

The Florida Senate
BILL ANALYSIS AND FISCAL IMPACT STATEMENT

(This document is based on the provisions contained in the legislation as of the latest date listed below.)

Prepared By: The Professional Staff of the Governmental Oversight and Accountability Committee

BILL: CS/SB 1144

INTRODUCER: Governmental Oversight and Accountability Committee and Senator Garcia

SUBJECT: State and Local Government Relations with Cuba or Syria

DATE: February 23, 2012 **REVISED:** _____

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	McKay	Roberts	GO	Fav/CS
2.			BC	
3.				
4.				
5.				
6.				

Please see Section VIII. for Additional Information:

A. COMMITTEE SUBSTITUTE..... Statement of Substantial Changes

B. AMENDMENTS..... Technical amendments were recommended

Amendments were recommended

Significant amendments were recommended

I. Summary:

This bill would prohibit the State Board of Administration from acting as a fiduciary with respect to voting on, or in favor of, any proxy resolution advocating expanded US trade with Cuba or Syria. The bill also prohibits agencies and local governments from having a contract for greater than \$1 million with any entity engaged in business operations in Cuba or Syria.

The bill amends sections 215.471 and 287.135 of the Florida Statutes.

II. Present Situation:

The State Board of Administration

The State Board of Administration (SBA) is created in Art. IV, s. 4 (e) of the State Constitution. Its members are the Governor, the Chief Financial Officer, and the Attorney General. The board derives its powers to oversee state funds from Art. XII, s. 9 of the State Constitution.

The SBA has responsibility for oversight of the Florida Retirement System (FRS) Pension Plan and the FRS Investment Plan, which represent approximately \$128 billion, or 86 percent, of the

\$149 billion in assets managed by the SBA, as of October 31, 2011. The Pension Plan is a defined benefit plan and the Investment Plan is a defined contribution plan that employees choose in lieu of the Pension Plan. The SBA also manages 33 other investment portfolios, with combined assets of \$21 billion, including the Florida Hurricane Catastrophe Fund (CAT Fund), the Florida Lottery Fund, the Florida Pre-Paid College Plan, and various debt-service accounts for state bond issues.¹

Divestiture from Cuba

Section 215.471, F.S., enacted in 1993, prohibits the SBA from investing in stocks, securities, or other obligations of:

- Any institution or company domiciled in the United States that does business of any kind with Cuba, in violation of federal law.
- Any institution or company domiciled outside of the United States if the President of the United States has applied sanctions against the foreign country in which the institution or company is domiciled, pursuant to s. 4 of the Cuban Democracy Act of 1992.

Section 215.472, F.S., prohibits each state agency from investing in:

- Any financial institution or company domiciled in the United States, or foreign subsidiary of a company domiciled in the United States, which directly or through a United States or foreign subsidiary, makes any loan, extends credit of any kind or character, advances funds in any manner, or purchases or trades any goods or services with Cuba, the government of Cuba, or any company doing business in or with Cuba in violation of federal law.
- Any financial institution or company domiciled outside of the United States if the President of the United States has applied sanctions against the foreign country in which the institution or company is domiciled pursuant to s. 4 of the Cuban Democracy Act of 1992.

According to information provided by staff of the SBA, in order to comply with this legislation, the Cuban Affairs Section at the U.S. State Department or the Treasury Department's Office of Foreign Assets Control (OFAC) are contacted periodically to confirm that no sanctions have been implemented. Since the Act's inception, sanctions have never been issued against any country.

The Protecting Florida's Investments Act

In 2007, the Legislature enacted² the Protecting Florida's Investments Act (PFIA). The PFIA requires the SBA, acting on behalf of the Florida Retirement System Trust Fund (FRSTF), to assemble and publish a list of "Scrutinized Companies" that have prohibited business operations in Sudan and Iran. Once placed on the list of Scrutinized Companies, the SBA and its investment managers are prohibited from acquiring those companies' securities and are required to divest those securities if the companies do not cease the prohibited activities or take certain

¹ State Board of Administration "Monthly Performance Report to the Trustees" as of October 31, 2011, issued November 30, 2011.

² Chapter 2007-88, L.O.F.; Senate Bill 2142.

compensating actions. The implementation of the PFIA by the SBA does not affect any FRSTF investments in U.S. companies; the PFIA affects foreign companies with certain business operations in Sudan and Iran involving the petroleum or energy sector, oil or mineral extraction, power production, or military support activities.

