PAPERS

Pennsylvania Association of Public Employee Retirement Systems
PO Box 61543, Harrisburg, PA 17106-1543
Website: *www.pa-pers.org*

Winter 2010 (Vol. 5, No. 1)

In This Issue

If you're interested in overnight lodging for the Forum

Harrisburg Hilton
One North Second St
Harrisburg, PA

The 6th annual PAPERS Forum will begin with breakfast on Thursday, May 20, 2010 and continue through early afternoon on Friday, May 21.

PAPERS has arranged a special room rate for attendees at the Forum who desire overnight lodging on May 19th and/or 20th. The group rate of $124 per night can only be guaranteed if reservations are made on or before April 15, 2010.

To make room reservations on-line, use the following link: http://www.hilton.com/en/hi/groups/personalized/MDTHHHF-PAP-20100519/index.jhtml?WT.mc_id=POG

To make room reservations by phone, please call the Harrisburg Hilton at 717-237-6434 and ask for group code PAP (PA Assn of Public Employee Retirement Systems).

Announcing the 6th Annual

PAPERS Forum

The PAPERS Forum returns May 20-21, 2010 to the Harrisburg Hilton on Market Square in downtown Harrisburg. The hotel is conveniently located at One North Second Street just steps away from "Restaurant Row".

Who Should Attend:

- Pension Fund Staff and Board of Trustees
- Public Pension Investment Officers, Portfolio Managers
- Investment Consultants, Asset Managers, Banks, Other Pension Service Providers

Why You Should Attend:

- Learn how other pension fund executives are strategizing for the coming year to deal with the current economic turmoil.
- Enjoy a highly interactive and educational program specifically tailored for institutional investors in Pennsylvania.
- The Forum brings together nearly 200 attendees from Pennsylvania's public pension plans and asset managers in one location.
- Meet your peers, hear their firsthand experiences and share your ideas.
- Network with asset managers, service providers, consultants and asset managers.
- Take advantage of the panelists' presentations provided in the conference hand-out materials.
- Analyze various potential innovative investment opportunities available to pension funds.
- Obtain Continuing Professional Education credits

The tentative agenda can be found inside on pages 4-6 and the conference registration form is on page 7. You may also access all this information on the PAPERS website (www.pa-pers.org).

From the PAPERS Executive Director

The date for the 2010 PAPERS Forum is fast approaching. We have put together an excellent educational program that will help to address the issues that are on most of your minds this year. The economic turmoil and liquidity crisis has placed a huge burden on the budgets of all pension plans across the Commonwealth. If we all work together sharing ideas and analyzing possible solutions, we can come out of these troubled times with stronger asset allocations and better funding plans for our members.

One of the best ways to say on top of issues that could affect your Pension Plan is to attend the PAPERS Annual Forum and Fall Workshop. These programs provide you with excellent opportunities to hear from industry professionals and to interact with your peers around the state. It is important that you are aware of developing issues so you can formulate your own positions on the various issues that may affect your pension plan.

As a member of PAPERS you are eligible to receive weekly news updates from Public Pensions Online (PPOL). PPOL updates are a quick and easy way to keep informed about what is happening in the industry. To receive your own copy of the PPOL Update, go to: **www.publicpensionsonline.com/registration.html** and register to receive the weekly News Updates. It is free for PAPERS members. If any of these articles peak your interest and you would like to know more about these subjects drop me an email and I will try to help you explore these issues more thoroughly.

Thank you for participating in PAPERS and I hope that you find the organization helpful in your efforts to be a better guardian of your member's pension benefits. I look forward to seeing you at the 6th Annual PAPERS FORUM on May 20-21, 2010 at the Hilton in downtown Harrisburg.

Jim Perry
PAPERS Executive Director

Special Thanks to our Sponsors

(as of 2/26/2010)

Sponsors provide financial support beyond regular conference registration fees. Additional sponsorship opportunities for the 2010 PAPERS Forum are still available. Contact PAPERS Executive Director Jim Perry *(717-651-0792 or perryja1@comcast.net)* today for more details about the various levels of support your company can provide.

Sponsorship Levels

Gold................................$5,000

- Named sponsor of meal function
- 4 complimentary registrations
- Recognition in program
- Complimentary exhibit space

Silver Exhibitor.................................$3,000

- 2 complimentary registrations
- Recognition in program
- Complimentary exhibit space

Silver..$2,500

- 2 complimentary registrations
- Recognition in program

Gold Sponsors

- **Barroway Topaz Kessler Meltzer Check, LLP**
  280 King of Prussia Rd
  Radnor, PA 19087
- **Federated Investments**
  1101 Liberty Ave
  Pittsburgh, PA 15222
- **Nomura Asset Management**
  Two World financial Center, 22nd 1101
  New York, NY 10281-1712

Silver Exhibitors

- **Renaissance Capital LLC**
  Two Greenwich Plaza
  Greenwich, CT 06830
- **The Bank of New York Mellon**
  500 Grant St
  Pittsburgh PA 15258

Silver Sponsors

- **Biondo Investment Advisors LLC**
  PO Box 909
  Milford, PA 18337
- **Cheevers & Company, Inc.**
  440 S. LaSalle Street, Suite 700
  Chicago, IL 60605
- **Gabriel, Roeder, Smith & Company**
  One Towne Square, Suite 800
  Southfield, MI 48076-3723
- **Lord, Abbett & Co.**
  90 Hudson St
  Jersey City NH 07201
- **Neuberger Berman**
  605 Third Avenue, 3rd Fl
  New York, NY 10158

Directions to Harrisburg and the 2010 Forum

From New York/ New Jersey

Take the George Washington Bridge to I-80 West, take 287 South to I-78 West to I-81 South, Exit 66. Take Front Street south approximately 5.5 miles to Market Street. Turn left onto Market Street; the hotel entrance is one block on the left just after crossing Second St.

From Philadelphia

Take PA Turnpike 76 West, get off at Exit 247, take I-283 North to I-83 south to Exit 43 (Second Street-Capitol complex). At the fourth traffic light, turn right onto Market Street and the hotel entrance is on the left.

From Baltimore/Washington

Take I-83 North to Exit 43 (Second Street-Capitol complex). At the fourth traffic light, turn right onto Market Street and the hotel entrance is on the left.

