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TEACHERS RETIREMENT SYSTEM
EMPLOYEES' RETIREMENT SYSTEM

February 21, 2011

Elizabeth M. Murphy, Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: Comments on Securities and Exchange Commission Release No. 34-63576; File No. S7-45-10

Ladies and Gentlemen:

Thank you for the opportunity to comment on the Proposed Rules entitled *Registration of Municipal Advisors* (SEC Release No. 34-63576; File No. S7-45-10) (the "Proposed Rules"). I am writing on behalf of the Employees' Retirement System of Georgia ("ERS") and the Teachers Retirement System of Georgia ("TRS") (together, the "Retirement Systems") to express concern with the overly broad proposed definition of "investment strategies" and with the application of the Proposed Rules to individuals who are appointed rather than elected to municipal boards. The Commission's proposed definition of "investment strategies" would require board members of the Retirement Systems to register as Municipal Advisors despite the fact that these board members have a fiduciary duty to the Retirement Systems and the pensions they oversee are not funded by the issuance of municipal securities. We believe the Proposed Rules exceed the authority granted by the statute and interfere with a State's power of appointment. As a practical matter, we believe it will discourage individuals from serving on these and similar boards.

Description of the Retirement Systems:

A brief overview of the Retirement Systems may assist the Commission in understanding how the Proposed Rules impact the Retirement Systems and why appointed Board members should not be required to register as Municipal Advisors.

The Retirement Systems were created by statute in the State of Georgia. Both TRS and ERS possess "the powers and privileges of a public corporation" under Georgia law.[1] As such, they possess the power to sue and be sued.[2]

TRS was established for the purpose of providing retirement allowances and other benefits for teachers of this state.[3] TRS is a vehicle for collecting employee and employer contributions, investing accumulated funds, and disbursing retirement benefits to members and beneficiaries. ERS was established for the purpose of providing retirement allowances and other benefits for employees of the state and political subdivisions thereof.[4] Neither TRS nor ERS fund their respective pension obligations through the issuance of municipal financial products or municipal securities.

As required by Georgia law, the system is examined on an annual basis by an independent actuarial firm that specializes in pension and retirement plans. The firm prepares a yearly valuation on the contingent assets and liabilities of the system, thus revealing its ability to meet future obligations. In addition, an independent accounting firm audits the system annually.

Administration of the Retirement Systems is ultimately the responsibility of their respective Boards of Trustees, while daily management of system operations is the responsibility of the executive director. The relevant provisions of the Georgia Code describe in detail the qualifications of a person who can serve in each board seat as well as how they will be nominated, elected or appointed.[5]

The TRS Board consists of 10 members as follows:

- State Auditor, ex officio appointed by the General Assembly
- State Treasurer, ex officio appointed by State Depository Board
- Two classroom teachers (both active members of TRS) appointed by the Governor
- One school administrator (an active member of TRS) appointed by the Governor

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[1] Teachers Retirement Sys. v. City of Atlanta, 249 Ga. 196-197, 288 S.E.2d 200 (1982); Arneson v. Board of Trustees of the Employees' Retirement Sys., 259 Ga. 579, 385 S.E.2d 651 (1987).
[2] O.C.G.A. §47-3-20.
[3] O.C.G.A. §47-3-21.
[4] O.C.G.A. §47-2-20.
[5] O.C.G.A. §47-2-21 and §47-3-21.

- One Board of Regents employee (an active member of TRS) appointed by the Board of Regents
- One trustee appointed by the Governor who must be an active member of TRS
- One trustee appointed by the Governor
- One retired member of TRS elected by the trustees
- One citizen (not a TRS member) experienced in the investment of money elected by the trustee board members who are not ex officio to serve a 3-year term.

The board convenes bi-monthly to review investment performance, retirement statistics, the system budget, and various other issues. The Trustees are generally paid a per diem expense allowance set by the General Assembly for attending meetings of the Board of Trustees, but are otherwise not compensated.

The Retirement Systems' investments are managed internally by the Division of Investment Services of TRS and by one or more independent professional investment managers registered with the SEC. The Division of Investment Services handles day-to-day investment transactions.[6] Six members of the TRS Board of Trustees along with the executive director comprise the Investment Committee. Committee members convene with the directors of the Investment Services Division and hear recommendations from outside investment advisors at monthly meetings. Georgia law strictly defines the type of investments that the Retirement Systems are authorized to make.[7] Investment recommendations made by the committee require approval by the entire board.

