



PENSION OBSERVER

THE OFFICIAL PUBLICATION OF THE TEXAS ASSOCIATION OF PUBLIC EMPLOYEE RETIREMENT SYSTEMS

Max Patterson Plans for TEXPERS

At the April meeting the TEXPERS Board of Directors voted to confirm the appointment of Max L. Patterson to the position of TEXPERS Executive Director. Max was selected from a final field of three highly qualified candidates to assume the position made available upon the retirement of Bill Blythe who had served the Association for 17 years.

Max is no stranger to public pension issues. He has had a varied career in the public sector dealing with pension matters during the past fifteen years, including eight years as executive director of the Houston Firefighters' Relief & Retirement Fund. He also served as deputy director of the City of Houston Department of Finance and Administra-



tion. In addition, he was appointed City of Houston Treasurer and was a fiduciary on the city's three pension funds.

Max would like to see TEXPERS influence grow—both regionally and nationally—into the foremost voice of Texas public pension plans. His plans to expand and strengthen the impact of TEXPERS include concentrating on three primary areas: enhancing the quality and depth of training for trustees and administrators; strengthening relationships with the

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Globalization and Equity Investing

By Kurt Umbarger

Global economic growth has been remarkably strong in recent years. While helped by a cyclical recovery of the major economies, this expansion has also been boosted by the acceleration of a more secular trend. As businesses and capital have increasingly moved beyond domestic boundaries to diverse markets around the globe, they have broadened and deepened the links among different countries and regions. Global trade has grown from approximately 20% of world gross domestic product (GDP) in the 1970s to about 55% today. While the trend has been apparent for decades, its pace has demonstrably quickened in recent years.

In the last decade, declining transport costs, widening access to technology, and improved information-sharing have enhanced the pace of globalization. This dynamic, structural change has far-reaching implications at both the macro- and microeconomic levels. Barriers to entry are eroded, allowing firms to compete globally and sell in new markets. Frequent interchanges of

multinational corporations comprise an increasing share of foreign direct investment flows, particularly in Latin America and emerging Asia. Led by the so-called BRICs (Brazil, Russia, India and China), emerging countries have become increasingly integrated into the global economy, and companies have moved production overseas to take advantage of cheaper labor costs.

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trade flows, intellectual capital and business processes allow best practices to be replicated more quickly across sectors and countries, and enable the strategic frameworks of mature industries to be applied overseas.

One measurable result of this drive to globalization is the dramatic increase in cross-border merger and acquisition activity since the mid-1990s. Additionally,

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SEC to Further Restrict But Not Ban 'Soft Dollars'

The Securities and Exchange Commission (SEC) will publish new guidance on money managers' use of client commissions to pay for brokerage and research services under the "soft dollars" safe harbor. Soft dollars are non-monetary credits given to money managers by brokerages in exchange for payment by the managers of above-market commission rates for execution of buy and sell orders. The credits commonly go to managers of mutual funds, hedge funds, pension funds and other institutions.

The practice, which started in the 1970s, has become widely used despite some controversy. SEC officials voted 5-0 on July 12 to approve the new official guidance to try to stem the alleged corruption in the use of soft dollars.

Critics of soft dollar deals want them banned on the grounds that they sometimes are spent on products and services that benefit managers, not fund investors. Soft dollars have been used in some cases to pay for conferences, telephone calls, and even college tuition for managers' kids. The new SEC rules will limit the permissible uses of soft-dollar credits to paying for research, including advice, analysis and reports, as well as certain brokerage services and other "reasonable" products and services.

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The SEC guidance (the agency calls it an "Interpretive Release") articulates that the analysis of "brokerage and research services" under Section 28(e) of the Securities Exchange Act of 1934 requires a three-step process: the application of eligibility criteria; the money manager's

lawful and appropriate use of the items; and the money manager's good-faith determination that the commissions paid are reasonable in light of the value of the services received.

The Interpretive Release states that money managers may use client commissions to pay only for eligible brokerage and research services. Eligible research services are limited to advice, analyses, and reports under Section 28(e). This means that traditional research reports, market data, and other items that satisfy the eligibility criteria of Section 28(e) are eligible for the safe harbor as research, but other things, such as computer hardware, are not.

