This history is confirmed by a Nebraska Attorney General's Opinion, which Senator Krist has distributed to you. That's dated January 21, 1998. And I'm just going to highlight a small portion of that Opinion that gets to the essence. And that Opinion says, "This office,"

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meaning the Attorney General's Office, "has indicated in previous Opinions that constitutional officers such as the State Treasurer have certain core functions and inherent constitutional authority which cannot be removed by legislative enactment." The Opinion goes on, "Since Article VII, Section 10 of the Nebraska Constitution," which provides the general government of the University of Nebraska shall under the direction of the Legislature be vested in the Board of Regents, "must be read together with Article IV, Section 1," which creates the Office of State Treasurer, "and since the core functions of the State Treasurer seem to include the matters above, we believe that the general government of the University of Nebraska vested in the Board of Regents under the Nebraska Constitution may only be exercised in such a way as to preserve the Treasurer's general authority over the custody of state funds and the supervision of the state's relationships with state and national banks." That was an Opinion given 15 years ago to then-State Treasurer Dave Heineman involving the question of whether the University of Nebraska could have its own credit card contract, and the Opinion concluded they could not. And as of today, the university still operates under a credit card contract entered into by the State Treasurer's Office. Now the university argues that the money used to pay health insurance benefits to University of Nebraska employees is not money of the state and therefore not subject to the custody of the State Treasurer. And the university points to an Attorney General's Opinion dated February 1, 2012, which said that once funds are paid to a labor union that provides health insurance for the members of the State Patrol, that the money ceases to be the money of the state. The basis for that Opinion is that the union is not a part of state government and that, therefore, once a payment is made to the union, the funds cease to be state funds. Clearly that Opinion does not apply here. The university cannot seriously argue that it is not a part of the state government, nor can the university seriously argue that just because these funds have been set aside for a particular purpose, in this case the payment of health insurance claims, that the funds cease to be money of the state. There are several University of Nebraska funds that are set aside for statutorily specified purposes which are under the custody and control of the State Treasurer and are invested by the Nebraska Investment Council. You can find a list of those funds at 85-122 in the Nebraska statutes. In addition, even if the health insurance funds were not deemed to be the money of the state, the Legislature still has the authority to place it under the custody and control of the State Treasurer. For example, the Nebraska College Savings Program created by state law names the State Treasurer as the trustee. None of the money in that trust is the money of the state. It all comes from investments made by individuals who are saving for college for their children, grandchildren, nieces, and nephews. LB138 is consistent with the requirements of the Nebraska Constitution concerning constitutional authority of the State Treasurer and is consistent with the passage of numerous statutes dating back to 1869 repeatedly designating the State Treasurer as the custodian of the university funds. It is very important, I think, to understand that if LB138 becomes law, the university would retain complete control of the university's health insurance plan. The university would continue to select the insurance company that would manage the plan. The university would

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decide what coverage is available. The university would decide what the employee contributions would be. The university would decide what the employer contributions that they would make to the plan would be. And the university would make all policy decisions concerning the university health insurance plan. The State Treasurer would simply expend funds at the direction of the University of Nebraska, as the Treasurer now does with other University of Nebraska funds, and the money would be invested by the Nebraska Investment Council, which already invests many of the other funds of the University of Nebraska. Now, from my perspective as former state attorney general and the State Treasurer, you know, why does this matter? And I think it matters because it's a separation of power issue that's set forth in our State Constitution that dates back to the founding of our state back in the 1860s. And it's a little bit easier to understand with a few examples that are a little bit, maybe, absurd but I think help understand the issue. For example, there's currently a vacancy in the Board of Regents at the University of Nebraska because one of the regents was recently appointed Lieutenant Governor. Now it's pretty clear under our state constitution that the Governor makes that appointment. But what if the university were to say, well, you know, we really understand the Board of Regents better than the Governor; this will be a colleague of ours; we really understand what the qualifications of a regent should be; we should make that appointment. Or they might say, you know, we're not satisfied with the way the Secretary of State handles these elections for the Board of Regents; and the Board of Regents are the core of the general government of the university, and so we ought to handle those elections. Or--and I think this is a more likely example--they might say, you know, the State Auditor, he's really just a politician; you know, he gets elected, and we need a real auditor; and so we're going to go out and hire our own auditor and then we're not going to let the State Auditor review our records because we think we can do it better. I think those are all easier to see, maybe, than the handling of the state's money, but the same principle is in effect. This is a system that has been in effect under our constitution and state statutes, in this case, since 1869. And I think it's important we preserve that as a part of the separation of powers and a check and balance on the expenditure of funds of the state for state employees, in this case University of Nebraska employees. With that, I'd be happy to answer questions. [LB138]

SENATOR NORDQUIST: Thank you, Mr. Stenberg. Any questions from the committee? Senator Mello. [LB138]

SENATOR MELLO: Thank you, Chairman Nordquist, and thank you, Treasurer Stenberg. I've been thinking through this issue for a while, in part, obviously, as a member of the Performance Audit Committee that was involved with this performance audit that...both with Senator Krist as the bill introducer as well as with State Auditor Foley. And while I'm not an attorney I guess this is just something I just would like your opinion on. The issue at hand, to some extent, is when does...when legally does a payment to an employee become their actual payment instead of it becoming state funds? Because I've been trying to wrestle with this issue: when the university pays an

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employee, that payment becomes the employee's and then they ultimately give the payment back for health insurance. Isn't that some of the issue that we're kind of discussing here, legally, is trying to make the definition of when does that actually occur and when does the money ultimately leave the state's hands, in the case of the university, go into a nonstate employee...or a nonstate hands, i.e., the employee, and then go back into some other trust fund? [LB138]

DON STENBERG: Well, that's what...I think that's the argument the university is going to make; and I think they're going to testify and they're going to say, you know, this isn't the money of the state because part of the money has been deducted from paychecks to pay the employee portion of the health insurance. But part of it is state General Fund money, the employer match. And I think what this legislation is intended to do is have the Legislature answer the question you just asked and say that this...whether you want to define this as money of the state or simply trust funds that the state has a great interest in, that these are going to be put in a trust through the state process under the Department of Administrative Services. It will be expended the way almost all other university funds are expended, which is, basically, the university asks for a payment, and within two days that payment is made. So the question you ask, I think, is answered by LB138, if it is passed. And I would point out, as I mentioned in my initial testimony, in some cases the State Treasurer is responsible for funds that clearly are not funds of the state, as in the case of the College Savings Program. [LB138]

SENATOR MELLO: Yep. [LB138]

DON STENBERG: Here I think there's a great interest, public interest, that however you define these funds, that they are critical to the health insurance of the employees of the University of Nebraska, which is, I think, over 10,000 people. And clearly the money originated with the state. Clearly the Treasurer and the legal...and the Nebraska Investment Council already handle most of the other funds of the university, so this is nothing out of the ordinary at all. It would be consistent with pretty much the handling of other University of Nebraska funds. [LB138]

SENATOR MELLO: Okay. All right. Thank you. [LB138]

SENATOR NORDQUIST: Senator Conrad. [LB138]

SENATOR CONRAD: Thank you, Mr. Treasurer. Just a quick question just so that I'm clear and to set the record straight. There is a legal and a technical compliance argument, and then there's also some of these policy considerations related to oversight and accountability that are at issue with this legislation. In your knowledge, based upon the existing situation at hand, are you aware of any sort of waste, fraud, or abuse of these funds in their current designation? [LB138]

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DON STENBERG: No, I'm certainly not. Not an auditor, haven't audited. [LB138]

SENATOR CONRAD: Sure. Yes. [LB138]

DON STENBERG: And I think, though, that the reason you have separation of powers and you have this division of duties is so that you minimize the chances for that to happen. [LB138]

