

## KEN DONNELLY ELECTED TO THE MASSACHUSETTS SENATE FORMER PERAC COMMISSIONER TAKES HIS SEAT IN THE SENATE

**F**ormer long-time PERAC Commissioner Kenneth J. Donnelly was sworn in by Governor Patrick on January 7, 2009 as the Senator representing the 4th Middlesex District. Senator Donnelly approaches his position with a distinguished resume in public service and public policy including, of course, public pension policy development.



Senator Donnelly

firefighter and former Secretary-Treasurer of the Professional Firefighters of Massachusetts (PFFM). PERAC Chairman Domenic J.F. Russo took the opportunity to thank Commissioner Donnelly for his outstanding service to the Commission:

"I know that all the Commissioners join me in saluting our distinguished former colleague Ken Donnelly for all his efforts on behalf of PERAC, the Massachusetts pension community, and the citizens of Massachusetts during his long tenure

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Commissioner Donnelly is a retired

## ROBERT B. MCCARTHY APPOINTED COMMISSIONER

**M**r. Robert B. McCarthy, President of the Professional Fire Fighters of Massachusetts, has been appointed Commissioner of PERAC by State Auditor A. Joseph DeNucci. Mr. McCarthy will assume the seat assigned in statute to the President of the Massachusetts AFL-CIO or his designee. PERAC Chairman Domenic J. F. Russo and Executive Director Joseph E. Connarton welcomed



Commissioner McCarthy

Commissioner McCarthy to his first Commission meeting on January 27, 2009 and wished him well as he assumed the seat previously held by newly elected Massachusetts State Senator Kenneth J. Donnelly.

Chairman Russo noted:

"It is a distinct pleasure as PERAC Chairman and on behalf of the other Commissioners to welcome Mr. Robert B. McCarthy to PERAC. He joins us

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## PERAC RELEASES STATE OF THE PENSION SYSTEM STUDY

By Joseph I. Martin  
Deputy Executive Director

**P**ERAC recently released a study providing an overview of the funding, investment, and benefit structure of the Massachusetts pension systems as well as an assessment of the impact of 2008 investment losses on those systems. Noting that estimates of

2008 expected returns are in the range of -25 to -30%, the agency emphasized the long-term nature of the liabilities of pension funds and the fact that, in spite of such losses, the returns of many systems over the last two decades will continue to meet their investment return assumption.

In discussing returns it should be noted

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### 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](http://www.mass.gov/perac)

**The Honorable Domenic J. F. Russo**  
Chairman

**The Honorable A. Joseph DeNucci**  
Auditor of the Commonwealth  
Vice Chairman

**The Honorable Deval Patrick**  
Governor of the Commonwealth

**The Honorable Paul V. Doane**  
Executive Director  
Arkansas Teacher Retirement System

**James M. Machado**  
Sergeant  
Fall River Police Department

**Donald R. Marquis**  
Former Town Manager  
Arlington

**Robert B. McCarthy**  
President of the Professional  
Firefighters of Massachusetts

**Joseph E. Connarton**  
Executive Director

**Michael DeVito**  
Editor



By Robert Dennis  
Investment Director

Investors still remain shocked by the extraordinary market events of 2008. The fact that US stocks declined nearly 40%, their third worst year ever and worst since the Great Depression, was bad enough but equally discouraging was that, other than cash and US Treasury securities, there was no asset class that provided significant diversification benefits. Everything else was down, not only traditional asset classes like investment grade bonds and junk bonds but also the alternative asset classes that were expected to provide meaningful diversification benefits against a declining stock market.

Did diversification fail? Have all those preaching the benefits of diversification been proven wrong? The contention that a well-diversified portfolio consisting of several imperfectly correlated asset classes can reduce overall risk without reducing expected return has not been definitively discredited. What can be learned from 2008 is that it can be a mistake to consider the concept in overly simplistic terms since there are some types of risk that diversification can reduce but others that it cannot.

The major risk not sufficiently considered in typical asset allocation discussions is the risk associated with the valuation of an asset class. The fact is that, by the second half of 2007, almost every asset class was vulnerable to a correction. For stock investors, after five years of a bull market in stocks, it was increasingly difficult to find stocks that were cheap and the market itself was fully valued by traditional price/earnings measures. For bond investors, yield spreads between both high and low quality corporate bonds and Treasuries narrowed to unusually narrow levels after several years of strong economic growth. Although several years of easy money had contributed to annual housing price increases well above long-term trends and some investors began to wonder if price appreciation had gone too far, most real estate investors saw no end to the continued rise in both commercial and residential markets.