According to staff of the SBA, the PFIA imposes the following reporting, engagement, and investment requirements on the SBA, including:

- Quarterly reporting to the Board of Trustees of every equity security in which the SBA has invested for the quarter, along with its industry category. This report is posted on the SBA website.
- Quarterly presentation to the Trustees of a “Scrutinized Companies” list for both Sudan and Iran for their approval. Scrutinized Company lists are available on the SBA’s website, along with information on the FRSTF direct and indirect holdings of Scrutinized Companies.
- Written notice to external investment managers of all PFIA requirements. Letters request that the managers of actively managed commingled vehicles (i.e., those with FRSTF and other clients’ assets) consider removing Scrutinized Companies from the product or create a similar actively managed product that excludes such companies. Similar written requests must be provided to relevant investment managers within the Investment Plan.
- Written notice to any company with inactive business operations in Sudan or Iran, informing the company of the PFIA and encouraging it to continue to refrain from reinitiating active business operations. Such correspondence continues semiannually.
- Written notice to any Scrutinized Company with active business operations, informing the company of its Scrutinized Company status and that it may become subject to divestment. The written notice must inform the company of the opportunity to clarify its Sudan-related or Iran-related activities and encourage the company, within 90 days, to cease its scrutinized business operations or convert such operations to inactive status.
- A prohibition on further investment on behalf of the FRSTF in any Scrutinized Company once the Sudan and Iran scrutinized lists have been approved by the Trustees. All publicly traded securities of Scrutinized Companies must be divested within 12 months after the company’s initial (and continued) appearance on the Scrutinized Companies list. Divestment does not apply to indirect holdings in actively managed commingled investment funds—i.e., where the SBA is not the sole investor in the fund. Private equity funds are considered to be actively managed.
- Reporting to each member of the Board of Trustees, President of the Senate, and the Speaker of the House of Representatives of Scrutinized Company lists within 30 days of creation, and public disclosure of each list.
- Quarterly reporting of the following to each member of the Board of Trustees, the President of the Senate, the Speaker of the House of Representatives, the United States

Presidential Special Envoy to Sudan, and the United States Presidential Special Envoy to Iran.³ The report must include the following:

- A summary of correspondence with engaged companies;
 - A listing of all investments sold, redeemed, divested, or withdrawn;
 - A listing of all prohibited investments;
 - A description of any progress related to external managers offering PFIA compliant funds; and
 - A list of all publicly traded securities held directly by the state.
- Adoption and incorporation into the FRSTF Investment Policy Statement (IPS) of SBA actions taken in accordance with the PFIA. Changes to the IPS are reviewed by the Investment Advisory Council (IAC) and approved by the Trustees.
 - Relevant Sudan or Iran portions of the PFIA are discontinued if the Congress or President of the United States passes legislation, executive order, or other written certification that:
 - Darfur genocide has been halted for at least 12 months;
 - Sanctions imposed against the Government of Sudan are revoked;
 - Government of Sudan honors its commitments to cease attacks on civilians, demobilize and demilitarize the Janjaweed and associated militias, grant free and unfettered access for deliveries of humanitarian assistance, and allow for the safe and voluntary return of refugees and internally displaced persons;
 - Government of Iran has ceased to acquire weapons of mass destruction and support international terrorism;
 - Sanctions imposed against the government of Iran are revoked; or
 - Mandatory divestment of the type provided for by the PFIA interferes with the conduct of U.S. foreign policy.
 - Cessation of divestment and/or reinvestment into previously divested companies may occur if the value of all FRSTF assets under management decreases by 50 basis points (0.5 percent) or more as a result of divestment. If cessation of divestment is triggered, the SBA is required to provide a written report to each member of the Board of Trustees, the President of the Senate, and the Speaker of the House of Representatives prior to initial reinvestment. Such condition is required to be updated semiannually.

Section 121.4501(7), F.S., enacted in 2009, requires the SBA to identify and offer, by March 1, 2010, at least one terror-free investment product for the FRS Investment Plan.⁴ The product must allocate its funds among securities not subject to divestiture, as provided in the PFIA.

Prohibition Against Contracting with Scrutinized Companies

Section 287.135(2), F.S., prohibits a company on the Scrutinized Companies with Activities in Sudan List or on the Scrutinized Companies with Activities in the Iran Petroleum Energy Sector

³ Section 215.473(4)(b), F.S.

⁴ Section 1 of Ch. 2009-97, L.O.F.; Senate Bill 538.

List from bidding on, submitting a proposal for, or entering into or renewing a contract with an agency⁵ or local governmental entity for goods or services of \$1 million or more. “Local governmental entity,” for the purposes of s. 287.135, F.S., means a county, municipality, special district, or other political subdivision of the state.

