PAPERS PENNSYLVANIA ASSOCIATION OF PUBLIC EMPLOYEES RETIREMENT SYSTEMS

PAPERS P.O. BOX 6817 HARRISBURG PA 17112 | TEL: 717-545-3901 | E-MAIL: perryjal@comcast.net

The mission of the Pennsylvania Association of Public Employee Retirement Systems (PAPERS) shall be to encourage and facilitate the education of its membership in all matters related to their duties as fiduciaries overseeing the assets of the pension funds with which they have been entrusted. It will be PAPERS' primary purpose to conduct an annual educational forum that provides the basis for improved financial and operational performance of the public employee retirement systems in the State. PAPERS will function as a central resource for educational purposes and act as a networking agent for all public plan staff and board members.

Winter 2009 (Vol. 4, No. 1)

In This Issue

If you're interested in overnight lodging for the Forum

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Exit 80, I-81
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Single or double rate $95/night
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This year's Forum is being produced by the Board, Corporate Advisory Committee and staff of PAPERS. You'll enjoy the usual great program at a substantial savings.

Announcing the 5th Annual

PAPERS Forum

May 4-5, 2009 at Holiday Inn Harrisburg-Hershey

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.

From the PAPERS Executive Director

The date for the 2009 PAPERS Forum is fast approaching. We have put together an exciting educational program that will attempt to address the issues that are on most of our minds this year. The economic turmoil and liquidity crisis we have experienced has placed a huge burden on retirement systems across the Commonwealth and across the country. 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.

We hope that you will take this opportunity to join us on May 4^{th} and 5^{th} at the Holiday Inn Harrisburg-Hershey (Grantville, PA) for the 5^{th} Annual PAPERS Forum. A draft agenda is included on pages 4-5 of this newsletter for your review. Complete the registration form on page 6 right away so you don't miss any of the great educational and networking events at this year's Forum.

I'll look forward to meeting you there!

Jim Perry

PAPERS Executive Director

ANOTHER PAPERS OPPORTUNITY

Plan to join PAPERS for more education and networking at our fall one-day workshop in the Pittsburgh area in September. Details forthcoming at the Forum and in the PAPERS summer newsletter.

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(as of 3/20/2009)

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Sponsors provide financial support beyond regular conference registration fees. Additional sponsorship opportunities for the 2009 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.

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Exhibitor $3,500
- 2 complimentary registrations
- Recognition in program
- Complimentary exhibit space

Silver.. $2,500
- 2 complimentary registrations
- Recognition in program

Directions to Grantville & the 2009 PAPERS Forum

Grantville, PA is conveniently located at Exit 80 of I-81, just minutes from the attractions of Harrisburg and Hershey. The Penn National Race Course and Hollywood Casino is ¼ mile from the hotel.

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, Hershey Exit 80

From Philadelphia
Take PA Turnpike 76 West, get off at Exit 247, take I-283 North to I-83 North to I-81 North, Hershey Exit 80

From Baltimore/Washington
Take I-83 North to I-81 North. Hotel is located just off I-81, Hershey Exit 80

From Pittsburgh
Take PA Turnpike 76, get off at Exit 226, follow signs to I-81 North, take I-81 North. Hotel is located just off I-81, Hershey Exit 80

2009 PAPERS Forum Agenda

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

Sunday, May 3, 2008

7:00 p.m..........Conference Registration (hotel lobby) – Closes at 8:30 p.m.