SENATOR CONRAD: Okay. [LB138]

DON STENBERG: And I think that's the...why things have been done this way. Obviously, the Legislature back in 1907 decided, you know, let's make this official. We'll make the State Treasurer the treasurer of the University of Nebraska. That continues to be the policy of the Legislature. That statute remains in effect more than 100 years later. And I think the other thing is that, from a public disclosure, state point of view, having this as part of the state accounting and expenditure system makes it much easier to audit it, much easier for the Legislature to keep track of what's going on, the size of that fund, and take that into account as they appropriate funds for the University of Nebraska. If they've already got \$143 million sitting there for health insurance, maybe they don't need as much of a General Fund for a while. So, I mean, I think that would be of benefit to the Legislature to have that information readily available through the state accounting system. [LB138]

SENATOR CONRAD: Okay. Thank you. [LB138]

SENATOR NORDQUIST: Any additional questions from the committee? Seeing none, thank you. [LB138]

DON STENBERG: Okay. Thank you very much. [LB138]

SENATOR NORDQUIST: Any additional proponent testimony? Seeing none, any opponent testimony? [LB138]

DAVID LECHNER: (Exhibit 4) Good afternoon, Senators. [LB138]

SENATOR NORDQUIST: Welcome. [LB138]

DAVID LECHNER: My name is David Lechner, spelled L-e-c-h-n-e-r. I'm senior vice president and CFO of the University of Nebraska, and I'm here to speak in opposition to LB138. The bill at its essence seeks to move health insurance funds held by a trustee bank on behalf of university employees and their families to State Treasurer and to the State Investment Officer. My opposition is simply premised: If it ain't broke, don't fix it. The catalyst for this bill was a performance audit by the State Auditor. That report

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overall was very complimentary to the operations of the university's health plan. It chronicled that the plan operates at \$10,000 less per employee than comparable plans, based on family coverage. Administrative costs are a fraction of the other plans. It has, as of now, about ten months in reserve. By virtually every benchmark, that report validated the successful management of the plan. The audit report questioned whether the Board of Regents could legally establish trust accounts. Our answer to that question is clearly yes. The university obtained a legal opinion from outside counsel that the board was within its constitutional powers in establishing the trust. We also have an AG's Opinion on point, referred to earlier, that supports the board's ability to establish accounts like the health trust. The report attempts to buttress its arguments supporting a change in the management of our health trust and custody of the funds by referring to the funds held by the trustee as state funds. That description is inaccurate and should be discarded. Once the funds are paid into the trust, they become property of the plan and its members and can only be used, per the terms of the trust agreement, for medical, pharmacy, and dental claims, and related costs. Even if one were to try to parse through those commingled funds now the property of the trust, proportion originating from state appropriation would only be about 30 percent. The rest comes from employee contributions, auxiliary operations, and federal grants and contracts. Another point that speaks against LB138 is efficiency. I am not sure what is envisioned, but am wary of passing bills in order to find out the details. We currently have a one-day process for paying claims with BlueCross BlueShield and CVS/Caremark. Under our current way of doing business, doctors, pharmacies, hospitals, and other providers across the state get paid on a prompt basis. I'm certain the new system, whatever it might be, cannot improve on one day. Accounting for claims in a second set of books, which this would entail, introduces many new levels of complexity and cost. The university would likely have to hire a clerk and train a backup. It would increase the workload at DAS. It would increase the workload at State Treasurer's Office. It would increase the workload at the state investment officer's office. With increased workload at DAS, Treasurer, and SIO, this proposal starts to sound like three steps back for one step forward. Worst of all, none of this increased activity would provide any additional value to employees who count on the health plan. We, in concert with our bank trustee, have been good fiduciaries, as measured by investment returns by the trust. It has not been established as to how the trust would be invested under this proposal. But had the health trust reserves been invested in the state's short-term investment pool last year, it would have earned about 2.6 percent. While very good for short-term money, our trust earned 4.24 percent last year, a difference of about \$1.8 million. That difference represents increased health premiums of about 15 bucks a month for every employee. I am not opposed to oversight. But oversight does not require change in management. I applaud and testified in favor of the alternative approach offered by Senator Harms in LB620, where we, along with DAS, would provide annual reports to the Legislature on the status of the plan. I would also like to note, we have provided to Senator Harms and the Performance Audit Committee guidelines we're using to plan management. We welcome this means of reporting and providing insights to legislators, plan members,

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and other interested parties. Another note about oversight. These funds are included in our annual audit, our annual general purpose audit. Auditor Foley signs off on that audit each year, so they are subject to audit. Secondly, when it comes to legislative oversight, I am certain that Legislative Fiscal provides a briefing on this plan every year to Appropriations. So there has been oversight, but we welcome the additional offered by LB620. In summary, we have been good stewards and fiduciaries in the area of providing health benefits to employees. By virtually every benchmark cited in that performance audit report, we are doing an outstanding job. Our plan is competitive with our peers. We're earning good returns to offset employer and employee premiums. We've run the plan at a relatively low cost and minimal administrative costs. In closing, those of you who know me know that I view one of my primary jobs in serving President Milliken, the board, campuses, the Legislature, and, ultimately, taxpayers as always looking for ways to decrease costs and increase efficiencies. I can safely tell you this proposal will absolutely increase costs and does not provide any increased value to our plan members. Please, I ask we not take three steps back to take one step forward. [LB138]

SENATOR NORDQUIST: Great. Thank you, Dave. [LB138]

DAVID LECHNER: Thank you, Senator. [LB138]

SENATOR NORDQUIST: Can you just address that on from...maybe summarize the legal opinion that you have, how you're not out of compliance with the 1869 and 1907 statutes? [LB138]

DAVID LECHNER: Senator, if I could defer legal questions to my general counsel, who's going to come right up behind me. [LB138]

SENATOR NORDQUIST: You bet. Sure. All right. No problem. [LB138]

DAVID LECHNER: I'm just the accountant who keeps track of the money. [LB138]

SENATOR NORDQUIST: Sure. No problem. Other questions. [LB138]

SENATOR CONRAD: Thank you, Mr. Lechner. [LB138]

DAVID LECHNER: Thank you, Senator. [LB138]

SENATOR CONRAD: And, as the accountant, I just wanted to clarify for the record because, having a chance to visit with our fiscal analysts about this office...or this issue a little bit, I understand that an additional...in addition to the briefings that they provide to the committee and the Legislature, there's also a quarterly report that the university makes to the Fiscal Office in regards to this fund. Is that right? [LB138]

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DAVID LECHNER: You're absolutely right. And I'd forgotten about that, too, because on a quarterly basis since Moses was a pup we've sent in a (laughter) quarterly report, talks about the fund balance. So it's not a big, deep, dark secret. [LB138]

SENATOR CONRAD: Sure. And that's just on a voluntary basis right now, or is it part of some other requirement, are you aware of, where that emanate from? [LB138]

DAVID LECHNER: I'm not sure how that got started, Senator. [LB138]

SENATOR CONRAD: Okay. [LB138]

DAVID LECHNER: But I...we've sent that in forever and ever. [LB138]

SENATOR CONRAD: Very good. Thank you. [LB138]

DAVID LECHNER: Thank you for reminding me of that. [LB138]

SENATOR NORDQUIST: Additional questions? Senator Davis. [LB138]

SENATOR DAVIS: Mr. Lechner, thank you for your testimony. How do you determine the amount of General Fund revenue you're going to ask for each year? [LB138]