Many strategists were recommending increased allocation to international stocks, both developed and emerging markets, even though five years of significant outperformance of these markets relative to the US had essentially eliminated the valuation disparity that had existed in favor of these markets at the beginning of the decade and even though the weak US dollar, whose downward trend had enhanced the performance of foreign stocks for US investors, was likely due for a rebound.

Thus, the extended good economic times of the middle part of the decade as well as the playing out of some long-term market relationship trends led to nearly every asset class being fully valued to a point where future returns might not compensate for the inherent riskiness of the assets. In other words, most markets were at price levels at which investors might question whether they are being paid to take on the risk. The extremely lax credit standards that led to the surge in subprime mortgage origination during those years was further symptomatic of a period when lenders and investors across a wide spectrum acted as if traditional measures of risk no longer applied.

The inevitable surge in subprime mortgage defaults was the match that lit the fire that led to the basic reversion of all overvalued asset classes back to their historic mean valuations. The economic damage that has ensued has now led the revaluation of many asset classes to not stop at fair value but to continue to levels of seemingly highly attractive undervaluation.

While the weakening economy is making it difficult to forecast future corporate profit levels, most analysts agree that price earnings ratios for S&P 500 companies have fallen to levels that render the stock market at least fairly valued and possibly very undervalued. The yield advantage of investment grade corporate bonds widened from a very narrow 1% to an historically attractive 6% by year-end 2008. After several years of strong performance, high yield junk bond yields were only 3 ½% higher than Treasuries in

early 2007 but widened to a gaping 18% at year-end 2008. At these valuations, downgrades and defaults to an extent far beyond current expectations are assumed. Commercial real estate held up better and longer than residential real estate but when cracks began to inevitably occur, last year's 37% loss by REITs as well as the 6.5% decline in the NCREIF private property index (its first loss in sixteen years) should not have been a surprise. Real estate investors with financing are now finding very attractive values among troubled shopping malls, office buildings, hotels, and industrial space.

Through 2007, institutional investors with access to top-tier managers had enjoyed several years of impressive returns from private equity that were well above those of the public markets. In light of all the money being allocated to private equity by institutional investors, general partners had to pay higher and higher valuations to get deals done. Following last year's dramatic declines in the public markets (NASDAQ was off 40%), investors in buy-out and venture capital partnerships are likely to see sharp writedowns of partnership share values over the coming year. At the same time, however, new investors in alternative investments will be doing so at company valuations more attractive than in previous years.

The great allure of hedge funds in recent years was their promise to achieve returns not dependent on market results but on their manager's ability to isolate and capitalize on aberrations within and among the markets. In 2008, the freezing of the credit markets and the carnage in the stock market was so severe that even the most skilled and experienced managers could not overcome these formidable obstacles and navigate their funds to positive absolute returns. The unexpected negative returns from hedge funds provided a double whammy to those investors who used them as their source of alpha in portable alpha strategies. Nevertheless, since hedge funds are intended to be much more manager dependent than market dependent, it cannot be said that hedge funds are now an undervalued asset class. Furthermore, hedge fund managers who

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## 2009 DISABILITY SEMINARS

The Public Employee Retirement Administration Commission is pleased to announce that it will provide several disability training sessions for retirement boards in 2009. These seminars are targeted toward new retirement board staff members; however, all are welcome to participate. Seminar presenters will include staff members from PERAC's Disability, Actuarial, and Fraud Prevention Units. Their focus will be on disability basics, Workers' Compensation calculations, and the 91A process. PERAC is currently engaged in revising the *Physician's Statement Pertaining to a Member's Application for Disability*

*Retirement* and the revisions will be discussed at the seminar. We will also update seminar participants on the next phase of PERAC's Electronic Content Management System (ECM). Beginning this month, our disability data collection process will be streamlined by capturing key data elements and storing images of documents.

The first disability seminar of 2009 will be held at PERAC in Somerville on March 19, 2009. Registration forms were mailed to retirement boards in mid-February. A second seminar will be held on May 14, 2009 at PERAC. Please note if demand exceeds the seating capacity of PERAC's

seminar room, additional sessions will be scheduled in Somerville. Disability seminars will also be presented in Western Massachusetts on dates and locations to be announced.

