



Public Safety Professionals Get Valuable Education at 2010 Public Safety Conference

NCPERS president Pat McElligott kicked off the 2010 Public Safety Employees Pension & Benefits Conference in Palms Springs, California. In his opening remarks he addressed the attacks on Defined Benefit (DB) plans and how they will be a target in the coming years. He encouraged attendees to “become a voice for pensions and be aggressive on why DB plans are important.” McElligott also assured audience members that they would leave the conference with “a more educated and more defined voice on why DB plans are important to us.”

George Iwanicki of J.P. Morgan Asset Management provided an economic forecast for the upcoming year. According to Iwanicki, the U.S. economy is in a “sluggish/half-speed recovery.” Although there is still a fair amount of wealth destruction and high unemployment, debt levels, in general, are coming down. Fund members Aaron Hanson of the Omaha Police Union 101 IUPA and Steve LeClaire of the Omaha Professional Firefighters, IAFF Local 385, shared information on negotiating an employment contract when a fund is in distress. Based on a case study of Omaha Police and Fire, which is less than 40 percent prefunded, the presentation gave attendees valuable infor-



mation that they can use back home. The issue of meeting the energy challenge was addressed by Irving Mintzer, who spoke on the implications for renewable energy and clean technologies. Mintzer said, “The pattern of U.S. energy supply is placing a huge fiscal burden on our economy and brings with it important environmental risks.”

Greg Kinczewski of Marco Consulting Group spoke to members about preparing to exercise institutional investors’ newly gained right to vote on corporate executive pay. Terri Mumford from Ice Miller LLP

provided an IRS update, and Kevin Lindahl and Todd Seaver discussed credit rating agencies and the impact

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Risk Management – Now More Important than Ever

For most investors, the global financial crisis will perhaps be remembered as a time of extremes. Early on, equity markets declined as the crisis spread around the globe; in the U.S., the S&P 500 Index was down by as much as 56% from its October, 2007 high. In 2009, the U.S. equity market reversed course finishing the year up 23%. Most markets around the world followed suit. As we enter the final quarter of 2010, investors are still questioning how they will be able to make up the lost value of their portfolios stemming from the extraordinary market events the global financial crisis left in its wake.

INVESTORS NEED ALPHA.

And because the key to investment success is not the capture of gains nearly as much as the avoidance of large relative losses, *it is more critical than perhaps ever before to identify managers who can provide alpha, while at the same time attempting to manage risk.* The risk controls must be embedded within the investment process to assist in minimizing track-

ing error especially during times of extreme market turbulence. It is the large relative losses, either in amplitude or in time, that are the critical inhibitors of investing success, in either relative or absolute terms. The reality is that anomalous – or “black swan” – events occur more frequently than thought making an investment process *without* tight risk management more vulnerable to large relative losses.

SO HOW SHOULD AN INVESTOR EVALUATE AN INVESTMENT PROCESS TO DETERMINE WHETHER A REASONABLE LEVEL OF RISK CONTROL EXISTS?