DAVID LECHNER: We did not ask in the coming biennium for any health trust, because what we're planning to do is lose money next year to bring down that trust balance, and that's part of the guidelines we discussed with Senator Harms and Performance Audit, sir, is that we're going to draw the fund down. We were considering a holiday, similar to the state, but I've received some good counsel from others that said with all this changing in healthcare, this isn't a good time to be making changes. For example, if we get into the Patient Protection Act and we don't cover all of our employees, there's a \$20 million penalty we get to pay. So we are planning...in the first year we didn't request health funds. We did in the second year. Because our trend overall has been 8 percent for about 20 years. And as you are all aware, if you're using one-time funds for base costs that are increasing at a rate of 8 percent, once you start chasing that train, it really gets rugged. And I had to come here in 2001, Senator, and beg for a little bit of money because our plan wasn't doing well, just like the one at the state. I said I'd never do that again, and I pledge to you, we're working on those health trust balances. That will be part of the report, along with a lot of details to what our costs are, and we are working at moving that down and we've filed that with Performance Audit. [LB138]

SENATOR DAVIS: Okay. Thank you. [LB138]

DAVID LECHNER: Thank you for the question. [LB138]

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SENATOR NORDQUIST: Any additional questions? Senator Mello. [LB138]

SENATOR MELLO: Thank you, Chairman Nordquist, and thank you, David, for your testimony. I guess it's more of a general question, and by all means I hope, if anything, that the university would take this as a request on behalf of probably, no doubt, myself but the committee, is, Senator Krist, obviously, I serve with Senator Krist on Performance Audit Committee, and this was an issue we discussed at length. And I think Senator Krist brought LB138, I think, in the best of intentions of trying to provide more oversight over an issue that, as Auditor Foley mentioned, had very little oversight in terms of legislators and policymakers in regards to determining what our policy or our fiscal policies were, were being impacted in regards to healthcare...health insurance funds. Is there anything that, I think, beyond LB620, that the university thinks they could work on with Senator Krist to try to address the issue that he's trying to address in LB138, I think, which is beyond moving it to the State Treasurer? Is there any other ideas or suggestions that you would have that you would be able to work with Senator Krist on in regards to proving more transparency over this issue? [LB138]

DAVID LECHNER: Absolutely. And I've got a great case in point that involves the state investment officer, in fact. We have certain funds that are given to the University of Nebraska Foundation. There is joint oversight over those, where Mr. States sits with the foundation in doing, looking at investment managers and so on. Senator, there's plenty of middle ground here without recreating the wheel. And we would welcome that opportunity. I'm willing to make that report to LB620, whatever you think it might be. I think it'd be very insightful, and I also think it'd help colleagues at the state in looking at best practices between the two so we can solve this health insurance cost problem. I welcome it. [LB138]

SENATOR MELLO: Okay. Thank you. [LB138]

SENATOR NORDQUIST: Any other questions? Seeing none, thank you. [LB138]

DAVID LECHNER: Thank you, sir. [LB138]

SENATOR NORDQUIST: Additional opponent testimony? Welcome. [LB138]

JOEL PEDERSEN: Good afternoon. I'm Joel Pedersen. I'm general counsel at the university, after my introduction from my colleague. I do want to say I don't have prepared testimony but I was here to answer in the event there were some legal questions. I also wanted to thank Senator Krist. I was at the meeting. I think we've had good conversations about this and people have brought earnest and authentic issues as well. The Auditor has been very straightforward in approaching this issue. We've had a lot of conversations around this. And I think, you know, we're doing our best to be

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receptive and be responsive. We do want to be accountable to our employees especially who expect us to do well on this. But we also do have to answer those hard legal questions. So if there aren't any other questions, I'll head right to that one that Senator Nordquist asked. We did have outside counsel take a look at this. Fraser Stryker is a firm who's done work for the university but who's not, you know, embedded with us. So we wanted an independent look at this issue. And there is a 17-page opinion about this. I don't plan to go through that with you, but you certainly, as committee members, are entitled to see that. If you haven't seen it already, I will get that to you directly. The other issue that comes up is, of course, I wouldn't be general counsel of the university without mentioning the 1977 case Board of Regents v. Exon. And that does answer, in part at least, this historical question. There was a constitutional convention in 1871. Prior to that time, and in 1869 in particular, the university existed under the plenary authority of the Legislature. So they were really a child of the Legislature at that point. After 1871, we have kind of the current structure, where the university is a component unit of the state under the financial guidelines. Under the legal guidelines, we are a separate constitutional entity. We're a body corporate of the state of Nebraska. And so that collegial is a much more accurate representation. We're separate but not entirely so. And I think that helps, in a number of respects, understand the issues here. In the private sector, for example, it'd be rare where that kind of a separate entity, even on a collegial or related affiliated entity, would borrow a treasurer from the other entity. You just don't see that. And I think, for our purposes, we have to acknowledge we're a public sector and there are these separation of powers issues that Don Stenberg talked about. You know, and I do appreciate that he sent a letter; that's part of the reason why I'm here. So he's been very up-front with us and the university in framing the issues and getting us to talk about the history and what it means for his office to be involved here. So I am very grateful for that and respect his thinking on this quite a bit. My view of it, and I think it's shared by outside counsel, is it revolves around the issue that Senator Mello...we do have trust funds here. This isn't a bank account. And I understand the AG's Opinion about establishing banking relationships. You'll see in that 17-page opinion, that's all under the trust statutes in Nebraska, which are entirely separate. That's in a different article than all of the banking and depository regulations. You know, while it is Wells Fargo and they do operate a bank in Nebraska, you know, I'm not sure how their corporate organization runs, but this is handled by their trust folks, not their banking folks. And I realize there may be some policy issues that overlap with the NEST example, and I think that's a better analogy. That's really what we're talking about here from the policy point of view. Do you want to look at this healthcare trust fund and then say, you know, really, the state of Nebraska wants this, these funds that have been established for the...in trust for the benefit of the university employees to be handled by the State Treasurer? And as the president said, if that's your determination as a matter of policy, we're willing to do that. But I think Dave has identified some of the reasons why we're questioning that. You know, is that the best practice? Is that the best value? Is that going to protect the interests of the university employees? The last thing I'll mention, and if there's any other questions I'm happy to address them, that Exon

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case in 1977 did address the issue of whether university employees are state employees. And we have a separate personnel system. We do not go through DAS. HR resources are entirely separate; and that is part of the governance of the university, is the pay and the employment of university employees. So that is a separate function. [LB138]

SENATOR NORDQUIST: Okay. Thank you, Joel. Questions from the committee? Senator Conrad. [LB138]

SENATOR CONRAD: Thank you, Mr. Pedersen. I would hope that all of us who are attorneys in the room could apply for CLE credits after this (laughter) discussion today with a vibrant review of history and legal policy surrounding this issue. It's actually very interesting from that perspective. My question to you is, is there an opportunity potentially through amendments to LB138 or in some other vehicle to...or is there an opportunity or a need to clarify the university's ability to carry out their functions as they currently exist? [LB138]

JOEL PEDERSEN: Perhaps. [LB138]

SENATOR CONRAD: Okay. [LB138]

JOEL PEDERSEN: I, of course, I'm also supportive of LB620. [LB138]

SENATOR CONRAD: Yes, I appreciate that. [LB138]

JOEL PEDERSEN: I think that's the better answer here on the accountability and oversight. For our purposes, I guess we do have a number of other trust funds, and I don't think that's the question here. Could we write legislation about that? Sure. But, again, I go back to the governance of the university over our employment and HR, and I think the first place I'd start with that is with the Board of Regents. And I think our oversight and accountability, the separation of powers issues are directly addressed by reporting. And we're certainly willing to do that. [LB138]

SENATOR CONRAD: Okay. Very good. [LB138]

SENATOR NORDQUIST: Additional questions? Seeing none, thank you. [LB138]

JOEL PEDERSEN: You bet. [LB138]

SENATOR NORDQUIST: Any additional opponent testimony? Seeing none, any neutral testimony on this bill? Seeing none, Senator Krist. [LB138]

SENATOR KRIST: (Exhibit 5) Thank you, committee members, and thank you to Mr.