Prospective seminar participants are encouraged to contact the Disability Unit (either Barbara Lagorio, Director of Disability, at ext. 952 or Kate Hogan, Manager of Medical Services, at ext. 949) about the disability issues that are of particular interest to them. Such information will aid us in customizing the seminars to ensure that each student's needs are met.

## 2008 ANNUAL STATEMENT TRAINING SESSIONS EVOLVE INTO PERAC "HELP DESK FORMAT" FOR THE CURRENT FILING SEASON

### PERAC STAFF AVAILABLE VIA EMAIL "HELP DESK"

By Frank Valeri  
Deputy Director

The May 1st filing deadline for the 106 local, regional, and state retirement systems to complete and submit their Annual Statements is fast approaching. Although the format and template for the filing is virtually unchanged from last year, PERAC's training approach is different.

The change is driven by the recognition of the electronic evolution of this required annual financial statement for Massachusetts public pension systems. Most of the accounting standards, reporting criteria, and data requirements have remained the same for several decades. However, the one significant aspect that has changed over the past decade is the electronic processing of the systems' financial reporting. The significant reliance by most systems on the various pension software programs has changed the landscape for direct training of board staff in the proper completion of this statement. Future efforts by this agency may be directed towards greater interaction with vendors and board administrators to ensure the accuracy of the data used to develop this financial statement.

With this change in mind, early in 2009, PERAC held 4 regional training sessions,

which provided a less structured presentation and an introduction of a more informal "help desk" approach. This approach gave board staff members the opportunity to share their individual experiences with the Auditor assigned to work with them and receive personalized technical assistance as needed. Chief Auditor Harry Chadwick and Deputy Chief Auditor Jim Tivnan were responsible for coordinating the training sessions.

Prior to the sessions, the Annual Statement publications were distributed via compact disc (CD) to all of the retirement boards. Included on the (CD) was a booklet with specific instructions for preparing an Annual Statement including sample adjusting journal entries and closing journal entries; another booklet providing line-by-line references for the sources of data required to complete the Annual Statement; and a blank Annual Statement providing the format and template for the filing. Hard copies of these materials were also made available at the regional sessions.

Regional sessions were held on:

- January 22, at the PERAC Offices in Somerville
- January 29, at the Stoneham Town Hall
- February 5, at the Clarion Hotel in Northampton

- February 12, at the Taunton Public Library

At each location, one-on-one consultations about preparation basics were conducted, the process in general was reviewed, and common year-end pitfalls were highlighted.

PERAC stands ready to provide help to anyone who requests it during the current filing season. The 2008 Annual Statement process will include a new e-mail "Help Desk" address which will be utilized to respond to questions that may arise during this process. Inquiries should be directed to [AnnualStatement-2008@per.state.ma.us](mailto:AnnualStatement-2008@per.state.ma.us).

Upon request, a PERAC auditor will be assigned to visit boards and provide assistance during the closing process. Merely contact Harry Chadwick to take advantage of this offer. This should not be construed as a substitute for support from a board's software/hardware vendor.

Retirement boards that absolutely cannot meet the filing deadline of May 1st, should mail a letter by May 1st to PERAC Executive Director Joseph E. Connarton wherein the cause for the delay is stated, an extension is requested, and an estimate of when PERAC can expect to receive the final report is provided.

## IRS DETERMINATION LETTER REQUESTS FILED

By Judith Corrigan  
Deputy Legal Counsel

The Internal Revenue Service's "Cycle C" year ended on January 31, 2009, but not before the Massachusetts' public pension systems established under Chapter 32 filed their requests for IRS Determination Letters. The State Board of Retirement, the Teachers' Retirement Board, and the Boston Retirement Board each filed separate requests with the IRS, but the other 103 retirement boards filed through PERAC, utilizing a so-called "template approach."

At a conference last year, the IRS declared that they had been "underserving" the public pension community and invited all public pension plans in the United States to file requests for determination letters. Such letters declare a given retirement plan to be in compliance with the federal law regarding pensions. (The State Board of Retirement received such a letter in the

early 1970s.) The IRS requested that all public pension plans submit applications for a determination letter during its so-called "Cycle C."