From Pittsburgh

Take PA Turnpike 76 to Exit 242, Take I-83 north to Exit 43 (Second Street-Capitol complex). At the fourth traffic light, turn right onto Market Street and the hotel entrance is on the left.

Parking - To access the Walnut Street Parking Garage connected to the Hilton Hotel, travel on Market Street just past the hotel, turn left onto Court Street and follow the signs to enter the garage.

2010 PAPERS Forum Agenda

Agenda Subject to Change; Final Agenda will be Distributed at Forum

Wednesday, May 19, 2010

7:00 p.m. .... CONFERENCE REGISTRATION – Closes at 8:30 p.m.

Thursday, May 20, 2010

7:00 a.m............. CONFERENCE REGISTRATION

7:30 a.m............. CONTINENTAL BREAKFAST - Entertainment by the Central Dauphin High School Jazz Band

8:15 a.m............. WELCOME from the PAPERS Board

KEYNOTE ADDRESS – *UNDERSTANDING YOUR FIDUCIARY DUTIES IN THESE TOUGH TIMES*
Presenter: ***Eugene F. Maloney***, Federated Investments Executive Vice President & Corporate Counsel

Mr. Maloney will explain the concept of a process-driven approach to due diligence. He will also discuss and describe the different roles an intermediary can occupy in providing an investment menu with an emphasis on integrating non-traditional assets or asset classes (i.e., hedge funds, private equity, etc.) into a well-diversified portfolio.

9:00 a.m............. HEDGE FUND PANEL – *WHERE THEY HAVE BEEN & WHERE THEY ARE GOING*
Moderator: ***Tom Brier***, State Employees' Retirement System Director of Alternative Investments
Panelists: SERS General Consultant and a Hedge Fund Manager

The panel will discuss Hedge Fund investing with a macro view. They will discuss some of the different ways investors use Hedge Strategies to achieve different objectives whether it is for the purpose of purely diversifying risk or to achieve other goals within an asset class. They will also address some of the changes expected in the regulatory arena and other dynamics affecting the industry – such as the potential effect of the Volker Rule (requiring that commercial banks exit the HF business) will have in creating more opportunities for them.

10:00 a.m............. WHIP-SAWED – TWO ROLLER COASTER YEARS IN HIGH YIELD & THE MARKET OUTLOOK
Presenters: ***Mark Meyer***, Nomura Asset Management Head of Institutional Business Development
David Crall, Nomura Asset Management Corporate Research Chief Investment Officer

The presenters will review the 2008 sell-off and the 2009 rally in high yield securities and the underlying reasons for these massive market moves. An investment outlook for the high yield market in 2010 and beyond will also be reviewed for the audience.

10:45 a.m............. REFRESHMENT BREAK

11:00 a.m............. EQUITY INVESTING: A LONG-TERM VIEW FROM THE GLOBAL PERSPECTIVE
Presenter: ***Joseph Biondo, Jr.***, The Biondo Group Chief Investment Officer

11:45 a.m............. READY FOR ANOTHER SURPRISE FROM GASB?
"Market Value of Liabilities: What You Need to Know"
Speaker: ***David Kausch***, Gabriel, Roeder, Smith & Co.

Interested in higher and more volatile pension costs? The Governmental Accounting Standards Board (GASB) is currently reviewing accounting Statements Nos. 25 and 27 to see if, where, and how MVL would fit in to public sector pension accounting. The differences between MVL and AAL may come as an unpleasant surprise to the public sector potentially increasing costs and introducing more volatility. Just what are those differences and what would the impact to your system and your sponsoring government be using MVL? Find out what you need to know.

12:30 p.m. .... LUNCHEON - Sponsored by: ***Nomura Asset Management, USA***
Speaker: ***Vice Chairman, U.S. House of Representatives Committee on Pensions***

(continued on page 5)

1:15 p.m. .... TWO CONCURRENT TRACKS OF PRESENTATIONS

	TRACK A **ROLE OF ACTIVE MANAGEMENT IN PENSION RISK AND INVESTMENT MANAGEMENT**	**TRACK B** **ROLE OF INDEXING IN PENSION RISK AND INVESTMENT MANAGEMENT** Moderator for all Sessions: ***Albert Neubert***
1:15 p.m.	**CURRENT STATUS OF THE GLOBAL REAL ESTATE MARKET** Presenter**:** ***Todd Briddell,*** Urdang Investment Advisors	**LUCK vs. SKILL – WHAT CAN PENSION FUNDS LEARN FROM THE EVIDENCE?** *We will examine the latest findings of Fama & French and the impact of trading costs and management fees. We will examine the evidence to determine if can you identify good active management performance and poor active management in advance. Finally we discuss what sort of process should be used to select active managers including incorporating risk in the equation.*
2:00 p.m.	**NO COUNTRY (ALLOCATION) FOR OLD MEN: RATIONAL EXPECTATIONS FOR NON-U.S. INVESTMENT STRATEGIES** Presenter: ***Erik Gosule*****,** D.E. Shaw Product Specialist *This presentation briefly outlines a case for rethinking the return expectations of active non-U.S. equity strategies. Country selection appears to have been a major driver of outperformance in active non-U.S. equity strategies throughout much of the 1980s and 1990s.*	**SHOULD EXCHANGE TRADED FUNDS HAVE A PLACE IN YOUR FUND?** *The presenter will do a quick review of ETFs and the current ETF landscape. Then try to determine if small pension funds should consider all-ETFs portfolios. We will explore how large pension funds use ETFs.*
2:45 p.m.	**OPPORTUNITIES IN THE IPO MARKETS** Presenter: ***Kathleen Shelton Smith*****,** *Renaissance Capital Founder & Chairman* *This session will focus on the unique attributes of IPOs and highlight the benefits of incorporating IPOs in the asset allocation strategy, with a focus on diversification, liquidity and transparency. The presenter will also address the current state of the IPO market, provide insights into IPO performance in environments of low and high issuance volume, and discuss the outlook for IPOs for the remainder of 2010 and beyond.*	**INDEXING IN VOLATILE AND BEAR MARKETS** *Here we will discuss if indexing works in Bear Markets? Are there indexing strategies that can take advantage of market volatility? Does fixed income indexing make more sense now than ever before? Do risk adjusted returns become more variable for active managers versus index funds in the environment we are currently experiencing?*
3:30 p.m.	**Refreshment Break**	
3:45 p.m.	**DO TIPS MAKE SENSE IN THIS ENVIRONMENT?** Presenter: ***Tom Marthaler***, Neuberger Berman	**THE ONGING DEBATE IN THE ARGUMENT OF PASSIVE vs. ACTIVE MANAGEMENT** Presenter: Vanguard *The presenter will attempt to answer these questions. Does indexing work in inefficient markets, and how do we define inefficiency? Does more indexing create the opportunity for lower fees in active management? Does it make sense to time the market in terms of active or passive management? Has the proliferation and improvement of benchmark technology affected passive and active management?*

