CYPEN & CYPEN NEWSLETTER for JUNE 26, 2014

Stephen H. Cypen, Esq., Editor

Never Forget September 11, 2001

and

Always Remember May 2, 2011

1. FPPTA 30TH ANNUAL CONFERENCE: The Florida Public Pension Trustees Association's 30th Annual Conference will take place on June 29 – July 2, 2014 at the Hilton Bonnet Creek, Orlando. A link on FPPTA's web site, www.fppta.org, will take you to the Hilton Bonnet Creek site to make your room reservations. You may access information and updates about the Conference at FPPTA's website. All police officer and firefighter plan participants, board of trustee members, plan sponsors and anyone interested in the administration and operation of the Chapters 175 and 185 pension plans should take advantage of this Conference.

2. HALIBURTON FAILED TO SHOW A SPECIAL JUSTIFICATION FOR OVERRULING PRESUMPTION OF RELIANCE IN SECURITIES FRAUD CASE: Investors can recover damages in a private securities fraud action only if they prove that they relied on a

defendant's misrepresentation in deciding to buy or sell a company's stock. The U.S. Supreme Court has previously held that investors could satisfy this reliance requirement by invoking a presumption that the price of stock traded in an efficient market reflects all public, material information, including material misrepresentations. However, a defendant could rebut this presumption by showing that the alleged misrepresentation did not actually affect the stock price, that is, it had no "price impact." Erica P. John Fund, Inc. filed a putative class action against Halliburton and one of its executives, alleging that they made misrepresentations designed to inflate Halliburton's stock price in violation of section 10(b) of the Securities Exchange Act of 1934 and Securities and Exchange Commission Rule 10b-5. The District Court initially denied EPJ Fund's class certification motion, and the Fifth Circuit affirmed. However, the Supreme Court vacated that judgment, concluding that securities fraud plaintiffs need not prove loss causation -- a causal connection between the defendants' alleged misrepresentations and the plaintiffs' economic losses -- at the class certification stage in order to invoke the presumption of reliance. On remand, Halliburton argued that class certification was nonetheless inappropriate because the evidence it had earlier introduced to disprove loss causation also showed that its alleged misrepresentations had not affected its stock price. By demonstrating the absence of any price impact, Halliburton contended, it had rebutted the presumption. Without benefit of that presumption, investors would have to prove reliance on an individual basis, meaning that individual issues would predominate over common ones, and class certification would be inappropriate under the Federal Rules of Civil Procedure. The District Court rejected Halliburton's argument, and certified the class. The Fifth Circuit affirmed, concluding that Halliburton could use its price impact evidence to rebut the presumption only at trial, not at the class certification stage. On certiorari to the United States Court of Appeals for the Fifth Circuit, the U.S. Supreme Court held that Halliburton had not shown the "special justification" for over ruling the presumption of reliance. The Court did agree with Halliburton, however, that defendants must be afforded an opportunity to rebut the presumption of reliance before class certification with evidence of a lack of price impact. *Halliburton Co. v. Erica P. John Fund, Inc.*, Case No. 13-317 (U.S. June 23, 2014).

3. POLICE GENERALLY MAY NOT, WITHOUT A WARRANT,

SEARCH DIGITAL INFORMATION ON A CELL PHONE SEIZED FROM AN INDIVIDUAL WHO HAS BEEN ARRESTED: The Supreme Court of the United States recently considered two important search and seizure cases:

- (A) In the first case, Riley was stopped for a traffic violation, which eventually led to his arrest on weapons charges. An officer searching Riley incident to the arrest seized a cell phone from Riley's pants pocket. The officer accessed information on the phone and noticed the repeated use of a term associated with a street gang. At the station, two hours later, a detective specializing in gangs further examined the phone's digital contents. Based in part on photographs and videos the detective found, the State of California charged Riley in connection with a shooting that had occurred a few weeks earlier, and sought an enhanced sentence based on Riley's gang membership. Riley moved to suppress all evidence that the police had obtained from his cell phone. The trial court denied the motion, and Riley was convicted. The California Court of Appeal affirmed. On certiorari to the California Fourth District Court of Appeal, the U.S. Supreme Court reversed and remanded.
- (B) In the second case, Wurie was arrested after police observed him participate in an apparent drug sale. At the police station, the officers seized a cell phone from Wurie's person, and noticed that the phone was receiving multiple calls from a source identified as "my house" on its external screen. The officers opened the phone, accessed its call log, determined the number associated with the "my house" label and traced that number to what they suspected was Wurie's apartment. They secured a search warrant and found drugs, a firearm, ammunition and cash in the ensuing search. Wurie was then charged with drug and firearm offenses. He moved to suppress the evidence obtained from the warrant of the apartment. The United States District Court denied the motion, and Wurie was convicted. The First U.S. Circuit Court of Appeals reversed denial of the motion to suppress and vacated relevant convictions. On certiorari to the U.S. Circuit Court of Appeal for the First Circuit, the U.S. Supreme Court affirmed.