Monday, May 4, 2009

7:00 a.m..........Conference Registration

7:30 a.m..........Continental Breakfast sponsored by: ***Nomura Asset Management***

8:30 a.m..........WELCOME from the PAPERS Board - *Jeffrey B. Clay*

KEYNOTE ADDRESS
Rob McCord, State Treasurer, Pennsylvania Department of Treasury

9:00 a.m..........TEN TOP REASONS FOR THE FINANCIAL CRISIS
Moderator: To be announced
Presenters: *Al Murphy*, PMG Advisors Principal/Director of Marketing
Greg Nowak, Pepper Hamilton LLP

9:45 a.m..........CHIEF INVESTMENT OFFICER ROUNDTABLE
Overview of the current market and the strategies they are employing to combat the current economic downturn
Moderator: ***Professor James Bicksler***, Rutgers University
Panelists: **Chief Investment Officers**

- ***Alan Van Noord***, Pennsylvania School Employees Retirement System
- ***Bill Clark***, New Jersey State Board of Investments
- ***Mansco Perry***, Maryland State Board of Investments
- ***Mark Flaherty,*** Allegheny County Controller

10:45 a.m.........Refreshment Break sponsored by: ***Barroway Topaz Kessler Meltzer Check, LLP***

11:00 a.m.........MANAGING YOUR MANAGERS - Hiring, Monitoring, Retaining, Terminating
Moderator: ***Alan Randzin***, Chester County Treasurer
Panelists: ***Seth Yablonovitz***, Ashford Consulting Group
David Lindberg, Wilshire Associates Managing Director
Michael Shone, Peirce Park Group President

11:45 a.m.........THE LONG AND SHORT OF COMMODITY INVESTING
Moderator: ***Tim Haluszczak***, ,Allegiant Asset Management
Presenter: ***Chris Walvoord***, Guidance Capital LLC Principal

12:30 p.m.........Luncheon sponsored by: ***Allegiant Asset Management Group***

1:15 p.m..........THE STATE OF THE ECONOMY
Speaker: ***Chris Probyn*,** State Street Chief Economist

1:45 p.m..........PLAN SPONSOR ROUNDTABLE DISCUSSION
An overview of the current state of pension systems. Pension executives from across the Keystone State will discuss and debate significant issues facing public pension plans. From funding issues to rising administration & healthcare costs, hear first hand how your counterparts are handling them.
Moderator: ***Michael Bush,*** Merrill Lynch consultant
Panelists: **Local plan administrators**

- ***Krista Rogers,*** Lycoming County Controller
- ***Jim Allen***, Pennsylvania Municipal Retirement System Secretary
- ***Alan Butkovitz***, City of Philadelphia Director of Finance
- ***Craig Ebersole***, Lancaster County Treasurer

2009 PAPERS Forum Agenda *(continued)*

Monday, May 4th

2:45 p.m.……….FIXED INCOME…..WHERE DO WE GO FROM HERE?
Moderator**:** ***Jed Robie*****,** Federated Investments
Presenter**:** ***Robert J. Ostrowski*****,** Federated Investments Executive Vice President

3:30 p.m.……….Refreshment Break sponsored by: ***Federated Investments***

3:45 p.m.……….OPPORTUNITIES IN FIXED INCOME
Moderator: ***Mark Meyer***, Nomura Asset Management
Presenters: ***Rajiv Sobti***, Nomura Global Alpha LLC Chief Investment Officer
Cinda Hughes, Lord Abbett Partner/Client Portfolio Manager

4:30 p.m.……….LEGAL ISSUES ROUNDTABLE
Moderator: ***Joauna Riley***, Phila. Board of Pensions & Retirement Senior Legal Assist.
Presenter: ***John Nixon*** – Wolfe Block *(The IRS and Public Pension Funds)*

5:30 p.m.……….Cocktail Reception sponsored by: ***AFSCME Council 13***

Tuesday May 5th

7:00 a.m.……….Conference Registration

7:30 a.m. ………Continental Breakfast sponsored by: ***Nomura Asset Management***

8:30 a.m.……….FIDUCIARY DUTY & CORPORATE GOVERNANCE
Moderator: ***Professor James Bicksler***, Rutgers University
Presenter: ***Darren Check***, Barroway Topaz Kessler Meltzer & Check, LLP

9:15 a.m.……….WHY SHOULD YOU CONSIDER INDEXING?
WHEN IS INDEXING A GOOD SUBSTITUTE FOR ACTIVE MANAGEMENT?
Walter Lenhard, Vanguard Quantitative Equity Group Senior Investment Analyst