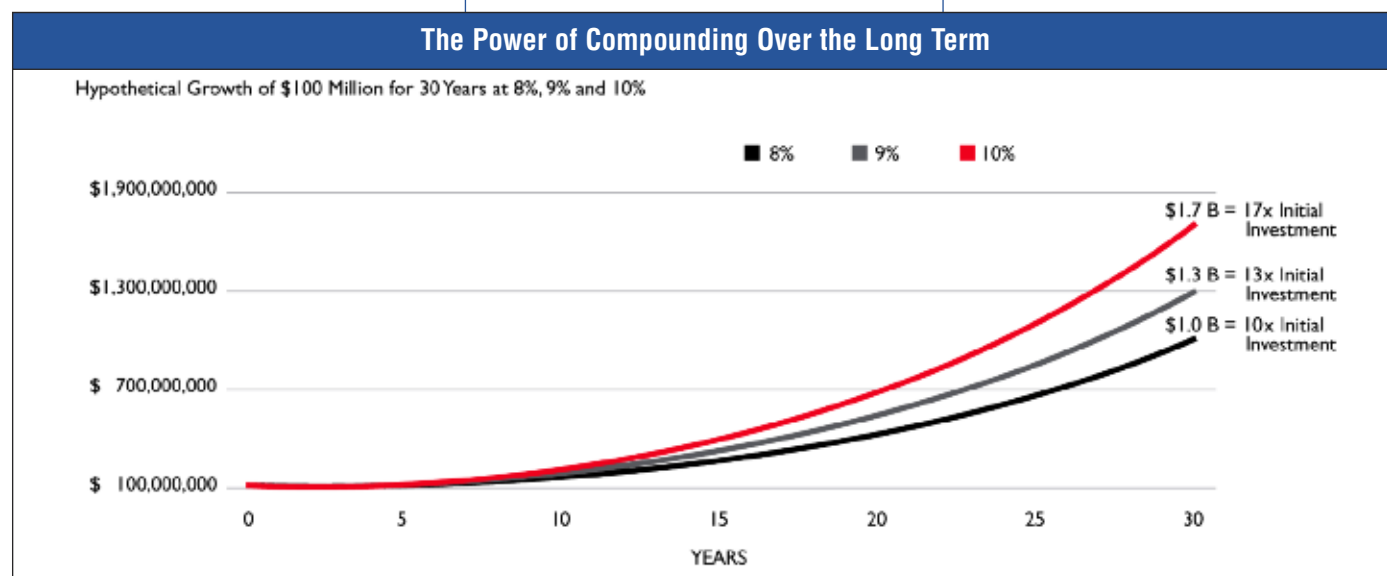
While the ideal manager-candidate should possess an historical record of consistently outperforming the benchmark, without incurring additional relative risk, an investor should first want to determine if there is a high probability the investment process will continue to produce the expected results over the long term. This means evaluating the t statistic and one tail significance as well as determining if there is a good *a priori* expectation that the manager will continue to provide alpha in the

future, with a low tracking error. And not to be overlooked is information ratio – a manager with a 0.75 information ratio has a greater than 95% chance of beating the benchmark over a 10-year period.*

Selecting a manager with a credible risk-managed investment process is, indeed, a process that requires considerable due diligence. However, the potential rewards can be substantial. A plan sponsor should focus on a manager’s ability to consistently provide alpha remembering that even modest incremental improvements in performance above the benchmark can make a significant difference in benefits over the long term.

For example, as the chart below demonstrates, compounding just 1% to 2% excess return per year can have a meaningful impact on meeting long-term goals. As observed, adding just 1% annually in excess return to a hypothetical investment compounded at 8% per year would yield an additional 30% in value or 13 times the original investment at the end of 30 years. Two percent annual-

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Fall 2010 Legal Update

By Robert D. Klausner, NCPERS General Counsel

Following the rules of the Plan document is critical to successful completion of the fiduciary mission. The following recent court decisions from around the country address the rewards and consequences associated with daily management issues of retirement plans.

STATE BOARD OF ADMINISTRATION NOT LIABLE FOR INVESTMENT LOSSES DURING WAITING PERIOD.

Appellant voluntarily chose to participate in the Florida Retirement System's (FRS) self-directed investment plan account. Appellant understood that Section 121.591(1), Florida Statutes (2008), provides that participants in the Florida Retirement System (FRS) cannot withdraw their funds until three months after retirement. When he called the "MyFRS Financial Guidance Line" to inquire about distribution of the funds in his account, he was advised that participants are allowed to take a ten percent distribution after one month after retirement. By the time the participant requested distribution of his account, the account had lost over \$100,000 in value. The appellant claimed that the State Board of Administration (SBA) was liable to him for the losses, arguing that "the SBA concealed a material fact by failing to notify him that he still had the ability to reallocate his investment funds within the options available in the FRS Investment Plan during the three-month waiting period." The court acknowledged that Florida law follows ERISA in shielding plan fiduciaries from liability for losses experienced by participants in self-directed accounts, except when the fiduciary conceals a material non-public fact from participants. The court affirmed the SBA's refusal to reimburse the par-

ticipant for his losses and found that there was substantial competent evidence that the SBA did not conceal a material non-public fact.