5:30 p.m. .... COCKTAIL RECEPTION - Sponsored by: **Federated Investment**

(continued on page 6)

2010 PAPERS Forum Agenda

Agenda Subject to Change; Final Agenda will be Distributed at Forum

Friday, May 21st

7:00 a.m............. CONFERENCE REGISTRATION

7:30 a.m. .... CONTINENTAL BREAKFAST

8:30 a.m............. DEALING WITH THE FUNDING GAPS THAT WE ALL NOW FACE
Moderator: ***Michael Shone*****,** Peirce Park Group

Panelists will discuss the impact of the market declines of the past two years on the funded status of their pension plans and talk about what measures they are taking to address these issues. They will explore different strategies to insure the long term viability of the Plans and look at the implications for their futures budgets.

9:15 a.m............. A REVIEW OF THE LATEST DEVELOPMENTS IN CORPORATE GOVERNANCE
Presenter: ***Darren Check***, Barroway Topaz Kessler Meltzer & Check, LLP

Corporate governance and what it means to a public retirement system; Shareholder rights and the power of proxy voting; Legal rights when prudent investments are caught in a web of fraud; Remediation and recouping damages

9:00 a.m............. FRAUD DETECTION AND PREVENTION
Moderator: ***Don Halke***, Public School Employees' Retirement System Internal Auditor
Presenter: ***Jim Downing***, Cheevers & Company, Inc. Chief Compliance Officer

Join us for a discussion on why fraud occurs and how to prevent and detect fraud in the workplace. The presentation explores commonalities often existent in fraud, risk analysis, internal controls, essential methods of fraud prevention, employee & management awareness, and fraud detection techniques.

9:45 a.m............. REFRESHMENT BREAK

10:00 a.m............. PANEL DISCUSSION: DISABILITY RETIREMENT ADMINISTRATION
Moderator: ***Joauna Riley***, City of Philadelphia Board of Pensions & Retirement

The panel will discuss the nuts and bolts of disability eligibility determination and talk about the different methods they use to properly certify participants for disability benefits. They will also discuss some of the methods they use to follow-up on ongoing claims.

10:45 a.m............. IS THE IRS COMING TO A PENSION PLAN NEAR YOU?
Moderator: ***Joauna Riley***, City of Philadelphia Board of Pensions & Retirement
Presenter: ***John Nixon, Esq***., Duane Morris

11:30 a.m............. FUNDAMENTALS OF INVESTING
Presenter: ***Eric Smith,*** Consulting Services Support Corporation Chairman & Chief Executive Officer

12:30 p.m. .... LUNCHEON - Sponsored by: ***Barroway Topaz Kessler Meltzer & Check, LLP***

1:30 p.m. .... TRUSTEE EDUCATION/CERTIFICATION PROGRAM
Presenter: ***Peter Hapgood,*** SPOON Executive Director

This session is designed to explain the Trustee Certification program that will be offered by PAPERS to help Trustees improve their understanding of the responsibility they have as a Trustee and to help them develop skills to better exercise their fiduciary duty.

2:30 p.m. .... 6th ANNUAL PAPERS FORUM CONCLUDES

See you at the PAPERS Fall Workshop on Thursday, September 23, 2010, at The Desmond Hotel & Conference Center in Malvern, PA. Watch for details later this summer.

Registration for 6th Annual PAPERS Forum

May 20-21, 2010 at Hilton Hotel in downtown Harrisburg, PA

Each individual must complete a separate registration form. Please check appropriate category:

- ❑ ***Pension Plan Representatives*** – Current (2010) PAPERS Participating Membership required
  - o First individual from pension plan – complimentary
  - o Each additional individual - $75
- ❑ ***Service Provider Representatives -*** Firms providing investment management and legal services Current (2010) PAPERS Associate Membership required
  - o Each individual from organization - $750
- ❑ ***Service Provider Representatives -*** Firms providing consulting services, exclusive of investment/legal Current (2010) PAPERS Affiliate Membership required
  - o Each individual from organization - $375
- ❑ **Speaker/Presenter/Moderator**
- ❑ **Gold Sponsors**
  - o Four complimentary registrations
  - o Each additional registration - $750
- ❑ **Silver Sponsors & Silver Exhibitors**
  - o Two complimentary registrations
  - o Each additional registration - $750

Individual's name ____

Preferred name for name tag ______________________________________

Representing (name of pension plan or service provider) ______________________

Mailing address ____

City, State, Zip ____

Telephone number (_____) _____-________ E-mail address ______________________

Please indicate all Forum events that you plan to attend. This information is needed so arrangements for adequate seating & meals can be made.

Thursday, May 20, 2010
- ❑ Continental breakfast
- ❑ Morning sessions
- ❑ Lunch
- ❑ Afternoon sessions
- ❑ Cocktail reception

Friday, May 21, 2010
- ❑ Continental breakfast
- ❑ Morning sessions
- ❑ Lunch
- ❑ Afternoon sessions

Please complete and return this form no later than May 1, 2010. Full payment of any fees due must be included with this registration.

You may pay the registration fee either by check or electronically through PayPal.