10:00 a.m.………Refreshment Break sponsored by: ***Barroway Topaz Kessler Meltzer Check, LLP***

10:15 a.m.………HOW YOUR PENSION FUND CAN AFFECT YOUR BUDGET
Asset smoothing, benefit design, economic assumptions, contribution rate stability, interaction between your actuary and your investment consultant(s)
Moderator: ***Jeffrey B. Clay***, Public School Employees' Retirement System Executive Director
Panelists: ***Greg Stump***, EFI Actuaries Vice President
Michael Shone, Peirce Park Group President
Charles B. Friedlander, Municipal Finance Partners Director

11:00 a.m.………HEDGE FUNDS – BEFORE AND AFTER
Tony Cottone, Meridian Partners

11:45 a.m.………LEGISLATIVE UPDATE
James McAneny, Public Employee Retirement Commission Executive Director

12:30 p.m.………LUNCH sponsored by: ***Broadridge Financial Solutions***
Motivational speaker – To be announced

1:30 p.m.……….DEALING WITH THE LOCAL PRESS *(Get your message heard and enlist the press as an ally)*
Speakers*:* ***Evelyn Tatkovski****,* Public School Employees' Retirement System Press Secretary
Robert Gentzel*,* State Employees' Retirement System Communications Officer

2:15 p.m.……….TOP 10 THINGS YOU CAN DO TO REDUCE HEALTHCARE COSTS
Moderator**:** ***Andrew Abramowitz,*** Spector Roseman Kodroff & Willis, P.C. Partner
Presenter: ***Jeffrey Kodroff***, Spector Roseman Kodroff & Willis, P.C. Partner

3:00 p.m.……….Refreshment Break sponsored by: ***Federated Investments***

3:15 p.m.……….LIFE SETTLMENTS: An Uncorrelated Asset Class with Certainty of Performance
Moderator**:** ***Jim Manley*****,** Manley Associates President
Presenter**:** ***Paul Biko*****,** Strategic Marketing Resources President

4:00 p.m. ………5th Annual PAPERS Forum Concludes – *See you at the Fall Workshop in Pittsburgh!*

Registration for 5th Annual PAPERS Forum

May 4-5, 2009 at Holiday Inn Harrisburg-Hershey, Grantville, PA

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

- ☐ ***Pension Plan Representatives*** – Current (2009) PAPERS Participating Membership required
  - ☐ First individual from pension plan – complimentary
  - ☐ Each additional individual - $75
- ☐ ***Service Provider Representatives*** – Current (2009) PAPERS Associate Membership required
  - ☐ Each individual from organization - $750
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  - ☐ Two complimentary registrations
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Individual's name ______________________________

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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.

<u>Monday, May 4, 2009</u>

- ☐ Continental breakfast
- ☐ Morning sessions
- ☐ Lunch
- ☐ Afternoon sessions
- ☐ Cocktail reception

<u>Tuesday, May 5, 2009</u>

- ☐ Continental breakfast
- ☐ Morning sessions
- ☐ Lunch
- ☐ Afternoon sessions

Please complete and return this form no later than April 25, 2009. Full payment of any fees due must be included with this registration.

Make <u>checks</u> payable to: *PAPERS*
(Yes, we're working toward on-line credit card payments but unfortunately can't accept them just yet)

Mail to: *PAPERS, PO Box 6817, Harrisburg, PA 17112*

The Challenge of Keeping a Watchful Eye on Plan Fiduciaries:

The Hard Lessons of the Madoff Implosion

By Andrew D. Abramowitz
(PAPERS Advisory Committee & Spector, Roseman, Kodroff & Willis, P.C.)