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Lechner and Mr. Pedersen for coming and presenting a view. And I hope it's clear to you we didn't play "I got a secret." We went to everyone, had everyone weigh in. At issue, though, here, I think, and very importantly, is not whether or not you lose \$1.8 million in investment by taking it outside should be the litmus test of whether or not you should comply with the statute. The statutes are clear. The Treasurer is the Treasurer, period. Now should they want to amend the bill or come back, or the Treasurer would sit down and talk with the university and say: I own the funds; I have...I oversee the funds, I'm sorry; I have oversight and you can continue to invest them here, but I need to see some kind of expenditure or invoice on a system. That's between the Treasurer. To say that LB620 is an alternative to this bill is an injustice. We in Performance Audit see things every day that need to take...we need to take action. Now the action part of the performance audit finding was to put oversight in place so this never happens again. That's what LB620 does. Then when we see an issue, it requires legislation, potentially. What I think you'll see here, too, the argument was made they can do things in one day. The Auditor...I'm sorry, the Treasurer, I think, was very specific. Ask him for a check; you get a check in two days. Is that so strenuous? I'm not sure. I think the issue here, again, is not management. We're not questioning management. We're not questioning the way they run their ship. There might be a question about how DAS has run the state ship, but we're not questioning how they've run their ship. But how do you get from zero to 60 in 2.5 seconds, the \$143 million, and not have that oversight by the Treasurer, who, going back to the 1800s, should have been your oversight capability? Finally, I guess just in terms of the overall picture, and I won't throw any mud, but I will point this out. In real estate, the old saying is "location, location, location." In government, it's "perception, perception, perception" and "accountability, accountability, accountability." It would not be necessary to expend \$7,084.14 out of the University Group Health Trust Fund for a legal opinion if you were trying to maintain a trust fund and spend that kind of money that needed to be spent on premium reduction for the citizens of Nebraska who are employed by the university. I'll leave this with you as part of your input. They can make the copies as necessary. With that, I will take any questions that you have for me. [LB138]

SENATOR NORDQUIST: Thank you, Senator Krist. Any questions from the committee? Senator Conrad. [LB138]

SENATOR CONRAD: Thank you, Senator Krist. I'm not familiar with the invoice that you're going to pass around, but that's in relation to the Fraser Stryker opinion that was solicited on this topic? Is that what that refers to? [LB138]

SENATOR KRIST: Yes, ma'am. Yes, ma'am. [LB138]

SENATOR CONRAD: Okay. Thank you. [LB138]

SENATOR NORDQUIST: Any additional questions? Senator Mello. [LB138]

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SENATOR MELLO: Thank you, Chairman Nordquist. And Senator Krist, you heard my comments to the university. I do applaud the sense of the work we did on the Performance Audit Committee in bringing LB138. I would agree it's not...LB620 is not an alternative to this. I think that it's an appropriate way, it's another issue involving the audit which ultimately moves things forward. But as I asked the university...and it seemed that they were amenable to continue to work on potential language and changes to LB138 to try to find a way for them to get to yes as well as, I think, with what I understand your underlying intention to be in LB138. And I hope that those conversations continue to move forward. [LB138]

SENATOR KRIST: Absolutely. [LB138]

SENATOR MELLO: But I appreciate you bringing the bill forward. [LB138]

SENATOR KRIST: Absolutely. Thank you. [LB138]

SENATOR NORDQUIST: Thank you. No further questions; thank you, Senator. [LB138]

SENATOR KRIST: Thank you. [LB138]

SENATOR NORDQUIST: All right, we will move to LB77. Senator Avery, please come on up. Welcome. [LB77]

SENATOR AVERY: Good afternoon, Mr. Chair. My name is Bill Avery, B-i-l-l A-v-e-r-y, representing District 28 here in south-central Lincoln. The bill before you, LB77, creates the Nebraska Iran Divestment Act and would prevent Nebraska's public funds, including public employee retirement funds, from being used to support Iran's power, nuclear, and military sectors. This legislation is part of a larger nationwide divestment campaign to isolate economically the Iranian regime to force a change in their roguish and dangerous behavior in the world. The United States has a responsibility as the most complete superpower ever assembled to encourage and, if needed, enforce lawful and peaceful behavior among other states because the international system lacks an effective rule-making and rule-enforcing mechanism. So states have, over time, evolved a system in which a major power emerges that takes that responsibility. And that happens to be the United States in this century. In July of 2010 Congress recognized that federal sanctions against Iran might not be enough; and as a result, Congress overwhelmingly passed the federal Comprehensive Iran Sanctions, Accountability, and Divestment Act, which specifically authorized state governments to impose sanctions against Iran. So this legislation is authorized by and is consistent with that law. Nebraska would join the federal government and 23 other states plus the District of Columbia in this divestment effort. LB77 directs the Office of the Nebraska Attorney General to assemble a comprehensive list of "scrutinized companies," companies that

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hold more than 10 percent of revenue from contracts or provide any supplies or services related to power production activities, mineral extraction, or military equipment to the government of Iran. The Attorney General will update the scrutinized list annually based on continuing information from nonprofit organizations, research firms, international organizations, and governmental entities. The Attorney General will then transmit the list to the chief investment officer of the Nebraska Investment Council. The council is prohibited from pursuing any acquisitions in direct holdings of a company that is on the scrutinized list, unless...and there are a couple of exceptions. If the federal government excludes a company from the scrutinized list, obviously we would not continue to keep them on the list. Also, if some action would result in the breach of fiduciary duty of the council, if the council decides that their fiduciary duty to their shareholders would be compromised, then they could opt not to participate. It is important to note that the Investment Council does have a mechanism in this bill to override the provisions that are contained in the bill should a situation arise where their professional duties and obligations would be compromised. This was a fairly significant point of compromise between the Attorney General's Office and the Investment Council. The Divestment Act does not apply to direct holdings in social or humanitarian development companies, any companies authorized by the U.S. government to have business operations in Iran, or indirect holdings in companies. Furthermore, the Divestment Act will terminate if Iran is removed from the U.S. State Department's terrorist list or if the President of the United States deems that state divestment legislation interferes with national foreign policy. It is important to note that the Office of the Attorney General has stated his willingness to absorb all financial responsibility for this initiative. They will generate the list of scrutinized companies based on existing information about Iran's investors; they will send letters to Nebraska fund managers outlining new state policy prohibiting acquisitions in these scrutinized companies; and they will follow through with enforcement of the act. It is probably clear to you by now that this bill is less of a divestment bill than it is a prospective noninvestment in companies affiliated with Iran. No existing investments will be affected. I am pleased to sponsor this bill with the support of the Attorney General, because Iran does pose a real threat to the safety of our allies in the Middle East, ultimately also to world peace. We progressively work to protect our nation's national security. I think it's important for Nebraska to join in that effort, and this legislation would help us do that. One historical note: You probably know this already, but Nebraska has been a leader in divestment in the past. So this is not the first time that we have had an opportunity to do something like this. Senator Chambers, way back in 1980, led Nebraska to be the first nation to withdraw financial investments from apartheid South Africa, and that was the beginning of the worldwide effort that led to the change of government in that country. Maybe we can be a part of another effort with this legislation. Thank you. [LB77]

SENATOR NORDQUIST: Thank you. Thank you, Senator Avery. Senator Mello. [LB77]