1. ***To pay by check.*** Please make check payable to: **PAPERS** and return with this application to: **PAPERS, P.O. Box 61543, Harrisburg, PA 17106-1543**

2. ***To use PayPal.*** Please access the PAPERS website (www.pa-pers.org) and click on "Spring Forum". Select the appropriate type of registration from the drop down box and follow the directions to have PayPal transfer the applicable fees automatically from your bank account to PAPERS. Your completed conference registration may either be mailed to: ***PAPERS, PO Box 61543, Harrisburg, PA 17106-1543*** or scanned, saved and e-mailed to: ***douglas.b@verizon.net.***

Group rates for overnight lodging reservations at the Hilton guaranteed only through 4/15/2010.

Fed Up? The Effects of a Rate Rise

By: Milton Ezrati, Lord Abbett

The picture is fairly clear:
The market will welcome rate hikes if they are gradual and today's steep yield curve will flatten from the short end.

As investors, commentators, and even the Federal Reserve itself anticipate a policy shift to draw down excess liquidity in markets, there is much talk of interest rate increases and their impact on markets. Frustratingly, the historical picture of past responses to Fed rate hikes is far from consistent. Each event occurred within a very different context. Still, the picture for 2010 is reasonably clear. If rate increases occur gradually, as is probable, they should receive a welcome in markets, a way to stem the longer-term inflationary pressure implicit in past emergency liquidity injections. That sort of a welcome will likely foster stability among longer bond maturities even as short rates rise or even muster a modest rally. Today's steep yield curve, in other words, will likely flatten from the short end.

Table 1 gives a good idea of how context shaped very different responses to the last three Fed rate increases: during the 15 months from January 1994 to April 1995, during the 14 months from May 1999 to July 2000, and during the 33 months from May 2004 to February 2007:

- The first incident was the most intense. It came in the middle of an economic expansion and in response to an inflation scare—an issue that had tremendous market power at the time, since memories of the great inflations of the 1970s and early 1980s were still relatively fresh. The Fed moved quickly, pushing the fed funds rate up 300 basis points (bps) within that rather compressed time frame, averaging 20 bps in hikes per month. Bonds clearly suffered capital losses during the tightening, though their high current yields—over 9.0% on 'Baa' corporates, for instance—kept total returns positive. The Fed's sudden reversal of policy later in 1995 promoted strong subsequent bond returns.
- The second bout of rate increases was much less intense, but the hikes shocked markets nonetheless, coming, as they did, in a sudden reversal from a previous easing policy. Though the pace at which the Fed raised rates was much slower than in the 1990s, the sudden turn clearly produced significant capital losses in bonds.
- The most recent incident (2004–07) was very different. Though the cumulative rate hikes exceeded the prior two times, they unfolded over a much longer time frame so that the pace at which rates rose was far from intense. Neither was the market shocked. Policy before the tightening had remained relatively stable, and the fed funds rate moved off what then seemed like a very low base of 1.0%. The Fed had also thoroughly advertised its tightening policy. Indeed, the poor performance of the Barclays Capital U.S. Aggregate Bond Index[1] in the prior 12 months speaks to the market's anticipation of these rate hikes. All this permitted relatively good returns to bonds during the period of increasing short-term rates.

Anticipating this next round of rate increases, probably commencing during the second half of this year, there are more similarities with 2004–2007 than with the earlier incidents. The move has been widely advertised and is widely expected. Rates also are coming off extremely low levels, with the fed funds rate presently at only 25 bps. Neither is there an inflation scare, at least not an immediate one. So far, all measures of inflation have remained subdued. Longer-term inflation concerns have grown, but a Fed action to raise rates as part of a plan to withdraw excess liquidity should ameliorate such concerns and perhaps allow some longer yields to decline even as the Fed raises short-term rates and forces up shorter intermediate rates in the process, a pattern that clearly also occurred as short rates rose between 2004 and 2007.

(continued on page 9)

Fed Up? The Effects of a Rate Rise

(continued from page 8)

Intermingled with this picture of Fed policy and its effects, fixed-income markets going into the second half of 2010 also will see the effects of a continued unwinding of the flight to quality that so dominated 2008 and early 2009. Even at this date, the legacy of that fear has kept Treasury yields low and credit spreads wide by historical standards, though they are well in from their widest in late 2008/early 2009. Under the influence of this continued unwinding, long Treasury yields may well rise, even as relief from inflation fears brings down yields on longer-term, credit-sensitive corporate and municipal bonds. If the confluence of these considerations prevents yield declines in corporates and municipals, it should promote stability in such credit-sensitive yields even as Treasury yields rise all along the curve.

It would be easy to know exactly what will happen if all past incidents of Fed rate increases had a uniform market response. But even though the historical record presents relationships that are far from mechanical, the picture at present is nonetheless relatively clear, at least on how fixed-income markets will likely respond to the expected Fed policy change.

Table 1. Bond Returns—Three Most Recent Periods of Fed Rate Hikes

	January 1994–April 1995			May 1999–July 2000			May 2004–February 2007		
	12 Mos. Previous	During	12 Mos. Following	12 Mos. Previous	During	12 Mos. Following	12 Mos. Previous	During	12 Mos. Following
Cumulative rate move (bps)	+3	+300	-83	-75	+180	-277	-26	+426	-228
Basis points per month	+0.25	+20	-6.9	-6.25	+12.9	-23	-2.2	+12.9	-19
Return Barclay's Aggregate[1] (%)	9.75%	1.36%	12.25%	6.27%	1.21%	13.12%	1.82%	6.11%	6.12%
Return, High Yield	16.69	3.57	17.39	3.23	-3.98	3.72	14.74	15.66	11.73

Source: Federal Reserve Board.

[1] I would like to thank Mike Weldon, Lord Abbett Director of Marketing, for suggesting this line of analysis.

[1] The Barclays Capital U.S. Aggregate Bond Index represents securities that are U.S. domestic, taxable, nonconvertible, and dollar denominated. The index covers the investment-grade, fixed-rate bond market, with index components for government and corporate securities, mortgage pass-through securities, and asset-backed securities.

Milton Ezrati, Partner and Senior Economist and Market Strategist for Lord Abbett, has been widely published in a wide variety of magazines, scholarly journals, and newspapers, including **The New York Times, Financial Times, The Wall Street Journal, The Christian Science Monitor,** ***and*** **Foreign Affairs*****, on a broad spectrum of investment management topics. Prior to joining Lord Abbett, Mr. Ezrati was Senior Vice President and head of investing in the Americas for Nomura Asset Management, where he helped direct investment strategies for both equity and fixed-income investment management.***

Market Value of Liabilities – Are you Ready?