Cycle C commenced on February 1, 2008. Almost immediately, representatives from the State Board, the Teachers' Board, and PERAC arranged to meet with IRS officials in Washington, D.C., to see how the request for a determination letter should be made in our unusual circumstances. Although all the boards emanate from the same "plan document," Chapter 32, there are in fact 106 separate boards so emanating. It wasn't clear at first what the IRS would prefer: a single submission from the 106 boards, 106 separate submissions, or something in between. Eventually, the IRS decided to accept separate filings from Boston, Teachers, and the State, and another filing from PERAC incorporating the determination letter requests of the 103 other boards under a template approach.

At the outset, we did not anticipate having all 103 boards join with our template. Although we hoped that would be the case, it was not unthinkable that one or more boards would hire tax counsel and file on their own. Ultimately, however, all 103 boards choose to join PERAC's template. After much work on the part of both the boards and PERAC, the request for 103 determination letters was filed with the IRS. At the end of January, each of the 103 boards received a notice that the IRS had received their application for a determination. The applications are currently in Covington, Kentucky for data entry. After that is completed, the applications will move on for consideration by an Employee Plans Specialist in Cincinnati, Ohio. It is not known how long the decision process will actually take.

This massive undertaking exemplifies a spirit of extreme cooperation between the retirement boards and PERAC. Thanks to all who made this possible.

## PERAC 2009-2010 LEGISLATION FILED TWO BILLS SUBMITTED FOR THE NEW SESSION

By Michael DeVito  
Director of Public Affairs

The Public Employee Retirement Administration Commission has submitted two pension reform bills for the 2009-2010 session of the Massachusetts General Court.

Executive Director Joseph E. Connarton commented:

"PERAC has refiled its pension governance reform bill as well as a bill seeking to eliminate the inappropriately inflated pensions that result from concurrent service in two or more Massachusetts public pension systems. The governance measure is a consensus bill arrived at with the Massachusetts Association of Contributory Retirement Systems (MACRS) and the Retired State County and Municipal Employee's Association (RSCMEA). Building on the last session's progress and cooperation, we look forward to achieving passage of these bills early in 2009."

### 1. AN ACT RELATIVE TO PENSION GOVERNANCE REFORM

Under the enactment of Chapter 306 of the Acts of 1996, PERAC was established for the oversight, guidance, monitoring and regulation of all public pension systems throughout the Commonwealth. After ten years in operation, the Commission conducted a major reexamination of PERAC's statutory authority to oversee the 106 retirement systems.

The governance reform bill grew out of that reexamination and extensive discussions with representatives of MACRS and RSCMEA. The bill seeks to update PERAC's ability to effectively and efficiently oversee these systems. It also provides governance enhancements for the boards to help ensure their sound operation and thereby further safeguard the assets of the members. The bill has twice been reported favorably by the Joint Committee on Public Service. The House Ways and Means Committee also reported the bill favorably last session, but with changes that were not considered acceptable by

PERAC. PERAC is hopeful this year that this bill will be enacted as a sound accompaniment to any other pension reform that the General Court may pass.

The bill would:

1. Update retirement board investment restrictions;
2. Institute financial disclosure requirements for retirement board members;
3. Mandate a competitive bidding process for services provided to retirement boards including: investment, audit, accounting and legal;
4. Institute mandatory yet reasonable continuing education requirements for all board members;
5. Clarify PERAC's ability to take strong concerted action to protect the assets of the systems, including debarment of individuals convicted of certain crimes; and,
6. Require that any employer, entering into a collective bargaining agreement with an employee organization, must provide a copy of that agreement to the employees' retirement board. The retirement board will review collective bargaining agree-

ments for compliance with the provisions of chapter 32. All retirement systems must maintain files of all active collective bargaining agreements which cover the system's members and make them available to the commission for review upon request.

Note: This bill has the same text as H. 4011 of the 2007-2008 Legislative session – the bill text agreed to by PERAC and representatives of MACRS and RSCMEA.

## 2. AN ACT RELATIVE TO DUAL MEMBERSHIP AND REGULAR COMPENSATION

### PENSIONS A KEY ISSUE AS THE LEGISLATURE RECONVENES DISCUSSION INTENSIFIES ON PENSION REFORM AND RELATED ISSUES

By Michael DeVito  
Director of Public Affairs

As the Massachusetts Legislature convenes for its 186th biennial session, budgetary considerations have taken center stage as Governor Deval Patrick and the General Court grapple with the realities of plummeting revenues and budget cuts. Joining the budget as a priority issue is pension reform, which could see early action in the 2009-2010 legislative session.