SENATOR MELLO: Thank you, Chairman Nordquist. And thank you, Senator Avery. I

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preface my comments with...and maybe it's questions that I need to probably ask the Investment Council when they come up and testify, as much as anything else. I generally...obviously am supportive of divestment legislation that you've brought before this committee in regard to Sudan divestment issues. And no doubt, I imagine there are other, no doubt, foreign countries in the future that may also need to follow a similar divestment strategy for this state. The question, though, is--in your feedback...and once again it's something I'll ask, no doubt, the Attorney General's Office, if they testify, and the Investment Council--is the precedent that we'd be setting with language in this bill. Where the current statute...you mention it on reference: Statute 72-1239.01, the language about, "No assets of the retirement systems or the Nebraska educational savings plan trust shall be invested or reinvested if the sole or primary investment objective is for economic development or social purposes or objectives." I understand the language caveat that was in the bill, in your bill. The question I have is, should that be essentially the new precedent we set as a committee and as a Legislature for all future, I would say, investment or divestment legislation, whether it's economic development-related and/or social purpose-related, is to give the Investment Council, essentially, that authority to override the policies that are put forward in statute in certain investment or divestment legislation? [LB77]

SENATOR AVERY: I think the Investment Council ought not to be able to make their own policy independent of the will of the Legislature. So I'd be reluctant to give them blanket authority to override. I do, however, recognize that there are many, many ways that the Investment Council can invest public money and do quite well. I remember when my own retirement fund, from the university, went through a period when there was great discussion about, why is it that we can't have a socially responsible investment alternative? And TIAA-CREF, the investment fund, said, well, because it would actually punish our shareholders because we'd earn less money. Well, finally the pressure became so heavy that they did open up a socially responsible investment fund. It outperformed the rest of the funds. So, you know, a lot of what we think we know about how investments might perform...maybe we don't know as much as we think. So I doubt that we have to invest in these areas where human rights abuses are rampant and where we have unlawful behavior, such as Iran, where Iran is seeking to have weapons of mass destruction. I mean, this case we know about. This is not Iraq. We know about this one. And it seems to me that there is no reason why we need to be investing state money in those areas. I have been a long proponent of divestment in some of those areas. Sudan you mentioned; I appreciate the fact that you remembered that and brought it up. [LB77]

SENATOR MELLO: I...well, I, Senator Avery, I appreciate your comments. I would agree with you on...with your feedback and your general principles and views on the issue, as well as the bill. It's something that, depending upon what the committee chooses to do, the underlying issue is less, I think, about the divestment but more, I think, possibly the precedent we'd be setting moving forward, which...I personally am

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okay setting a different precedent; as the committee knows, I've brought issues up before on this issue. So I appreciate it. [LB77]

SENATOR AVERY: I've always been mystified by the Investment Council's resistance to legislation of this kind, as if they don't have the means to find other ways to invest the money. Of course, they do. And they're smart enough to make good decisions and still have a good return on the investment. And I used that example of TIAA-CREF because they were so sure that all those fuzzy-headed professors back there that wanted to do the socially responsible investment would be a disaster. And they're still outperforming the rest of the portfolios. [LB77]

SENATOR MELLO: Hmm. [LB77]

SENATOR NORDQUIST: Hmm. Thank you, Senator Avery. Any additional questions? Seeing none, thank you. [LB77]

SENATOR AVERY: Thank you. [LB77]

SENATOR NORDQUIST: We'll take proponent testimony. [LB77]

DAVE LOPEZ: Good afternoon, Chairman Nordquist, members of the committee. My name is Dave Lopez, D-a-v-e L-o-p-e-z. I am an assistant attorney general with the Nebraska Department of Justice. I offer my testimony today in support of LB77 on behalf of Attorney General Bruning. Our office partnered with Senator Avery to design a bill that would protect Nebraska's public funds from being invested in companies with links to Iran. At a time when investment decisions are made on a global scale and when our troops, allies, and national security interests are under increased threat from an Iranian regime which actively funds terrorist activities and disregards human rights, it's more important than ever to be part of a collective effort to increase the economic pressure on Iran. As Senator Avery mentioned, LB77 would place Nebraska among the ranks of 23 states plus the District of Columbia and the federal government which have enacted either policies or statutes of divesting public funds from companies which do business in Iran. Such state sanctions are expressly authorized in federal law under the Comprehensive Iran Sanctions, Accountability, and Divestment Act, which was originally passed in 1996 and was reauthorized with overwhelming bipartisan support in Congress and signed into law by President Obama in 2010. LB77 is fairly straightforward from an administrative standpoint. It would require our office, the Attorney General's Office, to assemble a list of "scrutinized companies" on an annual basis. The state investment officer is not required to divest any current holdings but would be required to not add to those holdings going forward, with regard to any companies that are on the comprehensive scrutinized companies list. As Senator Avery mentioned, this was a major compromise with the SIO in terms of adding in a mechanism by which they can override a noninvestment decision if it would result in a

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breach of their fiduciary duties to plan-holders. So there is ample room for the SIO to continue to embark upon their fiduciary duties with regard to plan participants. The Divestment Act only applies to direct holdings; it doesn't apply to indirect holdings. But with regard to indirect holdings, the Attorney General's Office would send a policy statement letter to the managers of each of those holdings on an annual basis basically stating the policy of the Legislature and encouraging them to, as much as possible, avoid holdings in companies which we would ordinarily prohibit through the direct holdings prohibition. Finally, given that the SIO is not mandated to actually divest any current holdings, and given the Attorney General's preparation to absorb the administrative costs of assembling the scrutinized companies list, this bill carries a fiscal impact of zero, which is always nice. In conclusion, I would only add that LB77 is consistent with the tradition here in Nebraska to ensure our public funds do not subsidize human rights abuses worldwide. As Senator Avery mentioned, I'll mention again: in the '80s and with the leadership of Senator Chambers, this state became one of the first in the country to pass legislation to divest firms doing business in apartheid South Africa. So it's with that spirit of global awareness and moral imperative that we would urge this committee's support of LB77. And I'm happy to answer any questions. [LB77]

SENATOR NORDQUIST: Thank you, Dave. Questions? Senator Mello. [LB77]

SENATOR MELLO: Thank you, Chairman Nordquist. And thank you, Mr. Lopez, for your testimony. And it's the same question I asked Senator Avery. And I'll ask the same thing to Mr. States. This is a new precedent that essentially is going to be set if we move forward on LB77, which...I know, as I mentioned before, I was supportive of Senator Avery's previous bill to divest in regard...divestment activities in regard to Sudan, but in part it ran counter to the statute I read earlier that said we shouldn't...the SIO should not be doing any investments in regard for economic development or social objectives. Is the Attorney General's Office comfortable in future endeavors providing a zero fiscal note when other divestment bills come forward that mirror this language, that mirror this model? The Attorney General's Office feels comfortable in following through very similar policies in regard to being able to do this kind of workload for other countries that we may choose to no longer invest in in the future? [LB77]

DAVE LOPEZ: Well, that's an important question, and I think that depends on the situational aspects of future targets of divestment. If there's one advantage with Iran to being somewhat late to the party, there's already a very mature universe of information out there coming from institutions, other governments, academic institutions, NGOs that have already pursued divestment legislation. So it's somewhat easier for us to piggyback on that wealth of knowledge that's already out there. So from the standpoint of whether we would be comfortable doing it going forward, that would entirely depend on future legislation. With regard to the precedent, it's the kind of thing that absolutely does set a precedent. I mean, you are running counter to what should be the general

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base commitment, that the SIO's goal is to maximize returns for plan participants. But I think that has to yield to a principle that the Legislature is to be trusted to determine when there are policy imperatives to direct the investment of those funds. And I think, you know, it's tough to develop a mechanical or arbitrary threshold at when it's important enough. This is one of those things. So... [LB77]