Police generally may not, without a warrant, search digital information on a cell phone seized from an individual who has been arrested. A

warrantless search is reasonable only if it falls within a specific exception to the Fourth Amendment's warrant requirement. The well-established exception at issue in these cases applies when a warrantless search is conducted incident to a lawful arrest. Three related precedents govern the extent to which officers may search property found on or near an arrestee: (a) a search incident to arrest must be limited to the area within the arrestee's immediate control, (b) where the arrest is justified by interests in officer safety and (c) is justified to prevent evidence destruction. Digital data stored on cell phones does not present such risks. *Riley v. California*, Case Nos. 13-132, 13-212 (U.S. June 25, 2014).

4. ESOP FIDUCIARIES ARE NOT ENTITLED TO ANY SPECIAL PRESUMPTION OR PRUDENCE: Fifth Third Bancorp maintained a defined contribution retirement savings plan for its employees. Participants may direct their contributions into any of a number of investment options, including an Employee Stock Ownership Plan (ESOP), which invests its funds primarily in Fifth Third stock. Former Fifth Third employees and ESOP participants filed a lawsuit against Fifth Third and alleged fiduciaries of the ESOP. The complaint alleged that Fifth Third and the fiduciaries had breached their duty of prudence imposed by the Employee Retirement Income Security Act of 1974. Specifically, the complaint alleged that they should have known -- on the basis of both publicly available information and inside information available to them because they were Fifth Third insiders -- that Fifth Third stock was overpriced and excessively risky. The complaint further alleged that a prudent fiduciary in their position would have responded to this information by selling off the ESOP's holdings of Fifth Third stock, refraining from purchasing more or disclosing the negative inside information so that the market would correct the stock's price downward. According to the complaint, they did none of these things, and the price of Fifth Third stock ultimately fell, reducing the retirement savings of the former employees and participants. The United States District Court dismissed the complaint for failure to state a claim, but the Sixth Circuit reversed. The latter court concluded that ESOP fiduciaries are entitled to a "presumption of prudence" that does not apply to other ERISA fiduciaries, but that the presumption is an evidentiary one and therefore does not apply at the pleading stage. The court went on to hold that the complaint stated a claim for breach of fiduciary duty. On certiorari to the United

States Court of Appeals for the Sixth Circuit, the United States Supreme Court held that ESOP fiduciaries are not entitled to any special presumption of prudence. Rather, they are subject to the same duty of prudence that applies to ERISA fiduciaries in general, except that they need not diversify the fund's assets. This conclusion follows from the relevant provisions of ERISA that impose a prudent person standard by which to measure fiduciaries' investment decisions and disposition of assets. Thus, aside from the fact ESOP fiduciaries are not liable for losses that result from a failure to diversify, they are subject to the duty of prudence like other ERISA fiduciaries. On remand, the Sixth Circuit should reconsider whether the complaint stated a claim. *Fifth Third Bancorp v. Dudenhoeffer*, Case No. No. 12-751 (U.S. June 25, 2014).

5. WHERE WORKERS' COMPENSATION CLAIMANT CONTRIBUTED TO PENSION FUND SUPPLYING DISABILITY BENEFITS, EXCLUDING SUCH BENEFITS FROM OFFSET WAS PROPER: The employer appealed an order of the Florida judge of compensation claims, denying an offset asserted by the employer against Sikalos's workers' compensation disability benefits. The District Court of Appeal affirmed. Sikalos was a deputy sheriff, who suffered a compensable injury, for which he received temporary total disability benefits under section 440.15(2), Florida Statutes. His average weekly wage is $851.27, making his compensation rate $567.54 per week. On account of his injury, Sikalos also received $1,470.00 per month social security disability benefits and $2,530.81 per month in-line-of-duty disability benefits from the Florida Retirement System. The total disability benefits Claimant received from all of the above sources for his compensable injury is $6,441.23 monthly, or $1,497.96 per week. The weekly amount exceeds his average weekly wage of $851.27 by $646.69. Because of the overage, the employer began taking an offset against Sikalos's workers' compensation disability benefits on June 28, 2013, under the purported authority of Escambia County Sheriff's Department v. Grice, 692 So. 2d 896 (Fla. 1997), in which the Florida Supreme Court held that an injured worker, except where expressly given such a right by contract, may not receive benefits from his employer and other collateral sources which, when totaled, exceed 100% of his average weekly wage. When that occurs, the employer is entitled to offset the excess by reducing workers' compensation disability benefits