PENSION BOARD CANNOT CHARGE ADMINISTRATIVE EXPENSES TO ACCOUNT'S PRINCIPAL BALANCE WHERE LEGISLATURE INTENDED FOR ADMINISTRATIVE EXPENSES TO BE PAID FROM INTEREST EARNED AND EMPLOYER CONTRIBUTIONS.

The Oregon Public Employees Retirement system maintains a regular account and a variable account, with options available for participants to have specified percentages of their contributions directed to the variable account. During 2001 and 2002, both the regular account and the variable account sustained losses. For those years, the board charged the variable account's pro rata share of the administrative expenses of the retirement system against the account's principal balance. For the same time period, the board charged the regular account's pro rata portion of administrative expenses to employer contributions. The statute governing administrative expenses of the plan, which applies to both the regular account and the variable account, provides that administrative expenses shall be paid from interest earned by the system, and that if such interest is insufficient to pay all administrative expenses, the excess shall be paid from employer contributions. However, the statute specifically governing the variable account only provided that administrative expenses

shall be paid from interest earned by the account, without specifying how administrative expenses should be paid if the interest earned is insufficient. In reversing the board's action in charging administrative expenses against the variable account's principal, the court reasoned that the language in the variable account statute clearly indicates the legislature's intent to refrain from using principal to pay administrative expenses. The court rejected the board's argument that its action equated to using the account's "negative interest" to pay administrative expenses. The court ruled that the variable account's pro rata share of the system's administrative expenses should be paid out of the variable account's interest, and the excess expenses should be paid pursuant to the general statute: interest earned by the balance of the system and then employer contributions.

Murray v. Public Employees Retirement Board, 230 P.3d 993 (Or. Ct. App. 2010)

RETIREMENT SYSTEM BOARD PROPERLY FOLLOWED ITS ADMINISTRATIVE RULE IN REFUSING TO CREDIT VARIABLE ACCOUNT WITH PARTICIPANT'S REDEPOSIT OF FUNDS.

Petitioner participated in retirement system's variable account program, which included having funds credited to both the system's regular account and variable account. After terminat-

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of the Dodd-Frank Financial Reform law. Richard Tettamant, Administrator of the Dallas Police & Fire Pension Fund, spoke on the topic of Deferred Retirement Option Plans (DROP) and their sustainability.

The second day of the conference continued with a presentation from Lawrence Blum, who offered insight on reducing and managing stress in the public safety profession. He spoke on ways to maintain mental, physical, and spiritual health to reduce stress and sustain good work performance. Karl Johnson from the Government Accounting Standards Board updated the attendees on the proposed new pension accounting rules and the next steps

in the process. EFI Actuaries' Greg Stump discussed the impact of alternatives to a five-year increase in the retirement age for public safety officials, while Marlon Kimpson of Motley Rice and Kurt Rumsfeld of Woodley McGillvary delivered practical pointers to help trustees fulfill their fiduciary duties. William Robinson of Gallagher Benefit Services provided a thorough overview and analysis of health care reform and its impact on public safety employees.

Day three included an informative interactive workshop on how to effectively communicate with the public and media, facilitated by Rebecca Shaw of Spaeth Communications. Shaw gave tips on message development, buzzwords,

and the use of statistics and data in media relations. Barbara Maynard of Maynard Consulting Group spoke about the battles pensions have faced in Los Angeles, and Hank Kim, NCPERS Executive Director, gave an overview of the new NCPERS pension defense toolkit and what to expect in 2011. Hank Kim and Anthony Roda of Williams & Jensen wrapped up the conference with a legislative update on the latest developments in Washington, D.C. Finally, attendees were given an opportunity to network and seek advice from others during the Trustee Open Forum. Full presentations from the 2010 Public Safety Conference can be viewed at http://www.ncpers.org/Conferences/SEP_BC.php. ❖



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ly in excess return will have an even greater impact – 70% more in value at the end of 30 years or 17 times the original investment.

For plan sponsors who need alpha, risk management matters.

