Pennsylvania Association of Public Employee Retirement Systems
PO Box 61543, Harrisburg, PA 17106-1543

Summer 2011 (Vol. 6, No. 2)

In This Issue

PAPERS 5th Annual Fall Workshop

Wed., Sept. 21, 2011

The Four Points Sheraton Pittsburgh North

Registration starts at 7:00 a.m.
Workshops begin at 8:20 a.m.

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One Free Registration for each Participating Member Pension Fund

Registration Form on Page 4
(deadline 9/1/2011)

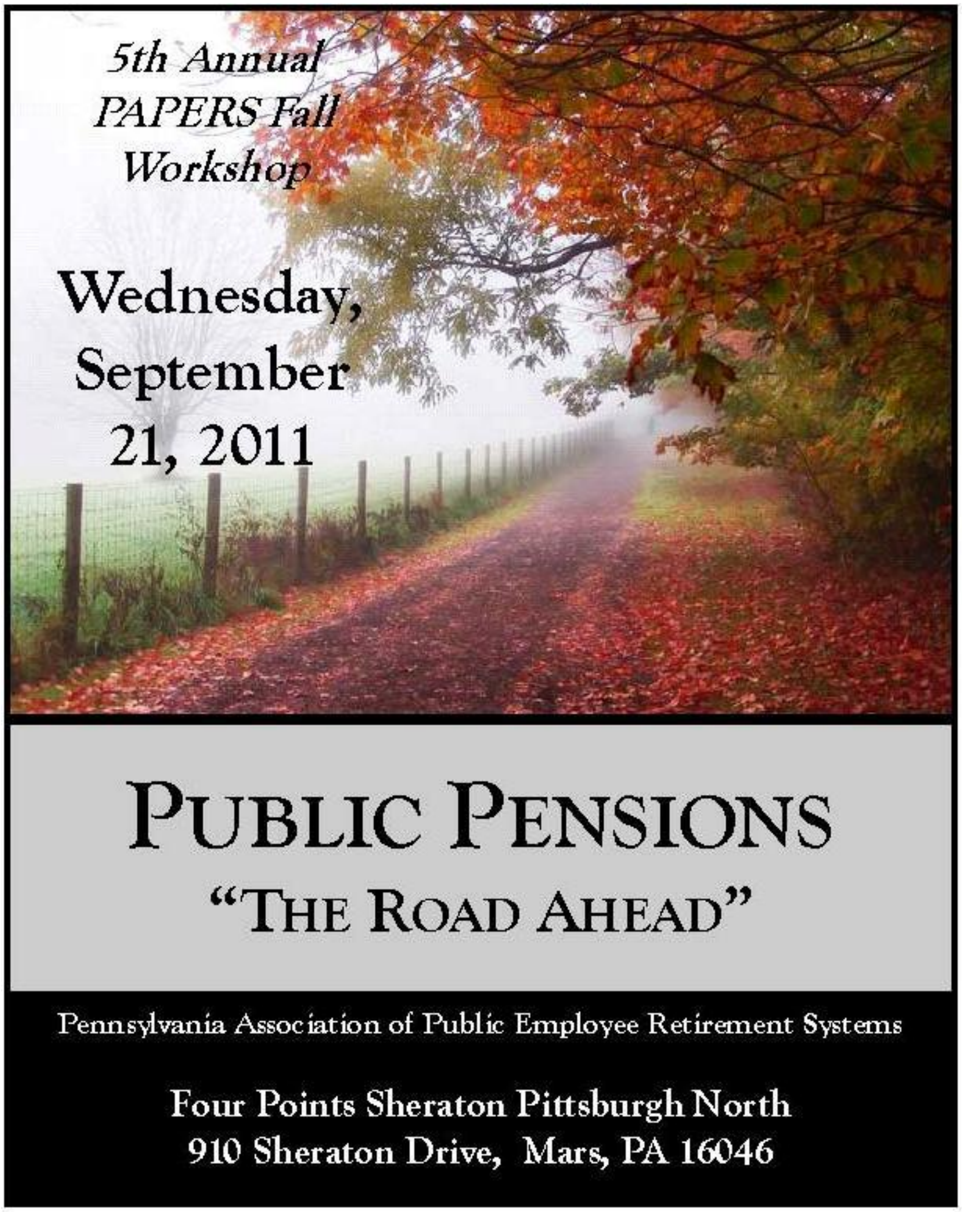
Interested in Overnight Lodging at the Workshop?

Special Conference Rate
$110/double or king + 14% tax

For Reservations Call:
Toll-Free 1-888-627-8175

Reservation Deadline for Special Conference Rate is 8/30/2011

Hotel Information & Driving Directions on Page 5



Special Thanks to our Workshop Sponsors

The generous financial support of these PAPERS corporate (Associate & Affiliate) members makes the Fall Workshop possible.