By: **David Kausch** & **David Hoffman** of Gabriel, Roeder, Smith & Company

David Hoffman has served as a consultant with Gabriel, Roeder, Smith & Company since 1984. He provides actuarial and consulting services to municipal and county retirement systems in Michigan and several statewide retirement systems in Arkansas.

David Kausch is a Fellow of the Society of Actuaries (FSA) with 15 years of pension consulting experience. He provides actuarial and consulting services for many state and local public employee retirement systems in Michigan, Missouri, New Hampshire, New Mexico and Rhode Island.

Interested in higher and more volatile pension costs? Recent changes in corporate pension accounting and funding rules require the use of a Market Value of Liability (MVL) rather than the actuarial accrued liability (AAL) which is currently used by most public pension plans. The Governmental Accounting Standards Board (GASB) is currently reviewing accounting Statements Nos. 25 and 27 to see if, where, and how MVL would fit in to public sector pension accounting. The differences between MVL and AAL may come as an unpleasant surprise to the public sector potentially increasing near-term costs and introducing more volatility. Just what are those differences and what would the impact to your system and your sponsoring government be using MVL?

The idea behind MVL is that the liability associated with any member's accrued benefit should have the same value or price of publicly traded securities which would provide cash flows that match the member's lifetime benefit payments. Step two of this thought process is that lifetime benefit payments are more like bond coupon payments than stock returns, so the value of the liability should be much more like the price of a bond than the price of a share of stock.

Implications? This method of pricing is equivalent to saying liabilities should be discounted at bond yields, not the expected return on assets. Depending on the bond yield, this alone could increase pension liabilities 30% to 50% in the current environment. But bond yields and prices change all the time – as with any marketable security – which means that market value pension liabilities will fluctuate all the time like the prices of securities. Recap: MVL will be higher and more volatile than conventional AAL.

Had enough yet? Those who favor this approach typically don't smooth assets for funding purposes either. The philosophy is that the market value of assets is what is available to pay benefits, not a smoothed value. Moreover, the difference between the MVL and the market value of assets is viewed as the plan sponsor's obligation and therefore belongs on the sponsor's balance sheet. Most likely in this market MVL will exceed the market value of assets making the difference a debt on the balance sheet. The annual expense – in the purest form of this approach – is simply the debt at the end of the year minus the debt at the beginning of the year.

Is GASB serious? GASB is listening to both MVL and conventional AAL proponents. Will they flip to the MVL approach? Unclear. If and when they make any change, they will probably strive for some middle ground or at least provide for a transition.

The seismic shift in this philosophy is clear. It is also unlikely that this issue will go away entirely. We believe that it is important for stakeholders in public plans to become more knowledgeable on the subject and to participate in the debate that is emerging.

This article is solely the opinion of its authors. It does not necessarily express the opinions of Gabriel, Roeder, Smith & Company."

CORPORATE GOVERNANCE UPDATE

By: **Rosemary Kelly**, PAPERS Corporate Advisory Committee & Broadridge Investor Communication

For Proxy Season 2010 institutional investors have submitted shareholder proposals to public companies focusing on the need for greater director accountability and for more reasonable executive compensation. Types of shareholder proposals submitted include:

- Proxy Access - shareholder-nominated board candidates will be listed on the company proxy (SEC Proxy Access rule to be finalized in 2010)
- Majority voting - if a director receives less than 50% favorable vote, the director resigns (Many companies have implemented majority voting policies or by-laws)
- Separate Chair and CEO Positions
- Independent Compensation Advisor
- Board Diversity
- Declassification of the Board – elimination of varied service term lengths
- Disclosure of political campaign contributions
- Disclosure of global climate change risks (The SEC is considering whether to publish an interpretive release with guidance on company disclosure)
- Annual Advisory Vote on Executive Compensation
- Executive Compensation:
    - Set performance measures for top executives over multi-year periods
    - Require senior executives to hold a percentage of equity shares until two years past retirement
    - Limit change-in-control payments
    - Eliminate tax gross up payments
    - Eliminate/limit significant compensation after the death of a CEO

Regulatory Update

Proxy Disclosure - The SEC has issued rule enhancements effective February 28, 2010, requiring new or revised disclosure by companies:

- Compensation policies and practices that present material risks to the company
- Stock and options awards of executives and directors
- Director and nominee qualifications and legal proceedings
- Board leadership structure
- Board role in risk oversight
- Compensation consultant potential conflicts of interest

Broker Discretionary Vote - The SEC approved the elimination of the NYSE broker discretionary vote for meetings held on or after January 1, 2010. Brokers can no longer issue a vote on behalf of their customers who have not voted.

SEC Initiatives

- SEC Reorganization
- Proxy Access
- Notice and Access Rule Enhancements
- Credit Rating Agencies
- Protection of Investor Assets
- Regulation SHO – short selling
- Risk Assessment
- Hedge Fund Regulation
- Flash Trading/Dark Pools

Current Legislative Proposals

- Restoring American Financial Stability Act – Senator Chris Dodd (Democrat-CT)
- Corporate and financial Institution Compensation Fairness Act – Representative Barney Frank (Democrat-MA)
- Shareholder Empowerment Act – Representative Gary Peters (Democrat-MI)
- Shareholder Bill of Rights Act – Senator Charles Schumer (Democrat-NY)
- Excessive Pay Shareholder Approval Act and Capped Deduction Act – Senator Richard Durbin (Democrat-IL)
- Compensation Fairness Act – Senator Max Baucus (Democrat – MT)
- Taxpayer Protection Act –Senator Byron Dorgan (Democrat – SD)

__Rosemary Kelly__ is a Vice President in the Institution Relations Group at Broadridge Investor Communication Solutions (previously ADP Investor Communication Services) with responsibility for developing and maintaining executive level relationships and disseminating corporate governance and industry issues related to the proxy voting process. Rosemary began her association with ADP in 1992.