There has been no shortage of painful investment lessons over the past several months. ***Beware of those collateralized debt obligations. Beware of mortgage-backed securities. Beware of those strange transactional devices called "swaps."*** **But the revelations about Bernie Madoff's monstrous Ponzi scheme have underscored the need to ask a slightly different type of question: we know who are fiduciaries are, but do we know who our fiduciaries are trusting?**

For all of you cave-dwellers out there, Madoff is the broker-dealer and investment advisor whose client base included large institutions, individuals with enormous personal wealth, and charitable foundations – and who serviced these clients by putting their money in an investment scheme that, in his words, was "just one big lie." The lie came crashing down last December, and it may have cost investors as much as $50 billion.

A lawsuit recently filed in federal court in Philadelphia by the Pension Fund for Hospital and Health Care Employees – Philadelphia and Vicinity (the "Fund") raises questions about the nature of fiduciary responsibility that bear on all investors, including public pension funds. The suit alleges that Austin Capital Management, an investment management firm and fiduciary to many employee benefit plans, directed money into Madoff entities despite the existence of numerous "red flags" that should have tipped off Austin that these investments were not secure.

Essentially, the Fund – which is an employee pension benefit fund and must operate for the exclusive benefit of its participants – retained an investment consultant to supervise various investment managers and to act as a fiduciary of the Fund in terms of asset allocation. That investment consultant then retained Austin to act as a fiduciary of the Fund in managing a portion of the Fund's assets. The lawsuit alleges that Austin, in breach of its fiduciary obligations to the Fund, ignored various "red flags" and invested a portion of the Fund's assets in Madoff entities.

Apparently, the Fund was not the only victim of Austin's fiduciary breach – the Massachusetts Pension Board, the New Mexico Education Retirement Board, and others all lost millions through Austin's investments with Madoff, according to the lawsuit.

The case against Austin was only very recently filed, and the outcome is far from certain. However, it – and the Madoff situation in general – crystallizes an issue that public pensions and investors of all kinds should consider: we may not have our hands on all of the people who undertake a fiduciary duty to invest our money prudently and in our sole interest. We hire people to act as our fiduciaries, but those people may hire others to act as our fiduciaries, and those people may hire others still. Of course, all down the chain these individuals bear the highest level of responsibility toward us, but an element of control is surrendered as those who are investing for us are further and further away.

We must be careful. It is hard enough to know who to trust. It is even harder to know who others are trusting on our behalf.[1]

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[1] For those interested in reading more about this lawsuit, here is the caption information: *Pension Fund for Hospital and Health Care Employees – Philadelphia and Vicinity v. Austin Capital Management Ltd.*, Civil Action No. 09-615 (PBT) (E.D. Pa.).

Environmental Markets:
A Segment to Watch

By: Ronnee Ades
(PAPERS Advisory Committee and Head of Alternatives, FTSE Group)

Ronnee Ades is Head of the Alternatives Business Unit for FTSE Group. She is responsible for driving index growth within alternative asset classes including real estate (with the world's most widely known FTSE EPRA/NAREIT Global Real Estate Series & the FTSE NAREIT U.S. Real Estate Indices), hedge funds, private banking and infrastructure. She is also responsible for identifying opportunities in new alternative asset classes. She works alongside the Business Unit Heads of Equities, Data & Distribution Services, Responsible Investment, and Fixed Income. She is based in FTSE's New York office.

Environmental markets today represent an estimated $250 billion in value. The sectors representing environmental markets include renewable energy, energy efficiency, water technology, and waste and pollution control. These markets are expected to continue to grow in both size and scope over the long term, notwithstanding the current financial market conditions. Socio-political factors driving this growth include proposed legislation by both the United States federal government and the European Union to limit emissions and encourage energy efficiency, as well the United Nations' global "Green New Deal."

In the United States, President Barack Obama has committed to "make the U.S. a leader in combating climate change around the world," proposing in the Obama-Biden Comprehensive New Energy for America plan to:

- Help create five million new jobs by strategically investing $150 billion over the next ten years to catalyze private efforts to build a clean energy future.
- Within 10 years save more oil than the United States currently imports from the Middle East and Venezuela combined.
- Put 1 million Plug-In Hybrid cars -- cars that can get up to 150 miles per gallon -- on the road by 2015.
- Ensure 10% of United States electricity comes from renewable sources by 2012, and 25% by 2025.
- Implement an economy-wide cap-and-trade program to reduce greenhouse gas emissions 80% by 2050.