The guidance also indicates that mass-marketed publications are not eligible under the safe harbor. Eligible brokerage includes those products and services that relate to the execution of the trade from the point at which the money manager communicates with the broker-dealer for the purpose of transmitting an order for execution, through the point at which funds or securities are delivered or credited to the advised account. In order to operate under the safe harbor, "the money manager must use the eligible brokerage and research services in a manner that provides lawful and appropriate assistance."

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Another quarter has gone by with a dramatic swing in the market. From an investor's standpoint the road is pretty rough. As pension trustees we have come to learn that we are in this for the long haul, and have been on this ride before.

TEXPERS is busy working on your behalf and watching the radar screen for any items of interest to our members. Max Patterson, our new Executive Director of TEXPERS, has been working closely with me on all issues both federal and state. Max and I have been attending meetings of the State Pension Review Board and interim committee meetings as well as meeting with committee chairmen, and going over strategic planning with our lobbyists for this coming legislative session.

You will notice some changes to this year's venue that came about as a result of meetings and an exchange of ideas between us and the associate members.

It has been a pleasure working with Max in this arena. He is committed to this organization and its members and has the support of the TEXPERS Board of Directors.

The staff has worked diligently to make sure that this coming Summer Educational Forum will be one of the best. You will notice some changes to this year's venue that came about as a result of meetings and an exchange of ideas between us and the associate members. TEXPERS is known nationwide for providing some of the best educational opportunities anywhere to its members. We are committed to insuring that we continue building that established

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STATE CAPITOL REPORT

By Neal T. "Buddy" Jones

The first interim committee hearings on pension matters have been scheduled for August 7-8, 2006 in the House Pensions and Investments Committee. The hearings will discuss seven interim charges given to the committee by House Speaker Tom Craddick. The seven charges include:

1. Study the role of actuaries in monitoring the financial health of public pension plans, and evaluate the need for regulation in regard to their qualifications, the setting of actuarial assumptions and oversight.

2. Evaluate the criteria which would be provided to the Pension Review Board that would signal a major change in the financial condition of a public pension system, including the necessary data, frequency of reports, costs to the system, and its source of funding.

3. Examine the feasibility of facilitating the creation of a large, consolidated risk pool and other strategies to give governmental entities statewide relief from high premiums for health care benefits for employees and retirees.

4. Review the eligibility criteria for the Law Enforcement and Custodial Officers Supplemental (LECOS) retirement program and the impact of these guidelines on funding needed for the pension fund.

5. Analyze the impact of targeted investment strategies on state retirement funds.

6. Review the Proportionate Retirement Programs and their effects on state pension funds.

7. Monitor the agencies and programs under the committee's jurisdiction. TEXPERS members plan to testify on the first 3 charges listed.

The Senate Committee on Intergovernmental Affairs has not, to date, scheduled any interim hearings. The chairman of this committee, Senator Frank Madla, has resigned his Senate seat after being defeated for

re-election in the Democratic primary in March. No hearings are expected to be held until a new chairman is appointed.

On November 7, 2006, Texans will go to the polls to elect state officials and congressmen for the next 2 to 4 years. This election cycle promises to be an exciting one with four viable candidates certified on the ballot to run for Governor of Texas.

At this time no big political upsets are anticipated. The present Texas Legislature and Governor Perry have received high marks for their work in the latest special session.

The Texas Secretary of State has certified Carole Keeton Strayhorn and Richard "Kinky" Friedman to run as Independents in the Governor's race. They join Republican Governor Rick Perry and Democratic candidate Chris Bell. This will surely be the most expensive Governor's race in Texas history. As of the June 30th campaign finance report, Governor Perry had \$10 million in cash on hand, Ms. Strayhorn showed to have \$8 million, Friedman had \$500,000, and Democrat Chris Bell had \$650,000 in the bank.