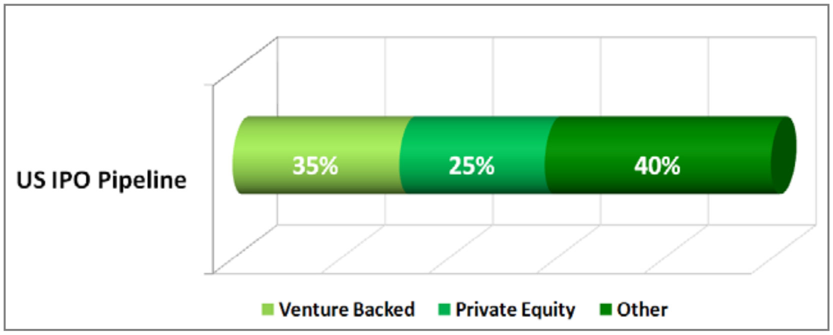
Is there a way to capitalize on the resurgence of the IPO market?

By: Kathleen S. Smith, Chairman & Principal, Renaissance Capital LLC, Greenwich, CT

Kathleen Smith is Chairman of Renaissance Capital LLC, a global IPO research and money management firm that she co-founded in 1991. Previously, Kathy was a director of Merrill Lynch Capital Markets' Technology and Emerging Growth Investment Banking Group. Her experience includes mergers & acquisitions, and numerous public equity offerings. Ms. Smith received an MBA in Finance from Wharton and a BA in Political Science and Chinese Language from Pennsylvania State University.

In our first piece on the IPO market, which was published in the fall 2009 of the PAPERS' e-newsletter, we talked about the role of the private equity industry in the recovery of the IPO market. As we predicted, the private equity industry has emerged as a major contributor to the IPO pipeline, and several of the PE-backed IPOs we mentioned have since gone public. Among them: Dollar General, Vitamin Shoppe, Ancestry.com, Addus HomeCare and RailAmerica. Investors remained highly price sensitive, allowing companies to go public only at significant discounts, unless their growth trajectories were strong. Those that did not discount their shares enough were postponed.

In a recent breakfast event that we hosted with our index partner FTSE and the New York Society of Securities Analysts (NYSSA), we asked four distinguished IPO practitioners from Warburg Pincus, Federated Kaufmann Fund and Citigroup's and Lazard's equity capital markets (ECM) desks about their outlook for the IPO market. From the private equity side we learned that unlike past downturns, the latest recession impacted all of their portfolio companies, all at the same time and all in the same way with regards to their present condition and future cash flows. While the IPO market is indecisive at the moment, Warburg Pincus plans to be opportunistic in bringing portfolio holdings to market, viewing the IPO as only one step in the realization of value. Institutional investors, such as Federated Kaufmann, scour the IPO market to find unique investment opportunities. From the ECM desks we learned that secondary issuance activity has picked up significantly coming out of the downturn, which should bode well for IPO activity, which typically represents about one third of total global equity capital raised. Overall, our panelists were quite optimistic about the future of IPOs, and the pipeline confirms that.



Of the 85 companies currently in the active IPO pipeline, 30 are backed by venture capital firms and 21 are backed by private-equity firms, together representing 60% of our backlog.

10 Largest Recent Private Equity Filings (based on sales)

Company	Filing Date	Business Description	LTM Sales (in MM)	EBITDA Margin	Proposed Deal Size (in MM)
Ryerson Holding	22-Jan-10	Distributor of steel, aluminum and other metals.	$3,398	2.5%	$350
West Corporation	02-Oct-09	Leading conferencing and call center provider.	$2,384	28.4%	$500
Graham Packaging	02-Nov-09	Leading supplier of plastic containers.	$2,292	19.2%	$350
Americold Realty Trust	14-Dec-09	REIT focused on ownership and development of warehouses.	$1,614 *	16.0%	$690
Metals USA Holdings	19-May-08	Leading provider of value-added processed metals.	$1,310	0.1%	$200
Sensata Technologies	25-Nov-09	Texas Instruments' former sensors and controls business.	$1,064	28.4%	$500
Freedom Group	21-Oct-09	Manufacturer of firearms, ammunition and accessories.	$866	20.7%	$200
Noranda Aluminum	08-May-08	Producer of value-added primary aluminum products.	$802	18.1%	$250
InfrastruX Group	10-Aug-09	US electric power and natural gas infrastructure contractor.	$742	10.1%	$290
Mitel Networks	22-Dec-09	Leading provider of communications equipment.	$735	10.7%	$230

Source: Renaissance Capital.
** Reflects annualized pro forma 2009 results.*

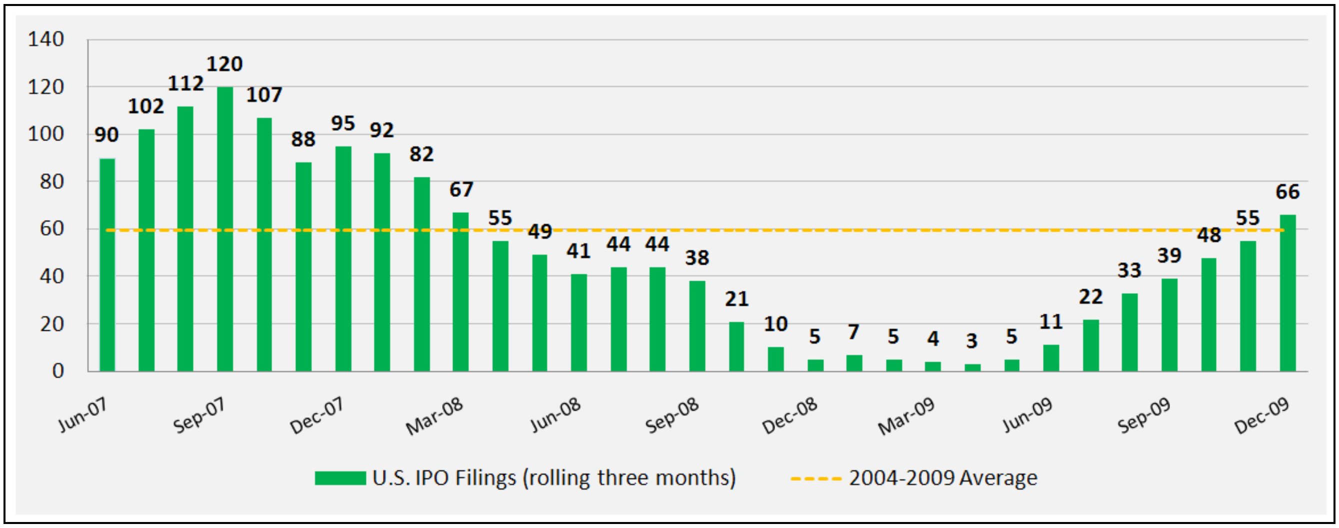
(continued on page 13)

Is there a way to capitalize on the resurgence of the IPO market?