SENATOR MELLO: I guess...and maybe it's something that we could follow up with Senator Avery's office afterwards as well as the Attorney General's Office. The concern I have, generally, is...for an example, I would want Senator Avery to bring back his Sudan divestment bill, because I know other states, multiple states, have passed similar legislation that Senator Avery has introduced in front of this committee before. So my question...and it's...please, please accept this as not a "we need an answer today in front of the hearing"; it's something that can go back to the Attorney General's Office and speak with your fiscal officers and the Attorney General himself to figure out how we could make this work moving forward. If we're going to set a precedent for LB77 and Iran, my thought would be, then, the Attorney General's Office would be able to do this for other divestment legislation bills, moving forward, assuming it follows a similar model, assuming that other states have followed, as they have with a divestment in Sudan, that they have lists created of other companies and direct holdings as well that they've divested in and have no longer done investment in. And I imagine there are other countries as well that state governments have also chosen to divest in future...or divest and/or not invest in future holdings, direct holdings, in relation to other foreign countries that have violated human rights, sanctions, that Iran and Sudan has. It's more of that precedent issue I'm asking, in the sense of a fiscal question, that if the Attorney General's Office is willing to do this for Iran, are they willing to do it for Sudan? Are they willing to do it for other countries which the United States may have sanctions against as well, in regard to encouraging state governments to divest their retirement assets in, for future pieces of legislation? It's something that if you can't give an answer today, it is an answer I would like prior to us being able to take action on this, because I think it sets the precedent where...I don't want to single out Senator Avery's previous bill, but I think there's...it really does set the precedent. We should be revisiting his prior bill as well as other issues that move forward, as, no doubt, the...our global, international relations do change on a moment's notice. And this could be something this committee takes up next year in relation to another country, and the year after that another country. So I would encourage the Attorney General's Office to provide, I think, a little bit more feedback on the precedent they're willing to set in regard to staff time and fiscal awareness to move forward on this policy. [LB77]

DAVE LOPEZ: Sure. Absolutely. [LB77]

SENATOR MELLO: Thank you. [LB77]

SENATOR NORDQUIST: Thank you. Senator Conrad. [LB77]

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SENATOR CONRAD: Mr. Lopez, thank you so much; your testimony was excellent. I have two questions. One is, based upon your research in examining how other states have approached this issue, sometimes it's helpful when we're kind of in this academic kind of discussion about the policy before us, if you...could you provide a concrete example of a company that has been subject to this kind of divestment in other jurisdictions, if you know. [LB77]

DAVE LOPEZ: I wouldn't want to single out individual companies. There have been, I mean, it...divestment legislation like this is effective in two ways. It works from the economic standpoint: that when you have a critical mass of institutions and public entities that begin to pull money out of them, it becomes an economic decision as to whether they will continue the behavior that put them there in the first place; and also from kind of a public shaming standpoint. We haven't done an extensive audit of what companies might already be in our portfolio. That's how other states' statutes have worked, from a mechanical standpoint. I wouldn't necessarily want to explore, since we haven't done that research yet, what companies could... [LB77]

SENATOR CONRAD: Sure. [LB77]

DAVE LOPEZ: ...be subject to prospective noninvestment. [LB77]

SENATOR CONRAD: Okay. Very good. And then my final question relates to Section 6 of the legislation, which discusses the provision related to the council's other fiduciary responsibilities and duties. And I understand, through the course of the hearing today, that that language has been kind of negotiated by your office, Senator Avery, and others involved in this issue to address some of the concerns that have been brought forward previously. But I'm worried, in reading it, it really seems to remove all of the teeth to this legislation, in my opinion. And I appreciate that compromise is part of the political process. But, in essence, to me, then, this legislation, with that section as currently written, is really a resolution; it's really a suggestion, because it allows a very broad grant of authority to the council to otherwise determine what their fiduciary duty would be. And if they're always going to be able to maximize returns by investing in companies that have these kinds of conflicts, are we really doing anything, are we...other than maybe just putting forward legislative intent that we'd hope they don't do business with these kinds of companies? So if you'd like...I know that's kind of a long statement, but if you'd like to just discuss that section and that language in particular, I'm really struggling with that. [LB77]

DAVE LOPEZ: Well...and obviously that section was included to ensure...I mean, at the end of the day, the purpose of the SIO, the purpose of the Nebraska Investment Council, is to provide a maximum return for retirement plan participants. [LB77]

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SENATOR CONRAD: Right. Yes. [LB77]

DAVE LOPEZ: And we wanted to ensure that if a remarkable situation arose where there might be a conflict and it was truly going to be a massive fiduciary breach for them--which we wouldn't...I mean, I would imagine that that would be fairly rare--that they would have a mechanism to protect their obligations to their stakeholders. That said, the federal legislation that actually authorizes all of the state divestment acts... [LB77]

SENATOR CONRAD: Um-hum. [LB77]

DAVE LOPEZ: ...specifically states that divestment of these kinds of scrutinized companies doing business in Iran would not result in a fiduciary breach with regard to ERISA... [LB77]

SENATOR CONRAD: Right. [LB77]

DAVE LOPEZ: ...obligations and the like. So I...it doesn't set a black-and-white requirement, but I suppose you can imagine the scenario whereby we would have a company on the list, and so, you know...it would be difficult to imagine a scenario whereby the SIO would not actually see it as a fiduciary responsibility to ensure that that company was not added to... [LB77]

SENATOR CONRAD: Um-hum. [LB77]

DAVE LOPEZ: ...in terms of our holdings... [LB77]

SENATOR CONRAD: Um-hum. [LB77]

DAVE LOPEZ: ...so... [LB77]

SENATOR CONRAD: Okay. And I'm hopeful that if the committee decides to move forward on this legislation, we could continue the dialogue about the technical aspects of that language. [LB77]

DAVE LOPEZ: Absolutely. [LB77]

SENATOR CONRAD: But, in your opinion, if, for example, we were to set this as the policy of the state, include it in state law, would it be an abrogation of anyone's fiduciary duty if they're simply following state law, even if that means a loss of potential income from the investment decision? [LB77]

DAVE LOPEZ: No. And I think Section 11... [LB77]

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SENATOR CONRAD: Right. [LB77]

DAVE LOPEZ: ...which is the other piece of this bill that touches on the fiduciary obligations. They kind of work to complement each other. [LB77]

SENATOR CONRAD: Yes. [LB77]

DAVE LOPEZ: Section 11 specifically states that it would not be a fiduciary breach, any action that was taken in pursuant of LB77. So, I mean, even without Section 6, you could still argue that their fiduciary obligations are protected. [LB77]

SENATOR CONRAD: Right. And, again, I appreciate that compromise is part of the process and to address legitimate issues that have been brought forward by people on all sides of this issue. But I'm worried that it does provide enough wiggle room for that rare instance that...that may exist where we're saying, gosh, we believe that this is good policy except for that rare case where the return is just too good. And I think that just really undermines the intent of the legislation. So I look forward to working with you and Senator Avery in regard to that issue. Thank you... [LB77]

DAVE LOPEZ: Absolutely. [LB77]

SENATOR CONRAD: Thank you very much. [LB77]

DAVE LOPEZ: Thank you. [LB77]

SENATOR NORDQUIST: Thank you. Senator Davis has a question. [LB77]

SENATOR DAVIS: Just a...one question that...if you can elaborate for me. You talked about direct holdings and indirect holdings; can you tell me what you mean by those phrases? [LB77]

DAVE LOPEZ: So an indirect holding would be, like, an index fund that the investment officer acquires an interest in. So, you know, it's a vehicle that then, you know, invests in, say, 1,000 other different companies. It becomes, as you get deeper into...down the layers of investment layers, you wind up creating something that you can't really track. So we wanted to...not to mention, according to our conversations with the SIO, about three-quarters of the funds that are implicated by this act are indirect, and the remaining quarter is direct. So you have a smaller universe, relative to the full portfolio, that are direct holdings. So just to take a random stock out of the blue: Ford Motor Company. If they acquired just, you know, 1,000 shares of Ford Motor Company, that would be a direct holding that would be subject to the requirements of this act. [LB77]