accordingly. The "*Grice* offset" is determined by totaling the disability benefits a claimant receives from all sources (including workers' compensation), calculating a weekly total and subtracting 100% of the claimant's average weekly wage. Because the offset here exceeded the amount of workers' compensation disability benefits the employer would otherwise would pay, the employer paid Sikalos the statutory minimum amount of $20 per week. When Sikalos challenged the offset, the judge of compensation claims excluded his in-line-of-duty disability benefits from the offset calculation, because Sikalos contributed to the pension fund supplying those benefits. His pension plan, FRS, from which the in-line-of-duty disability benefits are paid, was fully employer funded until July 7, 2011, when, statutory amendments, required FRS members to begin contributing 3% of their compensation to fund the plan. The judge of compensation claims relied on an earlier Supreme Court of Florida case holding that where the pension fund is funded at least in part with employees' contributions, decreasing workers' compensation benefits on account of pension benefits runs afoul of Section 440.21, Florida Statutes. Thus, once it is determined that the pension plan is funded with employees' contributions, workers' compensation benefits are primary and it is the pension fund that is entitled to the benefit of the offset. The holding should not be read to mean that in all other cases workers' compensation fund automatically receives the benefit of the offset; rather, where the fund is employee-contributory, it would violate Section 440.21, Florida Statutes for workers' compensation benefits to be reduced. Section 440.21, Florida Statutes, invalidates any agreement by an employee to pay any portion of premium paid by his employer to a carrier or to contribute to a benefit fund or department maintained by the employer for the purpose of providing compensation or medical services and supplies as required by Chapter 440. Offsetting workers' compensation benefits to account for collateral benefits a claimant receives from an employee-contributory pension fund is tantamount to requiring the claimant to contribute to a benefit fund maintained by the employer for the purpose of providing workers' compensation benefits, a circumstance prohibited by Section 440.21, Florida Statutes. The employer also argued that Section 440.21, Florida Statutes, does not apply to a situation where, like here, the in-line-of-duty disability benefit fund (FRS) is not maintained by the employer, but by the state. The court declined to read such a distinction into the statute, because doing so would create disparate

results for claimants employed by state government entities and claimants employed by non-state government entities participating in the FRS. *Hernando County Sheriff's Office/North American Risk Services v. Sikalos*, 39 Fla. L. Weekly D1333 (Fla. 1st DCA June 25, 2014).

6. MARDEN CONTINUES TO REFOCUS THE LENS: Susan Marden, Florida Public Pension Trustees Association Public Relations Consultant, recently lamented the pervading view that public employees should somehow feel more grateful for their compensation than their private sector counterparts, and tried to refocus the lens to remind readers about why taxpayers are really angry about public worker benefits -- namely, because they have so few themselves. (See C & C Newsletter for June 5, 2014, Item 4). She also enumerated some of the reasons why American businesses have been pulling away from defined benefit plans. Chiefly, it is because legislative regulations intended to protect workers from corporate malfeasance had the unintended effect of making pension plans prohibitively expensive for American businesses. In addition, American businesses have chosen to secure their competitive position in a global marketplace by shifting cost and risk for retirement to their employees, rather than absorb those expenses and risks at possible peril to themselves. Ironically, Marden writes, there is a strongly positive view of pension plan benefits shared by both employers and employees in the private sector. Numerous studies and surveys during the past few years reveal a clear preference for stronger retirement benefits by both workers and business owners. National Conference on Public Employee Retirement Systems recently had a survey conducted, which reached a total of 500 small business owners nationwide, with businesses ranging from 2 to 49 employees. Here are some key findings:

- Small business owners are acutely aware of the need for better options for retirement savings. A solid majority (56%) worry about their own retirement security and nearly two-thirds (65%) worry that their employees will not have enough money to retire.
- Nearly all small business owners (82%) agree that offering a retirement benefit helps to recruit and retain good employees.
- Almost three-quarters of small business owners (73%) feel a responsibility to provide some kind of retirement benefit.