#### SPECIAL HOUSE COMMITTEE ON PENSION REFORM

Shortly after the beginning of the session, former House Speaker Salvatore F. DiMasi appointed a Special House Committee on Pension Reform chaired by Representative Jay R. Kaufman. The Special Committee filed its report in the House on February 11, 2009. The report included the following recommendations (language taken directly from the report):

**HD 2064**, An act to preserve and protect the integrity of the state pension system, seeks to end some of the inequities and excesses of the current pension system.

- The bill seeks to address some of the most egregious abuses, shortcomings, and excesses of the state pension system. The centerpiece of the bill is an amendment to the definition of "Regular Compensation" in Chapter 32. The bill clarifies the definition and eliminates ambiguities that have led to many of the inequities, lawsuits and

Under current statute, an individual who has received regular compensation from two or more systems concurrently may receive a benefit based on the average of the highest three years of compensation which is determined by adding the compensation of all the individual's positions.

In order to eliminate the appearance of abuse and to provide a more equitable benefit calculation for retirement systems and their members, this bill provides that the retirement allowance in such situations will be calculated as though the member were retiring solely from each system.

problems we have experienced.

- In addition, the Special House Committee proposes eliminating the practice of granting some public employees a full year of creditable service for as little as one day of work, proposing instead that pensions be based only on actual time employed.
- The Special House Committee proposes, too, some changes to another provision of the law originally designed to protect those in "politically sensitive" positions. Chapter 32, Section 10 allows some pension enhancement for long-term public employees dismissed because of a political firing, elimination of the position, etc. Currently, elected officials are also granted enhanced benefits if they "fail of nomination or re-election, or fail to become a candidate for nomination, re-election or election" but the Special House Committee suggests eliminating this protection for elected officials.

**HD 242**, An act relative to pension reform, in largely similar form, was before the legislature last session and, while it received a favorable report from the Committee on Public Service, it was not acted on by the House and Senate.

- It is designed to bring PERAC's authority in line with its responsibilities for overseeing the local and regional retirement systems. It addresses matters of ethics and training for board members and staff, and clarifies proceedings

Each system shall pay the superannuation retirement allowance to the member attributable to membership in that system notwithstanding Chapter 32, Section 3(8)(c). (Please note this will not apply to a member who has received part-time creditable service in one or more systems.)

PERAC hopes that the General Court will undertake prompt and favorable consideration of these two proposals and that they will be on Governor Patrick's desk either independently or as components of any pension reform enacted this year.

when action by PERAC is required.

The Special House Committee recommends swift action to pass this bill. (PERAC NOTE: This is the PERAC board governance reform bill.)

**HD 3965**, An act related to sick leave banks, filed by the Governor, closely tracks a bill passed by the Committee on Public Service last term to shift from a legislation-based to administrative decision-making on granting additional sick leave time to ailing public sector employees.

- The practice of filing legislation and requiring a hearing and complete legislative review is, at best, an inappropriate way to meet the needs of sick staff members. The Special House Committee knows of no other state that so treats its ailing employees.

**HD 2543**, An act making certain changes to the accidental disability retirement allowance, addresses another abused section of the pension law.

- Currently in some cities and towns, a firefighter or police officer who fills in for his superior receives that position's higher salary while there. If that individual goes out on a disability retirement while serving in that position, his retirement is calculated on that higher salary, regardless of the amount of time spent in that position. This legislation changes this calculation to the average salary received in the last 12 months before retirement.

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## ROBERT B. MCCARTHY APPOINTED COMMISSIONER (continued from page 1)

with years of experience in pension issues and his expertise will be most welcome. While we greet the resignation of Ken Donnelly with sadness, we are pleased that his successor will be equally well-qualified to immediately contribute to the Commission's deliberations. We all look forward to working 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 welcomed the new Commissioner:

"On behalf of the PERAC staff, I want to

welcome Commissioner Bob McCarthy to the table as the newest PERAC Commissioner. Certainly, Commissioner McCarthy is no stranger to pension issues having been a major participant in all of the important pension decisions in Massachusetts for many years. His vast experience and expertise will be put to solid use from the outset. To be able to replace a tremendous talent like Ken Donnelly with the vast experience and expertise of a major player on pension issues in Massachusetts for the past quarter century is certainly a unique and very positive opportunity for PERAC. Both in

his Commission and Subcommittee efforts, Bob will be a tremendous asset to the PERAC Team."