- **AllianceBernstein,** New York, NY
- **Bank of New York Mellon,** Pittsburgh, PA/New York, NY
- **Federated Investors,** Pittsburgh, PA
- **Foster & Foster, Inc.**, Fort Myers, FL
- **Kessler Topaz Meltzer & Check, LLP**, Radnor PA
- **Milberg LLP,** New York, NY 10119

From PAPERS' Executive Director

Being a pension board member and **trustee** brings with it a serious responsibility for public officials and others appointed to local pension boards. As a trustee you have a **fiduciary duty** to protect and nurture the funds that have been entrusted to your care. The employees you represent deserve the best possible management of their trust funds.

To that end, you as a trustee have an obligation to seek out the best education you can find in the subject areas related to your duties to manage the funds and control the liabilities of these pension plans. PAPERS has been incorporated with a mission to provide the most cost efficient high quality education possible for local trustees in Pennsylvania. We hope that you will give us a chance to show you what we have to offer by attending one of our Fall Workshops or our Annual Forums.

This summer PAPERS staff and Board are working hard on the production of our 5th annual Fall Workshop which will be held on September 23rd at Four Points Sheraton Pittsburgh North 910 Sheraton Drive Mars, PA 16046

The PAPERS Fall Workshop provides an opportunity for you to participate in an excellent series of educational workshops. In addition it gives you a chance to meet with your plan sponsor peers and with professionals who provide consulting, investment, actuarial and legal services to the pension community. All PAPERS's member systems receive one complimentary registration to both the Spring Forum and the Fall Workshop. .To qualify you must submit a registration form so that we will be able to plan for the proper number of attendees. This year you can also earn credits toward your Certified Public Pension Trustee (CPPT) certificate at the Fall Workshop.

We have put together an agenda that addresses some of the basic skills trustees must master to fulfill their fiduciary duty to the members of their Plan. The success of the Fall Workshop and of PAPERS as an organization is dependent on your participation and support. I look forward to seeing you at the PAPERS fall workshop on September 23rd in Pittsburgh. You'll find the Workshop reservation form waiting for you to complete on page.??

***Jim Perry*, PAPERS Executive Director**

Municipal Pension plan Trustees should be aware that in addition to pension benefits retirees often receive medical benefits as well. Governmental accounting standards [GASB 45] require an actuarial valuation to calculate the accrued liability and ARC for retiree medical benefits. A simplified method is allowed for small plans under certain circumstances

Foster & Foster, Inc. has developed proprietary software to assist small plans in complying with GASB rules. A link to Foster & Foster will soon be added to the PAPERS website, providing more detailed information.

PUBLIC PENSIONS

"THE ROAD AHEAD"

Wednesday, September 21, 2011

7:00–8:00 am	**Registration & Continental Breakfast**
8:00–8:45 am	**Welcome to PAPERS Fall Workshop** Jim Perry, *Executive Director PAPERS* **Perspective on Local Government in Pennsylvania** Keynote Speaker: Doug Hill, *Executive Director*, Co. *Commissioners Assoc. of PA*
8:45–9:30 am	**Economic Overview** **Is There a Light at the End of the Tunnel?** To Be Announced – Bank of New York Mellon
9:30–10:15 am	**Local & Municipal Revenue Outlook for 2012** Moderator: John Kehoe, *Senior Partner, Kessler Meltzer Topaz & Check LLP* Presenter: Michael Wood, *Research Director, PA Budget & Policy Center*
10:15–10:30 am	**Morning Refreshment Break**
10:30–11:15 am	**Investing in Emerging Markets** Presenter: Nichola Noriega, CFA Int'l Equity Strategist, Federated Investors
11:15 am-12 noon	**Building a Real Estate Portfolio** Presenter: Paul Nassser, CFO *Intercontinental Real Estate* Corp.
12:00–1:00 pm	**Lunch**
1:00–1:45 pm	**Hedge Fund Investing** Presenter: Jim Grossman, *Managing Director of External Public Markets, Risk & Compliance, PSERS*
1:45–2:30 pm	**A Discussion of the Latest GASB Exposure Drafts** Presenter: Michael Merlob, *Foster & Foster Consulting Actuaries*
2:30–2:45 pm	**Afternoon Refreshment Break**
2:45–4:00 pm	**Public Pension Plan Roundtable** Moderator: Peter Saferstein, *Partner, Milberg, LLC* Panelists: *PAPERS Board of Directors*

Announcing the:

5th Annual PAPERS Fall Workshop

Wednesday, September 21, 2011

7:00 a.m. – 5:00 p.m.
Continental breakfast and lunch included

Held at The Four Points Sheraton Pittsburgh North
910 Sheraton Drive, Mars, PA 16046

Continuing its mission to facilitate education for persons affiliated with Pennsylvania's public pension plans, PAPERS is pleased to announce plans for this one-day educational workshop in the Pittsburgh area.

Registration for PAPERS Fall Workshop (9/21/2011)

Please check appropriate category:

- ❑ ***Participating Members*** (Pension Plans/Retirement Systems) – One complimentary registration; $50/person registration fee for each additional staff/trustee
- ❑ ***Associate Members*** (legal & investment service providers) – $400/person registration fee
- ❑ ***Affiliate Members*** (all other service providers) - $200/person registration fee

Individual's name ____

Representing (pension plan or company) ______________________________

Mailing address ____

City, State, Zip ____

Telephone number (______) ________________ **E-mail address** ____________________

Complete, detach at dotted line and return no later than Sept. 1, 2011, with any payment due.