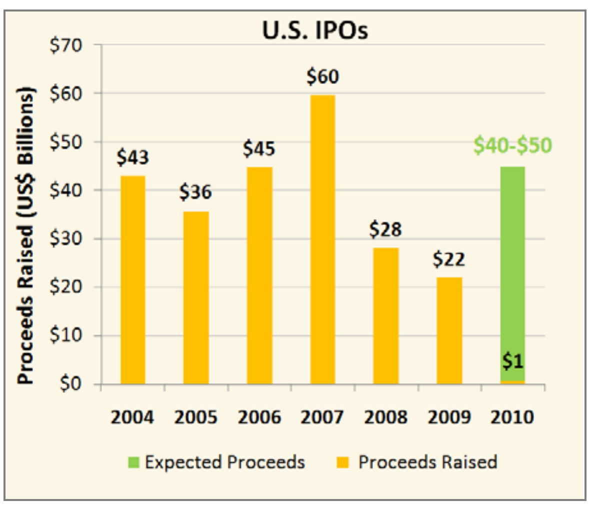
(continued from page 12)

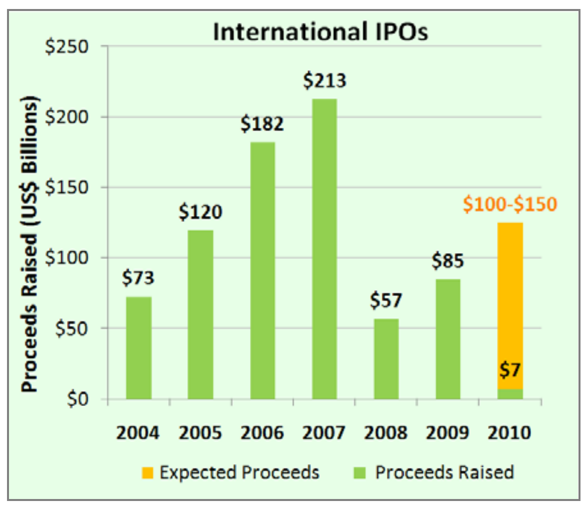
So, is there a way to capitalize on the resurgence of the IPO market?

There is. The US IPO window has started to reopen, with 50 IPOs priced over the past five months, and eight companies scheduled to tap the equity markets in February 2010. Recent filing activity has surpassed its historical average, and there are a number of noteworthy deals in the pipeline, including Tesla Motors, Linkage Technologies and William F. Sharpe's Financial Engines. Perhaps we will also see the long-awaited IPO of Facebook in 2010.



Renaissance Capital's 2010 IPO recovery scenario assumes a shift to a broader recovery and return to growth in the U.S. We anticipate 100-150 IPOs in 2010 with proceeds totaling $40-$50 billion, of which we expect one third to be venture backed and 20% to be PE-backed. Outside the U.S., we anticipate continued gains in China, a rebound in Europe, and several multi-billion dollar IPOs, including large privatizations, with total proceeds in the range of $100-$150 billion.





For more information about the IPO market, including calendars of upcoming IPOs, please visit our website www.renaissancecapital.com or contact me at renaissance@ipohome.com or 203.622.2978. I will also be a speaker at this year's PAPERS Spring Forum in Harrisburg in May and look forward to meeting you at our booth.

About Us

Renaissance Capital LLC, founded in Greenwich, CT in 1991, is the global leader in IPO research. Its clients represent the "Who's Who" list of the largest and most active institutional IPO investors. In addition to IPO research, Renaissance Capital, in conjunction with its index partner FTSE Group, maintains the FTSE Renaissance IPO Composite Index, the definitive benchmark of IPO activity and performance, and it is about to launch a new IPO index series focused on the Asia Pacific ex Japan region. Renaissance Capital also provides IPO-focused investment management services as the advisor to the IPO Plus Fund (IPOSX), the first mutual fund to focus solely on investing in IPOs, and through separately managed institutional accounts.

New SEC Rules Address Compensation and Corporate Governance

By: Andrew D. Abramowitz
PAPERS Corporate Advisory Committee &
Partner, Spector Roseman Kodroff & Willis, P.C.

This past holiday season, the SEC brought good cheer to investors – or as much good cheer as can be brought in the current economic environment – in the form of amendments to SEC rules regarding corporate disclosures. Continuing to respond to the public clamor for greater transparency and oversight, the SEC adopted amendments that heighten the information that companies must provide investors relating to their compensation structure, risk management, and other corporate governance matters.

The amendments are not insignificant. They represent the Commission's attempt to maximize a prospective shareholder's vantage point when making an investment decision, specifically with respect to how the leadership of a company compensates itself. At the 4th Annual Proxy Disclosure Conference in San Francisco last November, Shelley Parratt, Deputy Director of the SEC in the Division of Corporate Finance, addressed the subject head-on: "There is no reason to believe that the scrutiny of executive compensation practices at public companies will subside anytime soon." And she clearly articulated the Commission's motives, stating that "[t]he SEC's role in this area is not to regulate *how* companies compensate their executives, but rather to see that investors have the critical disclosure they need to make informed investment and voting decisions."

Accordingly, the new rules require a company to report how its compensation policies and procedures affect its risk management practices if the risks arising from those compensation policies could have a material impact on the company's performance. The materiality component of the rule might be triggered if, for example, the compensation policies relate to a business unit that carries a significant portion of the entire company's risk profile, or if the compensation policies of one business unit depart significantly from those of the rest of the company. In such instances, the company might need to describe philosophy underlying the compensation structure or the company's risk assessment or incentive considerations in the structure of its compensation policies. As Deputy Director Parratt stated, "[a] company's analysis of its compensation decisions should present shareholders with meaningful insight into its compensation policies and decisions, including the reasons behind them."