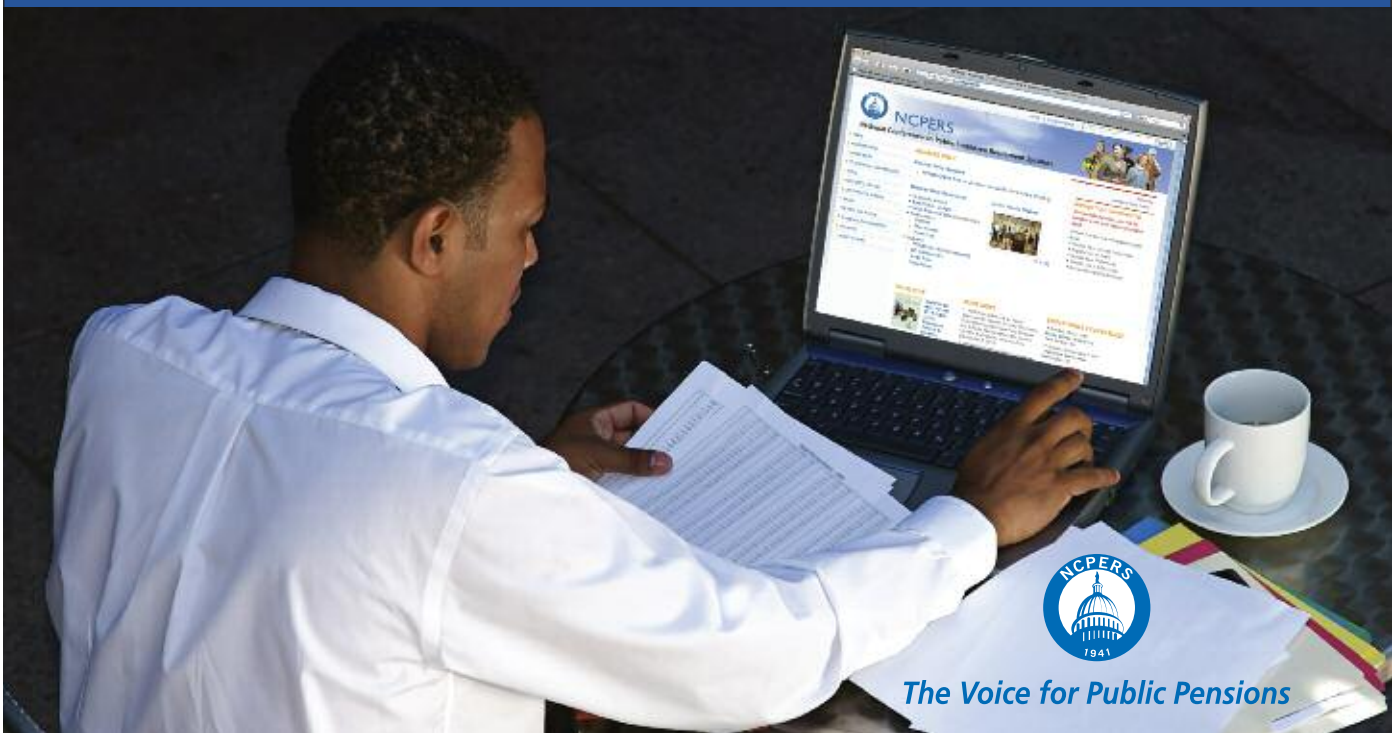
*Information Ratio = Excess Return ÷ Tracking Error. Favorable information ratio may not be indicative of positive absolute performance.

Past performance does not guarantee future results. ❖

Jennifer Young, CFA, President and Co-Chief Executive Officer, joined INTECH in June of 1999 and since that time has been a key contributor in helping INTECH grow from a single-product provider to a solutions-based global investment manager. Ms. Young has more than 23 years experience in portfolio management and marketing financial assets, as well as extensive experience in client and consultant relations. She joined INTECH from Manning & Napier Advisors Inc., where she was primarily responsible for the marketing effort of the firm's consulting services division. Prior to that, Ms. Young spent 11 years in portfolio management and marketing/consultant relations for the former Marine Midland Bank and HSBC Asset

Management Americas Inc. in both their domestic and international investment divisions. As of September 30, 2010, INTECH, which was founded in 1987, managed approximately \$42.4 billion for institutional clients worldwide, including public funds, pension funds, foundations, endowments and other not-for-profit entities. Ms. Young holds an M.B.A. in Finance from Clarkson University and a B.A. in Economics from St. Lawrence University. She has earned the right to use the Chartered Financial Analyst designation. Ms. Young has presented at various investment conferences on topics including the importance of risk management, active versus passive management and the application of stochastic portfolio theory.