Make checks payable to: ***PAPERS;*** **Mail to:** ***PAPERS, PO Box 61543, Harrisburg, PA 17106-1543***
On-line payment via PayPal also available at: www.pa-pers.org

Conference rate overnight lodging ($110/double or king + 14% tax): Contact The Sheraton at 1-888-627-8175 no later than August 30, 2011.

5th Annual PAPERS Fall Workshop

Wednesday, September 21, 2011

If you're interested in overnight lodging for the Fall Workshop

The Four Points Sheraton Pittsburgh North

910 Sheraton Drive, Mars, PA 16046

Conference Rate: $110/double or king + 14% tax

Conference Rate Guaranteed only through August 30, 2011

For Reservations:

Call toll-free: 1-888-627-8175

Driving Directions to The Four Points Sheraton Pittsburgh North

From Pittsburgh International Airport

Follow Route 60 South to Interstate 79 North. Take Exit 76 (exit from left)and merge onto State Route 19 North. Proceed to the first light and turn right onto Freeport Road. Continue 1 block, turn right onto Sheraton Drive.

From East

Take the Pennsylvania Turnpike to Exit 28 (Cranberry). Turn right and take Route 19 South to the first intersection, Turn left onto Freeport Road. At the first intersection, then turn right onto Sheraton Drive.

From North

Take I-79 South to Exit 78. Exit right to the first intersection and turn left. Take Route 19 South and travel .5 miles to the 3rd light. Turn left on Freeport Road. Proceed 1 block to the intersection and turn right onto Sheraton Drive.

From West

From the Pennsylvania Turnpike (Interstate 76). Take Exit 28. Take Route 19 South to the first traffic light, turn left unto Freeport Road. Proceed one block at the first intersection, turn right onto Sheraton Drive.

It's Time to Enroll

Pension Certification Program Open to Trustees/Staff

The PAPERS CPPT (Certified Public Pension Trustee) Program first tested the waters at the 2010 Fall Workshop and interested parties were eligible to earn CPPT credits towards their certification. This year's Spring Forum marked the official beginning of the PAPERS CPPT Program with CPPT testing. With the two events, participating members now have a potential 18 CPPT credits towards their 36 credit certification.

The goal of the CPPT Program is to provide an educational setting that is conducive to the development of well-informed individuals, so that they will be able to actively and meaningfully participate in the management of their retirement boards.

The CPPT Program has been set up to accommodate both the novice just starting in the pension trustee role, as well as the pro who has already served many terms. Following a core curriculum, you will gain an understanding of investment principles and public pension issues. Each workshop addresses a specific topic related to public retirement.

You will learn from a team of expert money managers, investment professionals, attorneys and financial consultants. These individuals are well respected in their fields and have extensive experience offering educational seminars. Trustees will be held accountable for the knowledge they acquire at the Spring Forum and Fall Workshop and will be tested following each event on the topics covered at the conference.

The PAPERS CPPT Program was modeled after and built in conjunction with the Florida Public Pensions Trustees Association who created their own very successful CPPT Program over 14 years ago. The FPPTA now has 600+ active participants in their certification program and have certified thousands of others throughout Florida setting a new standard of trustee education in the industry. We hope to see similar success with the PAPERS organization but that cannot come without your participation.

This year's Spring Forum successfully addressed pertinent industry topics and issues and fell in line with the mission of PAPERS and the CPPT Program to better educate retirement board trustees, staff and industry professionals.

Participation in the new CPPT program is still modest; however the board of directors recognizes that attaining certification in this program will better prepare you for your fiduciary role as a contributing member in your retirement system. While the PAPERS organization sees the value in this program it is up to you, the members, to participate and make this program as successful as its Florida counterpart.

On the following page (Page 7) you will find more information on the CPPT program and how to register.

CPE (Continuing Professional Education) Credits

Attendance at all sessions of the Fall Workshop will earn 8 CPE credits. An attendance record form will be available at the Workshop for participants to submit, certifying their attendance.

CPPT Program Credits

Attendance at all sessions of the Fall Workshop and successful completion of the follow-up on-line testing will earn 8 CPPT credits.

Become a Member of PAPERS

A current year PAPERS membership is required for attendance at the Spring Forum and/or Fall Workshop and to receive credits in the CPE and/or CPPT programs.

