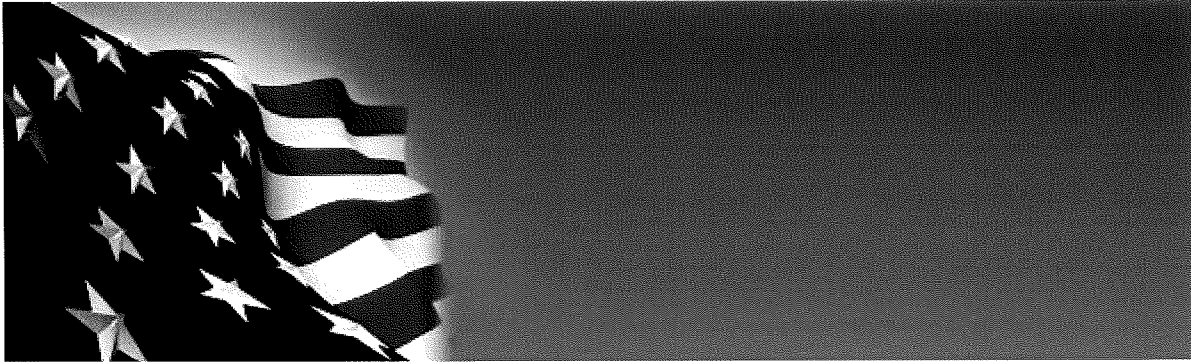


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# CYPEN & CYPEN NEWSLETTER for DECEMBER 4, 2014

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Stephen H. Cypen, Esq., Editor

Never Forget September 11, 2001

and

Always Remember May 2, 2011

**1. PUBLIC PENSIONS STILL MODEST:** Writing in the *Palm Beach Post*, Kim Ryals, CEO of Florida Public Pension Trustees Association, says the average annual benefit for retired public employees in Florida is \$19,000 (for state workers) and \$23,000 (for municipal workers). For most municipal workers, a 30-or-35-year career yields modest benefits that strengthen retirement security and the local economy, which is a critical factor for the many who do not receive Social Security. More than two-thirds of Florida's municipal pension plans are adequately funded, with many others rebuilding after the collapsed stock market of the Great Recession. FPPTA's research shows that nearly every city in Broward County has made cuts to employee benefits, and restructured funding, to secure pension benefits. Similar results show up in Lee and Miami-Dade Counties. Last year, state Senator Jeremy Ring (D-Margate) brokered a deal with public worker unions and municipal pension sponsors to allow previously mandated "extra benefits" to be earmarked for purposes

other than increased retirement checks. For example, they could be used to pay down unfunded liabilities. But the House Speaker did not allow a vote on the measure.

**2. WHO WILL WIN WHEN “LOSER PAYS”:** Law Professor John Coffee wrote a column in the *New York Law Journal* about a largely unnoticed trend toward bylaw and charter provisions that imposed some form of a "loser pays" rule on plaintiffs in intracorporate litigation. First, between May 29, 2014 and Sept. 29, 2014, some 24 companies had adopted such a provision (always applicable only to plaintiffs and always without a vote of the shareholders). The response was obviously to the Delaware Supreme Court's decision in *ATP Tour v. Deutscher Tennis Bund* (see C & C Newsletter for October 30, 2014, Item 4). *ATP Tour* upheld the facial validity of such a bylaw that had been adopted by a Delaware non-stock corporation. Since then, the number has grown further, and some of the better known law firms appear to be adopting this tactic as part of their standard Initial Public Offering playbook. Second, although the board approved bylaw route used in *ATP Tour* has been followed by others, the more common route is to amend the certificate of incorporation of a firm about to undergo an IPO. The greater use of this technique may reflect the fear that mature "reporting" companies have of alienating their proxy advisors. If Institutional Shareholder Services were offended by a board approved bylaw, they might support a hedge fund activist or a shareholder effort to reverse the bylaw through a precatory shareholder vote. In an era of high hedge fund activism, seasoned issuers do not pick fights with proxy advisors. Third, most of the firms adopting a one-way "loser pays" bylaw or charter provision did not simply require the losing plaintiff to pay the various defendants' legal expenses; rather, they also required a winning plaintiff to pay if it did not achieve a standard of "complete success," which they defined to mean that a reimbursement obligation arose to repay all fees, costs and expenses of every kind and description of all defendants if the plaintiff does not obtain a judgment on the merits that substantially achieves in substance and amount the full remedy sought. Drafted very aggressively, these provisions applied not only to the actual plaintiff but to any other person acting on behalf of plaintiff who joins, offers substantial assistance or has a direct financial interest in any claim filed against the corporation or a director, officer, employee or affiliate thereof. Finally, these provisions cover not only lawsuits, but