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ing his employment, petitioner requested withdrawal of all funds from his account. He later obtained employment that qualified him for participation in the retirement system and sought to redeposit the withdrawn funds. The board redeposited all of the petitioner's contributions to the regular account and refused to credit the variable account. At all relevant times, an administrative rule specified that the retirement system "shall" credit member lump sum payments to a member's regular account." The court held that the board properly refused to credit the member's variable account because the administrative rule clearly required the entire repayment to be credited to the regular account. *Smith v. Public Employees Retirement Board*, 230 P. 3d 88 (Or. Ct. App. 2010)

EMPLOYER REQUIRED TO PAY EMPLOYER'S AND EMPLOYEE'S RETROACTIVE CONTRIBUTIONS TO RETIREMENT SYS-

TEM WHEN EMPLOYER ERRONEOUSLY FAILED TO ENROLL EMPLOYEE IN RETIREMENT SYSTEM.

A public employee was also a volunteer firefighter and a member of the firefighters' pension system. The employer was incorrectly advised by a retirement system representative that the employee could not be a member of two different state funded retirement systems. As such, neither the employer nor the employee made contributions to the retirement system on behalf of the employee. Contrary to the advice received by the retirement system representative, state law specifically provided that an employee can be a member of multiple state-funded retirement systems in certain situations. The retirement system found that the employee's participation in the system was mandatory and invoiced the employer for both the employer's and the employee's share of unpaid contributions. The employer argued that it reasonably relied on representations made by the retire-

ment system. However, the court rejected the employer's argument by reasoning that the employer was bound by the law and cannot be excused from following the law due to its ignorance. The court also ruled that state law requires an employer to pay the employer's share and the employee's share of retirement contributions when the employer makes an error in calculation or participation coverage.

Poteau Valley Improvement Authority v. Oklahoma Public Employees Retirement System, 233 P.3d 423 (Okla. Civ. App. 2010) ❖

This article is a regular feature of PERSist. Robert D. Klausner, a well-known lawyer specializing in public pension law throughout the United States, is General Counsel of NCPERS as well as a lecturer and law professor. While all efforts have been made to insure the accuracy of this section, the materials presented here are for the education of NCPERS members and are not intended as specific legal advice. For more information go to www.robertdklausner.com

PPCC Standards Award Application Process is Now Open November 2010

NCPERS members are now able to apply for the Standards Award Program developed by the Public Pension Coordinating Council (PPCC). The PPCC is a coalition of three associations--NCPERS, National Association of State Retirement Administrators, and National Council on Teacher Retirement--that represent public pension funds which provide benefits to the vast majority of public employees.

This is the seventh year the PPCC is offering the PPCC Standards Award Program to public retirement systems in this form. The Public Pension Standards are intended to reflect minimum expectations for public retirement system management and administration, as well as serve as a benchmark by which all defined benefit public plans should be measured. The retirement systems and the state and local governments that sponsor them are encouraged to meet these standards.

2011 NCPERS Legislative Conference



January 30 – February 1, 2011

Hyatt Regency Washington Hotel
Washington, DC

The Voice for Public Pensions
National Conference on
Public Employee Retirement Systems



www.NCPERS.org

EARLY BIRD REGISTRATION DEADLINE JANUARY 10, 2011

Visit www.NCPERS.org/legconf to register and book your hotel room online.



The Voice for Public Pensions

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National Conference
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Calendar of Events 2011

Legislative Conference

January 30–February 1, 2011
Hyatt Regency Capitol Hill
Washington, DC

Trustee Educational Seminar (TEDS)

May 21–22, 2011
Fontainebleau Hotel
Miami, FL

Annual Conference & Exhibition

May 22–26, 2011
Fontainebleau Hotel
Miami, FL



National Conference on Public Employee Retirement Systems

444 North Capitol St., NW Suite 630
Washington, D.C. 20001

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2010-2011

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