Public employee retirement systems (pension funds) can apply to become Participating Members; each Participating Membership includes one complimentary admission to both the Spring Forum and the Fall Workshop. Corporate providers of service to pension plans can apply to become Associate or Affiliate Members online at **www.pa-pers.org** or by contacting:

PAPERS
PO Box 61543, Harrisburg, PA 17106-1543

James A. Perry, *Executive Director*
Phone: 717-545-3901; **E-mail:** perryja1@comcast.net

Douglas A. Bonsall, *Office Manager*
Phone: 717-921-1957;**E-mail:** douglas.b@verizon.net

PAPERS

CPPT Certification Program Application

Participant Information:

Name: ____

(Please print your name the way you would like it on your certification plaque)

Organization: ____

Address: ____

____

City: ____________________ State: ________ Zip: ________________

Telephone: ____________________ Fax: ______________________

E-Mail: ____

Signature: ____

Payment Information:

In order to make the PAPERS CPPT Program successful there is a $300 participation fee to cover administrative costs. We understand it is a difficult time for state and municipal budgets; please indicate if you would like to pay in entirety or three (3) installments of $100.

☐ Pay in full ($300) ☐ Pay in three (3) $100 installments

☐ Check on site ☐ Send invoice

☐ Invoice to be sent to other than participant.

Billing Name: ____

Billing Address: ____

City: ____________________ State: ________ Zip: ________________

Please submit CPPT application to:
Public Pensions, Inc.
c/o PAPERS CPPT
P.O. Box 550
Sturbridge, MA 01566

Or: smckinstry@publicpensionsinc.com

Office Use Only:

☐ Paid in advance ☐ Paid on site ☐ Invoice

Amount Paid: ______ Date Paid: _______ Balance Amount: _______ Date Paid: ________

Level 1 Start Date: __________ Level 1 Completion Date: ___________

Level 2 Start Date: __________ Level 2 Completion Date: ___________

What's Wrong with Chinese IPOs?

By: Linda R. Killian, CFA, Principal and Portfolio Manager
Renaissance Capital, Greenwich, CT

Another wave of Chinese IPOs is hitting the US equity market, but this time many US investors are staying dry. The reasons for this growing aversion are several, but paramount among them are evidence of actual fraud at a handful of companies, skepticism about business models and growth rates, inadequate financial controls and opaque financial disclosures. As a result, Chinese IPOs have been one of the worst performing groups in the US IPO market, which furthers investor avoidance of the sector. If an investor bought every Chinese IPO since 2008, the average return though mid-June would have been a 33% loss, compared to a 26% gain on the average non-Chinese IPO.

Historical Activity and Performance of US Listed China IPOs 2008-2011

	2008	2009	2010	2011 YTD	2008-2011
US Listed China IPOs	4	12	41	11	**68**
% of US Total	12.9%	19.0%	26.6%	15.5%	**21.3%**
Total Return	-44.4%	-25.5%	-14.3%	-17.2%	**-33.4%**
US Listed IPOs (ex China)	27	51	113	60	**251**
% of US Total	87.1%	81.0%	73.4%	84.5%	**78.7%**
Total Return	28.0%	38.8%	27.9%	12.4%	**26.4%**

Source: www.RenaissanceCapital.com

Total return measured as offer price to 6/8/11 close. Includes IPOs with an initial market capitalization of more than $50 million.

The ongoing fraud investigations of Longtop Financial and other Chinese issuers coupled with the Securities and Exchange Commission's suspensions of trading in some Chinese "reverse merger" US shell companies have caused investors to be suspicious of all Chinese IPOs. Despite these problems, issuance activity of Chinese companies in the US has continued unabated since 2009.

To understand why this is happening to the initial public offerings of entrepreneurial companies from one of the largest and fastest growing countries in the world, it is helpful to review how Chinese IPOs have evolved. Back in the 1990s when nascent Chinese Communist capitalists first tested the US IPO market, the companies raising money were old-line manufacturing companies, utilities and infrastructure plays. Bicycle makers, for example. Towards the end of the decade Chinese issuance in the US was dominated by strategic state privatizations, most notably of China Telecom, China Unicom, China Petroleum and Petro China. Although these IPOs were initially lapped up by investors starved for a public way to play China, many did poorly because they weren't managed to developed markets' standards of public companies.

Then, the character of Chinese issuance changed entirely. Starting in 2005 with the search engine Baidu, Chinese IPOs represented innovative and growing companies that reflected China's emergence from a developing economy to a broad-based, post-modern society. During this period, Chinese IPOs included: Ctrip.com, a leading travel portal; Home Inns, an inexpensive hotel chain; New Oriental Education, a chain of English language schools; and Mindray Medical, a maker of high quality medical equipment.

By this time, China had become a dominant manufacturer in strategically important industries. Solar panels in particular. The PRC flexed its muscle with large numbers of Chinese solar manufacturer IPOs during this period, including Sun-Tech, LDK and Trina. US investors fell over themselves to get stock and the prices of the shares of these companies, regardless of quality or underlying fundamentals, soared.

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What's Wrong With Chinese IPOs?

(continued from page 8)

As Chinese IPOs proliferated, the Chinese government discovered the Hong Kong Stock Exchange as an alternative to the New York Stock Exchange and the NASDAQ. This served two purposes: it showed the US government that the PRC didn't need the US capital markets to raise vast amounts of money and it provided a convenient way for the government to dispose of government privatizations in which US investors had limited interest. US institutional investors are more amenable to risk assets. Thus, slow growing Chinese IPOs head to Hong Kong; growth companies embark for New York.