Section 287.135(3), F.S., provides that any contract with an agency or local governmental entity for goods or services of \$1 million or more entered into or renewed on or after July 1, 2011, must contain a provision that allows for the termination of such contract at the option of the awarding body if the company is found to have submitted a false certification or has been placed on the Scrutinized Companies with Activities in Sudan List or the Scrutinized Companies with Activities in the Iran Petroleum Energy Sector List.

Section 287.135(4), F.S., allows an agency or local governmental entity to make a case-by-case exception to the prohibition if:

- The scrutinized business operations⁶ were made before July 1, 2011;
- The scrutinized business operations have not been expanded or renewed after July 1, 2011;
- The agency or local governmental entity determines that it is in the best interest of the state or local community to contract with the company;
- The company has adopted, has publicized, and is implementing a formal plan to cease scrutinized business operations and to refrain from engaging in any new scrutinized business operations; *and*
- *One* of the following occurs:
 - The local governmental entity makes a public finding that, absent such an exemption, the local governmental entity would be unable to obtain the goods or services for which the contract is offered.
 - For a contract with an executive agency, the Governor makes a public finding that, absent such an exemption, the agency would be unable to obtain the goods or services for which the contract is offered.
 - For a contract with an office of a state constitutional officer other than the Governor, the state constitutional officer makes a public finding that, absent such an exemption, the office would be unable to obtain the goods or services for which the contract is offered.

An agency or local governmental entity must require a company that submits a bid or proposal for, or that otherwise proposes to enter into or renew, a contract with the agency or local governmental entity for goods or services of \$1 million or more to certify, at the time a bid or proposal is submitted or before a contract is executed or renewed, that the company is not a scrutinized business operation under s. 215.473, F.S.

If an agency or local governmental entity determines that a company has submitted a false certification that it is not a scrutinized business operation and has provided the company with written notice and 90 days to respond in writing to such determination, and the company fails to

⁵ Agency is defined in s. 287.012(1), F.S., as any of the various state officers, departments, boards, commissions, divisions, bureaus, and councils and any other unit of organization, however designated, of the executive branch of state government. “Agency” does not include the university and college boards of trustees or the state universities and colleges.

⁶ S. 215.473(1)(s), F.S., defines “scrutinized business operations” to mean “business operations that have resulted in a company becoming a scrutinized company.”

demonstrate that it has ceased its engagement in scrutinized business operations, then the awarding body *must* bring a civil action against the company. If a civil action is brought and the court determines that the company submitted a false certification, the company shall pay all reasonable attorney's fees and costs (including costs for investigations that led to the finding of false certification) and a civil penalty equal to the greater of \$2 million or twice the amount of the contract for which the false certification was submitted. A civil action to collect the penalties must commence within 3 years after the date the false certification is made.

Section 287.135(6), F.S., specifies that only the awarding body may cause a civil action to be brought, and that the section does not create or authorize a private right of action or enforcement of the provided penalties. An unsuccessful bidder, or any other person other than the awarding body, may not protest the award or contract renewal on the basis of a false certification.

Section 287.135(7), F.S., specifies that this section preempts any ordinance or rule of any local governmental entity involving public contracts for goods or services of \$1 million or more with a company engaged in scrutinized business operations.

In accordance with the requirements of federal law,⁷ the Department of Management Services must submit a written notice describing the act to the Attorney General of the United States within 30 days after July 1, 2011. Section 287.035, F.S., becomes inoperative on the date that federal law ceases to authorize the state to adopt and enforce the contracting prohibitions of the type provided for in the section.

Fiduciary Standards

The fiduciary standards for the SBA are specified out as follows in s. 215.47(10), F.S.:

Investments made by the State Board of Administration shall be designed to maximize the financial return to the fund consistent with the risks incumbent in each investment and shall be designed to preserve an appropriate diversification of the portfolio. The board shall discharge its duties with respect to a plan solely in the interest of its participants and beneficiaries. The board in performing the above investment duties shall comply with the fiduciary standards set forth in the Employee Retirement Income Security Act of 1974 (ERISA) at 29 U.S.C. s. 1104(a)(1)(A) through (C). In case of conflict with other provisions of law authorizing investments, the investment and fiduciary standards set forth in this subsection shall prevail.

The ERISA standard at 29 U.S.C. s. 1104(a)(1)(A) - (C) provides for the "prudent man standard of care," requiring a fiduciary to:

discharge his duties with respect to a plan solely in the interest of the participants and beneficiaries and—
(A) for the exclusive purpose of:

⁷ The Sudan Accountability and Divestment Act of 2007, Pub. L. No. 110-174, §§ 1 to 12, Dec. 31, 2007, 121 Stat. 2516, as amended Pub. L. No. 111-195, Title II, § 205(a), July 1, 2010, 124 Stat. 1344.