Meeting U.S. and global emission reduction goals will require companies to employ significant amounts of investment in both alternative/renewable energy sources and energy efficiency. While this industry is in early stages of growth as companies commit to further developing the technology and products it is a good time to start paying close attention to the leaders. One way of measuring how well these types of companies are doing is to use the FTSE Environmental Markets Indexes. The series measures the performance of companies with significant involvement in environmental business activities, as well as those that derive the majority of their business from the development or deployment of environmental technologies. As we experience a shift to a low carbon economy, this series tracks the performance of those companies best positioned to operate and profit in such an environment.

Pennsylvania Pension Fund Conference on Shareholder Responsibility

Radnor Hotel • Radnor, Pennsylvania

Join your colleagues from public and labor pension funds across Pennsylvania to learn more about shareholder rights and responsibilities and how you can protect and assert those rights.

In these turbulent financial times it is more important than ever to make sure that your fund is aware of all instances where it can recover losses and help improve the value of its investments. You will also hear from investment professionals and plan consultants on the latest trends in investing and fiduciary responsibility.

Lead sponsor Barroway Topaz Kessler Meltzer & Check, LLP welcomes you to a conference that will bring together experts from the pension, investment, legal and political community to discuss issues important to pension funds of all sizes.

After the conference join us for dinner and a ball game at Citizens Bank Park as the World Series Champions, the Philadelphia Phillies, take on the Los Angeles Dodgers

(Transportation provided from the Radnor Hotel)

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Conference Open to Qualified Pension Representatives Only

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PAPERS PENNSYLVANIA ASSOCIATION OF PUBLIC EMPLOYEES RETIREMENT SYSTEM

Wednesday May 13, 2009

Registration 9–9:30 a.m.
Conference 10 a.m.–4 p.m.

Some of the topics to be discussed:

- Corporate governance: What does it mean to you?
- Filing settlement claims: Are you getting back the money owed to you?
- Taking action: Serving as a plaintiff in a class action, derivative action, or takeover action.
- The subprime meltdown, the credit crisis, Bernie Madoff. Where do we go from here and how can investor confidence be restored?
- Investor legislation in the new administration: What does it mean for your fund?
- Investment trends: What does the future hold for those struggling to meet funding obligations?
- The evolution of fiduciary responsibilities.

To register for this event or for more information please e-mail paconference@btkmc.com or call Darren Check at (610) 822-2235.

Managed Volatility: Reducing Risk by Ignoring the Benchmark

Ric Thomas, CFA
State Street Global Advisors

Ric is a Senior Managing Director of State Street Global Advisors and is Head of Alternative Investments. Ric works across and with SSgA's investment teams to build alternative and absolute return solutions for clients. Previously, Ric served as the Head of the North American Enhanced Equity team, where he helped design and manage large-cap, small-cap, and 130 / 30 strategies. In addition, Ric is a member of the SSgA Technical Committee and a member of the Senior Management Group.

Overview

The past year and a half provided an unwelcome reminder that equity market volatility bears no resemblance to the volatility of a pension fund's liabilities. Pension fund liabilities look pretty much the same as they did two years ago. The same cannot be said for the value of equity portfolios.

This observation is not new, but it reinforces the need to find low-volatility asset classes or investment strategies. Pension funds have been moving into alternative investments over the past decade or so in hopes of taming the volatility of their plan, without sacrificing potential returns. But alternative strategies and fund-of-fund allocations come with their own challenges, many of which came to light in the past year. In particular, many hedge funds contain the following:

- Leverage
- Illiquidity
- High Fees
- Opaqueness
- Beta

So, what's a pension fund to do? Either it accepts the volatility of the underlying asset classes or it ventures into a world which contains all of the above characteristics. Many plan sponsors are left scratching their heads, looking for a way out of this madness.

