

SUZANNE BUMP SWORN IN AS AUDITOR OF THE COMMONWEALTH

New State Auditor to Help Lead PERAC

State Auditor Suzanne M. Bump has assumed her statutory role as a member of the Public Employee Retirement Administration Commission, succeeding former Auditor A. Joseph DeNucci. Following her swearing-in by Governor Deval Patrick on January 19, 2011, Auditor Bump assumed the *ex officio* seat reserved for the Constitutional Office.

"I greatly look forward to working with the other PERAC commissioners on creating and implementing meaningful pension reform," said Auditor Bump. "We need a program that balances the retirement needs of public employees who pay into the system with one the State and municipalities can sustain. I am a strong supporter of our defined benefit pension plan for our public employees, and, while supporting reforms that will improve the system, I am also committed to challenging those who seek to undermine the system."

Auditor Bump has enjoyed a long and productive career in government leading to her new role as State Auditor where she is committed to making government work better.

"I intend to make the State Auditor's Office a catalyst for making state government more efficient, accountable and transparent by strengthening our Audit Operations."

The Auditor's biography summarizes her background and experience:

Prior to her election, Auditor Bump



Auditor Suzanne M. Bump

was appointed in 2007 by Governor Deval Patrick and served for 3 years as Secretary of the Executive Office of Labor and Workforce Development. As a cabinet Secretary, she led the reorganization of the Commonwealth's public sector labor relations agencies, depoliticizing and professionalizing management and establishing an oversight panel. She also launched an initiative to identify the workforce needs of businesses in each region of the state and to create data tools to better plan, manage and measure the effectiveness of strategies to close persistent skills gaps.

Auditor Bump, a native of Whitman, Massachusetts, was a member of the House of Representatives, serving for eight years in the Legislature on the Commerce and Labor Committee, including two as Chairman. She served as counsel to companies large and small and has also held positions on the boards

(Continued on page 2)

Also In This Issue

- NEW CHAIRS APPOINTED FOR THE PUBLIC SERVICE COMMITTEE
- 2010 INVESTMENT RETURNS
- COMMISSIONER ROBERT B. MCCARTHY REAPPOINTED
- AN OVERVIEW OF INVESTMENT REGULATORY ISSUES
- GOVERNOR PATRICK FILES "PENSION REFORM III" LEGISLATION
- PERAC MEDICAL PANEL PHYSICIANS RESPOND
- VIDEO TRAINING INTRODUCED FOR 2010 ANNUAL STATEMENTS

Public Employee Retirement Administration Commission

Five Middlesex Avenue, Suite 304
Somerville, MA 02145

ph 617 666 4446

fax 617 628 4002

web www.mass.gov/perac

The Honorable Domenic J. F. Russo
Chairman

The Honorable Suzanne M. Bump
Auditor of the Commonwealth

The Honorable Paul V. Doane
Investment Professional

James M. Machado
Sergeant
Fall River Police Department

Donald R. Marquis
Former Town Manager
Arlington

Robert B. McCarthy
Immediate Past President of the Professional Firefighters of Massachusetts

Gregory R. Mennis
Assistant Secretary, Finance and Infrastructure
Executive Office of Administration & Finance

Joseph E. Connarton
Executive Director

Michael DeVito
Editor



NEW CHAIRS APPOINTED FOR THE PUBLIC SERVICE COMMITTEE

Committee leadership changes for the 2011-2012 session

By Michael DeVito
Director of Public Affairs

The Joint Committee on Public Service leadership will have a new look this session. Senator Katherine Clark (D-Melrose) has been appointed by Senate President Therese Murray as Senate Chair of the Committee succeeding Senator Thomas M. McGee.



Senator Katherine Clark

Senator Clark served in the Massachusetts House from 2008-2010 before joining the Senate this year. Previously she served on the Melrose School Committee from 2001-2007. She holds a BA degree from St. Lawrence University, a JD degree from Cornell University and an MPA degree from the John F. Kennedy School of Government at Harvard University.

Representative John W. Scibak (D-South Hadley) was tabbed by Speaker Robert A. DeLeo as House Chair of the Committee. He succeeds former Representative Robert Spellane who did not seek re-election.

Representative Scibak has served in the Massachusetts House since 2003 and previously as a Selectman in the Town of South Hadley from 1991-2002. He

holds BA, MA and Ph.D degrees from the University of Notre Dame.



Representative John W. Scibak

Patrick Charles will continue to serve as Counsel to and Research Director of the Committee. He will be assisted by staff Research Analyst Jacob Sanders.

2010 INVESTMENT RETURNS

By Robert Dennis
Investment Director

The process of compiling and analyzing 2010 investment performance by the local systems is underway.