The composition of the ERS Board and the duties and responsibilities of the Trustees generally mirror those of the TRS Board.[8] Significantly, the Trustees of both entities have a fiduciary duty to that retirement system. In fact, each Retirement System Trustee is required to take an oath upon appointment that "he will diligently and honestly administer the affairs of the Board of Trustees which have been entrusted to him and that he will not knowingly violate or willingly permit to be violated any law applicable to the retirement system."[9] The existence of this fiduciary duty is significant because the Commission's proposed regulation of appointed Board members is premised on the mistaken notion that appointed members are not accountable for the performance to the citizens of the municipal entities.[10]

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[6] The investment division of TRS provides these same services to ERS through an intergovernmental contract.

[7] O.C.G.A. §47-20-83.1

[8] O.C.G.A. §47-2-21(b)

[9] O.C.G.A §47-2-21(e) and §47-3-21(d); *see also*, O.C.G.A §53-12-3.

[10] Proposed Rules at p. 41 ("The Commission does not believe that appointed members of a governing body of a municipal entity that are not elected ex officio members should be excluded from the definition of a 'municipal advisor.' . . . [T]he Commission is concerned that appointed members, unlike elected officials and elected ex officio members, are not directly accountable for their performance to the citizens of the municipal entity.")

Definition of Investment Strategies

Based on our review of the Proposed Rules, it appears that the Commission's registration requirements would apply to appointed members of the Retirement Systems solely as a result of the Commission expanding the definition of "investment strategies" in 15B(e)(5) to the point where it is divorced from "municipal financial products" or the "issuance of municipal securities" which are necessary prerequisites under the statute to the obligation to register as a municipal advisor.

Specifically, Section 975 of Title IX of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank") amended Section 15B of the Securities Exchange Act of 1934 (as amended, the "Exchange Act") to require municipal advisors to register as such with the Securities and Exchange Commission (the "Commission" or the "SEC"). Section 15B(e)(4)(A) of the Exchange Act, as amended by the Dodd-Frank Act, defines the term "municipal advisor" to mean

> "a person (who is not a municipal entity or an employee of a municipal entity) (i) that provides advice to or on behalf of a municipal entity or obligated person *with respect to municipal financial products or the issuance of municipal securities*, including advice with respect to the structure, timing, terms, and other similar matters concerning such financial products or issues, or (ii) undertakes a solicitation of a municipal entity." (emphasis added).

Section 15B(e)(5) provides that the term "municipal financial product" means:

> "municipal derivatives, guaranteed investment contracts, and investment strategies."

Exchange Act Section 15B(e)(3) provides that "the term 'investment strategies' includes:

> "plans or programs *for the investment of the proceeds of municipal securities* that are not municipal derivatives, guaranteed investment contracts, and the *recommendation of and brokerage of municipal escrow investments*." (emphasis added).

Given the context within the definition, it appears likely that Congress intended "municipal escrow investments" to be limited to accounts holding the proceeds of municipal securities pending deployment. The Proposed Rules expand upon Dodd-Frank's directive and state "[t]he Commission believes it was Congress' intent to include in the definition of "municipal advisor" persons that provide advice with respect to plans, programs or pools of assets that invest funds held by, or on behalf of, a municipal entity, such as a 529 college savings plan, LGIP or public pension plan."[11] Although the Proposed Rules state that this interpretation follows from the definition municipal entity,

[11] Proposed Rules at p. 22.

the only way to arrive at this conclusion is by 'reading out' the "with respect to" in the first part of the definition of municipal advisor. We believe this expansive interpretation goes beyond Congress' clear intent. Congress provided a limited definition which specifically references the issuance of and the investment of the proceeds of municipal securities and the recommendation of and brokerage of municipal escrow investments.

Legislative intent is of particular importance in this circumstance where, with Dodd-Frank, Congress was dramatically increasing the SEC's authority to regulate those who interact with municipalities. As the Proposed Rules acknowledge, prior to the 1970s, municipal advisors were largely unregulated by the SEC. This was due to an express concern regarding "any constitutional difficulties that might arise with reference to the inclusion of State and municipal obligations. . . "[12] The amendments in 1975 were due to concerns regarding sales practices by broker dealers, not due to any concern that investors needed protection from municipal entities or that municipalities needed the federal government to protect them.[13] Congress has taken a cautious approach to regulation at the State level. Although Dodd-Frank has expanded the SEC's reach over municipal activities, we believe the Commission's interpretation goes far beyond Congress' intent and encroaches upon areas still left with the municipalities.