Mr. McCarthy has served as the President of the Professional Fire Fighters of Massachusetts since 1987 representing over 12,000 paid professional union fire fighters. He is a retired Captain of the Watertown Fire Department and served in his field for 34 years. Mr. McCarthy served as Legislative Agent of the Professional Fire Fighters of Massachusetts from 1985-1987.

## KEN DONNELLY ELECTED TO THE MASSACHUSETTS SENATE (continued from page 1)

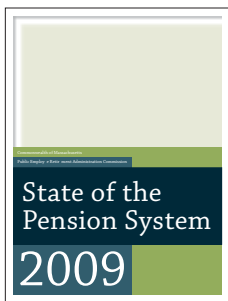
as a member of the Commission. As he moves on to even greater responsibilities in the Massachusetts Senate, we want to wish Senator Donnelly well as he tackles the many challenges that face the Commonwealth in these difficult times."

PERAC's Executive Director Joseph E. Connarton also added his thanks and good wishes:

"It has been a great privilege and pleasure to work with Ken Donnelly during his many years as member of the Commission. He was a dedicated and very valued member and I know that the entire staff joins with me in thanking Ken for his many years of tireless service to the Commission and the people of the Commonwealth. As he approaches his new duties in the Massachusetts Senate, all of the staff look forward to working

with Senator Ken Donnelly as the General Court considers issues of great importance to the Massachusetts pension community. We wish Senator Donnelly all the best as he approaches his new duties and look forward to a continued close working relationship with our good friend and former colleague."

## PERAC RELEASES STATE OF THE PENSION SYSTEM STUDY (continued from page 1)



that just as past positive returns are not predictors of future experience, the same applies to negative returns. PERAC also recounted the fact that, as recently as 2003,

PRIT achieved a return of 26.33% and, in past years, local systems such as Andover, Malden, Marblehead, Lynn, Northampton, North Adams, Swampscott, Woburn, and Cambridge exceeded one-year returns of 30%.

The study reviewed funding options in light of this investment experience and found that, in some systems, budgetary relief could be provided through a combination of adjusting the funding schedule length and annual rate of amortization payment increase. However, it was

acknowledged that a legislative solution may be needed and urged that, "Any legislation should provide maximum flexibility to enable an assessment of individual circumstances and to tailor separate strategies to deal with each unique situation." Outlining the funding history of the plans, PERAC noted that in 1987, 100 of the 106 pension systems in the state were less than 50% funded, only 2 had a funded ratio above 75%, and the other 4 had a funded ratio of between 50% and 75%. Prior to the 2008 market collapse, this situation had reversed itself and 99 systems had a funded ratio above 50%, with 38 funded at a ratio above 75%. Only 7 were funded at a ratio below 50%. That progress should guide us in crafting solutions to the present crisis.

Finally, the document took on some of the persistent myths that unfairly color the debate about public pension systems in Massachusetts stating, "The assertion

that public employee pension benefits are too generous in Massachusetts is now so commonplace in our public discourse as to possess a credibility that is not warranted." Employees, unlike those in most states, are not eligible for Social Security and must rely entirely on their public pension in retirement. In addition, our employees fare worse than their counterparts across the nation in employee contribution rates, limitations on benefits, vesting, and COLAs. In fact, the study found that as a result of high contribution rates for new employees, an individual in the most common classification hired after 1996 at age 25 with a starting salary of \$30,000 will have accumulated in contributions plus earnings over his or her working lifetime \$1.8 million to cover a benefit at 65 worth \$1.5 million, resulting in lowering other plan costs to the employer by \$300,000.

A copy of the Study is available at the PERAC Web Site ([www.Mass.gov/perac/](http://www.Mass.gov/perac/)).

In addition, recommendations 5 through 10 suggest areas where the Special House Committee would urge the Committee on Public Service and the Special Commission on Pensions to consider further actions and/or reforms.

For a copy of the Special Committee's report, please e-mail Michael DeVito, PERAC's legislative director, at [mjdevito@per.state.ma.us](mailto:mjdevito@per.state.ma.us).