As has been reported, PRIM's return for 2010 was 13.59%. Preliminary returns from most of the 51 local systems that invest predominantly on their own indicate a range between 11% and 17%.

A review of PERAC's year-end Financial Market Review (posted 1-14-11) will indicate

some of the major drivers of performance. Boards that had healthy allocations to small and midcap stocks did better than those whose domestic equity allocations were concentrated in large caps. Boards that had meaningful allocations to emerging markets did better than those whose international equity accounts were limited to developed market (i.e., EAFE) mandates. Those whose fixed income allocations included meaningful exposure to high yield bonds or to opportunistic areas like structured credit or emerging markets debt did better than those predominantly or solely invested in investment grade bonds. Boards with exposure

to last year's impressive returns from real estate investment trusts also benefited.

In short, last year's investment results once again demonstrated the benefits of diversification among and within asset classes. As always, however, having investment managers who meet or beat their benchmarks was also crucial, no matter what the asset allocation.

A more complete analysis of 2010 performance will be distributed when all returns have been finalized.

SUZANNE BUMP SWORN IN AS AUDITOR OF THE COMMONWEALTH (continued from page 1)

of several non-profit organizations.

Auditor Bump is personally and professionally dedicated to creating opportunities and achieving excellence. She has been honored by numerous organizations over the years, including awards bestowed in 2009 by Boston Archdiocese's Labor Guild, the Women's Bar Association and the Massachusetts Association of Women Lawyers.

Auditor Bump earned an A.B. in English from Boston College and a J.D. from Suffolk University Law School.

PERAC Chairman Domenic J. F. Russo welcomed the Auditor to PERAC:

I know that all the other PERAC Commissioners join me in enthusiastically welcoming our newest member, Auditor Suzanne Bump to the Public Employee Retirement Administration Commission. We look forward to working with the Auditor, in overseeing the Commonwealth's retirement systems that implement Chapter 32 of the Massachusetts General Laws including the significant pension reforms enacted in the past two years. We are also looking forward to taking advantage of the Auditor's experience and expertise as we provide input to the General Court as they consider the new and major pension reform

initiatives currently under consideration on Beacon Hill. Welcome Auditor Bump!

Chairman Russo's sentiments were echoed by PERAC's Executive Director Joseph E. Connarton:

On behalf of the entire PERAC staff I want to take this opportunity to welcome Auditor Bump to the Commission. The Auditor's experience in government in both the legislative and administrative branches will be a tremendous asset to the Commission as it deliberates the important and truly groundbreaking issues facing the pension community today. The Auditor's legislative and administrative experience will be a most welcome asset to the Commission.

COMMISSIONER ROBERT B. MCCARTHY REAPPOINTED

Full Five-Year Term Began on November 3, 2010

By Michael DeVito
Director of Public Affairs

PERAC Commissioner Robert B. McCarthy was reappointed and sworn in by the Honorable A. Joseph DeNucci, then Auditor of the Commonwealth, to a full five-year term that began on November 3, 2010. Commissioner McCarthy had previously filled the remainder of the unexpired term of former Commissioner Kenneth Donnelly, who was elected to the Massachusetts Senate. Mr. McCarthy will continue to hold the seat assigned in statute to the President of the Massachusetts AFL-CIO or his designee (appointed by the Auditor).

Mr. McCarthy served as the President of the Professional Fire Fighters of Massachusetts from his election to the post in 1987 until his retirement on January 21st of 2011. Prior to becoming the union's President, Mr. McCarthy served as their Legislative Agent from 1985-1987. Mr. McCarthy is a retired Captain of the Watertown Fire



Commissioner Robert B. McCarthy

Department and served in his field for 34 years.

PERAC Chairman Domenic J. F. Russo and Executive Director Joseph E. Connarton welcomed Commissioner McCarthy's reappointment to the Commission and wished him well as he assumed his full-five-year term.

Chairman Russo noted:

On behalf of all his fellow Commissioners, I am pleased to congratulate Commissioner Bob McCarthy

upon his reappointment as a PERAC Commissioner. Bob will continue to bring his years of experience in pension issues to our table. We all look forward to continuing to work with Bob as we embark on the next challenging phase of the public debate on pensions and pension reform.

Executive Director Joseph E. Connarton also expressed his congratulations:

I want to pass along the good wishes of the entire PERAC staff to Commissioner Bob McCarthy on his reappointment. Commissioner McCarthy possesses unique expertise having been a major participant in important Massachusetts pension decisions for many years. His knowledge of the issues and tenacious advocacy for the labor constituency he represents provide an important component of the diverse elements represented on the Commission. Bob is a great asset to the Commission and we are pleased by his reappointment.