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The Texas Senate has only one race in which both candidates are raising large amounts of money. Senator Elliot Shapleigh, from El Paso, is facing a well-financed opponent, Donald "Dee" Margo. In the Texas House there are several contested races in which incumbents could lose. It appears there will not be enough Democratic victories to change the Republican control of the Texas House of Representatives.

The Pension Review Board met on June 22, 2006, for its summer quarter meeting. In what has become a regular event at Pension Review Board meetings, representatives of the El Paso Firemen's and Policemen's Pension Funds and representatives of the City of El Paso testified about actions being taken to reduce the amortization period of their fund. It was pointed out that the city plans to issue pension obligation bonds to help reduce the amortization period. They also testified they have agreed on a mediator to help develop a plan to make the fund amortization sound.

Other plans which have amortization periods exceeding 40 years were asked to testify. These were the Fort Worth Employees' Retirement Fund, the University Park Firefighters Relief and Retirement Fund, and the Greenville Firemen's Relief and Retirement Fund. All outlined their plans to make their funds amortization sound.

Finally, the Pension Review Board is considering a requirement that all public pension funds file quarterly reports regarding their financial soundness. A workshop regarding filing of these reports was held by the Pension Review Board on July 19, 2006.

Neal T. "Buddy" Jones, attorney and industry consultant, is based in Austin, Texas.

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Washington Outlook

By Matt Aukofer
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For “mixed-use” items that are partly eligible and partly ineligible, the Interpretive Release states that money managers must make a “reasonable” allocation of client commissions in accordance with the eligible and ineligible uses of the items. It reiterates the statutory requirement that money managers

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must determine in good faith that the commissions they pay are reasonable in relation to the value of the brokerage and research services that they obtain.

The guidance states that the safe harbor is available when a money manager does business with a broker-dealer that is involved in “effecting” the money manager’s trades and “provides” the research. In order to be “effecting” transactions, the broker-dealer must either execute, clear, or settle the trade, or perform one of four specified functions and allocate the other functions to other broker-dealers.

The Interpretive Release will be effective upon publication in the Federal Register, but market participants will be able to rely on prior Commission guidance for a period of six months following publication. 🇺🇸

Matt Aukofer, journalist and consultant, is based in Washington, D.C.

President's Corner

By Paul R. Brown
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reputation, and are striving to improve in any other areas that benefit all TEXPERS members.

Though we look forward to our trip to beautiful San Antonio, it is with heavy heart that we will miss the presence of Judy Jones. Judy has been the staple that helped hold things together, and has been a big influence for many of us.

My thanks go out to every one for helping the staff get through this very rough time. They have endured some dramatic changes virtually over night, including having to move the entire office over one weekend. On behalf of the Board of Directors I want to thank Max and staff for all of their hard work.

Please make sure you register for the TEXPERS Summer Educational Forum. I look forward to seeing you in San Antonio. 🇺🇸

Globalization and Equity Investing

By Kurt Umbarger

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In 2005, approximately 40% of global imports were from developing countries compared to 30% in 1990.

Consequently, it is becoming less likely that the best investment ideas will always be found at home. Viewing the world as one

Globally diversified portfolios provide an investor with the opportunity to generate higher returns for a given level of risk than could be achieved with a domestic-only portfolio

large investment universe can provide asset managers with the opportunity to invest in the best companies wherever they may be located, and to shift among geographic regions, sectors, and industries as opportunities appear and disappear. In the increasingly global

world, a stock's country of listing is becoming less important than its base and scope of operations. As best practices are replicated very quickly around the world, a global equity portfolio allows active managers to enhance alpha by finding patterns of dynamic change. As an investment product, the appeal of a global equity strategy increases as cross-border transaction and information costs fall and regulatory barriers are lowered. The global investment universe, represented by the MSCI World and MSCI All Country Indices, is larger, more liquid, and more diverse than regional and individual country indices. Structurally, local-market indices contain fewer stocks and are more concentrated in a handful of large equities than global indices, making it harder to diversify against risk.

Although globalization is having a far-reaching impact on the worldwide economy, many investors have not changed their

approach to equity investing. Many U.S. investors still follow the traditional asset allocation approach, holding diversified U.S. and non-U.S. portfolios. Employing a global approach to equity investing can reduce home country bias and risk while also providing the potential for additional alpha. This increased diversification is one of the primary benefits of employing a global approach to equity investing.