Leaving aside the scandal-ridden Longtop and other outright frauds, too many constituents of recent vintages of Chinese IPOs share undesirable investment characteristics that reflect the opportunism of Chinese entrepreneurs and a lingering misperception that US investors are so eager to get in on China Inc. that they disregard basic investment standards. Such is not the case, as is demonstrated by the recent difficult debuts and disappointing performance of Chinese IPOs.

The problems of Chinese issuers are many. A number of recent Chinese IPOs have moved forward with poorly described business plans that portray the company as something it is not, or not yet. Some omitted key government policy changes that would restrict the number of products the company could sell. Other tactics make it difficult for prospectus readers to make period to period comparisons of key metrics.

Financial sloppiness, including estimated revenues, extremely high receivables and skimpy analysis of financial performance abound. A number of Chinese companies had only recently hired a Chief Financial Officer and supporting staff. Perhaps this is motivated by unwillingness to add an experienced and expensive English-speaking CFO to overhead, but it is inexcusable. Until recently some companies also used second and third tier auditors. Several issuers also had obviously quickly cobbled together businesses that had no history of operational integration. The mistrust of Chinese IPOs has been aggravated by recent auditor resignations.

The mistrust appears mutual. Several of the Chinese managements have shown arrogance towards prospective US investors, by pointing out, for example, that Chinese car buyers prefer European models to a roomful of US investors. When answering questions, key executives routinely gloss over specific concerns about their business models or recent trends. To some extent, the attitude of not wanting to admit weakness is cultural and understandable. However, being a publicly traded company is a privilege, not a right and prospective US investors are entirely legitimate in demanding full disclosure, candor and confidence that in the future information will be disclosed in a timely and appropriate manner.

To be sure, some of the Chinese IPOs understand and accept the concept of full and fair disclosure as the foundation of public markets. The businesses are clearly defined and well-described. Growth is organic, meets an unmet need and has been well executed. Valuation rationales aren't supported by unlikely assumptions of vastly accelerating revenues and fattening margins. The key executives have relevant experience and have reasonable tenures at the company. Financial statements are clear, fully explained and audited by a major international firm.

When China first began tapping the IPO market twenty years ago, the People's Republic of China was in the driver's seat, offering investors only what the PRC wanted to sell. Today, it is the potential purchasers who are delineating the standards for the types of businesses, valuation and disclosure under which they are willing to invest. While the US SEC can tighten its regulatory purview, the ultimate responsibility for complete and accurate disclosure lies with company management and others involved in preparation for an IPO. In the end, if prospective Chinese IPOs learn the tough lessons of today's flawed IPOs and the PRC steps up its regulatory and audit oversight, China will produce many well-run, innovative companies deserving of public investment.

Foreign Exchange Trading: Secret Profits and Hidden Losses

By: Darren J. Check, Esq., Naumon A. Amjed, Esq. and Ryan T. Degnan, Esq.
Kessler Topaz Meltzer & Check, LLP

Custodial banks' foreign exchange ("FX") trading practices have recently drawn scrutiny for manipulating FX rates charged to the banks' clients. In short, custodial banks offer FX trading services to allow their clients to convert currencies in order to buy and sell foreign securities and to engage in other transactions. However, custodial banks have come under fire for secretly charging their clients less favorable FX rates than those incurred by the bank when the FX trade is executed. This practice has resulted in the banks reaping enormous profits at their clients' expense. To date, three whistleblower (or *qui tam*) actions alleging improper FX trading practices at custodial banks have been unsealed. Two class actions, including one filed by Kessler Topaz, have also been filed against custodial banks. Additionally, several other funds (including ones in Ohio and Massachusetts) have publically claimed to have been victimized by custodial banks that charged excessive FX rates.[1] Additionally, the Securities and Exchange Commission ("SEC") recently began investigating BNY Mellon's and State Street's FX related disclosures to their custodial clients.

The first *qui tam* action to be unsealed against a custodial bank, *The People of the State of California v. State Street Corp., et al.*, alleged that State Street overcharged California's state pension funds by manipulating FX rates.[2] State Street then disguised its conduct by entering false FX rates into State Street's reporting system and then supplying the pension funds with reports that lacked time stamps. The other two *qui tam* actions, one in Virginia and one in Florida, made similar allegations against BNY Mellon.[3]

Separate from the government actions, two class actions have also been filed. First, in February 2011, the Arkansas Teacher Retirement System filed a class action complaint against State Street.[4] Second, Kessler Topaz, representing the Southeastern Pennsylvania Transportation Authority ("SEPTA"), filed a class action against BNY Mellon.[5]

These recent actions and investigations have alerted pension and retirement funds that their custodial bank may have been using FX operations to secretly profit at their expense. As alleged in these actions, the use of manipulated FX rates and fabricated trading reports has effectively concealed the hidden losses custodial clients have been suffering for several years.

More information on this topic may be found on the PAPERS website at: http://www.papers.org/newweb/documents/ForeignExchangeTrading-SecretProfitsandHiddenLosses.pdf.