AN OVERVIEW OF INVESTMENT REGULATORY ISSUES

By Robert Dennis
Investment Director

PERAC Memo #34, 2010 provided an important clarification of the meaning of the acknowledgement letters we send to retirement boards upon satisfactory receipt and review of regulatory documents pertaining to the selection of new investment managers. As explained, these letters do not authorize a board to enter into a contract with the manager without regard to whether that manager has promised to comply with all the investment regulations. The board and its legal counsel will typically seek separate assurances of regulatory compliance.

Historically, there have been only a few PERAC investment regulations that prospective managers have found difficult to comply with and our forthcoming proposed revised regulations will address most of these validly-raised concerns. Nevertheless, PERAC will continue to consider supplementary regulation requests on behalf of managers that provide rationale explana-

tions for being unable to comply with specific regulations.

Massachusetts public pension systems have not seen the type of pay-to-play scandals that have rocked other states in recent years and PERAC has been well ahead of many states in requiring manager disclosures. Nevertheless, PERAC's forthcoming proposed revised investment regulations will require stricter disclosure of third party marketing arrangements and related matters. Since strict penalties may be exacted on managers who fail to provide full and accurate disclosures, boards should begin exercising closer review of disclosure statements in terms of their completeness and specificity.

Recent articles in *The Wall Street Journal* have reported on claims by some major investment management firms as well as some large public pension plans that they have been over-charged by their custodian banks for currency trades made in conjunction with the execution of international security transactions. Although the sums

involved in these disputes may not be significant relative to a board's total assets and annual performance, it may be wise for boards to raise the issue with their investment consultants and international stock and bond managers in order to gain assurance that their managers' trades on their behalf are being executed efficiently and fairly.

PERAC has been and will continue to be committed to giving local retirement boards as much flexibility as reasonably possible in developing and implementing their investment programs. Boards face few if any restrictions in determining their asset allocations and some of the few remaining restrictions will be removed in the forthcoming proposed revised regulations. There are essentially no asset classes that are off-limits to retirement boards. Although PRIT's size and clout may enable it to invest in certain asset classes more effectively and/or efficiently than many local systems, there is no asset class that PRIT invests in that local systems cannot. Indeed, we have authorized some boards to invest in certain

GOVERNOR PATRICK FILES “PENSION REFORM III” LEGISLATION Major Reform Bill Sent to the Public Service Committee

By Michael DeVito
Director of Public Affairs

In another of the Administration’s major reform initiatives, Governor Deval Patrick has sent the Legislature a major pension reform bill, “An Act Providing for Additional Pension Reform and Benefits Modernization.” House 35 proposes major changes in pension calculations and benefits that will primarily impact new hires. The bill was sent to the Joint Committee on Public Service.

In his letter to the Senate and House proposing, “Pension Reform III,” Governor Patrick outlined his objectives:

“Providing a fair, fiscally sustainable and publicly credible pension system for public employees is in the best interests of the Commonwealth, taxpayers and public employees. This legislation continues the progress of the Administration and the Legislature in overhauling the state pension system to make it more equitable and sustainable. In the last few years, the Governor and the Legislature worked together to enact significant changes that closed

loopholes and curbed the most egregious abuses in the system. Additional reforms are needed in order to address the system’s large unfunded liability and to ensure that the pension system will be sustainable for the future.

The legislation proposes further pension reforms to achieve the following objectives:

- Update the system to reflect demographic changes, such as the fact that people are living and working longer;
- Eliminate abuses, through anti-spiking measures, extending the number of years used to calculate pension benefits, and increasing scrutiny of legislation benefiting individual employees; and
- Address fairness issues, through updating purchase of creditable service and buyback provisions; eliminating early retirement incentives; pro-rating benefits based on employment history; eliminating the right to receive a pension while receiving compensation for service in an

elected position; and allowing retirees who married a person of the same sex (within the first year after it became legal) to change their retirement option to provide a benefit to their spouse.”

Among the proposed changes that will primarily impact employees hired after July 1, 2011 are the following:

- Extend the final average salary computation from three to five years;
- Increase the retirement age:
 - ~From 55-65 to 65-67 for Group 1 employees;
 - ~From 55-60 to 55 -62 for Group 2 employees;
 - ~From 45-55 to 50-57 for Group 4 employees.
- Increase the years of service required for Group 3 employees to attain maximum benefit to 30 from 25.

A copy of the bill is available on the General Court Web site at: www.malegislature.gov/bills/Search (In the “Bill Number” box, type h35.)