any proceeding, whether civil, criminal, administrative or investigative, and any assertion of a claim or counterclaim. Thus, a shareholder whistleblower who advises the Securities and Exchange Commission or some other agency about alleged misconduct or a former employee/shareholder who brings a claim for wrongful termination, could be held liable (at least if he were a present or former shareholder and were not completely successful). There is a familiar pattern evident. The aggressive transaction planner tries to draft a provision with the maximum impact, so as to chill any prospect of litigation of any kind. This draftsman may feel that his side has nothing to lose from his attempt to intimidate. But this mistake could be serious. In pushing the envelope this far, the transaction planner may either invite a federal court to discover a conflict between the fee shifting provision and policies underlying the federal securities laws (and thus rule that federal law preempts the provision) or encourage the Delaware Chancery Court to find that the provision had an "improper purpose." Delaware courts have a long history of holding that the corporation may still not be used for an improper purpose. The decision in *ATP Tour* alluded to this line of cases, but also observed that the goal of deterring litigation was not "necessarily improper." Yet, even if attempting to discourage frivolous litigation seems fair enough, the analysis changes when a bylaw or charter provision demands complete success. Then, it seemingly moves beyond a proper purpose and intentionally seeks to discourage meritorious litigation. That end may be too much for Delaware, which has little desire to ensure extinction of intracorporate litigation. So, what alternatives are possible for Delaware? One, such action could provide that a "loser pays" provision could only be adopted by a shareholder vote taken after the company had become a public corporation (that is, reported under §12 of the Securities Exchange Act). Two, some form of ceiling to be placed on fee shifting. After all, it should not take much of a sanction to chill the fly-by-night plaintiff firms behind most state court merger and acquisition litigation. If the goal is to deter the pointless and extortionate M&A class action, a modest ceiling could do that (one can reasonably debate whether it should be \$500,000 or \$1,000,000, and it could be automatically inflation indexed.) If the rule were so limited, reputable plaintiffs' counsel could obtain insurance, but the marginal plaintiffs' firms that bring but never actually litigate M&A cases could probably not afford such insurance. Three, the "loser pays" rule might be to limit the fee

“CCC+” to “BB-” with a stable outlook. Vallejo did made deep cuts in police and firefighters, and closed several fire stations. The current budget called for hiring 18 police officers, two dispatchers, 10 police cadets, 10 firefighters and one deputy fire chief.

**4. IN ERISA CASE, TRIAL COURT PROPERLY HELD THAT CLAIM FOR DISABILITY BENEFITS WAS BARRED BY “BORROWED” STATUTE OF LIMITATIONS:** On an appeal, the U.S. Eleventh Circuit Court of Appeal had to determine whether Witt’s lawsuit seeking to recover disability benefits allegedly due from May 1997 was barred by the applicable statute of limitations, and, if so, whether defendants waived that statute of limitations defense. After careful review, the appellate court affirmed the grant of summary judgment in favor of defendants. Witt’s complaint was untimely under the applicable statute of limitations (“borrowed” from Alabama), which began to run when Witt had reason to know that defendant MetLife clearly repudiated his benefits claim. Such repudiation occurred, at the latest, on May 1, 1998. Defendant MetLife’s subsequent courtesy review did not restart the statutory clock. In addition, defendant MetLife did not waive any defense based on the statute of limitations by failing to specify untimeliness as a basis for denying the claim after its courtesy review. *Witt v. Metropolitan Life Insurance Co.*, 25 Fla. L. Weekly Fed. C665 (U.S. 11<sup>th</sup> Cir. November 25, 2014).