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SENATOR DAVIS: Okay, so I'll just use as my example Berkshire Hathaway, which I know doesn't have any (inaudible) investment there. But Berkshire owns Burlington Northern. So now if Burlington Northern is doing business in Iran, are they going to...will Berkshire stock then be subject to this? [LB77]

DAVE LOPEZ: That would depend on whether they have a revenue stream from Iran that is greater than 10 percent...that would meet the "scrutinized company" definition. [LB77]

SENATOR DAVIS: I mean, the intent is good. I just wonder, when you start parsing it out, how far out into the weeds you're going to get. [LB77]

DAVE LOPEZ: And...not that far. I mean, it becomes almost administratively impossible. And I know there's an organization that will be testifying in support sometime after me that does...that kind of specializes in this kind of...in Iran divestment legislation, and I'm sure he can speak to that. But as far as this legislation would go, we're really talking about top-line, direct holdings in a parent company. [LB77]

SENATOR DAVIS: So do you see...let's say Senator Conrad had some concerns with something that was going on in Saudi Arabia, for example, and she brought a Saudi Arabia divestment act; do you see yourself having to take a position on that? [LB77]

DAVE LOPEZ: Well, and like I said in response to Senator Mello, I think that's situational in terms of the fiscal impact. It's...the structure that we've designed here, I think, could be applied to virtually any kind of divestment legislation. So the framework would work anywhere. As far as the fiscal question would go, it's not that I'm trying to be coy about whether we would support it against another country; it's just we...there's not a guarantee that the information that's available with regard to Iran would be available with regard to another country such that the process of developing the scrutinized companies list would be as low-effort as it is with Iran. [LB77]

SENATOR DAVIS: Which is why I asked that question, you know. I'm just wondering if...and supposing Senator Mello decided we wanted to do something to divest ourselves from sugar-producing...soda companies. You know, this is where you kind of can get wandering off the course of what a well-intentioned bill you've got here, and you can really get sidetracked, which concerns me. [LB77]

DAVE LOPEZ: Sure. And that's understandable in light of what the chief principle of the SIO would be. Our position is simply that with regard to determining when it's a good idea to have a policy of divestment, whatever that threshold is, divesting from Iran is above it. And that's obviously...that...there's no other answer than that has to be a decision that's made on a case-by-case basis by the Legislature. [LB77]

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SENATOR DAVIS: Okay. Thank you. [LB77]

SENATOR NORDQUIST: Thank you. Any additional questions? Seeing none, thank you. [LB77]

DAVE LOPEZ: Thank you. [LB77]

SENATOR NORDQUIST: All right. We have the room for about ten minutes. So for the additional testifiers, we'll go ahead. Additional proponent testimony. Welcome, Alan. Thank you. [LB77]

ALAN POTASH: (Exhibit 6) Good afternoon. Thank you for all you do for Nebraska. I'm Alan Potash, A-l-a-n P-o-t-a-s-h. I'm a regional director for the Anti-Defamation League, Plains States Region. The Anti-Defamation League was founded in 1913 with a mandate to fight defamation of the Jewish people and to secure fair treatment for all. Today the ADL is one of the country's leading civil rights and human services organizations combating anti-Semitism and bigotry of all kinds. The Plains States Region covers Nebraska, Iowa, and Kansas, and I'm based out of Omaha. We submit this testimony today to express our strong support for LB77 to adopt the Nebraska Iran Divestment Act. The ADL generally has reservations about boycotts and divestment campaigns, given the fact that the Jewish people and the state of Israel have long been targets of such initiatives. However, in extraordinary circumstances such as this, we support this type of campaign. We believe that Iran, through its nuclear weapons program, extremism, and state sponsorship of terrorism, is a grave threat not only to the United States but to the rest of the world as well. Additionally, the anti-Semitic and anti-Israel sentiments expressed by Iranian President Ahmadinejad have placed him and his regime among the foremost threats to Jews in Israel. Consequently we believe the circumstances justify this divestment effort against Iran. Iran has repeatedly rebuffed international efforts to ascertain the extent and purposes of its nuclear program by stonewalling the International Atomic Energy Agency, rejecting a series of United Nations Security Council resolutions ordering it to suspend its uranium-enrichment program. A nuclear-armed Iran poses a threat to America's closest allies in the Middle East. Israel is most at risk, as Iran's leaders have reportedly declared that Israel should be wiped off the map. America's Arab allies, such as Saudi Arabia, Egypt, the United Arab Emirates, Bahrain, are already alarmed at Iran's aggressive regional policy and would feel increasingly threatened by a nuclear-armed Iran. A nuclear-armed Iran would likely embolden Iran's already aggressive foreign policy, resulting in greater confrontations with the international community, and support the extremists. Iran's nuclear program would likely spark a nuclear arms race in the Middle East that would further destabilize the volatile and vital region. Such a development would dramatically affect America's interest. LB77 sends a strong message that Nebraska does not endorse regimes that will not cooperate with the international community's efforts to reduce nuclear threats and that sanction state-sponsored terrorism. Furthermore, LB77

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protects state investments, and Nebraskans can feel secure knowing that their investment portfolios are safe. And that's why we support LB77. [LB77]

SENATOR NORDQUIST: Thank you, Alan. [LB77]

ALAN POTASH: The lighting in here isn't so good for people with bad eyes. [LB77]

SENATOR NORDQUIST: Yeah, I hear you. Any questions? Seeing none... [LB77]

ALAN POTASH: Thank you guys. [LB77]

SENATOR NORDQUIST: ...thank you. [LB77]

ALAN POTASH: Yep. [LB77]

SENATOR NORDQUIST: Any additional proponents? Welcome. [LB77]

DAVID IBSEN: Thank you very much, Mr. Chair and members of the committee. I know time is brief, so I will also be somewhat truncated in my comments. I'm happy to answer any questions that you may have, though. My name is David Ibsen, I-b-s-e-n. I represent a group called United against a Nuclear Iran, or UANI, which is a bipartisan advocacy group that was founded in 2008 specifically to raise awareness of the dangers posed by the Iranian regime. We're led by a advisory board of international and national figures including Jim Woolsey, Dennis Ross, Fouad Ajami, Meir Dagan, Irwin Cotler, Fran Townsend, and many, many others. And I'm here today to express my strong support for LB77 on behalf of those individuals and our entire group. And the reason is very, very simple. I think we've seen over the last couple of years that there's an ever-increasing sentiment that the very tremendous and unique threat posed by the Iranian regime cannot and should not be addressed merely by lawmakers in Washington, D.C., or diplomats at the United Nations alone, but that local communities, state communities, in Nebraska and elsewhere, have a strong role to play and can adopt strong measures to ensure that Iran feels consequences for its behavior. Certainly LB77 reflects that sentiment. As we all know, this legislation presents entities, firms, corporations with a very clear and distinct choice: you can do business with Iran or you can be eligible to receive lucrative investments from the people of the great state of Nebraska. In the course of our organization's work, we found that the specter of "debarment"...the specter of divestment is one of the most, if not the most, compelling means to force firms to end their Iran business. Just like the U.S. federal government, state governments collectively offer billions of dollars in prospective investment funds and procurement contracts every single year. No responsible corporation, profit-minded corporation, would jeopardize these potential lucrative sources of investment by doing business in Iran. As was noted by the previous testifiers, the federal government has explicitly authorized states to assist in the implementation of national policy in

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sanctioning Iran. And as a result, a number of other communities across the country have adopted similar or comparable either divestment- or procurement-related measures, many of them by, you know, with near-unanimous support. So LB77 will enable Nebraska to join this very select group of states. LB77 demonstrates that communities and states across the country do have a vital role to play, and, if passed, it will ensure that Nebraska is at the forefront of this vital effort to isolate Iran and, as I learned today from Senator Avery, will remain at the forefront of efforts, generally, to divest from countries that are engaged in nefarious actions across the world. So thank you very much. [LB77]