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[1] *See* Carrick Mollenkamp, *New Front Opens in Massachusetts for Forex Dispute,* THE WALL STREET JOURNAL (June 14, 2011); and Dan McCrum, *Forex practiced under scrutiny in Ohio,* FINANCIAL TIMES (June 15, 2011).

[2] *The People of the State of California v. State Street Corp., et al.*, Case No. 34-2008-8457-CU-MC-GDS, p. 2 (Cal. Superior complaint in intervention filed Oct. 20, 2009).

[3] *Commonwealth of Virginia, ex rel. FX Analytics v. The Bank of New York Mellon Corp.*, No. CL-2009-15377 (Va. Cir. unsealed Jan. 21, 2011); *State of Florida, ex rel. FX Analytics v. The Bank of New York Mellon Corp*., No. 2009-ca-4140 (Fla. Cir. unsealed Feb. 7, 2011).

[4] *See Arkansas Teacher Retirement System v. State Street Corp., et al.*, Case No. 11-cv-10230 (D. Mass. Feb. 2, 2011).

[5] *See Southeastern Pennsylvania Transportation Authority v. The Bank of New York Mellon Corp.*, Case No. 11-cv-1628 (E.D. Pa. Mar. 7, 2011).

MARKET INSIGHTS: TIPS May Not Address Investors' Inflation Concerns

By: Zane Brown, Lord Abbett Partner and Fixed Income Strategist

As the number of policies aimed at reviving economic growth have mounted, so too have investors' concerns that these measures might culminate in a disruptive level of inflation. Yet, those seeking protection against inflation should be aware that the adjustment on Treasury Inflation-Protected Securities (TIPS) occurs to the principal amount, not to the coupon. And TIPS coupons already are among the lowest in the fixed-income universe since they do not include a premium for future inflation expectations because the principal adjusts for inflation.

As a result of the securities' low, fixed coupons, TIPS investors could find themselves with less income than they expected in an environment of rising prices, and potentially exposed to the accompanying risks from rising interest rates. A theoretical scenario in which the Consumer Price Index (CPI) rises by 2% next year shows how this dynamic could occur. Investors owning a $1,000 TIPS issue with a 1% coupon may expect that their 1% coupon would be adjusted by the CPI rate of 2% to give them a 3% coupon, which would theoretically provide annual interest of $30.00.

Instead, what actually would happen is that the principal would adjust from $1,000 to $1,020, and the 1% coupon on this TIPS issue would increase the annual interest payment, but only by 20 cents—from $10.00 to $10.20. This may be an unpleasant surprise to income-seeking investors who mistakenly expected an increase to $30.00.

The low level of income also compromises investors' ability to take advantage of rising interest rates. If rates rise and bond prices fall, the TIPS investor described above has only $10.20 in annual interest payments to reinvest in lower-priced, high-yielding securities. Conversely, securities with higher coupons could provide investors with more cash to reinvest in an environment of rising interest rates.

Given these characteristics, TIPS could exhibit unexpected price volatility, including a declining market value, if interest rates are expected to rise. This occurred in 2010, when the market value of a recent 10-year TIPS issue ranged from a discount of $972 to a premium of $1,099.

Finally, each year that the principal of a TIPS issue increases, that amount is taxed as current income, even if an investor intends to hold the issue until maturity. The principal also can adjust downward if the CPI turns negative in a deflationary environment, although the issue would still mature at least at par, even if it were previously trading at a discount. Investors seeking to realize inflation-adjusted income while reducing interest-rate risk may want to look past TIPS, to other inflation-focused investments in order to address their inflation concerns.

Important Information: The Consumer Price Index (CPS) measures the price changes for each item in a predetermined basket of goods and services, and the inputs are weighted according to their importance to consumers. Treasury Inflation Protected Securities (TIPS) are treasury securities that are indexed to inflation in order to protect investors from the negative effects of inflation. TIPS are backed by the U.S. government and their par value rises with inflation, as measured by the Consumer Price Index, while their interest rate remains fixed. Interest on TIPS is paid semiannually.

A Note about Risk: The value of investments in fixed-income securities will fluctuate in response to market movements. When interest rates rise, the prices of fixed-income securities are likely to decline, and when interest rates fall, the prices of debt securities tend to rise. No investing strategy can overcome all market volatility or guarantee future results.

National Institute on Retirement Security
1730 Rhode Island Avenue, NW
Washington, DC 20036
202.457.8190

NEW STUDY IDENTIFIES KEY FEATURES OF WELL-FUNDED PUBLIC PENSION PLANS

For Pensions Examined, Funding Policy, Benefit Design, and Economic Assumptions Critical Elements for Weathering Market Turmoil

JUNE 29, 2011, Washington, D.C. - A new research report released today by the National Institute on Retirement Security examines selected statewide defined benefit public pension plans to identify common elements of plans that remained well funded despite two severe economic downturns. The study identifies six features that enabled those plans examined to remain sustainable and affordable:

- Employer pension contributions that pay the full amount of the annual required contribution (ARC), and that maintain stability in the contribution rate over time;
- Employee contributions to help share in the cost of the plan;
- Benefit improvements, such as multiplier increases, that are actuarially valued before adoption and properly funded upon adoption;
- Cost of living adjustments (COLAs) that are granted responsibly, for example through an ad hoc COLA that is amortized quickly, or an automatic COLA that is capped at a modest level;
- "Anti-spiking" measures that ensure actuarial integrity and transparency in pension benefit determination; and
- Economic actuarial assumptions, including both the discount rate and inflation rate, that can reasonably be expected to be achieved over the long term.