**5. AOI HEDGE FUND PRINCIPLES:** The Alignment of Interests Association is a non-profit, investor-driven organization based on strengthening the alignment between hedge fund industry participants. Its mission is to foster investor collaboration, provide an independent forum for exchange of ideas and contribute to the sharing of educational resources among investors. Through an Investment Steering Committee of more than a dozen hedge fund investors (including Florida Retirement System), AOI serves to add institutional guidance and continuity on its objectives, and helps to determine which issues merit member collaboration and communication. The following are the AOI Hedge Fund Investing Principles, dealing with three major areas:

- Economic and Liquidity Terms
- Documentation and Governance
- Transparency, Valuation and Disclosures

shifting to costs incurred up to the decision on the motion to dismiss. The initial rationale here would be that a case that survives a motion to dismiss is clearly not frivolous. In a federal securities class action based on Rule 10b-5, surviving a motion to dismiss means that the complaint did plead with specificity facts giving rise to a strong inference of fraud; that is not a low standard. In a derivative action, surviving the motion to dismiss means that the plaintiff has pleaded facts showing that demand on the board should be excused as futile; that hurdle is more difficult.

### **3. CALPENSIONS.COM DEALS WITH CaIPERS, CaISTERS AND OTHER GOVERNMENT PENSIONS:**

A recent release poses the rhetorical question of what happens when a bankrupt city does not cut its largest debt, pensions, which city has higher average pensions and higher CalPERS rates than the two larger cities (Stockton and San Bernardino) still in bankruptcy? Vallejo was the forerunner, choosing not to try to cut pensions before exiting a 3½ year bankruptcy three years ago. City council members said later CalPERS had threatened a long and costly legal battle. Stockton's plan to exit bankruptcy without cutting pensions was approved in October. The judge ruled that CalPERS pensions can be cut in bankruptcy. But Stockton does not want to cut pensions, saying they are needed to be competitive on the job market. San Bernardino, cash short, skipped payments to CalPERS for most of a fiscal year. Last month the city formally announced that under an agreement with CalPERS last June, the missed payments are being repaid and pensions will not be cut in bankruptcy. So, will the bankrupt cities regret passing up a chance to cut growing pension costs that take funds needed for other services? A leader among the critics of public pension cost reporting, credit rater Moody's, warned that failure of the three bankrupt California cities to cut pensions risks a return to insolvency. Vallejo may be a good post-bankruptcy test, not only because it was first in and first out, but also because of its high pension costs. The rate that Vallejo pays CalPERS is significantly higher than the rates paid by the other two bankrupt cities. The Vallejo safety rate (police and firefighter), 57.6% of pay next fiscal year, is projected by CalPERS to reach 72% of pay in 2021. Vallejo's city manager boasts the first structurally balanced city budget in 10 years. The city received its first unqualified audit in over seven years, re-entered the debt market with an \$18 million water bond, and debt issued in 1999 was recently upgraded from

The entire document can be accessed at [http://www.altaoi.org/wp-content/uploads/2014/12/AOI-Hedge-Fund-Principles\\_2014.pdf](http://www.altaoi.org/wp-content/uploads/2014/12/AOI-Hedge-Fund-Principles_2014.pdf).

**6. PENSION FUNDS D.I.Y.:** State Street has issued “Pension Funds D.I.Y., A Hands-On Future for Asset Owners.” Five trends are reshaping the pension industry. Pension funds are restructuring for a new investment climate. They are becoming more hands-on in the way they manage their investment portfolios. This proactive approach extends to all aspects of their operations and governance. Research reveals key trends that are radically reshaping almost every aspect of how pension funds manage their investments and deliver long-term value to their members.