Globally diversified portfolios provide an investor with the opportunity to generate higher returns for a given level of risk than could be achieved with a domestic-only portfolio. As the global economy integrates further, active managers need the relevant skills and expertise to effectively exploit market inefficiencies arising from the patterns of structural dynamic change. A global mindset, a sophisticated approach to risk management, and the ability to act locally are prerequisites to achieving success. 🇺🇸

Kurt Umbarger is a Global Equity Portfolio Specialist for T. Rowe Price in Baltimore, Maryland.

Max Patterson Plans for TEXPERS

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representatives in the legislature to deal with important pension issues; and relaying critical pension plan issues to members of the organization.

Max would like to see TEXPERS influence grow, both regionally and nationally, into the foremost voice of Texas public pension plans.

"I believe it's important to focus on two to three major areas and refine them," Max said. "It's more effective to change three major areas than to do half a job focusing on many more."

One of his first projects as executive director of TEXPERS was to initiate a membership satisfaction survey to solicit feedback from system members on how well TEXPERS operates.

"As an association we want to meet the needs of our members," Max said. To achieve

this he would like to introduce what he calls "conference themes" to educate the system members. "I want to move toward focusing on what's impacting pensions today," Max said. "I don't want to have a conference focus solely on investing because that's just one of the responsibilities facing pension trustees and administrators."

Among other issues, he believes that it is important to build influence in government circles in order to strongly represent public pension plans and their individual members. An integral part of supporting TEXPERS goals means being proactive in Austin, which requires being knowledgeable about key legislation before, during and after its inception. He wants to help all public pension funds, both large and small, maintain a respected voice in Austin.

In addition to his position as executive director of TEXPERS, Max remains active in the Government Finance Officers Association. He has served as a member of the Committee on Retirement and Benefit Administration and as a past board member. He also currently serves

as the Governor's appointee to the Texas Emergency Services Retirement Board. 🇺🇸

MARK YOUR CALENDARS

Upcoming Conferences

TEXPERS Summer Educational Forum

August 20 & 21, 2006
San Antonio, TX

TEXPERS 18th Annual Conference

March 18 - 21, 2007; Austin, TX
Marriott at the Capitol

2007 Summer Educational Forum

August 19 - 20, 2007
San Antonio, TX
Westin Riverwalk

In Memory of Judy Jones (1940-2006)

It is with profound sadness that we report the death of Judy Jones, Director of Office Administration at TEXPERS. She passed away unexpectedly at St. Luke's Hospital in Houston on June 18, 2006.

Judy served TEXPERS, its board members and associates for 15 years with her own delightful blend of outstanding capability, hard work, high spirits and can-do attitude. To know Judy was to admire and respect her character and to enjoy her cheerful company.

To know Judy was to admire and respect her character and to enjoy her cheerful company.

She will be missed by all who knew her and deeply mourned at TEXPERS by her coworkers, board members, Executive Director Max Patterson, former Executive Director Bill Blythe and many others.

Judy loved her wonderful family, her church, her friends and Republican Party politics. She was a founding member of the Heritage Republican Women's Club and spent years working in grassroots Harris County and Texas Republican party politics.



She chaired two successful campaigns to elect her late husband, Sonny Jones, to the Texas House of Representatives as the first Republican elected to that body since Reconstruction. While he was in office, Judy worked to give Harris County and Texas a Republican majority.

In lieu of flowers, the family asked that donations be made to her beloved St. Thomas Episcopal Church at 4900 Jackwood Houston, TX 77096, or to the Texas Blue Hole Fund at the Village of Wimberley. Judy vacationed in Wimberley yearly with her cousin and best friend, Marje Harris, and she loved to share stories of her times at her favorite swimming hole. We're going to miss those stories this year.

Carolyn Butterworth has been assigned Judy's responsibilities at TEXPERS on an interim basis. She will be handling sponsorship and program information as well as administrative duties. 🇺🇸

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Pension Observer

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