These findings are contained in the new study, "*Lessons from Well-Funded Public Pensions: An Analysis of Six Plans that Weathered the Financial Storm.*" The report was led by Dr. Jun Peng, associate professor at the University of Arizona, and co-authored by Ilana Boivie, an economist and NIRS director of programs.

"Unfortunately, scant attention is focused on public pension plans that were structured in ways that enabled them to weather severe market turmoil," said Diane Oakley, NIRS executive director. "Separate from this study, data show that the vast majority of public pensions were well-funded going into the financial crisis, took a severe blow like all investors, and are recovering as the financial markets rebound. As such, we hope this new study serves to re-focus pension policy debate on a productive, pragmatic examination of pension plans that remained strong even after a decade of unprecedented financial market ups and downs," Oakley said.

Ilana Boivie, NIRS director of programs added, "This new analysis can serve as a valuable tool for policymakers working to strengthen public pensions so the plans can continue to keep their retirement commitment to millions of working Americans at the lowest cost to taxpayers." Boivie added, "It's important to note, however, that these six common features are NOT a 'one-size-fits-all' approach. Every pension plan is unique, and so too is their funding policy, benefit design, and economic assumptions. All six well-funded plans we studied remained sound even though their approaches may have differed."

The study was conducted via a comprehensive analysis of the funding policy, benefit design and economic assumptions for the following six public pension plans selected for analysis:

- Delaware State Employees Pension Plan
- Idaho Public Employee Retirement Fund
- Illinois Municipal Retirement Fund
- New York State Teachers' Retirement System
- North Carolina Teachers & State Employees Retirement System
- Teacher Retirement System of Texas

The full report is available at www.nirsonline.org.

About NIRS

The National Institute on Retirement Security is a not-for-profit, non-partisan organization established to contribute to informed policymaking by fostering a deep understanding of the value of retirement security to employees, employers, and the economy through national research and education programs. Located in Washington, D.C., NIRS has a diverse membership of organizations interested in retirement security including financial services firms, retirement plan sponsors and service providers, and trade associations among others. More information is available www.nirsonline.org.

Morrison: A Year Later

By Andrew D. Abramowitz
Spector Roseman Kodroff & Willis, P.C.

Last fall, I wrote in this newsletter about the Supreme Court's decision in *Morrison v. National Australia Bank*, the seminal case that essentially excludes from participation in U.S. class actions any securities purchased on a foreign exchange. The Supreme Court found that what is important in determining whether a fraud that touches foreign soil should be litigated in U.S. courts is whether there has been a purchase or sale of a security on a U.S. exchange (as opposed to where the fraudulent conduct took place).

It has now been a year since that June 2010 opinion was issued. The sky has not quite fallen, but in the past year, it has only grown more apparent how drastic an impact *Morrison* has had, and will continue to have, on efforts by investors – including public pension funds – to recover lost monies under the federal securities laws. The subject is far from stale, as it routinely reaches the agendas of investing and pension conferences across the country (and abroad).

What seems more likely than ever is that investors with holdings in foreign companies may need to look overseas to find recourse in instances of fraud. It is now a matter of having no meaningful alternative. The availability of recovery under non-U.S. legal systems continues to develop, and includes such countries as Australia, Belgium, Canada, and The Netherlands. A notable example is the *In re SCOR Holding (Switzerland) AG Securities Litigation* (formerly *In re Converium Holding*). In that case, in addition to claims litigated in federal court in New York, the parties reached a settlement on behalf of non-U.S. investors that is being adjudicated before the Court of Appeals in Amsterdam under a specific Dutch statute. The Netherlands is an investor-friendly jurisdiction, and given what has been accomplished thus far in the *SCOR* case, it is likely that more U.S. investors will be able to obtain recoveries there now that *Morrison* has severely narrowed the types of cases that can be brought in U.S. courts.

The reality is that investing in multi-national corporations is more prevalent now than ever; the *Morrison* decision will not change that. But as we have seen on numerous occasions, foreign companies are as prone to fraud as U.S. ones. Accordingly, U.S. investors will need to evolve and start looking across our borders with increasing frequency to accomplish what is no longer available in the states.

GASB Proposes Major Improvements for Pension Reporting

GASB has issued two Exposure Drafts proposing improvements to financial reporting of pensions by state and local governments, specifically, to improve how the costs and obligations associated with the pensions that governments provide to their employees are calculated and reported. The deadline for submitting written comments is September 30, 2011. The Exposure Drafts, including instructions on how to submit written comments, are available for download at:

Accounting and Financial Reporting for Pensions—an amendment of GASB Statement No. 27 – primarily relates to reporting by governments that provide pensions to their employees.