PERAC MEDICAL PANEL PHYSICIANS RESPOND

By Frank E. Valeri
Deputy Director

The PERAC Disability Unit strives to process the medical panel requests in a timely manner to best serve the retirement boards, member applicants and the employers. The Unit’s efforts have generally focused on perfecting our internal process to ensure that comprehensive medical panel reports are completed in an optimal time frame. Essentially, the process requires effective communication and efficient interaction with retirement board staff and applicants to meet the objective of setting up the most suitable panel for

each case by contracting with medical vendors and physician’s offices. Despite our record of diligence in handling medical panel requests, the logistical realities of scheduling; providing required notice to the members; and difficulties in locating appropriately specialized physicians had made it impossible to enhance the medical panel processing time periods.

However, in the fall of 2009, in the midst of PERAC’s annual physician recruitment efforts, Disability Unit Director Barbara Lagorio and Manager of Medical Services Kate Hogan sought the cooperation of medical panel physicians in adjusting their

reporting time frame. It was suggested that if participating physicians would complete a quality comprehensive report and file it within 30 days instead of the statutorily authorized 60 day period, it could improve PERAC’s efforts to serve the members and boards in the disability application process. The request was simple, but we are pleased to report that it has resulted in significant improvements to PERAC’s overall processing of completed medical panel reports.

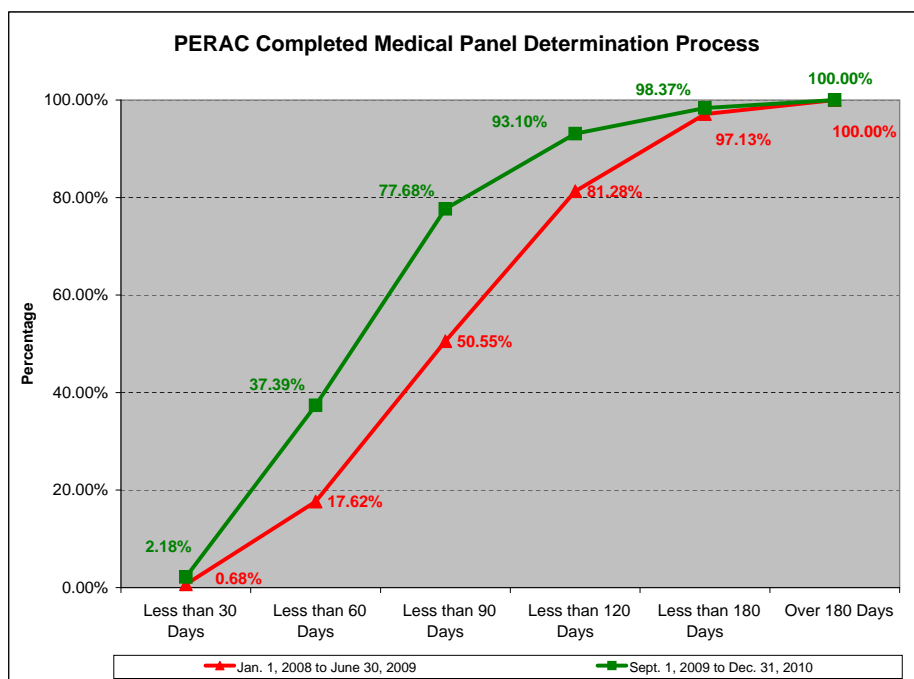
Medical panel physicians responded to our request and reduced the time they took to file panel reports. As a result, 78 percent of

(Continued on next page)

PERAC MEDICAL PANEL PHYSICIANS RESPOND (continued from page 4)

the medical panel requests are now being completed and returned to retirement boards for final action with 90 days of being filed. In contrast, prior to implementing this change, 55% of medical panel requests were being processed within the 90 day time frame.

The change initiated by PERAC was prompted by recent media reports highlighting certain disability cases. The reporting was critical of perceived elongated time periods that seemed to extend improperly beyond the 180 day time frame. Most of the parties directly involved in the administration of the complicated disability application process required by statute often find it very challenging to complete the entire protocol within the designated period. However, the difficulty involved should not discourage those concerned from trying to improve the situation. With the cooperation of PERAC's contracting physicians and medical vendors, we are pleased to report that we have been able to shorten the process without sacrificing quality.



The above graph compares two different time periods involved with PERAC's processing of Medical Panel requests. It includes the time from when a request is made by the board to the time a completed Report is given back to the retirement board.

The period from 1/1/08 to 6/30/09 represented by the (Red line in graph) identifies 551 Medical Panel requests received and closed during that period. During that time our examining physicians were required to make a final Report on a disability application within 60 days of examination.