Definition of Municipal Advisor Should Exclude Both Elected and Appointed Members of Governing Entities

Under the Exchange Act, the term "municipal advisor" excludes employees of a municipal entity. In the Proposed Rules, the SEC wisely proposes to extend this exclusion to elected and appointed and elected *ex officio* members of a governing body of a municipal entity. It does not go so far as to extend this exclusion to appointed members of the same board. We believe that this distinction between elected and appointed members of municipal boards is artificial at best, may be unconstitutional and would be harmful to the effective operation of municipal boards if adopted.

The Distinction is Artificial

We believe that Congress intended to include officers and directors of a governing entity in the exclusion it provided by referencing municipal entity or employee of a municipal entity. Although board members are not technically employees, it seems clear that Congress recognized that a municipal entity should not be subject to registration provisions as a municipal advisor when it advises itself. Because an entity necessarily acts through natural persons or groups of natural persons, we believe the reference to

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[12] 78 Cong. Rec. 8669 (1934); H.R. Rep. No. 1838, 73d Cong., 2d Session. (1934) (discussing the exemptions for municipal securities from the Securities Act of 1933).

[13] Statement of Mr. Williams: Statements on Introduced Bills and Joint Resolutions"The Municipal Securities Act of 1973" S.2474 Federal Securities Law Legislative History 1933-1982, Volume II, page 2408.

employees includes individuals when they could be said to be acting for the entity, and not merely providing third party services to the entity.

As a general rule, board members of a municipal entity have the same fiduciary duties regardless of whether they were appointed or elected to serve. The relevant sections of the Georgia Code creating ERS and TRS were not enacted in derogation of the principles of common law pertaining to fiduciary duties of trustees in any relevant respect. This is evidenced by the fact that each board member (known as a trustee) shall (without respect to whether that trustee was elected or appointed), "within ten days after his appointment or election, take an oath of office that so far as it devolves upon him he will diligently and honestly administer the affairs of the board of trustees and that he will not knowingly violate or willingly permit to be violated any laws applicable to the retirement system." Additionally, the board members are subject to the same rules of ethics and can be removed in the same manner as the elected members[14].

The Distinction May be Unconstitutional

A strong argument can be made that the proposed regulatory scheme infringes on the sovereignty of the State of Georgia by infringing on the appointment power of state and local elected officials. This is particularly the case insofar as the regulatory scheme limits the power of state and local officials to govern with respect to expenditures of public funds, a power that is specifically granted to the state legislature under the Georgia Constitution.[15] Specifically, the SEC's proposed actions arguably run afoul of the Tenth Amendment as the Supreme Court has interpreted it in the cases of *New York v. United States*, 505 U.S. 144 (1992) and *Printz v. United States*, 521 U.S. 898 (1997).

The gravamen of the possible constitutional objection to the regulations is that, while the federal government does possess great powers to regulate based on its Commerce Clause authority, it may not compel a state to adopt particular legislation or compel state officials to administer a federal program. In this case, the proposed regulations would effectively amend Georgia law and create new limitations on the required qualifications for those who sit on municipal boards. The federal government may encourage states to take particular actions, but it must always leave the states the ability to refuse, even though such refusal might lead to a loss of federal funds or to preemptive federal legislation. This distinction is well described in *New York* by Justice O'Connor:

> First, under Congress' spending power, "Congress may attach conditions on the receipt of federal funds." Such conditions must (among other requirements) bear some relationship to the purpose of the federal spending; otherwise, of course, the spending power could render academic the Constitution's other grants and limits of federal authority. Where the

[14] O.C.G.A. §§47-2-21 and 47-3-21.
[15] *See* GA. CONST. art. III, § I, para. I; GA. CONST. art. III, § X, para. I, IV.

recipient of federal funds is a State, as is not unusual today, the conditions attached to the funds by Congress may influence a State's legislative choices. [*South Dakota v.*] *Dole* was one such case: The Court found no constitutional flaw in a federal statute directing the Secretary of Transportation to withhold federal highway funds from States failing to adopt Congress' choice of a minimum drinking age. Similar examples abound.

Second, where Congress has the authority to regulate private activity under the Commerce Clause, we have recognized Congress' power to offer States the choice of regulating that activity according to federal standards or having state law pre-empted by federal regulation. This arrangement, which has been termed "a program of cooperative federalism," is replicated in numerous federal statutory schemes. These include the Clean Water Act; the Occupational Safety and Health Act of 1970; the Resource Conservation and Recovery Act of 1976; and the Alaska National Interest Lands Conservation Act.