Another area addressed by the new SEC amendments is the qualifications of the directors. A company must now disclose each director's or nominee's experience and qualifications for serving as a director. This rule seeks specificity, and corporations must describe "specific experience, qualifications, and attributes or skills that qualify that person to serve as a director… *and as a member of any committee* that the person serves on or is chosen to serve on…." Thus, for instance, if a director is selected to serve on the audit committee, that person's relevant experience and qualifications must be disclosed.

These amendments are certainly extensive and they certainly impose a weighty burden on public companies – both in terms of their management choices as well as in preparing the Compensation Discussion and Analysis section of their proxy statements. None of these measures appears to be the panacea for corporate misconduct, but they all seem to promote greater transparency. The hope is that as corporate disclosures become more understandable and meaningful, the investment community will be better equipped to make informed decisions.

Andrew D. Abramowitz is a partner of Spector Roseman Kodroff & Willis, P.C. in the firm's domestic and international securities practice. His practice focuses on investor protection issues, including litigation under federal securities law, state law governing fiduciary duties, and ERISA. Mr. Abramowitz graduated from Franklin & Marshall College and from the University of Maryland School of Law.

Liability Driven Investing (LDI):
A Strategy For The Changing Pension Landscape

Submitted by: **PNC Capital Advisors -- Fixed Income Team**

What is LDI?

Liability driven investing (LDI) is an investment process that focuses on the management of assets relative to the risks of the associated liabilities. LDI is not new, as insurance companies have been using LDI for years under the name Asset Liability Management. What is new is that Plan Sponsors of defined benefit plans are also beginning to manage plan assets relative to plan liabilities, with a focus on managing the overall plan's funding status or surplus (assets minus liabilities.)

The primary goal of LDI is to manage the risk between assets and liabilities. This usually includes adjusting the interest rate sensitivity (usually quantified by duration) of assets to more closely match that of the liabilities.

Why Now?

Pension plans of corporations are subject to both ERISA and FASB rules. The recent rule changes now impact liabilities, not just the assets. Therefore, any mismatch between the assets and liabilities increases the risk of violating ERISA and/or FASB rules and could potentially become a costly problem for plan sponsors. By reducing the mismatch, the plan's risk will be reduced.

What is Different about LDI Investing?

LDI focuses on the risk of the liabilities relative to assets, hence the term Liability Driven Investment. Within an LDI framework, risk is not measured in terms of absolute risk, but the relative risk of assets versus liabilities. The primary focus of LDI is to maximize return for a given level of relative risk, where the acceptable level of relative risk is usually quite low. Common risk metrics within LDI include duration, tracking error and relative VAR. LDI is foremost about maintaining a plan's funding surplus by minimizing the mismatch between assets and liabilities, and then seeking incremental returns, ultimately increasing the surplus.

How is LDI Implemented?

Since each pension plan is unique due to its liabilities, risk and return objectives, guidelines and constraints, a customized long term solution should be developed. This requires a partnership between you and your actuaries, accountants and investment manager to be successful in developing the LDI process and strategy.

The most commonly used investment vehicles to manage the interest rate risk of a plan's assets to liabilities include long bonds, strips (zero-coupon bonds), futures and swaps.
Additional return can be achieved by accepting credit risk (agency and corporate long bonds), security selection within the corporate bond market, sector rotation, market timing strategies (duration and yield curve) and overlay strategies (such as portable alpha, absolute return, etc.).

(continued on page 16)

Liability Driven Investing

(continued from page 15)

Future of LDI

Given the recent regulatory changes, we believe that liability driven investing will dominate defined benefit plans for the foreseeable future. Other approaches are just too risky and potentially costly to plan sponsors. Derivatives will probably increase in usage by plan sponsors, as they can offer an efficient vehicle to manage interest rate risks and help facilitate the use of overlay strategies to increase return.

With the clock ticking, plan sponsors must soon move from LDI theory to reality.

<table>
<tr><th>Financial Accounting Standards Board Statement No. 158</th><th>Worker, Retiree and Employer Recovery Act of 2008</th></tr>
<tr><td>▪ Funding shortfalls of Plan impacts financial statements.</td><td rowspan="3">▪ PPA established phased-in funding “targets. If a plan missed its funding target for a year, its funding target for the succeeding year would be 100% instead of the phase-in target percentage. Under WRERA, a plan that misses its funding target for a year will only be required to fund up to its target percentage for the following year, not 100% as under PPA.
▪ Plans may “look back” at the previous year’s funded percentage while determining whether a freeze in benefit accruals is necessary.
▪ Allows for limited “smoothing” of asset values where anticipated fund earnings may be taken into account when determining the value of plan assets.</td></tr>
<tr><th>Pension Protection Act of 2006*</th></tr>
<tr><td>2008
▪ Asset/Liability maximum smoothing (asset averaging) period reduced from 5 to 2 years.
▪ If funding falls under 80%, Plan is classified as “at risk” and subject to special catch-up provisions. If “at risk” for more than 2 years, Plan is subject to special load factors and increase in Pension Benefit Guarantee premiums.
2011
▪ Plan must be 100% funded.
▪ Transition relief from 2008 to 2011.
▪ Required to amortize funding shortfalls over seven years, in equal installments.</td></tr>
</table>

	Focus	Objective	Risk Measure
Traditional:	Manage Returns	Maximize Returns	Absolute Risk
LDI:	Manage Surplus	Minimize Risk	Relative Risk

The views expressed in this article represent the opinions of PNC Capital Advisors, LLC and are not intended to predict or depict performance of any investment. All information contained herein is for informational purposes and should not be construed as investment advice. It does not constitute an offer, solicitation or recommendation to purchase any security. The information herein was obtained by various sources; we do not guarantee its accuracy or completeness. Past performance does not guarantee future results. These views are as of the date of this publication and are subject to change based on subsequent developments.

PNC Capital Advisors, LLC is registered with the Securities and Exchange Commission ("SEC") as an investment adviser under the Investment Advisers Act of 1940, as amended. PNC Capital Advisors, LLC is a subsidiary of The PNC Financial Services Group, Inc.