### **SPECIAL COMMISSION**

In addition, a Special Commission to Study the Massachusetts Contributory Retirement Systems was created by Outside Section 111 of Chapter 182 of the Acts of 2008 (the annual State budget). This Commission's 15 members include the following individuals (or their designees): the secretary of administration and finance, the auditor of the commonwealth, the executive director of the public employee retirement administration commission, the executive director of the state retirement board, and the executive director of the teachers' retirement board. Joining them will be three members of the house of representatives, three members of the senate, and four members appointed by the governor: a private citizen who is not a member of any of the 106 contributory retirement systems who will chair the commission; an individual who has professional experience in employee benefits or in actuarial science; a member of the Massachusetts Municipal Association (MMA); and a member of RSCMEA.

Some members of the Commission have been appointed, but the Commission has not yet met. The Commission is to make a comprehensive study of the Massachusetts contributory retirement systems. The study should include but not be limited to: contribution rates paid by employers and employees; vesting periods; the weight given to age versus years of service in the current system; the portability of benefits in the current system; cost-of-living-adjustments with special attention paid to the cost of increasing the cost-of-living-adjustments base; and the cost of any recommendations the commission may make. A report is expected July 1, 2009.

This Commission could become a key element in helping to fashion recommendations on changes to the pension system.

### **PENSION RELATED PROPOSALS FROM THE GOVERNOR**

#### **House 1, FY 2010 Budget**

Governor Deval Patrick's Administration has offered several proposals that impact pensions and pension-related issues. House 1, the Governor's budget included a proposed 3% COLA authorization (Outside Section 31) and funding from the Phillip Morris tobacco settlement for the retiree health care (OPEB) unfunded liability (Outside Section 9).

#### **House 104, An Act Strengthening the Commonwealth's Partnership with its Municipalities**

In the Governor's, "An Act Strengthening the Commonwealth's Partnership with its Municipalities," proposals related to transferring retirement board assets to the PRIT fund and retirement system funding relief were included:

#### **Revised Provisions for Transfer of Municipal Retirement Systems into PRIT**

**Section 13** Paragraph (c1/2) of subdivision (8) of section 22 of chapter 32 of the General Laws, as inserted by section 2 of chapter 68 of the acts of 2007, is hereby amended by inserting after the word "perpetuity", in the first paragraph, the following words: -, but a system that has voluntarily transferred ownership and control of all of its assets to the PRIM board before receiving a notice from the commission that the system is underperforming, as determined under this section, shall not be subject to the requirement that the transfer be in perpetuity.

**Section 14** Said paragraph (c1/2) of subdivision (8) of section 22 of chapter 32, as so inserted, is hereby further amended by striking out the fourth paragraph and inserting in place thereof the following paragraph:-

A system ordered by the commission to transfer its assets under this paragraph may appeal to the commission for an exemption by filing written notice of its appeal with the commission not later than 30 days after receiving the commission's order to transfer its assets. The commission may grant an exemption from the transfer requirement of this paragraph if the system's rate of return has exceeded the PRIT Fund rate

of return for the previous 2 years or if the system's rate of return was affected by other extenuating circumstances. The commission may also consider the system's management costs, its risk return ratio and any other factors it considers appropriate. A system may seek judicial review of the commission's decision to deny an exemption in the manner provided in section 14 of chapter 30A. An exemption granted by the commission under this paragraph shall take effect only upon the approval of a majority of the local governing body as follows: in a county, by the county commissioners, in a city having a Plan D or Plan E charter, by the city council and the manager, in any other city the city council and the mayor, in a town shall, by the board of selectmen, in a regional retirement system by the regional retirement board advisory council and in all other districts, by the governing board. The local governing body shall vote whether or not to approve the commission's grant of exemption within 30 days after the commission's decision to provide an exemption.

#### **Retirement System Funding Relief**

**Section 54** Notwithstanding any general or special law to the contrary, the actuary of the public employee retirement administration commission may establish appropriations in fiscal years 2010 and 2011 that are equal to the appropriations made in fiscal year 2009. In any system which chooses to conduct an actuarial valuation as of January 1, 2009, the actuary may establish the following appropriations in fiscal years 2010 to 2012: (a) in fiscal year 2010, an appropriation may be established that is less than the appropriation made in fiscal year 2009 but at least 90 per cent of the appropriation made in fiscal year 2009; (b) in fiscal year 2011, an appropriation may be established that is less than the appropriation made in fiscal year 2009 but at least 95 per cent of the appropriation made in fiscal year 2009; and (c) in fiscal year 2012, an appropriation may be established that is equal to the appropriation made in fiscal year 2009.