Towers Watson released a 2012 report showing Americans have an increasing awareness of the positive impact defined benefit pensions have on their retirement security. A head-to-head question was what employees want more: a guaranteed pension or other benefits. A large plurality (49%) chose the pension over the opportunity to earn a bigger bonus. Pensions also ranked higher than paid vacations, an increased chance at a promotion and larger salary increases. A recent report of a survey by National Institutes on Retirement Security found:

- An overwhelming majority of Americans (85%) continues to report concern about their retirement prospects, with more than half (55%) very concerned.
- A large majority of Americans (83%), reports favorable views of pensions, and 82% say those with pensions are more likely to have a secure retirement.
- Moreover, 84% indicate that all Americans should have access to a pension to be self-sufficient in retirement.

So, it would seem that nobody is really against retirement security -- the challenge is to achieve it for more Americans. The problem is not insurmountable, but the pending crisis is far more serious than current public plan underfunded liability or temporary stock market corrections. **According to NCPERS, there is a deficit of more than $8.5 trillion between what American 401(k) account holders should have and what they do have.** Over the next 10 to 15 years, the bulk of the 78 million Baby Boomers will be of retirement age, giving the U.S. the largest over-65 population in its history. Public employee retirement systems should lead the way in adapting to new economic realities, develop investment strategies that will mitigate market volatility, and accept compromise on what benefits can realistically be achieved and pre-funded. Taxpayers too should accept that public services are provided to them at enormous cost-savings by highly trained, professional employees, not just public servants. As has so often been the case in America's history, the public sector can develop breakthrough ideas.

7. *GOVERNING* GUIDE TO FINANCIAL LITERACY: You are involved in government because you want to accomplish something. Maybe you want to fight poverty or reform public schools. Maybe you want to cut taxes or privatize government services. Maybe you think government mostly gets it right, so you want to protect policies or

programs. Regardless of why you got involved, by now you have realized you cannot accomplish much if you cannot speak the language of public finance. In fact, many policymakers lament that they spend more time than ever on budgets and tax policy, and less time on the policies and programs they care about most. The goal of Governing's Guide to Financial Literacy is to help you speak that language. Or, put differently, to help you become financially literate. You are financially literate if you understand your jurisdiction's "financial story." That story has several parts, and those parts are the major sections of the Guide. How does your jurisdiction get and spend its money? How does it finance big ticket items like infrastructure improvements? Is it in sound financial shape? To that end, the Guide covers three main types of information related to each part of the financial story:

- **Technical knowledge.** Once you have read the Guide you will have a much clearer sense of how governments collect taxes, analyze costs, borrow money and prepare financial statements.
- **Essential questions**. As a leader in your government, you have two main responsibilities with respect to money. The first is your fiduciary duty, the second is ensuring that public resources are put to their best possible use. The Guide outlines questions that every state and local official should know to ask.
- **What not to do.** There are many splashy examples of financial illiteracy. More often than not, these misunderstandings follow from some flawed, but widely held, ideas about how public finance works. The Guide tries to identify and clear up some of those misconceptions.

The Governing Institute demands better government by focusing on improved outcomes through research, decisions support and executive education to help public sector leaders govern more effectively. For additional information, visit www.governing.com/finance101.

8. TENNESSEE ADOPTS "MODEL" PENSION LAW: Tennessee Governor Bill Haslam has approved Senate Bill No. 2079, enacting Public Chapter No. 990, to amend Tennessee law relative to financial security for public defined benefit pension plans. The state treasurer is required to develop and recommend to the board of trustees a funding

policy with respect to obligations to the Tennessee Consolidated Retirement System. The board of trustees shall adopt a funding policy which complies with said provisions. The new law defines "actuarially determined contribution" (ADC), formally known as "actuarially required contribution" (ARC) to mean the actuarially determined annual required contribution that incorporates both normal costs of benefits and amortization of the pension plan's unfunded accrued liability.

9. WHY TEACHERS DRINK: Q. What does "varicose" mean? A. Nearby.

10. TODAY IN HISTORY: In 1963, U.S. President John Kennedy visits West Berlin "Ich bin ein Berliner" ("I am a Berliner"; or is it "I am a doughnut").

11. KEEP THOSE CARDS AND LETTERS COMING: Several readers regularly supply us with suggestions or tips for newsletter items. Please feel free to send us or point us to matters you think would be of interest to our readers. Subject to editorial discretion, we may print them. Rest assured that we will not publish any names as referring sources.

12. PLEASE SHARE OUR NEWSLETTER: Our newsletter readership is not limited to the number of people who choose to enter a free subscription. Many pension board administrators provide hard copies in their meeting agenda. Other administrators forward the newsletter electronically to trustees. In any event, please tell those you feel may be interested that they can subscribe to their own free copy of the newsletter at http://www.cypen.com/subscribe.htm.

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