Financial Reporting for Pension Plans—an amendment of GASB Statement No. 25 – addresses the reporting by the pension plans that administer those benefits.

Pension Accounting and Financial Reporting ♣

Investing in Emerging Markets:
Local Opportunities and Risks

By: Conrad Saldanha, Portfolio Manager, Emerging Market Equities, Neuberger Berman

I recently wrote a research paper that discusses the factors and trends that are driving growth in emerging markets and includes an analysis of the potential opportunities and risks associated with investing in emerging market companies. In this summary, I share some of our key views and findings.

Investors seek exposure to emerging markets for their potential for above-average economic growth, which is typically associated with stronger earnings growth and higher stock returns. To be sure, growth of emerging market economies over the past decade has been impressive, exceeding that of the developed world. Within emerging markets, the most compelling investment opportunity, I argue, can be found at the local level, where companies with a strong domestic position may benefit from a growing consumer base and rising disposable income.

Our research sought to identify how the share prices of companies serving a rapidly growing middle class have performed in recent years and what returns might look like going forward. To do this, we separated emerging market companies into two categories—those whose end markets are primarily global and those who target local needs. A comparison of the two groups reveals that the average market capitalization of local companies is smaller than that of globally focused emerging market companies. However, we believe locally driven emerging market companies may enjoy superior growth rates, and given that they are trading at only a slight premium in terms of price-to-earnings ratio, in our opinion, they present an attractive investment opportunity.

It is important to note that companies at the smaller market capitalization level present certain risks, including liquidity issues, family or entrepreneurial control, transparency and auditor quality concerns. We believe there are ways to mitigate these risks with careful bottom-up due diligence and adequate diversification.

We feel that identifying those firms that are well positioned for growth, regardless of size, and combining the resulting ideas into a portfolio that manages risk, should be an important component of emerging market investing in the years ahead.

To read more on this subject, you can access the full research document on the PAPERS website at: http://www.pa-pers.org/newweb/documents/InvestinginEmergingMarkets-LocalOpportunitiesandRisks.pdf .

Rise of the Emerging Market Consumer

By: Curtiss Scott, CFA (left) & William O'Connor , CEBS (right) - Todd Veredus Asset Management

Middle class consumers in the US and other large developed economies have been a key source of demand in the global economy for the past 50 years. However, a new middle class consumer has grown significantly in the emerging market, especially Asia. This new global middle class will provide competition for labor and resources, but also enormous opportunities for providing consumer goods and services.

There is no universal definition for what constitutes the middle class due to varying income levels between advanced and emerging market economies. For the purposes of this article we will use the Organization of Economic Co-operation and Development (OECD) definition of 'all those households with daily per capita incomes between $10 and $100 per day, adjusted for local purchasing power'. As a result of the recent global financial crisis, households in the developed world are being forced to rethink their debt loads and spending patterns while those in the emerging markets are moving in the opposite direction. These consumers are in the early stages of their credit cycle and will have greater flexibility for consumption growth.

The OECD in January 2010 published a paper on the emerging market consumer and disclosed that the size of the global middle class may increase from the current 1.8 billion people to 3.2 billion in 2020 with a rise to 4.9 billion in 2030. Eighty five percent of this increase is expected to come from Asia (China, India, and Indonesia).

Importantly, growth in purchasing power of this middle class will rise from $21 trillion to $56 trillion by 2030. As highlighted in the table below, over 80% of the growth in demand comes from Asia. The bulk of this will come from two countries: China and India. In 2009 those two nations comprised over 5% of global middle class consumer spending. In 20 years it will increase to 41%. Optimists will point out that Asian consumers may substitute for US consumers. Simply, Asia could be large enough to offset the stagnant purchasing power most analysts see in the develop world.

Spending By Global Middle Class 2009-2030

($ millions)

	2009		2020		2030	
North America	5602	26%	5863	17%	5837	10%
Europe	8138	38%	10301	29%	11337	20%
Central & South America	1534	7%	2315	7%	3117	6%
Asia Pacific	4952	23%	14798	42%	32596	59%
Sub-Saharan Africa	256	1%	448	1%	827	1%
Middle East & North Africa	796	4%	1321	4%	1966	4%
World	21278	100%	35045	100	55680	100%

Source: OECD (1/2010)

The staggering rise in the middle class of the emerging market economies presents immense opportunities for global multinational companies that offer goods and services. YUM! Brands (KFC, Pizza Hut and Taco Bell) have increased their exposure to emerging markets to 50% from 10% in 2000. Other consumer brand name companies from Coca Cola, Coach, Nike, as well as, infrastructure entities such as Caterpillar, Deere and General Electric will be beneficiaries of this growing emerging market consumer.

In all, robust growth is projected in healthcare (pharmaceuticals), education, recreation, communications (mobile phones, pc, internet), autos, personal care products and financial services.