The period from 9/1/09 to 12/31/10 represented by the (Green line in graph) identifies 732 Medical Panel requests received after PERAC requested our examining physicians to shorten the reporting period to 30 days.

AN OVERVIEW OF INVESTMENT REGULATORY ISSUES (continued from page 3)

strategies without regard to whether PRIT has invested in similar products. I am always pleased to hear from prospective investment managers who may wish to discuss whether their products might be appropriate for Massachusetts local public pension systems.

While boards should consider many factors in determining their asset allocations, we continue to encourage boards to seek as much asset class diversification as they are comfortable with. Over time, well diversified portfolios have performed better than those limited to stocks and bonds.

Hedge funds have provided significant diversification benefits against the equity market's historic volatility of the past decade. Since their original issuance in 2002 and through subsequent revisions, PERAC's hedge fund guidelines have been very successful in allowing local systems

to participate in this important asset class but to do so in a way that has enabled them to avoid any meaningful losses from single hedge funds. While we have strictly enforced the guidelines' requirements for fund and strategy diversification and for limited volatility, we did institute a new practice in 2010 under which we may enforce these and other guidelines in the context of a board's total hedge fund portfolio rather than every specific fund of funds.

Although the hedge fund guidelines are the only instance where PERAC mandates specific diversification requirements for an asset class, boards should seek to have good diversification within (as well as among) all asset classes, particularly in alternative asset classes such as real estate and private equity (unquestionably the riskiest asset class that systems invest in).

As we have previously noted, boards and their consultants should examine their RFPs to ensure the appropriateness of all questions. Many RFPs still ask prospective managers to declare whether their products are PERAC-approved, despite the fact that this agency has no procedure for approving or rejecting managers prior to their selection by retirement boards. Subject to prospective managers' compliance with PERAC regulations and their basic qualifications for a particular mandate, there are no limits to the universe of managers (or consultants) that boards may consider for selection in their RFP processes.

The Investment Unit welcomes any questions pertaining to the investment regulations and the regulatory process. We also welcome inquiries for advice on substantive investment issues. As always, we would welcome invitations to attend and participate in retirement board meetings.

VIDEO TRAINING INTRODUCED FOR 2010 ANNUAL STATEMENTS

Approach Augments Customary Training Provided To Boards

By Frank E. Valeri
Deputy Director

In 2011, for the first time, PERAC'S training approach included videotaped instructions on the annual filing of a sworn statement of each retirement system's financial condition.

On the video, PERAC Chief Auditor Harry Chadwick and Deputy Chief Auditor Jim Tivnan summarize how to prepare the 2010 Annual Statement. Their summary includes Annual Statement preparation basics, the process in general, and the same issues generally reviewed at the in-person training classes. The video also includes information about revisions in the 2010 Annual Statement that are related to recent statutory changes, including accounting for the 3 percent interest on refunds, and early retirement incentive (ERI) funds contributed by an employer. Mr. Chadwick and Mr. Tivnan also review certain recent alterations to PERAC's *Accounting Manual for Massachusetts Public Pension Systems* including accounting for buyback agreements as assets and the use of new general ledger accounts.

A useful feature of the video is a table of contents that makes it easier to return to a particular segment. The video can be used by retirement boards at their own convenience as a quick refresher about navigating problem areas likely to be encountered during the filing process. The DVD video was sent to all boards as an attachment to PERAC Memo #10 of 2011.

The video approach is intended to augment the traditional training classes that PERAC will continue to offer in classrooms. PERAC's 2011 traditional training format remained the same as that which the Commission offered last year - with two formal sessions being held in February. One session was held at the PERAC office in Somerville on February 8th and another in West Springfield on February 17th. Prior to these training sessions, the Annual Statement publications were distributed via compact disc (CD) to the retirement boards. The files on the CD included an Annual Statement instructional booklet with sample adjusting journal entries and closing journal entries; another booklet that provided line-by-line references for the sources of data required

to complete the Annual Statement; and a blank Annual Statement that serves as a template for filing.

Also consistent with last year's approach, the Audit staff is making a concerted effort this year to be available to work with the retirement board staff. Auditors have been assigned to work directly with retirement boards to provide technical assistance. As was the case last year, an e-mail "Help Desk" address has been established to respond to questions that may come up during the filing process. This electronic communication will provide responses conveniently. It also affords another avenue to convey the details about specific issues encountered during compilation of the Statement. This information will better enable us to document and address such issues in the future. Please direct your inquiries to AnnualStatement-2010@per.state.ma.us.

We hope you find our new video training approach helpful and look forward to hearing your comments about our initial offering.