- (i) providing benefits to participants and their beneficiaries; and
- (ii) defraying reasonable expenses of administering the plan;
- (B) with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims;
- (C) by diversifying the investments of the plan so as to minimize the risk of large losses, unless under the circumstances it is clearly prudent not to do so;

III. Effect of Proposed Changes:

The bill amends s. 215.471, F.S., to prohibit the SBA from acting as a fiduciary with respect to voting on, or in favor of, any proxy resolution advocating expanded US trade with Cuba or Syria. The SBA must report on its activities in its annual proxy voting report.

The bill amends s. 287.135, F.S., to provide that a company engaged in business operations in Cuba or Syria is ineligible to contract with an agency or local governmental entity for goods or services of \$1 million or more. Any contract with an agency or local government, after July 1, 2012, must include a provision allowing for termination if the company:

- is found to have submitted a false certification concerning a Scrutinized Companies list or business operations in Cuba or Syria;
- has been placed on a Scrutinized Companies list; or
- has been engaged in business operations in Cuba or Syria.

For purposes of Cuba or Syria, the bill defines “business operations” as engaging in commerce in any form in Cuba or Syria, including, but not limited to, acquiring, developing, maintaining, owning, selling, possessing, leasing, or operating equipment, facilities, personnel, products, services, personal property, real property, military equipment, or any other apparatus of business or commerce.

The bill allows an agency or local governmental entity to make a case-by-case exception to the prohibition of contracting with a company which has business operations in Cuba or Syria if all of the following conditions are met:

- The business operations were made before July 1, 2012;
- The business operations have not been expanded or renewed after July 1, 2012;
- The agency or local government entity determines that it is in the best interest of the state or local community to contract with the company; and
- The company has adopted, has publicized, and is implementing a formal plan to cease business operations and to refrain from engaging in any new business operations.

The Department of Management Services must, by July 30, 2012, apprise the Attorney General of the United States of the inclusion of companies with business operations in Cuba or Syria within the provisions of s. 287.135, F.S.

The bill takes effect July 1, 2012.

IV. Constitutional Issues:

A. Municipality/County Mandates Restrictions:

None.

B. Public Records/Open Meetings Issues:

None.

C. Trust Funds Restrictions:

None.

D. Other Constitutional Issues:

Under the Supremacy Clause of the United States Constitution,⁸ where the federal government and a state government legislates on the same subject, the federal law is supreme and will, in general, have the effect of voiding the conflicting state law.⁹ The Supremacy Clause applies when state law is inconsistent with federal law. If state law attempts to invalidate the substance of a federal law or treaty, the state law cannot stand. Similarly, state law which encourages conduct inconsistent with that required by federal law is invalid. The same result holds if state law forbids conduct that federal law allows, or interferes with the achievement of a federal objective.¹⁰ However, states are generally free to legislate in areas not controlled by federal law.

Congress, however, has authorized the type of contractual restrictions included in this bill and current law contains a provision that specifically makes it inoperative if Congress ever rescinds that authority. Therefore, this bill does not appear to be in conflict with the Supremacy Clause of the U.S. Constitution.

V. Fiscal Impact Statement:

A. Tax/Fee Issues:

None.

B. Private Sector Impact:

Indeterminate.

C. Government Sector Impact:

Indeterminate.

⁸ U.S. Const. art. VI, cl. 2.

⁹ See, *Northwest Central Pipeline Corp. v. State Corp. Comm'n of Kansas*, 489 U.S. 493, 509 (1989).

¹⁰ *Perez v. Campbell*, 402 U.S. 637 (1971); *McCulloch v. Maryland*, 17 U.S. (4 Wheat.) 316 (1819).

VI. Technical Deficiencies:

None.

VII. Related Issues:

None.

VIII. Additional Information:**A. Committee Substitute – Statement of Substantial Changes:**

(Summarizing differences between the Committee Substitute and the prior version of the bill.)

CS by Governmental Oversight and Accountability on February 22, 1012:

The CS removes the prohibition on the SBA from investing in companies that have specified business relationships with Cuba and Syria, and removes the requirement to create a Scrutinized Companies with Activities in Cuba List or Scrutinized Companies with Activities in Syria List. Instead, the SBA is prohibited from acting as a fiduciary with respect to voting on, or in favor of, any proxy resolution advocating expanded US trade with Cuba or Syria.

The CS also prohibits agencies and local governments from having a contract for greater than \$1 million with any entity engaged in business operations in Cuba or Syria.

B. Amendments:

None.