Fortunately, there is a competing potential solution to this dilemma. It turns out that volatility within the equity market is not compensated.[2] Therefore, a "managed volatility" approach to equity investing seems to significantly tame the downside risk of the equity market without sacrificing potential returns.

Before I explain this approach, I will warn you. Some of this analysis directly contradicts the Capital Asset Pricing Model (CAPM), so strict believers in this model may wish to stop reading this article.

The CAPM is a theory that was developed over 40 years ago by William Sharpe and John Lintner. The theory predicts several things, one of which is that expected returns should increase as market risk (or beta) increases. The zero-beta portfolio should equal the risk free rate of return and the relationship between return and beta is positive and linear. Exhibit 1 shows this graphically.

(continued on page 11)

[2] Blitz, David and Van Vliet, Pim,The Volatility Effect: Lower Risk Without Lower Return (April 2007, 07). Journal of Portfolio Management, pp. 102-113, Fall 2007.

Managed Volatility *(continued from page 10)*

Unfortunately for CAPM believers (are you still reading this?) Exhibit 2 directly contradicts this prediction. Each month we grouped portfolios based on low to high beta and held them for a month. Surprisingly, this chart shows that low beta stocks have done better than high beta stocks, even though the market has risen significantly over this time period. In addition, high beta stocks have been much more volatile over this time period than have low beta stocks (not shown here). This suggests that beta may be a poor predictor of return, but a great predictor of volatility. This makes beta an undesirable characteristic for a stock to posses.

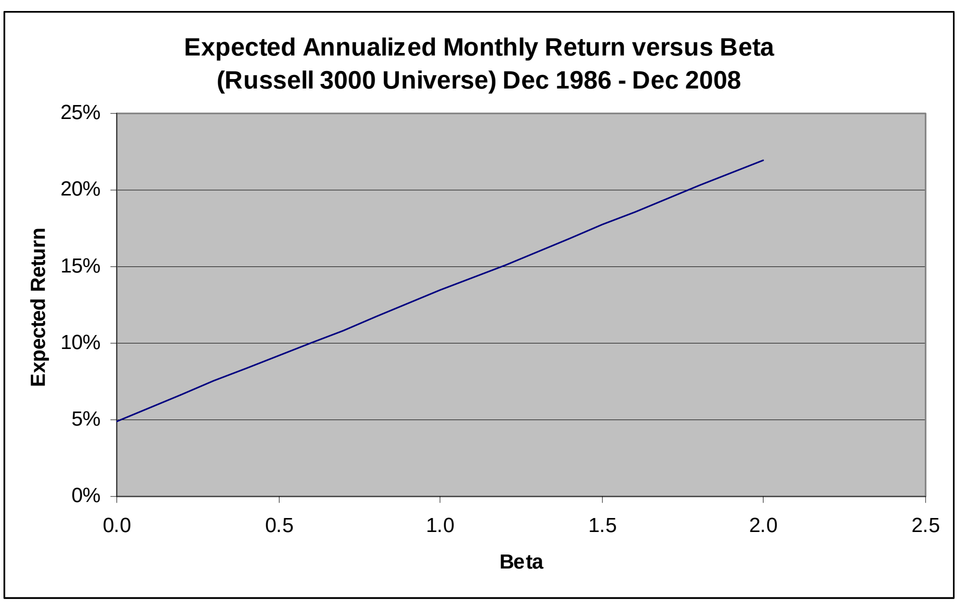
Why does this happen and should it continue? We think it will continue because high beta stocks tend to attract the crowds. Portfolio managers assume that high beta stocks do better than low beta stocks in an up market and likely attempt to boost portfolio beta in direct proportion to their market optimism. This generally leads to overcrowding in high beta stocks, which can lead to lower future returns (see for example, August 2007).