PERAC will be monitoring all pension legislation and tracking pension reform issues closely. Please watch for updates in the PERAC Pension News and for breaking developments in PERAC Pension Newsflashes.

survived last year's horrors will have to work hard to dispel the notion that many investors may have had an unrealistically high level of confidence in their managers' ability to overcome adverse conditions. As long as hedge funds were performing well, investors also were reluctant to consider the possible risks involved in so much new money flowing into the funds and in the fact that most funds employed leverage, many to a significant extent.

While the mortgage crisis and its wide ramifications have seen a wide range of assets go from over to under relative to their normal valuations, it has simultaneously spurred another market to an unrealistically high valuation. As a result of Fed easing, the weakening economy, and investors' comfort with investments guaranteed to simply pay

back principal, interest rates along the US Treasury yield curve have declined to historic lows that don't appear sustainable. Unless the US is headed for an extended period of negligible inflation or even deflation, US Treasury securities at year-end levels (2.25% for the ten-year note) seemed as fully priced as stock prices were at their peak or as residential real estate was before the crash. The massive amount of new debt issuance that will accompany the Administration's economic stimulus program, along with the possible long-term inflationary effects of today's historically loose monetary policy, are among the factors that made year-end levels on government debt seem very vulnerable. Indeed, the yield on the ten-year T-note rose to nearly 3% during January.

While assembling a portfolio of risky assets

will usually serve to reduce overall risk, it doesn't erase the fact that they remain risky assets. When the stars align so that nearly all the risky assets are over-valued, even diversification cannot forestall or mitigate the inevitable unhappy endings.

It is certainly not easy to accurately gauge the proper valuation of a particular asset class. The global financial system has become so complex that it is increasingly difficult to understand how markets really work and how they relate to each other. Furthermore, "market timing" is certainly not a typically successful or recommended long-term strategy. However, recognizing that prospective returns from asset classes are dependent on starting valuations can be a useful input into asset allocation decisions.

## 2008 ANNUAL STATEMENT OF EARNED INCOME

On February 20, 2009, PERAC mailed the 2008 Annual Statement of Earned Income with instructions to the 15,000 disability retirees. The Statements must be completed in their entirety and filed with PERAC, along with copies of relevant tax forms and schedules, by April 15, 2009. Questions about the Statements should be directed to Ms. Sandra King at 617-666-4446, ext. 947 or Ms. Ellen Aucoin at ext. 957.

## IN MEMORIAM

Brian Leahy, executive officer and an elected board member of the Massachusetts Water Resources Authority (MWRA) Retirement Board, died suddenly on January 11th. Brian had served at the MWRA since 1986, first as the manager of intergovernmental affairs. In 1994 he assumed the position of executive officer of the MWRA Retirement System. In 2007 he was elected by the employees of the authority to serve on the retirement board. Prior to his service at the MWRA, he was named by Mayor Kevin White in 1980 to head the Boston Retirement Board.

This "gentle giant" from Dorchester was very well-known and respected throughout the Massachusetts retirement community. He was an elected executive board member of MACRS and participated in many PERAC regional and state training seminars. He was also selected by Executive Director Joseph Connarton to serve on the Public Pension Advisory Group (PPAG) with other retirement board administrators to provide input to the Commission on the development of more efficient public pension administration. However, what most of us often experienced, was Brian's great loyalty towards his staff, his retirement board colleagues, and the entire membership of the MWRA Retirement System. He relentlessly fought for the rights, benefits, and fair treatment of the members and his staff at all levels.

His lifetime dedication to his community and family was even more important than his contributions to public service. His daughter, Ann McGough, in her tribute to her dad, published in the Dorchester Reporter noted, "While he is so profoundly missed by so many, it is a gift that we were touched by Brian M. Leahy. How he spent his last day on earth sums up the beautiful way in which he lived his life; he was civically active, he was a man of strong faith, and he always made time for his friends and family."

To say Brian will be missed would be an understatement; we extend the sincere condolences of the Commission and staff to the entire Leahy family and friends at this time of sorrow.



Brian Leahy  
(Photo courtesy of RSCMEA)