

Memorandum

MEETING DATE
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AGENDA ITEM # 6

Date: January 19, 2011

To: CCCERA Board of Retirement

From: Cary Hally, Chief Investment Officer
Chih-chi Chu, Retirement Investment Analyst

Subject: Security Litigation Monitoring Services

Recommendation

We recommend the Board instruct staff to issue a Request for Information (RFI) for security litigation monitoring services, and authorize senior staff to select two or three firms to perform this service for CCCERA with a recommendation brought back to the Board for approval.

Background

CCCERA currently relies on its custodian bank, State Street, to file claims brought by class action security litigation. The custodian bank custodies all the public-traded securities purchased by CCCERA's investment managers, except for commingled funds such as JP Morgan, Progress and GMO. Therefore, State Street is aware of the class action lawsuits against the securities owned by CCCERA, and files claims on behalf of CCCERA.

The security litigation monitoring process does not end with filing the claim. When the settlements are announced, a class member's interest may be impaired by the limits on the scope of the class. For example, if the scope on a particular settlement requires both IPO and open market purchases, owners of the shares through the open market purchases may get minimal participation, if anything at all, in the final settlement. With legal analysis on settlements, CCCERA may be better informed.

The current process with State Street has minimal staff involvement with all costs imbedded in the overall custodian fee. There are areas that can be improved in the current process. For example, an independent platform to monitor the filings by State Street could notify staff if claims are not filed before the deadline. In cases where CCCERA suffers significant loss, the access to legal analysis on the viability of potential lawsuits may be useful for CCCERA to determine its prudent course of action.

A security litigation monitoring report could also be used as a tool to evaluate investment managers. In a customized report, the securities involved in class action lawsuits can be categorized by investment manager who purchased them. An investment manager who consistently owns more securities named in class action lawsuits than other investment managers is potentially of concern.

It should be noted that securities in commingled vehicles are not covered in the monitoring services, regardless of the type of service provider.

Overview on Peer Group

To understand our peers’ policies in monitoring security litigations, the staff conducted a survey among CALAPRS members. The table below is a summary of the 11 responses to our survey.

<i>Type of Service Provider Chosen</i>	<u>Number of Survey Returns²</u>	<u>Pro</u>	<u>Con</u>
<i>Law Firms</i>	6	Provide free monitor services and legal analysis, as well as the viability to go outside of a class action	Some firms may be aggressive in pressuring clients into separate (or lead plaintiff) lawsuits, which take significant staff time
<i>IRSS¹</i>	4	Provides monitor services; does not pressure clients into filing separate lawsuits	Monitoring service not free; lack of legal analysis
<i>Custodian Bank</i>	2	Low maintenance, no (or low) cost	Lack of legal analysis; no cross-check on whether claims are filed; no follow-up on the settlements

¹Investors Responsibility Support Services

²Numbers sum to 12 as one county utilizes the services of both law firms and IRSS. Responding to our survey include Alameda County, Santa Barbara County, San Mateo County, LA County, San Francisco City & County, City Of Fresno, Fresno County, Orange County, San Joaquin County, Stanislaus County, and Sonoma County.

Summary

As summarized by the table above, a majority of the respondents to our survey retain law firms for securities litigation monitoring services and legal analysis, while a few hire IRSS to provide monitoring services to cross-check custodian bank’s claim filing. Our preference is for the monitoring services provided by law firms. There is no fee for these services, and they are typically accompanied with access to their analysis when needed. We also feel that since there is no fee it makes sense to have two or three firms perform this service. We recommend sending a RFI to the well known firms providing this service for CCCERA’s peer systems.

One of the potential drawbacks is a firm selected to provide this service may aggressively pursue CCCERA’s participation in legal actions, which may take up considerable staff time and resources. At the February Board meeting we will revisit the securities litigation policy to insure the dollar threshold is properly set for consideration as lead or out of class participation.