- **Trend 1: Getting Hands-on with Investment Risk.** Pension funds are re-evaluating their attitude toward risk as they seek to deliver value to their members in a difficult investment climate. More than three-quarters of respondents expected their institutions’ investment risk appetite to increase over the next three years. The rise in risk appetite is driven by pension funds’ need to boost lackluster returns. Interest rates have remained at historically low levels. Traditionally popular asset classes such as equities and fixed income may look pricey. Research shows that pension funds are making a major shift in allocations to less-familiar asset classes, such as alternatives, to drive growth and meet long-term liabilities.
- **Trend 2: Big Bets on Alternatives.** For pension funds, alternative investments have typically constituted a small part of the portfolio. Now, pension funds find that a small allocation to alternatives is not sufficient to generate the required growth. They are forced to place bigger bets on alternatives. Private equity emerges as a hot area for investment, with 60% of respondents anticipating increased allocations into this asset class. A significant proportion of pension funds will invest more in direct loans (54%), real estate (46%) and infrastructure (39%).
- **Trend 3: D.I.Y. on Asset Management.** The trend toward the insourcing of asset management will accelerate over the next three years. Globally, 81% of pension funds say they intend to increase the proportion of their portfolio that is managed in-house. Cost is a big driver for insourcing strategies. On average,

funds spent 46 basis points on their external management, compared to 8 basis points on internal investment capabilities. Asset owners also believe they can increase their oversight of assets by bringing them in-house.

- **Trend 4: The Relationship with Asset Managers Evolves.** The relationship between the pension funds and their asset managers adds another layer of complexity to risk and performance management. Building a holistic view of risk across a multi-asset portfolio is doubly difficult if you are aggregating risk data from multiple managers. Fifty-eight percent say it is a challenge to gain a complete picture of risk-adjusted performance. Almost one in five describe this challenge as major. More than half of pension funds (52%) also find it difficult to ensure that their asset managers' interests are aligned with their own. Cost is also an issue: almost one-third of pension funds (29%) say it is a challenge to justify fees from their asset managers (although only 6% see it as a major challenge). Pension funds will still pay a premium for managers with proven investment skills and ideas. Only the very largest and most sophisticated funds, for example, will have the skills to manage all aspects of today's multi-asset class portfolios in-house.
- **Trend 5: Fortifying Governance.** Several forces have combined to put a new focus on the governance model for pension funds. More than half of respondents in the survey view strengthening their overall governance as a high priority for the next three years. Pension funds need an approach that emphasizes oversight, transparency and disclosure. Regulation is a factor in this trend. The increased use of complex alternatives may also require pension funds to bring in more professional trustees or specialist advisors. Good governance also requires pension funds to take a broader perspective on risk management.

The research sheds light on several important questions, as pension funds adapt to a new landscape:

- How will pension funds balance their increase in risk appetite with demands for a more robust approach to risk management?

- How can pension funds pursue a strategic approach to insourcing that delivers both cost savings and improved performance?
- What criteria will pension funds use to select external asset managers and service providers?
- How can pension funds fortify their governance foundations as they take on the risks associated with DIY fund management?
- Where do pension funds need to invest in new tools and talent to ensure they have the capabilities to succeed in this demanding new environment?

**7. FRANKLIN TEMPLETON APPEALS STOCKTON'S BANKRUPTCY PLAN:** A major investment firm has challenged a court approved bankruptcy plan for the city of Stockton, California, possibly jeopardizing resolution of one of the country's biggest city bankruptcies stemming from the 2008 housing burst. According to kcra.com, Franklin Templeton Investments, an assets management firm, filed an appeal against Stockton's bankruptcy deal. City officials had successfully negotiated with creditors to eliminate more than \$2 billion in long-term debt, without cutting the city's pension obligations. Franklin Templeton was the only major creditor not to sign off on the settlement. The investment firm said the city should have cut employee pensions rather than scrub the \$32.5 million it owed Franklin Templeton. The federal bankruptcy judge, in approving the bankruptcy plan, noted that the city had cut employees pay and benefits, and pensions for new employees.