How can we take advantage of this? Managers, including SSgA, have developed strategies that seek to buy low beta stocks with low volatility. We call this a "managed volatility" approach. Essentially, managers can use a risk model to construct the equity portfolio expected to yield the lowest risk in the market, subject to some realistic constraints (i.e., limits on stock and sector exposures). Interestingly, these portfolios have outpaced the market over time with about 70 percent of the risk. [i]

While these strategies have low total risk, they have high active risk versus a cap-weighted benchmark. This is because the objective of the portfolio construction is to minimize total risk, not to minimize tracking error. Because of this, the final portfolio will have low beta (though fully invested) and sector weights that are noticeably different than a cap-weighted index.

Therefore, this should not be thought of as a beta 1 allocation. Some think of it almost as a new asset class, or as an absolute return investment approach. But unlike other approaches, it is transparent, liquid, not levered, long only, and reasonably priced. We suspect these characteristics are likely to resonate with investors for the foreseeable future.

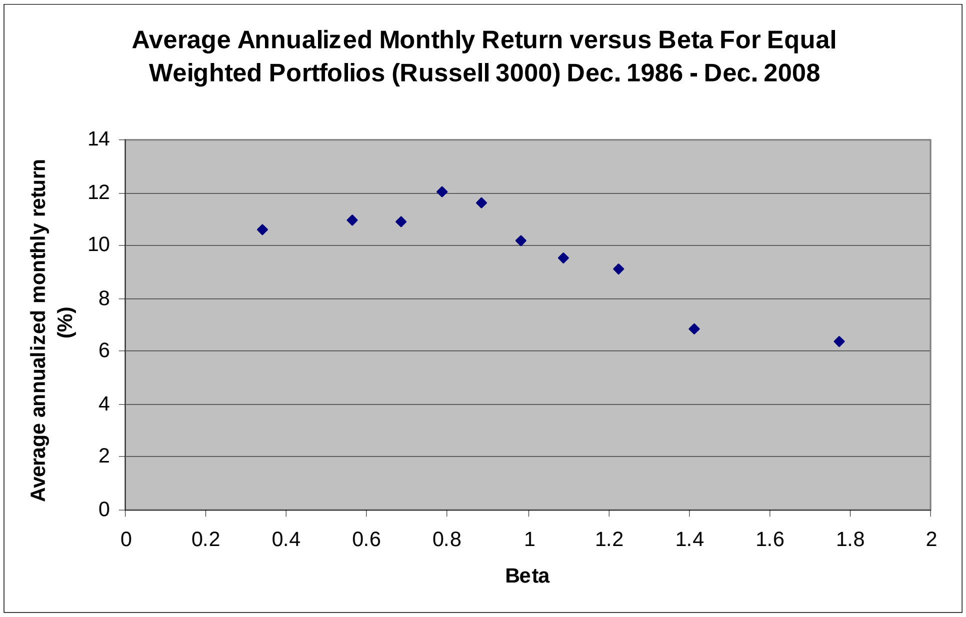
Exhibit 1[ii]



(continued on page 12)

Managed Volatility *(continued from page 11)*

Exhibit 2



Source: SSgA, Barra

The views expressed are the views of Ric Thomas only through the period ended January 31, 2009 and are subject to change based on market and other conditions. The opinions expressed may differ from those with different investment philosophies. The information we provide does not constitute investment advice and it should not be relied on as such. It should not be considered a solicitation to buy or an offer to sell a security. It does not take into account any investor's particular investment objectives, strategies, tax status or investment horizon. We encourage you to consult your tax or financial advisor. All material has been obtained from sources believed to be reliable, but its accuracy is not guaranteed. There is no representation or warranty as to the current accuracy of, nor liability for, decisions based on such information. Past performance is no guarantee of future results.

Investing involves risk including the risk of loss of principal.

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[i] Source: SSgA, Past performance is no guarantee of future results.
[ii] CAPM Illustration. The information outlined above is intended for illustrative purposes only. The information is not intended to be investment advice.