SENATOR NORDQUIST: Great. Thank you for your testimony. Any questions? Seeing none, thank you. [LB77]

DAVID IBSEN: Thanks. [LB77]

SENATOR NORDQUIST: Any additional proponent testimony? Thank you. Welcome. [LB77]

GARY JAVITCH: Hello, my name is Gary, G-a-r-y, Javitch, J-a-v-i-t-c-h, and I am testifying today in support of LB77. And I'd like to just begin with a parameter: I am not going to discuss the technical details; rather, I wanted to discuss my interest in this based on a personal interest as someone who has followed world, national, and local events. At the same time, I have been very active in a number of advocacy organizations, but I am not representing them today, speaking just as an individual. I wanted to support this bill because I believe that it is going to add to the worldwide pressure on Iran to halt...to force them to halt their march towards a nuclear capability that has the potential to threaten the entire world. And this threat comes in the form of not only economic but also political and social dislocation and with an opportunity to create chaos around the world. And Nebraska is not immune to any of this; and that, as a Nebraskan, I want to emphasize. This...the role that Iran plays in the world and could potentially further play in the world as a holder of a nuclear weapon can affect even Nebraskans. So besides...so I'd like to make three points. One...and I'll outline them... [LB77]

SENATOR NORDQUIST: Um-hum. [LB77]

GARY JAVITCH: ...in a little more detail in a bit. [LB77]

SENATOR NORDQUIST: Well, I need you to...we've only got about another minute or two... [LB77]

GARY JAVITCH: Okay. [LB77]

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SENATOR NORDQUIST: ...and I've got you to wrap up. [LB77]

GARY JAVITCH: Iran is a world threat. We need to engage them as Nebraskans, and we need to support the federal effort. Some people may think that Iran, thousands of miles away, cannot affect us. But Iran, through its proxies, terrorist organizations like Hezbollah and Hamas, can actually do that. Hezbollah, for example, has gone around the world, most recently in Bulgaria, and murdered Israeli citizens. They have, in Buenos Aires, Argentina, for example, in 1994 destroyed a community center. And you may not know this, but Omaha is going to be the home of a tri-faith campus: Jews, Muslims, Episcopalians. This is the perfect target for people who want to destroy the "Great Satan" and peace in America. And since I'm short of time, I want to say I think it's our moral obligation to support this. Despite some of your well-chosen reservations, we have to step forward; it's part of an entire U.S. effort. [LB77]

SENATOR NORDQUIST: Okay, great. [LB77]

GARY JAVITCH: Thank you very much. [LB77]

SENATOR NORDQUIST: Thank you. Any questions? Seeing none, thank you. Any additional proponents? Seeing none, any opponent testimony? Just so I know, are there any other testifiers on this bill, in opponent or neutral? Okay, Jeff will be our last, and Senator Avery has waived closing. Thanks, Jeff; welcome. [LB77]

JEFF STATES: (Exhibit 7) Mr. Chairman, members of the committee, my name is Jeff States; it's J-e-f S-t-a-t-e-s. And I am the state investment officer for the Nebraska Investment Council. I come here on behalf of myself as the state investment officer and the Investment Council to oppose LB77. I think you've heard discussed a number of the issues, but I do think the council feels, first of all, very fortunate that historically this legislative body...Legislature and the Governor's office have tended not to want to politicize our investment process so that the council can do what it's been appointed to do, which is to focus on producing the best investment return for the participants in the plans. And I specifically draw that back to the asset base that we're significantly talking about here, which are the state's retirement funds. We've kind of glossed over the issue about who is and what a fiduciary duty is. But the statute says...and it states, in part, that the council is to discharge their duties with respect to the assets of the retirement system and the Nebraska educational savings plan trust solely in the interest of the members and beneficiaries of the retirement system or the interests of the participants and beneficiaries of the Nebraska educational savings plan trust. That...and I don't want to get too involved in this issue, but nowhere does that say that interest is the social or political or economic interests of this legislative body or other special-interest groups that want to come before you. The council, for the retirement assets, is managing them for the benefit of the beneficiaries and participants in the trust. And you know, clearly, that the cost of those programs is an issue today. Our objective needs to be focused on

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trying to make sure that we achieve a good investment return. This one single event, and I'm sure there will be a question about it, won't greatly disrupt us, but we are concerned about the implications that it creates for precedents, for having to deal with many other special-interest groups and entities, all of which are very noble and just causes. I...we're not arguing over that. But it distracts us from performing the duty that the council is appointed to. The Investment Council members themselves are appointed to the council because of their financial expertise and their investment expertise; it's not expertise in trying to pick and choose, except from a financial perspective, what investments should or should not be participated in. So that's our primary objective. We do have some other, lesser issues. One is that as this bill takes the scrutinized list...and the AG would directly communicate with our investment managers to me...raises some issue with respect to who they're contracting with. Our contracts say that they only take direction from me or the council. How do they view a letter from the Attorney General saying that it's the state's policy...because they've contracted with us. And so it just creates some minor rifts there, anyway, with the potential as to who's managing the funds with respect to what you do. Finally, we think, quite honestly, that when these issues become attractive enough...or I shouldn't say attractive enough, but influential enough to affect the economics of a transaction, as Iran investments have, that those filter through our process and they do affect the bottom line, corporate profitability. And we don't invest in bad actors, because bad actors, over time, do not produce good returns, and our investment managers are aware of that. As it relates to the federal government's effort to regulate this, we think they're the perfect entity to do that: they should set foreign policy. I would say, from what I've observed over looking at the history of this, they have been effective in the last three or four years, through their sanction efforts, to, in fact, influence companies to further step away from any involvement or connection there, which makes the possibility of us having exposure pretty small in this issue. But we really think that that's where the expertise lies and that their influence and their actions should dictate how this issue is implemented. And we require our managers as well as ourselves to follow federal and state law and regulations, and so it's illegal for U.S. companies to invest. And so I will stop there if you...but we do have a strong concern about this, both from the implications of this as well as the longer-term implications. [LB77]

SENATOR NORDQUIST: All right. Jeff, I've got to... [LB77]

JEFF STATES: This has no fiscal impact, but in the future... [LB77]

SENATOR NORDQUIST: ...cut you... [LB77]

JEFF STATES: ...other actions might. I'm sorry. [LB77]

SENATOR NORDQUIST: Great. I have to cut you off here. We've got one quick question... [LB77]

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JEFF STATES: Sure. [LB77]

SENATOR NORDQUIST: ...and then we've got to get out of here because... [LB77]

SENATOR MELLO: And it's not even really a question, Jeff. I think part of it is it's just a timing thing, because I have to go to Appropriations Committee right now. The reality is I generally am supportive of this concept of what LB77 is trying to do, as we've explored it in other areas, as has Senator Avery introduced other bills. My question is, if there's a way to follow up with the committee in regard to the precedent that essentially gets set with the language they utilize giving you the authority to make...to essentially override certain direct investments. I know we can't do that right now because we have to go. I would like more information from the Investment Council, if possible, on that language, to see if...to understand what precedent would be set if the committee moves on this issue. [LB77]

JEFF STATES: And we'd...I mean, they put that language there at my request... [LB77]

SENATOR MELLO: Okay. [LB77]

JEFF STATES: ...so I'm happy to discuss it. [LB77]

SENATOR MELLO: Okay, thank you. [LB77]

SENATOR NORDQUIST: Thank you. Thank you. Thank you. And if we have any other questions, we'll follow up with you, Jeff, no problem. That concludes our hearing today. Thank you all for attending. [LB77]