**8. THREE YEARS LATER, RHODE ISLAND PENSION LAW STILL IN LIMBO:** Three years ago, Rhode Island Governor Lincoln Chafee signed what remains the most sweeping overhaul of a state pension system ever seen in the United States, saving taxpayers billions, but angering many government workers and retirees in the process, according to wpri.com. Now Chafee will leave office, to be succeeded by the architect of the pension overhaul, Governor-elect Gina Raimondo. But a suit challenging the law is still in pretrial limbo, and there is now growing momentum in favor of reaching a deal to resolve the issue once and for all. Talk of settlement may come as a surprise, considering a previous attempt to craft one collapsed, when police

officers voted against it. Yet, state and union leaders are keenly aware that with so much money at stake (roughly \$4 billion, or nearly half the state's annual budget) the way they resolve the pension battle is one of the most consequential policy decisions facing Rhode Island today. Raimondo, who initially resisted efforts to mediate, suggested she remains open to settling but only if she can preserve the lion's share of the savings from the original 2011 law: the previous settlement reduced the state's pension shortfall by \$3.86 billion, about 94% of the \$4.09 billion the law saved.

#### **9. RETIREMENT BENEFITS DECISIONS BY STATE AND LOCAL**

**GOVERNMENTS:** An Issue Brief from Center for State & Local Government Excellence stresses that the importance of supplemental retirement saving plans to public employees, in part, depend on the terms and generosity of other retirement plans that the state or local government offers. A prior issue brief described in detail the characteristics of supplemental retirement saving plans offered by 20 city and county governments across the country. This follow-up issue brief reviews, for those same 20 public employers, the parameters of primary retirement plans and retiree health insurance. Expectation is that public employees' use of supplemental retirement plans will be influenced by whether those employees are covered by Social Security, what the key characteristics of their primary retirement plans are, how generous their plans are and whether their governments provide health insurance to retired employees. This issue brief examines each of such retirement benefits, and provides a background for the forthcoming third brief, which will assess average worker participation in voluntary retirement plans.

**10. THE ANSWER IS "567"...WHAT IS THE QUESTION?:** The number 567 is the answer to the question "How many options does a married couple have for deciding when and how to file for the Social Security benefits?" That number was determined by Center for Retirement Research at Boston College. Nevertheless, we think we will verify it with reader F.N. in Ft. Lauderdale.

**11. FOLLOW UP ON *LANE* CASE:** In our November 26, 2014 Newsletter, we mentioned *Lane v. Franks*. Now, on remand from the United States Supreme Court, the Eleventh U.S. Circuit Court of Appeals has determined that Lane's claim against Franks's successor

as community college president, seeking relief of reinstatement, was not barred by Eleventh Amendment. *Lane v. Central Alabama Community College*, 25 Fla. L. Weekly Fed. C675 (U.S. 11<sup>th</sup> Cir. November 24, 2014).

**12. MIAMI RANKED FIFTH WORST FOR VETERANS:**

Southflorida.citybizlist.com ranks Lincoln, Nebraska; Gilbert, Arizona; and Irvine, California; as the three best cities for military veterans, while Newark, New Jersey; Chicago and Memphis, Tennessee; are the worst. In 2013, there were 21.4 million military veterans in the U.S., according to Bureau of Labor Statistics data. About 722,000 were unemployed, many because of disabilities that resulted from their service. As of June 2014, nearly 300,000 were deprived of emergency jobless compensation. In order to identify the best and worst cities in veteran living, the personal finance website analyzed 100 of the most populated U.S. cities across two equally weighted key dimensions, including "Economic Wellness" and "Environment, Education and Health." Then 19 metrics relevant to those dimensions, including percentage of military skill-related jobs, veteran unemployment rate, veteran-owned businesses per veteran population, housing affordability, cost of living and number of veterans per capita. Here are some placements of interest: Miami (96), Hialeah (74), Orlando (71), Tampa (62), Jacksonville (61) and St. Petersburg (54).

**13. DILLERISMS:** Housework cannot kill you, but why take a chance?  
-Phyllis Diller

**14. STUFF YOU DID NOT KNOW:** The first novel ever written on a typewriter, Tom Sawyer.

**15. TODAY IN HISTORY:** In 1954, the first Burger King is opened in Miami, Florida.

**16. 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.

**17. 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>.

**18. REMEMBER, YOU CAN NEVER OUTLIVE YOUR DEFINED RETIREMENT BENEFIT.**

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