By either of these methods, as by any other permissible method of encouraging a State to conform to federal policy choices, the residents of the State retain the ultimate decision as to whether or not the State will comply. If a State's citizens view federal policy as sufficiently contrary to local interests, they may elect to decline a federal grant. If state residents would prefer their government to devote its attention and resources to problems other than those deemed important by Congress, they may choose to have the Federal Government rather than the State bear the expense of a federally mandated regulatory program, and they may continue to supplement that program to the extent state law is not pre-empted. Where Congress encourages state regulation rather than compelling it, state governments remain responsive to the local electorate's preferences; state officials remain accountable to the people

By contrast, where the Federal Government compels States to regulate, the accountability of both state and federal officials is diminished. If the citizens of New York, for example, do not consider that making provision for the disposal of radioactive waste is in their best interest, they may elect state officials who share their view. That view can always be pre-empted under the Supremacy Clause if is contrary to the national view, but in such a case it is the Federal Government that makes the decision in full view of the public, and it will be federal officials that suffer the consequences if the decision turns out to be detrimental or unpopular. But where the Federal Government directs the States to regulate, it may be state officials who will bear the brunt of public disapproval, while the federal officials who devised the regulatory program may remain insulated from the electoral ramifications of their decision. Accountability is thus diminished

> when, due to federal coercion, elected state officials cannot regulate in accordance with the views of the local electorate in matters not pre-empted by federal regulation.[16]

The final passage is particularly applicable here, given that the Commission's purported justifications include a "lack of accountability" by appointed Board members. *New York* makes clear that it is the federal government that lacks of accountability when it compels state action.

Moreover, the regulations at issue here do not appear to fall into one of the permissible categories of federal encouragement discussed in *New York*. Rather, the regulations, which would effectively amend state law with respect to appointments by implementing federal standards for Board members, appear more like a direct federal command to the State and local officials, which have been found unconstitutional.

While *New York* dealt with compelled legislation, *Printz* addressed the question of whether the federal government could compel state officials to administer a federal program without directing any state legislation. In particular, in *Printz*, the Court analyzed the issue of whether the Brady Law could compel local officials to run background checks on gun purchasers. The *Printz* Court determined such a law was beyond the constitutional authority of Congress. While the opinion is worthy of review, its holding alone makes the important point—the federal government may not compel state officials to administer a federal program:

> We held in *New York* that Congress cannot compel the States to enact or enforce a federal regulatory program. Today we hold that Congress cannot circumvent that prohibition by conscripting the State's officers directly. The Federal Government may neither issue directives requiring the States to address particular problems, nor command the States' officers, or those of their political subdivisions, to administer or enforce a federal regulatory program. It matters not whether policymaking is involved, and no case by case weighing of the burdens or benefits is necessary; such commands are fundamentally incompatible with our constitutional system of dual sovereignty.[17]

It seems clear that the proposed regulations are similar to *Printz* in that they effectively require state officials to administer a federal program controlling the local appointment of Board members. Thus, the issues of state sovereignty in general and the Tenth Amendment in particular, as implicated by the proposed regulatory scheme, are significant and could provide a basis for litigation challenging the proposed regulations should they go into effect as currently drafted.

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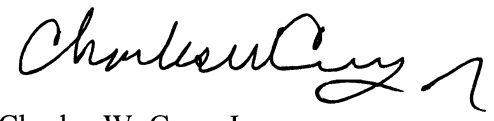
[16] 505 U.S. at 167-69 (internal citations omitted).
[17] 521 U.S. at 944.

The Distinction Would Impact the Ability to Find Qualified Board Members

The application of the Proposed Rules to appointed members of municipal boards would interfere with the sound operation of the retirement systems. Classroom teachers, school administrators, retirement system members, and other citizens who volunteer their time and abilities through service on the boards of trustees of ERS and TRS would be affected and burdened by the Proposed Rules. Imposing registration requirements, compliance with which would be costly and would require the disclosure of private information about individuals as a precondition to service on a municipal board, would greatly reduce the number of qualified individuals willing to accept an appointment on such a board. The very people whose participation would best serve the interests of the system members and their beneficiaries would be discouraged from service by the onerous requirements the Proposed Rules would impose on them. The extent of the potential chilling effect on board participation cannot be understated. The nonparticipation of these citizens would leave the appointing government officials little choice but to seek out financial industry professionals to serve, many of whom will have inherent conflicts of interest. Weakening in this manner the boards who administer state and local government core activities would appear to be contrary to the underlying principles behind Dodd-Frank.

We appreciate this opportunity to comment. We urge the SEC to reconsider its interpretations. If you have any questions concerning these comments or desire any additional information regarding the Retirement Systems, please contact the undersigned.

Sincerely,



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